

**PUBLIC COMMENTS RECEIVED ON THE DISCUSSION DRAFT ON THE ATTRIBUTION OF PROFITS TO PERMANENT ESTABLISHMENTS –
PART II (SPECIAL CONSIDERATIONS FOR APPLYING THE WORKING HYPOTHESIS TO PERMANENT ESTABLISHMENTS OF BANKS)**

New York Clearing House

1. The New York Clearing House Association L.L.C. (the “Clearing House”), an association of major United States commercial banks¹, is writing to comment on the OECD’s discussion draft on the attribution of profits to permanent establishments (the “Discussion Draft”). The Clearing House commends the OECD on its efforts to develop a uniform approach for attributing profit to a permanent establishment and to achieve a consensus on the interpretation of Article 7 of the OECD Model Tax Convention on Income and Capital. The Clearing House also commends the OECD for preserving the principle that the “force of attraction” does not apply to a permanent establishment, and we would suggest that this be emphasised in any final proposals.

2. The Clearing House would like to comment on several issues addressed in the discussion draft on which our members share the same concerns. There are many other issues raised by the Discussion Draft on which the Clearing House members have strong views on which we have not commented; instead, individual members of the Clearing House may comment separately on these issues or may join with other industry groups that are commenting on these issues (*e.g.*, the allocation of “free capital” and “intangibles” to a permanent establishment).

3. The Clearing House supports the Discussion Draft’s objective of a uniform interpretation of Article 7 and the avoidance of double taxation. Our expectation, based upon past experience, however, suggests that many countries will not adopt all of the rules suggested by the OECD. We are therefore concerned that unless the proposals are adopted by all countries on a uniform basis, there will be a tremendous amount of resources devoted to developing and implementing these proposals without substantially reducing the problems caused by inconsistent tax laws (*e.g.*, double taxation). Accordingly, the Clearing House recommends that the OECD suggest that individual tax jurisdictions implement new rules in this area only if substantially all of the OECD members adopt the rules as proposed by the OECD.

4. Moreover, the Clearing House has other concerns that should be addressed before the proposals are finalised for presentation to the OECD members. The proposals are included in the Discussion Draft would require a substantial investment of time and resources to gather and organise the necessary data. For example, the allocation of assets among multiple branches in accordance with the proposal would require that banks capture and organise data in ways that differ from the ways such data is captured and organised for other purposes. This would require the creation and maintenance of extensive separate software and databases solely for tax purposes. The Clearing House believes that the Discussion Draft has not adequately justified the need to impose such costs; in other words, it is not clear that the value of improved tax administration, if any, would exceed the very substantial costs that the world’s financial institutions would incur in implementing these proposals. In the unlikely event that imposing these costs on the world’s financial institutions can be justified, at a minimum it is essential that any changes along these lines be prospective, and allow sufficient time for the design and implementation of adequate systems to comply with the increased record keeping necessitated by the proposals.

1. The members of the Clearing House are Bank of America, National Association; The Bank of New York; Bank One, National Association; Bankers Trust Company; The Chase Manhattan Bank; Citibank, N.A.; European American Bank; First Union National Bank; Fleet National Bank, HSBC Bank USA, Morgan Guaranty Trust Company of New York and Wells Fargo Bank, National Association.

5. The Clearing House is also concerned by the suggestion in the Discussion Draft that certain head office expenses may not be properly allocated to a permanent enterprise. While we understand that there are certain head office expenses that provide no separately identifiable benefit to a branch, each branch benefits from the support received from the head office and from the other activities of the head office. These activities in many cases allow the branch to conduct its own activities more efficiently or the branch may benefit less directly from the activities (*e.g.*, the branch may benefit from the goodwill or other non-quantifiable intangibles created by the head office). The Clearing House therefore believes that the proposal could inappropriately lead to a significant reduction in the allocation of head office expenses, because the proposal fails to insure that the costs of maintaining large scale, integrated financial services operations are properly allocated among all of the bank's activities. We have similar concerns with respect to the treatment of transactions between permanent establishments.

6. The Clearing House also believes that assets generally should be allocated to the permanent enterprise at which they are recorded for book purposes, and that the financial statements of a permanent enterprise generally should be the starting point for the determination of profit and loss. A bank's financial statements are used for substantial non-tax purposes, including reports to bank regulators, and provide an objective, reliable basis for attributing profits to permanent establishments. If functions (*e.g.*, marking, or credit) are performed at other locations, profits can be properly attributed to those locations by imputing fees for services. The reliance on booking locations avoids the need to create deemed or fictional transfers of all, or part, of financial assets. If these deemed transfers are created, it would be necessary to determine how a deemed transfer would be characterised. If the deemed transfer is treated as a sale, lease or license, it would be necessary to determine the pricing at which this fictional transaction occurs. There is no reason to believe that this will be any easier or more accurate than arm's-length fees for services. Moreover, requiring that fictional sales, leases or licensing be created for tax purposes increases the risk of lack of uniformity (and therefore double taxation) because different jurisdictions may not respect other jurisdictions' characterisations of the fictional transaction or the "prices" at which fictional transactions between branches are deemed to occur.

7. Finally, the Clearing House notes that a number of related issues remain under study by the OECD, in particular global trading of financial instruments. The Clearing House feels strongly that it would not be appropriate to adopt proposals with respect to the attribution of profits to permanent establishments of financial institutions in advance of thorough consideration of these related issues.