Capital Markets Tax Committee of Asia

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Mr Jeffrey Owens
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By email: jeffrey.owens@oecd.org

Dear Mr Owens,

Comments on report by the Informal Consultative Group on the Taxation of Collective Investment Vehicles and Procedures for Tax Relief for Cross-Border Investors (ICG)

This submission is respectfully made in response to your invitation for comments on the public discussion draft issued by the Pilot Group on Improving Procedures for Tax Relief for Cross-Border Investors (Pilot Group). In that report, the Pilot Group made various proposals relating to the application of tax treaty benefits to investors in Collective Investment Vehicles (CIVs).

We wish to thank you for giving us the opportunity to provide our comments.

1. What is the Capital Markets Tax Committee of Asia ("CMTC")

By way of introduction, the Capital Markets Tax Committee of Asia (CMTC) is a financial services industry body consisting of a number of banks, investment banks, securities firms and other diversified financial services institutions operating in Asia who are represented through their regional tax directors, most of whom are Hong Kong based.

CMTC's membership comprises ABN Amro, ANZ Bank, American Express, Bank of America Merrill Lynch, Bank of China International, Barclays Capital, BNP Paribas, Citigroup, CLSA, Credit Agricole CiB, Credit Suisse, Daiwa Securities SMBC HK Ltd, DBS, Deutsche Bank, Fidelity Investments, Fortis Bank, Goldman Sachs, Hang Seng Bank, HSBC, ING, JP Morgan Chase Bank, Macquarie Bank, Morgan Stanley, Nomura, Rabobank, Royal Bank of Canada Capital Markets, Royal Bank of Scotland, Société Générale, Standard Bank Asia, Standard Chartered Bank, Swiss Reinsurance Co and UBS.

The main objects of the CMTC, according to its constitution, are "to provide a forum for discussion by corporate tax managers responsible for the tax affairs of investment banks, securities firms, banks and other diversified financial services institutions of topical taxation issues in Asia affecting their capital and securities markets and similar activities; … to keep members informed of up to date information on taxation matters affecting capital and securities markets, and to exchange views on the technical analysis thereof; [and] to represent the interests of its members through acting as the respected voice of investment banks, securities firms, banks and other diversified financial

services institutions, and to participate in liaison or advocacy activities on tax matters either directly or indirectly through representation with other groups or societies concerned with or by fiscal matters".

2. A wider perspective

We actually have little to say about the report of the Pilot Group in terms of the specific proposals contained therein and we support its aims.

Instead, our main goal in providing you with this submission is to make some higher-level comments about the growing trend towards increased routine provision of information procedures around the world that involve financial institutions. We hope that these comments can be fed into the CFA's deliberations. Our goal is to seek to alleviate the growing burdens that are being imposed on financial institutions due to what we perceive to be different approaches that are being taken, and which will continue to be taken over the coming years, by tax administrations in different jurisdictions.

We emphasize that we are not criticizing the work of the Pilot Group. Indeed, the work of the Pilot Group will result in standardized tax relief arrangements and this is obviously a significant benefit for those institutions that will opt to become Authorized Intermediaries. We would suggest, however, that more steps could be taken to unify the information reporting procedures proposed by the Pilot Group with procedures that have already been adopted by tax administrations in other contexts, and which are likely to be proposed by tax administrations in the future in other contexts.

To explain this further, the CMTC has been following closely recent developments around the world with respect to reporting by financial institutions of information concerning their customers. We have no objection to rules and regulations that require our members to provide reasonable, legally available customer and account information to tax administrations for the purpose of ensuring the efficient enforcement of tax laws and the prevention of tax evasion. Indeed, because of their unique position in the global economy, it is inevitable that financial institutions will be increasingly called upon to make such information available to tax administrators.

However, because of the plethora of countries involved, our members are very concerned to ensure that attempts by tax administrations to gather information are coordinated, in order to avoid separate disclosure regimes applying in different contexts and in different jurisdictions. In our view, a high degree of standardization is necessary to minimize the compliance burdens that will be increasingly levied on financial institutions, in order to avoid costly inefficiencies arising.

To achieve such standardization, much coordination will be required. It appears to us that the OECD is the best-placed body to spearhead such coordination. This is because of the OECD's unique role in representing the interests of major tax administrations, its policy of seeking to achieve a fair and reasonable balance between the interests of tax administrators and taxpayers, and of course the fact that the OECD has historically served as the major global body in identifying and harmonizing tax procedures with respect to cross-border activities.

We appreciate that such cross-border information gathering and information exchange represents the new reality of the global economy. Our concerns relate to making such systems as efficient as possible, so that the burdens on financial institutions are as streamlined as possible. Because of their inevitable involvement in such information gathering and information exchanges, it is inevitable that greater burdens will be imposed on financial institutions as these enforcement steps increase.

This enforcement will involve more countries over time, who are both members and non-members of the OECD. In our respectful submission, it is essential that steps be taken now to ensure that these routine provision of information procedures be coordinated and standardized, so that the

financial institutions on whom increasing burdens fall are able to discharge the obligations efficiently and effectively.

In this context, we submit that standardization is required with respect to the following matters, amongst others.

i. The types of information to be provided to tax administrations.

ii. The procedures whereby such information is to be provided.

iii. The format whereby information should be provided (which will necessarily be through secure electronic filing means). This is important to ensure that financial institutions are not required to adopt different procedures, and bear different consequences, from one tax administration to another, and from one context to another. Developing IT solutions to reflect different permutations and changes can be very expensive. As financial institutions are called on more and more to collect and provide information to the tax authorities so they perform their compliance initiatives, there needs to be a recognition that all of this costs money. It's not that financial institutions are asking to be reimbursed for this cost; what financial institutions seek is a recognition by the various tax authorities of this material cost being incurred, and a commitment from the various tax authorities to seriously consider the writing of uniform rules up front.

iv. The consequences of mistakes being made.

v. The scope of "know your customer" standards and due diligence that institutions should be required to follow in verifying customer information, both at the outset and periodically thereafter.

As you will observe, we are not simply addressing the proposals of the ICG. We can see that the information reporting requirements of the proposals may represent a "first step" towards increasing provision of information requirements, and we therefore hope that these proposals could coordinated with other steps that have been taken, and will increasingly be taken, by tax administrations across the world.

The sooner this is done, the better. Our obvious fear is that, if tax administrations later impose more provision of information requirements in other contexts, in addition to the ICG's proposals the result will be unnecessary overlaps and ultimately unviable systems of ad hoc provision of information requirements.

3. An example of inconsistency – ICG v FATCA

By way of example, we turn to contrast the different standards that are imposed upon financial institutions under the ICG's proposals, and the new US requirements under the Foreign Account Tax Compliance Act (FATCA) which will be effective 01/01/2013.

a. The ICG's proposals in the context of CIVs

The ICG has made certain proposals whereby so-called Authorized Intermediaries would be entitled to seek on behalf of portfolio investors the application of tax treaty preferred withholding tax rates.

In exchange, the Authorized Intermediaries would agree to provide to the tax administrations of the jurisdictions out of which the payments are made (source jurisdictions) certain information about the ultimate investors involved. The ICG contemplates that the tax administration in the source jurisdiction would then share that information with the tax administration of the investor's own

jurisdiction (residence jurisdiction). The tax administration in the residence jurisdiction would then presumably

i. correlate that information with its own taxpayer records,

ii. ensure that the investor declares the income from the CIV in its home jurisdiction tax returns where appropriate, and

iii. inform the tax administration of the source jurisdiction if its records reveal that such investor is not in fact a resident of the residence jurisdiction and is therefore not entitled to claim tax treaty benefits pursuant to the tax treaty between the two jurisdictions.

The ICG does not contemplate that these proposals will be mandatory for financial institutions. If a financial institution chooses not to become an Authorised Intermediary, neither the financial intermediary nor the underlying investors, for which it acts, will be able to benefit from the simplified procedures – i.e. use of the Investor Self-Declaration etc.

Of note, if the Authorized Intermediary follows proper procedures but erroneously treats an investor as being entitled to reduced withholding rates (e.g., because the investor provided false information; or the investor erroneously claims treaty entitlement), the ICG proposes that the Authorized Intermediary will be strictly liable to refund the correct amount of tax to the source jurisdiction. We believe that there is some lack of balance within the proposals in that elements that would help an Authorised Intermediary manage such liability through the source country providing detailed guidance regarding treaty entitlement and tax rate information appears to be lacking. We recommend thought be given as to how such guidance could be given.

b. The US FATCA rules

FATCA imposes a regime under which investors who hold investment assets through financial institutions outside the source jurisdiction (in this case, the USA) will be subjected to the maximum withholding tax rate on their US sourced income, unless the financial institution voluntarily agrees to abide by the requirements in FATCA.

In the case of FATCA, to avoid full-blown reporting and onerous withholding on its own US source income, the overseas financial institution is required to enter into an agreement with the IRS to be treated as a qualified foreign institution investor (“QFII”) whereby it undertakes to comply with certain disclosure obligations vis-à-vis the IRS. In particular, a QFII is required to:

i. obtain information from each account holder necessary to determine which accounts are US-owned

ii. comply with certain verification and due diligence procedures with respect to the identification of US-owned accounts

iii. report annually certain information with respect to any US-owned account

iv. comply with requests by the IRS for additional information with respect to any US-owned account

v. withhold 30% from any “pass thru payment” that is made to (i) a “recalcitrant” account-holder, (ii) a non-QFII, or (iii) a QFII that has elected to suffer the maximum withholding tax with respect to the portion of payment allocable to a recalcitrant account-holder or to a non-QFII

vi. attempt to obtain a waiver in any case in which the foreign law would (but for the waiver) prevent the reporting of the required information required with respect to any US-owned account maintained by the QFII; if a waiver is not obtained, the QFII is obliged to close the account.

The reporting provisions will apply with respect to US-owned accounts maintained both by the QFII and by the non-QFII members of the "expanded affiliated group".

c. Significant differences between the two regimes

Although the ICG's proposals and FATCA apply in different factual circumstances, they have a common goal of facilitating the provision of information by financial institutions (and the subsequent exchange of such information with other tax administrations). Yet, in important areas of detail, the two proposals differ. Financial institutions are therefore potentially subjected to different requirements and obligations under these separate regimes.

By way of example:

i. A QFII may rely on certification received from an account-holder as to whether an account is a US-owned account, and as to the name, address and taxpayer identification number of each specified US person and substantial US owner, only if neither the QFII nor any entity that is a member of its expanded affiliated group knows (or has reason to know) that any information provided by the account-holder in the certification is incorrect. This is in contrast to the "strict liability" standard under the ICG's proposals with respect to CIVs.

ii. A QFII is subject to annual reporting requirements under FATCA. These oblige the QFII to report to the IRS, in addition to taxpayer identification details, the account balance or value, and details of the gross receipts and gross withdrawals or payments from the account. This is in contrast to the limited taxpayer information which an authorized intermediary will be obliged to automatically disclose under the ICG's proposals with respect to CIVs.

iii. A QFII is deemed to comply with the FATCA requirements if it has and complies with prescribed procedures to ensure that it does not maintain US accounts, and meets such other requirements as the Treasury Secretary may prescribe with respect to accounts of other QFIIs. A QFII may also be exempted from these requirements if the Treasury Secretary has determined that the requirements are not necessary to carry out the purposes of these provisions. The rationale behind this broad exemption is to reduce the burdens on those financial institutions who are clearly reputable and who have no track record of non-compliance. This is in contrast to the ICG's proposals which do not provide such safe harbors.

These examples show that, without any attempted coordination, different tax administrations will impose different standards for the provision of information. Financial institutions therefore will be required to establish different systems to deal with each of these different requirements. It would obviously be more efficient and less costly if the standards of information exchange were the same under both these and other routine provision of information regimes. Better coordination would also reduce the associated audit / review requirements and thus lower costs for financial intermediaries and by extension investors, consumers and the tax authorities.

4. Need for reconciliation of different information reporting regimes

The USA is the first tax administration that has taken extensive steps to impose information reporting obligations on foreign financial institutions, first through the Qualified Intermediary program and later under FATCA.

The purpose of this letter is to respectfully request the OECD to coordinate its proposals , and any future proposals with automatic provision of information provisions in other contexts, with the provision of information regimes imposed by tax administrations of OECD members , such as the USA , and non-OECD members, and regional bodies such as the European Union. The purpose of this would be to establish a uniform benchmark for jurisdictions to apply when seeking to gather routine information from financial institutions, and thereby ensure that the compliance burdens on financial institutions are reduced as far as possible, but still consistent with the objectives of such routine provision of information regimes.

5. Coordination of the ICG's proposals with FATCA

The ICG's proposals in their current form apply only to Authorised Intermediaries who would be required to report to the source jurisdiction, whereas FATCA involves all foreign banks who are required to report to the IRS. We submit that steps should be taken to meld the reporting components of these two systems together. Ultimately, both of these regimes have some similarities, and both of them are susceptible to standardization.

It would be very beneficial to coordinate their coverage and procedures, in order to avoid financial institutions being subjected to two separate sets of rules.

We have identified in part 3(c) above three fundamental ways in which the two regimes differ. Of course, the rules differ in numerous other ways, but those three differences are substantive and graphically highlight the concerns that our members have. These areas of divergence are all capable of being standardized.

To achieve uniformity between the two regimes, we would respectfully recommend, as a minimum, the following steps be taken.

i. *The ICG's proposal to impose strict liability on authorized intermediaries should be amended to the same "reasonable care" standard that applies under FATCA.*

   In other words, an Authorized Intermediary should not be liable to reimburse to the source jurisdiction any reduction in withholding taxes that has arisen in circumstances in which the Authorized Institution has taken reasonable steps to verify information about the investor and to satisfy itself that the provisions of the tax treaty between the source jurisdiction and the residence jurisdiction apply to the investor concerned.

   Whether such reasonable care has been taken could be the subject of review by the independent reviewer who will be required to investigate the Authorized Intermediary's compliance with the ICG's proposals.

   The rationale for our proposal is rooted in concepts of fairness and reasonable behavior. If the investor were dealing directly with the tax administration of the source jurisdiction to negotiate the application of a reduced withholding rate, false or otherwise incorrect information might be provided, and the tax administration might make a mistake despite having behaved quite correctly in the circumstances. To hold an Authorized

Intermediary to a higher standard and to make it personally liable in such circumstances is to effectively make it a guarantor for the investor. This seems unfair in situations where the Authorized Intermediary in acting only for the purpose of facilitating proper tax administration and where it derives no benefit from the reasonable mistake.

The CMTC believes that a "strict liability" standard is harsh and punitive, and frankly unrealistic. In today's compliance climate, financial institutions will always endeavor to take reasonable steps to ascertain the identities of their account-holders, just as Authorized Intermediaries will take reasonable steps to establish the identity of investors in CIVs, but it is harsh to impose a strict liability standard in these cases. FATCA adopts a "reasonableness" standard, and we urge the ICG to apply a similar standard.

ii. *The ICG's proposals should be amended to permit optional "two-way" reporting, both to the source and the residence jurisdiction.*

FATCA will require reporting to the US IRS of information in relation to US accounts located outside the United States. If the ICG's proposals were changed to permit optional simultaneous "two-way" reporting, then such a procedure (under which reporting could be made to the US IRS as a residence jurisdiction) could possibly provide a platform for the US Treasury and IRS, when writing regulations under FATCA, to limit the amount of information about US accounts that would otherwise need to be reported. (e.g., limiting the full details of all in-flows and out-flows relating to a US account). Permitting two-way reporting could provide a framework around which information could be provided in an efficient and effective manner and thus allow a better balance between the objectives behind these proposals and the concerns of financial institutions, without undercutting the goals behind the ICG's proposals and FATCA.

iii. *The ICG's proposal should be amended to permit source jurisdictions to exempt certain Authorized Intermediaries from compliance with the automatic reporting obligations where there are grounds to expect that the AuthorizedIintermediary is reputable and can be expected to comply with its obligations to verify the entitlement of investors in the CIV to tax treaty benefits.*

The rationale behind this proposal is simple. Imposing reporting obligations on trustworthy institutions is unnecessary and merely serves to increase the compliance burdens that financial institutions already face. Also, in the case of US investors, such information is already subject to regulation under FATCA. Limited spot check reviews may be a compromise solution acceptable to both government and to business.

6. Role of the OECD in achieving standardization

Whatever is the specific outcome, what the CMTC primarily seeks is consistency.

We accept that, at the moment, the FATCA and ICG proposals are limited and that each of these regimes applies in specific and different situations. However, it is inevitable that demands by tax authorities for the routine provision of information will increase over time, so it is necessary to "get it right" at the beginning rather than wait until financial institutions are subjected to a plethora of different provision of information reporting regimes. If this were to happen, inevitably the result

will be that, at some stage, steps will need to be taken to undo the problems that arise. In our respectful submission, it is important that the issue of standardization be addressed now, at an early stage, before it is too late.

Because of the OECD's unique position to seek a consensus among its members on tax administration issues and thus attain harmonization, it is appropriate for the OECD to lead this initiative. Tax administrations in various jurisdictions might also find it more palatable if they are seen to be imposing an internationally-accepted standard for the routine provision of information, rather than having each country formulate and impose its own rules.

At the end of the day, the only people who would lose under a standardized approach would be those people who are not properly disclosing their taxable income. From the perspective of the OECD, the tax administrations of the various countries concerned, the financial institutions that are at the forefront of providing information to tax administrations, and the investing public, standardization would be a win-win solution.

We therefore urge the OECD to expand its initiatives with respect to the enhancement of tax reporting and tax compliance in a systematic and standardized manner that alleviates the burdens on those institutions from which information will increasingly be routinely sought.

7. Timing issue

FATCA will come into force on 01/01/2013, and implementing regulations will be released shortly. It would therefore be helpful if the OECD could engage in dialogue with the US Treasury Department with respect to these issues as soon as possible.

Also, we expect that other jurisdictions are considering imposing similar types of reporting from foreign financial institutions. We further note that the European Union is considering proposals similar to that of the Implementation Package and again there may be some common reporting issues that should be considered now. The OECD is best placed to identify those jurisdictions concerned. We therefore urge the OECD to commence discussions with all such jurisdictions now in order to encourage uniformity and to seek a consensus for harmonization of routine provision of information procedures.

8. Final points

We are aware that the ICG's proposal is a voluntary one, in that intermediaries can decide not to sign an agreement with the source jurisdiction. We also note that FATCA is voluntary in that foreign financial institutions can decide not to enter into a QFII agreement with the IRS, and thereby subject themselves to the maximum US withholding tax rates.

That being said, the reality is that this is no answer to justify the lack of harmonization. As a practical manner, these provisions will de facto be mandatory, because customers of financial institutions will almost always seek to ensure that they receive the most advantageous rates under tax treaties to which they are entitled. In such circumstances, it is essential that a fair balance be struck and that, in return for financial institutions providing information, steps be taken to reduce their compliance burdens insofar as is consistent with the objectives of tax administrators in receiving pertinent information.

As you can see, the CMTC's membership comprises banks. Many of our members would also be Authorized Intermediaries under the ICG's proposals. Hence, the duplication of reporting regimes is a real issue to our members.

We emphasize that our request for standardization is not motivated by any desire to assist customers to evade their tax liabilities. Our members are willing to cooperate with tax administrations. We

are not particularly concerned about what the substance of routine provision of information requirements will be (within reasonable limits). Our concern, and what we seek on behalf of our members, is that reporting requirements be standardized to make our businesses more efficient and less costly.

We are very grateful for your attention in considering our submission. As we have discussed FATCA in this submission, we are also copying pertinent U.S. Government officials as you will see below.

We would of course be very happy to discuss these issues with you further should you wish. Please contact Archie Parnell, who is leading this particular CMTC effort, at +852-2978-1688. Archie's email address is archie.parnell@gs.com. I am currently the CMTC Chair and, as you will see below, can be reached at +852-3961-3356 and/or at james.badenbach@rbs.com.

Yours sincerely,

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