



The voice of banking
& financial services

NOTICE 2010-60, Notice and Request for Comments Regarding Implementation of Information Reporting and Withholding Under Chapter 4 of the Code ('the Notice')

1. The British Bankers' Association ("BBA") is the leading association for banking and financial services in the UK. We represent 230 banking organisations from 60 countries and have 40 professional service firms within our associate membership.
2. The BBA welcomes the opportunity to comment on the Notice and information reporting and withholding under Chapter 4 of the Internal Revenue Code ("FATCA"). We would, of course, be happy to clarify any points raised in these comments, or to discuss further any issues related to our understanding of the IRS's intentions. We look forward to continuing this dialogue and to further meetings at the appropriate stage.
3. The BBA re-affirms its commitment to transparency and openness in its dealings with the U.S. Authorities and the observations and comments that follow are provided in that light.

General Comments

Increased International Cooperation

4. The BBA's members understand the intention of the FATCA legislation, to combat evasion of U.S. taxes. The BBA and its membership will continue to pursue a highly cooperative approach with the U.S. Authorities to try to find an administrable way to reach FATCA's goal of identifying U.S. persons offshore. We offer the following comments and suggestions to assist the Treasury and IRS in establishing a regime that is consistent with the UK and EU's legal and regulatory framework, as set out in the DLA Piper opinion of 9 July 2010 ("DLA Piper opinion") which can be found at enclosure 1.
5. In the short term, the BBA proposes that some of the tensions highlighted by the DLA Piper opinion may be alleviated by expanding the existing scope for exception – refer to our comments at paragraphs 47 to 49 of this letter, and in particular paragraph 48.
6. In the longer term, we urge the U.S. and other nations to work towards an alternative global multilateral solution, where there would be reciprocal arrangements for all jurisdictions, and where information could be collected and exchanged between governments. We propose that consideration of a multilateral solution be an agenda item for upcoming meetings of the G20 since this is clearly an issue of international concern that requires a coordinated response.

Proportionality

7. BBA believes that if FATCA is to achieve its objective of maximizing the flow of usable information to U.S. tax authorities, the legislation must be guided by the principle of proportionality.
8. The principle of proportionality is embodied in the legislation. In a number of areas, the legislation provides the Secretary with discretion to grant exemptive relief to institutions, individuals, or payment types where the likelihood of tax evasion is low and/or where enforcement is unnecessary to achieve the objectives of FATCA. We consider that the

success or failure of FATCA will depend on making use of that flexibility to ensure that the compliance burden is proportionate.

9. We believe FATCA's goal of identifying U.S. persons investing offshore will only be achieved if the target Foreign Financial Institutions ("FFIs") and Non-Financial Foreign Entities ("NFFEs") participate in the new system and supply the data identifying their U.S. customers and owners. For most FFIs and NFFEs, the decision about whether or not to participate will essentially be based on commercial and economic considerations as to whether such participation is justified by reference to the costs, burdens and risks of complying with FATCA.

10. *IRS Question: Treasury and the IRS request comments on the issues addressed in this Notice and the priority of other issues that should be addressed in future guidance.*

BBA Answer:

Priority of Providing Future Guidance/Regulations

11. The BBA currently has some fundamental concerns relating to the operability of FATCA given the legal tensions noted above. However, in the expectation that the IRS/Treasury will resolve these tensions, although we are presently unsure as to how this will be achieved, we provide the following comments on the priority areas for future guidance/regulations. The BBA trusts that these comments will be useful to the IRS and Treasury in working with the financial services industry to facilitate implementation of FATCA.
12. Financial institutions will typically require a minimum period of eighteen months to develop and test systems changes of the breadth and coverage required by FATCA. The timelines for design, build, test and parallel performance run for any new system requires systems design work to commence no later than the end of the first quarter of 2011.
13. By the end of the first quarter of 2011, therefore, the BBA suggests that the priority of IRS/Treasury should be to advise FFIs of the requirements that define the scope of the legislation and will drive core aspects of the systems and process design. The BBA considers that the following requirements should be prioritised in guidance and that this guidance should be provided to intending participating FFIs by the end of the first quarter of 2011;
 - Confirmation of FFIs, NFFEs, beneficial owners and Financial Accounts excepted from FATCA.
 - Confirmation that an affiliated group can elect to report at the group, entity, branch or line of business/systems level. This could alleviate, inter alia, certain cross-border data protection issues.
 - Specific documentation requirements that an FFI would have to retain as evidence that a customer had been properly categorised under FATCA, the extent to which this may be satisfied by self-certification by customers (for example by way of modified Forms W-8 series and W-9 or other form of self-certification) and the extent to which this data will need to be electronically searchable.
 - Customer standing data for reporting (the BBA understands this will be limited to name, address and U.S. Taxpayer Identification Number) but it is vital that these data elements are clarified to facilitate system design requirements.
 - Handling of multiple-owner accounts, e.g. joint accounts (including partnerships, undesignated client accounts, clubs and societies, associations, cooperatives etc.).
 - Account information for reporting:
 - Confirmation of whether accounts held by the same customer within an entity of the FFI are to be aggregated or may be reported at an account level.

- Confirmation of what will constitute a receipt or withdrawal (but see comments at paragraph 92).
- Confirmation of account balance/valuation and currency translation rules (but see comments at paragraphs 86, 87 and 88).
- Confirmation of what could constitute “additional information” to be provided upon request to the IRS and for what period of time this information will need to be retained
- Clarification regarding re-examination requirements for determining whether average balances on existing accounts held by an account holder are less than \$50,000 and whether average balances on existing accounts exceed \$1,000,000 (but see comments at paragraph 65).
- Confirmation of any specific requirements for maintaining a record of customer communications and related information that may contain U.S. indicia.

14. Certain other requirements of FATCA will be more configurable in nature and may therefore be accommodated later in the process, by mid-2011. The BBA suggests that the following would fall into this second category:

- Format of electronic reporting of customer and account information to the IRS.
- Reporting deadlines.
- Requirement for, and scope of, reporting to the account holder or substantial U.S. owner (if any).
- Format of reporting amounts withheld where required on withholdable payments and arrangements for depositing the amounts withheld with the IRS.
- Formats of W-8 series and W-9 forms if amended from their current form and of other permitted self-certification of FATCA status by customers.
- Content of the FFI agreement.
- Ability of, and requirement for, a participating FFI to check an IRS register of participating FFIs to verify whether a customer is included.

Section I: Grandfathered Obligations

15. Such obligations comprise legal agreements that produce or could produce withholdable payments which are outstanding on March 18, 2012. However this does not include:

- equities
- legal agreements without a definitive expiration
- brokerage, custodial and similar agreements to hold assets on behalf of others and make and receive payments in respect of such assets

16. The BBA notes that the second bullet could create a distinction between fixed term bank deposits and other bank deposits. We question whether this is intended or desirable.

17. There is another important exception - where there is a “material modification” of an obligation, the obligation will be treated as newly issued on the effective date of such modification. For debt obligations, this would equate to a significant modification under 1.1000-3. The BBA would emphasise that the ability of issuers and information providers to distinguish on this basis will be crucial in terms of the ability of a participating FFI to comply.

Section II: FFIs and NFFEs

A. Definition of “Financial Institution”

18. Sub section 3 (page 7 of the Notice) refers, inter alia, to exchange traded funds falling under the definition of Financial Institution. However, this seems to run contrary to 1471(d)(2) which excepts equity or debt interests in a Financial Institution “which are

regularly traded on an established securities market” from the definition of Financial Account. The BBA would appreciate further clarification on this point.

19. The Notice states that it is contemplated that future guidance will provide guidelines for determining what types of activity, carried on in whole or in part, constitutes the business of investing, reinvesting, or trading, and when an entity is primarily engaged in such a business. A participating FFI will wish to eliminate any reputational, compliance or financial tax risk associated in complying with FATCA. It is unlikely to want to be in a position of having to make a potentially subjective determination in order to classify an entity as engaged primarily in the business of investing, reinvesting, or trading in securities.
20. As such we believe it is important that the entity in question should be responsible for this primary determination. Such an entity will be aware of the relevant facts and as long as appropriate guidance is issued that is clear and capable of practical implementation, it should be able to make the necessary relevant determination. We would suggest that the entity would evidence its determination by means of a self-certification or suitably modified W-8BEN or W-8IMY.

B. Entities Excluded from Definition of Financial Institution and/or Otherwise Exempt from Some or All of the Obligations Imposed by Chapter 4

21. Sub section 1 (page 9) provides that a foreign entity that otherwise satisfies the definition of a Financial Institution solely because it is primarily engaged in investing, reinvesting or trading in securities may be excepted where it falls within one of the described classes – certain holding companies, start-up companies (but only for the first 24 months), non-financial foreign entities that are emerging from reorganisation of bankruptcy or hedging/financial centres of a non-financial group.

22. *IRS Question: Treasury and the IRS request comments as to how the classes of entities discussed above may be more specifically defined in regulations, what mechanisms withholding agents could use to properly identify such entities (including self certification, as appropriate) and whether other classes of entities should be similarly excluded.*

23. **BBA Answer:** The above entities all seem fairly peripheral and it is difficult for us to determine how they can be more specifically defined in regulations. Given that a higher tier Financial Institution may not necessarily be in a position to make a definitive determination in this regard, a self certification or a suitably modified W-8BEN or W-8IMY would seem to be the most appropriate way of determining status. This should be accompanied by clear and unambiguous guidance to enable the entity to complete the relevant declaration. See BBA comments at paragraphs 47 and 48 for our suggestions in relation to other classes of entity that should be similarly excluded from the definition of Financial Institution.

Insurance Companies

24. Sub section 2 (page 11) proposes to except insurance companies when whose business consists solely of issuing contracts without cash value (e.g. property and casualty insurance).

25. *IRS Question: Treasury and the IRS request comments with respect to the appropriate treatment under chapter 4 of entities that issue cash value insurance contracts, annuity contracts, or similar arrangements, and with respect to the appropriate definition of cash value insurance contracts, annuity contracts and similar arrangements for this purpose.*

26. **BBA Answer:** The intention of the Notice would appear to be to except “classical” insurance business while ensuring that insurance business that is essentially equivalent to mutual funds is included. However, it is not clear whether insurance companies neatly fall within one or the other of these two categories. There are likely to be a number of insurance companies that run both types of business and would therefore not be excluded by virtue of the “solely” test. The BBA considers that the exception should be extended to mixed business insurance companies, to the extent that the assets relate to non cash value products. We also believe that cash value products should be given the benefit of any exceptions that may subsequently be afforded to ordinary mutual funds. We suggest that definitional points are best taken up with the insurance industry.

Entities with Certain Identified Owners

27. Sub section 3 (page 12) proposes that a foreign entity that meets the definition of a Financial Institution solely because it is primarily engaged in investing, reinvesting or trading in securities be treated as a deemed-compliant FFI if the withholding agent (i) specifically identifies each individual, specified U.S. person, or excepted NFFE that has an interest in such entity, either directly or through one or more other entities, (ii) obtains required documentation from each such person as if the person were a new account holder or direct payee of the withholding agent, and (iii) the withholding agent reports required details in relation to such person. An example of such an entity may be a small family trust.

28. *IRS Question: Treasury and the IRS request comments as to whether certain small FFIs should be required, for purposes of applying chapter 4, to be treated as NFFEs, regardless of whether withholding agents currently determine the direct and indirect owners of such entities for purposes of complying with local law or regulatory obligations.*

29. **BBA Answer:** If a distinction is to be drawn between “small” FFIs and other FFIs, then “small” has to be clearly – and practically – defined; for example, is it by reference to the value of U.S./total investments, the number of U.S./other persons etc.? Additionally, what happens if there is a change in circumstances by reference to the relevant criteria from one year to another?

30. The BBA considers that it may be more appropriate not to distinguish between “small” entities and other entities, in the same way as size is not a criterion for NQIs that furnish details of underlying beneficial owners.

31. The BBA considers that this proposal is a step in the right direction but it may be of limited application. For example, it could not extend to a discretionary trust with no clear set of beneficiaries. There may also be differences in the interpretation of beneficial ownership under the law in the country in which the trust is established and U.S. law. In addition, similar to the situation for NQIs, there may be a reluctance to enter into such arrangements on the part of upper tier Financial Institutions. Accordingly, and for the avoidance of doubt, the use of such arrangements must be subject to agreement by the “small” FFI and the upper tier Financial Institution.

32. To the extent that an upper tier Financial Institution is willing to enter into such arrangements, the necessary information should be derived by means of a self certification or a suitably modified W-8BEN or W-8IMY from the “small” FFI.

33. The BBA would emphasise that in the UK trusts are a very broad category, including but not limited to: trust administrator companies; collective investment vehicles e.g. investment trusts and unit trusts; family trusts; pension funds etc. Furthermore, it should be noted that the trustees are deemed the owners of the income for tax purposes unless

the beneficiaries receive the income as an immediate and absolute right, such as in the case of bare trusts and interest in possession trusts. Under the U.S. model, trusts are determined to be either grantor (where the settlor is the "owner"), simple (where the beneficiaries are the owner), or complex (where the trust itself is the owner). It would appear to us to be difficult to make the types of UK trusts fit the U.S. model. We are aware that there are similar problems in other trust jurisdictions.

34. We would urge the U.S. Authorities to be advised by the Society of Trust and Estate Practitioners on these points.

Financial Institutions Organized in U.S. Territories

35. Sub section 4 (page 13 of the Notice) proposes that a Territory-Organised Financial Institution will not generally be treated as an FFI. Rather, a Territory-Organised Financial Institution acting as intermediary may confirm that it is acting as a U.S. withholding agent and a Territory-Organised Financial Institution that meets the definition of a Financial Institution solely because it is primarily engaged in investing, reinvesting or trading in securities may be treated as a NFFE.

36. The BBA considers that as a higher tier Financial Institution may not necessarily be in a position to make a definitive determination with regard to the position of a particular Territory-Organised Financial Institution, a self certification or a suitably modified W-8BEN or W-8IMY would seem to be the most appropriate way of determining status and potentially securing any further required information.

C. Retirement Plans

37. The Notice proposes that payments beneficially owned by retirement plans will be exempt from withholding where the retirement plan (i) qualifies as a retirement plan under the law of the country in which it is established, (ii) is sponsored by a foreign employer, and (iii) does not allow U.S. participants or beneficiaries other than employees that worked for the foreign employer in the country in which such retirement plan is established during the period in which benefits accrued.

38. *IRS Question: Comments are requested on the definition of a retirement plan for this purpose, and on how such a plan could appropriately identify or document itself to a withholding agent to verify its compliance with any such definitional requirements. In addition, comments are requested as to whether other categories of foreign employee benefit or deferred compensation plans should be subject to the same treatment as foreign retirement plans for chapter 4 purposes.*

39. **BBA Answer:** The conditions at (i) to (iii) are unnecessarily restrictive. Condition (i) does not take into account various national pension scheme arrangements often established, but not necessarily funded, by Governments to enable individuals to save for their retirement. The BBA considers that the criteria here should be expanded accordingly. Condition (ii) would exclude retirement plans operated for employees of UK branches of U.S. banks (and other organisations) as there is not a "foreign employer", even though the retirement plan would be regarded as an entirely separate (and UK resident) legal entity from the plan sponsor. And condition (iii) would seem to disqualify a retirement plan where there is a U.S. dependant "beneficiary", such as a spouse, partner or child, linked to an employee covered by the plan and would likely be incapable of application. We suggest that the suggested expanded criteria at condition (i) should be sufficient to qualify a retirement plan for this exception.

40. We believe that a self certification or a suitably modified W-8BEN would be the most

appropriate way of determining status.

41. We also believe that this exception should be extended to foreign pension fund pooling vehicles - see BBA letter dated 27th April 2010 ("BBA letter"), which can be found at enclosure 2 [point 3], regulated/authorised foreign personal pension plans and foreign share plans (including any such plans operated through a foreign branch of a U.S. company for the benefit of the employees of the foreign branch).
42. We understand that the Association of British Insurers will be commenting further on this point and we may wish to supplement these comments at a later stage.

D. Treatment of Certain Other Classes of Entities

U.S. Branches of FFIs

43. Sub section 1 (page 16 of the Notice) proposes that a U.S. branch of a Foreign Financial Institution would be excepted from withholding in the case of effectively connected income and would be permitted to document its account holders for Chapter 4 withholding purposes under the requirements to be imposed on U.S. Financial Institutions where it acts as an intermediary. Coordinating rules are anticipated to relieve duplicative reporting stemming from separate FFI and U.S. reporting requirements.

44. *IRS Question: Comments are requested as to other possible rules or methods that withholding agents could use to determine the application of the ECI exclusion.*
45. **BBA Answer:** We are not clear as to why a U.S. branch should generally be treated as an FFI, as it will already be subject to U.S. reporting and withholding rules. We believe that the existing ECI exclusion should be retained. We believe that a self certification or a suitably modified W-8BEN or W-8IMY would be the most appropriate way of determining status.

General Comments

46. *IRS Question: Treasury and the IRS request comments concerning the treatment under section 1471 of the entities described above, as well as the treatment of other foreign entities, including, for example, any foreign charitable organizations that may fall within the definition of an FFI. In particular, Treasury and the IRS request comments providing specific suggestions for defining and identifying specific classes of foreign entities that should be: (i) excluded from the definition of FFI; (ii) deemed to meet the requirements of section 1471(b) pursuant to section 1471(b)(2); or (iii) identified as posing a low risk of tax evasion pursuant to section 1471(f).*
47. **BBA Answer:** We believe that a foreign charitable/not for profit organisations qualifying under the law in which it is established (e.g. registered with the UK Charities Commission) should be excluded from the definition of FFI, as well as investment vehicles utilised by charities – see BBA letter [point 3].
48. We believe that the following types of FFI should be deemed to meet the requirements of section 1471(b) pursuant to section 1471(b)(2)(B):
 - FFIs that are (a) subject to comprehensive reporting and (b) established in a country that (i) has entered into a tax treaty containing an exchange of information clause or tax information exchange agreement with the U.S. and (ii) is regarded by the U.S. as actively complying with exchange of information requirements, perhaps by reference to the Global Forum criteria - see BBA letter [point 1.5]

- Widely held CIVs - see BBA letter [point 1.7].

49. Please also refer to our comments at paragraphs 74 and 80, in respect of NFFEs (i) in treaty/exchange of information agreement countries and (ii) engaged in active trade or business, respectively.

50. We consider that such FFIs and NFFEs are best identified by means of a self certification or a suitably modified W-8BEN or W-8IMY.

51. We would propose that non interest bearing current/checking accounts be excepted from the definition of Financial Account on the basis that these accounts do not produce withholdable payments and hence pose a low risk of tax evasion. In the UK, our members have tens of millions of such retail accounts and the current proposals would result in a significant administrative burden and cost. This is particularly so where an FFI elects not to apply the \$50,000 threshold. Additionally, we would argue that individuals and clubs and societies holding money transmission accounts and on demand savings accounts pose a low threat of tax evasion given the extremely low returns generated on these accounts.

Section III: Collection of Information and Identification of Persons by Financial Institutions Under Sections 1471 and 1472

52. This section covers general procedures for documenting and categorising accounts. It raises a number of issues and some specific questions which we highlight/respond to below.

B. Participating FFIs

53. The BBA believes that it will be important to manage the practical implications attached to potential verification of participating FFIs from a list (page 37 of the Notice), particularly so far as changes (additions/deletions) to that list are concerned. We have identified the following possible mechanisms for such management:

- electronically searchable on-line database with recent changes posted to a separate IRS website page. Participating FFIs would be required to check the latter website page at regular intervals (say no less frequently than quarterly).
- e-mail notification facility whereby e-mails are dispatched to participating FFIs as and when the list is updated.

54. Participating FFIs would be reliant upon the accuracy of the IRS database and should not be liable for any errors arising from that reliance.

Pre-existing Individual Accounts

55. **Thresholds:** The BBA understands that the \$50,000 threshold applies to each FFI legal entity rather than being aggregated across all of the Affiliates within the group. Although this would be a forward step, there are significant practical and regulatory obstacles where the FFI has within a single legal entity multiple lines of business, systems and countries of operation. For example:

- the systems used by certain lines of business may not be capable of computing average values as those businesses may not customarily provide valuations of non-cash assets.
- the sharing of certain information across national borders will create regulatory issues.

- the aggregation of data across jurisdictions and disparate line of business systems may represent a disproportionate development due to lack of common customer identifiers and the relatively limited likelihood of common customer relationships subsequently being identified.
 - the requirement to convert values into U.S. dollars will create problems, particularly where exchange rates fluctuate during the year and values are close to the threshold level - but see our comments at paragraph 87.
56. It is therefore helpful to have the option not to apply the \$50,000 threshold. In order to maximise the possibility of this threshold being utilised, the BBA urges that separate elections should be capable of being made on the \$50,000 threshold for, and that there should be no requirement for an FFI to aggregate data across, different business lines/ systems and jurisdictions in recognition of the issues mentioned above. If such disaggregation is not possible, then the BBA would suggest that the current \$50,000 threshold be substantially increased for those participating FFIs that are able to apply it.
57. The BBA notes that the thresholds apply to “depository accounts”. However, this term is not defined. We assume that it encompasses deposit accounts and securities accounts but it is important for this to be confirmed (or otherwise).
58. The BBA interprets the Notice as meaning that the \$1,000,000 threshold is applied on a non-aggregated basis – i.e. it applies at the level of each account and not as an aggregation of all accounts held by the account holder as stated for the \$50,000 threshold. See further comments at paragraph 64 regarding two year/five year requirements.
59. **Electronically searchable information:** It is helpful that the principle of electronic searches has been accepted for pre-existing accounts. We believe that this is the only practical alternative for such accounts. We also believe that it is clear that electronically searchable information is confined to structured data held on databases and does not extend to all information that is stored in electronic format.
60. **Indicia of potential U.S. status:** For accounts containing indicia of potential U.S. status, the FFI must obtain Form W-9 (category i), Form W-9 or Form W-8BEN and documentary evidence (category ii & iii), or Form W-9 or Form W-8BEN or documentary evidence (category iv, v & vi).
61. Where there is an indication of U.S. residence or citizenship (category i), the requirement to obtain Form W-9 is absolute. The BBA considers that there should be an option for the individual to be able to establish non-U.S. status and for the FFI to correct its records in this regard.
62. Where there is a sole address that is an in care of / hold mail / P.O. address (category iv), this triggers a requirement to secure Form W-9 or W-8BEN or documentary evidence in order to determine status. The BBA would point out that there are certain jurisdictions where the only address in existence is a P.O. address and requests therefore that if the account holder is resident in such a jurisdiction and the sole address is a P.O. address there should be no requirement, in the absence of any U.S. indicia, for the FFI to secure any further documentation or documentary evidence from the customer in order to determine status.
63. The BBA considers that an alternative of an ad-hoc certification should be available so that customers with U.S. indicia who are not invested in U.S. securities do not have to complete Form W-9 or Form W-8BEN, consistent with the BBA letter [point 4.1].

64. **Two/five year requirement:** The ability to alleviate the two and five year requirements to subject pre-existing individual accounts not treated as U.S. accounts to the procedures for new individual accounts depends, inter alia, on the FFI holding satisfactory documentation or documentary evidence, respectively, and status being reflected in electronically searchable form. Therefore, the net result is that within five years, all pre-existing accounts will be subject to the procedures for new individual accounts unless the FFI has maintained documentary evidence to establish their status. Where the FFI has elected not to apply the \$50,000 threshold, this would necessitate re-papering every account within five years, regardless of whether or not U.S. indicia is present.
65. The basic documentation/classification requirement is extensive and the BBA does not consider that the further two/five year requirements can be justified in terms of the additional cost and administrative burdens that they would create. The BBA urges that they be replaced with the application of a “reason to know” standard where further information subsequently comes to light, perhaps as a result of further periodic electronic searches of pre-existing accounts.

New Individual Accounts

66. **New account relationship:** If for any reason an existing customer establishes a new account relationship, the FFI must treat them as a new customer. It is not clear whether this impacts new accounts of a similar type to existing accounts. For example, if an existing pound sterling cash account holder opened a pound sterling fixed cash deposit, would this constitute a new account relationship? What if that customer opened a euro cash account? The BBA believes that further guidance is required in terms of what is meant by new account relationship. We would suggest that a new account relationship is formed when the customer is obliged to enter into a new contractual agreement with the FFI in relation to a particular product offering that has not previously been provided to that customer.
67. **Threshold:** See comments in relation to the \$50,000 threshold at paragraphs 55 and 56 and further comments at paragraph 69 below regarding the reapplication requirement.
68. **Indicia of potential U.S. status:** Our comments at paragraphs 60 to 63 in respect of pre-existing accounts also broadly extend to new accounts.
69. **Reapplication requirement:** There is a possible requirement to reapply the procedures for accounts that are treated as other than U.S. accounts by virtue of the \$50,000 threshold where the account subsequently exceeds that threshold for a later year. The BBA considers that the wording of the Notice is somewhat ambiguous as to whether this threshold should be applied on an aggregated basis or at the level of each account and would appreciate confirmation of this point. We consider that the system programming complexities attached to the requirement to continue to compute and track account values and convert to U.S. dollars is likely to encourage many FFIs to opt not to apply the initial \$50,000 threshold for new accounts.

Pre-existing Entity Accounts

70. **Electronically searchable information:** It is helpful that the principle of electronic searches has been accepted for pre-existing accounts. We believe that this is the only practical alternative for such accounts.
71. **Potential report of FFIs providing documentation indicating participating FFI status but no FFI EIN:** The BBA would emphasise the importance of being able to verify participating FFI status, refer to our previous comments at paragraphs 53 and 54.

72. **Active trade or business:** As noted in our response at paragraph 80, the BBA generally welcomes the possibility of excepting companies that are involved in an active trade or business. However, we note that there is currently an obligation for the FFI to check whether there is evidence to support the categorisation of an entity account holder as being engaged in an active trade or business. The BBA believes that FFIs should have the option not to invoke this check, so that entity account holders are deemed not to be involved in such trade or business.

73. **Transitional periods:** The further transitional periods of one/two years (pages 34, 35, 36, 38 & 39 of the Notice) to secure documentation are welcomed.

74. **Identification of specified U.S. persons with interest in NFFE:** The Notice proposes that in the case of an NFFE other than an excepted NFFE, the FFI must specifically identify each individual, and each other specified U.S. person that has a direct or indirect interest in such entity (subject to certain exceptions). If a specified U.S. person is identified, the FFI should treat the account as a U.S. account and obtain with respect to each such U.S. person the documentation that the participating FFI would be required to obtain from such person if such person were a new account holder and report the specified U.S. person to the IRS. This requirement overturns the statutory requirement at 1472(b) (see page 41 of the Notice), which targets substantial U.S. owners of an NFFE rather than each individual that has an interest in the NFFE. The BBA is concerned by this extension of scope, which we feel would be unmanageable in many cases, and therefore should be reversed. We consider that the IRS/Treasury should instead be considering ways to reduce the burden. For example:

- Substantial U.S. owners ownerships levels should be revised to 25% or any alternative percentage required under relevant AML/KYC requirements - see BBA letter [point 4.3].
- A payment that is made to a NFFE that is established in a country that (i) has entered into a tax treaty containing an exchange of information clause or tax information exchange agreement with the U.S. and (ii) is regarded by the U.S. as actively complying with exchange of information requirements should be regarded as a class of payment identified as posing a low risk of tax evasion under section 1472(c)(2) - see BBA letter [point 2].

75. We would emphasise that a UK FFI cannot report a customer without the customer's specific authority or a change in UK law - see the BBA letter [point 4.4] and DLA Piper opinion.

76. *IRS Question: Treasury and the IRS also request comments regarding the development of presumptions on which a participating FFI could rely to determine whether a U.S. person is a specified U.S. person.*

77. **BBA Answer:** We would reiterate the suggestion made in the BBA letter [point 4.2] that any U.S. person should be deemed to be a specified U.S. person unless there is evidence (such as a self-certification or modified Form W-9) to the contrary.

78. The BBA considers that an FFI should be entitled to rely on self-certification or modified Form W-9.

79. *IRS Question: Treasury and the IRS request comments about the level of evidence that should be sufficient to establish under step 4(a) that an entity is engaged in an active trade or business, as well as ways in which step 4(a) can be structured to ensure that it is not subject to abuse.*

80. **BBA Answer:** The BBA welcomes the possibility of an FFI being able to treat an entity as an excepted NFFE based on evidence on the entity's account file that it is engaged in an active trade or business (other than an FI business). The BBA additionally believes that this exception should be extended to unincorporated account holders that are similarly engaged in an active trade or business (other than an FI business). With regard to the level of evidence required, we consider that in the absence of a satisfactory self-certification or suitably modified W-8BEN form, the FFI may rely on any information in its possession, including that which is obtained from external sources (provided its provenance is recorded and can be verified) that confirms that an entity is engaged in an active trade or business.

New Entity Accounts

81. The Notice anticipates that the procedures for new entity accounts will be similar to those for pre-existing accounts, except that reference must be made to all information collected by the FFI for AML/account maintenance purposes, not just information available in electronically searchable files. Consequently the comments at paragraphs 71, 72 and 74 also apply. The issue set out at paragraph 74 is of particular concern.

82. *IRS Question: Treasury and the IRS request comments regarding appropriate procedures for identifying participating FFIs, deemed-compliant FFIs, nonparticipating FFIs, entities described in section 1471(f), excepted NFFEs, and other NFFEs from among new account holders of USFIs.*

83. **BBA Answer:** The BBA considers that categorisation should be based on self-certification or suitably modified Forms W-8BEN or W-8IMY.

Section IV: Reporting on U.S. Accounts

84. This section covers proposed arrangements for the provision of relevant information on U.S. accounts. It raises a number of questions and some further issues which we address below.

Account Balance or Value

85. *IRS Question: Comments are requested regarding the above approaches, and regarding other potential approaches that may provide adequate information in a manner that will be administrable by participating FFIs without being subject to manipulation by U.S. account holders. Comments on possible currency translation conventions are requested. Comments on specific situations in which foreign laws may prevent the reporting of the information described above are also requested, along with descriptions of the steps that would be required of a participating FFI (and account holders of U.S. accounts maintained by the FFI) in order to overcome or waive any such restriction.*

86. **BBA Answer:** The BBA believes that "non-core" data such as balance/value should be reported on specific request and on reasonable notice - refer to BBA letter [point 5.5]. This would also be consistent with the proposed approach in relation to the additional account related information referred to on page 49 of the Notice.

87. BBA members have a number of concerns in relation to currency translation conventions, which vary according to the relevant systems structure. Therefore, we consider that a flexible approach should be adopted:

- it would be appropriate not to mandate the use of U.S. dollars but to allow an FFI to

report in the currency of the transaction or account or the currency used for its local financial and tax reporting purposes.

- it would be proportionate to allow FFIs to use existing currency conversion methodology
- it would be prudent to additionally provide specific prospective IRS rates on a calendar year basis for each currency for those FFIs that choose to convert from source country currency to U.S. dollars.

88. The BBA also believes that the highest balance/highest value requirement would be a significant challenge for banks, with varied impact according to the relevant systems structure that is in place. We believe that a non-prescriptive approach would be most effective, allowing participating FFIs to compute balance/value on any reasonable basis.

89. Refer to BBA letter [points 4.1 and 4.4] and DLA Piper opinion regarding UK law tensions in relation to the reporting of customer information. We believe such tensions would be best resolved by means of a multilateral solution, as set out in our general comments at the head of this letter.

90. In certain other jurisdictions, the BBA understands that the reporting of certain customer data to U.S. regulators, or sharing of this data otherwise outside the jurisdiction concerned, is not permitted under local regulations, even where explicit customer consent has been obtained. The BBA understands that specific permission from the local regulator is required in some such jurisdictions to enable this data reporting/sharing, and that in at least one instance, this permission is believed to be unlikely to be given. Further investigations are being carried out in the jurisdictions concerned. The BBA would urge the IRS/Treasury to consider deeming the provisions of FATCA not to apply to operations in such jurisdictions, where an FFI has requested but been denied local regulator permission to report/share this data cross border, pending resolution of the conflict of FATCA with local legislation.

Gross Receipts and Withdrawals

91. *IRS Question: Treasury and the IRS request comments as to how to minimize burdens on participating FFIs with respect to such reporting.*

92. **BBA Answer:** The BBA believes that “non-core” data such as gross receipts/withdrawals should be reported on specific request and on reasonable notice - refer to BBA letter [point 5.5]. This would also be consistent with the proposed approach in relation to the additional account related information referred to on page 49 of the Notice.

Section 1471(c)(2) Election

93. *IRS Question: Treasury and the IRS request comments regarding whether and in what circumstances a participating FFI should be permitted to make the election with respect to a subset of its accounts without making the election for all of its accounts (for example, whether a participating FFI should be permitted to make the election with respect to accounts held by individuals without requiring that the FFI make the election with respect to accounts held by entities).*

94. **BBA Answer:** The BBA considers that as a practical matter this election should be made according to line of business and associated system capability.

95. The BBA would appreciate IRS/Treasury clarification as to whether cost basis reporting is envisaged under the participating FFI arrangements.

Elimination of duplicative reporting

96. The BBA considers that as a general principle reporting responsibility should rest with the financial institution immediately before the investor. We would point out that it is debateable whether, in the case of the specific example given in the Notice, the fund would know who the end investor is. It is likely that in these specific circumstances only the custodian, acting for the investor, would be in a position to report.

Reporting with Regard to Recalcitrant Accounts

97. The BBA believes that the requirements for a participating FFI to report the number and aggregate value of financial accounts held by recalcitrant account holders and the number and aggregate value of financial accounts held by related or unrelated nonparticipating FFI are a positive feature and compatible with the proposition made in the BBA letter [point 4.4].

Section V: Request for Specific Comments

98. This section raises a number of residual questions and one further issue which we address below.

99. *IRS Question: Treasury and the IRS request comments about the procedures performed by public accountants or other external auditors when conducting an AML/KYC audit or similar engagement, including information about the objectives of such engagements, the types of procedures performed, and the types of reports issued as part of such engagements. In addition, Treasury and the IRS are exploring the possibility of relying in some circumstances on written certifications by high-level management employees of the applicable financial institution regarding the steps taken to comply with chapter 4. Treasury and IRS request comments on the information and representations that should be included in such certifications and the extent to which public accountants or other external auditors rely on written certifications of compliance provided by officers or other responsible management employees of the applicable financial institution in the course of AML/KYC audits or similar engagements. Treasury and the IRS request comments concerning the extent to which the format of reports associated with such engagements could be appropriately modified to further compliance with chapter 4. Treasury and the IRS further request comments as to the extent to which public accountants would be able to perform, consistent with their attestation or other accounting standards, verification procedures and reporting with respect to FFIs under engagements that are not agreed-upon procedures.*

100. **BBA Answer:** BBA members have considered the various alternatives in great detail – our conviction is that the only practical option is self-certification based on the existing controls and tests already employed by regulated FFIs.

Treatment of Passthru Payments

101. *IRS Question: Comments are requested as to methods that a participating FFI could use to determine whether payments it makes are attributable to withholdable payments, including any associated information reporting that may be necessary, and which take into account the administrative burden imposed by any such approach.*

102. **BBA Answer:** The BBA is concerned that an unconnected financial institution will have insufficient information in relation to a particular payment in order to determine whether

that payment is attributable to a withholdable payment and therefore should be treated as a 'passthru payment'. We consider that this is a systemic problem for which there is no readily identifiable solution and is potentially a major disincentive to become a participating FFI.

Election to be Withheld Upon

103. **IRS Question:** *Treasury and the IRS have received comments regarding the administrative challenges that may be raised by an election under section 1471(b)(3). Comments are requested as to the appropriate scope of such an election. In particular, comments are requested as to the types of financial accounts for which such an election should be available. In addition, comments are requested as to the type of information reporting an electing FFI would need to provide to a withholding agent so that the appropriate amount of tax could be deducted and withheld from any withholdable payments or other passthru payments made to the electing FFI.*

104. **BBA Answer:** The BBA has previously identified the challenges associated with an election under section 1471(b)(3) in the BBA letter [point 5.4]. If these challenges cannot be satisfactorily resolved, this issue is likely to remain academic. However, there seems to be no obvious reason to distinguish between types of financial accounts. We believe that information reporting mechanisms are likely to be determined according to the systems in place between the two parties concerned; therefore specific prescription is unlikely to be helpful – it should simply be sufficient that the reporting enables the appropriate amount of tax to be deducted.

Sanctions With Respect to Recalcitrant Account Holders

105. **IRS Question:** *Treasury and the IRS request comments on what measures should be taken to address long-term recalcitrant accounts, including whether, and in what circumstances, Treasury and the IRS should consider terminating FFI Agreements due to the number of recalcitrant account holders remaining after a reasonable period of time.*

106. **BBA Answer:** The BBA is concerned that the Notice emphasizes that the IRS considers that applying withholding should not be a permanent substitute for collecting and reporting information with respect to U.S. accounts. We believe that in practice the vast number of "recalcitrant" account holders will be non-U.S. investors invested in non-U.S. accounts with no nexus with the United States (and therefore no understanding of the requirement for them to satisfy the FATCA requirements) and with no local law obligation to cooperate with a participating FFI seeking the relevant information.

107. As previously noted by the BBA, the current FATCA requirements create tensions with UK and European Union law, including the ability of a participating FFI to deny account facilities to customers that have otherwise satisfied local regulatory requirements - see BBA letter [point 4.4 – last sentence before Executive Summary] and DLA Piper opinion. Consistent with our general comments at the head of this letter, we are strongly of the view that the U.S. Treasury should work towards a multilateral solution, so that there is then a domestic legal requirement for account holders to comply. We fear that without such a solution, the BBA's member banks will be placed in the invidious position of being able to comply with either their home state law or that of FATCA, but not both.

FFIs Subject to Restrictions Prohibiting U.S. Account Holders

108. **IRS Question:** *Treasury and the IRS thus request further comments on the following:*
- (1) specific information about the applicable laws and regulations that may result in an investment vehicle's determination to prohibit sales of its interests to U.S. persons;*
 - (2) the categories of investment vehicles that may be covered by such laws and regulations;*
 - (3) examples of the distribution or similar agreements that prohibit sales of interests to U.S. persons;*
 - (4) information regarding the legally binding nature of such prohibitions and the penalties applicable to a violation of such prohibitions;*
 - (5) the extent to which the AML/KYC laws used to enforce such a prohibition would apply in identifying U.S. persons (as defined for U.S. tax purposes) that may invest in such vehicles, directly or through ownership in one or more other entities;*
 - (6) the extent to which purchases of interests by non-participating FFIs would be treated as unsuitable investments and the extent to which and mechanisms by which non-participating FFIs could be prohibited from purchasing such interests; and*
 - (7) approaches that would allow Treasury and the IRS to verify or otherwise ensure compliance with such prohibitions.*

Treasury and the IRS are also considering whether such requirements or similar factors are an appropriate basis for applying section 1471(b)(2)(A) to other types of investment vehicles or FFIs.

109. **BBA Answer:** The BBA considers that this is principally a matter for the fund management industry.

Electronic Filing Requirements for Financial Institutions

110. The Notice reflects the intention of IRS/Treasury to require most financial institutions to file their returns electronically (both in respect of FATCA and QI).
111. The BBA is concerned that a compulsion to file returns in electronic form may dissuade smaller financial institutions from becoming a participating FFI.

Application of Chapter 4 by U.S. Withholding Agents Other than USFIs

112. **IRS Question:** *Treasury and the IRS contemplate permitting U.S. withholding agents other than USFIs to rely on a foreign entity's certification as to its classification for chapter 4 purposes, absent reason to know that such certification is unreliable or incorrect. These requirements would also apply with respect to withholdable payments made by FFIs and USFIs to NFFEs that are not holders of financial accounts maintained by the financial institution. Treasury and IRS request comments on the form of such certifications, their renewal provisions, and circumstances under which a withholding agent should not be required to solicit such certifications from certain classes of persons or with respect to certain classes of payments, such as arm's-length payments made for goods or services in the ordinary course of the withholding agent's trade or business.*

113. **BBA Answer:** The above fact pattern is not relevant to BBA members and consequently the BBA offers no comments.

114. **IRS Question:** *Treasury and the IRS also anticipate providing an exception in guidance to the withholding required under section 1472 for payments made to an NFFE engaged in an active trade or business by withholding agents other than financial*

institutions. Comments are requested regarding the appropriateness of such an exception, how a withholding agent may determine whether an NFFE is engaged in an active trade or business, and other exceptions to withholding under section 1472 that may be appropriate.

115. **BBA Answer:** The above fact pattern is not relevant to BBA members and consequently the BBA offers no comments.

Potential Modifications to Chapter 4 Requirements Based on Availability of Information from Other Sources

116. **IRS Question:** *Treasury and the IRS intend to consider approaches that will help minimize the burden on participating FFIs. For example, Treasury and the IRS are considering whether to exempt a participating FFI from the obligation to perform withholding on passthru payments to individual recalcitrant account holders where reporting by the participating FFI to the IRS is sufficient to permit the IRS to obtain information about the identities of those recalcitrant account holders through an information exchange request to a foreign jurisdiction. Treasury and the IRS solicit comments on possible approaches to reduce the burden imposed on participating FFIs by chapter 4.*

117. **BBA Answer:** The BBA would not regard information exchange requests as being a proper systemic basis for the provision of information in relation to recalcitrant account holders. We fear this would be a cumbersome solution, not only for the participating FFIs but also for the tax authority in the FFI's country of operation, which apparently would not benefit from a reciprocal arrangement. As noted above, FATCA presently creates a number of conflicts with UK and European Union laws; we are also cognisant of similar legal concerns in other jurisdictions. These conflicts could be alleviated if the U.S. were to consider certain existing tax information reporting regimes, for example the European Union Savings Directive. The optimum approach may be for the U.S. to work towards an alternative global multilateral solution as set out in our general comments at the head of this letter. Please also refer to the BBA letter [conclusion].

Friday 29 October 2010
British Bankers' Association

Our ref

British Bankers' Association
Pinners Hall
105-108 Old Broad Street
London
EC2N 1EX

UKM/30316914

F.A.O: Sarah Wulff-Cochrane

9 July 2010

Dear Sirs

FOREIGN ACCOUNT TAX COMPLIANCE ACT PROVISIONS

1. INTRODUCTION

- 1.1 DLA Piper UK LLP ("**DLA Piper**") have been instructed by the British Bankers' Association ("**BBA**") to provide an opinion relating to various provisions of the *Foreign Account Tax Compliance Act* ("**FATCA**") that have been incorporated into the *Hiring Incentives to Restore Employment Act* ("**HIRE**") (Pub. L. No 111-147) signed into law by President Obama on 18 March 2010. We have noted the comments submitted by the BBA on 27 April 2010 to Messrs Shay, Musher and Danilack and to Ms Corwin.
- 1.2 Our opinion seeks solely to set out certain legal constraints imposed upon foreign financial institutions ("**FFIs**") in the UK, rather than to comment on any of the considerably more numerous practical constraints. The legal constraints arise principally in relation to the identification of "US owned accounts" (hereinafter referred to as "US Accounts"), reporting and associated procedural issues.
- 1.3 The provisions of FATCA relevant to this opinion can be summarised as follows:
- 1.3.1 an obligation to withhold 30% of "withholdable payments" is imposed on all FFIs¹;

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A limited liability partnership registered in England and Wales (number OC307847) which is a law firm and part of DLA Piper, an international legal practice.

A list of members is open for inspection at its registered office and principal place of business, 3 Noble Street, London, EC2V 7EE and at the address at the top of this letter. Partner denotes member of a limited liability partnership.

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¹ A "withholdable payment" is broadly defined to include *inter alia* any payment of interest (including original issue discount), dividends, rents, salaries, wages, premiums, annuities, compensations, remunerations, emoluments and other fixed or determinable annual or periodical gains, profits and income from sources within the United States; interest paid on deposits by non-US branches of US banks and gross proceeds from the sale or other disposition of US stocks and securities.



- 1.3.2 withholding is not required if an FFI enters into an agreement with the Internal Revenue Service ("IRS") in the US to be treated as a "qualified FFI" and complies with certain disclosure obligations, which include (but are not limited to) the following:
- 1.3.2.1 **obtaining information from each account holder necessary to determine which accounts are 'US-owned accounts'**² (*emphasis added*);
 - 1.3.2.2 complying with certain verification and due diligence procedures with respect to the identification of US-owned accounts;
 - 1.3.2.3 reporting annually certain information with respect to any US Account;
 - 1.3.2.4 withholding 30% from any "passthru payment" that is made to a recalcitrant account holder³, a non qualified FFI or a qualified FFI that has elected to be withheld upon with respect to the portion of a payment allocable to a recalcitrant account holder or a non qualified FFI; and
 - 1.3.2.5 attempting to obtain a waiver in any case in which any foreign law would (but for the waiver) prevent the reporting of the information required with respect to any US-owned account maintained by the FFI; if a waiver is not obtained then the qualifying FFI is required to close the account.
- 1.3.3 These provisions will apply in respect of any US-owned accounts maintained both by a qualified FFI and by FFIs who are members of the same "expanded affiliated group (unless the affiliated FFI has its own agreement with the IRS)"⁴.

² *i.e.* a financial account held by one or more Specified US persons or US-owned foreign entities. The term "financial account, except as otherwise provided by regulations, means (1) any depository account maintained by the FFI, (2) any custodial account maintained by the FFI and (3) non-publicly traded debt or equity interests in the FFI. The qualified FFI may rely on certification received from an account holder as to whether an account is a US-owned account, and the name, address and TIN of each specified US person and substantial US owner based on due diligence procedures to be provided by regulations; for example, such regulations might require that an FFI may rely on an account holder's certification only if neither the qualified FFI 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).

³ *i.e.* an account holder that: (i) fails to comply with reasonable requests for information necessary to determine if the account is a US owned account; (ii) fails to provide the name, address, and TIN of each specified US person and each substantial US owner of a US-owned foreign entity; or (iii) fails to provide a waiver of any foreign law that would prevent the qualified FFI from reporting any requisite information.

⁴ An expanded affiliated group is an affiliated group where as a general rule there is a common ownership of more than 50%. A partnership or any other entity that is not a corporation is treated as a member of an expanded affiliated group if the entity is controlled by members of the group.

2. IDENTIFICATION OF US ACCOUNTS

2.1 New account holders

- 2.1.1 It is anticipated that FFIs will need to ask prospective account holders not simply for confirmation of their nationality or citizenship (as many US born individuals have acquired British nationality without relinquishing their US nationality) but also specific questions as to their state of tax residence and nationality. This would be a retrograde step in the light of current UK regulations and policy concerning customer due diligence ("CDD") which specifically do not require information of this nature.
- 2.1.2 UK money laundering regulations adopt a risk based approach to CDD, enabling individual banks to design a proportionate control framework according to the nature of the risk that their customers, products or distribution channels may pose.
- 2.1.3 CDD measures must be applied when a new banking relationship is established. The legislation does not prescribe what documentation should be used to identify the customer or the methodology of validation. In some cases, third party databases and credit scoring techniques are used to validate information given by the customer.
- 2.1.4 In relation to "wholesale" accounts, banks need to identify the key parties to the account and the beneficial owners of 25% or more of the legal entity account holder. It is not necessary to identify beneficial owners where their interest is as little as 10%.
- 2.1.5 Banks are entitled to rely on the CDD performed by a third party, providing that party is regulated and has given consent.
- 2.1.6 Further information may be sought from prospective customers for sound administration. This might typically include telephone numbers, date of birth, passport or driving licence numbers, occupation and marital status. Generally, however, other than by certain private banks, the place of birth or nationality is not specifically requested.
- 2.1.7 As place of birth or nationality data is not specifically required under UK legislation, it is currently a matter of judgment for each FFI whether to accept the customer's mandate and establish the relationship, in light of whatever information is provided.

- 2.1.8 As part of a current political initiative, it is proposed that every individual in the UK should have the right of access to basic banking facilities and that account opening procedures, subject to the key CDD requirements of identification, should be simplified to facilitate this. UK FFIs fear that, if and when the proposal is enacted, they will no longer be able to exercise judgment as to whether to refuse to open an account if, for example, the prospective customer fails to answer a question or provide evidence as to nationality/place of birth, or fails to provide the requisite authorisation to disclose account holder details, etc., to the IRS. UK FFIs may be legally obliged to open an account without knowing if it is a US Account.

2.2 Existing Account Holders

- 2.2.1 It is our belief that very few UK FFIs have captured any data that would enable them to identify US Accounts within their customer base, easily or at all. In passing, it should be noted that there was no regulatory requirement to identify beneficial owners of trust or corporate accounts prior to 15 December 2007.
- 2.2.2 It should also be noted that the trustees of a trust account are regarded as the account holders of the FFI in the UK. UK FFIs will frequently not know the identity or details of settlors, beneficiaries or potential beneficiaries. Whilst they may ask the trustees to provide details of any US settlor or beneficiary, the trustees are not obliged (and may be unable) to respond.
- 2.2.3 Whilst UK FFIs could issue letters to customers asking for details of their nationality or place of birth, and authorisation to disclose this information to the IRS if it indicates a US Account, they have no effective sanction if the customer fails to respond or provide the relevant authorisation.
- 2.2.4 Having accepted the customer's mandate on the basis of whatever information, undertakings or documentation was provided at the time, the bank has a fiduciary duty to hold the customer's deposit and provide banking facilities and services as set out in the contract between the parties.
- 2.2.5 A bank in the UK has no authority or right to withhold tax on behalf of a foreign government; it is solely authorised to withhold an amount representing tax at the basic rate in the UK and accounts for this on a quarterly basis to Her Majesty's Revenue and Customs ("HMRC") pursuant to UK legislation. In certain, specified circumstances (such as those contained in s.866 of the *Income Tax Act 2007*), accounts held by various categories of customer that have provided relevant documentation or are held on specified terms, must have any interest credited without the deduction of tax.

- 2.2.6 If any UK FFI sought to levy a charge based on the quantum of interest paid and not in relation to the costs of operating the account, the Financial Services Authority ("FSA") would undoubtedly take action to prevent this and in all likelihood would penalise the FFI.
- 2.2.7 We note that the 'passthru' provisions⁵ have not been tested in the courts. Apart from the likelihood that they will be legally impossible to enforce in the UK, it may be that the initiating FATCA legislation is also ineffective in other jurisdictions.
- 2.2.8 Without the consent of the customer, a UK FFI can only close accounts in certain limited circumstances:
- 2.2.8.1 if the customer has breached the terms of the mandate, the FFI can refuse to continue banking services.
 - 2.2.8.2 in bankruptcy, the account is frozen until evidence of the trustee in bankruptcy is received.
 - 2.2.8.3 on notification of death, the account is frozen until evidence of probate is received.
 - 2.2.8.4 on divorce and upon receipt of a Court Order, the account may be frozen or the terms altered to require both parties' signature.
 - 2.2.8.5 the *Proceeds of Crime Act 2002* and the Joint Money Laundering Steering Group ("JMLSG") guidance require disclosure where there is knowledge, suspicion, or reasonable grounds to know or suspect money laundering or attempted money laundering. The FFI nevertheless does not immediately close the account.
 - 2.2.8.6 the *Dormant Bank and Building Society Accounts Act 2008* provides for balances to be transferred to the reclaim fund, following which the FFI has no obligation to the former customer.

⁵ whereby income paid by a UK FFI may be deemed to be a withholdable payment to the extent that the FFI has itself received a withholdable payment and hence is subject to the FATCA withholding provisions for recalcitrant account holders.

2.2.9 Accordingly, without the express or implied consent of a customer, a UK FFI cannot unilaterally close an account or withdraw from the relationship without a UK Court Order or unless required to under specific UK legislation.

3. LEGAL CONSTRAINTS ON REPORTING

3.1 Under UK law, a UK FFI owes its customers a contractual duty of confidentiality as established in the Court of Appeal case of *Tournier v National Provincial and Union Bank of England*⁶ ("*Tournier*"). This duty extends beyond information relating to the actual state of the customer's account to cover all information acquired by the bank in its role as such. The confidence therefore applies to any and all information relating to the customer, the customer's account and his transactions with the bank.

3.2 This duty of secrecy is not absolute and is qualified by four defined 'reasonable exceptions' under which a bank *is* permitted to divulge information about a customer's account, namely:

3.2.1 the bank is compelled to do so by law;

3.2.2 the circumstances give rise to a public duty of disclosure;

3.2.3 the protection of the bank's own interests requires it; and/or

3.2.4 the customer agrees to the information being disclosed.

3.3 This duty and its exceptions are now enshrined in both the *Banking Code* and the *Business Banking Code*. In order for a UK FFI to disclose information about a customer, one of these exceptions must apply.

3.4 Compulsion by law

3.4.1 The application of the first exception in relation to foreign laws was explored in the case *FDC Co Ltd v Chase Manhattan Bank NA*⁷. In this case, the Hong Kong Court of Appeal held that the compulsion had to stem from the law governing the relevant account. In that instance, a compulsion to disclose under US law was not seen as sufficient to trigger the exception and allow the FFI to breach its duty of confidentiality.

3.4.2 Accordingly, in the absence of any UK law requiring such disclosures, the provisions of FATCA will not allow UK FFIs to breach their duty of confidence to their customers without the application of one of the other exceptions.

⁶ [1924] Kings Bench 461

⁷ (1984) unreported, Hong Kong CA

3.5 Duty to the Public

- 3.5.1 This exception is to be interpreted as applying only in very limited circumstances. For example, the giving of information to the police with regards to a customer suspected of a crime (beyond the statutory duties of disclosure for example under anti money laundering legislation, which will qualify under the first exception) would not be covered by this exception.
- 3.5.2 It has also been held in the courts that the public interest in preserving confidentiality between UK FFIs and their customers is subject to being overridden by the greater public interest in making confidential documents relating to the alleged fraud of an international bank available for the purposes of uncovering that fraud. However, this has not yet been applied in practice and such disclosures would be limited to what is reasonably necessary to achieve the purpose of the public interest disclosure⁸.
- 3.5.3 The requirement that all UK FFIs disclose information pertaining to any US-owned accounts as part of an ongoing campaign against international tax evasion by the US government is highly unlikely to satisfy this criteria and thus qualify under this exception.

3.6 Protection of the banker's own interests

- 3.6.1 This exception applies in situations such as a statement in a writ or legal pleadings of the amount of a customer's overdraft and would not apply in relation to disclosure requests pursuant to FATCA.
- 3.6.2 With disclosure requests pursuant to FATCA incapable of falling under the first three exceptions, UK FFIs will not be able under UK law to disclose information relating to the ownership of a customer's account (as required by FATCA) except to the extent that the fourth 'exceptional circumstance' applies, *i.e.* unless they have consent from the customer to do so.

3.7 Conflict of Laws

- 3.7.1 The provisions of FATCA require that in any case in which any foreign law would prevent the reporting of required information (in this instance, the fact that a particular account held at a UK FFI is US-owned), an FFI must attempt to obtain a waiver. If a waiver is not obtained, FATCA requires the FFI to close the account.

⁸ *Pharaon v Bank of Credit and Commerce International SA (in liquidation)* [1998] 4 All ER 455

- 3.7.2 Accordingly, in order to comply with the disclosure requirements under FATCA (and to avoid the imposition of a withholding charge, itself of questionable legal application: see paragraph 2.2.5 above) UK FFIs would be required to seek consent from all customers believed to have US-owned accounts in order to report this fact to the IRS.
- 3.7.3 If UK FFIs failed to obtain such a consent, they would be required under FATCA to deny those customers account facilities (*i.e.* they would be required to close the accounts).
- 3.7.4 However, as set out at paragraphs 2.2.8 to 2.2.9 above, a UK FFI may be unable to do this in accordance with UK law.
- 3.7.5 This leaves UK FFIs in an impossible position to the extent that UK law will prevent them complying with the requirements of FATCA (either by disclosing personal data about its customers in the first instance or denying them account facilities in the second) unless they can obtain consent to do so.
- 3.7.6 With reference to the related but separate provision at section 6038D of FATCA requiring yearly disclosure in relation to foreign financial assets, failure to disclose due to 'reasonable causes' avoids the usual penalty (see subsection (g)). However, the same section specifies that the fact that a foreign jurisdiction would impose a civil or criminal penalty for disclosing the required information is *not* considered a reasonable cause. Although the disclosure requirements under section 1471 do not necessarily go as far in their definition of what will constitute compliance, s.6038D serves as a stark illustration of the onerous impact that FATCA is apparently intended to have on FFIs, and the extent to which they will be expected to comply with its provisions.

3.8 **Data Protection Act 1998**

- 3.8.1 In addition to the duty of confidence established in *Tournier*, UK FFIs must also comply with the *Data Protection Act 1998* ("**DPA**"). This Act regulates the processing of personal data (defined as information which alone, or in conjunction with other information in the possession of or likely to come into the possession of, the data controller, identifies a living individual). Processing is widely defined in the DPA and includes the obtaining, holding, use, deletion or disclosure of such information.

3.8.2 The DPA provides the following obligations in relation to the processing of personal data:

3.8.2.1 The First Data Protection Principle provides that personal data must be processed fairly and lawfully and must not be processed unless one of a number of legitimising grounds are present. The available grounds, which are set out in schedule 2 of the DPA, are where:

- (a) the data subject has given his or her consent to the processing;
- (b) the processing is necessary for the performance of a contract to which the data subject is a party, or for taking steps to enter into a contract;
- (c) processing is necessary to comply with a legal obligation, other than one arising under contract;
- (d) the processing is necessary for certain public purposes, such as the administration of justice; or
- (e) the processing is justified if it is 'necessary for the purposes of legitimate interests pursued by the data controller or by third parties to whom the data are disclosed, except where the processing is unwarranted in a particular case by reason of prejudice to the rights and freedoms or legitimate interests of the data subject.

3.8.2.2 In the case of sensitive personal data (data relating to a person's physical or mental health, religious or political views, trade union membership, sexual life, commission or alleged commission of offences and associated proceedings), one of the grounds in schedule 2 of the DPA must be present, together with one of the grounds in schedule 3. The grounds in schedule 3 are narrower than those in schedule 2 and do not include the wide ranging "legitimate interest" ground referred to in paragraph 3.8.2.1(e) above.

- 3.8.2.3 As well as requiring legitimising grounds to be identified, the First Data Protection Principle also requires data subjects to be given what is known as fair processing information, that is, the name of the data controller, the purposes for which the data is processed, and any other information needed in the circumstances to ensure that the processing is fair (*e.g.* disclosures of the data which will be made). This is normally achieved through the "data privacy notice" provided to customers when the account is opened.
- 3.8.2.4 The Second Data Protection Principle requires that personal data must be obtained for specified purposes and used only in ways compatible with those purposes. If a data controller wishes to use the data for purposes other than those which are compatible with those originally specified, consent from the data subject must be obtained. The purposes for which the data are processed can be "specified" in two ways. This information can either be included in the fair processing information required to be given under the first principle, or it can be included in the notification which the data controller must file with the Information Commissioner's Office ("**ICO**"), the authority which is responsible for the enforcement of the DPA.
- 3.8.2.5 Personal data must also be adequate, relevant and not excessive in relation to the purpose for which the data are processed; it must also be accurate and, where necessary, kept up to date; and it must not be kept longer than is necessary for the specified purpose or purposes for which it is lawfully required.
- 3.8.2.6 Any disclosure of personal data must take account of the right of the 'data subject' (*i.e.* the customer in this instance) to object to processing likely to cause damage or distress.
- 3.8.2.7 Appropriate security measures are to be taken against unauthorised or unlawful processing and against accidental loss. This includes the requirement to ensure contracts with service providers handling the data contain appropriate provisions regarding the handling of personal data.

- 3.8.2.8 The data processor, or other third party commits an offence if he knowingly or recklessly obtains or procures or discloses personal data without the consent of the data controller.
- 3.8.2.9 The Eighth Data Protection Principle states that personal data must not be transferred to a country outside of the European Economic Area ("EEA") unless that country provides an adequate level of protection for personal data. A small number of countries have been certified as providing an adequate level of protection for personal data (known as the white listed countries). In order to transfer data to other non-EEA countries without infringing the DPA, the transfer may be made subject to a set of binding contractual clauses approved by the European Commission (known as the model clauses). In the case of transfers to the US, transfers can be legitimately made to recipients who have signed up to the Safe-Harbor programme. Other transfers are only legitimate if they fall within one of the permitted exemptions contained in Schedule 4 of the DPA.
- 3.8.2.10 All data controllers which are established in the UK and which process personal data in the context of that establishment, or which are not established in the UK or any other EU country but which use equipment in the UK for the processing of personal data, unless for transit purposes only, are required to notify their data processing to the ICO. A limited number of exemptions apply to the notification requirement.
- 3.8.3 The DPA makes no provision for a UK FFI to avoid its duty of confidentiality, or its duties to process personal data fairly and lawfully, even if required to do so under foreign law. Further, the DPA specifically limits the instances where a UK FFI can pass any personal data to the US, and establishes that a UK FFI would be vulnerable to legal sanctions in the event that it disclosed personal data in certain circumstances without a customer's consent.

4. CONCLUSION

4.1 The provisions of FATCA present various and serious legal challenges for UK FFIs.

4.1.1 In the first instance, they would require UK FFIs to take retrograde, and highly onerous, steps in light of current UK regulations in relation to due diligence procedures relating to new customers;

4.1.2 In relation to existing account holders, following any failure on the part of a customer to supply the relevant information, it is at best doubtful whether the UK FFI would be able under UK law to either:

4.1.2.1 withhold tax on behalf of the US government; and/or

4.1.2.2 unilaterally withdraw from the relationship without a UK Court Order;

as required under FATCA.

4.1.3 Further, even if a UK FFI has access to the relevant information, UK law then places a duty of confidentiality on the FFI (through common law and the DPA) preventing the disclosure of this information without the account holder's consent.

4.2 UK law may therefore prevent UK FFIs from complying with various provisions of FATCA. The corollary of is that they may have no alternative but to disinvest in US securities and disassociate themselves from relevant counterparties. In turn, this may of course have unintended consequences in the US that may far outweigh any perceived benefits in relation to the mischief that FATCA was intended to address.

Should you have any queries in relation to the contents of this letter or generally, please do not hesitate to contact Mr Simon Airey or Mrs Aileen Barry of this office who will be happy to assist.

Yours faithfully



DLA PIPER UK LLP