

[TEXT OF THE FATCA POSITION PAPER SUBMITTED BY CEA]

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Position Paper

CEA's response to IRS consultation on Implementation of
Foreign Accounts Tax Compliance Act

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Related CEA documents:

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Summary

The CEA, the European insurance and reinsurance federation, appreciates providing comments as requested by the U.S. Internal Revenue Service (IRS) and U.S. Treasury (Treasury) about the new reporting provisions under the recently enacted Foreign Account Tax Compliance Act (FATCA) provisions as included in the Hiring Incentives to Restore Employment Act, Pub. L. 111-147. The CEA would like to use this opportunity to suggest practical approaches for insurers to achieve compliance.

The CEA, which is based in Brussels, represents all types of insurance and reinsurance undertakings, including pan-European companies, monoliners and mutuals, through its 33 members, the national insurance associations.

The CEA understands that insurance companies may be included in the concept of "Foreign Financial Institution" (FFI) as defined under FATCA. Although insurers do not fit squarely within the definition of FFI, the Technical Explanation prepared by The Joint Committee on Taxation states on page 44 that *"It is anticipated that the Secretary may prescribe special rules addressing the circumstances in which certain categories of companies, such as insurance companies, are financial institutions, or the circumstances in which certain contracts or policies, for example annuity contracts or cash value life insurance contracts, are financial accounts or United States accounts for these purposes."*

In this paper, the CEA seeks to explain the practical difficulties in application of the FATCA rules to some insurance products and the demanding regulatory rules that are imposed currently on the insurance sector. In particular, the CEA seeks to explain why Property and Casualty (P&C) insurers and reinsurers should be excluded from the definition of FFI, and that any application of FATCA to life insurers should be narrowly and carefully tailored, due to the practical difficulties in application of the rules to life insurance products. The CEA recognises that the key objective of the FATCA requirements is to expose tax evasion, therefore whilst drafting the implementing rules the IRS and the Treasury should be mindful of whether achievement of this objective necessitates the collection of data in a particular instant. In instances where the FATCA requirements could be deemed to apply, we urge IRS and Treasury to consider whether this objective necessitates the enormous administrative burdens that may be incurred for minor additional tax revenue. Our recommendations are as follows:

1. Foreign P&C insurers, reinsurers and health insurers should be excluded

P&C insurers, or non-life insurers, provide insurance policies under terms where a payment occurs only if the risk covered occurs (e.g., the insured's building suffers earthquake damage). Apart from policies issued for home and auto coverages to individuals, P&C policies are issued to companies and businesses. P&C products do not operate in any sense like investment accounts where premiums can be refunded with an enhanced value for investment returns. Returns of premiums usually are net of significant insurer imposed costs or penalties, along with reduced or terminated risk coverages.

Reinsurers (both life and non-life) are accepting risks ceded by an insurer or another reinsurer. Reinsurance allows insurers by facilitating a wider distribution of risks at worldwide level, to have a higher underwriting capacity to engage in insurance business and provide insurance cover and also to reduce their capital costs. These operations are exclusively business to business transactions. Individual policyholders are in no way affected by reinsurance as the insurer remains liable to the policyholder for insurance policy benefits and claims.

P&C insurance and reinsurance should not be assimilated into FATCA as they do not generate revenue owned by US policyholders. Thus, these products do not present a risk of tax evasion. P&C policies cover risks associated with the occurrence of fortuitous event where policy claims are subject to detailed review by the insurers prior to payment, and claim payments reimburse policyholders for losses those policyholders have already incurred. These factors make it extremely unlikely, if not impossible, for US policyholders to effectively employ P&C policies as a vehicle to escape US tax. Therefore, the CEA believes treatment of P&C insurers and reinsurers as FFIs under new Internal Revenue Code sections 1471(d)(4) and (5) would be inappropriate.

The same applies to health insurers.

The CEA notes the discretion granted in section 1471(b)(2)(B) for the Secretary to determine a "*class of institutions with respect to which the Secretary has determined that the application of this section is not necessary to carry out the purposes of this section.*" As foreign P&C insurers, reinsurers and health insurers present no risk of tax evasion, the CEA recommends these institutions to be designated as a class of institution under section 1471(b)(2)(B) and as such should not be subject to any FATCA reporting requirements.

2. Foreign Life Insurers should only be included from 2013 onwards and in certain circumstances

The Technical Explanation accompanying the FATCA provisions noted that "*It is anticipated that the Secretary may prescribe special rules addressing circumstances in which certain contracts or policies, for example annuity contracts or cash value life insurance contracts, are financial accounts or United States accounts for these purposes.*"

The CEA believes that the FATCA rules, as written, are very broad and as a result could place an extremely large cost on the life insurance industry in return for a modest tax revenue increase. While some life insurance policies could come under the FATCA rules, we are concerned that achieving compliance before the effective date of January 1, 2013 may be extremely difficult, especially given the broad scope of the new rules.

For policies effective from January 1, 2013 and thereafter, we provide several suggestions aimed at reducing the concerns of the life insurance industry that we believe also would help the U.S. government to obtain useful information.

A) Exclude reporting on existing policies

The CEA is very concerned by the potential application of FATCA reporting to life insurance policies issued prior to 2013. To include these contracts in the FATCA scope would mean recovering and verifying information included in hundreds of millions of insurance contracts.

The systematic confirmation of the data at stake as required by the FATCA rules would place a disproportionate administrative burden on the industry with only minor tax revenues for the U.S. government. The CEA believes it is doubtful that the information necessary to identify a U.S. taxpayer was collected as part of the intake process for all life insurance policies, in particular for those policies entered into prior to FATCA's enactment. Considering the disproportionate

burden at stake, the CEA suggests exempting life insurance policies issued prior to 2013 from the FATCA reporting obligations.

B) Require reporting only when insurers make payments

Life insurance policies are normally long-lasting contracts that have been subscribed to on an extended basis. Until now, foreign life insurance companies had no obligation to collect and report information to the IRS. The CEA believes it is doubtful that the information necessary to identify a U.S. taxpayer was collected as part of the intake process for all life insurance policies, in particular for those policies entered into prior to FATCA's enactment. A more practical approach would be to require the reporting obligation triggered by significant insurer payments to the policyholder. We believe that insurance companies would have the best information about the identity of the policyholder when such payments are made.

C) Consider legal liability issues for foreign life insurers

European data protection rules could pose serious obstacles to disclosing policyholder information, which, if not addressed properly, may expose insurers to substantial legal liability issues. This is particularly the case for contracts issued in the past which do not explicitly refer to such possibility.

D) Grant insurers more time to respond to FATCA reporting

The complexities of the new reporting system mean that it is unlikely that foreign life insurers will be prepared to implement even a more modest reporting obligation in so limited time. We highly recommend extending the deadline for FATCA compliance for insurance companies for at least another one to two years beyond 2013. This would permit the insurance industry time to work with IRS and Treasury to help craft appropriate reporting guidance.

E) Exclude certain policies posing no risk of tax evasion

The CEA believes that even from 2013 onwards certain life insurance policies should not come under the FATCA scope as they pose no risk of tax evasion.

i. Payments upon death ~ exclude

Policies under which payments are made exclusively upon death of the policyholder should be excluded from the FATCA scope as they are not comparable with the targeted financial accounts. These policies entail classic risk coverage where insurers do not make payments unless their insureds die.

**ii. Group life insurance and group annuity policies
~ exclude**

Group life insurance and group annuity policies should be excluded from the FATCA scope. These policies are issued to companies or groups of companies. As these policies neither entail financial (i.e., non-insurance) elements nor individualised cash values that could qualify them as a Foreign Accounts, they should be excluded from the FATCA scope.

iii. Policies with a cash conversion value ~ not exceeding \$ 50,000 ~ exclude

To the extent that IRS and Treasury are concerned about policies with a cash conversion value, we recommend that Treasury apply the same \$ 50,000 threshold to such policies that would be applied to "U.S. accounts" in Section 1471(d)(1)(B). Accordingly, reporting would only be required where the reporting value exceeds \$ 50,000. We also recommend the drafting of clear and easy to apply rules for insurers to calculate the U.S. dollar value of such policies.

F) Consider challenges imposed by Solvency II ~ outline a delayed and phased FATCA compliance approach

Finally, we recall that the FATCA effective date of January 1, 2013 is particularly problematic for the European insurers as this is also the target date to implement the new solvency rules (Solvency II capital rules). Once these rules are issued, the European Insurers' priorities will turn to implementing new IT compatible systems thus compromising the IT resources available. For these reasons, the CEA recommends a delayed and phased FATCA compliance approach.

4. Consolidated FFI election (affiliated groups)

Many of our members are multi-national groups, and therefore, they are concerned about the affiliation approach. In this respect, the CEA fully supports the recommendations filed April 23 by the European Banking Federation (the "EBF") and the Institute of International Bankers (the "IIB"), at page 17 of their FATCA comments letter to you, "that (1) an electing FFI should be able to specify at the time of its election whether the election extends to other members of its worldwide affiliated group, and (2) to the extent specified by the FFI, this election extend to any entities formed, controlled or sponsored by the FFI (. . .). If an FFI indicates that it will file a consolidated FFI annual report on behalf of its group, then all

members of the FFI's worldwide group would be presumed covered unless the FFI specifies which entities or categories of entities it does not intend to cover in its reports." They also recommended that the guidance "permit various entities, divisions or locations within the affiliated group to file separate annual reports and should not require the consolidation of information that is gathered from separate data systems onto a single report.