

[TEXT OF THE FATCA COMMENT LETTER SUBMITTED BY  
GERMAN BANKING INDUSTRY COMMITTEE]

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**Re: FATCA**

Berlin, 05-10-2011  
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Ref. DK: USQ  
Ref. BdB: ST.20.02 - Sk/Gg

Dear Ms. Corwin and Messrs. Danilack, Musher and Caballero:

The German Banking Industry Committee (“Die Deutsche Kreditwirtschaft”) is the joint committee operated by the central associations of the German banking industry. These associations are the Bundesverband der Deutschen Volksbanken und Raiffeisenbanken (BVR), for the cooperative banks, Bundesverband deutscher Banken (BdB), for the private commercial banks, the Bundesverband Öffentlicher Banken (VOB) for the public-sector banks, the Deutscher Sparkassen-und Giroverband

(DSGV), for the savings banks, and the Verband der Pfandbriefbanken (vdp), for the Pfandbrief banks. Collectively, we represent more than 2,300 banks.

We are contacting you again prior to the announced issuance of proposed regulations implementing the Foreign Account Tax Compliance Act (FATCA) in order to highlight areas in which we believe action is especially essential. In particular, we would like to draw your attention also to some important special features of the German financial market environment.

We appreciate the difficult task facing the IRS/Treasury in promulgating these regulations and hope that the issues highlighted in this letter will be helpful in the process.

### **1. Passthru Payment and Passthru Payment Percentage**

It is understood that one of the purposes of the concept of passthru payments is to encourage FFIs to enter into FFI agreements even if the FFI in question does not directly hold assets that produce withholdable (i.e., US source) payments. The passthru payment rule is designed to prevent the circumvention of withholding by the interposition of a “blocker entity” especially to address payments that are attributable to withholdable payments.

Some of the key concerns raised by this concept include the following:

- Application of the concept to active businesses such as banks, as opposed to more passive vehicles such as investment funds, creates conceptual as well as practical problems. Furthermore, it is important to note that USFIs are not required to withhold on passthru payments, notwithstanding the fact that it would appear possible to use a USFI as a “blocker” with similar effect.
- To the extent that the PFFI determines that withholding or termination of a business relationship is required under FATCA, it may be subject to legal risks if the affected party has contractual or other grounds (such as local statutes) to contest the decision and/or to seek reimbursement.
- The proportional asset allocation approach for determining payments that are attributable to withholdable payments will be extremely complex to apply, particularly in the case of large integrated financial groups with multi-tiered structures. Accurate implementation will require detailed and timely guidance from the IRS and at least a central database introduced by

the IRS. As proposed, the passthru payment percentage (“PPP”) calculation requires financial information which may be difficult to obtain and which will necessarily be subject to complicated calculations and adjustments to avoid a cascading effect.

- Because of the apparent broad application of the concept across the global financial system, it will compel FFIs that have no connection with the US (either direct or indirect) to participate. As a result, businesses which present a low risk in terms of US tax avoidance will nonetheless bear the high cost of participation.
- The law itself does not contain definitions which limit the scope of certain key terms. In the absence of detailed guidance from the IRS, withholding will apply to a variety of financial products and transactions in an unintended manner that does not advance the stated objectives of the law.
- Taking into account the issues briefly outlined above, implementation of the passthru payment concept as it currently stands will result in additional stress and disruption to the global financial system with the inherent risk of a diminution in the holdings of US assets, the total costs of which are impossible to estimate.

## **2. Deemed Compliant Status Requirements-local banks and local FFI members**

The concept of the deemed compliant status is highly appreciated. The German banking sector regards this approach as a core element in reducing the onerous burden of FATCA compliance.

Being “deemed-compliant”, however, requires that a local bank or a local FFI member of a participating FFI group neither maintain business activities nor solicit account holders “outside its country of organization”. This approach is inconsistent with the “EU Passport Concept”, which allows a bank to be licensed in one country yet provide services throughout the European Union. A constructive definition of “local” should also allow for cross-border relationships, these being just as common within the EU or the European Economic Area as it is between the fifty states of the USA. Geographic limitations on business activities beyond the exclusion of US clients would make it more or less impossible for the vast majority of German local banks, as well as subsidiary FFIs of a German parent PFFI to obtain the “deemed compliant status”.

We therefore propose that geographical limitations be either removed generally from the definition of deemed compliant status or expanded to the European Economic Area (i.e., the member states of the European Union plus the four member states of the European Free Trade Association). Moreover we recommend for compliance purposes (i) a one-time due diligence upon entering into the agreement of the DCFFI and (ii) a certification of respective internal policies and processes after their implementation on a regular basis.

### **3. Existing IT Infrastructure / PFFI Group Aggregation**

It is imperative that disproportionate (IT) expenditures be avoided, i.e. FATCA specific requirements must principally be implementable within existing heterogeneous IT landscapes, particularly in a cross-border context.

For purposes of determining the balances or values of the pre-existing accounts an FFI will be required to treat as a single account all accounts maintained by the FFI or its affiliates that are associated with one another due to partial or complete common ownership of the accounts. This means that in principle, it requires the aggregation of accounts across legal entities and regions to the extent that the accounts have common ownership ~ either partial or complete common ownership ~ and treating them as a single account. However, in *Notice 2011-34* it was confirmed that this aggregation into a single account is only required if it can be accomplished under the FFI's existing computerized information management, accounting, tax reporting, or other recordkeeping systems. To the extent that is not the case, the accounts must be analyzed separately and individually under the tests contained in *Notice 2011-34*.

The clarification in *Notice 2011-34* does not answer the question of whether FFIs are still required to aggregate accounts for purposes other than the numerical tests. We understand the clarification, however, as an acknowledgement of the heterogeneous IT landscape within banks and a recognition of limiting the costs and burdens. We kindly ask you to support this understanding of the Notice's clarification with further examples.

### **4. Conflicts of Law**

It is essential to address situations in which FATCA requirements and relevant compulsory national law(s) would result in a conflict.

The most obvious potential legal conflicts are: (i) national data protection laws conflicting with FATCA reporting requirements, (ii) national public and/or civil laws conflicting with the requirement to terminate certain customer relationships and (iii) national civil law(s) conflicting with FATCA withholding requirements.

For instance, in the case of a recalcitrant account holder who refuses to waive local data protection rights FATCA states that the account will be required to ultimately be closed. Many banks, however, operate in countries in which closing a depository account is either not permissible or may only be

permissible after a certain period of time. Similar legal conflicts may arise when a PFFI withholds on payments made to NPPFIs or recalcitrant account holders.

We therefore propose that a FFI and its expanded affiliated group be protected from non-compliant status in the event of a conflict between national and/or local laws and requirements contained in the forthcoming FFI agreement. The existence of such conflicts should not prevent a FFI from obtaining or maintaining PFFI status. We recognize that other mechanisms must be developed to address such situations.

## **5. Paper Due Diligence**

In addition to the complexities and problems associated with defining the term “private banking”, the “anything and everything” approach to the paper due diligence requirement is a cost factor of mammoth proportions, as execution necessitates manual work. Indeed, the screening of long term client relationship files by the relationship manager in search of US Indicia may be extensive.

We urge limiting the review to a twelve month period i.e. one year in retrospect as at June 30th, 2013, this being the effective date for FFI written policies and procedures prohibiting its employees from advising U.S. account holders on how to avoid having their accounts identified. Additionally paper file reviews for accounts opened after that date should not be mandatory.

## **6. Recognition of Withholding Tax Deduction by another FFI**

FATCA does not provide an opportunity to detect whether another FFI has deducted withholding tax by reason of the recipient FFI not being compliant. With respect to sales proceeds and cash payments there are ~ in contrast to the payments relevant within the QI-regime ~ no indicia to evaluate the correctness of the relevant initial amount.

Thus, the system requires an indicator for each transaction, signifying whether or not withholding tax has been deducted in order to avoid double taxation on the same amount.

## **7. Identification of Withholdable Payments in Monetary Transactions**

The information on monetary transactions is insufficient in order to recognize bank transfers relating to FDAP, for example a bank transfer initiated by a USFI customer to a recalcitrant account holder of an FFI. The transfer may be regularly repeated (e.g. monthly) but the FFI would be unable to determine whether withholding liability is applicable. As a matter of prudence and avoiding any violation of the FFI agreement the FFI will likely deduct withholding tax on the payment. As the customer is not part of the agreement and there is no legal binding rule the customer would be entitled to claim the amount deducted from the FFI

Aside from the required withholding tax deduction concerning recalcitrant account holders, the information is also necessary in order to comply with reporting requirements relating to documented US accounts.

Beyond this conflict we see an open issue of whether FATCA withholding is required when the FFI has control of funds as an agent, e.g. when providing cash management products, but the FFI does not know enough about their source and character to determine if they are withholdable payments or not. We would encourage the IRS to provide guidance as to FATCA's applicability for products payments and accounts which do not allow for a practical determination of the source or character of the payments.

## **8. Low Risk Accounts/Entities**

We welcome the confirmation provided in *Notice 2011-34* that the IRS intends to exclude certain accounts and entities which pose a low risk of tax evasion from the application of FATCA requirements. In this regard we believe that the types of transactions described below entail a low risk of U.S. tax evasion.

### **1) Accounts held by account holders under legal authority**

There are certain official legal matters with respect to which the formal account holder cares for the identity of the beneficial owner. These official legal matters are:

- Insolvency Administration
- Legal Custody
- Deposit of Payments
- Legal Trust

The objective of these types of accounts is always a safe temporary deposit i.e. the accounts will be used just for processing of official legal matters and there is no further investment strategy or investment management. Under German law the responsibilities mentioned above can only be fulfilled by a specific group of persons, all subject to tight governmental scrutiny, assuring compliance with all national, European and international AML laws as well as KYC rules, e.g. Notare (notary), Rechtsanwalt (lawyer), Steuerberater (certified tax accountant), Wirtschaftsprüfer (certified public accountant), Insolvenzverwalter (Insolvency Trustee), Patentanwalt (patent attorney).

These escrow-type accounts are opened in the name of these persons as an individual or according to their organization as an entity. However, the person will not act on his own behalf but, rather, in the limited circumstances described above, will function as an agent for the ultimate client. We believe that they should be exempt from FATCA withholding requirements to the extent they carry out responsibilities of public administration totally unrelated to any purpose involving US tax evasion.

With respect to the principles of exempting certain persons and structures with a low risk of U.S. tax evasion, we understand that it is essential to eliminate without a doubt any possibility of such persons,

and structures becoming mechanisms for evading US taxation. Nonetheless, we stress that escrow accounts opened by the group of persons mentioned above qualify as posing a low risk of tax evasion because the account holder (i) is under legal authority of Germany or other countries of the European Union, (ii) is bound by law to the same AML legislation and KYC rules as the FFI in charge of the account (iii) explicitly segregates all financial assets of other beneficial owners from its own and (iv) the financial assets are mainly cash or held for discharging official legal affairs determined by law without any specific investment strategy.

## **2) Building and loan associations**

A further example of posing a low risk of tax evasion is a Building and Loan Association, According to the Home Savings and Loan Associations Act (“Gesetz über Bausparkassen”), individuals may accrue savings in order to obtain a home savings loan at a reduced rate of interest after a certain saving period (Contractual Savings for Housing). The designated use of the accrued savings must be specifically set forth in the respective home loan and savings agreement with the client. The interest on the savings account during this period is very low (currently about 1%) with regard to the right to receive a construction loan. According to statutory provisions, the building and loan associations have very limited possibilities to invest the funds (only very conservative investments especially within Europe). This practice and the Building and Loan Associations themselves are regulated by the German Federal Financial Supervisory Agency.

Hence, saving through a Building and Loan Association is not suitable for tax evasion. These institutions, while technically *regarded* as FFIs, and thus, subject to all FATCA obligations – should therefore be exempt from the scope of FATCA affected entities. Thus, we request that Building and Loan Associations be treated as deemed-compliant FFIs within the meaning of IRC 1471(b)(2)(A) and thus exempt from the due diligence, verification, and reporting requirements generally applicable to PFFIs. Moreover, in the event an FFI offers both traditional banking services as well as such Contractual Savings for Housing, these Contractual Savings for Housing accounts should be excluded from the definition of “US Account”.

## **3) Development Banks**

A definite need to exclude entities from the application of FATCA exists for German development banks as they are posing no risk of tax evasion at all. These state development banks (“Förderbanken”) are either owned by one of the 16 states (“Länder”) of the Federal Republic of Germany or of the Federal Republic of Germany itself.

Development Banks are established corresponding to Federal or state law in a special legal form as public sector entities (“Anstalten öffentlichen Rechts”) and are under continuous control of the state audit office (“Rechnungshof”). Like all public sector entities they are exempt from corporate tax. Using development banks as a vehicle for tax evasion is impossible as earnings are entirely and directly paid to the state or the Federal Republic of Germany.

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It is critical for all concerned that feasible and manageable solutions are found to the major concerns outlined above. We strongly support the approach being considered in the course of the ongoing high-level talks between the IRS/Treasury and the European Commission of using mechanisms and instruments which have been developed in the EU (e.g. revised EU Savings Tax Directive, anti-money laundering regulations) as a way forward in dealing with many of FATCA's objectives.

Please do not hesitate to contact us if you would like us to provide additional information or answer any questions regarding the matters set forth in this letter.

Yours sincerely,

for the above-mentioned  
associations, Association of German  
Banks

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