The City of London Law Society

4 College Hill
London EC4R 2RB

Tel +44 (0)20 7329 2173
Fax +44 (0)20 7329 2190
DX 98936 - Cheapside 2

mail@citysolicitors.org.uk

www.citysolicitors.org.uk

Attention: Neil Higgins
HM Revenue & Customs,
CTIAA FPST,
Room 3C/04,
100 Parliament Street,
London, SW1A 2BQ.

23rd November 2012

By post and by email (to: fatca.consultation@hmrc.gsi.gov.uk)

Dear Sir

Revenue Law Committee response to Implementing the UK-US FATCA Agreement (the "Agreement") Consultation of 18 September 2012

The City of London Law Society ("CLLS") represents approximately 14,000 City lawyers through individual and corporate membership including some of the largest international law firms in the world. These law firms advise a variety of clients from multinational companies and financial institutions to Government departments, often in relation to complex, multi jurisdictional legal issues.

The CLLS responds to a variety of consultations on issues of importance to its members through its 17 specialist committees. This response has been prepared by the CLLS Revenue Law Committee.

GENERAL POINTS

The CLLS is appreciative of HM Government's efforts in signing the Agreement and welcomes the opportunity to comment on its implementation. The addition of Article 7 and correction to the drafting error in Article 4 of the model IGA are particularly appreciated. We have set out responses below to those of the specific questions in the consultation document on which members have views. We also have the following more general comments:

1. We think it should be an overriding policy of the implementing legislation that it is intended to minimise the cost and administrative burden of FATCA to UK businesses and should therefore not (ultimately) impose any obligations which go beyond those in the US FATCA law and regulations themselves. For data protection and other reasons it may be necessary for the implementing legislation to include elections concerning which data to report in order to achieve this objective.

2. Some members of the CLLS represent large multinational financial institutions which anticipate complying with FATCA under the Agreement in the UK, in the form set out in the FATCA regulations in a number of jurisdictions, and under other anticipated intergovernmental agreements in jurisdictions which have them. We applaud HM Government for being able to add Article 7 to the Agreement, not just because this ensures that UK financial institutions should benefit from any concessions negotiated by governments of other jurisdictions but perhaps more importantly because it will set a precedent which should hopefully lead to an equivalent clause in all other IGAs. This gives a chance of there only being one form of IGA in practice, representing the best that any IGA jurisdiction is able to negotiate. It should be an overriding principle in implementing the IGA to minimise the administrative burden for UK financial institutions. This may mean giving such institutions the option to comply with the more onerous requirements of the FATCA regulations in order that they can apply consistent processes across all jurisdictions.

3. Given the wide range of different institutions potentially affected by FATCA, there is a difficult tension between on the one hand allowing entities to report information in the same format in which they already hold that information (without having to carry out difficult tax analysis) and on the other hand ensuring the information reporting complies with data protection law and the entity's own terms of business. It is conceivable that specific FATCA-related amendments to data protection law, perhaps at a European level, may be the only way to fully resolve the data protection issue. For example we assume part of the rationale behind the somewhat odd concept in Article 1 that undefined terms should be interpreted in accordance with UK tax law is to avoid the need for financial institutions which report "income" for UK tax purposes to analyse whether that would also be "income" for FATCA purposes in order to comply with the information reporting requirements under the IGA. However the concept gives rise to uncertainty. For example is profit on the sale of a loan relationship, which is taxed as income under those rules, "income" for these purposes? What about the "income" arising from the deemed release of a loan relationship? In the absence of data protection and other legal concerns it should be possible to provide financial institutions flexibility on this point, so that for example if they hold information on "income" deemed to be such under the offshore funds rules they would report that even if not strictly required under FATCA. However for the reasons explained in our response to question 18 below this may cause data protection and other issues. If two different financial institutions are reporting the same information differently (for example because one strictly reports "income" as required under FATCA and another reports income which is deemed to be such under obscure UK tax provisions) it is difficult to draft legislation which can be said to "require" both.

4. Timing is important, as is flexibility, and the implementing legislation should be designed so as to be able to adapt to any relaxations in the FATCA regime or the

IGA regime (which may be brought about under Article 7 as a result of other nations which have taken longer to negotiate their IGAs achieving concessions from the US government).

5. Whilst technically outside the scope of the consultation, we believe we may have identified a flaw in the drafting of the IGA itself. The FATCA regulations and guidance in the US appear to include investment entities which invest on their own account, and do not have "customers" as such. The IGA definition of "Investment Entity" is limited to entities which conduct certain operations for or on behalf of a customer. Therefore it appears that entities such as securitisation companies and holding companies of groups which include a bank subsidiary could be FFI's for FATCA purposes but not under the IGA[1]. Is it intended that there may be UK entities which are within the definition of FFI for FATCA purposes but which do not benefit from the IGA, in which case presumably they are expected to enter into FATCA agreements with the IRS or face being withheld upon? This would seem an odd result and we would welcome clarification from HM Government and the IRS on this issue.

RESPONSES TO SPECFIC QUESTIONS

1. **Are there practical issues with applying the definition of Custodial Institution? If so, what are they and how would they arise? How could these issues be addressed in UK legislation or guidance?**

   It should generally be clear whether or not an entity constitutes a Custodial Institution on the basis of the definition. It would, however, be helpful if HMRC guidance gives clear examples of:

   (a) the type of entities which are expected to fall within the remit of the definition; and

   (b) the circumstances in which income will be treated as attributable to the holding of assets and related financial services.

   We also think it would be helpful if the legislation could specifically "white-list" solicitors' firms and their related service entities from being "Custodial Institutions". Whilst in normal circumstances it is difficult to think of an example of a situation where a solicitors' firm would fail the "20% test", as solicitors' firms should not be "Financial Institutions" under FATCA it should be made clear that they cannot be caught by the reporting obligations imposed under the implementing legislation.

2. **Are there concerns that the reference to "similar business", when read in conjunction with other parts of the Agreement, could result in institutions**

---

[1] We believe securitisation companies are financial institutions within subparagraph (iii) of §1.1471-5(e)(1) of the proposed US FATCA regulations because their primary business is investing in securities, but they do not fall within the definition of investment entity in the UK IGA because this requires operating on behalf of a customer. Holding companies of groups which include a bank subsidiary (including groups for which finance is not the principal business) may also fall within the subparagraph referred to above but the exclusion for holding companies (contained at (e)(5)(i) of §1.1471-5 in the regulations) does not apply if one or more subsidiaries is a financial institution. Such a holding company would not, however, be a financial institution for the purposes of the IGA.

being caught unintentionally? If so, what are they and when would they arise?

The reference to "similar business" is potentially ambiguous and could result in institutions being caught unintentionally solely as a result of holding client accounts. It may, therefore, be clearer if the UK legislation were either:

(a) to refer to deposit-takers which are required to be regulated under the Financial Services and Markets Act 2000 and Chapter II of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001; or

(b) to set out a list of relevant exclusions from the definition of Depositary Institution.

See our answer to question 1 in relation to solicitors' firms.

3. **Do you agree that it would it be most appropriate for the fund to carry the obligations imposed on financial institutions and for the fund manager or other service provider to carry out the reporting on behalf of the fund? Is there a suitable alternative and if so how could it be provided for?**

We agree that it would it be most appropriate for the fund to carry the obligations imposed on financial institutions. We would, however, note that the way in which funds are operated will vary depending on their legal forms and whether they are authorised or unauthorised vehicles. We consider, therefore, it will be difficult to provide for a "one size fits all" reporting process and that it would be preferable for the UK legislation to allow funds the flexibility to carry out the reporting obligations in the way most appropriate on a case-by-case basis.

4. **Are there any other definitions in Article 1 that give rise to uncertainty or raise practical issues which could usefully be clarified in the UK legislation or guidance, and if so how?**

4.1 The definition of "Investment Entity" in Article 1(1)(j) would cover entities such as fund managers and administrators which would, as recognised by HMRC in paragraph 3.10 of the Consultation, potentially give rise to duplicative obligations. This issue should be dealt with under the terms of the UK legislation by clarifying that such entities are not subject to any reporting or due diligence obligations in respect of fund investors to the extent that such reporting and/or due diligence is carried out either by them or another person in relation to such investor's investment in the relevant fund.

4.2 The term "payments" in Article 4(1)(b) is not defined and could be far wider in scope than the payments intended to be caught by the FATCA provisions. "Payments" should, therefore, be a defined term in this context.

4.3 The term "US source" has a specific meaning under US law. It would, therefore, be helpful if the guidance clearly sets out the most common types of payments which will constitute "US Source Withholdable Payments" in order to assist Financial Institutions in carrying out their obligations under FATCA without having to incur the additional expense of US tax advice.

5. **Are there any classes of product, aside from certain insurance policies or insurance products where it would be appropriate to use a reporting period other than the calendar year and if so why?**

No comment.

6. **In what circumstances would imposing a UK definition of "other income" include income types not included under FATCA? What would be the best way to address this issue, balancing reporting on a broader category of income with the administrative burdens of separating different types of income?**

6.1 See general point 3 above on the difficulties caused by interpreting undefined terms in accordance with UK tax law. Guidance could clarify what is meant by, for example, "income", but that would not address the concern raised in that general point that different entities may have collected information based on different definitions and the implementing legislation needs to avoid them having to recalculate it on a different basis to the extent possible.

6.2 Imposing a UK definition of "other income" would potentially include many income types not otherwise included under FATCA, including but not limited to:

(a) reportable but undistributed income in reporting offshore funds arising under the offshore funds rules;

(b) capital gains arising upon the disposal of interests in non-reporting offshore funds;

(c) gains treated as arising in respect of life insurance policies and contracts under the chargeable events rules; and

(d) deemed income under the "transfers of income streams" rules.

6.3 Use of a UK definition would, however, make it easier for UK financial institutions to be certain that they are acting within the terms of data protection law when reporting the relevant information. Such flexibility is necessary not only from an administrative perspective, but also from a practical perspective, as it may be burdensome for institutions to seek US advice in respect of every transaction they undertake.

6.4 In order to give financial institutions the necessary protection without forcing them to report unnecessarily, it would, therefore, be preferable to require them to report on a broader category of income under the terms of the UK legislation, but permit them the option of reporting only on "other income" as defined under the FATCA regulations.

7. **What would be the main concerns, especially for entities new to reporting account information, to take into account when considering whether to specify the data format and method of transmission?**

Given the fact that many financial institutions will be subject to FATCA rules across a number of IGA jurisdictions, it may be preferable either:

(a) to focus on the legal basis for reporting whilst leaving a certain amount of flexibility in the way in which entities are required to report to enable them to adopt a consistent approach across the various jurisdictions; or

(b) agree a consistent approach for reporting with other FATCA partners.

Given timing concerns, the former option may be more practical.

Notwithstanding this timing/practicality concern the CLLS note that the Business and Industry Advisory Committee to the OECD ("BIAC") has already held several meetings focussing on the mechanical reporting aspects of FATCA and (acting through its Treaty Relief and Compliance Enhancement ("TRACE") Committee) has reported on its conclusions to the OECD. Where HM Government believes that there is value in pursuing some form of multi-jurisdictional agreement on consistent approaches to FATCA reporting, BIAC and TRACE would appear to be sensible potential starting points (as would a discussion with the IRS on its views on the information exchange framework proposed by TRACE).

8. **By when would you need to know the data format and transmission method in order to be in a position to report in the first half of 2015? Would any transitional measures (such as phasing in the requirements) be useful to allow for any necessary systems changes to take place?**

No comment.

9. **Would it be reasonable to restrict the availability of transitional measures to financial institutions which have to report on fewer numbers of accounts? What should the limit on the number of accounts be?**

No comment.

10. **Do you have any concerns regarding the implementation of Article 4 and if so how could they be addressed in UK legislation or guidance?**

10.1 As stated above, the term "payments" in Article 4(1)(b) is not defined and could be far wider in scope than the payments intended to be caught by the FATCA provisions. "Payments" should, therefore, be a defined term in this context.

10.2 The drafting of Article 4.1(e) of the IGA is somewhat unclear. In particular debate has arisen as to whether the article is designed to cover both (i) US Source Withholdable Payments made by a UK FFI as an intermediary (where the US FFI is not a Qualified Intermediary that has elected to assume primary withholding responsibility for US tax purposes – such payments being covered by Article 4.1(d)) and (ii) US Source Withholdable Payments made by a UK FFI otherwise in than in an intermediary capacity, or if the Article only covers payments under (i).

10.3 There is an argument that, notwithstanding the "makes a payment of, or acts as an intermediary with respect to" language contained in Article 4.1(e), it is only intended to cover payments made by a UK FFI in an intermediary capacity. This is on the basis that we believe that Article 4.1(d) and (e) were drafted based upon long-standing US law (section 1441 of the Code) and simply aim to deal with the two alternative types of UK FFI that may receive a payment as an intermediary (i.e. intermediaries that are QIs with primary withholding responsibility and intermediaries which are not).

10.4 If Article 4.1(e) only applies to payments made in an intermediary capacity, there will always be an "immediate payor" so the obligation can be complied with. If

Article 4.1(e) is intended to cover payments made otherwise than in an intermediary capacity, it is possible that there will be no "immediate payor" in which case it is unclear whether a UK FFI which does nothing has complied with Article 4.1(e) or not.

10.5 Clarification of the intended scope of Article 4.1(e) in light of the potential ambiguity of the "makes a payment of, or acts as an intermediary with respect to" and the "any immediate payor" language is necessary.

10.6 Guidance should be provided in relation to the application of Article 4(5)(c) to highlight the type of circumstances in which this provision is intended to bite and, in particular, confirm that it should not restrict generic internal marketing activities.

11. **Does UK legislation need to include provisions regarding a suitable period for repair of any errors where they are spotted by the financial institution or HMRC? Also we would welcome views on any potential difficulties with applying HMRC's existing penalty regimes to non-compliance with the Agreement.**

11.1 The UK legislation should include provisions enabling financial institutions to repair any errors. Such provisions should be sufficiently flexible to deal with the challenges and complexities presented by the FATCA rules, particularly during the early stages of implementation. Consideration should be given to addressing the risk of inadvertent breaches of the Data Protection Act 1998 where accounts are disclosed in error during the bedding-in period.

11.2 As stated above, we would also note, as a general point, that there may be some merit in drafting the obligations under the UK legislation relatively broadly, using terminology with which UK financial institutions will be familiar. Financial institutions should then be permitted, to report in accordance with the terms of the US FATCA regulations should they so elect (but see question 16 below as to data protection issues).

12. **Would it be desirable to have examples of minor and significant non-compliance contained in guidance material?**

Yes.

13. **We think there would be benefits in having a nominated individual undertaking certain compliance responsibilities and providing assurance that the financial institution's obligations have been met. We would welcome thoughts on such a role, and on its potential scope.**

The CLLS is not in favour of imposing any obligations beyond those which are absolutely necessary. We agree with the suggestion in the consultation paper that any such nominated individual should not be personally liable for non-compliance as it is not in our view fair to impose personal liability on a UK individual in relation to compliance with a US tax measure which is sufficiently far reaching that non-compliance could easily be inadvertent (especially as it is likely, at least at first, to be subject to regular change). Having a nominated individual who is not personally liable does not seem to add anything meaningful over and above merely making the financial institution itself liable. We believe it should be left to financial institutions to choose their own procedures in order to minimise

the risk of such liability and that therefore the UK legislation should not provide for there to be a nominated individual.

14. **Do you have any concerns regarding the implementation of Article 5 and if so how could they be addressed in UK legislation or guidance?**

No comment.

15. **Do you have any concerns regarding the implementation of the commitment to require UK financial institutions to obtain and report US TINs and if so how could they be aligned with other data gathering requirements in UK legislation?**

No comment.

16. **We welcome comments on any circumstances where applying the US Regulations provide a less burdensome approach than applying the terms of the Agreement.**

Given the fact that many financial institutions will be subject to FATCA rules across a number of jurisdictions (including non-IGA jurisdictions), it is conceivable that there may be circumstances where it would be more efficient for financial institutions to follow procedures under the US FATCA regulations in order to standardise and streamline processes across the business and/or group. This may particularly be the case where such financial institutions outsource the data processing for these purposes to a central hub. It may, therefore, be appropriate to permit UK financial institutions to comply with the US FATCA Regulations, either in whole or part, where they consider such compliance to be beneficial.

If this approach is adopted, care will need to be taken to ensure that financial institutions can do so without breaching data protection principles, for example by finding a way to impose this as an obligation (see further question 18 below).

17. **Comments are welcomed on whether the use of the term "value" in relation to specific financial products causes any difficulties for product providers.**

No comment.

18. **Do respondents feel that the ability under an election to choose whether to apply the limits set out in Annex II cause data protection issues? If so could you state why and provide examples?**

Yes, we do consider that an ability to choose whether to apply limits in this case could cause data protection issues, and potentially also issues under financial institutions' own terms of business, depending on how the ability is formulated. Under the Data Protection Act 1998 ("DPA") all data must be processed in accordance with the principles set out in Schedule 1 to the DPA. Principle 1 states that personal data shall be processed fairly and lawfully and, in particular, shall not be processed unless at least one of the conditions in Schedule 2 is met. It is our expectation that financial institutions will need to rely on either condition 1 (that the data subject has consented) or condition 3 (the processing is necessary for compliance with any legal obligation to which the data controller is subject,

other than an obligation imposed by contract) of Schedule 2 to justify disclosure to HMRC.

In practice, consent cannot provide a full solution. Principally this is because (i) consent may be withdrawn by the data subject; (ii) consent must be freely given (and there is doubt over whether consent in this context could ever be freely given, in view of the fact that customers would be faced with forced closure of accounts or a refusal to open an account if they do not consent); and (iii) it is generally accepted[2] that financial institutions are unable unilaterally to vary an existing consent or introduce a consent into existing agreements, meaning that obtaining consent would be an expensive and labour-intensive task with no guarantee of success.

Accordingly, financial institutions may only disclose data to HMRC where such disclosure is *necessary for compliance with* the implementing legislation. It is therefore essential that such legislation does impose an obligation to disclose (as opposed to an option to disclose) all information that may be required.

One solution may be to impose an obligation to disclose all data (irrespective of limits) but to allow financial institutions the option of electing not to disclose or to disclose on an aggregated basis details of any accounts below the specified limits.

Additionally, it will be crucial to ensure that the legislation is drafted unambiguously in terms of defining the accounts in relation to which financial institutions will be required to report, and that such definition is both objective and practicable. For example, financial institutions could be required to report accounts belonging to persons "identified as US Persons" rather than simply accounts "belonging to US Persons" which would impose a wider obligation that the financial institution may be unable to meet. Guidance should also be used to help ensure that the reporting obligations are clear.

We would expect that to the extent financial institutions have confidentiality obligations under their own terms of business, they are likely to have an exclusion for disclosures which are necessary to comply with law, so the same point arises in that context.

19. **We would welcome comments on the type issues that should be taken into account when considering the format of a similar agreed form. For example with regard to the interaction between financial institutions and third party service providers undertaking the necessary AML or in relation to electronic accounts such as internet banking.**

No comment.

20. **We welcome comments with regard to the role of a relationship manager and on how to define this term appropriately for UK institutions.**

No comment.

---

[2] See for example (at para 10.4 of) the recent letter from the Article 29 Working Party dated 21/06/12 and addressed to the Director General of Taxation and Customs Union at the European Commission

21. **We again welcome comments on whether the ability to have such a choice is desirable as well as examples of when and why such a choice might be useful.**

21.1 Whilst flexibility in the way in which the FATCA requirements may be applied by financial institutions is something which should be welcomed, it will be essential to ensure that such flexibility does not result in (or risk) financial institutions falling foul of data protection requirements.

21.2 It may, therefore, be preferable (as set out in our response to question 18 above) for the UK legislation to apply *prima facie* to all accounts regardless of whether they satisfy the *de minimis* thresholds, but for financial institutions to be permitted to opt out of providing data relating to accounts that fall below the specified thresholds. As an alternative, albeit less satisfactorily, this option could be set out in guidance.

22. **We welcome comments on how respondents see this process impacting on differing operating procedures, particularly regarding any timing issues this will raise and how this process will work where third party service providers are used to carry out the AML process.**

No comment.

23. **We welcome comments on whether institutions would favour the definition of a change of circumstances to be set out only in guidance or also defined in the legislation. What would be the pros and cons of either approach?**

No comment.

24. **Does this aggregation process cause any particular difficulties for businesses? For example where systems can link accounts together but don't go as far as totalling up separate balances. How would this affect an entity's ability to undertake the due diligence required?**

No comment.

Yours faithfully,

Bradley Phillips
Chair
The City of London Law Society Revenue Law Committee

THE CITY OF LONDON LAW SOCIETY
REVENUE LAW COMMITTEE

Individuals and firms represented on this committee are as follows.

B.S. Phillips (Herbert Smith Freehills LLP) (Chairman)

H. Barclay (Macfarlanes LLP)

C.N. Bates (Norton Rose LLP)

B. Coleman (Weil, Gotshall & Manges LLP)

D. Friel (Latham & Watkins LLP)

P.D. Hale (Simmons & Simmons LLP)

M.J. Hardwick (Linklaters LLP)

C. Hargreaves (Freshfields Bruckhaus Deringer)

K. Hughes (Lovells LLP)

N. Mace (Clifford Chance LLP)

G. Miles (Slaughter and May)

J. Scobie (Kirkland & Ellis LLP)

C.G. Vanderspar (Berwin Leighton Paisner LLP)

S. Yates (Travers Smith LLP)

C. Yorke (Allen & Overy LLP)