U.S. Department of the Treasury
1500 Pennsylvania Avenue, NW
Washington, DC 20220

via the Federal eRulemaking Portal at:
www.regulations.gov

31 July 2017
EBF_028279

Subject: EBF Response to Treasury Request for Information published on 14 June 2017 (82 F.R. 27217)

Dear Sir/Madam,

I am writing to you following the Executive Orders 13771 and 13777 ("the Executive Orders") to reduce regulation and control regulatory costs and further to the Request for Information subsequently published on 14 June 2017 (82 F.R. 27217) by the Treasury.

The European Banking Federation (EBF), which is the voice of European banks, welcomes the opportunity which is provided in that context to comment on Section 871(m) of the U.S. Internal Revenue Code and on the unintended consequences of the Foreign Accounts Tax Compliance Act (FATCA).

Section 871(m) of the U.S. Internal Revenue Code

Section 871(m) of the Internal Revenue Code was enacted as part of the HIRE Act in 2010 under the headline "withholding on dividend equivalent payments".

It was meant to address former tax avoidance opportunities which allowed offshore hedge funds to receive the economics of U.S. dividends tax-free by engaging in short dated swap transactions (so-called "notional principal contracts", NPC) or stock loans (i.e. repo and security lending transactions) rather than directly holding the underlying stock referenced in these transactions.

The statute provides that a "dividend equivalent payment" includes any payment to a non-resident alien that references the payment of a dividend from an underlying U.S. security pursuant to a securities lending or a sale-repurchase transaction or a specified NPC. These dividend equivalents should be treated by withholding agents and qualified intermediaries like dividends from a US source and therefore they would be withholdable payments under Chapter 3 and 4.

The Treasury and the IRS issued final regulations in September 2015 that widened the scope of the Section 871(m) withholding obligations dramatically by introducing rules regarding so-called "equity linked instruments" (ELI). For simple transactions, a calculation of the 'delta' of the transaction – the extent to which the value of the transaction is linked to the underlying value of the US equities – will be required; only transactions with a delta >0.80 at inception will be caught. For complex transactions, a more complex 'substantial equivalence' calculation will be required.

The effective date was determined to be 1 January 2017. However, to reduce the burden of implementation, a phased-in approach was announced in 2016. Therefore withholding obligations are limited to so-called "Delta-One-Transactions" during 2017.

As a result, typical retail products like warrants and securitized structured notes, which are acquired purely for speculative reasons and not for tax evasion purposes, became affected by Section 871(m), with tremendous side effects on the European securities market and particularly on non-US banks operating in that market. In addition, implementation efforts required from Financial Institutions providing custodial and depository services are far beyond what seems appropriate with respect to the objectives of the law.

Moreover, the implementation of Section 871(m) may be a source of tensions with a number of jurisdictions as explained in the letter that the G5 countries (F, G, IT, ES and the UK) have sent to the U.S. Treasury in 2016 considering that dividend equivalent payments do not qualify as dividends under the applicable tax treaties and that tax withheld on such dividend equivalent payments is not considered to be creditable against local income taxes. This situation will be exacerbated from 1 January 2018 with a lack of clarity and guidance concerning the treatment of cascading withholding/taxation of dividends received by non-US banks and the issues created for systems build and implementation.

To our knowledge, the US have not yet resolved this point with the G5 Countries. As a result, foreign custodial institutions might have to choose between compliance with the QI agreements and their local tax requirements. We therefore call for the US government to discuss the implementation of Section 871(m) with these jurisdictions in the framework of their respective Double Tax Treaties.

In the light of the above, the implementation of Section 871(m), with the scope intended by the final regulations, appears to be a very complex project, which requires significant efforts and resources and costs may exceed the amount of tax that Treasury can expect to collect as a result of the new rules.

Section 871(m) affects Financial Institutions in different ways, often depending on the Foreign Financial Institutions' country of residence, the variety of retail financial products and the differences in securities processing systems in certain jurisdictions.

We strongly believe that warrants and securitized structured notes have not been within the initial scope of the statute, simply because these type of products do not have the potential for tax-avoidance, and that the final regulations in their current form go far beyond what is necessary to address abuse.

Against this background, we would like to make the following recommendations:

- In order to reduce unnecessary burdens, the September 2015 and January 2017 regulations should be withdrawn or substantially modified. Instead, the statutory withholding rules that were in effect up until December 31, 2016 should be applied indefinitely.
- If they were not repealed, then the scope should at least be limited to delta one transactions.
- Any issues arising from Section 871(m) regulations under applicable income tax treaties and/or international law should be cleared with relevant jurisdictions before the implementation of the Regulations. Sufficient lead-time should be provided for financial institutions to discuss any related domestic legal impediments with their home authorities.

The unintended consequences of FATCA

FATCA requires Foreign Financial Institutions to review their client base in order to identify US reportable accounts based on defined US indicia. When an indicium is found, the accountholder is presumed to be a US reportable accountholder, unless information (self-certification and corroborating evidence) is received by the FI that the accountholder is not a US reportable accountholder. Financial Institutions have reached out to their customers with US indicia and have encountered the following issues:

- Many customers have not responded to these requests yet. Based on the presumption rule, these accounts then need to be classified as US reportable accounts. Obviously, no Tax Identification Number (TIN) is available for these accounts as in many cases the indicia will either be a false positive or the indicia may be cured as the accountholder is not a US person.
- Some customers have responded back that they cannot be considered as US Tax Payers evoking a number of reasons, including the fact that they left the US 50 years ago and never went back or they were only born in the US and stayed for a few months/ weeks only. This is the "accidental American" situation which has previously been acknowledged by the Treasury and IRS. These customers do not have a TIN and would encounter difficulties and long delays in obtaining one only to renounce US citizenship subsequently.

As of the reporting on 2017, it is mandatory to include a TIN in the reporting of US reportable accounts. The IRS has issued a FAQ stating that replacing a TIN with a string of nine zeros will result in error notifications. For a reporting FI, the ultimate sanction of not complying with FATCA is a 30% withholding tax on all income streams from the US, for both itself and its customers. Given its magnitude, this issue may lead to disruption of the financial markets and liquidity issues which could lead to another financial crisis.

Banks are therefore now faced with a dilemma: Continue to provide financial services, including basic banking services, to European citizens that also have a US indicium but have no US TIN; or to exclude them.

Estimates of the number of Americans outside of the United States are around 6million. Only about 1 million of them file US tax returns. A preliminary survey conducted by the EBF and the Dutch Banking Association suggests that 50% of the US reportable accountholders might have no TIN. That would mean that approximately 3 million US persons living outside of the US could be excluded from the financial system in addition to those presumed to be US due to uncured indicia.

If not addressed, and considering possible huge sanction that banks may incur if considered non-compliant, this will likely force banks to terminate existing contracts with customers who are unable or unwilling to provide the US TIN. This, in turn, will lead to financial exclusion, i.e. will prevent access to finance for a very significant number of European (dual) citizens. As such this would be contrary to the G20 goals to widen financial inclusion and access to finance.

We therefore call for the US to provide pragmatic solutions and guidelines which may read as follows:

- If no US TIN is communicated and reasons for its non-availability are not communicated by the customer, the Financial Institution should be allowed to report the date of birth of the customer if he is a natural person and a commercial register number or VAT identification number if it is an entity.

- Like under the Common Reporting Standard, Financial Institutions should make reasonable efforts to receive the US TIN from pre-existing customers within 2 years after the accounts of the customer have been identified as reportable.
- Reasonable efforts consist for instance of asking the relevant questions to the customer in person or per mail, per telephone, e-mail or other tools such as SMS messaging.
- If the US TIN has not been obtained, the customer should be contacted once per year.
- If it has made reasonable efforts, the Financial Institution should keep its FATCA-compliant status and should not be subject to any penalty even if US TINs are missing. The scope of the default reporting should be limited only to entities for which US indicia have been identified in relation to the entity or one or more of its Controlling Persons based on AML/KYC or other information.

Yours faithfully,

Wim Mijs, Chief Executive Officer, EBF