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The Honorable David J. Kautter
Assistant Secretary for Tax Policy
U.S. Department of the Treasury
1500 Pennsylvania Avenue, NW
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William M. Paul
Acting Chief Counsel
Internal Revenue Service
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Dear Sirs,

Subject: Repeal of Section 958(b)(4) IRC – unintended Form 1099 reporting consequences

The European Banking Federation (EBF), which is the voice of European banks, is very concerned about the unintended consequence of repealing Internal Revenue Code Section 958(b)(4) by the Tax Cuts and Jobs Act of 2017 (TCJA).

As the repeal of Section 958(b)(4) impacts European banks that are part of multinational groups with U.S. subsidiaries, the EBF commentary are as follows:

Prior to the repeal of Section 958(b)(4) by the TCJA, foreign subsidiaries of foreign financial institutions were primarily only subject to U.S. Form 1099 tax reporting and backup withholding with regard to U.S. source income obligations. After the repeal of Section 958(b)(4) IRC by the TCJA, the unintended consequence of such repeal created large quantities of new controlled foreign corporations (new CFCs).[1]

New CFCs include non-U.S. subsidiaries of foreign banks, if the bank group also has a U.S. subsidiary. We understand that the intent of the repeal of Section 958(b)(4) was to ensure that CFC status could not be avoided by U.S. shareholders through transfer of stock of a foreign subsidiary to a foreign related person.

Originally, Section 958(b)(4) IRC prevented the downward attribution of such stock to the U.S. shareholder and thus, the U.S. shareholder could avoid certain income tax reporting. The repeal of Section 958(b)(4) IRC now results in a downward attribution of stock from the non-U.S. subsidiary to the U.S. subsidiary. This unintentionally transforms the non-U.S. subsidiary into a new CFC and also, a U.S. Payor.[2]

As a new CFC, the non-U.S. subsidiary is also a U.S. Payor with expanded Form 1099 reporting and backup withholding tax requirements. Since the new CFC is now a U.S. Payor, it must file Forms 1099 for both U.S. and non-U.S. source reportable payments (for

1 A foreign corporation is considered a CFC if a U.S. shareholder owns more than 50 percent of the corporation's shares by vote or value.
2 See U.S. Treas. Reg. Section 1.6049-5(c)(5)(i)(C) which defines a CFC as a U.S. Payor.

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example, interest, dividends, sales proceeds including cost basis information). Also, any payments on Form 1099 may be subject to backup withholding tax if the payee's U.S. TIN is not provided or not provided accurately on Form W-9. Thus, expanded reporting to non-U.S. reportable payments will also expand the possibility of having to apply backup withholding tax. Prior to the repeal of Section 958(b)(4) IRC, the non-U.S. subsidiary would have been considered a non-U.S. Payor and generally exempt from Form 1099 and backup withholding tax requirements for non-U.S. source income paid outside the U.S.[3]

The expanded Form 1099 reporting and backup withholding tax requirements for new CFCs are difficult to implement operationally and legally for several reasons:

- New CFCs may violate local data privacy laws by reporting Form 1099 directly to the IRS. Also, new CFCs may violate local law when having to apply backup withholding tax.

- Since the repeal of Section 958(b)(4) new CFCs have not had appropriate time or guidance to implement expanded reporting and withholding requirements and thus, are unfairly subject to IRS penalties and withholding liabilities.

- Such reporting would frustrate and conflict with the extensive network of FATCA Intergovernmental Agreements (IGAs) entered into between the IRS and over 100 foreign countries. IGAs were intended to "address … legal impediments to compliance, simplify practical implementation, and reduce FFI [Foreign Financial Institution] costs."[4]
  Form 1099 reporting by CFCs, however, would undermine this purpose by imposing new requirements that may violate local laws.

- The New CFCs must implement necessary operational processes including new system requirements, training of personnel, set up of cash ledger accounts and a method to deposit backup withholding tax, etc. This is a substantial burden for new CFCs that have not previously been required to perform reporting on Form 1099, moreover non-US source income have now to be reported.

A second consequence that new CFCs might be facing is the potential loss of the portfolio interest exemption, which could disrupt common intercompany financing transactions. They may not be able to benefit from this relief because if the interest is received by a CFC, it does not qualify for the portfolio interest exemption.

Moreover, with the effective date of the TCJA being 2017, the affected entities seem to be non-compliant as of today and in many cases probably are even unaware of their non-compliant status. This non-compliance status is an imminent concern that should be resolved as soon as possible.

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3 See U.S. Treas. Reg. § 1.6041-4(a)(2); §1.6042-3(b)(1)(iv); §1.6049-5(b)(6).
4 See Joint Statement from the United States, France, Germany, Italy, Spain and the United Kingdom Regarding an Intergovernmental Approach to Improving International Tax Compliance and Implementing FATCA, Feb. 7, 2012, available at https://www.treasury.gov/resource-center/tax-policy/treaties/Documents/FATCA-Joint-Statement-US-Fr-Ger-It-Sp-UK-02-07-2012.pdf

On behalf of European banks impacted by the repeal of Section 958(b)(4) under the TCJA, the EBF respectfully requests that the IRS issue a notice clarifying and redefining the definition of U.S. payor so that new CFCs created solely on account of the repeal of Section 958(b)(4) will not be treated as U.S. payors and will not be disqualified from the portfolio interest exemption due to their CFC status.

Yours sincerely,

Wim Mijs
Chief Executive Officer

cc:

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