Position Paper

Insurance Europe response to the OECD Consultation on a global system of automatic exchange of information

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Introduction

Insurance Europe welcomes the opportunity to provide comments on the OECD's Working Party No. 10 consultation paper on "Developing a Secure, Effective and Standardised Model of Automatic Exchange for Financial Account Information (AEOI)".

Insurance Europe in general supports measures aimed at combating tax evasion. Whilst tax evasion is corrosive to the fairness of a tax system, any rules that are introduced to prevent tax evasion need to be targeted and proportionate.

In developing reporting and transmission standards to prevent tax evasion, Insurance Europe believes that:

- A global standardised solution for tax information exchange is needed;
- Such a system needs to be proportionate to the inherent risk;
- Information exchange requirements need to be in line with data protection rules; and,
- The impact on customers and the insurance industry needs to be minimised.

Against this background, Insurance Europe is supportive of the work on automatic exchange of information undertaken by the OECD to develop a uniform global approach. National or regional tax information regimes would lead to duplicate reporting, excessive costs, and complex system designs for the insurance industry. European insurance companies could potentially be subject to several different reporting regimes: Domestic reporting regimes; the European Union Savings Directive (EUSD); FATCA; the Administrative Cooperation Directive (ACD).

However, any moves into automatic exchange of information should be assessed against existing and envisaged regulatory measures. Insurers are currently grappling with a number of regulatory changes at domestic, EU and global level. All these changes come at cost and global AEOI will add to this cost. Furthermore, differences between business models and between insurance products and other financial

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products must be considered as the new system is designed. Most of the existing financial reporting regimes were designed with the banking industry in mind and other industries have had to fit within a regime afterwards. This has led to considerable administrative issues.

With this response, Insurance Europe sets out its key concerns regarding the overall principles that should govern the AEOI. Next, we specifically comment on the questions raised by the OECD in its consultation document. We would, of course, be happy to clarify any points raised in these comments and look forward to continuing this dialogue and to contributing to further consultation at the appropriate stage.

General Comments

Insurance Europe believes that in designing the global system of exchange of information, the OECD should take into account the following points:

- (1) The nature of insurance products ;
- (2) Industry concerns around pre-existing contracts;
- (3) Low risk of tax evasion from pension products.

<u>(1) The nature of insurance products</u>

A) Re-insurance, Property & Casualty, and Non-Cash-Value contracts

The objective and design of a typical insurance product is very different from the type of business that exchange of information legislation for tax purposes targets. A typical insurance contract is designed to provide financial protection against an unforeseen event, such as flooding, accidents, burglary, death, disability or illness. In this respect, general insurance companies do not create financial accounts and as a result do not accept deposits and do not engage primarily in the business of investing, reinvesting or trading in securities for their policyholders.

With this mind, in Insurance Europe's view, the following categories of policies should be excluded from the scope of AEOI as they will not be used for tax evasion:

- Reinsurance contracts (life and non-life)

Reinsurance products are business to business transactions sold only to insurance companies. The insurer and not the reinsurer is liable to the policyholder, therefore reinsurance provides no potential investment return to individual natural persons and does not implicate the concerns of tax evasion.

- Property & Casualty (P&C) contracts

Such insurance policies are designed to reimburse the insureds for damages caused by insured events. P&C policies do not resemble investment products. They cover P&C risks that create payments to policyholders and/or to the injured person only when insurable events occur.

- Contracts without Cash Value

Contracts without a cash value only pay out on the happening of an insured event and therefore will not be used as a method of tax evasion. Insurance Europe lists below some such policies, however, due to the diversity and plurality of types of life insurance contracts across Europe this list should not be viewed as exhaustive:

(1) Term life policies insure the life of a person under which the payout arises only in the event of death. These products can be subscribed either by individuals or groups (i.e., plans obtained by employers).

(2) Accident, health, medical and disability policies also pay only when triggered by the occurrence of an insured event. These products do not build up a cash value. These products also can be subscribed by individuals or groups.

B) Cash-value contracts

Only a limited amount of insurance products can be regarded as products with a cash value component which may give rise to tax evasion concerns. These are life insurance products, with an investment/savings element which can be accessed before death. Therefore in a global AEOI system these are the only subset of insurance products that should require reporting.

The global system of exchange of information should take into account the following characteristics of cash value insurance contracts:

- With regard to cash value insurance policies, the client asset is the insurance contract that contains the insurer's promise to pay. The underlying assets are owned by the insurance companies, which also bear the risk of default. In other words, a contract with guaranteed capital has no relation whatsoever with the assets held. Having regard to the contractual nature of insurance contracts, both parties of an insurance contract- the insurance company and the insured person - are bound by the terms and conditions agreed at the moment of signing an insurance contract. It is therefore generally impossible for an insurer to change the existing policies with new reporting requirements.

- Cash value insurance contracts are maintained over a long period of time. The duration can be anywhere up to 40+ years depending on the profile of the insured. As a result of this long-term nature of life insurance products, in contrast with other financial service industries, life insurers typically have limited client interaction following the initiation of a policy.

(2) Pre-existing contracts

Insurance Europe believes that pre-existing insurance contracts should be excluded from the scope of AEOI. Their inclusion would give rise to disproportionate administrative costs compared to the low level of risk of tax evasion these policies present. Both the proposed EUSD and the US FATCA have recognised this. Indeed, the proposed EUSD excludes all insurance contracts subscribed before 1 July 2014 and the FATCA Model IGA under certain conditions allows insurers to exempt existing polices from its scope.

European insurers, despite their best intentions, will have great difficulty in complying in respect of existing accounts, as the data held on existing policies will not in all cases be sufficient to determine the residency status. Existing life policies and annuities were designed prior to any system on automatic exchange of information. Therefore, the information necessary to identify a foreign tax person is often not available for review as existing systems have never been designed to capture and store this data or permit an electronic search.

Insurers will also have significant difficulty in amending older IT systems, on which many of the existing products are administered, to include new data fields or create search programs. These changes would be very costly and problematic due to limitations inherent in the IT and the availability of IT expertise in the legacy languages and hardware on which the systems are maintained.

Furthermore, the number of policies in force makes any manual searching practically impossible.

In practice, in order to make a determination of a policyholder's residence status, insurers would be required to ask for additional information from policyholders. This would be very burdensome and impractical to do because:

- Life-insurers have limited client interaction following the initiation of a policy as a result of the long-term nature of the products offered. Experience has shown that trying to obtain supplemental information from existing customers typically generates a very low level of response.
- Insurers lack the power to compel the provision of such information.

(3) Low risk of tax evasion of pension products.

Insurance Europe believes that pension plans and tax favoured retirement products (2^{nd} and 3^{rd} pillar) should be exempt from AEOI because of the low or non-existent risk of tax evasion associated with such products.

While retirement plans and tax favoured pension products are designed somewhat differently across European countries, they all focus on providing an appropriate individual pension benefit to a citizen or resident, rather than being used for income generation purposes.

Furthermore, the majority of EU countries require pension schemes and retirement products providers to deduct income tax at source from payments to pension scheme recipient, often at high income tax rates.

Finally, European countries have introduced significant restrictions on how and when benefits can be withdrawn.

Finally, all aspects of these plans – eligibility, contributions, portability, payments and taxation - are highly regulated by law in each EU country.

Insurance Europe comments on the OECD questions

1. THRESHOLDS

Do you intend to apply a threshold, where it is available, for purposes of reporting U.S. accountholders in connection with FATCA Model 1 IGA reporting? Why or why not?

As explained above, pre-existing insurance contracts should be excluded from the AEOI scope. Therefore, in our response on thresholds we focus on new policies.
With respect to new policies, Insurance Europe understands that, some European insurers prefer to report on all accounts regardless of the value. The European insurers find the application of a threshold problematic because:

- It is operationally easier to check all contracts at the moment of opening, rather than waiting until the account value exceeds one of the limits.
- Insurers are under an obligation to constantly monitor policies, as exchange rate and investment rate fluctuations will mean that the account could regularly change from being in scope to being out of scope.
- There is no need to aggregate accounts.

However, given the global reach of insurance and that some small insurers would prefer to use thresholds[1] in order to reduce the costs of implementation, Insurance Europe recommends that financial institutions should be provided with the option of using thresholds.

Assuming a system that requires reporting not just of U.S. accountholders but also accountholders from a large number of other jurisdictions, what would be the implication for business of eliminating threshold amounts? Please consider this question from the perspective of reporting, due diligence and excluded financial institutions and products. Please also consider issues of account aggregation (i.e., account aggregation would not be necessary if there were no thresholds). Do the answers depend on which threshold is being discussed (e.g., pre-existing accounts, individual accounts versus entity accounts, thresholds for cash value insurance)?

As outlined earlier, all pre-existing accounts should be excluded as European insurers will not have sufficient information to determine the residency status.

[1] For example, FATCA provides for a threshold of 50.000 USD for each contract.

In case the exemption on pre-existing accounts is not granted, the OECD should apply:

- A sufficiently high cut-off threshold[2], removing the annual requirement to check for higher value accounts.
- Electronic indicia searches for pre-existing accounts only limited to addresses.

This would remove the great majority of pre-existing policies from AEOI scope and significantly reduce the burden on European insurance companies regarding AEOI reporting obligations. Furthermore, by requiring European insurance companies to report only on the largest policies the tax authorities would be able to focus on the policies that have the greatest potential for being used for tax evasion purposes.

Alternatively, insurers are required to verify policyholders at the point of pay out to ensure the funds go to the right person. As part of this process the address will be gathered. At this point, insurers will be able to make an assumption on tax residency and report on the payment if necessary.

How important is it that this question is dealt with in the same way in different jurisdictions?

Insurance Europe believes that a multi-lateral AEOI would only work effectively if maximum consistency and standardisation at the national level is achieved. Therefore, it is very important that every jurisdiction deals with this issue in the same way.

If individual jurisdictions have various rules, the compliance process will be much more burdensome and costly for insurance companies and they will be obliged to manually determine which information is sent to which local authorities.

Therefore, Insurance Europe believes that it is crucial that thresholds are applied consistently across jurisdictions. However, as outlined earlier AEOI should give financial institutions flexibility in applying thresholds.

2. EXCEPTIONS TO REPORTABLE ACCOUNTHOLDERS.

In a multilateral context, could FIs operate a system where every residence country specified a similar (but different) list of different exceptions for entities by reference to its domestic law?

As a general remark, Insurance Europe believes that exceptions should be considered not only on the level of reportable entity, but also at the level of a product. When considering the exceptions to reportable accounts and institutions, this should be determined using a risk-based approach from the perspective of whether a product or entity does really have high risks of tax evasion or not.

In our view, in some cases an exception can only be based on the principle of "substance over form", thereby looking at the underlying product and what it provides rather than just its legal form. For example, in the EU pension products are provided by different financial institutions, including insurance companies, pension funds, banks etc. Therefore, in order to reflect the entire market an effective exemption of retirement products is only possible if the exemption is at product level.

The only way that exemptions could work in a multi-lateral system and give a high level of certainty to financial institutions in each jurisdiction is that the different products and entities are described in local law. The local jurisdictions are best placed to understand what kind of entities and products might be used for tax evasion purposes. The assessment of local jurisdictions could be based on a leading principle(s) identified by the OECD.

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[2] For example, FATCA provides for a threshold of 250.000 USD for pre-existing accounts.

In this respect, Insurance Europe believes that the definition of insurance product from FATCA Model 1 IGA, (which is based on a cash-value life insurance product, combined with national lists of exemptions for entities and products similar to annex 2) could be workable, as it allows for national specificities to be applied and allows for national authorities to determine the level of required reporting.

Furthermore, as outlined above, all life insurance products without cash value, all pension and tax favoured retirement products (2nd and 3rd pillar), nonlife insurance, reinsurance and pure protection products should be outside the scope.

As an alternative, could certain categories be defined generically (e.g. governments, central banks etc.,) and still be administrable by and provide sufficient certainty to financial institutions?

In addition to its response to the previous question, Insurance Europe would like to underline that a generic definition of insurance product cannot be applied on a multi-lateral level without deferring to the local jurisdiction. It is practically impossible to draft a single definition of insurance product provision which would be workable on hundreds, if not thousands of insurance products across the world. Indeed, the insurance sector is inherently a local business, as insurance companies are licensed and regulated under the jurisdictions in which they issue policies and sell their products. The US approach of referring to "cash value" is now well understood and jurisdictions around the world have analysed this in the context of their market. Therefore there is a good understanding of the type of insurance products that should be reported on. We would therefore not want to see a divergence from this approach.

If so, which categories do you think could be/could not be defined generically in a way that would be administrable, and how would you see the process working?

Please refer to the answer to the questions above.

3. DUE DILIGENCE PROCEDURES AND REQUIRED INFORMATION.

What are the cost implications of reviewing the existing customer database for reportable account holders with respect to multiple residence countries and what aspects of due diligence affect costs the most (e.g., does the length of the look-back period affect costs, and if so, how)?

The most significant cost of reviewing and reporting on existing customer base include contacting of customers. As outlined earlier, European insurers do not hold sufficient data in order to determine the residency status of policyholders. As a result, insurers would be required to come back to existing policyholders and ask for additional information. This would place not only a tremendous burden on insurers, but would also be impractical mainly because of the low response rate to requests for additional information from policyholders. Therefore, all pre-existing insurance accounts should be excluded from the AEOI.

Furthermore, manual searches of existing records substantially impact the cost of a pre-existing account review. For insurance companies with a client base that is almost entirely local, these costs would be disproportionately high.

In case the exemption on pre-existing accounts is not granted, the OECD should apply a sufficiently high cut-off threshold, removing the annual requirement to check for higher value accounts. Furthermore, a shorter look back period (for example max. 5 years) would also lower impact on the cost of a pre-existing account review.

Is the date of birth of individual account holders available information to financial institutions with respect to pre-existing accounts? Do financial institutions collect the date of birth and/or place of birth as part of account opening? Have AML rules affected the process? If date of birth is collected is it recorded electronically?

In general, European insurers collect a policyholder's date of birth. Date of birth is generally recorded electronically for new accounts openings. However, for some older policies this may not have been a case.

Same questions as above with respect to the place of birth.

European insurers do not collect data on policyholders' place of birth. However, Insurance Europe is not clear about the relevance of the place of birth. This will only be relevant for countries that tax non-resident citizens. Given the need for consistency and simplicity in a global system, Insurance Europe believes that it should be assumed that taxation of individuals will be based on residency.

Would financial institutions prefer countries (if possible) to introduce a comprehensive domestic reporting regime from the beginning, perhaps as an option? (i.e., instead of requiring reporting with respect to residents of a few countries, require reporting (or customer due diligence) with respect to all non-resident accountholders or those of countries with which exchange relationships exist)?

We are unsure of the objective of this question. If the question is about consistency between regional and global reporting systems, our preference is to have harmonised global system of information which is compatible with national and reporting systems. Therefore, Insurance Europe is supportive of the work on global automatic exchange of information undertaken by the OECD.

Could financial institutions review all accounts to identify the residence country when they review the account base for FATCA purposes, whether or not resident/citizen of the United States? Would the absence of thresholds in this context make a difference in that regard?

Insurance companies are able to collect required information about the residence country at account opening from a policyholder for new accounts and report it subsequently to tax administration (legal basis is needed for data protection reasons). However, given the complexity of the determination of tax residency, insurance companies are unable to determine the policyholder's tax residency.

As outlined above, thresholds are not critical with respect to the new policies. However, in case the exemption on pre-existing accounts is not granted, it is important that the AEOI introduces a sufficiently high cut-off threshold[3].

What other measures could be envisaged to reduce the burden associated with different cut-off dates for distinguishing pre-existing and new accounts?

It is crucial that cut-off dates for distinguishing between pre-existing and new policies are applied in a consistent way across all jurisdictions. If different jurisdictions have different rules, it will be very complex and expensive for insurance companies to implement multiple cut-off dates.

For pre-existing entity accounts, what type of information and documentation are available to financial institutions to determine the tax residence of the entity in the multilateral context (e.g., to determine the place of incorporation or organisation or the place of effective management)?

[3] For example, FATCA provides for a threshold of 250.000 USD for pre-existing accounts.

It is difficult to answer this question in general way. Very little information is available to identify the tax residence of a pre-existing entity account e.g. the registered mailing addresses, and the customer's name. However such accounts are rare for insurance companies.

In the multilateral context, it is less clear how an indicia approach would work: while indicia of citizenship (such as place of birth) could be eliminated, a question to be addressed is how to deal with cases in which the various indicia with respect to a particular account are inconsistent (e.g. a phone number in one country, address in another and a standing order to transfer funds to a third country). How often do you think you would be confronted with conflicting indicia, if such an approach were applied in a multilateral context?

Insurance Europe agrees that using the indicia approach would lead to many conflicts. Even if indicia of foreign residency are to be found, under "treating your customer fairly" provisions an insurance company would probably "cure" the indicia before reporting. However, this comes with additional costs and as outlined before, there is still no guarantee that an insurance company will receive response from the account holder.

With this in mind, in Insurance Europe's view the only workable option for new policies would be to get the policyholder to self-certify their tax residency at the onboarding stage, and include into terms and conditions of the insurance policy that the policyholder must inform the insurance company about any changes.

It follows that in determining tax residency a FI should not be required to "reasonable assess" the self-certification as with FATCA. This is because it is likely that in some cases conflicting indicia would be found and they would have to be "cured" through self-certification.

From a business perspective, what would be a workable approach to deal with such cases? For pre-existing accounts would self-certification be a workable option in such cases?

As outlined earlier all pre-existing insurance accounts should be excluded from AEOI given the low risk of tax evasion. In case they are not exempted, the best possible solution is the indicia approach. The self-certification would not be workable for existing policies because of low response rate to requests for additional information from policyholders.

Are there situations for new accounts in which it would not be feasible to obtain a self-certification regarding tax residence?

For insurance products, there can be the situation where the beneficiary of a contract is a minor. The "self-certification" in this case would have to come from a parent or guardian.

Are you aware of any concrete example of types of financial institutions that would qualify for the Local Bank exception?

Due to overly restrictive nature of the conditions to qualify for the Local Bank exception, it is practically impossible to fall within this exception.

4. OTHER QUESTIONS

Are there other aspects of the definitions or due diligence procedures that raise issues that are particular to reporting in a multilateral context?
Are there other factors that would make reporting in a multilateral context easier or more difficult?

Before European insurance companies can proceed with reporting under the AEOI, the ongoing data protection issue needs to be resolved at EU-level. Currently, the European insurance companies would not be able to report the information under the AEOI to many non-European jurisdictions without violating the national EU member state laws that have transposed the EU Data Protection Directive. Violations of national data protection laws that have transposed the EU Data Protection Directive can include fines and, in some cases, imprisonment.

According to article 25 of EU current Data Protection Directive, an adequate level of protection has to exist in a third country for transmittal of identified data. As a number of non-EU jurisdictions, including the US, do not offer such an adequate level of privacy protection, it is our understanding that transmittal of such data would not be allowed without the insured's explicit consent. Of course the consents of policyholders, so called "waivers", were never obtained for insurance policies sold prior to FATCA as provision of this information was never anticipated at this point. It should be noted that this consent has to be 'freely given' therefore it cannot be obtained retrospectively.

In general, in order to enable multilateral data exchange, a clear national legal base is needed.