insurance europe

Position Paper

Insurance Europe response o the Foreign Account Tax Compliance Act (FATCA) - Proposed Treasury Regulations &1471-1474

Our reference:	TAX-12-066	Date:	11 May 2012
Referring to:	Proposed FATCA Regulations (REG-121647-10)		
Related documents:	TAX-10-135; TAX-11-058; TAX-11-106		
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Pages:	11	Transparency Register ID no.:	33213703459-54

Summary

I. Introduction

Insurance Europe[1] , the European insurance and reinsurance federation, welcomes the opportunity to provide comments on the FATCA draft regulations (REG-121647-10) (Proposed Regulations) that were issued by the US Treasury on 8 February, 2012.

This submission should be read in conjunction with our previous submissions FATCA of 17th November 2010 (ref. number ‚TAX-10-135'), of 22nd June 2011 (ref. number ‚TAX-11-058') and of 12th October 2011 (TAX-11-106).

This is the first time insurance specific issues have been addressed in detail. Insurance Europe appreciates the US Treasury (Treasury) and the Internal Revenue Services' (IRS) efforts to provide greater clarity and detail with respect to the application of FATCA to the insurance industry. We especially appreciate that the Proposed Regulations exclude from the due diligence procedures pre-existing life insurance and annuity contracts with a cash values of $250,000 or less and that manual review of paper records are limited to accounts with a balance or value that exceeds $ 1,000,000.

However, we believe that the Proposed Regulations needs to be modified in certain areas to better reflect the specifics of the insurance sector. In this respect, we urge Treasury and the IRS to take into consideration the points raised in this paper when finalising the final FATCA regulations.

[1] *Insurance Europe is the European insurance and reinsurance federation. Through its 34 member bodies — the national insurance associations — the Insurance Europe represents all types of insurance and reinsurance undertakings, eg pan-European companies, monoliners, mutuals and SMEs. The Insurance Europe, which is based in Brussels, represents undertakings that account for around 95% of total European premium income. Insurance makes a major contribution to Europe's economic growth and development. European insurers generate premium income of over €1 100bn, employ nearly one million people and invest almost €7 500bn in the economy.*

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While our comments concentrated specifically on the draft regulations, it is important to remember that European insurers still cannot comply with the FATCA obligations due to:

- EU Data Protection laws
- Inability to unilaterally cancel contract
- That there is no legislative mechanism for European insurance companies to withhold on our policyholders

In this respect, Insurance Europe welcomes the intergovernmental approach to FATCA implementation that was announced on 8 February 2012. We hope that this approach will allow the European insurance industry to overcome the existing impediments to comply with FATCA requirements. Furthermore, in our view the intergovernmental approach is the best way to provide clarity on country specific products and compliance issues.

II. Executive Summary

Insurance Europe would like to bring the following issues to the Treasury and IRS's attention:

- European pension accounts should be excluded from the definition of financial account as they do not represent a risk of US tax evasion and are highly regulated. In this respect, retirement and pension plans which qualify as a retirement or pension plan under the law of the country in which they are established should be excluded from the scope of FATCA.

- It follows that if retirement and pension plans were to be exempt from FATCA in the accumulation phase then consistent with that policy the fund should continue to be exempt on withdrawal, for example the use of those accumulated funds in purchasing a pension annuity for the remainder of the individual's life

- The final regulations should remove the requirement for each member of an expanded affiliated group (EAG) to be a participating FFI or a registered deemed-compliant FFI no later than January 1, 2016. In this regard, a compliant FFI or an FFI resident in a country with which the US have or are negotiating IGAs should be able to retain its status by ensuring ring-fencing of deemed and registered compliance status for the jurisdictions complying with FATCA.

- Extension of deemed-compliance status to insurance companies – In this respect, we recommend to apply the conditions for the local FFI deemed compliant status with a few modifications to reflect that: the FFI could be a member of an EAG, the European Economic Area should be treated as one jurisdiction, and it is illegal to unilaterally cancel insurance contracts.

- Reporting requirements need to be adapted to the specificities of the insurance sector.

    - Clarification is needed with respect to the types of AML/KYC rules that qualify as being acceptable for FATCA purposes
    - Insurers should be permitted to report to the IRS only on the event of pay-out.
    - Insurers should be allowed to use- third-party documentation for customer identification;
    - Re-validation of documentation should only be required when the account holder provides the insurer with new information relating to US indicia or the account holder changes.
    - The Proposed Regulations should (if at all) only determine the general requirement of internal reviews, but should not comprise further details concerning scope and content.

- Due to significant differences in local definitions of life insurance and annuity contracts, they should be defined as an account that is regulated as a life insurance or annuity contract by the jurisdiction in which the issuer operates.

- Modifications to some of the definitions included in the draft regulation are needed.

    - Annuities with no cash value should be explicitly excluded from the definition of financial account.
    - The definition of "grandfathered obligations" should be modified in order to apply to all life insurance and annuity contracts in existence on January 1, 2013.
    - The definition of "term life insurance contract" should be modified in order to remove the requirement that periodic premium payments need to be "equal" and paid "annually".
    - The Final Regulations should omit the rule that treats beneficiaries as owners of life insurance and annuity contracts.

- Reinsurance as well as property and casualty contracts should be explicitly excluded from the definition of financial accounts as they do not pose any risk of tax evasion.

- Trusts that contain one or more life insurance policies should be categorised as "life insurance trusts" and treated as grantor trusts.

- The Final Regulations should include de minimis threshold for new cash value insurance contracts to ensure a level playing field between financial institutions.

- The Final Regulations should clarify that insurance holding companies be treated as deemed-compliant FFIs where they only hold shares of participating and/or deemed-complaint FFIs.

In addition, the Insurance Europe would like to set out detailed comments below regarding the proposed FATCA draft regulations

III. Exclusion of European pension accounts

We appreciate the Treasury and IRS's efforts to exempt retirement and pension plans, however, the conditions in the Proposed Regulations are too strict and in consequence most European plans are included under the term "financial account". We believe retirement and pension plans should be exempt from FATCA because of the low or non-existent risk of tax evasion association with such products and the high degree of regulation to which the plans are subject to. It is worth mentioning that European pension scheme trustees have an obligation to deduct income tax at source from payments to pension scheme annuitants, often at income tax rates that exceed tax rates applicable to US individuals, therefore, pension schemes are very unlikely to be used as a method of sheltering income from taxation.

In this regard, we believe that the exceptions for retirement and pension accounts included in the Proposed Regulations are not broad enough.

In order to resolve this problem, we believe that, rather than specify detailed rules that almost certainly will not encompass the hundreds, if not thousands, of low-tax risk, government-registered retirement and savings plans that have been established pursuant to foreign jurisdictions' social-welfare legislation, the regulations instead should defer to the jurisdictions in which those plans are established.

Accordingly, <u>we recommend that, in lieu of detailed definitions of excluded retirement and savings accounts in the regulations, such accounts simply be defined as any account that the jurisdiction in which the FFI is organized has provided be registered or regulated in that jurisdiction as an account established for retirement or savings purposes.</u>

In the event that you do not follow the above recommendation, we urge you to widen the definition of retirement and pension accounts in §1.1471-5(b)(2)(i)(A)(2) that can be excluded from the definition of a financial account. This approach minimises unnecessary compliance for low risk products. This could be done by taking into account the following points:

- Annual contributions limited to $50,000 or less

The threshold of annual payments to $50 000 USD should be deleted. For example, in the UK current rules mean that an amount of £50,000 per annum can be contributed tax free into a pension.

Furthermore, there are also legitimate situations where the employer is obliged to make substantial extra payments to an employee retirement policy (defined benefit solutions) to make sure that the retirement benefits will be at an accurate level once the employee retires. This is typically the case when an employee late in his career gets a job with a big increase in salary. If according to the pension agreement the employee is guaranteed a defined benefit (for example 60 per cent of the employees' final salary) the employer must, in order to secure that the employee gets the retirement benefits he is entitled to, pay a onetime premium to "catch-up" and achieve the right level of retirement benefit.

The employer is allowed to deduct the one time premium calculated according to the agreement since he has not put aside enough contributions before. This does not mean that the he can deduct more than if he had set aside the right amount from the beginning. On the contrary, the tax legislation makes sure that overall the benefits for the employee evenly apportioned on his entire working life and the deduction possibilities are not exceeding the legislative levels in question. In order not make this situation disqualify a pension insurance product from being exempt from reporting we suggest that the wording would be altered in order to accommodate for these quite common situations.

- All of the contributions to be "limited by reference to earned income"

The requirement of earned income should be deleted as in the EU pension plans does not have such a limitation.

- Furthermore the reference to the "jurisdiction in which the account is maintained" should be supplemented with the words "the jurisdiction in which the member or holder is resident". Alternatively, the EEA could be defined as a single jurisdiction. This is because it is not uncommon for EU companies to sell pension plans in other jurisdictions. We have some members who do this. These plans, while maintained in one EEA country, meet the regulatory and tax favoured requirements of another EEA country where they are sold rather than of EEA country where they are maintained.

- The Proposed Regulations refer to "employees," which leaves a gap for accounts established by self-employed individuals. In order to include the same solutions for self-employed individuals who wish to top-up their retirement benefits, the wording of (b)(2)(i)(A)(1) and the condition that payments are to come from government, the employer or the employee, should be altered to make it possible for such solutions too.

- Insurance retirement products, that are regulated in the same strict way should also be exempted The only real difference is the nature of the product (account or insurance policy). If such pension insurance contracts would be exempted as well, the FATCA treatment will be equal regardless the nature of the product.

Having regard to the above, we believe that the requirements for accounts to be locally regulated as a retirement or pension account, be tax favoured, and to have penalties or restrictions on withdrawal should be sufficient on their own to identify a retirement or pension account that does not represent a risk of US tax evasion and as such can be excluded from the scope of FATCA.

Group life insurance policies

Similar to retirement plans group life insurance contracts pose a low risk of tax evasion. Group contracts are generally paid for with income earned from performance of services by employees and can be limited to those policies offered through employers and that do not allow US participants to participate if they work in the US.

Group life insurance policies are purchased by employers, companies, fraternal, social, and charitable organizations, and other groups for the benefit of a group of employees, self-employed or other individuals. Most of such insurance policies have no cash value and thus should be excluded from characterisation as US accounts. However, even if a group insurance policy has a cash value, we believe that in most instances policies should be excluded from the definition of a United States account, as the cash value cannot generally be accessed by individual group members. Furthermore, in such transactions, individual members of the pension scheme do not have a contractual relationship with the life insurer.

It is also worth mentioning that all aspects of group insurance policies are highly regulated by the employer's home country. In addition, in a number of European countries, the existence of double taxation treaties with the US means that pension plans are taxable in the country of residence, therefore reducing even further the likelihood of "group insurance policies" being used for tax avoidance by US citizens.

In view of these factors, we also urge the Treasury to exclude from the definition of United States accounts life insurance group contracts.

IV. Expanded affiliated approach

Under the draft regulations, each member of an EAG must be a participating foreign financial institution or a deemed-compliant FFI no later than January 1, 2016 otherwise all members of the EAG will be treated as nonparticipant FFI as of that date.

We are concerned that some countries will not amend their laws or enter into IGAs by 1st January 2016 and thus FFIs that are part of EAGs will find themselves unable to retain FFI status despite their best efforts to comply. The transition period is not sufficient as an appropriate amendment in the legal system cannot be influenced by the FFI in the respective country. Therefore, in order to allow an EAG to retain its FFI compliant

status, this deemed compliant status should not be affected by the FATCA status of any other expanded affiliate group member, including foreign branches.

V. Deemed-Compliant status.

1. <u>Deemed compliant status for local insurers</u>

The preamble to the draft regulations stated that *"consideration is being given … to providing a category of deemed-compliant FFIs for entities that issue certain insurance or annuity contracts that has requirements that are analogous to the requirements for local FFIs."*

Insurance Europe welcomes the Treasury and IRS's willingness to consider extending deemed compliant status to life insurance companies. We believe that such an approach would significantly reduce the administrative burden for life insurers and recognise the low risk of tax evasion of insurance products.

However, in order to permit life insurance companies to qualify for deemed compliance status the final regulations will need to reflect the specificities of the insurance sector. Therefore, the proposed requirements for local FFIs need to be modified in order to reflect that:

- The FFI could be a member of an EAG

The deemed-complaint status should apply to stand-alone insurance companies and those insurance companies that are members of an expanded affiliated group, the FFIs of which are each participating or deemed-compliant FFIs. The stand – alone subsidiary of a foreign-based multinational insurer or a foreign-based multinational is, for all practical purposes, no different than a local insurance company, and therefore the FFI affiliate of a EAG should not be treated differently under FATCA than a local stand-alone insurer.

The insurance business is inherently a local business. An insurance company is licensed and regulated under local law and typically organised in the jurisdiction in which it issues polices and sells products. An overwhelming majority of insurers do not market or sell life insurance products to residents outside of their home countries generally because of restrictions under local insurance regulatory, "know your customer" ("KYC") and anti-money laundering ("AML") rules. Around 95% of all insurance contracts are held be residents of the relevant foreign jurisdiction.

Furthermore, many of the countries impose significant local taxes, fees and charges on surrendering insurance products. . This, therefore, significantly limits the extent to which European life insurance companies could have "US persons" as customers, with US citizens living outside the US as the most likely, but very small, population of possible "US person" customers. This restriction covers all products sold by the life companies.

Furthermore, it is worth mentioning that life insurance and annuity contracts cannot be moved from one insurer to another easily, in contrast to money deposited in bank accounts. Even in the case of a surrender of one contract and a purchase of a new contract, the second insurer would always go through underwriting and other contract issuance procedures.

In addition, it is entirely possible that, due to changes in the insured's health or other factors, either the surrendering policyholder would be unable to find a replacement contract or such a contract would be prohibitively expensive. Regarding that Treasury and the IRS are concerned about expanding the scope of deemed-compliance status because of the possibility that an owner of an account in one member EAG could have its account moved to another member of the EAG and circumvent FATCA objectives, this concern is not applicable to life insurance companies. Thus, in our view it is necessary that the deemed-compliant rules treat allow the FFI to be a member of an EAG.

- European Economic Area (EEA) should be treated as one jurisdiction.

In the EEA the Consolidated Life Directive (2002/83/EC) allows a firm which is authorised and regulated by a competent authority in the EEA to provide services to another EEA state in relation to life business.

The EU has created an internal market for providing insurance services. European insurance companies and groups are subject to harmonised rules and obstacles to cross-border trade have been removed. Undertakings with cross-border business restricted to different EEA member countries should not be considered as separate jurisdictions as they are operating in the same internal market. Therefore, all references to 'country' in this paper in this context should be viewed as inclusive of the whole EEA region as a single country

- It is illegal to close down accounts as insurance policies are subject to contract law.

We believe that insurance companies should not be obliged to terminate a policyholder's contract. Insurance policies are legally enforceable contracts and governed by contract law. In any insurance contract, the insurer and policyholder fix the terms of the agreement at the beginning of the policy.

Therefore, an insurer can only request additional customer information from an existing policyholder. Experience has shown that policyholders have no incentive to agree to report their personal information to a foreign government.

Having regard to the above, we propose the following criteria for registered deemed-compliant insurer FFI:

- The FFI must be licenced and regulated under the laws of its jurisdiction (which must be FATF-compliant at the time the FFI registers for deemed-compliance status) as an insurance company.
- The FFI (taking into account its own operations and not that of any affiliate) has no fixed place of business outside its country of incorporation or organisation. However, any fixed place of business in the EEA of an entity incorporated in any EEA country will be deemed to be located in the entity's country of incorporation or organisation
- Does not solicit business account holders outside of the relevant foreign jurisdiction. However, any solicitation in the EU by an entity incorporated in any EEA country will be deemed to occur in the entity's country of incorporation or organisation.
- 95% of all insurance contracts are held by residents of the relevant foreign jurisdiction. An FFI which is organised in an EEA member state may treat policy holders that are residents (including corporate residents) of other EEA member states as residents of the country in which the FFI is incorporated or organised for the purposes of this calculation
- The FFI has policies in place to prevent opening of accounts by United States persons who are not residents of the country, non-participating FFIs, or entities controlled or beneficiary owned by US persons (as determined under Anti-Money Laundering due diligence procedures).

2. Deemed Compliance Status and Intergovernmental Agreements

In cases where IGAs are being negotiated with a country, we further recommend that all FFIs in that jurisdiction to be treated as deemed-compliant FFIs during the negotiations. That treatment would allow those FFIs to avoid the need to implement Chapter 4 compliance procedures that would be unnecessary upon execution of the IGA.

For example, if the Proposed Regulations are not amended to exempt the majority of foreign government-registered retirement or/and savings plans or accounts from the application of Chapter 4, FFIs will have to implement in the very near future processes to treat such accounts as U.S. accounts for purposes of Chapter 4, even though an IGA between the United States and the relevant foreign jurisdiction ultimately may exempt those accounts.

Treating all FFIs in a jurisdiction as deemed-compliant FFIs while an IGA between the United States and that jurisdiction is being negotiated would allow those FFIs to avoid having to adopt procedures or examine accounts that ultimately might prove to be unnecessary.

VI. Reporting

1. AML/KYC alignment

As an initial remark, we believe reporting standards for FATCA should leverage off existing standards used for Anti-Money Laundering ("AML") purposes. The current FATCA documentary evidence standards are similar to, but not fully aligned with the current AML standards.

The preamble to the proposed regulations includes the stated aim of relying on information collected during existing KYC/AML processes. However, the regulations themselves are not consistent with this aim. The EU AML/KYC procedures are risk based. Some of the products that may currently be caught by FATCA (although we consider they should be excluded) are not viewed as at risk of money laundering, and as such very little verification is done.

We recognise that not all AML/KYC requirements may be seen as sufficiently robust to fulfil FATCA reporting obligations. Therefore, clarity is needed with respect to the types of AML/KYC rules that qualify as being acceptable for FATC purposes.

2. Frequency of reporting

The Proposed Regulations require FFIs to report to the IRS on an annual basis as at 31 December. Given the long-term nature of insurance products and the fact that the income is not as accessible as a bank account, we recommend that reporting on policies should only be required when payments are made under policies. The pay-out stage is the only point at which the customer receives any benefit from the insurance contract; therefore, we do not believe that such a reporting regime would be able to be manipulated by US persons.

Irrespective of the above, reporting as at 31 December would be problematic from an insurance perspective. Insurance companies typically provide customers with an annual statement. However this will generally be done on the anniversary of when the product was taken out. Therefore it would be a costly exercise to do a further data runs on 31 December for FATCA purposes. We would therefore suggest that on 31 December we simply provide the most recent valuation that was done that year.

3. Renewal of documentation every three years

The Proposed Regulations provide that documents used to identify an account holder and his or her residence will need to be "renewed" every three years or (if earlier) upon the expiration of the identifying documents. We believe previously documented accounts should not require re-documentation unless the FFI becomes aware of a change in the client's US/non-US status.

We want to emphasize that once the life insurance contract is subscribed, the insurer does not have regular exchange with the policyholder. Certainly, the insurer must provide annual information to the subscriber on his contract, but the subscribed does not provide any information to the insurer. Instead, at the points of payment, the beneficiary and the insurer will have an actual exchange formalized the insurer may then ask questions to the client and beneficiary and collect additional information.

It is worth mentioning that that the FATF adopted new Anti-Money Laundering ("AML") standards, in February 2012. The new standards recognise that insurance is a relatively low-risk industry compared to other sectors of the financial services industry. In this respect, the new standards provide that the verification of the identity of the beneficiary should occur at the time of the pay-out. More specifically according to the new FATF standards, the insurance company shall not fall under the requirement to identify and verify the identity of the beneficial ownership, until such time there will be a pay-out to the beneficiary. This correctly reflects the fact that the beneficiary nominated in a life insurance policy, a role that in many countries is not mandatory or could change multiple times during the duration of the policy, only plays a role if the insured event occurs, for example in case of the death of the insured. In other words the beneficiary plays no role at the conclusion of the contract and during the duration of the life insurance contract, but only if the insured event occurs.

From a cost-benefit perspective, the likelihood of a client changing its status within three years is exceptionally low. However, the complexity and cost of re-documenting all new clients every three years is very high, and the customer reaction to this inconvenience is likely to be exceptionally negative. Currently, documentary evidence gathered for AML procedures is not renewed, even when it expires. Due to the long duration of many life insurance policies insurers typically have little, if any, regular contact with policyholders and often additional checks are only made just before pay-out.

Therefore, re-validation of documentation should only be required only when:

- the account holder provides the insurer with new information relating to US indicia;
- the account holder changes

4. Reliance on third-party documentation

European insurance companies frequently work with financial intermediaries and agents. When business is referred through financial intermediaries the insurance company receives a certificate which verifies that the individual's identity has been proven. Copies of the evidence collected by the intermediaries are generally not passed on to an insurance company. For this reason it is very important for European insurance companies to be able to rely on third party documentation for FATCA purposes.

In this respect, it is worth mentioning that some of our members provide both banking and insurance services. Often the banking side will refer business to the insurance part of the business. In this case the banking part would have already done verification checks on the individual concerned.

In this situation we ask that the insurance part of the business does not have to reduplicate the due diligence checks on the individual being sold an insurance product.

5. Internal review

Insurance Europe welcomes the consistent terminology of a "responsible officer" in the proposed regulations, replacing the terms „chief compliance officer or another equivalent-level officer" or „high-level management employees" used in the previous notices. A consistent terminology assures legal certainty

According to the Proposed Regulations, the verification process for determining a participating FFI's compliance with its FFI agreement will require (i) written compliance policies and procedures, (ii) periodic internal reviews of its compliance and (iii) periodically provided certification to the IRS. With regard to internal reviews, Insurance Europe rejects any regulatory determination of detailed requirements.

As laid down at present, the Proposed Regulations should (if at all) only determine the general requirement of internal reviews, but should not comprise further details concerning scope and content. It shall be left to the undertaking`s responsible officer to decide how to establish internal reviews. Detailed requirements create additional bureaucracy for insurance undertakings. Therefore, the organization of internal reviews must remain within the undertaking`s responsibility.

Next, for both initial certifications and ongoing certifications, to the maximum extent possible, an expanded affiliated group should have the option to minimize the number of such certifications by centralizing the responsibility. Under such global certification, the certifying responsible officer would rely on similar certifications made to her by responsible persons in the expanded affiliated group.

VII. Recognition of local definitions of life insurance and annuities contracts

The definition of "life insurance contracts" and "annuity contracts" would benefit from further clarification. "Life insurance contracts" are defined in the Proposed Regulations by cross-reference to sections 7702, 101(f) and 817(g). The cross references are confusing and may give rise to misinterpretation. Given that compliance with FATCA reporting obligations will likely fall on FFI operations personnel who are not versed in United States tax law, we think that it would be in the interest of both insurers and the IRS to make the underlying definitions clearer and thus easier to apply in practise. In addition, given the multitude of products issued by life insurance companies and the fact that the "customary practices" of insurers may differ among different jurisdictions, we believe there is a risk that the definition of life insurance and annuity contracts contained in the Proposed Regulations will not be uniformly understood or applied.

In order to avoid the foregoing problems, we recommend that life insurance and annuity contracts be defined as a contract that is regulated as a life insurance or annuity contract by the jurisdiction in which the issuer operates.

VIII. Revised definitions applicable to life insurance and annuity contracts

1. Revised definition of "Grandfathered Obligation"

The Proposed Regulations define a grandfathered obligation as any legal agreement in existence on January 1, 2013 that produces or could produce a passthru payment. This definition includes a life insurance contract payable on the earlier of attaining a stated age or death and a term certain annuity.

However, the Proposed Regulations are not clear as to whether annuities payable upon death are grandfathered. Although we recognize that such contracts do not have a term specified in years, they clearly do have a "stated expiration" as death remains an unavoidable event and the remaining length of such a contract can be actuarially determined. Thus, no withholding tax obligation should apply with respect to pre-existing life insurance contracts and annuities issued on or before January 1, 2013 as life insurance and annuity contracts are legal agreements with definitive terms and could produce passthru payments under chapter 4.

Furthermore, the definition of "Grandfathered Obligation" state that an obligation is outstanding on January 1, 2013, if a legally binding agreement establishing the obligation was executed between the parties before January 1, 2013. Any material modification of an outstanding obligation will result in the obligation being treated as newly issued or executed as of the effective date of such modification. However, it should be clarified further what is meant by a "material modification". Currently, the draft regulations only state that whether a modification of an obligation is material will be determined based upon all relevant facts and circumstances. In view of legal certainty, reference should be made to the definition of a "material modification" under local law.

2. Exclusion of annuities with no cash values from definition of financial account.

We believe the final regulations should exclude annuity contracts without cash value from the definition of financial accounts.

We understand that this definition was based on Treasury and the IRS's expectation that all annuities have a cash value to which an annuity owner can have access. In the European Union, insurance companies issue annuity contracts which_makes a series of future payments to the annuitant. However, the annuitant cannot access any cash value under the contract and the annuity terminates upon the death of the annuitant. Annuities of this type are one of the mechanisms by which retirement income can be drawn from pension savings accumulated in a plan. The annuity effectively converts the pension fund savings into a taxable income stream for life.

There is no reason why annuities with no cash value should be treated differently than life insurance contracts that lack cash value. Thus, these products do not pose a tax avoidance risk from a US tax perspective and they should be excluded from the Final Regulations.

3. Revise definition of "Term Life Insurance Contract"

The Proposed Regulations exclude term life insurance from the definition of a financial account. However, the Regulations exclude only level premium term life insurance policies. Many European countries have term life insurance policies that are clearly term policies under local law but yet would not meet the criteria proposed in the Proposed Regulations. The equal periodic payments are not a common feature of term life insurance policies in many European countries. For example, it is typical in countries that have experienced high rates of inflation to include an inflation index in the return on term insurance i.e.: a small amount above the aggregate premiums paid into the policy.

Furthermore, in the EU in some countries single premium term life policies still exist. As the definition in the regulations refers to "equal periodic premiums are payable annually" these policies will be caught. In addition, there are classes of contracts that have fixed premiums for a period but a clause in the contract to allow the policyholder to make the policy "paid-up" after which no additional premiums are due. As these policies are purely protection policies and have no cash value then such policies will not be used for tax evasion.

Next, there are some policies whereby if at the end of the term no claim has been made, a cash back of usually a very small percentage (maximum 10-15%) of the total value of the premiums paid is payable. This can be likened to the "free gifts" that general insurers may give policy holders to encourage business. While we do not think that these will be caught by the draft regulations we would appreciate clarity that this is the case.

We would therefore suggest that definition of "term life insurance contract" be modified in order to remove the requirement that periodic premium payments need to be "equal" and paid "annually".

4. Definition of Holder of Account

The Proposed Regulations contain special rules for identifying the "holders" of life insurance and annuity contracts that constitute financial accounts.

- if the owner can access the cash value of a contract then the contract owner is considered the "holder"
- if the contract holder cannot access the cash value then the beneficiary of the contract is considered the holder of the contract for Chapter 4 purposes.

The latter presumably means that an insurer must obtain account identification information for each beneficiary of a matured insurance or annuity contract before it can make payments to the beneficiary and otherwise must treat the beneficiary the way that it treated the contract owner prior to maturity

This is particularly problematic for insurance companies as the beneficiary plays no role at the conclusion of the contract and during the duration of the life insurance contract, but only if the insured event occurs. The beneficiary can only claim an insurance benefit when the insured event has taken place. As long as this event does not occur, the beneficiary is no involved party in the insurance contract. The insurance company is not entitled to request any information from the beneficiary of a contract.

Impose a search on absolute beneficiaries is impossible for material reasons. This is contrary to insurance sector practices, since insurers do not have relations with such beneficiary as they are not clients. More, this would lead to inconsistencies when the beneficiary dies before the insured person or when the account holder changes the designated beneficiary in the course of the contract.

For these reasons we would ask that these rules be deleted.

IX. Exclusion of Reinsurance and Property/Casualty contracts from the definition of "Cash Value Insurance Contracts"

The Proposed Regulations state that life insurance or annuity contracts without cash value, term life, accident/health/medical and disability, and other protection insurance policies should not be treated as financial accounts as they present no tax evasion risk. However, the proposed regulations are silent on treatment of life reinsurance and property/casualty contracts.

Reinsurance contracts are complex and highly structured transactions. Even if reinsurance contracts cannot be considered cash value insurance contracts or annuities, reinsurance companies issue payments with respect to financial accounts (maintained by the respective primary insurance companies ceding risk to the reinsurers) and, thus, could still be considered as financial institutions under the FATCA regime. For example, in the event of commutation i.e. transfer the risk back from the reinsurer to the original ceding company the reinsurer typically would pay funds at present value that are not yet due under the reinsurance agreement to the original ceding company to reflect the transfer of insurance risk back to the cedent. Depending on how Proposed Treasury Regulations §1.1471-5(b)(3)(v)(B) is interpreted, such amount could be considered evidence of "cash value" that the ceding company "is entitled to receive upon … termination of the contract."

Therefore, the regulations should not rely on the definition of "cash value" to exclude such contracts from treatment as cash value insurance contracts. This approach causes uncertainty over whether or not it is meant to be covered. Reinsurance policies indemnify an insurer against all or part of the loss that the insurer may sustain under the original policy or policies it has issued. These are business to business transactions sold only to other insurance companies. Reinsurance recoveries are not available to individuals or other non-insurance entities.

Similarly, the regulations should not rely on the definition of "cash value" to exclude such property and casualty contracts from treatment as cash value insurance contracts.

In this respect, the Final Regulations should clearly state that reinsurance and property and casualty contracts are outside the scope of definition of cash value insurance contracts.

X. Life Insurance Policy Trusts

Some European life insurance policies are written under trust. For the purpose of the regulations we would recommend that trusts that contain one or more life insurance policies be categorised as "life insurance trusts" and treated as grantor trusts, i.e. the individual identified (and hence subject to reporting) is the settlor/grantor.§1.1471-5(a)(3)(ii). In many cases the settlor will also be the trustee.

Typically a single trust will be used for each policy or plan and the person creating the trust is known as the settlor, and the settlor appoints the initial trustees and beneficiaries. Typically, the person who creates the trust (grantor) would be a trustee of a life policy trust anyway.

Under §1.1471-5(a)(3)(i) of the draft regulations a life insurance policy held in trust is not an individual account, but an entity account. There is also a question as to whether policies written in such a way would themselves be FFIs. Under the draft regulations, trusts are categorised according to US classification, such as grantor trust, simple trust or complex trust. If the above deemed compliant status is not granted, to would be a difficult, time consuming and hence expensive process to re-categorise European life insurance policy trusts according to US legislation and European trusts may not all map onto US definitions of trusts.

Furthermore, in some countries often (i.e.in the case of a discretionary trust) the grantor creates categories of „potential beneficiaries". These will typically include spouses, children and grandchildren, the names of whom are not always known, and in some circumstances they may not have even been born yet. No beneficiary has a legal right to demand either income of capital from the trust. Some potential beneficiaries may receive nothing at all from the trust as ultimately it is up to the discretion of the trustee(s).

Also, due to historic ways in which these trusts may have been recorded (e.g. the insurer may not have been told that this is a policy held in trust, nor seen the trust deed), it is not always possible for European life insurance companies to identify these accounts within existing records.

XI. Adoption of a De Minimis Exemption for Cash Value Insurance Contracts

The statute and the proposed regulation include a $50,000 de minimis threshold for depository accounts opened by a US person after the effective date of the FFI agreement by a US person. We ask that Treasury and the IRS consider adopting a similar de minimis exemption for cash value insurance contracts, to ensure an equitable position exists between financial institutions.

By not having a similar de minimis for new insurance contracts, FFIs carrying on insurance business will have an extra compliance burden than those carrying out banking business. Furthermore, for the reasons explained in our previous submissions on FATCA, insurance contracts with a cash value of $50,000 or less do not present any realistic risk of United States tax evasion.

For individual policies that do not exceed the de minimis threshold, ongoing administrative and FATCA monitoring costs related to the policies would be reduced by excluding them from U.S. account treatment. Furthermore, it would limit the amount of information both the IRS and other revenue authorities (who adopt an IGA) would collect and process, thus reducing the cost of FATCA for governments.

Indeed, there may be a good case for cash value insurance products to have a higher de minimis (as reflected in the de minimis for pre-accounts). The cash value for insurance products does not just reflect the investment element of the product, but often is used to fund expenses, guaranteed returns and protection type benefits such as mortality expenses.

XII. Insurance holding companies.

According to the Proposed Regulations an insurance holding company would be considered an FFI although it does not maintain any financial accounts. Such a holding company would be obligated to become a participating FFI since it could not become a registered deemed-compliant FFI pursuant to the requirements of Prop. Reg. § 1.1471-5(f) (1)(i)(B) (e.g., it has no “accounts” and lacks the ability under to transfer any such account it might have) or otherwise under any of the other deemed-compliant categories described in Prop. Reg. § 1.1471-5(f). We believe that the final regulations should clarify that insurance holding companies be treated as deemed-compliant FFIs where they only hold shares of participating and/or deemed-compliant FFIs.