

To: Taxation Committee
From: Macro-Economics, Life and Pensions department
cc: International Affairs & Reinsurance Committee
Date: 7 August 2012
Reference: TAX-12-076

Subject: US FATCA - Model IGAs potential IE actions

Action requested

Members are requested to:

1. Comment on whether Insurance Europe should send a letter) on the recently published Model Intergovernmental Agreement (IGA) to the US Internal Revenue Service (IRS) and 5 EU Member States (the UK, Spain, Italy, France and Germany).

If yes, members are invited to comment on the questions included in this memo and also to highlight other points not included in this memo which they believe Insurance Europe should include in a letter.

2. Inform Insurance Europe Secretariat whether their national legislation has a \$50,000 annual contribution limit on retirement and pension accounts as stated in the proposed FATCA regulations.

Comments are to be provided to madejski@insuranceeurope.eu, grant@insuranceeurope.eu and ostrauskiene@insuranceeurope.eu by **15 August cob**.

Summary of the model Intergovernmental Agreement

On 26 July the model Intergovernmental Agreement (model IGA) to facilitate the implementation of the Foreign Accounts Tax Compliance Act (FATCA) was published. This agreement with the US was negotiated by the UK, Spain, Italy, France and Germany. The IGA has been designed so that financial institutions that adopt it will look to this agreement and their own domestic law to comply with FATCA. There are two versions of the model agreement—a reciprocal version and a non-reciprocal version.

This memo provides a summary of the model Intergovernmental Agreement (IGA) and compares it to Insurance Europe requests (if applicable) in our submissions on the FATCA draft regulations and bilateral intergovernmental agreements. Based on this comparison we have identified potential issues that could be addressed in a potential Insurance Europe response to the model IGA.

I. The scope of Model IGA

In our recent submission, Insurance Europe stated that the scope of FATCA should be limited to cash value life insurance and annuity contracts. As a result, Insurance Europe requested that the following contracts be excluded from the FATCA scope:

- European pension products;
- annuities with no cash value; and
- property and casualty, and reinsurance contracts



In addition, Insurance Europe requested a \$ 50,000 de minimis threshold for new insurance contracts and the definition of "grandfathered obligations" to apply to all life insurance and annuity contracts in existence on January 1, 2013.

With respect to the above, the model IGA includes the following provisions:

1.) Definition of Financial Account

The model IGA limits FATCA application to cash value insurance contracts and annuity contract. The model IGA excludes from the definition of annuity contracts, contracts paid to an individual that monetise pension or disability benefits provided by an arrangement or a contract that is excluded from the definition of financial account in Annex II. Annuity contracts are defined as contracts providing for payments with respect to the life expectancy of an individual or individuals, as well as a contracts treated as annuities under the law of the FATCA partner.

(Insurance Europe remark) In line with Insurance Europe's request, the Model IGA FATCA application is limited to cash value insurance contracts and annuity contracts. Non- cash annuity contracts should be excluded from the definition of financial accounts in the country specific annex (Annex II).

2.) European pension and retirement products

The Model IGA states that that country specific annex (Annex II) to the agreement will contain the list of entities, plans and retirement products that will be excluded from the FATCA scope. This annex which is negotiated bilaterally between the U.S. and Member States is expected to be issued shortly.

(Insurance Europe remark) The above is in line with our latest submission where we stated that IGAs are the best way of allowing the United States and each IGA counterparty to identify accounts in a country that have low associated United States tax risk and that therefore should be excluded from treatment as U.S. accounts, such as pension products.

3.) De Minimis Exemption

The model IGAs provide an exclusion from the definition of cash value insurance contract for life insurance contracts with a cash value of \$50,000 or less, but they do not extend the exclusion to low-value annuity contracts.

(Insurance Europe remark) The model IGAs provide an exclusion from the definition of cash value insurance contract for life insurance contracts with a cash value of \$50,000 or less, but they do not extend the exclusion to low-value annuity contracts.

In this respect, members are requested to provide feedback on the following question:

Should Insurance Europe ask for extension of the \$50,000 threshold to annuity contracts?

4.) Grandfathering clause

The model IGAs exclude from the individual pre-existing account due diligence procedures any cash value insurance contracts and annuity contracts entered into on or before December 31, 2013, where U.S. law or the law of the FATCA partner effectively prevents the sale of such contracts to U.S. residents.

(Insurance Europe remark) This is in line with our recent submission, when we asked to extend the definition of "grandfathered obligations" to all life insurance and annuity contracts.

II. Definition of cash value insurance contract and annuity contract.

Insurance Europe requested that 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. Furthermore, Insurance Europe underlined that cash value should be defined as surrender value, taking into account surrender and other charges.

With respect to the above, the model IGA includes the following provisions:

1. Cash Value Insurance Contract

The model IGA defines an insurance contract as a contract under which the issuer agrees to pay an amount upon the occurrence of a specified contingency involving mortality, morbidity, accident, liability, or property risk. The term "cash value" is defined as (1) the amount that the policyholder is entitled to receive upon surrender or termination of the contract (determined without reduction for any surrender charge or policy loan), and (2) the amount the policyholder can borrow under or with regard to the contract. The cash value insurance contract definition excludes amounts payable for personal injury or sickness or indemnification of an economic loss incurred upon the occurrence of the event insured against; a premium refund due to cancellation, decrease in risk, or a correction; or a policyholder dividend based on the underwriting experience of the contract or group involved.

(Insurance Europe remark) In line with Insurance Europe's request, the model IGA recognises local definitions of annuities and defines cash value as a surrender value. However, the model IGA does not rely on local definition for life insurance contracts, but provides its own general definition.

In this respect, members are requested to provide feedback on the following question:

Is the definition of an insurance contract included in the IGA acceptable for European insurance companies?

2. Annuity Contract

The model IGA defines an annuity insurance contract as a contract under which the issuer agrees to make payments for a period of time determined in whole or in part by reference to the life expectancy of one or more individuals. The term also includes a contract that is considered to be an Annuity Contract in accordance with the law, regulation, or practice of the jurisdiction in which the contract was issued, and under which the issuer agrees to make payments for a term of years.

(Insurance Europe remark) In line with Insurance Europe's request, the model IGA recognises local definitions of annuities.

III. Expanded affiliated approach

Insurance Europe requested that in order to allow an expanded affiliated group to retain its FFI compliant status, the deemed compliant status should not be affected by the FATCA status of any other expanded affiliate group member, including foreign branches. 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.

With respect to the above, the model IGA recognised that there may be jurisdictions where local law will never permit an FFI operating therein to achieve full FATCA compliance. In this respect, the model IGAs permit FATCA-partner FFIs to remain compliant even if there is a non-compliant affiliate member within the EAG, so long as the non-compliant affiliate meets the following requirements:

- The limited FFI: (1) identifies itself as a non-participating foreign financial institution (NPFFI); (2) identifies its U.S. accounts and reports, when permitted; and (3) does not specifically solicit U.S. accounts that are held by non-residents or NPFFIs that are not established in the country where the limited FFI is operating; and
- The FATCA Partner Financial Institution does not use the limited FFI in its group to circumvent its obligations under the relevant rules.



(Insurance Europe remark) In line with Insurance Europe's request, the model IGAs permits FATCA-partner FFIs to remain compliant even if there is a non-compliant affiliate member within the EAG, so long as the EAG has members that are NPFFI.

IV. Reporting obligations

Insurance Europe requested that due diligence procedures should permit the use of local AML/KYC rules. With respect to reporting frequency, Insurance Europe requested that FATCA reporting be done at the payment stage; with insurance companies providing the most recent valuation that was done that year at the end of the year.

Next, regarding documentation requirements Insurance Europe requested that previously documented accounts should not be re-validated when an FFI becomes aware of a change in the client's US/non-US status and insurance companies should be able to rely on third party documentation.

Finally, Insurance Europe underlined that insurance companies should be allowed to identify beneficiary only when the insured event takes place. For consistency with other financial accounts, the beneficiaries of life insurance and annuity contracts should not be treated as the holders of accounts and be required to capture information about beneficiaries at maturity of a contract (maturity rule) or when they can access the cash value of a contract (cash access rule).

With respect to the above, the model IGA includes the following provisions:

1. Use of AML/KYC rules

The Model IGA allows the use of local AML/KYC rules in connection to FATCA due diligence procedures.

(Insurance Europe remark) This is in line with Insurance Europe's request.

2. Frequency of reporting and information to be exchanged

The Model IGA requires insurance companies to exchange FATCA required information annually. According to the Model IGA the information to be exchanged is the account value as of the end of the relevant calendar year or other appropriate reporting period or, if the account was closed during such year, immediately before closure.

(Insurance Europe remark) In its recent submission, Insurance Europe stated that insurers should be permitted to report to the IRS only on the event of pay-out.

In this respect, members are requested to provide feedback on the following question:

Should Insurance Europe ask to report on insurance policies only in the event of a pay-out?

3. Documentation requirements

The Model IGA allows FFIs to use third party service providers to fulfil their documentation obligations for FATCA purposes, but these obligations shall remain the responsibility of the reporting FFI.

(Insurance Europe remark) This is in line with Insurance Europe requests.

4. Definition of Account Holder

According to the model IGA the account holder is the person entitled to access the cash value (cash access rule) or to change the beneficiary. If there is no such person, then the account holder is the owner named in the contract and any person with a vested entitlement to payment. At maturity, the account holder is any person entitled to a payment under the contract (maturity rule).

(Insurance Europe remark) The definition of account holder as applied to cash value insurance and annuity contracts relies on the maturity and cash access rules.



In this respect, members are requested to provide feedback on the following question:

Should Insurance Europe ask for the maturity and cash access rules to be deleted?

V. Data Protection

Insurance Europe stated that without an appropriate legal basis European insurance companies will not be able to transfer FATCA required data to the US without being in breach of their national Member States laws that transposed the EU data protection directive.

The Model IGA states that the US will enter into an agreement with partner countries in order to establish the procedures for the automatic exchange obligations Under FATCA provisions.

(Insurance Europe remark) Under the IGA insurers will report the required information to their own tax administration and not directly to the IRS based on the agreement between US and partner country. This should not result in a breach of the data privacy laws.

VI. Other

Timeline

The Model IGA states that a Partner FFI may treat any account opened in 2013 as a pre-existing account, which means a delay in the requirement for on-boarding new accounts until January 1, 2014.

(Insurance Europe remark) The Model IGA contains a welcome modification to the account identification timeline.

Modification of definition of financial institution

The Model IGAs confirm that insurance companies that do not issue cash value life insurance contracts or annuity contracts are not FFIs, but rather are non-financial foreign entities (NFFEs). Only passive NFFEs are required to identify and report their substantial U.S. owners, if any. In this regard, the Model IGA provides that an NFFE will be considered active if:

- Less than 50% of the NFFE's gross income for the preceding calendar year or other appropriate reporting period is passive income and less than 50% of the assets held by the NFFE during the preceding calendar year or other appropriate reporting period are assets that produce or are held for the production of passive income; or
- The stock of the NFFE is regularly traded on an established securities market, or the NFFE is an entity related to an entity the stock of which is traded on an established securities market.

As a result, NFFE insurance companies that are resident in a country that enters into a model IGA and that are regularly traded on an established securities market, or are related to an entity that is so traded, will be active NFFEs and therefore exempt from the IGA's due diligence and reporting requirements. However, because there is no carve-out from passive income for investment income earned on the capital or reserves of an otherwise active insurance company, insurance companies that are not regularly traded, or related to a regularly traded entity, generally will be considered passive NFFEs and will be subject to the reporting requirements of the model IGA.

Background to the request for information on annual contribution limits for retirement and pension accounts

Under the proposed FATCA regulations an individual pension product in jurisdictions where the annual contribution limit is in excess of \$ 50 000 will be caught by FATCA. Insurance Europe in its and INIA comments on the FATCA draft regulations stated that the threshold of annual payments to \$ 50 000 should be deleted. As a follow up to these comments Insurance Europe together with American Council of Life Insurers (ACLI) and Canadian Life and Health Insurance Association (CLHIA) intend to provide the IRS with examples of



monetary contributions limits in individual countries that are higher than the \$50 000 annual limit in the FATCA proposed regulations.