THE ADVANCED DIPLOMA IN INTERNATIONAL TAXATION

June 2021

MODULE 3.05 – BANKING OPTION

SUGGESTED SOLUTIONS

PART A

Question 1

Part 1

Under s.46 of the criminal finances act, where the financial institution has a UK connection, failure to prevent the facilitation of non-UK tax evasion would be an offence.

However, an offence is only committed where it meets a requirement of dual criminality, therefore recognising that different countries approach the criminalisation of taxpayer non-compliance differently. The offence is a criminal offence in the country where it is committed but also the offense would be considered as the fraudulent evasion of tax in the UK.

Additionally, the facilitation offence must be a criminal offence in the jurisdiction where it is committed and would, if the foreign tax evasion offence were a UK tax evasion offence, also be a tax evasion facilitation offence in the UK.

In the case outlined, the German taxpayer, Mark, has committed an offence contrary to section 370 of the German Fiscal Code. He is assisted by an employee of Goal Bank GmbH who is also based in a branch in Germany.

There is therefore dual criminality at the taxpayer level as there is an equivalent offence in 106A of the Taxes Management Act 1970 (fraudulent evasion of income tax).

The facilitating acts of the staff of the bank would be an offence if done in the UK and Germany also has the equivalent offence, criminal facilitation of tax evasion, by virtue of sections 26-27 of the German Fiscal Code. (comment: 370 AO German General Fiscal Code, determines the criminality of tax evasion, section 26 and 27 StGB (German Criminal Law Act) – determine that a criminal offence also exists if a) there is an incitement (26 StGB) or a facilitation (27 StGB). You read them together: 370 AO and 27 StGB. If you do not have an incitement, don't cite it.

There is therefore dual criminality at the taxpayer and associated person levels.

Part 2

Goal Bank GmbH is within scope of the foreign tax evasion offence as it is a relevant body that carries on part of its business in the UK.

The fact that the company is incorporated under Swiss law, and that the facilitating acts of its associated person took place outside the UK, does not take it outside the scope of the Corporate criminal offence.

It is a legal person that carries out part of its business in the UK and is within scope of the foreign tax offence.

Goal Bank GmbH will be guilty of the foreign tax evasion offence unless it can establish the defence of having reasonable prevention procedures.

Maybe some Swiss students will want to mention that there is no criminal offence under German law for a legal person. Only individuals can be prosecuted that act for Goal Bank GmbH (at least that is what I have learned when studying German law) [for info, Switzerland does not extradite for tax crimes].

Part 3

For the purposes of the directive, an intermediary is defined as firstly any person with an EU connection that designs, markets, or organises, facilitates or manages the implementation of a reportable cross-border arrangement; and secondly anyone who provides aid, assistance or advice in respect of a reportable cross-border arrangement, or anyone who could be reasonably expected to know that such aid, assistance or advice relates to a reportable cross-border arrangement.

The DAC 6 reporting obligations apply mainly to intermediaries. Although secondary obligations do fall on the actual taxpayers themselves in cases where there is no intermediary, or no EU intermediary resident in the EU or whereby the intermediary is exempt from reporting because of legal professional privilege.

The intermediary must disclose information to the competent authorities on a reportable cross-border arrangement within thirty days beginning on the day after the arrangement is made available or is ready for implementation to the taxpayer or when the first step of such arrangement has been implemented.

Where there is no intermediary to report the arrangements, the taxpayer has the responsibility to disclose such information is within thirty days beginning on the day after the arrangement is available or is ready for implementation or when the first step of such arrangement has been implemented.

Additionally, taxpayers may file information about their use of reportable arrangements in each of the subsequent years for which the arrangement is used.

With regard to the deadlines for reporting historic cross border arrangements, that is from cross-border arrangements implemented between 25 June 2018 and 30 June 2020, transitional provisions are to allow for "*once-off reporting*" between 1 July 2020 and 31 December 2020.

The information required in the actual disclosure will include the identification of the intermediaries (if there are intermediaries) and relevant taxpayers, their country of residence and tax identification (TIN). In addition, a summary of the arrangement itself will have to be included, which would include details on the relevant hallmarks that make the cross-border arrangement reportable.

In addition, details on the timing of implementation, and information on the value of the reportable cross-border arrangement. Identification of Member State(s) that are affected or likely to be concerned by the reportable arrangement would be included, as would the identification of any other person(s) in Member State(s) likely to be impacted by the reportable cross-border arrangement – indicating to which member state such person is linked.

A reference number for the arrangement - so that if more than one intermediary or taxpayer is obliged to file the information, one single reference number should feature on all the exchanges so that they can be linked to a single arrangement.

<u>Part 4</u>

In order for cross-border arrangements to trigger a reporting obligation, at least one of the hallmarks must be met. Such hallmarks may be generic or specific. As regards the generic hallmarks and a number of specific hallmarks, these may only be taken into consideration as long as they meet the so-called "main benefit test". This test will be met if obtaining a tax advantage constitutes the main benefit or one of the main benefits that is expected to derive from an arrangement.

Generic hallmarks target features that are common to promoted schemes, such as the requirement for confidentiality or the payment of a premium fee. Generic hallmarks can be used to capture new and innovative tax planning arrangements as well as mass-marketed transactions that promoters may easily replicate and sell to a variety of taxpayers.

Specific hallmarks are used to target known weaknesses in the tax system and techniques that are commonly used in tax avoidance arrangements such as the use of loss creation, leasing and income conversion schemes.

In addition specific hallmarks exist for cross border transactions, for example deductible cross-border payments between associated enterprises in cases where the recipient is not resident for tax purposes in any jurisdiction, or the recipient is resident for tax purposes in a jurisdiction levying corporate income tax at the rate of zero or almost zero.

Specific hallmarks which relate to other cross-border transactions (for example deductions for the same depreciation, relief from double taxation in more than one Member State), transfer pricing and automatic exchange of information and beneficial ownership, which do not need to comply with the main benefits test, are also incorporated in the Directive.

Question 2

The Internal Audit (IA) recommendations recognise the following matter.

- Reporting dividend and interest and other income credited to clients' accounts not of any applicable withholding transaction taxes.

The following considers whether to report amounts net of applicable withholding taxes, this consideration will not address gross proceeds (as generally no withholding taxes are imposed on gross proceeds) nor account balances (as we understand that only amounts net of applicable withholding taxes are considered when determining the account balance).

Legal basis

The income amounts an FI needs to report with respect to a custodial account are the following:

The total gross amount of [income] …generated with respect to the assets held in the account, in each case paid or credited to the account (or with respect to the account) during the calendar year or other appropriate reporting period. (CRS Sec I.A.5.a, CRS MCAA Sec 2.2.e.1and e.g. Model 1 IGA Reciprocal, Pre-existing TIEA or DTC, 30 November 2012, Art 2.2.5.a; Treasury Regs. s1.1471-4(d)(iv)(B))

Noting that the Treasury Regulations do not similarly include the text "or with respect to the account" (Treasury Regs. s1.1471-4(d)(iv)(B))

Where the amount of payments made:

The amount…of payments made with respect to a US Reportable Account may be determined in accordance with the principles of the tax laws of the jurisdiction exchanging the information. (Model 1 IGA Reciprocal, Pre-existing TIEA or DTC, 30 November 2014, Art. 3.1)

FIs may choose between different options, e.g. to make the determination (Treasury Regs s1.1471-4(d)(4)(iv)(E))

Where the account balance:

is the balance or value calculated by the FI for purposes of reporting to the account holder (CRS Commentary, p98 para 12)

The balance or value of a financial account is the balance or value calculated by the FI for purposes of reporting to the account holder (Treasury Regs. S1.1471-5(b)(4)(i))

Analysis

From a review of the regulations it is noted that the regulatory obligations do not explicitly address the question of reporting gross or net of withholding tax, nor is there a definition of the term "gross amount" or guidance or examples of how to interpret the term "paid or credited to the account".

Having said that and considering the approach taken:

- The approach meets the "paid or credited to the account" requirements where the amount credited to the account holder is net of withholding tax;

- The approach is the consistent with the reporting of account balances. For example, if the account balance as of 31 December 202X is USD 100 and the account holder receives a dividend of USD 7 (after the deduction of WHT of 305) during the year 202X + 1, all other things being equal, the account balance as of 31 December 202X + 1 will be USD 107.

- The approach is consistent with the reporting to the account holder, even though the Bank not only reports income amounts net of applicable withholding taxes to its account holders but also provides them with the respective amounts prior to the deduction of withholding taxes.

Conversely:

- Whilst the approach places heavy reliance on the term "paid or credited to the account" it ignores the "gross amount" requirement.

- Although there is no CRS / FATCA definition of the term "gross amount", it can be argued that the term "gross amount" refers to the income amounts before the deduction of applicable withholding taxes. This reflects the fact that dividends, interest and other income are not typically reduced by any fees or commissions, i.e. any difference between the "gross amount" and the "net amount" is related to applicable taxes withheld.

- Following a literal interpretation of the Treasury Regs which do not make reference to the amount paid or credited "with respect to the account", in this context there is a conflict between the term "gross amount" and "paid or credited to the account", which can only be resolved by giving priority to one term over the other, it would seem unlikely that this interpretation is in line with the intention of the regulator.

Conclusion

From the above our interpretation of the regulations leads to the conclusion that the amounts reported should be gross of withholding tax.

In consequence we advise that all future returns should be filed on a gross of withholding tax basis.

Considering any remediation requirement, it should be noted that the regulations do not specify the exact circumstances requiring an FI to correct a prior year CRS or FATCA report or how back potential corrections need to be filed. To determine the remediation period the following should be considered:

- The significance of the not reported taxes withheld compared to the total income amounts actually reported for account holder;

- The year to which the relevant CRS / FATCA reports relate as the further in the past any such report is the relevance of the difference becomes less significant as it may be assumed that any related tax assessments on the reported persons will have already been closed; and

- If the relevant tax authorities generally expect amendments to prior year reports or if they apply penalty provisions for refiling.

Is this an Event of Default?

Based on our analysis, this is not an event of default considering the following:

- A material failure includes "a failure of the FFI to fulfil the requirements of the agreement if the failure was a result of a deliberate action….to avoid the requirements of the FFI agreement". Albeit the failure was deliberate it was on the understanding that the approach would be in-line with its FATCA obligations.

- Such a failure also includes "a failure of the FFI to fulfil the requirements of the FFI agreement if the failure.was an error attributable to a failure of the FFI to implement internal controls sufficient for the FFI to meet the requirements…". It is noted that the internal control and the subsequent follow-up resulted in the identification of the potential discrepancy, therefore this suggests that there are not insufficient internal controls.

- The examples provided in material failure include a “deliberate or systemic failure of the FFI to report accounts that it was required to treat as US accounts…”, whereas the approach taken did not result in any US account being excluded from FATCA reporting.

PART B

Question 3

Capital allocation approach/BIS ratio:

SafeBank Ltd has a Tier 1 capital ratio of 16.4% (7700/47000 *100).

The BIS ratio for the capital allocation approach would be 10% and the PE would need to be attributed 10% of the bank's Tier 1 capital.

The PE would have the same Tier 1 capital ratio of 16.4% as the bank as a whole i.e. £1,000.4m

Thin capitalisation approach: The PE would have an equity capital of £854m (£6,100m *14%) i.e. tier 1 ratio of 16% in line with independent banks carrying on similar activities in the PE host country.

Regulatory minimum capital ratio in the PE host country, in this example £549m (£6,100m *9%)

When the attributable capital has been calculated for a PE for tax purposes, it then needs to be analysed against the amount of free capital that has actually been booked in the branch balance sheet for accounting purposes.

If the free capital booked in the branch accounts is less than the capital attributable to the branch, and adjustment will likely have to be made to the amount of interest expense allowed in the branch in the host country in order to reflect the free capital that it actually needs to support the RWA on its balance sheet.

Part 2 of the OECD authorised approach OECD report on attribution of profit to PEs (2010) analyses the special considerations in applying the OECDs authorised approach to PEs of banks.

In the authorised OECD approach functional and factual analysis is used to delineate the PE as a hypothesised separate and independent enterprise. Functional and factual analysis will also consider the assets used and risks assumed because of performing those functions.

The functional and factual analysis ultimately determines the attribution of profits to the PE in accordance with its functions performed, assets used and risks assumed by the PE.

The OECDs approach places a key emphasis on the determination of the key entrepreneurial risk-taking functions of the enterprise and to the degree that the PE undertakes those key risk-taking functions. This is on the basis that the performance of those functions that leads to the assumption of the most significant risks and the authorised OECD approach attributes economic ownership of the income generating assets.

The OECD report defines the key entrepreneurial risk-taking functions and the ancillary office functions normally necessary both to create a new financial asset (loan) for the bank and to subsequently to manage the risks associated with those assets. In delineating the PE it is not sufficient to record loan assets in the accounts without consideration of where the key entrepreneurial risk-taking functions leading to their creation are performed on a case by case basis.

The creation of financial assets may often be a key entrepreneurial risk-taking function in a particular banking business. However the OECD highlight that other assets and risks will be attributed to the PE in accordance with a functional and factual analysis that identifies the significant people functions relevant to the economic ownership of assets and the significant people functions relevant to the assumption and management of risks, and any transfer of these risks.

In addition, it may not be the only significant people function, indeed there may be other such functions that relate to non-financial assets, for example, the development of valuable trade intangibles such as IT systems or marketing intangibles.

As well as analysing each of the functions performed by the PE in detail, it is also necessary to consider what assets are used and what risks are assumed in performing those functions.

In an ideal scenario accounting entry's will be consistent with, and follow from, the functional and factual analysis. Where this is in fact the case, the accounts provide a starting point for determining the profits attributable to the PE.

The OECD report highlights that bank's capital is principally required to support the risks assumed by the bank through its making of loans, and to support the risk associated with off-balance sheet items such as undrawn commitments to make loans. This capital must be regarded as following those risks i.e. the OECD state that capital is to be attributed to a PE by reference to the risks arising from its activities.

The attribution of free capital can have an important impact upon the amount of profit attributed to the PE. As a result the attribution of capital should be implemented in accordance with the arm's length principle, to ensure that an appropriate amount of profits is attributed to the PE. Therefore the bank PE should have sufficient capital to support the functions it undertakes, the assets it uses and the risks it assumes.

A key condition that the OECD identify of a banking enterprise operating through PEs is that capital and risks are not segregated from each other within the single legal entity. The OECD approach uses a functional and factual analysis to attribute assets and risks, it then attributes capital to support the risks attributed.

The OECD sight the example of a traditional banking business in commercial lending, where it is the sales/trading function and the risk management function that are considered the key entrepreneurial risk-taking functions. The risk management function is responsible for the initial assumption of the risk, and the sales/trading function for the ongoing management of the risks assumed. Such functions key entrepreneurial risk-taking functions involved in the creation and management of financial assets are likely to be performed in more than one jurisdiction, and the OECD acknowledge that this can create tax issues. An example of this is where loans originate in one location and are managed in another.

A PE is not the same as a subsidiary in that it is not legally or economically distinct from the rest of the enterprise of which it is a part. Indeed, all parts of a banking enterprise have the same creditworthiness. Therefore, dealings between a PE and the rest of the banking enterprise of which should generally be priced on the basis that both share the same creditworthiness. In addition the bank Head office (HO) has no scope to guarantee the PE's creditworthiness, or for the PE to guarantee the creditworthiness of the rest of the banking enterprise of which it is a part. However, a functional and factual analysis will establish if a real and identifiable event has occurred and should be taken into account as a dealing of economic significance between the PE and another part of the enterprise.

Where dealings are recognised, they may reflect a transfer of assets and/or risks between the PE and other parts of the enterprise to which it belongs. Therefore, the characterisation and recognition of dealings will affect the attribution of risks, assets and therefore capital to the PE. The OECD highlight that the dealings should be priced on an arm's length basis, assuming the PE and the rest of the enterprise of which it is a part to be independent of one another. Again this should be done by subsequent to a functional and factual analysis.

The OECD provide the example of lending and borrowing by a PE to and from the rest of the enterprise of which it is a part should generally be recognised where it meets the requirements for recognition as a dealing. Such borrowing may, however, be displaced by the attribution of capital to the PE's assets and risks, as indeed may third party borrowing.

In addition to the key entrepreneurial risk-taking functions, it will also be important to take account of other functions. Where the PE provides services to the part of the enterprise performing the key entrepreneurial risk-taking functions, that part is required under the second step of the authorised OECD approach to deal with the PE as if it were a separate and independent enterprise. This means that we would recognise any intra-entity dealing to compensate the service provider in accordance with the arm's length principle.

Question 4

Considering the Facts and Circumstances:

> US Treasuries > 3rd Party > Branch of Bank Beta > Bank Beta > Non US Institutional Investor < Substitute Interest < Interest Income

Interest received by the institutional Investor in respect of the USTs will give rise to interest equivalent, payable to Bank Beta who will in-turn pay an amount to the Branch of Bank Beta who will pay interest equivalent to the collateral-giver.

Bank Beta is a Withholding Agent.

In accordance with Treasury Regulations:

(i) *A Withholding Agent (WA) is "any person US or foreign that has the control, receipt, custody, disposal, or payment of an item of income of a foreign person subject to withholding."*
(ii) *Where "any person who meets the definition of a WA is required to deposit any tax withheld…. and to make the returns prescribed…"*
(Treasury Regulations s1.1441-7(a)(1))

Therefore the Branch of Bank Beta and Bank Beta could be considered WAs regardless of any requirement to withhold. However as the Branch of Bank Beta is not a separate legal entity the substitute interest payment from the Bank to its branch may be ignored.

US Treasury Interest is US Source Income.

A substitute interest payment made to the transferor of a security in a sale-repurchase transaction is treated the same as the interest on the transferred security (UST) where the interest in this instance is subject to portfolio interest exemption and not subject to withholding under chapter 3 in accordance with the Portfolio Interest Exemption.

Withholdable Payment

A witholdable payment is any source of US FDAP which would include the USTs in question, as the substitute interest is treated the same as the interest on the UST.

Should Bank Beta not be able to determine if the 3rd Party entity is an FFI or if it is an NFFE that fails to identify substantial US owners with necessary documentation the substitute interest payment would be subject to Chapter 4 withholding.

Backup Withholding

Should the third party be a non-exempt US Person who cannot provide a Tax ID Number (TIN) on a form W-9, Bank Beta will be required to apply back-up withholding on the substitute interest payment to the third party.

1042-S / 1042 / 1099 and 945 Reporting

As a WA Bank Beta has an obligation to provide a 1042-S information return to the IRS if the third party was documented as a foreign account holder together with a 1042 or to provide a 1099 in the event that the account holder was a US Person. Where backup withholding has been applied Bank Beta must file Form 945.

PART C

Question 5

Introduction

The OECD highlight that use of a cash pool is popular among multinational enterprises (MNEs) as a way of achieving more efficient cash management by bringing together, the balances on a number of separate bank accounts, either physically or notionally.

A cash pool has the potential to help to achieve more effective liquidity management, whereby reliance on external borrowing can be reduced or, where there is a cash surplus, an enhanced return may be earned on any aggregated cash balance. In addition, Financing costs may also be reduced by eliminating the bank spread embedded in the interest.

Types of cash pool
There are two distinguished forms of cash pooling, which can be used in combination. These are physical sweeping of cash, and notionally offsetting. Notionally offsetting means with no physical movement of cash. In response to the concerns over base erosion from tax authorities, the OECD have clarified their approach with respect to cash pooling arrangements.

Delineation of cash pooling transactions
The OECD highlight that the determination of the results of cash pooling that arise from deliberate concerted group actions must be established through a thorough functional analysis. Indeed, in the context of cash pooling arrangements, it is essential to determine the nature of the advantage or disadvantage, quantify the benefit or detriment provided, and determine that benefit or detriment should be divided among members of the MNE group.

A benefit of a well-established cash pooling arrangement may be the reduction of interest paid or the increase of interest received, which results from netting credit and debit balances. The amount of that group benefit, calculated by reference to the results that the cash pool members would have obtained had they transacted solely with independent enterprises, would generally be shared by the cash pool members. The OECD reference that this is on the provision that an appropriate reward is allocated to the cash pool leader for the functions it provides.

One of the practical difficulties of cash pooling is deciding how long a balance should be treated as part of the cash pool before it could be reclassified into something else, such as a long-term loan.
As cash pooling is intended to be a short-term, liquidity-driven arrangement, the OECD state that it may be appropriate to consider whether the consistent pattern is present year after year and to inspect what policies the MNE group's management has in place, given that yield on cash balances is a key financial management issue. Although the OECD acknowledge that it’s difficult to price such balances, which may fluctuate daily.

Determining the arm’s length price of cash pooling transactions: Rewarding the cash pool leader function

The suitable reward of the cash pool leader will depend on the facts and circumstances, the functions performed, the assets used, and the risks assumed in facilitating a cash pooling arrangement. Examples by the OECD are provided where a cash pool leader only performs a co-ordination function and thus receives limited remuneration as a service provider. Alternately the cash pool lender performs additional functions, controls and bears the financial risks contractually allocated to it, and has the financial capacity to bear those risks, such that an enhanced reward may be appropriate.

The allocation of benefit is a key area of the OECDs focus. It is essential to establish the nature of the advantage or indeed disadvantage, the value of the benefit or detriment provided, and thirdly how that benefit or detriment is allocated amongst the MNE. MNEs need to consider the functions, assets and risks of the group parties and the benefit should be allocated based on this.

Rewarding the cash pool members

The remuneration of the cash pool members will be calculated through the determination of the arm's length interest rates applicable to the debit and credit positions within the pool. It will generally be done once the remuneration of the cash pool leader has been calculated. Determining the arm's length interest rates for the cash pool intra-group transactions may be a difficult exercise due to the lack of comparable arrangements between unrelated parties.

The OECD suggest three approaches to apportion cash pool benefits to participating members. The first of these in increasing the interest rate for all participants. This would be suitable where there are both debit and credit balances in the pool, to benefit both borrowers and lenders with a larger interest rate if they contribute a larger balance to the pool.

The second approach is to apply the same interest rate for all participants. This method would be appropriate where all cash pool members have same or similar credit profile, irrespective if they are creditors or depositors in the pool. The third is allocating cash pooling benefits to depositors, and not borrowers, within the group specifically in in situations where there is genuine credit risk to the depositors.

Guarantees

In addition, as part of the cash pooling arrangement cross-guarantees and rights of set off may be required between participants in the cash pool. To the extent that this represents nothing more than credit enhancement attributable to the implicit support of other group members, no guarantee fee would be due. However, any support, in case of a default from another group member, should be regarded as a capital contribution.

Difficulty analysing Cash pooling arrangements

The OECD highlight a difficulty for tax administrations in analysing cash pooling arrangements is that the various entities in a cash pool may be resident across many of jurisdictions. This is likely to make it difficult to access sufficient information to verify the position as set out by the taxpayer. The OECD recommend that to assist tax authorities, MNE groups should provide information on the structuring of the cash pool and the returns to the cash pool leader and the members in the cash pool as part of their transfer pricing documentation.

Question 6

Part 1

The OECDs report suggests a number of observations with regards to the forms of establishment of subsidiaries and branches by non-resident banks. The OECD highlighted that some jurisdictions, for example Brazil, Mexico and Russia do not permit establishment of branches by non-resident foreign banks.

In contrast, in South Africa, while the establishment of branches by foreign institutions are nominally permitted in name, application for the establishment of a branch of a foreign institution requires that applicants comply with all applicable South African legislation. This includes the foreign institution being required to incorporate as an external company.

For members of the EU, procedures for establishment of branches contrast for EU-based applicants versus non-EU applicants. The establishment of a branch of a parent credit institution not established in the EU would be dependent on requirements set by the relevant member state. In contrast rules governing establishment of branches of EU-based institutions are set by law and are fully harmonised. Indeed in the UK, the Prudential Regulatory Authority (PRA) will permit non-EEA branches undertaking retail banking activities beyond de minimis levels, only if there is a very high level of assurance from the home states supervisors over resolvability of the non-resident institution including its UK branch. Additionally, non-EEA branches are expected to concentrate on wholesale banking and to do so at a level that is not critical to the UK economy.

In the U.S., branches are subject to fewer or less burdensome financial requirements than domestic banks. Unlike domestic banks, U.S. branches of non-resident banks are not subject to U.S. regulatory capital requirements or indeed stress testing requirements. This is on the basis that branches are a direct extension or the foreign bank.

Australia and New Zealand require establishment of a subsidiary for a foreign undertaking to carry out retail deposit taking that is of a significant size.

Part 2

The OECD study noted that overall, since the 2008 financial crisis most jurisdictions that have branches of non-resident banks have increased their governance process. The OECD highlighted that with one exception, all countries that permit the establishment of branches of non-resident banks enforce a certain level of governance requirements in relation to the branch Overall, the OECD identified that some countries have implemented. 'Fit and proper tests' whereby countries that impose governance requirements on branches apply a fit and proper test. Half of the countries in the study required the establishment of a board of directors.

In addition, some countries required a risk management and/or an audit function within the branch.

An example of this is France where branches of non-French banks must comply with governance and an internal control system including a risk management function. The non-French bank's head office is responsible for "*determining the branch's strategy as well as its risk appetite concerning both current and future risks*". Additionally, the senior management of the branch must communicate to the banks head office about significant risks, and risk mitigation policies.

By way of country specific examples, the OECD highlighted that non-resident banking organisations in the U.S. that are non-publicly traded and have total consolidated assets of $50 billion or more that maintain a branch in the U.S. are required to comply with specific risk committee requirements. If the group is publicly traded, the threshold is with total consolidated assets of $10 billion or more before specific requirements apply.

In Greece, where non-EU branches operate, they must comply with the same governance requirements as a domestic bank. In contrast, where EU banks operate in Greece through a branch, these do not have to comply with the Greek governance requirements because they are required to comply with their EU Member State's respective requirements.

As a result of the financial and governance requirements that are now being imposed, while the same or equivalent to domestic banks, may limit the attractiveness of branching going forward.

The majority of jurisdictions allow non-resident banks and credit institutions to establish branches. The OECD report highlights that the majority of jurisdictions permit these branches to carry out retail banking operations that do not differ in scope from that applying to domestic branches.

However, there are exception that include threshold requirements related to the size of deposits in Australia, Canada, and New Zealand, and in New Zealand systemic importance of the branch and subordination of local depositors to home jurisdiction depositors in a resolution.

Brazil does not allow branches of foreign banks. However, four branches of foreign undertakings were in situ prior to the 1988 ban of branching, and their banking license was grandfathered. This permitted them to carry out the same operations as a domestic Brazilian bank.

Question 7

The general rules in accordance with CAP 117 applies as shown in the following:

Article 19(1) requires that any person who effects a purchase or sale of HK Stock as principal or agent shall prepare a contract note and stamp the executed contract note in accordance with Head 2(1) in the First Schedule or Head 2(2) for voluntary dispositions inter vivos, where the contract note must be prepared in 2 days (s19(1)(b)(i)) after the sale or purchase unless it is effected elsewhere where it must be prepared within 30 days (s19(1)(b)(ii)). A security is considered HK Stock if there is a requirement for registration of the transfer on a register in Hong Kong. In accordance with Companies Ordinance (Cap 622) the share of a company incorporated in HK are HK stock.

Considering each of the OTC transactions in the light of the above:

HK listed Equities, on the appointment of a new trustee

As a HK listed equity (Art 2(1)) the security falls within the scope of Cap 117 and as an OTC transfer within a nominee account HK Stamp Duty would apply (19(1)), however the transfer is exempt - for effectuating the appointment of a new trustee. (27(5)).

HK listed ETF's as a distribution by a trustee to a beneficiary

As a distribution to a beneficiary this is an exempt transfer (27(5), also as this is a transfer of an ETF, then in accordance with Part 2 of the Eighth Schedule section 19(1) does not apply to the sale or exchange of an ETF.

HK listed equities between associated entities

Stamp duty under Head 2(1) shall not be charged on a transfer from one associated body corporate to another, where one is the BO of not less than 90% of the issued share capital of the other or a third such body is the BO of not less than 90% of the issued share capital of each – Cap 117, 45(1) and 45(2). Therefore in this instance stamp duty is not applicable.

HK listed equities, between two non-related parties, one resident in HK

There is a transfer between of BO of a HK listed security as such HK Stamp is applicable (19(1)).

HK listed DR (HDR), where the register is maintained in HK but the underlying securities are US common stock

A HK listed Depositary Receipt (HDR) if it maintains a register in HK, would be a HK security (2(1)) and as such subject to HK Stamp (19(1)). If the HDR does not maintain such a register and is deemed not to be a HK Security. In this instance HK Stamp Duty is applicable as the HDR in question maintains a register in HK.

Question 8

Under Italian law (Decree 239/1966) interest premium and other income, including the difference between the redemption amount and the issue price of a bond is subject to 26% substitute tax on payment of a coupon or on redemption and transfer of the bond, when received by non-Italian resident persons not acting through a permanent establishment in Italy.

The substitute tax is applied by the Italian Bank or other Financial Intermediary that intervenes in the payment of the income.

An exemption from substitute interest applies:

- Where the BO is resident in a state or territory which allows for the adequate exchange of information and is listed on the 'White List";

- Where the noteholder is an institutional investor i.e. whose activity consists of making or managing investments on its own behalf or on behalf of other persons established in states or territories included on the "White List"; or

- Where the noteholder is a central bank or is an international entity or organisation in accordance with international agreements.

To receive payment gross, the noteholder must:

- Deposit the bond with a bank or stockbroker resident in Italy or a PE of a non-resident bank or stockbroker or with an entity or company participating in a centralised securities management system connected with the Italian MOEF; and

- File with the bondholders direct custodian an indefinite exemption form prior to or concurrently with the deposit of the bond.