

Group of Thirty: Global Clearing and Settlement – A Plan of Action

Proposed Tax Relief Model

CONTENTS

1	Background
2	Current global tax relief arrangements
3	Main concepts of proposed tax relief model
4	Investment structure/interposition of intermediaries
5	Tax deduction responsibility
6	Principal mechanics of tax relief model
7	Changes potentially required to existing tax relief arrangements
8	Comments sought
Appendix 1	Direct investment by investor
Appendix 2	Indirect investment by investor via global custodian and custodian appointed by global custodian
Appendix 3	Indirect investment by investor via private bank, global custodian appointed by private bank and custodian appointed by global custodian

1. Background

In its report “Global Clearing and Settlement – A Plan of Action” issued on January 23, 2003, the Group of Thirty (G30) set out its recommended best practices for cross border clearance and settlement. Within this report, Recommendation 8 considered, inter alia, the need for automating and standardizing asset servicing processes, including tax relief arrangements. Specifically, in the case of tax relief arrangements, the G30 report recommends that:

“Market participants and public authorities should work together to minimize the administrative costs to each party involved in tax relief arrangements through standardization and automation of procedures and communication of information and through the use and acceptance of electronic data and documentation”

2. Current Global Tax Relief Arrangements

Current tax relief arrangements vary considerably between different countries of investment; no two countries operate the same tax system and investors presently face the prospect of having to complete various country-specific tax forms in order to facilitate tax relief on their global investments.

Some countries provide tax relief at the point of income payment (“relief at source”) while others provide for the retrospective reclamation of excess initial tax deductions (“tax reclaim”). Of these two tax relief methods, “relief at source” is preferred due to the optimized cash flow that it affords investors.

At one extreme, a small number of countries already operate a relief at source tax system in a way that is essentially compatible with the proposed tax relief model set out in the following sections of this paper. At the other end of the spectrum, the tax relief arrangements in a number of other countries presently render the provision of tax relief - either by means of relief at source or tax reclaim - a practical impossibility. The problems attached to the tax relief process in the latter countries include - but are not limited to - excessive investor documentation requirements, the imposition of local tax advisors to administer claims for tax relief and inordinate delays in the settlement of tax reclaim applications.

3. Main Concepts of Proposed Tax Relief Model

The proposed tax relief model set out in this paper has been prepared in response to G30 Recommendation 8. It is designed to fully satisfy the G30 criteria by:

- standardizing tax relief arrangements;
- creating a platform that facilitates the automation of associated procedures and the electronic communication of associated data; and by extension
- providing each party involved in the tax relief process with an opportunity to minimize associated costs

The proposed tax relief model is based on the optimal relief at source tax relief methodology. Accordingly, it envisages that appropriate tax relief will be secured on dividend and interest income arising from securities at the point of income payment and that it will not normally be necessary to file (electronic or physical) tax reclaim applications to secure this relief.

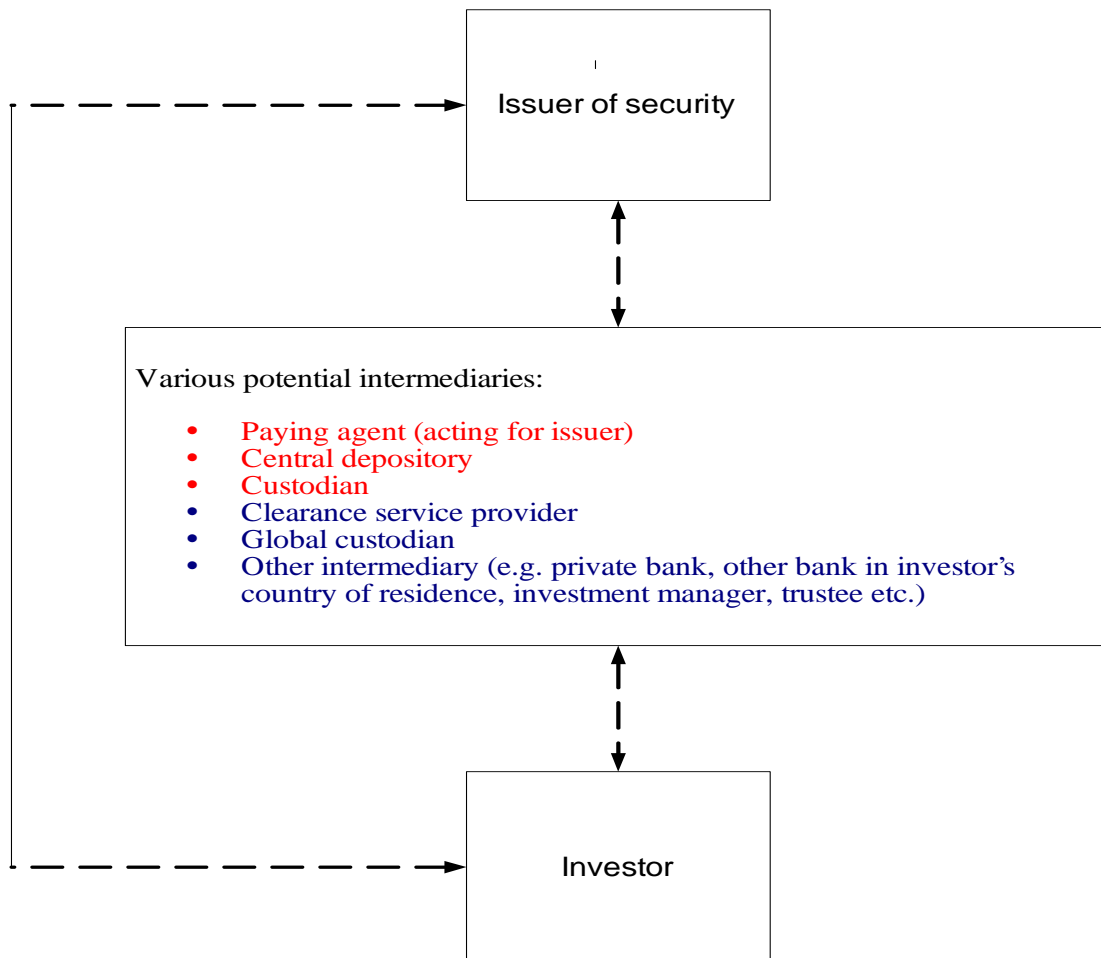
Moreover, the proposed tax relief model does not envisage any radical changes to existing practices and system capabilities. Rather, it largely builds on existing technology and best practices that are already used to secure tax relief in a number of countries of investment. By extending these best practices to all countries of investment and standardizing/centralizing investor tax documentation requirements, the proposed model provides a firm basis for streamlining the current tax relief process and optimizing future global tax relief arrangements for investors, market participants and public authorities.

Realistically, it is anticipated that the potential implementation of this proposed tax relief model would involve a phased approach, starting with a relatively small number of countries of investment where appropriate agreements can be reached between market participants and the relevant public authorities. Having established the practical working credentials of the model in these initial countries of investment, the aim would be to encourage market participants and relevant public authorities in other countries of investment to adopt the model standard at the earliest possible opportunity thereafter.

Subsequent sections of this paper consider the varied investment structures that need to be accommodated by the proposed tax relief model and the varied allocation of tax deduction responsibility within such structures. Fuller details of the principal mechanics of the proposed tax relief model and the changes potentially required to existing tax relief arrangements are also provided. The final section of this paper seeks feedback in respect of the proposed tax relief model and - subject to this - highlights certain aspects of the model that will need to be considered in more detail.

4. Investment Structure/Interposition of Intermediaries

The proposed tax relief model recognizes that there may be considerable variances in investment structure. In certain cases, the issuer of the security and the investor may have a direct relationship. In other cases, one or more intermediaries may be interposed between these two parties. This varied structure can be represented pictorially as follows:



5. Tax Deduction Responsibility

Typically, the intermediaries highlighted in red in the above diagram will be located in the country of investment. Together with the issuer of the security, one or more of these intermediaries may have tax deduction responsibility in respect of income arising from securities.

The intermediaries highlighted in blue in the above diagram are typically located outside the country of investment and usually do not have such tax deduction responsibility.

6. Principal Mechanics of Tax Relief Model

The proposed tax relief model is intended to facilitate direct investment by investors as well as indirect investment through one or more intermediaries. The essential concepts that underpin the model are summarized below:

Standardized investor tax documentation

- (a) The investor completes a standard tax declaration confirming (i) identity, (ii) residence (iii) generic category (i.e. individual, company, pension fund etc.) and (iv) tax treaty relief eligibility.

In the event that an investor fails to complete a declaration, the investor will not be entitled to any tax relief under this tax relief model. However other means of securing tax relief (e.g. retrospective tax reclaim application) may still be available to the investor.

- (b) The investor provides the declaration at (a) above to the issuer of the security or any authorized intermediary acting for the investor, as appropriate. See (f) below for further details of the authorization process for authorized intermediaries.

In certain countries, domestic tax relief may be available to certain types of investor. Such domestic tax relief may be more advantageous to the investor than the relief available to the investor under tax treaty. Where appropriate, the issuer of the security or the authorized intermediary may take due account of any domestic tax relief that may be available to the investor, based on the information at (i) to (iii) of the declaration at (a) above.

Pooling of assets and passing of tax rate information between authorized intermediaries/issuer

- (c) Where an authorized intermediary receives a declaration from the investor but does not have tax deduction responsibility, it is responsible for passing tax rate information to the upper-tier authorized intermediary or the issuer of the security, as appropriate. This may involve (i) segregation of assets into tax rate pools on the books of the upper-tier authorized intermediary/issuer or (ii) tax rate breakdown of income entitlements arising on assets held in a single pool on the books of the upper-tier authorized intermediary/issuer in accordance with the tax rates applicable to the underlying investors
- (d) Where information at (c) above is provided to an upper-tier authorized intermediary that does not have tax deduction responsibility, that authorized intermediary is responsible for relaying that information to the next upper-tier authorized intermediary or the issuer in conjunction with one of the methods outlined at (c)(i) or (ii).

Deduction of tax at appropriate reduced tax rates (relief at source)

- (e) The party with tax deduction responsibility applies appropriate reduced tax rates according to the information contained in the:
- investor declaration at (b); or
 - authorized intermediary tax rate information at (c) or (d)

Authorization of authorized intermediaries

- (f) Intermediaries must be authorized by their local tax authority to:
- receive investor declarations at (b) or authorized intermediary tax rate information at (c) or (d) and/or;
 - provide tax rate information at (c) or (d)

Where, exceptionally, an issuer has tax deduction responsibility it may also qualify for authorized intermediary status although it is not strictly an intermediary.

Authorization shall be based on standard criteria. Continued authorization shall be contingent on satisfactory performance - see (g) below.

Review of authorized intermediaries

- (g) Authorized intermediaries shall be subject to periodic review by their local tax authority. The object of such reviews is to ensure that, where appropriate, the intermediary:
- secures proper investor declarations or lower-tier authorized intermediary tax rate information
 - provides appropriate tax rate information to upper-tier authorized intermediaries
 - applies the correct rate of withholding

It is anticipated that such reviews will be primarily system oriented. However, the authorized intermediary will make more granular information available to the local tax authority upon request, where this is necessary to facilitate review.

The flowcharts at Appendix 1 - 3 illustrate the essential flow of documentation and tax rate information that is envisaged above in three random scenarios:

1. Direct investment by investor/tax deduction responsibility rests with paying agent acting for issuer
2. Indirect investment by investor via global custodian and custodian appointed by global custodian/tax deduction responsibility rests with custodian
3. Indirect investment by investor via private bank, global custodian appointed by private bank, custodian appointed by global custodian/tax deduction responsibility rests with paying agent acting for issuer

It should be noted that the varied allocation of tax deduction responsibility set out in these flowcharts is intended to illustrate existing practices across global markets of investment. The proposed tax relief model does not alter these existing tax deduction responsibilities.

7. Changes Potentially Required to Existing Tax Relief Arrangements

The changes required to facilitate the proposed tax relief model will vary from one country of investment to another. In some countries, the necessary changes would be limited. In other countries, the impact would be more significant. The following table summarizes the main areas where change is potentially required as a result of the proposed tax relief model and the possible scope of that change.

Proposal	Current practice/possible scope of change
Investor completes single tax declaration, covering all countries of investment	<p>Certain countries of investment (e.g. Australia) do not presently have a formal tax declaration. Other countries of investment (e.g. Belgium, Canada, France etc.) presently have varied tax declaration requirements, although the information gathered is essentially the same. Some countries of investment may require additional documentation such as a tax residency certificate issued by the investor's country of residence.</p> <p>It would be necessary for market participants and the public authorities in the various countries of investment to agree a single "global tax declaration" standard. This may require legislative or administrative change on the part of the public authorities.</p>
Pooling of assets – segregated asset pools for each reduced tax rate entitlement or single pool with tax rate breakdown provided at the point of income payment	<p>Certain countries of investment (e.g. Canada & USA) already operate essentially compatible asset pooling arrangements. Other countries of investment (e.g. France) have more restrictive pooling arrangements. Pooling is not accepted market practice in certain countries of investment (e.g. South Korea) where segregated securities accounts are currently required to be established at a beneficial owner level.</p> <p>Where necessary, it would be necessary for market participants and the public authorities in certain countries of investment to agree asset pooling arrangements compatible to those set out in the proposed model. This may require legislative change on the part of the public authorities.</p>
Tax relief to be provided by means of relief at source arrangements	<p>Relief at source arrangements represent the norm outside Western Europe. Within Western Europe, countries such as Germany and Switzerland do not generally allow tax relief to be conferred at source; it is usually necessary for retrospective tax reclaims to be filed on behalf of eligible investors.</p> <p>It would be necessary for the public authorities in the latter countries of investment to amend existing tax relief arrangements to facilitate tax relief at source, in consultation with market participants. This may require legislative or administrative change on the part of the public authorities.</p>

Proposal	Current practice/possible scope of change
Authorization of authorized intermediaries	<p>Many countries of investment (e.g. Australia, Belgium etc.) already require financial intermediaries established in the relevant country to perform certain tax related functions in order to satisfy domestic legislative requirements. However, it is less common for financial intermediaries to be formally evaluated and authorized to perform such functions; Ireland and UK are examples of countries with such evaluation and authorization arrangements.</p> <p>While the responsibilities for authorized intermediaries set out in the proposed tax relief model are broadly comparable with some existing arrangements in certain countries, it would be reasonable to state that at a detailed level, there is no known direct comparison.</p> <p>It would be necessary for market participants and the public authorities in the various countries of investment to agree relevant arrangements for the evaluation and conferral of authorized intermediary status. This may require legislative or administrative change on the part of the public authorities.</p>
Review of authorized intermediaries	<p>As indicated above, many countries of investment already require financial intermediaries to perform certain tax related functions. Where such requirements are in place, the public authorities will often subject financial intermediaries to periodic review, in order to ensure proper performance of these requirements.</p> <p>While the review scope for authorized intermediaries set out in the proposed tax relief model is broadly comparable with some existing arrangements in certain countries, it would be reasonable to state that at a detailed level, there is no known direct comparison.</p> <p>It would be necessary for market participants and the public authorities in the various countries of investment to agree relevant arrangements for the review of authorized intermediaries. This may require legislative or administrative change on the part of the public authorities.</p>

8. Comments Sought

The proposed tax relief model set out in this paper is intended to stimulate debate in terms of whether a standard tax relief model is desirable/achievable and if so, the form that tax relief model should take. To the extent that there is basic agreement on some or all of the main concepts at 6 (a) to (g), it is recognised that much further thought will be required, and much further detail will be needed to be added to the model, before these concepts can be converted into a practical working reality. A number of the issues that will need to be thought through as part of this process are detailed below. Some initial comments are also provided in order to assist consideration of these points:

Issue	Initial comments
1. Format/content/validity period of investor declaration	<ul style="list-style-type: none"> • Should aim to restrict content to that information reasonably required to justify tax relief. The content should gravitate to the “standard” investor, while still enabling “exceptions” to be readily identified. • Consideration should be given to including a matrix of “standard” treaty tax rates for the investor’s country of residence, for the investor to confirm or override. • Potential need to incorporate bank secrecy waiver for authorized intermediaries in certain jurisdictions. • Declaration should ideally be enduring, subject to investor obligation to notify authorized intermediary of any material change in information provided and authorized intermediary obligation to inform investor of any changes in “standard” treaty tax rates for the investor’s country of residence. • Format should lend itself to electronic delivery and – subject to satisfactory progress being made in terms of electronic signatures – electronic completion.
2. Possible need for, and if applicable validity period of, certificate of residence issued by investor’s local tax authority. [Note – such certificate may form part of investor declaration.]	<ul style="list-style-type: none"> • Should aim to eliminate requirement for tax residence certificate from investor’s tax office or at least restrict this to certain categories of investor where there is some reasonable doubt in terms of treaty eligibility. • To the extent that a tax residence certificate is required, it should be valid for 5 years from the date of issue. [This assumes investor is under obligation to notify authorized intermediary of any material change in information provided (see comments at 1 above) and that changes in tax residence constitute material change.]
3. Possible need for up-front agreement of treaty eligibility for certain types of investor with tax authority in country of investment – in particular, investors organized as collective investment vehicles	<ul style="list-style-type: none"> • It would be mutually beneficial for market participants to agree investor treaty eligibility with the public authorities in the country of investor residence and the country of investment. Details of eligible (and/or ineligible) investors could be included within investor declaration.
4. Procedures to be adopted to facilitate changes in investor tax treaty relief eligibility (e.g. when a new tax treaty enters into force)	<ul style="list-style-type: none"> • Authorized intermediary acting for investor should have obligation to inform investor of any changes in “standard” treaty tax rates for the investor’s country of residence – see comments at 1 above.
5. Electronic delivery options for investor declarations and authorized intermediary tax rate information at c(ii)	<ul style="list-style-type: none"> • See comments at 1 above regarding the electronic delivery and completion of investor declarations. • Similar considerations apply to authorized intermediary tax rate information. Additionally, consideration should be given to developing a dedicated SWIFT message type, to be used for this purpose.

Issue	Initial comments
6. Timing requirements in respect of tax rate information at c(ii)	<ul style="list-style-type: none"> • Need to consider in the light of ex date/record date/pay date conventions in relevant country of investment. • Subject to above comment, and considering that there may be a requirement to pass on information to an upper-tier authorized intermediary, tax rate information should ideally be delivered no later than pay date – 5.
7. Handling of asset reconciliation discrepancies between two authorised intermediaries or between an authorised intermediary and an issuer of a security	<ul style="list-style-type: none"> • Ultimately, this may be an issue for the two counterparts to agree between themselves. • However, it may be possible to agree universal defaults, e.g.: <ul style="list-style-type: none"> ➤ Where breakdown provided is in excess of recorded position, the shares allocated to the highest tax band(s) included in the breakdown are reduced by the amount of the excess. ➤ Where breakdown provided is less than recorded position, the shortfall is subject to the standard rate of tax.
8. Criteria to be satisfied by putative authorized intermediary	<ul style="list-style-type: none"> • Putative authorized intermediary must be subject to regulatory oversight by financial regulator in country of establishment, with such regulator being satisfied that authorized intermediary is reasonably equipped to discharge authorized intermediary responsibilities.
9. Required control measures to ensure that only properly authorized intermediaries benefit from authorized intermediary status	<ul style="list-style-type: none"> • Unique reference number allocated to authorized intermediary upon approval and included in subsequent communications by authorized intermediary. • Public authorities in each country of establishment maintain list of current authorized intermediaries. • Current authorized intermediaries in all countries of establishment notified of any additions/deletions from above list.
10. Authorized intermediary review arrangements	<ul style="list-style-type: none"> • Emphasis of review should be reaching a satisfactory level of comfort that necessary systems are in place to reasonably assure compliance. • The review may be supplemented by limited sample requests for the authorized intermediary to evidence: <ul style="list-style-type: none"> ➤ How is has allocated income payments between investors and lower tier intermediaries, and the rate(s) of tax applied ➤ Investor declarations and authorized intermediary tax rate information that it holds to justify relevant tax rate(s) • Consideration should be given to the possible use of external auditors in lieu of review by local tax authority • Loss of authorized intermediary status should be limited to cases of gross non compliance • Review arrangements must be consistent from one country of establishment to another, to assure a level playing field.

Issue	Initial comments
11. Need for, and if applicable scope of, “back up” tax reclaim system	<ul style="list-style-type: none"> • “Back up” tax reclaim system likely required to correct over-withholding in cases such as late delivery of investor declarations, asset reconciliation discrepancies etc. • Aim should be to link the “back up” reclaim system to the main relief at source arrangements, so far as is possible. • A standard tax reclaim form could be used for all countries of investment detailing (i) the income payment, tax suffered & reclaim requested and (ii) the investor (perhaps attaching a copy of the investor declaration). • Consideration needs to be given as to whether such claims should be filed via the upper tier authorized intermediary (if any), relevant public authority or either. • The development of an effective “back up” tax reclaim system would likely represent a major project in its own right.

Subject to the above, comments are now sought as to whether some or all of the components set out in this proposed model should be the basis for the standardised/automated tax relief process advocated in G30 Recommendation 8 or whether this recommendation could be better achieved through other means.

All feedback is welcomed and should be addressed to:

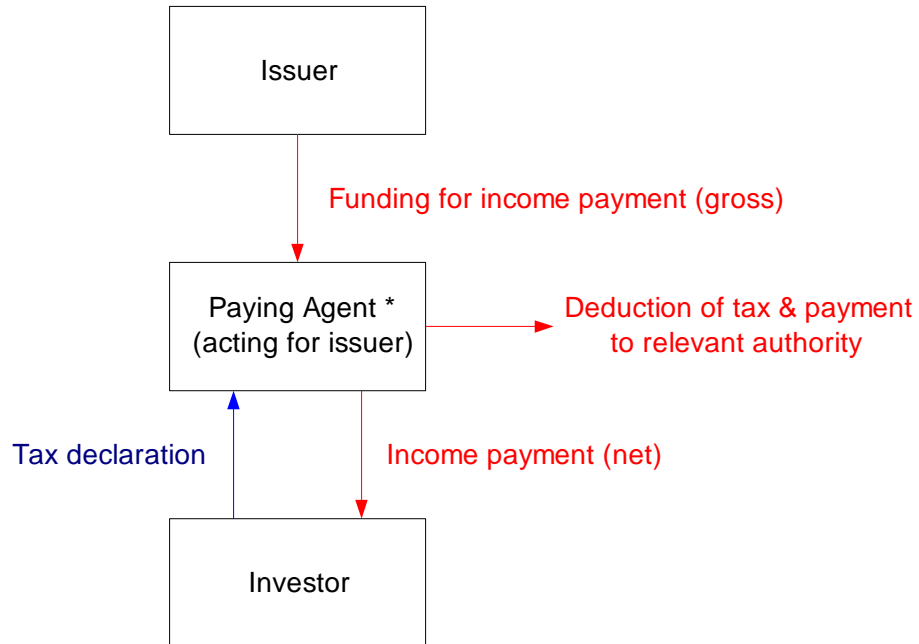
Chris Gilbert
Vice President – Investor Services
JPMorgan Chase Bank N.A.
Chaseside
Bournemouth
United Kingdom
BH7 7DA

Telephone: +44 (0) 1202 347741
Fax: +44 (0) 1202 341722
e-mail: christopher.m.gilbert@jpmorgan.com

Appendix 1

Direct investment by investor

Tax deduction responsibility rests with paying agent acting for issuer



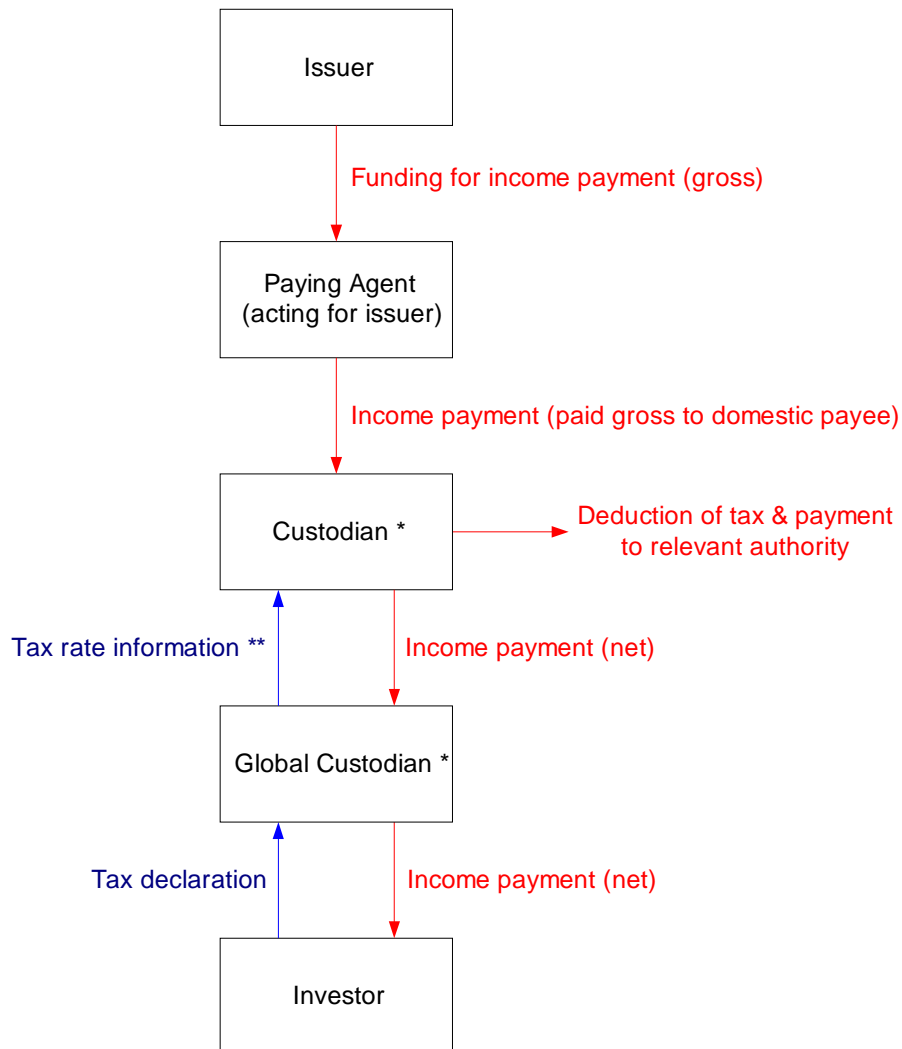
* Authorized intermediary - subject to review by local tax authority

Appendix 2

Indirect investment by investor via:

- global custodian
- custodian appointed by global custodian

Tax deduction responsibility rests with custodian



* Authorized intermediary - subject to review by local tax authority

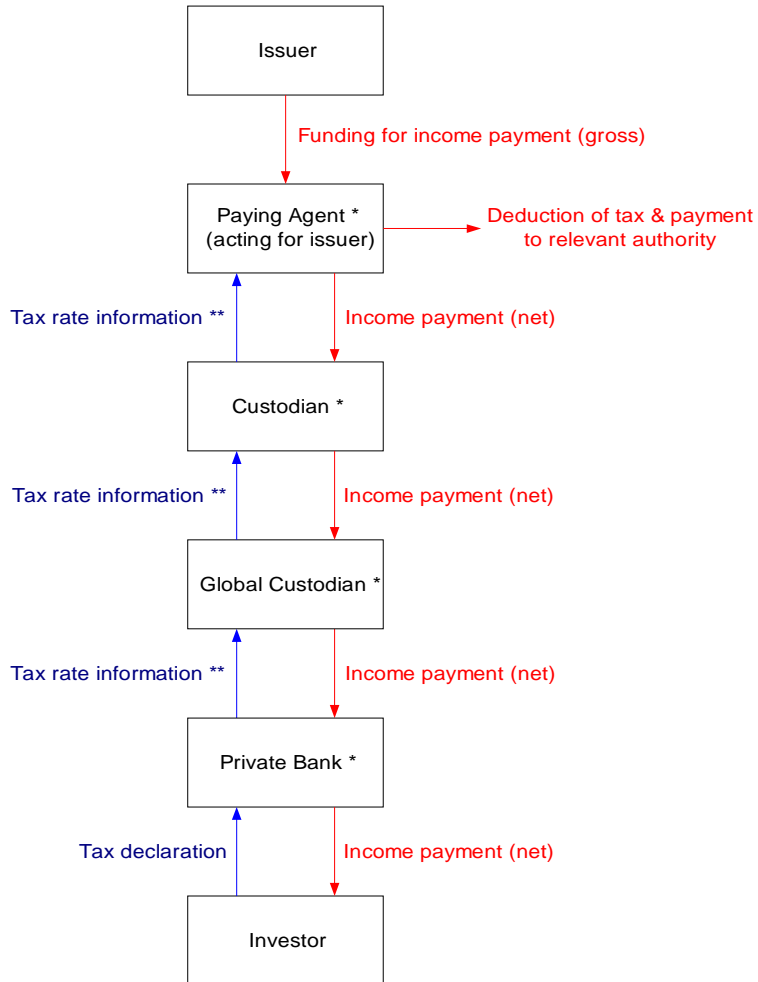
** Achieved by segregation of assets into tax rate pools on books of upper tier intermediary or tax rate breakdown of income payments arising on assets held in single pool on books of upper tier intermed

Appendix 3

Indirect investment by investor via:

- private bank
- global custodian appointed by private bank
- custodian appointed by global custodian

Tax deduction responsibility rests with paying agent acting for issuer



* Authorized intermediary - subject to review by local tax authority

** Achieved by segregation of assets into tax rate pools on books of upper tier intermediary or tax rate breakdown of income payments arising on assets held in single pool on books of upper tier intermed