



24 August 2012

Via Electronic Mail

Room 5205
Internal Revenue Service
P.O. Box 7604
Ben Franklin Station
Washington, DC 20044
U.S.A.

Dear Sirs/Madam,

Additional Clarification on the Proposed Foreign Account Tax Compliance Act
("FATCA") Regulations (the "Proposed Regulations")

In our last submission to you, we requested that Mandatory Provident Fund retirement plans ("MPFs") and certain Occupational Retirement Schemes Ordinance retirement plans ("ORSOs") in Hong Kong be granted certified "deemed-compliant FFI" status in upcoming FATCA final regulations by reason of their low risk of U.S. tax evasion and the considerable compliance difficulties and costs if exemption were not available. This submission provides elaboration on these ORSO plans, namely MPF-exempted ORSO Registered Plans (Appendix A), and our proposed legal definitions for a new category of deemed-complaint FFI status (Appendix B).

Since 2000, MPFs have been the default, government-mandated retirement plan for a majority of Hong Kong residents. However, some retirement plans established before the introduction of MPFs, namely, ORSOs, continue to be used for a variety of historical reasons described in Appendix A. Under certain circumstances, some ORSOs are recognized under Hong Kong law as permissible alternatives to MPFs, and certain contributions to these MPF Exempted ORSO Registered Plans ("Grandfathered ORSOs") may be made in lieu of mandatory contributions to an MPF.¹

As discussed below, given their historical background and the fact that Grandfathered ORSOs are subject to substantive regulation in Hong Kong, Grandfathered ORSOs do not present a high risk of U.S. tax evasion. However, Grandfathered ORSOs would not qualify for the certified deemed-compliant FFI category we have recommended for foreign government-mandated retirement plans because participation in a Grandfathered ORSO is not, strictly speaking, mandatory. We continue to believe

¹ Employers that offer Grandfathered ORSOs must also permit employees to participate in an MPF. An employee must then choose one of the two. For those employees who choose to participate in a Grandfathered ORSO, contributions are made in lieu of mandatory contributions to an MPF.

that a bright-line test for government-mandated retirement plans is useful and simple to apply. But we propose that a more narrowly tailored deemed-compliant category also be created for Grandfathered ORSOs and similar plans in other countries.

Most Grandfathered ORSOs were established long before FATCA (in fact, most were established before 1996).² In order to qualify as an alternative to MPFs, Grandfathered ORSOs must generally be subject to regulation in Hong Kong with respect to trusteeship and investments in accordance with the *Mandatory Provident Fund Schemes (Exemption) Regulation* (“MPF Exemption Regulation”).³ Participants in Grandfathered ORSOs are generally either employed in Hong Kong or have some employment relationship with a Hong Kong employer. The contributions of employees who became plan members prior to December 1, 2000 are subject to the Grandfathered ORSO’s plan rules.⁴ The contributions of new employees (*i.e.*, employees who became plan members after December 1, 2000) are subject to the preservation, portability and withdrawal provisions of the MPF Exemption Regulation up to the amount of their minimum MPF benefits.⁵ Other contributions of such new employees would remain subject to the Grandfathered ORSO’s plan rules.

We believe that Grandfathered ORSOs present a low risk of U.S. tax evasion for two reasons. First, Grandfathered ORSOs were generally created more than ten years ago, with terms and provisions that were drafted long before FATCA came into effect. They are offered by a limited universe of employers. Such Grandfathered ORSOs were not designed with U.S. tax evasion in mind. Second, Grandfathered ORSOs are subject to substantive regulation in Hong Kong. In addition, in some cases, employers place vesting or other limitations on withdrawals from Grandfathered ORSOs, making such Grandfathered ORSOs unattractive as a vehicle for U.S. tax evasion. Grandfathered ORSOs serve as a foreign government-permitted alternative to MPFs. However, without creation of a deemed-compliant category for Grandfathered ORSOs, these plans will face higher costs of compliance with FATCA. This would retroactively penalize Grandfathered ORSOs’ participants for choosing “incorrectly” between two foreign government-authorized retirement alternatives. Such plan members have limited ability to move their money out of Grandfathered ORSOs; plan members may, in general, only make a one-time election to participate in either an MPF or a Grandfathered ORSO.

We believe that our recommendations on “deemed-compliant FFI” status in the upcoming FATCA final regulations will make the regulations more flexible to accommodate the differing features of foreign retirement plans. We respectfully request that this amendment be made so that FATCA’s application to Hong Kong retirement plans becomes more equitable among members of Hong Kong’s working population and less onerous. We believe that this amendment will be equally applicable to other jurisdictions because globally, many jurisdictions are going

² ORSOs established after the introduction of MPFs may be granted “Grandfathered” status only if they form part of a restructuring or bona fide business transaction that affects an existing Grandfathered ORSO.

³ Trustees and managers appointed prior to the introduction of MPFs are grandfathered, but newly appointed trustees and investment managers must meet the MPF Exemption Regulation’s trusteeship and investment standards.

⁴ These plan members are referred to as “existing members” in Section 2 of the MPF Exemption Regulation.

⁵ These plan members are referred to as “new members” in Section 2 of the MPF Exemption Regulation. For further details on “minimum MPF benefits”, see the last paragraph of Appendix A.

through pension reforms and there will inevitably be legacy, grandfathered or other plans that run in tandem with the current government-mandated plans. Without such an additional category, a substantial part of these parallel pension plans, which pose low risks of US tax evasion, will fall outside the deemed-compliant category. We believe that this is not the intent of the US authorities and we would respectfully request the authorities to factor this in when finalizing the regulations.

We appreciate that you see intergovernmental agreements (“IGAs”), to be entered into between the US and certain foreign governments, as a way to tailor “deemed-compliant FFI” or other FATCA relief to the particular features of certain retirement plan categories specific to the country entering into the relevant IGA. While we commend such an approach, we emphasize the desirability of simultaneously having, in the FATCA final regulations, a practical set of retirement fund/account rules that takes into account some of the diversity of foreign retirement plans around the world. IGAs may not be available in every jurisdiction, but the rationale for excluding grandfathered retirement plans in such jurisdictions remains just as compelling. We see IGA tailoring as complementing, instead of acting as a substitute for, a well-functioning set of retirement fund/account rules in the FATCA final regulations.

For your consideration, we have attached as Appendix B draft potential regulations language regarding foreign government-mandated retirement plans and certain grandfathered retirement plans which may be chosen by plan members in lieu of a foreign government mandated plan.

We thank you for the opportunity to provide the above additional clarification of our originally submitted comments. If there is any further information required or questions raised by our comments and suggestions that you would like to address and discuss, please do not hesitate to contact us as follows:

Mr. Lennard Yong lennard.yong@ing.com.hk
Ms. Sally Wong hkifa@hkifa.org.hk
Ms. Ka Shi Lau lau.kashi@bcthk.com

Sincerely yours,



Ms. Agnes Choi, Chairman,
The Hong Kong Federation
of Insurers



Ms. Sally Wong, CEO
The Hong Kong Investment
Funds Association



Ms. Ka Shi Lau, Chairman
The Hong Kong Trustees'
Association Limited

APPENDIX A

MPF Exempted ORSO Registered Plans

Background

Prior to the introduction of the Mandatory Provident Fund (“MPF”) system in Hong Kong, some employers provided voluntary retirement plans to their employees. These plans, generally known as ORSO registered plans (or just ORSO plans), are subject to ongoing requirements with regard to plan asset arrangements, restrictions on investments, funding, audit and actuarial review, trusteeship and disclosure of information concerning plan operation under the Occupational Retirement Schemes Ordinance (“ORSO Ordinance”).

The MPF system was launched in 2000. To tie in with its implementation, ORSO plans that fulfilled certain conditions could, prior to the launch, apply for exemption from MPF requirements. For the employers who decided to continue to operate their ORSO plans as their “core” retirement plans after the operation of the MPF system, they were required to apply for MPF exemption status for their plans to become “*MPF Exempted ORSO Registered Plans*”. The last date for lodging such applications was 3 May 2000 and the applications were all processed by 31 July 2000. While not explicitly framed as such in the MPF legislation, MPF Exempted ORSO Registered Plans function as a grandfathered class of retirement plans that predated MPF plans (the foreign government-mandated retirement arrangements in question). Existing members of an MPF Exempted ORSO Registered Plan, as well as new employees eligible to join an MPF Exempted ORSO Registered Plan after the commencement of the MPF system, have a one-off option to choose between the ORSO plan and an MPF plan. Where an ORSO plan has not been granted MPF exemption, both existing and new employees must join an MPF plan, irrespective of whether the ORSO plan is maintained by the employer.

The MPF legislation (which launched the MPF system in Hong Kong in 2000) sets out the detailed arrangements for the interface of the ORSO plans with the MPF system. The objective of the interface arrangements is to minimize the interference caused by the then newly-introduced government-mandated MPF plans with these then established ORSO retirement plans and to avoid upsetting the existing contractual relationships between employers and employees. The interface arrangements would also provide equitable treatment to all employees and protect their rights and interests.

As of 1 August 2000, there was 6,388 MPF Exempted ORSO Registered Plans in Hong Kong. No further MPF exemption status has been granted to newly established ORSO plans thereafter save when all or a class of the members and assets of the plans were transferred from one or more MPF Exempted ORSO Registered Plans to a newly established plan as a result of plan restructuring or bona fide business transactions (such as mergers and acquisitions and other business transactions at the employer level). New applications to the Mandatory Provident Fund Schemes Authority (“MPFA”) for MPF exemption status will need to be submitted with various information and documents in support including, for example, (a) sale and purchase agreement, minutes of board meeting, correspondence, solicitor statement, evidencing a bona fide business transaction and/or (b) trust deeds of the original and the new

plans, employee communication booklets or leaflets, evidencing the plan restructuring.

Statistics

(a)	<i>Number of MPF Exempted ORSO Plans approved as of 1 August 2000</i>	6,388
(b)	<i>Number of MPF Exempted ORSO Plans that received approval for such status during the period from 1 August 2000 to 31 March 2011</i>	161
(c)	<i>Number of MPF Exempted ORSO Plans that withdrew from such status during the period from 1 August 2000 to 31 March 2011</i>	2,642
	<i>Number of MPF Exempted ORSO Plans as at 31 March 2011 [i.e. (a)+(b)-(c)]</i>	3,907
	<i>Number of members covered by the 3,907 MPF Exempted ORSO Plans as at 31 March 2011</i>	376,000
	<i>[Relevant employees under MPF system as of the same period end]</i>	<i>[2,310,000]</i>
	<i>Asset size held by the 3,907 MPF Exempted ORSO Registered Plans as at 31 March 2011</i>	HK\$ 235.9 billion (US\$30.2 billion)
	<i>[Asset size of MPF schemes as of the same period end]</i>	<i>[HK\$ 378.3 billion (US\$48.5 billion)]</i>

Eligibility for Approval of MPF Exemption/Robustness of Regulatory Framework

The regulation of both MPF plans and ORSO plans is under the MPFA's purview. ORSO plans applying for MPF exemption status should generally be established on or before 15 October 1995 and applications for ORSO registration should all have been received by the ORSO Registrar⁶ not later than 15 January 1996 (i.e. prior to the launch of the MPF system in 2000). Other than such applications, other applications (by, for example, newly established ORSO plans) would be entertained only if they form part of a plan restructuring or bona fide business transaction as described in the last paragraph of the section entitled "Background" above.

Where an employer provides both an MPF plan and an ORSO plan (which has been granted MPF exemption), in general, each relevant employee has a one-off option to choose between the two plans and he/she should notify the employer of his/her decision in writing within a prescribed period from various scenarios (such as his/her

⁶ The role of the ORSO Registrar in administering the ORSO Ordinance has now been assumed by the MPFA.

commencement of employment with such employer); otherwise he/she will be deemed to have chosen an MPF plan. In some cases, especially those large corporations/organizations, some employers continue to offer both types of plan for their employees to choose and both plans are co-existing.

Participants in MPF Exempted ORSO Registered Plans are generally either employed in Hong Kong or have some employment relationship with a Hong Kong employer. Also, MPF Exempted ORSO Registered Plans are generally required to meet the minimum standards on trusteeship and investments in accordance with the Mandatory Provident Fund Schemes (Exemption) Regulation (“MPF Exemption Regulation”).

More particularly, whilst MPF Exempted ORSO Registered Plans are permitted to accept participation by members after the introduction of the MPF regime (referred to as “new” members in the MPF Exemption Regulation), a portion of a “new” member’s benefits from an MPF Exempted ORSO Registered Plan (referred to in the MPF Exemption Regulation as “minimum MPF benefits” (“MMB”)) is subject to essentially the same preservation, portability and withdrawal requirements that are applicable to MPF plans. Whilst the MPF Exemption Regulation sets forth details on how to calculate the MMB of a “new” member of an MPF Exempted ORSO Registered Plan, such MMB can, for the purpose of illustration, be understood as the portion of the ORSO plan benefits of that member which would have been accrued from MPF mandatory contributions had he or she opted, after the introduction of the MPF system, for an MPF plan instead of an MPF Exempted ORSO Registered Plan. Other contributions of a “new” member of an MPF Exempted ORSO Registered Plan would be subject to the rules of such ORSO plan so that the withdrawal of the portion of the “new” member’s benefits accrued on top of the MMB is governed by the withdrawal restrictions of such ORSO plan’s rules.

APPENDIX B

Sample Draft Regulations Language

We recommend the addition of new certified deemed-compliant FFI categories as new Regulations Section 1.1471-5(f)(2)(ii)(A)(3) and (A)(4).^[1]

“An FFI meets the requirements of this paragraph (f)(2)(ii)(A)(3) if it is a **government-mandated retirement fund**. For this purpose, a retirement fund (‘Subject Fund’) will be treated as a government-mandated retirement fund if it is within a category of retirement funds as to which the government (including any agency, bureau, instrumentality, department, division, regulatory authority or other portion thereof) of the jurisdiction in which the Subject Fund is established (the ‘Subject Jurisdiction’) has provided written notification to the Internal Revenue Service stating that --

(i) the laws of the Subject Jurisdiction require employees meeting conditions specified in such laws, to make (and/or have made on their behalf) mandatory contributions to such category of retirement funds;

(ii) it is the understanding of such government that mandatory contributions were made to such category by more than 50% of the working employee population (as determined in the reasonable discretion of such government) in the Subject Jurisdiction during the last annual period for which such government had access to relevant data; and

(iii) such government shall promptly provide written notification to the Internal Revenue Service in the event that such government becomes aware that, with respect to any annual period subsequent to that described in paragraph (f)(2)(ii)(A)(3)(ii), the understanding described in such paragraph is no longer accurate.”

“An FFI meets the requirements of this paragraph (f)(2)(ii)(A)(4) if it is a **grandfathered retirement fund**. For this purpose, a retirement fund (‘Subject Fund’) will be treated as a grandfathered retirement fund if it is within a category of retirement funds as to which the government (including any agency, bureau, instrumentality, department, division, regulatory authority or other portion thereof) of the jurisdiction in which the Subject Fund is established (the ‘Subject Jurisdiction’) has provided written notification to the Internal Revenue Service to the effect that--

(i) the laws of the Subject Jurisdiction permit employees meeting conditions specified in such laws, to make (and/or have made on their behalf) contributions to such category of retirement funds that are in lieu of mandatory contributions to a government-mandated retirement fund (within the meaning of paragraph (f)(2)(ii)(A)(3)); and

^[1] The lead-in language in Prop. Treas. Reg. Section 1.1471-5(f)(2)(ii)(A) (i.e., the requirement that the FFI “be organized for the provision of retirement or pension benefits under the law of the country in which it is established or in which it operates”) would still be required to be met. We recommend that the word “country” in the foregoing quote be replaced with the word “jurisdiction”.

(ii) such category consists of retirement funds established prior to the introduction by the Subject Jurisdiction of legislation regarding government-mandated retirement funds (within the meaning of paragraph (f)(2)(ii)(A)(3)) and such category of retirement funds was described in such legislation (or in guidance issued by the Subject Jurisdiction related thereto) as effectively having grandfathered status, as well as any successors thereto that are also granted grandfathered status.”
