Roundtable Discussion
Foreign Account Tax Compliance Act (FATCA)

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FATCA

Introduction/Base Case Issues

- Effective March 18, 2010 enacted as part of the HIRE Act.
- U.S. taxpayers with specified foreign financial assets that exceed certain thresholds must report (starting for 2012 returns) those assets to the IRS on Form 8938 attached to their federal income tax return, starting this tax filing season.
- Foreign financial institutions (FFI's) must report information about financial accounts held by U.S. taxpayers, or held by foreign entities in which U.S. taxpayers hold a substantial ownership interest.
- Immediate Questions arose regarding FATCA's legitimacy outside the U.S.
  - Bank secrecy laws
  - Sovereignty Concerns
  - Compliance issues
  - Limits of existing international treaty networks
  - Recriminations against U.S. individual, financial institutions and companies
  - Undue U.S. withholding

FATCA: *Overview*

Enacted in 2010 as part of Hiring Incentives to Restore Employment ("HIRE") Act; Implemented per January 17, 2013 Final Regulations

- **Foreign Financial Institutions ("FFI's") report to I.R.S. information about "financial accounts" held by:**
  - U.S. persons, or
  - Foreign entities in which U.S. persons hold a substantial (≥ 10%) ownership interest

- **Requires FFI's to tell I.R.S. about offshore accounts controlled by U.S. persons if assets exceed $50,000 in value**

FATCA: *Withholding*

FATCA extends the equivalent of domestic "Backup Withholding" to foreign "accounts" held by U.S. persons

- **Unless exception applies, 30% FATCA withholding (new Chapter 4 withholding) *where*:**
  - FFI does not have FFI-EIN (i.e., new FATCA ID number), *or*
  - FFI-EIN is wrong (i.e., it does not match with I.R.S. published list)
- **FFI-EIN is now called GIIN, which stands for Global Intermediary Information Number**

FATCA: *Participating FFI obligations*

FFI Obligations

- **Due Diligence**
- **Reporting**
- **Withholding**
- **Globalization**

FATCA: *Participating FFI obligations*

Due Diligence Procedures:

- **Determine what accounts are owned by US persons & US owned foreign entities**

- **Different procedures depending upon:**
    - "Pre-existing" v. New Accounts
    - Individual v. Entity Accounts

FATCA: *Due diligence (cont)*

Individuals

Preexisting Individual Accounts

- **Accounts ≤ $50,000: No review needed**
- **Accounts > $50,000: Review Electronic records**
  - Look for US indicia (e.g., address, place of birth)
  - If find US indicia, further inquiry required
- **Accounts > $1MM: Review paper records**

New Individual Accounts

- **Person must certify as to status**

Entities

Preexisting Entity Accounts

- **Account ≤ $250,000: No review (until account balance exceeds $1MM)**
- **Accounts > $250,000: Must review**
  - Look at "information maintained for regulatory or customer relationship purposes"
    - AML/KYC Procedures

New Entity Accounts

- **More detailed rules**

FATCA: *FFI Reporting/Withholding*

Reporting to IRS:

- **Report to IRS information about accounts owned by U.S. persons & U.S. owned foreign entities**
- **The emphasis is placed on obtaining information from FFI's and NFFE's**
- **New W-8IMY Form and W-8BEN-E proposed for non-U.S. entities**

FATCA: *FFI Reporting/Withholding*

Payments subject to withholding tax

- **U.S. source FDAP**
- **Sales proceeds from the disposition of securities that produce U.S. source interest and dividends, and**
- **Pass-thru payments**

FATCA: *FFI Reporting/Withholding*

Withholding 30% tax on payment to an investor who is:

- **Non Participating FFI ("NPFFI")**
  - Investor is itself an FFI and chooses not to participate in FATCA reporting system *or*
- **Recalcitrant holder**
  - Investor in FFI who refuses to give requested information to the FFI is subject to withholding tax on pass-thru payments
  - Pass-thru Payment is a portion of payment to recalcitrant holder that is attributable to deployment of assets in the U.S. – Final definition is reserved at this time
  - Pass-thru payment concept makes NPFFI's "radioactive" for PFFI's with U.S. investments

FATCA: *Timetable (updated for Ann. 2012-42)*

January 1, 2013.

- FFI electronic application process expected to begin
- Grandfathered obligations. FATCA withholding not required on obligations outstanding on January 1, 2013 *unless* materially modified after that date

January 1, 2014

- New accounts: Withholding agents (including PFFIs & registered deemed compliant FFIs) must implement "new" account opening procedures
  - USFI's must withhold on U.S.-source FDAP payments to new accounts held by documented NPFFI's and presumed FFI's
  - PFFI's must withhold on U.S. source FDAP payments to undocumented new accounts and new accounts held by NPFFI's
- Preexisting Accounts: Accounts opened prior to January 1, 2014 are categorized as "pre-existing" and account due diligence must generally be completed prior to July 1, 2014 (for prima facie FFI) or by Dec. 31, 2014 (for high value individual accounts) or Dec. 31, 2015 (for other entity or individual accounts)
  - Withholding required after these deadlines

FATCA: *Timetable*

July 1, 2014

- For “preexisting” prima facie FFIs accounts, withholding must be imposed by USFIs & PFFIs *unless* documented that account holder is a PFFI, exempt FFI or not a FFI

January 1, 2015

- For “preexisting” high value individual accounts, withholding must be imposed by PFFIs *unless* documented that they are not US accounts

March 31, 2015

- PFFIs must file information reports for 2013 and 2014 calendar years

January 1, 2016

- For other “preexisting” accounts, withholding must be imposed by USFIs & PFFIs *unless* documented that they are not US accounts
- Expiration of certain phase-in exceptions regarding a PFFI's expanded affiliated group with local law restrictions to compliance must now comply

FATCA: *Timetable*

March 15, 2016

- USFFI’s & PFFIs must report 2015 US-sourced FDAP and gross proceeds paid to non-US accounts

January 1, 2017

- USFI’s begin withholding on gross proceeds from the sale of property that can produce U.S. source interest or dividends to all documented NPFFI’s and presumed FFI’s
- PFFI’s begin withholding on payments of gross proceeds from the sale of property that can produce U.S.-source interest or dividends to:
  - Preexisting, undocumented high value individual account holders, documented NPFFI’s, and prima facie FFI accounts
  - Undocumented new accounts and new accounts held by NPFFI’s
- Withholding on foreign pass-thru payments “may” begin

March 31, 2017

- PFFI’s must report gross proceeds in addition to all data fields reported previously

FATCA: *Globalization*

February 2012

- Joint Statement from the U.S., France, Germany, Italy, Spain and the U.K. regarding an intergovernmental approach to improving international tax compliance and Implementing FATCA

June 2012

- Joint Statement from the U.S. and Switzerland regarding implementation of FATCA
- Joint Statement from the U.S. and Japan regarding implementation of FATCA

July 2012

- Joint Communiqué by France, Germany, Italy, Spain, the U.K. ,and the U.S. regarding the publication of the Model Intergovernmental Agreement to Improve Tax Compliance and Implement FATCA

September 2012

- 1st IGA to be signed: US-UK IGA

November 14, 2012

- I.R.S. publishes Model 2 agreement that requires local FFI’s to report directly to the I.R.S.

FATCA: *Globalization-Cont'd*

January 2013

- **U.K draft legislation following up on its September 2012 IGA**
  - intended to clarify the status of certain entities as financial foreign entities (FFI) or non-financial foreign entities (NFFEs) and whether an institution operating in the UK is within the rules.
  - trusts that are not collective investment vehicles or managed by another investment entity are to be treated as NFFEs, and partnerships are considered UK residents if they are managed and controlled in the UK.
- **Bilateral agreements –U.S. and Mexico as well as U.S. and Denmark**

FATCA: *Two versions of the Model Agreement*

Reciprocal and Nonreciprocal Forms

- **Establish a framework for reporting by FFI's of certain financial account information to their respective tax authorities**
- **Automatic exchange of information under existing bilateral tax treaties or tax information exchange agreements**
- **Addresses the legal issues that had been raised in connection with FATCA and simplifies implementation for financial institutions**

FATCA: *Reciprocal Model Agreement*

Reciprocal Form

- **U.S. and partner country ("FATCA Partner") exchange information relating to the *other* country's residents owning accounts with an FI in the reporting country**
  - The exchange is made on an automatic basis (See Article 2)
  - Used by U.K., Germany, France, Italy and Spain, who agreed to this approach on February 8
    - Other countries to follow
    - Applies only to jurisdictions with which the U.S. has an income tax treaty or tax information exchange agreement
  - Reporting is required even if the account produces only income that arises from sources outside the U.S.

FATCA: *Reciprocal Model Agreement*

Reporting requirements <u>from</u> FATCA Partner to I.R.S.:

- Name, address, and U.S. TIN of each Specified U.S. Person that is an Account Holder
- Account number
- Name and identifying number of the Reporting Financial Institution
- Account balance or value as of end of relevant calendar year

U.S Reporting requirements <u>to</u> FATCA Partner:

- Name, address, and TIN of any person that is resident of FATCA Partner jurisdiction and is an Account Holder
- Account number
- Name & identifying number of Reporting U.S. Financial Institution
- Gross amount of U.S. source interest, dividends or other income paid or credited to the account

FATCA: *Reciprocal Model Agreement*

When must this information be given to the other country? Art. 3(5)

- **For reporting year 2013 information, not later than Sept. 30, 2015**
  - 1 year later than provided in the regulations

- **For information beginning from reporting year 2014, not later than 9 months of end of year**

FATCA: *Due diligence*

How does the FFI determine what accounts are owned by US persons or US owned foreign entity?

- **Annex I to each Model Agreement contains 15 pages of procedures to follow to identify US reportable accounts**
  - Follows the approach of the Proposed FATCA Regulations published in February

FATCA: *Additional Points*

FATCA Partner FFI

- **Need not withhold or close accounts of recalcitrant holders as long as U.S. gets information about holder (Art. 4(2))**
  - However, the closing of accounts held directly or indirectly by U.S. persons is common
- **If FFI does not "significantly comply," the U.S. notifies FATCA Partner (Art. 5(2))**
  - FATCA Partner contacts FFI to resolve problem
  - If problem not resolved within 18 months, FFI is categorized as a non-participating that becomes subject to FATCA withholding

FATCA: *Non-reciprocal Model Agreement*

Non-Reciprocal

- **Only FATCA Partner is obligated to supply information with respect to U.S. Reportable Accounts to the I.R.S. (See Article 2)**
  - Same reporting requirements imposed on the Foreign FATCA Partner
  - Participating Countries: To be announced

FATCA: *A tour d'horizon*

Model I IGA Agreements

Reciprocal Agreement	**Two-way Street** ▪U.S. & FATCA Partner country exchange information relating to ***other*** country's residents owning accounts with an FI in reporting country
Non-Reciprocal Agreement	**One-way Street** ▪Only FATCA Partner country is obligated to supply information with respect to US Reportable Accounts to IRS

FATCA: *A tour d'horizon*

Model II IGA Agreements

- **Treasury also announced a 3rd form of IGA for Japan and Switzerland, which they called Model II**
  - Non-reciprocal form of Agreement so only information is supplied to IRS
    - BUT FFI reports information directly to IRS and not to tax authorities in Japan or Switzerland
  - No form for this Agreement has yet been released

FATCA: *Reciprocal Model Agreement*

November 8, 2012

Treasury announced that it is in discussion with 50 other countries to adopt I.G.A.s, and it expects several to be adopted by year's end.

Signed IGA countries

- First I.G.A. signed was with the U.K.
  - Signed on September 14, 2012
  - Based on Model I reciprocal IGA
- Second I.G.A. signed was with Denmark
  - Signed on November 19, 2012
  - Based on the Model 1 reciprocal IGA
- Third I.G.A. was signed with Mexico
  - Signed on November 19, 2012
  - Based on the Model 1 reciprocal IGA
- Fourth I.G.A. was signed with Ireland
  - Signed on December 21, 2012
  - Based on the Model 1 reciprocal IGA

FATCA: *The Next Steps (Despite Original Objections)*

- **Final FATCA regulations (Done)**
  - **Build on IGA's**
  - **Phase in time lines for due diligence, reporting and withholding**
  - **Expand and clarify the scope of payments not subject to withholding**
  - **Refine and clarify the treatment of investment entities**
  - **Clarify the compliance and verification obligations of FFI's**
- **FFI Agreement**
- **Updated Form W-8BENs and Instructions**
- **More IGAs**

FATCA: *Final Regulations*

January 17, 2013 Final Regs.-544 pages

- F.F.I. Registration Portal to be Created by I.R.S.
  - Opens by July 15, 2013
  - F.F.I. must obtain a G.I.I.N. from the I.R.S. to eliminate withholding
    - Global Intermediary Identification Number
    - Can obtain it if resident of I.G.A. country or participating or registered deemed compliant F.F.I.
  - U.S. Withholding agents must check the G.I.I.N. against I.R.S. list in order to eliminate withholding
    - First list will be posted by Dec. 2, 2013
      - F.F.I. must apply for G.I.I.N. by October 25, 2013 to be on this list
    - FFIs not included in the December 2013 list may not be able to avoid withholding on January 1, 2014 for new accounts or contracts.

FATCA: *Final Regulations (cont)*

- Expansion of Grandfathering Rules:
  - Exempt from FATCA all obligations outstanding on Jan. 1, 2014
- New Category of exempt entities
  - Passive entities that are not professionally managed are not treated as an F.F.I., but rather as an N.F.F.E. so they are not subject to burdensome rules
- Reduced due diligence burden for pre-existing accounts, which are held prior to Jan. 1, 2014:
  - Exempt if account is:
    - $50,000 or less & held by individual
    - $250,000 or less & held by entity or is cash value insurance or annuity contract
    - Insurance contract with account balance of $50,000 or less
- Reduced due diligence for new entity accounts
  - Can rely on self-certification in most cases

FATCA: *Final Regulations (cont)*

- Time allowed to review Pre-existing Accounts (pre-Jan. 1, 2014 accounts)
  - Until Dec. 31, 2015, *unless* the account holder is a prima facie F.F.I
- Phased Implementation of Reporting:
  - For 2013 & 2014 calendar years, due by March 31, 2015
- Phased implementation of Withholding on Pass-through payments & gross proceeds from sales :
  - Exempt if occurs before Jan. 1, 2017
- Many other details to be reviewed
- Next steps from the I.R.S.: Publication of
  - Revenue Procedure that will contain all the requirements applicable to an F.F.I., *and*
  - Revised Form W-8BEN-E and other forms as well as the instructions

FACTA From the Client Perspective

- IGA awareness: Were clients aware of governments in the countries in which they operate intending to enter into an intergovernmental agreement with the IRS?
- Process revision: To what extent will clients revise their own client on-boarding, customer identification or documentation processes?
- Account identification requirements, documentation requirements and systems changes
- Existing program leverage: Leveraging of their AML/KYC compliance programs to help satisfy the FATCA requirements.

FACTA From the Client Perspective-Cont’d

- Categorize the client within the FATCA framework
  - USWAs
  - FFIs
  - NFFE’s
- Identify the expanded affiliated group subject to categorization
- Any changes in client’s business models?
  - Exit from U.S. investments or individuals?
  - Sell or hold strategies?

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