FATCA: WHERE ARE WE NOW?

Bahamas STEP Meeting
February 9, 2011

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Introduction

- FATCA - Detect, deter and discourage offshore tax evasion through the use of foreign financial institutions (FFI), close information reporting loopholes; and
- Regulate perceived abuses concerning the use of foreign trust property by U.S. persons
  - Sen. Max Baucus, Chair of S. Finance Comm. Cong. - Oct. 27, 2009
  - Aug 1 2006, Tax Haven Abuses: The Enablers, the Tools and Secrecy (S. Perm. Subcomm on Investigations)

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Key FATCA Sections

Foreign Financial Institution Reporting	Eff. Jan 1, 2013 (added IRC 1471 – 1474)
Use of Foreign Trust Property	Effective Mar 18, 2010 (IRC 643(i) changed)
Expansion of Foreign Grantor Trusts	Effective Mar 18, 2010 (IRC 679(c) changed)
Required PFIC reporting	Effective Mar 18, 2010 (changed IRC 6088)
Foreign Financial Asset Reporting	Effective Mar 18, 2010 (added IRC 6038D)

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FFI Reporting

- New Code Sections 1471 – 74 require certain FFIs that hold U.S. investments to:
  - Enter into agreement with IRS
  - Identify U.S taxpayers (direct and indirect)
  - Report information on U.S. taxpayers
  - Withhold 30% on payments to non-compliant account holders and FFIs that do not meet FATCA requirements

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What Is a FFI?

- Foreign entity which in its ordinary course of business accepts deposits, holds financial assets for others, or its primary business activity is investing, trading financial assets or commodities

- Includes:
  - Banks
  - Broker / Dealers
  - Foreign Hedge Funds
  - Private equity funds
  - Private investment funds
  - Pension funds
  - Insurance companies
  - Foreign Trust Companies
  - Foreign Trusts
  - Etc.

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FFI Reporting

- Thus:
  - A FFI which holds U.S. assets will be subject to the withholding, unless they fall within an exemption or they enter into a reporting agreement with the IRS by 31 Dec 2012
  - The 30% withholding is applicable on U.S. source income (dividends, interest, capital gains, etc.) even if such income is exempt from tax under IRC Sections 861 and 871

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IRS Agreements

- Six Requirements
  - Four apply to U.S. accounts maintained by FFI
    - Report U.S. account information
    - Withhold 30% for non-compliance, no agreement or FFI has made election
    - Comply with IRS information requests
    - Close account if U.S. account holder refuses to waive right of secrecy
  - Two apply without regard to maintaining U.S. accounts
    - Obtain information to determine U.S. / Non-U.S. account
    - Comply with due diligence requirements

IRS Agreements

- Exceptions to IRS agreements
  - Does not apply to publicly traded funds – IRC 1471(d)(2)(C)
  - Deemed Compliance
    - What FFI's will be deemed compliant
    - Non-U.S. Funds and others prohibiting U.S. Investors?
- Practical Issues
  - Determining investors (individual or institutional) / account holders U.S. status
  - Reporting U.S. account information
  - Withholding on non-compliant U.S. account holders

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U.S. Account

- Financial account held by one or more U.S. persons except:
  - a company, or its affiliates which includes at least one entity in the chain of ownership that is 80% owned by the parent, whose stock is traded on an established securities market,
  - tax-exempt organization or trust
  - division of the U.S. gov't or State gov't
  - bank, a REIT, a registered investment company, and a common trust fund

- U.S. account also includes a U.S. owned foreign entity
  - Includes foreign entities where a U.S. person has a 10% or greater ownership interest
  - IRC 1471(d)(1) and 1473(2)

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IRS Agreements

- U.S. Account Information to be Reported
  - Name, address and tax identification number of each U.S. person for directly owned accounts and / or each account of a U.S. foreign owned entity
  - Account number
  - Account balance or value
  - Gross receipts and withdrawals or payments from the account

Non-compliant Withholding

- Primarily issue for Non-U.S. Funds
  - U.S. Funds and financial institutions already required to withhold where foreign investor or account holder is undocumented or misidentified
- Pass-thru Payments
  - Determining amount
  - When is withholding required

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Pass-thru Payments

- Obligation to Withhold May Arise When:
  - U.S. source income or proceeds of sale are paid to non-U.S. fund / financial institution
    - No IRS agreement
    - Participating but non-compliant U.S. account holder
    - Non-compliant U.S. account holder sells or redeems fund or account assets

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Bottom Line

- FFI and Funds with U.S. Investments are subject to FATCA with limited exception
- Must Enter into Agreement with IRS, unless exempt or deemed compliant
- Determine U.S. and non-U.S. account holders
- Annually Report U.S. Account Information
- Withhold on non-compliant U.S. accounts

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Public Comments

- Request for Comments on regulations
- Announcements and Notices are issued requesting thoughts on implementation of law
- IRS Notice 2010-60 focused on the FFI withholding and exemptions from FFI definition - insurance pension products, and family trusts
- IRS Announcement 2010-22 broadly requested FATCA comments

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Treasury Regulations

- Income tax regulations are generally written by the Treasury Dept. (Asst. Sec. for Tax Policy) in conjunction with IRS Chief Counsel's Office
- Treasury recognizes there are significant costs associated with FATCA compliance

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Treasury Regulations

- Providing Treasury with comments
- Considerations
  - Spirit of the law (principles of law and jurisprudence)
  - Ability to administer and enforce
- Demonstrate and explain how comments and recommendations follow the spirit of the principles of law
- Provide recommendations on ability to administer

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Common Theme of Comments

- STEP USA
- American Bar Association
- American College of Trust & Estate Counsel (ACTEC)
- American Institute of Certified Public Accountants

- Exemptions from FFI reporting
- Requirements for determining U.S. Accounts
- Deemed Complaint FFIs
- Duplicative Reporting
- Determining value of account balance
- Valuation and distribution treatment of use of trust property

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U.S. Treasury Position

- Treasury is very aware of FATCA compliance costs
- Itai Grinberg, attorney-advisor to Treasury International Tax Counsel spoke at ABA Tax Section meeting

- FATCA panel for Treasury is taking the compliance burden very serious and studying comments with regard to:
  - Deemed compliant FFI
  - Excluded FFIs
  - Foreign retirement plans
  - Pass-through issues
  - Compliance burden
  - Overriding treaty issues

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U.S. Treasury Position

- Excluded FFIs
  - Notice 2010-60 stated that Treasury would consider excluding insurance companies that only issue insurance or reinsurance contracts without cash value
- Grinberg:
  - Confirmed this is likely

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U.S. Treasury Position

- Deemed Compliant FFIs
  - Notice 2010-60 indicates that small family trusts and investment funds will be considered deemed compliant FFIs
  - What is small – number of beneficiaries / owners?
- Grinberg:
  - Guidance will be provided as there was overwhelming public comments
  - Guidance is unlikely to provide exclusion based on number of persons involved

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U.S. Treasury Position

- Foreign Retirement Plans
  - Notice 2010 – 60 indicates Treasury is likely to provide exemption for foreign retirement plans from reporting
- Grinberg:
  - A regulation will be written but unlikely to provide specific list of foreign retirement plans but rather provide required guidelines for exemption

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U.S. Treasury Position

- Foreign retirement plans
- Grinberg:
  - Regulations are likely to provide additional guidance on what constitutes a retirement plan pursuant to local foreign law
  - Requirements regarding employer sponsorship
  - Allowable participants
  - Etc.

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U.S. Treasury Position

- Compliance Burden
  - Notice 2010-60 provides within 5 years after date on which FFI enters into IRS agreement all pre-existing non-U.S. accounts must be treated as new and subject to due diligence for determining if U.S. account
- Grinberg:
  - Stated that commentators considered this rule “the single largest cost driver” of compliance for FFIs
  - Panel will carefully study

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U.S. Treasury Position

- Treaty Override
  - FFI institutions are eligible for refund of withheld moneys only to the extent a treaty addresses such matter

- Grinberg:
  - Confirmed that a refund of withholding is required only where addressed by treaty
  - Refund for exempt U.S. source income is only provided if treaty provision exists

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New VDP

- IRS announced a new Voluntary Disclosure program focused on unreported offshore accounts
  - First mentioned by IRS Commissioner - December 2010
  - IRS is using initial VDP to develop new leads
  - Commissioner stated FATCA makes it riskier for U.S. persons to hide their income, hence more VDs before effective date of FFI reporting

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New VDP

- Almost 3,000 add'l disclosures have been made since the 2009 VDP ended and FATCA rules enacted
- Terms:
  - Ends August 31, 2011
  - Provide returns and payment
  - Period covered is 2003 through 2010
  - 25% and 12.5% international information return penalty
  - Interest, accuracy and underpayment penalties still apply

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Questions

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