FATCA: Catalyst for Global Cooperation on Exchange of Tax Information

In this article, the author describes the main features of the Foreign Account Tax Compliance Act (FATCA), the events that led to its enactment and the development of global cooperation for information exchange.

1. Introduction – G20 Sets the Stage for Global Exchange of Tax Information

The summit of the Group of 20 ("G20") Leaders in St. Petersburg, Russia, on 5-6 September 2013 marked the fifth anniversary of the G20 Summit.1 The meeting among the leaders of the world’s largest economies focused on a number of important issues relative to the world economy, including automatic exchange of tax information as a new global standard. The declaration2 issued at the conclusion of the G20 Summit sets forth the expectation that a single global standard will be presented by February 2014 and that the technical modalities will be finalized by mid-2014. Moreover, the G20 has committed to begin automatic exchange among its members by the end of 2015. The declaration thereby provides extraordinary support for the new single global automatic exchange of information standard.

Following the conclusion of the G20 summit, an informal meeting of the EU ECOFIN Council3 and the OECD took place in Vilnius, Lithuania. At that meeting, the European Union and the OECD agreed to foster the progress in the development of the global automatic exchange of information. In his remarks of 14 September 2013, Angel Gurria, OECD Secretary General, described the benefit in financial institutions in another country. The G20 has committed to begin automatic exchange among its members by the end of 2015. The declaration thereby provides extraordinary support for the new single global automatic exchange of information standard.

The exchange of global tax information is important to protect the integrity of the tax systems of countries. Without the exchange of tax information, residents of one country may be able to hide financial assets in accounts in financial institutions in another country. The G20 has been a leader in advancing international tax transparency and exchange of information since 2009, which is reflected in the current name and significance of the forum. See www.g20.org/about_g20.


5. It has been noted by many commentators that by enacting FATCA, the United States placed its capital markets at risk. Had foreign investors reduced or liquidated their US investments, the result would have been devastating to the US capital markets.
6. The position of Deputy Assistant Secretary (International Tax Affairs) is the highest ranking US Treasury official with responsibility for international tax affairs.
7. K.A. Parrillo & A. Velarde, U.S. Treasury Official Describes ‘Constructive’ Meetings with Indian Tax Officials, Tax Analysts (16 Sep 2013). Historically, it has been rare that a US Deputy Assistant Secretary (International Tax Affairs) has attended such high-level meetings. Because of the prominence and technical aspects of the tax issues, it would not be surprising if the inclusion of high level tax officials continues and expands to include tax officials from more of the G20 countries other than the United States, China and India.
The response of the United States to the use of unreported offshore accounts by US taxpayers was to enact the unilateral FATCA legislation that requires foreign financial institutions (FFIs) that receive US-source payments to report US account holders and certain US owners of foreign-entity account holders to the Internal Revenue Service (IRS). Under FATCA, if an FFI does not agree to report these account holders to the IRS, the US withholding agent must withhold 30% of the payment. Although the US Congress enacted FATCA in March 2010, it will not take effect until 1 July 2014. The implementation dates have been delayed several times, but Treasury officials have publicly confirmed that FATCA will become effective on 1 July 2014 and there will be no more extensions. The implementation of the act will be phased in over three years.

The final FATCA regulations, consisting of 543 pages, were officially published on 28 January 2013 in the Federal Register. Correcting amendments to those finalized regulations were issued on 10 September 2013. Substantive amendments to the final regulations are also anticipated, as well as conforming changes to the withholding and reporting regulations under chapters 3 (sections 1441-1464) and 61 (sections 6041-6050W) of the Internal Revenue code (IRC).

Additionally, the US Treasury Department has either signed or initiated Intergovernmental Agreements (IGAs) with 12 countries (including Switzerland) as of 29 November 2013. An IGA will enable FATCA-partner-country FFIs to comply with the FATCA requirements by permitting FFIs in a FATCA partner country to collect and provide the information about US account holders. As discussed above, this later development has accelerated

10. The G20 has pursued parallel developments in combating money laundering, financing of terrorists, and related threats to the international financial system. The FATCA regulations incorporate references to the Financial Action Task Force (FATF) standards.

11. The G20 leaders announced in April 2009 at the London summit that they were adopting measures to curtail tax havens and to target "non-cooperative jurisdictions." The summit communiqué expressly stated that G20 members, "agree ... to take action against non-cooperative jurisdictions, including tax havens. We stand ready to deploy sanctions to protect our public finances and financial systems. The era of banking secrecy is over." See G20, London Summit – Leaders' Statement (2 Apr. 2009). The G20 leaders also announced that they would support measures to effectuate this goal, including giving extra weight to the principles of tax transparency and information exchange when designing bilateral aid programs. See G20, Declaration on Strengthening the Financial System – London Summit (2 Apr. 2009).

12. OECD Agreement on Exchange of Information on Tax Matters (18 Apr. 2002), Models IBFD.

13. The so-called OECD "grey list" is a list first published in April 2009 by the Global Forum on Transparency and Exchange of Information for Tax Purposes, listing jurisdictions that had committed to implementing, but had not yet implemented, the Global Forum's international standards for the exchange of tax information. See www.oecd.org/tax/transparency/Frequently%20asked%20questions.pdf

14. The Global Forum on Transparency and Exchange of Information for Tax Purposes is a 120-member multinational framework sponsored by the OECD that has been meeting since 2000 to work on transparency and information exchange among OECD and non-OECD countries. See www.oecd.org/tax/transparency/abouttheglobalforum.htm


global cooperation to create an efficient and uniform automatic exchange of tax information.

Although efforts to engage in the exchange of tax information had begun prior to the enactment of FATCA, it was the threat of 30% withholding from US-source investment income to FFIs that caused government officials of other countries to accelerate discussions and planning for an automatic tax information exchange between governments. Although the G20 has committed to a single global standard of automatic information exchange, the IGAs will still serve a purpose because of the need to allow US withholding in cases of non-compliance.

2. Moving Forward

On the conclusion of the G20 summit of 5-6 September 2013 and the meeting of Finance Ministers and Central Bank Governors of 18-19 April 2013, the G20 issued a declaration and a communiqué, respectively, that announced the beginning of automatic information exchange among G20 members by the end of 2015 and that praised the progress made to date in the international movement toward automatic information exchange.29 The communiqué was issued following the release of the OECD Report to the finance ministers to update them on the OECD’s work to improve information exchange. The communiqué highlights the OECD’s efforts to achieve a global standard of automatic tax information exchange and identifies the Multilateral Convention on Mutual Administrative Assistance in Tax Matters (1988)29 as the forum to allow the participation of all countries.30 Subsequently, on 9 May 2013, the IRS announced that the United States, Australia, and the United Kingdom will share information involving trusts and companies that hold assets on behalf of residents throughout the world.31

According to the IRS news release, the three countries have each acquired a substantial amount of data revealing extensive use of such entities organized in a number of jurisdictions including Singapore, the British Virgin Islands, the Cayman Islands and the Cook Islands. The data contains both the identities of the individual owners of these entities, as well as the advisors who assisted in establishing the entity structure. The data and the analysis will be shared with tax administrators of countries that request the data.

It is noteworthy that Singapore, the Cayman Islands and the British Virgin Islands have all announced their intention to enter into an IGA with the United States.32

3. FATCA Background

3.1. Preceding events

In addition to the actions of the G20 described above, other events occurred in the United States that highlighted the need for better US tax compliance. Notably, the US Senate Permanent Subcommittee on Investigation (PSI) had been investigating, holding public hearings, and issuing reports on the use of tax haven institutions by US individuals to avoid US tax.33 As a result of those hearings and reports, several bills, for example, the Stop Tax Haven Abuse Act, were introduced in the US Congress to combat the abuses identified by the PSI.34

The public reports of the Department of Justice’s suit against Union Bank of Switzerland (UBS) for conspiring to defraud the United States by impeding IRS investigations35 focused attention on unreported accounts of numerous US account holders. Under US law, not only is a US taxpayer required to include income from foreign sources in gross income and pay tax on any foreign-source income, but a US person with an interest in, or signature or other authority over, any foreign financial accounts with an aggregate value of USD 10,000 or more is also required to report information about those accounts on Form TD F 90.22.1 (Report of Foreign Bank and Financial Accounts, FBAR) under the Bank Secrecy Act.36 As a result of UBS releasing the names of US account holders to the IRS, numerous US taxpayers have entered into a voluntary agreement with the IRS, leading to substantial tax revenues for the US government.

30. G20, supra n. 28, at para. 14. (“More needs to be done to address the issues of international tax avoidance and evasion, in particular through tax havens, as well as non-cooperative jurisdictions. We welcome the Global Forum’s report on the effectiveness of information exchange. We commend the progress made by many jurisdictions, but urge all jurisdictions to quickly implement the recommendations made, in particular the 14 jurisdictions, where the legal framework fails to comply with the standard. Moreover, we are looking forward to overall ratings to be allocated by year end to jurisdictions reviewed on their effective practice of information exchange and monitoring to be made on a continuous basis. In view of the next G20 Summit, we also strongly encourage all jurisdictions to sign or express interest in signing the Multilateral Convention on Mutual Administrative Assistance in Tax Matters and call on the OECD to report on progress.” We welcome progress made towards automatic exchange of information which is expected to be the standard and urge all jurisdictions to move towards exchanging information automatically with their treaty partners, as appropriate. We look forward to the OECD working with G20 countries to report back on the progress in developing of a new multilateral standard on automatic exchange of information, taking into account country-specific characteristics. The Global Forum will be in charge of monitoring. We welcome the progress made in the development of an action plan on tax base erosion and profit shifting by the OECD and look forward to a comprehensive proposal and a substantial discussion at our next meeting in July.”).
compliance program initiated by the IRS. The Department of Justice continues to investigate foreign banks it believes are shielding US taxpayers. Wegelin & Company, the oldest Swiss bank, pleaded guilty to criminal charges that it conspired to hide the accounts of 100 US taxpayers from 2002 through 2010 and paid USD 74 million in fines and restitution to the IRS. More recently, on 29 August 2013, the United States and Switzerland issued a Joint Statement on tax evasion investigations. The Department of Justice announced a program that encourages Swiss banks to cooperate in ongoing investigations of the use of foreign bank accounts to commit tax evasion. The Swiss Federal Department of Finance also issued a joint statement with the US Department of Justice that announced Switzerland will encourage its banks to participate in the US Department of Justice program.

3.2. Purpose of FATCA

Against the backdrop of reports of US taxpayers not reporting foreign accounts and earnings from those accounts, Congress enacted FATCA in 2010. The sole purpose of FATCA is to ensure that all US direct and indirect owners of foreign financial accounts annually report the value and income of those accounts to the IRS. To accomplish this goal, FATCA requires third-party FFIs, such as banks and securities brokers to report to the IRS identifying information about US account holders as well as the value and income of the account, similar to the domestic Form 1099 third-party reporting regime under which banks and brokers are required to file annual reports with the IRS on the income of US account holders.

Complementing FFI reporting, other FATCA provisions require the reporting of foreign accounts by US taxpayers similar to the 1099 reporting system, such that both third-party reporters and first-party reporters (i.e. the income recipient) are obligated to report the first party’s income. A US foreign account holder or owner of a foreign entity, in addition to reporting the income from foreign accounts on a US tax return, must report detailed information about the foreign account under section 6038D on Form 8938, which requires similar but not identical information as that required by the FBAR report. Additionally, US owners of foreign mutual funds and other investment vehicles known as Passive Foreign Investment Companies (PFICs) must report certain information about their PFIC holdings annually. Thus, FATCA replicates the domestic reporting regime in the cross-border context and requires both third-party payor and first-party taxpayer reporting.

3.3. General description of statutory provisions

As noted previously, the FATCA tax regime is designed to ensure that offshore income of US persons is reported and to verify whether deposits made in offshore accounts are after-tax income. To achieve that goal, all foreign entities are subject to US reporting or certification procedures. The FATCA provisions are triggered by the payment of a “withholdable payment” to a foreign entity. If the applicable requirements of FATCA are not satisfied, the US payor must withhold US tax equal to 30% of the payment made to the non-compliant foreign entity. In some cases, the 30% tax will be refundable where an income tax treaty applies. Under the FATCA rules, which are contained in sections 1471–74 of the IRC, foreign entities are divided into two classes: FFIs and non-financial foreign entities (NFFEs). FFIs include depository and investment banks, mutual funds and certain insurance companies that issue cash value insurance contracts or annuities. FFIs must enter into an agreement with the IRS in which they are obligated to determine which of their account holders are US persons and to provide to the IRS identifying information about the US account holder and the account. An NFFE is any foreign entity that is not an FFI. Although an NFFE has similar due diligence requirements to identify its substantial US owners, an NFFE is not required to enter into an agreement with the IRS. Instead the NFFE provides the US withholding agent payor with a certificate that either affirms that the NFFE has no US owners or identifies its US owners.

40. US Justice Department, Program for Non-Prosecution Agreements or Non-Target Letters for Swiss Banks. The Tax Division of the Department of Justice released comments concerning the program on 5 Nov. 2013. To participate in the program, a Swiss bank must send a letter of intent to the Department of Justice by 31 Dec. 2013. See www.justice.gov/tax/2013/Comments_on_Program_for_Non-Prosecution_Agreements_or_Non-Target_Letters_for_Swiss_Banks.pdf.
41. See supra n. 39.
42. Sec. 6041–6050W IRC. US taxpayers are familiar with this reporting system, whereby banks and other financial institutions issue Forms 1099 to US taxpayers and file copies of those reports with the IRS, so that the IRS can ensure that income is properly reported by a US taxpayer on the US taxpayer’s income tax return.
3.4. Impact of FATCA

Because the US capital market is the largest in the world, FFIs generally are not in a position to forgo investment in US equity securities and debt obligations, including Treasury securities. Thus, FFIs began meeting with US Treasury officials to identify the issues in FATCA implementation in their industry, including administrative burdens and costs. The FATCA statute is “bank-centric,” meaning that the statute refers to “accounts” and provides other rules that may not be readily adaptable to other industry business models, such as insurance companies that issue contracts instead of holding deposits or securities for customers as banks and brokers do. Moreover, non-US banks already have a role as Qualified Intermediaries (QIs) in the US reporting and withholding requirements applicable to foreign account holders. Non-US banks that serve as QIs already have familiarity with the US reporting system upon which FATCA is based.

One of the key burdens for all FFIs is the requirement to identify existing account holders whose accounts were opened prior to the passage of FATCA because US law previously did not require FFIs to identify US account holders and, therefore, FFIs did not collect that information. For non-bank FFIs, such as asset management FFIs and insurance companies, the bank-centric FATCA provisions are difficult to apply to their business models. Thus, the regulations needed to accommodate the different business models of different financial industries, such as the insurance and managed asset industries. Accordingly, representatives of trade groups began the long process of suggesting ways in which the FATCA provisions could be modified to apply to non-bank FFIs. This process involved the submission of almost 300 detailed comment letters and a lengthy public hearing. At the end of the process, the Treasury Department produced extremely detailed final regulations that respond to the numerous concerns raised by the large number of commentators representing many industries.

Although the FATCA legislation imposes significant burdens on FFIs, its goal was not to disrupt markets. A number of statutory provisions, such as the “grandfather” provision that exempts certain pre-existing obligations from withholding (but not reporting), were added to prevent market disruptions. Without the grandfather provision, FFIs may have been required to bear the economic cost of the 30% withholding on their customers’ accounts. The final regulations provide other provisions that are designed to reduce, where possible, the economic burdens of FATCA.

3.5. Conflicts of law

3.5.1. Data privacy laws

A major impediment to the implementation of FATCA is the conflicts of law between the FATCA requirements and local country privacy legislation and, in some cases, criminal codes that prohibit the collection and release of personal data except under certain conditions. While the United States has not enacted privacy legislation applicable to the private sector, other countries have enacted such laws. In the European Union, the EU Data Protection Directive, while not mandating any specific language or method, requires each member state to enact legislation consistent with its provisions. The principles of the EU Data Protection Directive govern the collection and disclosure of personal data. Under the Directive, data, such as whether an account holder is a US citizen or resident, would not be permitted to be collected. Moreover, even if such data could be legally collected, it could not be disclosed to the IRS as required under FATCA. Although many data privacy laws permit the collection and reporting of information required by the home country government, generally the disclosure of these reports to foreign governments is not permitted. However, if an FFI does not collect or disclose data to the IRS, the FFI will be subject to 30% withholding under FATCA. Although FATCA takes into account these data privacy laws by requiring a US account holder to waive any applicable foreign privacy law that would prevent reporting of the account, under some foreign laws, the waiver requirement may be viewed as coercive and, therefore, not permissible. No FFI can serve two masters.

3.5.2. The solution – intergovernmental agreements

The solution to the problem, the IGA, initially was developed by the US Treasury Department in conjunction with the tax administrators of the United Kingdom, Germany, France, Italy, and Spain. The IGA concept was first announced in a Joint Statement issued on 7 February 2012, by the United States and the five countries in conjunction with the proposed FATCA regulations. The IGA is designed to resolve the conflicts of law problem by requiring local FFIs to provide their FATCA reports to their country’s tax authorities rather than to the IRS. Since reporting to a local governmental body generally is permitted under the EU Data Protection Directive, the

60. For example, in the United Kingdom, personal information is protected not only under the Data Protection Act of 1998 but also under case law, which recognizes a contractual duty of confidentiality, and the Banking Code. In Canada, the Personal Information Protection and Electronic Documents Act limits collection and disclosure of personal information.


62. Sec. 1471 IRC.

63. Sec. 1471(b)(1)(F) IRC.


65. Id.
local FFIs would not be in violation of their local data privacy acts. Also, under an IGA, an IGA partner country would agree to pass any required enabling legislation to permit its FFIs to collect the information.

Notably, IGAs address only the collection of data and the reporting of data by FFIs, but are silent on the reporting requirements imposed on NFFEs. FATCA requires certain NFFEs to identify their substantial US owners and report that information to a US withholding agent. Since IGAs do not provide relief to NFFEs that are also subject to data privacy laws, it is not clear how NFFEs will be able to comply with FATCA. Both the final regulations and the IGAs are silent on this issue. Clearly, prior to the commencement of FATCA reporting in 2015, the issue will need to be resolved.

Following the announcement by the Group of Five (G5) and the Treasury Department about the development of an IGA, Japan and Switzerland also initiated discussions with the Treasury Department, and a second type of IGA, named Model 2, was announced, under which a FATCA partner would permit its FFIs to enter into FFI Agreements with the IRS and directly report US account information.

On 12 July 2013, the Treasury Department announced that it was negotiating with more than 80 jurisdictions concerning FATCA and would continue its outreach to interested jurisdictions. For example, the Qatar Central Bank held a meeting in December 2012 for invited senior government officials and financial institutions in the Gulf Cooperation Council to discuss FATCA and IGAs. Additionally, Treasury officials recently disclosed that the US Treasury Department has been working with the US State Department to implement a coordinated outreach to all jurisdictions that have not yet engaged with the US Treasury on FATCA.

For US purposes, the Treasury Department has adopted the position that an IGA, like a TIEA, is considered an executive agreement and not a treaty. A treaty requires the advice and consent of the Senate under article II, section 2, clause 2 of the US Constitution. The IRS has also adopted the position that TIEAs are also considered to be executive agreements and therefore do not require Senate approval.

3.5.3. Model 1 Agreements

Model 1 is the IGA under which FFIs report US account holders directly to their local tax authority which, in turn, provides the information to the IRS through an automatic exchange of information program authorized under a tax treaty exchange of information provision, a TIEA, or the Convention on Mutual Administrative Assistance in Tax Matters (1988). The Model 1 concept was agreed to by the G5 and the United States as evidenced in the statement of 7 February 2012. Under Model 1, the United States can agree to provide similar reporting on the US accounts of the other country’s residents (the reciprocal version) or, under the non-reciprocal version, not to agree. As of 15 September 2013, ten Model 1 IGAs have been signed. All of these IGAs have included an extensive list of FATCA partner exempt entities and accounts under Annex II. However, as discussed below, future IGAs likely will not contain detailed lists in Annex II as the Treasury Department announced that they will no longer negotiate over specific entities and accounts except in cases where it is not clear whether an entity or account would qualify as deemed-compliant or exempt under the FATCA final regulations.

Model 1 contains several articles, including articles on definitions, obligations to obtain and exchange information, the time and manner of exchange, and the application of FATCA to the FATCA partner country FFIs. It also details collaboration on compliance and enforcement, mutual commitment to enhance the effectiveness of information exchange and transparency, consistency of the application of FATCA, consultations and amendments, and two annexes. Some of those provisions are at variance with the final regulations. For example, the final regulations require reporting of a US owner of a foreign entity account holder if the US owner owns 10% or more of the foreign entity account holder. Under the Model 1 IGA, the Financial Action Task Force (FATF) reference is substituted, which generally is a 25% ownership level.

Annex I sets forth the due diligence requirements for FFIs to apply to identify and report US accounts. Annex II initially listed specific non-reporting FFIs and products, i.e. those FATCA partner FFIs and products that are not subject to withholding and are not required to report on US account holders or owners. Annex II, although no longer a customized list of FATCA partner FFIs and accounts that are considered to be low risk for tax avoidance and therefore are not subject to the FATCA provisions, may identify

66. Exceptions to reporting of US owners are provided for publicly traded companies the stock of which is regularly traded and active NFFEs. Notably, property and casualty insurance companies generally are treated as passive NFFEs because amounts earned by an insurance company in connection with its reserves for insurance and annuity contracts is treated as passive income. See Treas. Reg. 1.1472-1(c)(iv)(A)(11).


68. Id.


70. While the US Treasury has not made any official pronouncements, it has not submitted any IGAs to the Senate Foreign Relations Committee for review (the first step in the treaty process).


73. Treas. Reg. 1.1471-1(72).

74. For the list of countries that have signed or intalled IGAs, see www.treasury.gov/resource-center/tax-policy/treaties/Pages/FATCA-Archive.aspx.


76. Id.

77. Treas. Reg. 1.1473-1(b) (defining “substantial U.S. owner”).
certain FFIs and accounts as deemed-compliant under the new policy. Under the first IGAs, such as the one with the United Kingdom, various government-sponsored retirement plans and savings accounts are listed in Annex II. Annex II therefore permitted a FATCA partner to identify those retirement funds and savings accounts that may not have met all of the requirements for exemption under the final regulations.

However, once the final regulations were issued on 28 January 2013, the Treasury Department has announced that because of the detailed final regulations, the need for Annex II to provide certainty on which FATCA partner FFIs and accounts are exempt is not as imperative. Annex II therefore will not be used as a “comfort ruling” and will apply to a narrow set of circumstances where there is a legitimate question about the eligibility of an FFI for an exemption from FATCA under the final regulations. This position of the Treasury Department may be problematic for potential FATCA partners that have FFIs and accounts that will not meet the requirements for exemption imposed by the final regulations.

3.5.4. Model 2 Agreements

The other model IGA, Model 2, does not require FATCA reporting to be indirectly made to the IRS through local tax authorities. Rather, it permits local FFIs to directly report to the IRS in accordance with the FATCA regulations, supplemented by an exchange of information between the two governments concerning “recalcitrant” account holders that do not cooperate with the FATCA requirements. 78 Switzerland and Japan have signed a Model II IGA.

The Model 2 IGA is similar to the Model 1 IGA except that it provides legal authority for the Model 2 country FFIs to enter into FFI Agreements with the IRS and to report information about US account holders directly to the IRS under local law. Like Model 1 IGAs, the Model 2 IGA contains an Annex I and Annex II.

The IGA between the United States and Switzerland contains some interesting provisions. As expected, the IGA provides an “enabling” clause under which Swiss FFIs are authorized to enter into an FFI Agreement with the IRS and which expressly provides that a Swiss FFI that enters into an FFI Agreement is not liable to any penalty according to article 271 of the Swiss Criminal Code. 79

Perhaps the most interesting aspects of the IGA are found in article 5 that governs the exchange of information. Requests for the taxpayer identification number and other information of recalcitrant shareholders will be made under article 26 of the Switzerland–United States Income Tax Treaty (1996), as amended by the Protocol of September 2009. 80 Until the Protocol is in effect, no requests may be made. Moreover, information requests may only be made for the period beginning on the date of entry into force of the IGA. Because one US Senator has placed a “hold” on the Protocol, the delay is obviously a barrier to full implementation of the IGA at least with respect to recalcitrant account holders.

Additionally, under the Swiss IGA, the Swiss Federal Tax Administration is required to respond to a request for information within eight months or else the account will be treated as a recalcitrant account until the information is provided. Withholding on the recalcitrant account begins after the eight-month period runs. This is two months longer than the six months provided in the Model 2 IGA. Because of the most-favoured-nation provision in all IGAs, any subsequent Model 2 IGAs should be subject to the eight-month period. The provision makes clear that the burden of the withholding tax does not fall on the FFI but rather upon the account holder. This is important because FFIs have been concerned that they would bear the economic burden because local law would not permit an amount to be withheld from a payment to an account holder, and the 30% withholding tax would be a cost that the FFI could not pass on to its account holder. This provision clearly permits an FFI to pass on the cost of any withholding tax to a recalcitrant account holder.

Finally, article 13 leaves open the possibility of a Model 1 reciprocal agreement being negotiated, a provision that is also contained in the Model 2 Agreement.

3.5.5. “Free-standing” IGAs

The US Treasury Department recently announced that it will enter into a “free-standing” IGA with countries that do not have a tax information sharing relationship with the United States. 82 The “free-standing” IGA can be either a Model I or a Model II IGA, but the Model I IGA will be limited to a non-reciprocal IGA. 83 A “free-standing” IGA will contain the procedures and legal authority for an exchange of information that otherwise would be contained in a tax treaty, a TIEA, or a multilateral agreement. 84 The development of a “free-standing” IGA is important for such significant financial centre jurisdictions as Singapore and Hong Kong, which currently do not have a tax information exchange relationship with the United States. 85 A “free-standing” IGA is also important because the time to negotiate a TIEA or tax treaty would require a period that would extend beyond 1 July 2014, the revised FATCA effective date. 86

81. Although the Protocol has been signed and transmitted to the Senate, the Senate has not ratified it by the time of the writing of this article.
83. Id.
84. Id.
3.5.6. US reciprocal exchange of information

3.5.6.1. Current US exchange of information program

The United States currently is obligated to exchange tax information with its tax treaty and TIEA partners as well as with the original signatories to the Convention on Mutual Administrative Assistance in Tax Matters (1998). Information for those exchange agreements is collected by US withholding agents that make cross-border payments to non-US persons. Information collected includes the name of the beneficial owner of the payment, the address of the beneficial owner, the amount of the payment, the type of income, and any tax withheld under sections 1441 and 1442 of the IRC. Much like the Form 1099 reporting system for US residents, a withholding agent must provide a payee with a Form 1042-S (the equivalent to a Form 1099 or Form W-2), a copy of which is also filed with the IRS. The withholding agent must also file a return, Form 1042 (the equivalent to Form 941 or 945), which reports on an aggregate basis all of the payments made during a calendar year and all of the tax paid.

Although the IRS collects this information from US withholding agents, it is not clear whether effective tax information exchanges occur because there is no uniform method of providing the information to treaty partners. FATCA has accelerated the practical development of a common scheme to permit an efficient automatic exchange of tax information.

3.5.6.2. Final deposit interest reporting regulations

A major step toward FATCA implementation was the issuance of the final deposit interest reporting regulations on 17 April 2012, which require US banks, US middlemen, and other US payors of bank deposit interest to report deposit interest earned by non-resident alien individuals who reside in a country with which the United States has in force an exchange of information agreement.

Although all US-source interest other than deposit interest has been subject to reporting (and withholding to the extent it is not portfolio interest or exempt under a treaty) under sections 1441 and 1442 of the IRC, deposit interest of non-resident aliens has not been subject to reporting other than for deposit interest paid to Canadian residents since 2002. Deposit interest (including interest paid on an account with a bank, a savings institution, or an insurance company), although US-source interest, is not subject to US tax when paid to a foreign person under sections 871(ii)(2)(A) or 882(d) of the IRC and is not subject to section 1441. However, under current regulations, a foreign person must provide a Form W-8BEN in order to avoid reporting or backup withholding under section 6049. The final interest deposit reporting regulations permit a US financial institution to report a customer as a resident in the country based on the customer’s permanent address listed on Form W-8BEN. Forms W-8BEN are required to be signed under penalties of perjury.

The first reports for 2013 must be filed by 15 March 2014. Significantly, unlike other types of interest paid to foreign persons, reporting is not required on deposit interest earned by corporations and foreign governments. Consequently, only reporting on individual owners of bank deposits is currently required.

Revenue Procedure (Rev. Proc.) 2012-24 was issued simultaneously with the final deposit interest reporting regulations. Rev. Proc. 2012-24 provides a list of countries with which the United States has in effect an exchange of information agreement, either as part of an income tax treaty or as a separate agreement. Financial institutions that maintain deposits of customers who are resident in those countries will be required to report the interest earned by those deposits to the IRS on Form 1042-S for interest paid on those deposits beginning on 1 January 2013. Rev. Proc. 2012-24 also lists countries with which the United States automatically exchanges information. At present, automatic information exchanges occur only with Canada. Presumably, the five EU countries that joined in the Joint Statement will be added in the near future once those IGAs enter into legal effect.

The issuance of the final deposit interest reporting regulations is a necessary (but insufficient) step in FATCA implementation because of the promise by the United States to reciprocate in exchanging information on US accounts owned by FATCA partner country residents under the...
Joint Statement. Information exchanged on deposit interest may not be sufficient because FATCA applies to a broader range of income, requires identification of US owners of corporations, and the account balance. It is not clear how much reciprocity will be required by FATCA partners. However, reciprocity may not mean an equal amount of exchange between the United States and its FATCA partners because item-by-item information sharing will not necessarily be required.

The preamble to the final deposit interest reporting regulations addresses the major issues raised by commentators who object to the reporting of deposit interest. Although it is clear that business concerns are paramount to US banks, particularly those banks located in border regions, the commentators expressed concerns about the confidentiality and protection of the information and the use of the information for non-tax purposes. These concerns from various banking trade groups caused the 2001 deposit interest reporting regulations that would have applied to all non-resident aliens to be withdrawn and replaced by a proposal in 2002 that would have required reporting on residents of 16 designated countries or, at the option of the reporting entity, on all non-resident aliens.

In a lengthy discussion, the Treasury Department responded that automatic information exchanges would occur only with countries with which the United States has an information exchange agreement, if certain legal safeguards and other protections are provided, and then only if the country imposes tax on the interest when paid to its residents. The reassurance concerning legal safeguards and other protections was necessary given the political pressure from the border state banks and their elected representatives. However, it is not clear how the Treasury Department will be able to meet its reciprocal exchange of information obligations under IGAs if it is concerned about the protection of the information being exchanged.

Despite the reassurance provided by the Treasury Department in the preamble to the bank deposit interest reporting regulations, the Florida Bankers Association and the Texas Bankers Association filed a complaint for declaratory and injunctive relief on 18 April 2013 in the US District Court for the District of Columbia. The complaint seeks a declaratory judgment finding that the amendments to section 1.6049-4(b)(5) of the IRC and Treasury Regulation 1.6049-8 were promulgated in violation of the Administrative Procedures Act and the Regulatory Flexibility Act and an order staying the enforcement date of the amendments. On 22 July 2013, the US government filed its answer, claiming, among other defenses, that the plaintiffs lack standing to pursue their claims and that their claims are barred by the Anti-Injunction Act.

3.5.6.3. Future US information collection

Under the reciprocal version of the Model 1 IGA, the United States has agreed to collect and exchange information about IGA partner residents similar to the information that FATCA requires IGA partner FFIs to collect and exchange. The first step toward such US information collection on non-residents with US accounts was contained in the Fiscal Year 2014 Budget of the US Government. The line item merely provides for the reciprocal reporting of information in connection with the implementation of FATCA. No revenue numbers are attached to the provision. In addition to the information already collected, FATCA-like information collection would also require reporting of account balances and gross proceeds from the sale or disposition of securities. Reciprocal information reporting would also require determining the sub-

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105. The preamble to the final deposit interest reporting regulations expressly notes that the regulations will "facilitate intergovernmental cooperation on FATCA implementation by better enabling the IRS, in appropriate circumstances, to reciprocate by exchanging information with foreign governments for tax administration purposes." Guidance on Reporting Interest Paid to Non-resident Aliens, 77 Fed. Reg. 23,391, 23,392 (19 Apr. 2012).


108. See Guidance on Reporting of Deposit Interest Paid to Non-resident Aliens, 67 Fed. Reg. 50,386 (proposed 2 Aug. 2002). The 2002 proposed regulations were never finalized and were withdrawn by the 2011 proposed regulations, which proposed to reinstate reporting on all non-resident aliens. See Guidance on Reporting Interest Paid to Non-resident Aliens, 76 Fed. Reg. 1105 (proposed 7 Jan. 2011).
stantial IGA partner resident owners of an entity similar to the information required under FATCA. 114

4. “Classic” FATCA

4.1. Introductory remarks

Treasury Department and IRS officials refer to the final FATCA regulations as “classic” FATCA to distinguish the final regulations from the IGA rules, from which they may differ.

4.2. Risk-based approach

The preamble to the final regulations explains that the Treasury Department has applied a “risk-based” approach to the implementation of FATCA that effectively addresses policy considerations, eliminates unnecessary burdens and, to the extent possible, builds on existing practices and obligations. 115 This approach is implemented by expanding the scope of types of entities that are partially or wholly exempt from FATCA, the reduced requirements for due diligence on existing low value accounts, the extension of effective dates for grandfathering of certain types of transactions, the extension of effective dates for reporting and withholding, and the reliance on existing anti-money laundering “know your customer” (AML/KYC) procedures and documentation permitted by “classic” FATCA. 116 The Treasury Department responded to the many meetings and hundreds of detailed comment letters on the proposed regulations from the affected industries 117 in drafting the final regulations. Commentators requested detailed rules, and the Treasury Department complied with 543 pages of detailed procedures and rules.

In adopting a risk-based approach and broadening the scope of certain provisions, delaying the effective dates, and permitting the use of AML/KYC procedures and documentation, the Treasury Department exercised the broad regulatory authority granted to it to promulgate regulations that it considers necessary or appropriate to carry out the statute’s purposes and to prevent avoidance of the statute’s provisions. 118

4.3. Delayed implementation dates

The most common request from the almost 300 commentators on the proposed regulations was to delay the effective dates, so that FFIs would have more time to prepare for FATCA implementation. 119 The Treasury Department responded in the final regulations by:

- phasing in completion dates for identification of an FFI’s existing account holders; 120
- expanding the scope of existing accounts to accounts opened prior to 1 January 2014; 121
- delaying initial reporting on US account holders to March 2015; and
- delaying withholding until 1 January 2014, 122 except for gross proceeds (delayed until 1 January 2017). 123

As discussed above, the implementation dates generally were further delayed until 1 July 2014 by Notice 2013-43. Notice 2013-43, however, does not delay the implementation dates for withholding on foreign pass-thru payments and some other types of payments (1 January 2017).

Significantly, one of the most far-reaching provisions of FATCA, withholding on “foreign passthruth payments,”124 has been suspended at least until 1 January 2017, which is two and a half years after the general effective date for withholding by US withholding agents. 125 The Treasury Department reserved comment on the definition of the term “foreign pass thru payment,” but the concept is an anti-abuse rule that is designed to prevent a non-participating FFI from avoiding compliance with the FATCA rules by receiving payments through a participating FFI. 126 In other words, the “foreign pass thru payment” means that there will be withholding on a foreign-to-foreign payment, so that an FFI cannot avoid FATCA by investing in US capital markets through a participating FFI.

Earlier guidance had proposed that a portion of a payment from a participating FFI to a non-participating FFI, based upon a ratio of the participating FFI’s US assets over its worldwide assets, be subject to 30% withholding. 127 However, in the preamble to the proposed FATCA regulations, the Treasury Department first announced that withholding on foreign pass thru payments would be delayed until at least 1 January 2017, because of the numerous comments expressing concern about the costs, administrative complexity, and legal impediments associated with identifying and withholding on pass thru payments. 128 The Treasury Department further explained that the comments indicated that without additional time to work through these issues, it would be impossible for many FFIs to commit to fulfill their obligations under chapter 4. 129

114. Treas. Reg. 1.1471-1(i)(2) requires withholding agents to report of US. substantial IGA partner resident owners of an entity similar to the information required under FATCA.
115. Regulations on Certain Payments, supra n. 22, at 5876.
116. Id., at 5890.
118. Sec. 1474(f) IRC.
119. The delayed implementation dates were announced in response to multiple uniform comments that more time was required to implement FATCA. See Announcement 2012-42, 2012-47 I.R.B. 561 (published 19 Nov. 2012).
120. For pre-existing individual accounts, see Treas. Reg. 1.1471-1(f)(3). For pre-existing entity accounts, see Treas. Reg. 1.1471-4(c)(3)(ii).
121. Treas. Reg. 1.1471-1(b)(95)-(98).
124. Sec. 1471(d)(7) IRC.
125. Regulations on Certain Payments, supra n. 22, at 5944.
126. IRS. Notice 2010-60 at 54-55
129. Id.
4.4. Withholdable payment

The trigger for the application of FATCA is the payment of a withholding payment by a US withholding agent to a foreign entity.130 The term “withholdable payment” means:

- US-source fixed determinable annual periodic income, commonly referred to as “FDAP”, which is currently subject to US withholding tax when paid to a foreign person; and
- the gross proceeds from the sale of any property of a type that can produce US-source interest or dividend income.131

The latter category generally is capital gain income that is not subject to US tax when paid to a foreign person.132 Not only would FATCA potentially impose withholding tax on such capital gain income when paid to an FFI, but FATCA would also impose withholding tax on the gross proceeds with no basis offset, thereby potentially subjecting return of capital to withholding tax.133 For FFIs which receive such income for their own account and which are located in a country with which the United States does not have a tax treaty in effect, no refunds are permitted.134 Consequently, in that case, the withholding tax is a final tax.

4.5. Scope of FFI definition

4.5.1. Statutory FFIs

The statute only includes three categories of financial institutions:

- entities that accept deposits in the ordinary course of a banking or similar business;
- entities that, as a substantial portion of their business, hold financial assets for the accounts of others; and
- a broad category of entities that engage primarily in the business of investing, reinvesting, or trading in securities, partnership interests, commodities, or other interests such as futures or forward contracts or options.135

Additionally, the statute provides a category of “deemed-compliant” FFIs136 and a category of financial institutions that pose a low risk of tax evasion (foreign governments and international organizations) and are thus not subject to withholding under section 1471(a) of the IRC.137

4.5.2. Regulatory FFIs

The final regulations expand the scope of the definition of an FFI by adding two additional categories:

- a “specified” insurance company; and
- a holding company or treasury centre that is a member of an expanded affiliated group that includes an FFI or is used to avoid compliance with FATCA.138

The scope of the FFI definition was expanded to include other FFIs that would potentially be a safe haven for unreported accounts if not included. For example, if foreign life insurance companies that issue cash value and annuity contracts were not included, US persons could move their financial assets from banks to such foreign insurance companies.

A “specified” insurance company is an insurance company or a holding company with an insurance company member in its group that issues or makes payments on cash value insurance or annuity contracts.139 The regulations provide a definition of a “cash value insurance contract” that generally excludes property and casualty and reinsurance contracts, as well as term life insurance contracts.140 Consequently, a “specified” insurance company generally will be limited to a life insurance company.

While an insurance company was not identified as a financial institution by the statute, the Joint Committee on Taxation Staff Explanation had suggested that special rules would need to be provided for certain insurance companies.141 Moreover, section II.B.2 of Notice 2010-60 explained that the definition in section 1471(d)(5) of the IRC is broad enough to cover certain insurance companies, noting the broad grant of regulatory authority to determine the scope of the term FFI.

The final FFI category is a holding company or a treasury centre that is a member of an affiliated group of companies that includes another type of financial institution or is formed by, or availed of by, a collective investment fund or other enumerated fund to invest, reinvest or trade in financial assets.142 This definition provides an exception for holding companies and treasury centres that are members of an affiliated group that does not include a financial institution. The preamble to the final regulations notes and explains that the rules are designed as anti-abuse rules to prevent financial affiliated groups from using holding companies and treasury centres to shield payments made to non-participating FFIs or limited FFIs.143

4.5.3. Deemed-compliant FFI

Another example of the risk-based approach taken by the Treasury is the expansion of the deemed-compliant FFI (DCFFI) categories. These categories recognize certain types of entities that present a low risk of tax avoidance.

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130. Note that FATCA does not apply to a direct payment to an individual. Reporting and potential withholding is required under section 1441 of the IRC when a US-source payment is made to a foreign person and reporting and potential backup withholding applies to payments made to US persons under chapter 61 and section 3406 of the IRC.
131. Sec. 1473(a) IRC.
132. Sec. 871(a) (2013) and 881 IRC.
134. Sec. 1471(b)(1) IRC. Even if a refund is available to an FFI in a treaty country, the FFI must provide such information as required under regulations to claim such a refund and no interest is paid on the refund.
135. Sec. 1471(d)(5) IRC.
136. Sec. 1471(b)(2) IRC.
137. Sec. 1471(f) IRC.
139. Treas. Reg. 1.1471-5(c)(iv).
141. See Joint Comm. on Taxation, Technical Explanation of the Revenue Provisions Contained in Senate Amendment 3310, “the ‘Hiring Incentives to Restore Employment Act’, under Consideration by the Senate (JCX-4-10), at 43 (23 Feb 2010).
142. Treas. Reg. 1.1471-5(e)(v)(A), (B).
143. Regulations on Certain Payments, supra n. 22, at 5889.
based on their characteristics and their account holders. For example, an FFI that does business only in the country in which it is organized and does not market to non-residents of that country may qualify as a deemed-compliant “local FFI” because the local FFI does not solicit customers outside of its country of organization. It would not be soliciting US customers that are non-residents of that country. As a result, a DCFFI is subject to less stringent requirements than those imposed on an FFI.

The final regulations provide three categories of deemed-compliant FFIs:

- registered DCFFIs;
- certified DCFFIs; and
- owner-documented FFIs.

Each category contains further specific subcategories. Each subcategory provides specific requirements. For example, if an FFI meets those subcategory requirements, that FFI is treated as having met the withholding and reporting requirements of section 1471(b) of the IRC. Significantly, as a result, a DCFFI is not required to enter into an agreement with the IRS and is not subject to withholding on any withholdable payments made to it. A DCFFI, depending on which category applies, will have certain due diligence requirements with respect to its account holders.

4.6. Exempt beneficial owners

An exempt beneficial owner is a category of FFIs that are not subject to withholding. This category includes a foreign government, a political subdivision of a foreign government, an agency or instrumentality of a foreign government or one of its wholly owned subdivisions, an international organization or one of its wholly owned agencies or instrumentals, a foreign central bank of issue, any government of a US territory, certain retirement funds described in the FATCA regulations, or any person treated as such under an IGA.

An exempt beneficial owner, however, must certify to a withholding agent that it does qualify for that status by providing a withholding certificate (Form W-8EXP) or supporting documentation to the withholding agent. An international organization that is so designated by executive order under sections 288-288f of the US Code is not required to provide a withholding certificate if the international organization is not receiving the payment as an intermediary on behalf of another person.

4.7. Non-financial foreign entities

The other broad category of a foreign entity consists of non-financial foreign entities (NFFEs). An NFFE is simply defined as any foreign entity that is not an FFI or a foreign entity treated as an NFFE under an IGA. Although section 1472(a) of the IRC requires withholding on a withholdable payment to an NFFE unless the NFFE identifies its substantial US owners, most NFFEs will not be subject to withholding and the requirement to report any US owners. Withholdable payments made to an “excepted NFFE” are not subject to withholding.

An “excepted NFFE” includes:

- a publicly traded company the stock of which is regularly traded;
- subsidiaries of such a publicly traded company;
- entities organized in a US territory that are owned by bona fide residents of that US territory; and
- an “active” NFFE. An “active” NFFE is an NFFE that has gross income for the preceding taxable year which consists of less than 50% of passive income, i.e. dividends, interest, and other forms of investment income.

Notice 2013-69 announced that an active NFFE will also include under amended final regulations a “direct reporting NFFE” and a “sponsored direct reporting NFFE.” A “direct reporting NFFE” will register with the IRS and obtain a Global Intermediary Identification Number (GIIN) and will report any US substantial owners directly to the IRS instead of a withholding agent. A “sponsored direct reporting NFFE” will have a sponsor that will directly report any substantial US owners directly to the IRS.

The Notice explains that although a direct reporting NFFE will document itself to withholding agents and participating FFIs in a manner similar to a participating FFI, it will not be treated as a participating FFI and will not enter into an FFI agreement. Moreover, because the definition of a passive NFFE will be amended to exclude a direct reporting NFFE, an account held by a direct reporting NFFE will not be treated as a US account. Accordingly, a participating FFI with which the direct reporting NFFE has a financial account will not report that financial account to the IRS.

As a result of the exceptions, most NFFEs will not be subject to the FATCA provisions, other than the requirement to confirm excepted NFFE status to a withholding agent. However, as noted previously, most property and casualty (P&C) companies are treated as passive NFFEs subject to reporting of its substantial US owners to any withholding agents. However, the new categories
of direct reporting and sponsored direct reporting NFFEs will relieve such P&C insurance companies from potentially reporting their US owners to their customers if they make the election to be so treated.

4.8. Account identification – due diligence

An FFI is required to identify and report significant information about its US account holders, including the name of the account holder, address, taxpayer identification number, highest account balance during the year, the account number, and annual earnings.

For pre-existing accounts, this reporting requirement presented the most burdensome and costly requirement for FFIs. As the Treasury Department guidance evolved, the final regulations apply a risk-based approach under which an FFI may limit searches for indicia of a pre-existing account holder’s status as a US person to a one-time only search of its electronic files except for accounts in excess of USD 1 million. For accounts over USD 1 million, other records must be reviewed but limited to the prior five years. In addition, if there is a relationship manager, the relationship manager must be consulted.

A number of provisions that exclude certain low-value accounts from either the definition of a US account or from the pre-existing due diligence or account identification requirements reduce the burden and cost that would otherwise be imposed on FFIs to identify their US account holders. Depository accounts of USD 50,000 or less that are held by an individual are not included in the definition of the term “US account.” However, an FFI may disregard the exception and report the account. In addition to the statutory exception, the final regulations exclude from the definition of “cash value insurance contract” a cash value insurance contract of USD 50,000 or less. These exclusions mean that those accounts are not subject to FATCA, and no due diligence, documentation, withholding, or reporting of any US owners of such accounts is required.

In addition, the final regulations also exempt from review pre-existing entity accounts of USD 250,000 or less and cash value insurance contracts of USD 250,000 or less. All of these exclusions mean that the number of pre-existing accounts that are subject to review is greatly reduced, which, in turn, reduces the administrative burden and cost that otherwise would have been incurred by FFIs with respect to the excluded accounts.

For new accounts, i.e., those opened after 1 July 2014, the final regulations permit reliance on existing procedures and documentation that comply with AML/KYC rules. Documenting new accounts is not too burdensome because the required information can be gathered as part of the account opening procedures.

4.9. Recalcitrant account holder

The term “recalcitrant account holder” means an account holder of a participating FFI (PFFI) or a DCFFI that:

- does not provide identifying documentation;
- does not provide an effective waiver to foreign law that would otherwise prevent reporting on that account holder to the IRS; or
- provides passive NFFE documentation, but does not provide information about its owners.

A PFFI or DCFFI must withhold 30% on passtru payments made to such recalcitrant account holders. However, if the payment is a foreign passtru payment, no withholding is required prior to 1 January 2017.

4.10. Expanded affiliate group

The requirement that each member of an expanded affiliate group (EAG) must be a participating FFI or a DCFFI is problematic for multinational FFIs, which may have affiliates in jurisdictions where the affiliate is legally prohibited from complying with the FATCA collection of information and reporting requirements on pain of civil, regulatory, and possibly criminal sanctions. Without any relief from the rule, one EAG affiliate could prevent all of the other members of the EAG from becoming PFFIs, even if those other PFFIs could otherwise do so under local governing law.

The final regulations provide a transition rule, the “limited FFI rule,” to temporarily resolve this dilemma. While the existence of a “limited FFI” within an EAG will not prevent other members of the EAG from qualifying as a PFFI, the status will terminate after 31 December 2015. During this period, a “limited FFI” will need to become a DCFFI, enter into an FFI agreement or be a DCFFI under an IGA; otherwise all of the PFFI members of the EAG will become non-participating FFIs.

While a “limited FFI” will not cause other members of its EAG to become NPFFIs during the limited period until 1 January 2016, the “limited FFI” must register as a limited FFI, identify its account holders under the due diligence requirements, retain account documentation for six years, report on US accounts to the extent permitted under relevant law, agree to withhold any US accounts or NFFE accounts, and agree to identify itself as an NPFFI (thus being subject to withholding). Beginning 1 January
2016, a “limited FFI” that has not obtained PFFI status will lose its “limited FFI” status; consequently, each FFI member of its EAG will no longer be able to qualify as a PFFI. Therefore, withholding will apply to each withholdable payment made to an FFI in that EAG.

### 4.11. Implications for US non-financial companies

An important exception from FATCA is provided for certain payments for services, usually made in the ordinary course of business. This exception is not limited to non-financial companies. However, it is an important exception for non-financial companies because the exception, along with other payments not treated as withholdable payments, will exempt from FATCA most payments made by non-financial companies.

A US non-financial company is a FATCA withholding agent when it makes a cross-border payment to a foreign entity, which means that the company is subject to FATCA. However, certain payments, (excluded non-financial payments) are excluded from the definition of the term “withholdable payments” and not subject to the FATCA rules. These payments include typical accounts payable categories, such as payments for the use of property, office and equipment leases, software licences, transportation, freight, and interest on outstanding accounts payable arising from the acquisition of goods and services. Notably, however, a premium payment for an insurance contract, investment advisory fees, custodial fees, and bank or brokerage fees are expressly excluded from this exception, so that such payments are subject to FATCA even when paid by a US non-financial company.

Although excluded non-financial payments will be exempt from FATCA, such payments continue to be subject to the withholding and reporting requirements under section 1442 of the IRC, which require a US withholding agent when it makes a cross-border payment to a foreign entity, which means that the company is subject to FATCA. However, certain payments, (excluded non-financial payments) are excluded from the definition of the term “withholdable payments” and not subject to the FATCA rules. These payments include typical accounts payable categories, such as payments for the use of property, office and equipment leases, software licences, transportation, freight, and interest on outstanding accounts payable arising from the acquisition of goods and services. Notably, however, a premium payment for an insurance contract, investment advisory fees, custodial fees, and bank or brokerage fees are expressly excluded from this exception, so that such payments are subject to FATCA even when paid by a US non-financial company.

In addition to “excluded non-financial payments,” interest and original issue discount on short-term obligations (i.e. obligations with a term of 183 days or less) are not “withholdable payments.” This is an important exception for US multinational corporations that raise working capital through the issuance of short-term commercial paper to foreign persons in non-US financial markets. Also, payments consisting of effectively connected income are not considered withholdable payments, unless the income is exempt under an income tax permanent establishment provision.

The final category of excluded payments consists of gross proceeds from the sale of property that produces FDAP income that is excluded under one of the foregoing categories. Effectively connected income is generally US-source income that arises from the conduct of a US trade or business.

### 5. Implementation of FATCA

Although the final regulations have been promulgated and a number of IGAs have been signed or initialled, with others in various stages of negotiation, much remains to be accomplished before 1 July 2014. Additional substantive amendments, as well as conforming regulations to the other U.S. domestic and cross-border reporting and withholding provisions, are anticipated in early 2014. Moreover, regulations that address withholding on gross proceeds have not been issued to date, although proposed regulations are anticipated, as well as coordination regulations under chapters 3 and 61 of the IRC.

A draft FFI agreement that an FFI will be required to execute with the IRS was released on 29 October 2013. Notice 2013-69 confirmed that the draft FFI Agreement will be finalized by 31 December 2013, which according to the final regulations is the earliest date that FFI agreements will become effective for FFIs that have obtained a GIIN. Notice 2013-43, however, delayed the implementation dates and the assignment of GIINs by the IRS has been delayed until 2014. Originally, the final regulations announced that GIINs would be assigned beginning no later than 15 October 2013. Although some draft reporting forms W-8 were issued following the issuance of the proposed regulations, the changes made in the final regulations will necessitate new draft forms plus the reporting form to be used by FFIs to report US account holders to the IRS.

The operational side is being implemented by the IRS. Implementation of FATCA is a key priority of the IRS according to IRS officials. The FATCA portal or the electronic website for communications between the IRS and FFIs was to be available no later than 15 July 2013. However, Notice 2013-43 extended this date to 19 August 2013. The portal did open on 19 August 2013. Moreover, 25 April 2014 is the last day for an FFI to register with the IRS to be included on the list of FFIs to be published on 2 June 2014. On 18 September

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192. Sec. 864(c) IRC.
193. IRS Notice 2013-69, Section V.
194. Regulations on Certain Payments, supra n. 22, at 5881.
196. Regulations on Certain Payments, supra n. 22, at 5897.
198. Id.; at 5896.
199. Id.; at 5897.
2013, the IRS issued FATCA FAQs concerning the FATCA registration system and FAQs on Qualified Intermediaries, Withholding Foreign Partnerships, and WithholdingForeign Trusts. Since that time, the IRS has publicly said that it is ready to process large amounts of information. Furthermore, on 8 December 2013, IRS updated its FATCA Registration Online User Guide, correcting some reported problems and adding some enhancements.

6. Compliance and Enforcement

The IRS has made a serious commitment to the enforcement of FATCA. On the operational side, the Large Business and International (LB&I) Commissioner organized two new divisions: the Foreign Payments Office and the Office of International Data Management. Each of these divisions is headed by a director who reports either directly or indirectly to the LB&I Deputy Commissioner (International). The Office of the Associate Chief Counsel (International) created a new office that will be dedicated to FATCA and cross-border withholding issues. The establishment of the new LB&I division and the new office within Associate Chief Counsel (International) demonstrates the IRS’ commitment to the exchange of information program and the enforcement of FATCA.

7. Conclusions

FATCA has evolved from unilateral US legislation to a global cooperative agreement due to the need for exchange of tax information and transparency in tax matters. Although efforts to engage in the exchange of tax information had begun prior to the enactment of FATCA, it was the threat of 30% withholding from US-source investment income to FFIs that caused government officials of other countries to accelerate discussions and planning for an automatic tax information exchange between governments.

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