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From COKALA Tax Group
Extra eBulletin

FATCA: Steps you can take now to prepare operations for compliance with requirements of the Foreign Account Tax Compliance Act

In March of 2010, the HIRE Act (Hiring Incentives to Restore Employment Act of 2010 Pub.L. 111-147) added chapter 4 to Subtitle A of the Internal Revenue Code. Chapter 4, sections 1471 through 1474 of the tax code, enacted as the Foreign Account Tax Compliance Act (FATCA), imposes new information reporting requirements on foreign financial institutions with respect to U.S. accounts, and imposes new withholding, documentation and information reporting requirements on U.S. payers with respect to certain payments made to certain foreign entities.

The Act provides that the provisions of Chapter 4 are effective beginning in 2013. Because of the time needed for significant modifications to information management systems to facilitate compliance with FATCA requirements, the U.S. Department of Treasury determined that new tax regulations for FATCA would provide for a phased implementation of various FATCA provisions. In Notice 2011-53 issued several months ago, Treasury announced that certain FATCA obligations of foreign financial institutions will begin in 2013, while the section 1471(a) and 1472(a) FATCA withholding obligations of payers with respect to U.S.-source payments of fixed and determinable, annual or periodic payments (FDAP payments) will begin on January 1, 2014. For payments made on or after January 1, 2015, withholding will be required under section 1471(a) and section 1472(a) on all withholdable payments including both U.S.-source FDAP payments and gross proceeds described in section 1473(1)(A)(ii).

There are steps you can take now, which could help achieve a successful implementation of FATCA requirements.

“Accounts Payable” payers: Foreign financial institutions (FFIs) will probably not be carved out of AP payments as "exempt" from FATCA rules. More than likely, FFIs will subject to the 30% withholding required by FATCA on all payments of the types of U.S.-source income you now pay to them which are subject to the current 1042 process. Examples of such payments are: Interest; bank fees; loan guarantee payments; and even payments on notional principal contracts (swaps) and other hedges or derivatives, since we still do not see an exemption covering them. To avoid the withholding of 30% on these payments, the FFI payee will need to “register” with the IRS: to enter into an agreement with the IRS to identify in their records and disclose to the IRS their U.S. depositors, investors and shareholders. This registration process is now being hammered out within the IRS, and it would be wise to alert your FFI payees to the time lines outlined in Notice 2011-53, such as in an informational mailing to them. Inform them as to your expectations that they will be participating in registration with the IRS, and that you will be required to withhold if they chose not to participate, unless future IRS releases grant an exception.

To find these FFIs in your process:

1. Search for the term *bank* and other terms such as *securities*, *broker*, *insurance* and *reinsurance* (but focus only on life insurance) in as many languages as applicable in all of your payment systems. These are the obvious FFIs, where the rules will come into play earlier, with documentation required before year-end 2013 and withholding beginning in 2014.

2. Pay attention to ACH and other direct payment processes. When you search in your systems, you are looking for payments to banks and not to their account holders.
3. Talk to your Treasury group and solicit their help in location of current business with FFIs.
4. If you collect SIC or NAIC codes, sort and look for financial services. (We understand that these codes may also become part of any exemption process if one is introduced by the IRS, so you should look as to whether you have the codes and are tracking them for your payees.)
5. Although payers that are not U.S. financial entities have little reason to know when an FFI that they pay is a qualified intermediary (QI), for FATCA purposes this will be important information. Look for W-8IMY forms in your system and, where you find them, review the forms for FFI status, and add any FFIs to your mailing. Preserve all other W-8IMY information once you have found it, since those entities will also be target of new rules when the non-financial foreign entity (NFFE) rules are released later this year.

When the IRS releases proposed regulations, which we hope will be by the end of 2012, we will be able to identify further steps and plan to outline them in upcoming newsletters.

U.S. financial institutions: It is critical to note that the new FATCA requirements will have some form of due diligence component to them that in some ways may be like those now used to meet AML and "know your customer" requirements. Certification on a W-8 form may not be enough. You will need to incorporate everything you know about your payee. This is similar to the rules today in some regard, since currently if you have information in your files that contradicts what is provided on the W-8 certification, you have reason to doubt the form and must obtain additional documentation. FATCA brings a deeper dive into what you know. It may actually mean merging AML information with tax information to locate entities with U.S. owners. The steps identified at numbers 1 through 5 above are important for U.S. financial institutions, but add the following to the list:

1. Meet with those in your compliance and legal department who handle the AML compliance and know-your-customer rules. You will need to work together to begin to locate all foreign non-financial entities (NFFEs) with U.S. ownership that are not publicly traded. Many times for AML and other legal purposes, ownership of small foreign entities is disclosed and you know U.S. ownership. These entities need to be located. There will be due diligence on your part to use what information you have to locate and target NFFEs and FFIs subject to the FATCA rules.
2. Where you discover private foreign entities, a mailing should be made to them to alert them to the application of the new FATCA rules and remind them that if they are partnerships or trusts, the IRS has a program for them like the QI program that may include a FATCA solution. They should consider applying.
3. It may be hard to distinguish FFIs from NFFEs and the IRS is exploring many different solutions. New W-8 forms will be provided, but there may well be due diligence terms that go beyond the mere form solicitation. Learn what tools you have available, including whether you have SIC or NAIC codes in data. Many large institutions currently carry this information on all payees.
4. As instructed above, look for W-8IMYs for identify FFIs that are QIs and NQIs. All flow-through entities that are payees of U.S. financial institutions should have disclosed U.S. ownership as part of the W-8IMY process. Many will probably fall under the "possible" FFI category, and others will be NFFEs, but in either case, they will clearly be subject to the FATCA rules. If not an FFI, and not a withholding trust or a withholding partnership, they should be encouraged to become a withholding trust or withholding partnership as a

solution to this process. If an FFI then they should be made aware of the QI process if they are not already a QI.

As a Cokala subscriber, you have our support for questions about these and other tax information reporting and tax withholding issues. Please send your questions to clientservice@cokala.com.

Thank you for your business. It is a pleasure to serve you.

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