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Foreign Account Tax Compliance Act ("FATCA")



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Foreign Account Tax Compliance Act Overview

- On March 18, 2010, the Hiring Incentives to Restore Employment (“HIRE”) Act, P.L. 111-147 (the “HIRE Act”) was signed into law.
 - The HIRE Act included modified versions of the information reporting and withholding requirements of the Foreign Account Tax Compliance Act (“FATCA”), which was introduced in October 2009 by Senate Finance Committee Chairman Baucus (D-MT), Senate Finance Committee member John Kerry (D-MA), House Ways and Means Committee Chairman Rangel (D-NY), and House Ways and Means Select Revenue Subcommittee Chairman Richard Neal (D-MA).

Foreign Account Tax Compliance Act Overview

- In sum, FATCA provides for a new withholding and reporting regime that will:
 - Require foreign financial institutions (“FFIs”) to enter into an agreement with the IRS or face a 30% withholding tax on all “withholdable payments”; and
 - Require 30% withholding on certain payments to non-financial foreign entities (“NFFEs”)
- FATCA also contains provisions to:
 - Repeal the foreign-targeted exception to registered bond requirements;
 - Modify certain foreign trusts rules;
 - Require all individuals holding “specified foreign financial assets” to file a return with the IRS reporting such assets;
 - Require regular PFIC reporting; and
 - Source to the United States “any payment made pursuant to a notional principal contract that (directly or indirectly) is contingent upon, or determined by reference to, the payment of a dividend from sources within the United States” (e.g., substitute dividends and dividend equivalent payments)

Foreign Account Tax Compliance Act Overview

- The goal of the new information reporting and withholding regime is to provide information to the IRS identifying U.S. persons invested in non-U.S. bank or securities accounts.
 - The new provisions use U.S. source payments, and the ability of the United States to levy withholding tax on those payments, as leverage to require financial institutions to report on U.S. persons invested in non-U.S. accounts.

Foreign Account Tax Compliance Act Overview

- FATCA contains the framework for the new information reporting and withholding regime; Treasury and the IRS are now drafting more detailed guidance in accordance with the statutory framework
- Treasury and the IRS have received many comments on potential areas for FATCA guidance, particularly the new withholding and information reporting provisions applicable to foreign financial institutions.
 - On August 27, 2010, Treasury and the IRS released the first guidance on FATCA, Notice 2010-60.
 - On April 8, 2011, Treasury and the IRS released additional guidance in Notice 2011-34.

Foreign Account Tax Compliance Act Overview

- The new withholding and reporting regime generally applies to “withholdable payments” made to:
 - Foreign financial institutions (“FFIs”) and
 - Other non-financial foreign entities (“NFFEs”)
- A “withholdable payment” is defined as:
 - Any payment of interest (including any original issue discount), dividends, rents, salaries, wages, premiums, annuities, compensations, remunerations, emoluments, and other fixed or determinable annual or periodical gains, profits, and income, if such payment is from sources within the United States, and any gross proceeds from the sale of any property of a type which can produce interest or dividends from sources within the United States.

Foreign Account Tax Compliance Act Overview

- Withholdable payments will generally be subject to 30% withholding unless:
 - An FFI enters into an agreement with the IRS to identify and report on its U.S. accounts (or an exception applies)
 - A NFFE identifies substantial U.S. owners, certifies that it does not have substantial U.S. owners, or another exception applies
- The new regime applies to payments made after December 31, 2012.

Foreign Account Tax Compliance Act Overview - Refunds

- Amounts withheld on withholdable payments made to FFIs or NFFEs are refundable to the beneficial owner of such payments to the extent that such amounts would otherwise be refundable under the current nonresident withholding tax rules.
 - If the beneficial owner is an FFI, however, the FFI is only entitled to a credit or refund to the extent that it is entitled to a reduced rate of withholding under an applicable double income tax treaty, irrespective of whether the payment would not otherwise have been subject to U.S. withholding tax.
 - No interest is provided on refunds to FFIs.
- No credit or refund will be allowed to a beneficial owner that is an unless the owner provides U.S. Treasury with the information necessary to determine whether it is a "United States owned foreign entity" and identifies its "substantial United States owners."
 - For a corporation, "substantial United States owner" means 10% direct or indirect ownership by a specified U.S. person
 - For an investment vehicle, substantial United States owner means any ownership over 0%
- For non financial institution beneficial owners, interest will not be paid if refund is paid within 180 days after relevant return or refund claim is filed

“Foreign Financial Institution”

- A “financial institution” is defined in the new statute as any entity that, unless otherwise provided by the Secretary:
 - accepts deposits in the ordinary course of a banking or similar business;
 - holds financial assets for the account of others as a substantial portion of its business, or
 - is engaged (or holding itself out as being engaged) primarily in the business of investing, reinvesting, or trading in certain securities, partnership interests, commodities, or any interest in such items.
 - According to Notice 2010-60, the Treasury and IRS anticipate issuing regulations stating that whether an entity is engaged primarily in the business of investing, reinvesting, or trading in securities must be determined on the basis of all relevant facts and circumstances.
- A “foreign financial institution” is a financial institution that is a foreign entity.

“Foreign Financial Institution”

- Notice 2010-60 states that the Treasury and IRS intend to exclude certain entities from the definition of an FFI.
 - A foreign entity, the primary purpose of which is to act as a holding company for a subsidiary (or subsidiaries) that primarily engages in a trade or business other than that of a financial institution, will be excluded from the definition of an FFI, unless that holding company acts as an investment fund.
 - Foreign start-up companies investing capital in assets with the intent to operate a non-financial institution business will also be excluded from the definition of an FFI for the first 24 months after the entity's organization.
 - A foreign entity in the process of liquidating or reorganizing with the intent to continue or recommence operations as a non-financial institution may also be excluded from the definition of FFI if the entity was not a financial institution before its liquidation or reorganization.
 - Foreign entities primarily engaged in financing and hedging transactions with or for members of its expanded affiliated group that are not FFIs may also be excluded from the definition of FFI.
 - Certain investment entities with certain identified owners (such as a small family trust settled and funded by a single person) may also be exempted in future regulations if they meet certain requirements.

“Foreign Financial Institution” - Deemed Complaint

- Under the statute (section 1471(b)(2)), Treasury and the IRS may treat an FFI as meeting the information reporting and withholding requirements otherwise applicable to FFIs (a “deemed compliant FFI”) if the FFI:
 - Complies with procedures that Treasury/IRS may prescribe to ensure that the institution does not maintain U.S. accounts and meets other requirements as the Treasury/IRS may prescribe with respect to accounts of other FFIs maintained by the institution; or
 - Is a member of class of institutions with respect to which the Treasury/IRS determines the application of the new regime is not necessary to carry out the purposes of the new regime

“Foreign Financial Institution” - Deemed Complaint

- Notice 2011-34 states that a deemed-compliant FFI will be required to:
 - (1) apply for deemed-compliant status with the IRS;
 - (2) obtain an FFI identification number (FFI-EIN) from the IRS identifying it as a deemed-compliant FFI; and
 - (3) certify every three years to the IRS that it meets the requirements for such treatment.
- Notice 2011-34 states that certain local banks without operations outside their countries of organization and that do not solicit account holders outside their countries of organization may be treated as deemed complaint if certain requirements are met.

“Foreign Financial Institution” - Deemed Complaint

- Notice 2011-34 states that Treasury and the IRS intend to issue regulations under which each FFI in an “expanded affiliated group” will be treated as a deemed-compliant FFI under section 1471(b)(2)(A) if:
 - (1) each FFI in the expanded affiliated group is, under the laws of its country of organization, licensed and regulated as a bank or similar organization authorized to accept deposits in the ordinary course of its business and is not described in section 1471(d)(5)(C);
 - (2) all of the FFIs in the expanded affiliated group are organized in the same country;
 - (3) no FFI in the expanded affiliated group maintains operations outside the country of organization;
 - (4) no FFI in the expanded affiliated group solicits account holders outside its country of organization; and
 - (5) each FFI in the expanded affiliated group implements policies and procedures to ensure that it does not open or maintain accounts for non-residents, non-participating FFIs, or NFFEs (other than excepted NFFEs as defined in Notice 2010-60 that are organized and operating in the jurisdiction where all members of the expanded affiliated group are organized).

“Foreign Financial Institution” - Deemed Compliant Investment Vehicles

- Notice 2011-34 states that Treasury and the IRS intend to issue guidance under which certain collective investment vehicles and other investment funds would be treated as deemed-compliant under section 1471(b)(2)(A).
- Under this guidance, a fund will be deemed-compliant if it meets the following three requirements:
 - (1) all holders of record of direct interests in the fund (e.g., the holders of its units or global certificates) are participating FFIs or deemed-compliant FFIs holding on behalf of other investors, or entities described in section 1471(f);
 - (2) the fund prohibits the subscription for or acquisition of any interests in the fund by any person that is not a participating FFI, a deemed-compliant FFI, or an entity described in section 1471(f); and
 - (3) the fund certifies that any passthru payment percentages that it calculates and publishes will be done in accordance the applicable rules.

“Foreign Financial Institution” - Deemed Compliant Investment Vehicles

- In Notice 2011-34, Treasury and the IRS stated that they are considering under what circumstances certain foreign entities, all the interests in which are regularly traded on an established securities market (e.g., exchange-traded funds (ETFs)), could be deemed compliant under section 1471(b)(2)(A).
- Treasury and the IRS also stated that they continue to consider comments received regarding whether there may be a category of funds that may be treated as deemed-compliant because:
 - (i) all direct interest holders in the fund are participating FFIs, USFIs, deemed-compliant FFIs, entities described in section 1471(f), or non-participating FFIs acting as distributors;
 - (ii) distribution or similar agreements prohibit sales of interests to specified U.S. persons, NFFEs other than excepted NFFEs, and non-participating FFIs holding for their own account;
 - (iii) each distributor agrees to enforce the sales prohibitions described in (ii) above, and
 - (iv) the fund satisfies other requirements and meets other criteria relevant to the purposes of chapter 4.

“Foreign Financial Institution” - “Low Risk of Tax Evasion”

- The statute (section 1471(f)(4)) also provides Treasury with the authority to exempt FFIs posing a “low risk of tax evasion.”
- Notice 2010-60 states that non-U.S. retirement plans may technically be “financial institutions,” but that they pose a low risk of tax evasion and should be exempt from FATCA withholding.
 - Notice 2010-60 proposes that a retirement plan would be exempt from the definition of FFI if it qualifies as a retirement plan under local law, is sponsored by a non-U.S. employer, and does not allow U.S. participants or beneficiaries other than employees who worked in the country where the plan is established.
 - Notice 2011-34 states that Treasury and the IRS are still considering the many comments received regarding the types of foreign retirement plans that should be treated as posing a low risk of tax evasion under section 1471(f), and intend to provide further guidance on the types of foreign retirement plans that may qualify for such treatment.
 - In addition, Treasury and the IRS intend to provide further guidance on foreign retirement plans or retirement accounts that may be deemed compliant under section 1471(b)(2).

“Foreign Financial Institution” - Insurance Companies

- The JCT Technical Explanation to FATCA had suggested that special rules should apply to insurance companies: “It is anticipated that the Secretary may prescribe special rules addressing the circumstances in which certain categories of companies, such as certain insurance companies, are financial institutions, or the circumstances in which certain contracts or policies, for example annuity contracts or cash value life insurance contracts, are financial accounts or United States accounts for these purposes.”

“Foreign Financial Institution” - Insurance Companies

- Notice 2010-60 addresses whether insurance and reinsurance companies will be considered FFIs.
 - Because Treasury and the IRS “do not view the issuance of insurance or reinsurance contracts without cash value as implicating the concerns of [FATCA],” Treasury and the IRS plan to issue regulations treating entities whose business consists solely of issuing such contracts (e.g., most property and casualty insurance or reinsurance contracts or term life insurance contracts) as non-FFIs.
 - Notice 2010-60 states, however, that contracts that combine insurance protection with an investment component (such as cash value insurance contracts or annuity contracts) “may present the risk of U.S. tax evasion that [FATCA] is designed to prevent.”
 - The notice requested comments on how entities that issue those types of contracts should be treated under FATCA.

“Foreign Financial Institution” – U.S. Branches of FFIs

- Notice 2010-60 provides that U.S. branches of FFIs will be considered FFIs.
 - Will be subject to withholding on payments other than income effectively connected with their U.S. trades or businesses if they do not comply with the FFI Rules.
 - Treasury and the IRS are considering, however, allowing U.S. branches to elect to be treated as “U.S. Financial Institutions” (“USFIs”) with respect to payments for which they act as intermediaries.

“Foreign Financial Institution” – CFCs

- Notice 2010-60 also states that CFCs will not be exempt from the FFI regime because their current reporting requirements are “less stringent” than those that will be imposed under FATCA.
 - CFCs are not required to report on certain payments to domestic corporations
 - CFCs are generally not required to report on the U.S. owners of foreign entities for which they maintain accounts
 - No rules current require CFCs to obtain waivers from account holders (or, in the absence of a waiver, close the account) if reporting would otherwise be prohibited under foreign law
- Notice 2010-60 states, however, that there will be coordination with CFCs’ current Form 1099 obligations in order to avoid duplicative reporting.

“Foreign Financial Institution” – Territory-Organized FIs

- The statute states that, except as otherwise provided by the Treasury/IRS, financial institutions organized under the laws of a U.S. territory are not FFIs.
 - Notice 2010-60 states that “Treasury and the IRS intend to coordinate with the territorial governments in the course of provided guidance regarding the treatment of Territory-Organized FIs. In general, Treasury and the IRS do not intend to treat Territory-Organized FIs as FFIs. However, Treasury and the IRS believe that additional guidance is necessary to address the chapter 4 withholding obligations of Territory-Organized FIs and to address potential compliance concerns.”

FFI Agreement with IRS

- Withholding on payments made to FFIs will not be required if the financial institution enters into an agreement with the IRS to obtain, verify, and provide to the IRS information about U.S. accountholders.
- FATCA broadly outlines the requirements (see next slide) to be included in this agreement but leaves the Treasury and IRS to develop much of the substance of the agreement.

FFI Agreement with IRS

- FATCA provides that, in an agreement with the IRS, the FFI must agree to the following to avoid the new 30% withholding:
 - To obtain information from each holder of each account maintained by such institution “as is necessary” to determine which, if any, of such accounts are U.S. accounts;
 - To comply with such verification and due diligence procedures “as the [IRS] may require” with respect to the identification of U.S. accounts;
 - To comply “with requests by the [IRS] for additional information” with respect to any U.S. account maintained by such institution;
 - In any case in which any foreign law would (but for a specified waiver) prevent the reporting of certain required information, (i) attempt to obtain a valid and effective waiver of such law from each account holder of such account, and (ii) if a waiver is not obtained, close the account.

FFI Agreement with IRS

- In the case of any U.S. account maintained by such institution, the FFI must also agree to report on an annual basis (at such time and in such manner as the IRS may provide) certain information, including:
 - The name, address, and tax identification number (“TIN”) of each U.S. account holder;
 - In the case of any account holder which is a U.S.-owned foreign entity, the name address, and TIN of each “substantial U.S. owner of such entity;”
 - The account number;
 - The account balance or value (“determined at such time and in such manner as the [IRS] may provide”); and
 - The gross receipts and gross withdrawals or payments from the account (“determined for such period and in such manner as the [IRS] may provide”).

FFI Reporting Requirements

- The IRS will create a new form for the annual reporting of information about U.S. account holders and expects to require electronic filing of the form.

“U.S. Account”

- A “U.S. account” is defined as “any financial account which is held by one or more specified United States persons or United States owned foreign entities.”
 - A “specified United States person” includes any U.S. person (i.e., citizens, residents, green card holders, trusts, partnerships, estates)
 - Excludes publicly-traded corporations, government agencies/instrumentalities, certain tax-exempt institutions
 - A “U.S. owned foreign entity” is any foreign entity with one or more “substantial U.S. owner,” which generally includes:
 - Corporations, partnerships, or trusts where a specified U.S. person owns a greater than 10% interest (directly or indirectly)

“U.S. Account”

- Exceptions to definition of “U.S. account”:
 - Unless an FFI elects not to apply the exception, the term does not include any depository account maintained by an individual if the aggregate value of all depository accounts does not exceed \$50,000
 - Any financial account in an FFI if:
 - Such account is held by another financial institution that has entered into an agreement with the IRS; or
 - The holder of such account is otherwise subject to information reporting requirements that the Treasury determines would make the reporting duplicative

“Financial Account”

- A “financial account” means:
 - Any depository account;
 - Any custodial account;
 - Any equity or debt interest in such financial institution (other than interests which are regularly traded on an established securities market)

FFI Agreement with IRS Initial Guidance

- Notice 2010-60 and Notice 2011-34 address the agreement between the IRS and an FFI (“FFI Agreement”) in which the FFI agrees to undertake certain reporting, withholding, and due diligence responsibilities in order to avoid 30% withholding.
 - Under the FFI Agreement, FFIs will be required to undertake certain procedures to identify certain U.S. account holders. These procedures will distinguish between preexisting individual accounts and new individual accounts.

FFI Agreement with IRS

Initial Guidance on Preexisting Individual Accounts

- In response to comments, the preexisting account procedures described in Notice 2010-60 were modified in several respects by Notice 2011-34. The modified procedures are described in subsequent slides.
- For purposes of applying the procedures for preexisting accounts, the following rules apply:
 - A participating FFI may rely on documentation that is collected pursuant to the procedures or that is otherwise maintained in an account holder's files, unless it knows or has reason to know that such documentation is unreliable;
 - A participating FFI has maintained documentary evidence if the participating FFI retains either: (i) a copy of the documentary evidence or (ii) a record of the documentary evidence examined, including the type of document and the name of the employee that reviewed the documentary evidence;
 - A participating FFI has maintained a Form W-8BEN only if it maintains a copy of the form in its files;
 - For purposes of determining the balances or values (as relevant) of accounts in each of the below steps, an FFI will be required to treat as a single account all accounts maintained by the FFI or its affiliates that are associated with one another due to partial or complete common ownership of the accounts under the FFI's existing computerized information management, accounting, tax reporting, or other recordkeeping systems.

FFI Agreement with IRS

Initial Guidance on Preexisting Individual Accounts

- For preexisting individual accounts, the FFI must follow the following procedures:
 - Step 1 - All account holders already documented as U.S. persons for other tax purposes will be treated as specified U.S. persons, and those account holders' accounts will be treated as U.S. accounts.
 - Notwithstanding the foregoing, unless the FFI elects otherwise, an account is a non-U.S. account if: (i) the account is a depository account; (ii) each holder of such account is a natural person; and (iii) the balance or value of such account as of the end of the calendar year preceding the effective date of the FFI's FFI Agreement does not exceed \$50,000 (or the equivalent in foreign currency).
 - Step 2 – From those accounts not identified as U.S. accounts in Step 1, the FFI may treat an account as a non-U.S. account if the balance or value of the account as of the end of the calendar year preceding the effective date of the FFI's FFI Agreement does not exceed \$50,000 (or the equivalent in foreign currency).
 - An FFI may elect not to apply Step 2.

FFI Agreement with IRS

Initial Guidance on Preexisting Individual Accounts – Private Banking

- Step 3 – Private Banking Accounts
 - Notice 2011-34 added new detailed procedures for private banking accounts.
 - The procedures should be of particular interest to insurance companies. Notice 2011-34 states: “Treasury and the IRS are considering whether other FFIs should apply analogous procedures to certain classes of accounts they maintain. Accordingly, Treasury and the IRS seek comments concerning whether other FFIs, and in particular insurance companies, should perform procedures similar to those described above with respect to holders of preexisting individual accounts, including private placement life insurance.”

FFI Agreement with IRS

Initial Guidance on Preexisting Individual Accounts – Private Banking

- Notice 2011-34 provides broad definitions of “private banking account,” “private banking department,” “private banking relationship,” and “private banking relationship manager.”
- A “private banking account” is generally one maintained or serviced by an FFI’s private banking department or any account maintained or serviced as part of a private banking relationship.
- A “private banking department” is any department, unit, division, or similar part of an FFI:
 - That is referred to by the FFI as a private banking, wealth management, or “similar department”;
 - That focuses on servicing accounts and investments of individual clients (or their families) whose accounts with the FFI or whose income, earnings, or assets exceed certain thresholds, or who are otherwise identified as high-net worth individuals (or families), as determined under an FFI’s own policies and procedures;
 - That is considered a private banking department under AML or KYC requirements to which the FFI is subject; or
 - In which some or all of its employees, under formal, informal, or other guidelines for personnel, (a) ordinarily provide personalized services to individual clients or their families, such as banking, investment advisory, trust and fiduciary, estate planning, philanthropic, or other services, or (b) gather information about individual clients’ personal, professional, and financial histories in addition to the information ordinarily gathered with respect to the FFI’s retail customers.

FFI Agreement with IRS Initial Guidance on Preexisting Individual Accounts – Private Banking

- A “private banking relationship” exists when an employee of the FFI is assigned by the FFI to provide the services described above.
- A “private banking relationship manager” is an officer or employee of the FFI assigned responsibility for specific account holders, advises account holders regarding their banking, investment, trust, estate, or philanthropic needs, and recommends, makes referrals to, or arranges for the provision of financial products, services, or other assistance to meet those needs.

FFI Agreement with IRS

Initial Guidance on Preexisting Individual Accounts – Private Banking

- Under the procedures for private banking accounts, the FFI must ensure that all of the FFI's private banking relationship managers:
 - (i) identify any client of the private banking relationship manager for which the private banking relationship manager has actual knowledge that the client is a U.S. person and request that each such client provide a Form W-9;
 - (ii) perform a diligent review of the paper and electronic account files and other records for each client with respect to whom they serve as a private banking relationship manager, and identify each client (including any associated family members) who, to the best of the knowledge of the private banking relationship manager, has:
 - (a) U.S. citizenship or lawful permanent resident (green card) status;
 - (b) a U.S. birthplace;
 - (c) a U.S. residence address or a U.S. correspondence address (including a U.S. P.O. box);
 - (d) standing instructions to transfer funds to an account maintained in the United States, or directions regularly received from a U.S. address;
 - (e) an "in care of" address or a "hold mail" address that is the sole address with respect to the client; or
 - (f) a power of attorney or signatory authority granted to a person with a U.S. address.

FFI Agreement with IRS

Initial Guidance on Preexisting Individual Accounts – Private Banking

- (ii) perform a diligent review of the paper and electronic account files and other records for each client with respect to whom they serve as a private banking relationship manager, and identify each client (including any associated family members) who, to the best of the knowledge of the private banking relationship manager, has:
 - (a) U.S. citizenship or lawful permanent resident (green card) status;
 - (b) a U.S. birthplace;
 - (c) a U.S. residence address or a U.S. correspondence address (including a U.S. P.O. box);
 - (d) standing instructions to transfer funds to an account maintained in the United States, or directions regularly received from a U.S. address;
 - (e) an “in care of” address or a “hold mail” address that is the sole address with respect to the client; or
 - (f) a power of attorney or signatory authority granted to a person with a U.S. address.

FFI Agreement with IRS

Initial Guidance on Preexisting Individual Accounts – Private Banking

- (iii) with respect to each client identified in the immediately preceding step:
 - request documentation to establish whether the client's account is a U.S. account, including a Form W-9 if the client is identified as a U.S. citizen or permanent resident
 - In the case of any client identified as having a U.S. birthplace or address, the private banking relationship manager must request that the client provide either a Form W-9 establishing U.S. status, or a Form W-8BEN (or a substitute certification as may be provided in future guidance) and a non-U.S. passport or other similar government-issued evidence establishing the client's citizenship in a country other than the United States.
 - In addition, to establish non-U.S. status in the case of any client identified as having a U.S. birthplace, the private banking relationship manager will be required to obtain from the client a written explanation regarding the client's renunciation of U.S. citizenship or reason that the client did not acquire U.S. citizenship at birth.
 - In the case of any client identified as having standing instructions or directions, the private banking relationship manager must request that the client provide a Form W-9 establishing U.S. status, or a Form W-8BEN and documentary evidence establishing non-U.S. status of the client.
 - In the case of any client identified as having only an "in care of" or "hold mail" address or a power of attorney in Step 3(A)(ii)(e) or (f), the private banking relationship manager must request that the client provide a Form W-9 establishing U.S. status, a Form W-8BEN, or documentary evidence establishing non-U.S. status.
 - request that any client providing a Form W-9 establishing U.S. status in response to a request also provide a waiver of applicable restrictions, if any, on reporting of the client's information to the IRS.

FFI Agreement with IRS

Initial Guidance on Preexisting Individual Accounts – Private Banking

- (iv) treat all accounts associated with a client as U.S. accounts if the client is identified as a U.S. person, or is identified as having U.S. indicia and does not establish non-U.S. status as described in Step 3(A)(iii)(a).
 - Notwithstanding the prior sentence, an account held solely by a family member of the client who provides a Form W-8BEN and documentary evidence establishing the non-U.S. status of the family member will not be treated as a U.S. account, unless the private banking relationship manager knows or has reason to know the family member is acting as a nominee or agent for the client
- (v) create and retain lists of all existing clients whose accounts are U.S. accounts, non-U.S. accounts, or recalcitrant accounts.

FFI Agreement with IRS Initial Guidance on Preexisting Individual Accounts – Private Banking

- The FFI must complete the private banking procedures described above by the first year in which its FFI Agreement is in effect.
 - If a private banking relationship manager subsequently becomes aware that an account holder of a preexisting private banking account has any of the U.S. indicia described above, the private banking relationship manager must request the documentation described above, and, if the account holder does not establish non-U.S. status within one year of the date on which the private banking relationship manager discovers the U.S. indicia, include the account in the FFI's reporting of its U.S. accounts or treat the account as a recalcitrant account.

FFI Agreement with IRS

Initial Guidance on Preexisting Individual Accounts

- Step 4 - For those accounts not covered by the preceding steps, the FFI shall determine whether the electronically searchable information maintained by the FFI and associated with those accounts or account holders includes any of the following U.S. indicia:
 - (i) identification of an account holder as a U.S. resident or U.S. citizen;
 - (ii) a U.S. place of birth for an account holder;
 - (iii) a U.S. residence address or a U.S. correspondence address (including a U.S. P.O. box);
 - (iv) standing instructions to transfer funds to an account maintained in the United States;
 - (v) an “in care of” address or a “hold mail” address that is the sole address shown in the FFI’s electronically searchable information for the accountholder; or
 - (vi) a power of attorney or signatory authority granted to a person with a U.S address.

FFI Agreement with IRS

Initial Guidance on Preexisting Individual Accounts

- For all accounts identified as containing U.S. indicia, the FFI will be required within one year of the effective date of the FFI's FFI Agreement to request certain documentation to establish whether the account is a U.S. account.
 - If U.S. resident or citizen, the FFI shall request a Form W-9.
 - If U.S. birthplace or address, the FFI shall request either a Form W-9 establishing U.S. status, or a Form W-8BEN *and* a non-U.S. passport or other government-issued evidence of citizenship in a country other than the United States.
 - In addition, to establish non-U.S. status in the case of any account holder identified as having a U.S. birthplace, the account holder will be required to provide a written explanation regarding the account holder's renunciation of U.S. citizenship or reason that the account holder did not acquire U.S. citizenship at birth.
 - If standing instructions, the FFI shall request either a Form W-9 establishing U.S. status, or a Form W-8BEN (or a substitute certification as may be provided in future guidance) *and* documentary evidence establishing non-U.S. status.
 - If "in care of" or "hold mail" address or a power of attorney, the FFI shall request a Form W-9 establishing U.S. status, a Form W-8BEN, *or* documentary evidence establishing non-U.S. status.
- Account holders that have not provided appropriate documentation within two years of the effective date of the FFI's FFI Agreement will be classified as recalcitrant account holders from that date until the date on which appropriate documentation is received from the account holder by the participating FFI.

FFI Agreement with IRS

Initial Guidance on Preexisting Individual Accounts

- Step 5 - For all preexisting individual accounts that are not identified as U.S. accounts in Step 1, as non-U.S. accounts in Step 2, as private banking accounts in Step 3, or as accounts with U.S. indicia in Step 4, and that had a balance or value of \$500,000 or more at the end of the year preceding the effective date of the FFI's FFI Agreement ("high value accounts"), the FFI must perform a diligent review of the account files associated with the account.
 - To the extent that the account files contain any of the U.S. indicia described above, the FFI must obtain the appropriate documentation within two years of the effective date of the FFI's FFI Agreement or the account holder will be treated as recalcitrant.

FFI Agreement with IRS

Initial Guidance on Preexisting Individual Accounts

- Step 6 – Annual Retesting
 - Beginning in the third year following the effective date of the FFI Agreement, the FFI will be required to apply Step 5 annually to all preexisting individual accounts that did not previously satisfy the account balance or value threshold and other requirements to be treated as high value accounts, but that would be high value accounts under Step 5 if the account balance or value of the account were tested on the last day of the preceding year.
 - From among the accounts identified each year under this test, the FFI will be required to treat as recalcitrant any account for which the required documentation has not been provided by the end of the year.

FFI Agreement with IRS

Initial Guidance on Preexisting Individual Accounts

- Required Chief Compliance Officer Certification
 - The chief compliance officer or another equivalent-level officer of the FFI (“responsible officer”) must certify to the IRS when the FFI has completed the above procedures for its preexisting individual accounts.
 - The responsible officer will certify to the FFI’s completion of Steps 1 through 3 within one year after the effective date of the FFI’s FFI Agreement, and will certify to the FFI’s completion of Step 4 and Step 5 within two years after the effective date of the FFI’s FFI Agreement.
 - As part of these certifications, the responsible officer will be required to certify that, between April 8, 2011 (the publication date of Notice 2011-34) and the effective date of the FFI’s FFI Agreement, FFI management personnel did not engage in any activity, or have any formal or informal policies and procedures in place, directing, encouraging, or assisting account holders with respect to strategies for avoiding identification of their accounts as U.S. accounts under the procedures described above.
 - The responsible officer will further be required to certify that the FFI had written policies and procedures in place as of the effective date of the FFI’s FFI Agreement prohibiting its employees from advising U.S. account holders on how to avoid having their U.S. accounts identified.

FFI Agreement with IRS

Initial Guidance on New Individual Accounts

- Notice 2010-60 provided initial guidance on the procedures that FFIs must follow to identify and report their U.S. accounts.
 - Notice 2011-34 did not amend this initial guidance, but did provide definitions of many terms used in Notice 2010-60. Further, Notice 2011-34 amended the preexisting account procedures, many of which were similar to the new account procedures in Notice 2010-60.
 - As a result, it is likely that the new account procedures described in Notice 2010-60 will be amended to reflect the new definitions and changes to the preexisting account procedures.

FFI Agreement with IRS

Initial Guidance on New Individual Accounts

- Notice 2010-60 provided that, for new individual accounts, the FFI may treat a depository account as other than a U.S. account if the account balance did not exceed \$50,000.
 - For the remaining accounts, account holders already documented as U.S. persons would be treated as U.S. account holders.
 - Notice 2010-34 reverses these procedures for preexisting accounts, providing that all accounts documented as U.S. accounts are treated as U.S. persons, unless the account balance meets the \$50,000 depository account test. Then, from the accounts not identified as U.S. accounts, the FFI may treat an account as a non-U.S. account if the account balance does not exceed \$50,000.
 - Several institutions had remarked in comments that the \$50,000 exception had little practical application because of limitations in FFI information technology systems.

FFI Agreement with IRS

Initial Guidance on New Individual Accounts

- For those accounts not covered by the preceding steps, Notice 2010-60 provided that an FFI will be required to obtain and examine documentary evidence establishing U.S. or non-U.S. status.
- Notice 2011-34 defines “documentary evidence” as including:
 - (i) documentary evidence sufficient to establish the identity of an individual and the status of that person as a non-U.S. person (consistent with the documentary evidence that may be relied upon pursuant to §1.6049-5(c)(1)), which may include, but is not limited to, photo identification described in §1.1441-6(c)(4));
 - (ii) any valid document issued by an authorized governmental body that includes the individual's name and address and is typically used for identification purposes; and
 - (iii) with respect to an account maintained in a jurisdiction with AML/KYC rules that have been approved by the IRS in connection with a QI agreement (as referenced in §1.1441-1(e)(5)(iii)), any of the documents (other than a Form W-8) referenced in the jurisdiction's attachment for identifying natural persons, as shown on the IRS's webpage.
- In Notice 2010-60, because there was no definition of “documentary evidence,” it was unclear whether this step required an FFI to gather information above and beyond what it was currently collecting.

FFI Agreement with IRS

Initial Guidance on New Individual Accounts

- “Documentary evidence establishing non-U.S. status” is defined in Notice 2010-34 as meaning documentary evidence that includes the account holder’s name and indicates citizenship or residence outside the United States.
 - In Notice 2010-60, because there was no definition of “documentary evidence,” it was unclear whether this step required an FFI to gather information above and beyond what it was currently collecting.
 - Because Notice 2010-60 provided that an FFI will be required to obtain and examine documentary evidence establishing U.S. or non-U.S. status and Notice 2011-34 defines documentary evidence establishing non-U.S. status, this step now appears to create an affirmative requirement to obtain information with name and showing citizenship or residence outside the United States.

FFI Agreement with IRS

Initial Guidance on New Individual Accounts

- Next, Notice 2010-60 provided that an FFI will examine all other information collected in connection with the new account to identify indicia of potential U.S. status (i.e., the indicia described earlier).
 - For accounts with indicia of potential U.S. status, the notice also provided that an FFI will be required to obtain certain documentation if such documentation has not already been collected, reviewed and maintained, or treat the account holder as a recalcitrant account holder.
 - In general, the documentation required to be obtained for new account holders in Notice 2010-60 was similar to the documentation required to be obtained for preexisting accounts (i.e., certain documentation was required depending on which indicia were present).
 - In some cases, Notice 2011-60 allowed an FFI to gather “documentary evidence establishing non-U.S. status” to essentially rebut the U.S. indicia. Given that, because Notice 2011-34 provides definitions, the earlier step of gathering documentary evidence now appears to affirmatively require the gathering of certain evidence establishing non-U.S. status, this step would appear in certain cases to be redundant unless it means that *additional* documentary evidence establishing non-U.S. status must be gathered.

FFI Agreement with IRS Initial Guidance on Identification of Non-Individual Accounts

- With respect to financial accounts held by persons other than individuals as of the date an FFI's FFI Agreement becomes effective, Notice 2010-60 provided that the FFI will be required to carry out certain procedures to determine whether such accounts should be treated as:
 - ❑ U.S. accounts;
 - ❑ accounts of participating FFIs;
 - ❑ accounts of deemed-compliant FFIs, accounts of non-participating FFIs;
 - ❑ accounts of entities described in section 1471(f); accounts of recalcitrant account holders;
 - ❑ accounts of excepted NFFEs;
 - ❑ accounts of other NFFEs; or
 - ❑ other accounts.

FFI Agreement with IRS

Initial Guidance on Identification of Entities

- Notice 2010-60 provided procedures under which FFIs must classify financial accounts held by persons other than individuals:
 - Treat all account holders already identified as U.S. persons for other U.S. tax purposes as U.S. persons;
 - Identify any entities for which information maintained by the participating FFI in its electronically searchable files indicates that the entity account holder is a U.S. entity (e.g., place of incorporation in the United States);
 - All account holders not classified as U.S. persons in the preceding steps will be presumed to be foreign entities.

FFI Agreement with IRS - Notice 2010-60

Initial Guidance on Identification of Entities

- From among entity account holders presumed to be foreign entities, the participating FFI will determine whether the entity's name (or other information readily available to the participating FFI in its electronically searchable files regarding the entity account holder) clearly indicates that the entity is an FFI.
 - If so, the participating FFI will tentatively classify the entity as an FFI.
 - The participating FFI will request that the entity provide the participating FFI with the entity's FFI EIN and certification of participating FFI status.
 - If the entity provides its FFI EIN and certification, it will be treated as a participating FFI.
 - If the entity does not provide a valid FFI EIN and certification of participating FFI status, the FFI will request further documentation.
 - An entity that does not provide such documentation will be treated as a non-participating FFI.

FFI Agreement with IRS - Notice 2010-60 Initial Guidance on Identification of Entities

- With respect to any entity account holder not treated as a U.S. person or FFI after applying the preceding steps, the participating FFI will examine the entity's account file for evidence that the entity is engaged in a (non-financial institution) active trade or business.
 - Evidence may include statements of business activities, persons employed in business activities, etc.
 - An entity account holder identified as engaged in an active trade or business will be treated as an excepted NFFE and an account of such an entity will be treated as other than a U.S. account.

FFI Agreement with IRS - Notice 2010-60

Initial Guidance on Identification of Entities

- Entities not classified by the preceding steps may present documentation showing or certifying that they are a participating FFI, a deemed-compliant FFI, a non-participating FFI, a NFFE, or that they are described in an exception under section 1471(f).
 - The participating FFI will be permitted to rely on existing documentary evidence in its account files for this purpose unless the participating FFI knows or has reason to know that the documentation is unreliable or incorrect.
 - If the documentation provided by the account holder indicates that the account holder is an NFFE, the participating FFI must either obtain documentary evidence (or rely on existing documentary evidence in its account files) that:
 - The NFFE is an excepted NFFE, or
 - The FFI must:
 - Specifically identify each individual, and each other specified U.S. person that has an interest in such entity, and
 - If a specified U.S. person is identified, treat the account as a U.S. account and obtain with respect to each such person the documentation that the participating FFI would be required to obtain from such person if such person were a new account holder and report any such specified U.S. person to the IRS.
 - If the participating FFI is unable to obtain the required documentation, the account holder will be treated as a recalcitrant account holder.

FFI Agreement with IRS - Notice 2010-60 Initial Guidance on Identification of Entities

- For new entity accounts, the participating FFI will be required to classify accounts by following procedures similar to the procedures with regard to preexisting accounts.
 - FFIs must determine how to treat such accounts using all information collected by the FFI (e.g., through AML/KYC rules) regardless of whether such information is available in electronically searchable files.

“Passthru Payments”

- An FFI is required to withhold 30% of any “passthru payment” made to a recalcitrant account holder or a non-compliant FFI (and on withholdable payments made to an FFI that makes an election to be withheld upon).
 - “Passthru payments” include withholdable payments or other payments “attributable to” a withholdable payment.

“Passthru Payments”

- Notice 2011-34 provides guidance regarding the definition of the term “passthru payment,” stating that Treasury and the IRS intend to issue regulations providing that a payment made by an FFI (the “payor FFI”) will be a passthru payment to the extent of:
 - the amount of the payment that is a withholdable payment; plus
 - (ii) the amount of the payment that is not a withholdable payment multiplied by
 - in the case of a custodial payment, the passthru payment percentage of the entity that issued the interest or instrument, or
 - in the case of any other payment, the passthru payment percentage of the payor FFI.

“Passthru Payments”

- An FFI’s “passthru payment percentage” will be determined by dividing the sum of the FFI’s U.S. assets by the sum of the FFI’s total assets.
 - These amounts will be required to be determined as of quarterly testing dates.
 - “Assets” are generally any asset includible on a balance sheet of the FFI prepared under the FFI’s method of accounting for reporting to interest holders, an off-balance sheet transactions or positions to the extent provided in future guidance.
 - Assets held in a custodial account of an FFI will not be considered assets of the FFI for purposes of computing its passthru payment percentage.
 - Notice 2011-34 states that Treasury and the IRS intend to publish regulations defining a U.S. asset to include any asset to the extent that it is of a type that could give rise to a passthru payment.
- Alternatively, an FFI may elect to compute its passthru payment percentage in the first year of its FFI agreement based on its assets on a single testing date.
 - For the quarterly testing dates falling in each of the first three complete quarters after the effective date of the FFI’s FFI Agreement, the FFI will determine its passthru payment percentage by dividing the sum of the FFI’s U.S. assets held on the Initial Testing Date and each of the quarterly testing dates by the sum of the FFI’s total assets held on the Initial Testing Date and each of the quarterly testing dates.

Grandfathered Obligations

- Section 501(d)(2) of the HIRE Act provides an exemption from the new withholding requirements for any obligation outstanding on March 18, 2012 (or the gross proceeds from any disposition of such an obligation).
 - In Notice 2010-60, the Treasury and IRS stated that they intend to define the term “obligation” for purposes of this exception as a legal agreement that produces or could produce withholdable amounts, but excluding equity or any legal agreement that lacks a definitive expiration or term.
 - As a result, savings or demand deposits would not qualify for the grandfathered obligations exception.
 - In addition, the Treasury and IRS also intend to issue regulations providing that any “material modification” of an obligation (which, for obligations constituting debt for U.S. tax purposes, will be defined as any significant modification under Treas. Reg. § 1.1001-3) will result in the obligation being treated as newly issued.
 - As a result, any significant modification after March 18, 2012 of an obligation treated as debt for U.S. tax purposes will cause the obligation to lose its grandfathered status.