

Internal Revenue Service Issues Guidance Extending FATCA's Effective Date and Details a Timeline for Implementation

On July 14, 2011, the Internal Revenue Service (IRS) announced rules in Notice 2011-53 (the Notice) that modify FATCA's January 1, 2013 statutory effective date, as a result of the comments submitted to the IRS and Treasury Department (Treasury) relating to the practical challenges of implementing FATCA by the statutory effective date.¹

The Notice provides a complex timeline that would phase in certain of the statutory and due diligence requirements described in Notices 2010-60 and 2011-34 over a period of time beyond what had previously been stated, provided that the foreign financial institution (FFI) enters into an FFI agreement by June 30, 2013.² The IRS anticipates that it will be ready to enter into FFI Agreements no later than January 1, 2013.

As a general matter, no FATCA withholding taxes will be imposed until January 1, 2014; thus, to the extent that an FFI has entered into an FFI agreement by June 30, 2013, it should not have any withholding taxes imposed on payments made to it. The IRS will provide that the effective date of any FFI Agreement entered into prior to July 1, 2013 will be July 1, 2013. The effective date of an FFI Agreement entered into after June 30, 2013 will be the actual date the FFI enters into the agreement.

The IRS acknowledged concerns that withholding tax may be imposed on payments made to FFIs that enter into agreements after

June 30, 2013, but before January 1, 2014. This could occur in the instance where a US withholding agent may not have sufficient time to identify whether the payee is a participating FFI.

Effective Date for New Account Due Diligence

An FFI that has entered into an FFI Agreement will be required to apply the rules in Notice 2010-60 relating to new accounts (i.e. identifying new US accounts) as of the effective date of its FFI Agreement with respect to accounts opened on or after the effective date of its FFI Agreement.

Effective Date for Preexisting Account Due Diligence

With respect to preexisting accounts, the IRS will require the FFI to implement the due diligence procedures identified in Notices 2011-34 and 2010-60 in several phases. First, within one year after the effective date of its FFI Agreement, an FFI will be obligated to conduct the due diligence applicable to private banking accounts that have a balance equal to or greater than \$500,000 as of the effective date of the FFI Agreement. Second, as of the later of December 31, 2014, or a date that is one year after the effective date of its FFI Agreement, an FFI will be obligated to conduct the due diligence applicable to private banking accounts that have a balance less than \$500,000. An FFI will be required to conduct the due

diligence required by Notices 2010-60 and 2011-34 (and pursuant to forthcoming regulations) for all remaining preexisting accounts within two years of the effective date of its FFI Agreement.

Information Reporting for 2013

Any account for which a participating FFI has received a Form W-9 by June 30, 2014, must be reported to the IRS by September 30, 2014. Generally, this should include private banking accounts identified under the timeline discussed above, any new US accounts opened after the effective date of the FFI Agreement and any accounts documented as US accounts under the procedures in Notice 2011-34 relating to low value accounts, accounts subject to an electronic search of US indicia, or accounts with balances that exceed \$500,000.

An FFI that does not undertake “1099 reporting,” would only be obligated to report under the procedures described in Notice 2011-34, but in the first year would only be obligated to report certain identifying information regarding the owner (e.g., name, address, US taxpayer identification number), the account balance as of December 31, 2013 (or balance as of date of account closure, if the account was closed prior to December 31, 2013) and the account number. Reporting for future years would be made pursuant to the rules as described in Notice 2011-34.

An FFI that undertakes 1099 reporting would be permitted to report the identifying information of the owner and the account number for its first report filed by September 30, 2014.

To the extent that an account holder has not provided a waiver to the FFI, that client would be considered recalcitrant and would be subject to reporting as such pursuant to Notice 2010-60 (and future guidance).

Post 2013 Information Reporting

Reporting for post-2013 years will occur pursuant to the guidance issued in Notice 2010-60, Notice 2011-34 and future guidance.

Withholding Taxes on Withholdable and Passthru Payments

For payments made on or after January 1, 2014, withholding agents (whether US or non-US, including participating FFIs) will be obligated to withhold tax under section 1471(a) for only US source payments of “FDAP” (generally dividends, interest, rents, royalties and other fixed or determinable annual or periodic income). For payments made on or after January 1, 2015, withholding agents will be obligated to withhold pursuant to section 1471(a) for all withholdable payments (including both US source payments of FDAP and gross proceeds from the sale or other disposition of any property of a type which can produce interest or dividends from sources within the United States).

Passthru payments made prior to January 1, 2015 are not subject to withholding by a participating FFI. Participating FFIs will not be required to compute or publish their passthru payment percentage until the first quarter of 2014.

Qualified Intermediary and Other Withholding Agreements

All Qualified Intermediary (QI) Agreements that are scheduled to expire on December 31, 2012 are to be extended through December 31, 2013. Any FFI that enters into an FFI Agreement on or before December 31, 2013, will be considered to have renewed its QI Agreement or other Withholding Agreement.

Substantive Guidance

The Notice also contains two items of substantive guidance. First, the Notice clarifies that future regulations will contain additional guidance regarding the due diligence procedures applicable to private banking accounts. In

particular, this future guidance will provide that for purposes of applying the due diligence procedures applicable to private banking accounts: (i) although client relationship managers will continue to be required to disclose any actual knowledge they may have regarding the account holder's status as a US person, the review of client files may be accomplished by any person designated by the FFI, and (ii) accounts subject to due diligence procedures and identified as either US or non-US accounts will not be subject to additional due diligence procedures in subsequent years, unless the account undergoes a change of circumstance.

The Notice also provides additional guidance relating to the grandfathered obligation rule and passthru payments. In particular, the Notice provides that an obligation that qualifies for the grandfathered obligation rule includes any legal agreement that produces or that could produce passthru payments (including withholdable payments) but not including any instrument that is treated as equity for US tax purposes, or any legal instrument that lacks a definitive expiration or term.

Timeline for Future Guidance

Treasury and the IRS anticipate issuing proposed FATCA regulations by December 31, 2011. After the notice and comment period relating to the proposed regulations, it is expected that final FATCA regulations will be issued during the summer of 2012. In conjunction with the regulations, Treasury and the IRS will issue draft and, subsequently, final versions of the FFI agreement and reporting forms for use by withholding agents and participating FFIs in the summer of 2012.

Endnotes

¹ The term "FATCA" is an acronym referring to the Foreign Account Tax Compliance Act of 2009, proposed legislation that was substantially incorporated into Subtitle A of Title V of the Hiring Incentives to Restore Employment Act of 2010 (HIRE Act), P.L. 111-147, enacted on March 18, 2010. The HIRE Act, imposed new information reporting and withholding tax rules contained in chapter 4 (i.e., sections 1471 through 1472 of the Internal Revenue Code (the Code)).

All references herein, unless specified, are to the Code of 1986, as amended, and the regulations thereunder.

² For more information please see our previous discussion of these requirements in US Treasury Department and Internal Revenue Service Issue Supplementary FATCA Guidance (April 28, 2011) available at <http://www.mayerbrown.com/publications/article.asp?id=10895&nid=6>, and US IRS Issues Preliminary FATCA Guidance Establishing Due Diligence Procedures and Information Reporting Rules for Foreign Financial Institutions (Sept. 16, 2010) <http://www.mayerbrown.com/publications/article.asp?id=9644&nid=6>.

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