Treasury Department Releases Intergovernmental FATCA Agreement

The United States Treasury Department (Treasury) recently issued an intergovernmental agreement (Model Agreement) under the Foreign Account Tax Compliance Act (FATCA). Congress enacted FATCA in 2010 to prevent tax evasion by US taxpayers with offshore accounts. The Treasury developed the Model Agreement in conjunction with the governments of France, Germany, Italy, Spain and the United Kingdom to resolve certain legal concerns that have been raised in connection with the FATCA compliance now required of certain non-US financial institutions and other non-US entities, including certain investment funds. A covered entity located in one of the above-listed jurisdictions (or in any other jurisdiction that may enter into a Model Agreement) that would otherwise be required by FATCA to report information to the US Internal Revenue Service (IRS) will, instead, once its own government signs the Model Agreement, comply by reporting to its government.

> The Model Agreement reflects the intent of the US and other countries to collaborate in the fight against tax evasion by providing for intergovernmental information sharing.

Under FATCA, foreign financial institutions (FFIs) face a 30 percent withholding tax on the receipt of certain payments unless they (1) identify and report certain information about their US accounts to the Treasury and (2) withhold on certain payments made to nonparticipating FFIs, i.e., FFIs that do not comply with FATCA, and recalcitrant account holders, i.e., account holders that do not furnish required information to the FFIs and that fail to provide waivers of foreign laws that would prevent such reporting. FFIs include banks, certain insurance companies and investment funds, and certain other entities that hold investments on behalf of others. Other non-US entities also covered by FATCA do not appear to be covered by the Model Agreement. (The FATCA provisions are described in more detail in our Client Alert, "IRS Issues Proposed FATCA Regulations," published on April 4, 2012.)

FATCA's reporting requirements have raised concerns because they conflict with the privacy laws in many countries that prohibit divulging customer information. The Model Agreement effectively resolves these concerns. In countries that enter into the Model Agreement (partner countries), covered FFIs would not be required to report information directly to the Treasury. Instead, such FFIs would report certain information to their own governments, which would automatically provide such information to the US pursuant to an existing tax treaty or tax information exchange agreement provision.

The Model Agreement covers (1) any FFI resident in a partner country but excludes any branches of such FFIs that are located outside the partner country and (2) any FFI branch that is located in a partner country even if the FFI is not a resident in the partner country. Thus, FFIs and FFI branches are covered under the Model Agreement based on their residence in a partner country. Covered FFIs can avoid the FATCA withholding tax by satisfying the reporting and other requirements under the Model Agreement, as described below. However, a covered FFI does not need to fulfill the requirements under the Model Agreement to avoid the FATCA withholding tax if the FFI is exempt from the FATCA withholding tax by virtue of qualifying as a "deemed-compliant FFI," "exempt beneficial owner" or "excepted FFI" under the relevant FATCA regulations.

Under the Model Agreement, covered FFIs will be treated as FATCA-compliant and will not be subject to the FATCA withholding tax if the FFI meets the following requirements:

- The FFI must identify and report to its government certain information about its US accounts. The due diligence requirements under the Model Agreement for identifying account holders are similar in many respects to those under FATCA. Both, for instance, distinguish between preexisting and existing accounts, and individual and entity accounts. The government of the partner country generally must provide the information to the US within nine months after the end of the calendar year to which the information relates, e.g., for information relating to 2013, the deadline is extended to September 30, 2015.

- The FFI must report to its government the name of, and aggregate amount of payments made in 2015 and 2016 to each account holder that is a nonparticipating FFI. As noted above, the due diligence requirements under the Model Agreement for identifying account holders are similar to those under FATCA.

- To the extent that the FFI acts as a qualified intermediary with primary withholding responsibility, a withholding foreign partnership, or a withholding foreign trust, the FFI must withhold 30 percent of any US-sourced withholdable payment made to an account holder that is a nonparticipating FFI. All other FFIs that make a payment of, or act as an intermediary with respect to, a US-sourced withholdable payment to an account holder that is a nonparticipating FFI must provide to any immediate payer of such payment the information required for withholding and reporting to occur with respect to such payment.

- The FFI must comply with certain registration requirements.

- If the FFI reports the required information, it will not be required to withhold on payments made to accounts held by recalcitrant account holders or to close such accounts.

The Treasury has released two versions of the Model Agreement—a reciprocal version and a nonreciprocal version. Both versions require a partner country to provide the US with information about US accounts held by FFIs. The reciprocal version goes a step further by containing a policy commitment to pursue regulations and legislation that would require it to provide partner countries with equivalent information about accounts held in US financial institutions by residents of partner countries. For the purposes of determining if a country is qualified to enter into a reciprocal Model Agreement, the Treasury has indicated that it will assess whether the country has sufficient protection in place to ensure that the information is kept confidential and used only for tax purposes.

For more information, please contact any member of our Tax Practice.

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