

FATCA: IRS Releases Draft of FFI Agreement and Regulatory Updates

The US Internal Revenue Service (IRS) has issued further guidance on the Foreign Account Tax Compliance Act (FATCA) in the form of Notice 2013-69 (the Notice). FATCA is designed to police offshore investments, accounts and trust interests held by certain US persons. FATCA generally aims to achieve this objective by, among other things, requiring certain foreign financial institutions (FFIs) to comply with the terms of a so-called FFI Agreement with the IRS pursuant to which FFIs must report information about their so-called US accounts. The Notice provides a long-awaited draft of the FFI Agreement and also describes certain forthcoming FATCA-related changes to the Treasury Regulations.

Overview

FATCA impacts both FFIs (including non-US banks and certain non-US investment funds) and non-financial foreign entities (NFFEs). Specifically, the final FATCA Treasury regulations require certain FFIs to register with the IRS and enter into an FFI Agreement to act as “participating FFIs” by (i) identifying their US accounts using established due diligence procedures, (ii) reporting information about their US accounts to the IRS and (iii) withholding tax on certain payments made to (a) FFIs that do not enter into an FFI Agreement (so-called nonparticipating FFIs) and (b) certain account holders that fail to submit information to the FFI or that fail to provide a waiver of any non-US law that would prevent FATCA reporting by the FFI with respect to such accounts (so-called recalcitrant account holders). The final regulations generally require NFFEs to provide withholding agents (generally persons that make certain US-source payments to such NFFEs) with certain information about their substantial US owners or to certify that they have no such owners. FFIs and NFFEs that fail to satisfy these requirements may be subject to a 30 percent US withholding tax on certain US-source payments made to them, beginning July 1, 2014.

The US Treasury Department also has issued two model intergovernmental agreements (Model 1 IGA and Model 2 IGA), which provide FFIs in jurisdictions that enter into such agreements with alternative approaches for complying with FATCA. FFIs covered by a Model 1 IGA (Model 1 FFIs) are required to register with the IRS, but are not required to enter into an FFI Agreement. Thus, such FFIs are not required to report information directly to the IRS. Instead, they must report information about their US accounts to their local governments, which, in turn, will relay the information to the IRS. In contrast, FFIs covered by a Model 2 IGA (Model 2 FFIs) are required to comply with the terms of an FFI Agreement as modified by the Model 2 IGA. Such FFIs are required to report information directly to the IRS, although such information may be supplemented by a government-to-government exchange of information upon request. Several jurisdictions have already entered into intergovernmental agreements, including France, Germany, Switzerland, the UK and the Cayman Islands.

Draft of the FFI Agreement

The Notice contains a draft of the FFI Agreement, which substantially incorporates the final regulations and the modifications applicable to Model 2 FFIs. The Treasury intends to finalize the

FFI Agreement by the end of the year. FFIs will be able to register with the IRS and enter into an FFI Agreement via the FATCA registration website (the portal) beginning January 1, 2014. FFIs that register by April 25, 2014 are guaranteed that they will not be subject to FATCA withholding when it goes into effect on July 1, 2014, provided they comply with any applicable procedural requirements (e.g., providing withholding certificates to withholding agents). FFI Agreements generally will expire on December 31, 2016, and participating FFIs will need to renew their agreements via the portal prior to that date.

Forthcoming Changes to Treasury Regulations

The Notice also lists several forthcoming FATCA-related regulatory changes. These changes include the following:

- Coordination between FATCA and IRS Form 1099 Reporting. A non-US payor that is a participating FFI (including a Model 2 FFI) or a Model 1 FFI generally will be treated as satisfying its IRS Form 1099 reporting requirements with respect to a US payee if it reports the payee as an account holder pursuant to its FFI Agreement or applicable Model 1 IGA. However, IRS Form 1099 reporting still will be required for any payment for which so-called backup withholding is required. (Backup withholding may apply where, among other things, the payee does not provide its tax identification number or, in the case of interest and dividends, the IRS instructs the payor to withhold.)
- Coordination Between FATCA Withholding and Backup Withholding. With respect to payments that are subject both to FATCA and backup withholding, participating FFIs (including Model 2 FFIs) may choose to (i) withhold on the payments under FATCA (in which case they will be deemed to have satisfied their backup withholding requirement), or (ii) with respect to accounts held by recalcitrant account holders that are known US persons, satisfy their FATCA withholding requirement by backup withholding at the applicable rate (currently 28 percent).
- Direct Reporting NFFEs. NFFEs may elect to be treated as so-called direct reporting NFFEs. Such NFFEs will not be required to reveal the identity of their substantial US owners to withholding agents under FATCA. Rather, direct reporting NFFEs will register with, and report information about their substantial US owners directly to the IRS.
- Reporting of Foreign Reportable Amounts Paid to Nonparticipating FFIs. Under the current version of the final regulations, participating FFIs are required to report so-called foreign reportable amounts (i.e., certain fixed, determinable, annual or periodical payments) paid to a nonparticipating FFI for calendar years 2015 and 2016, regardless of whether such amounts are associated with a financial account. The IRS intends to narrow these rules, by requiring participating FFIs to report only those amounts that are paid with respect to a nonparticipating FFI's financial account.
- Section 953(d) Insurance Companies. A non-US insurance company that makes an election pursuant to Section 953(d) of the Internal Revenue Code of 1986, as amended, is subject to US income tax as if it were a US insurance company. To simplify FATCA compliance, the Treasury intends to modify the final regulations to treat such a company as a US person for FATCA purposes as well (provided the company is not a so-called "specified insurance

company,” i.e., generally a company that issues, or is obligated to make payments with respect to, a cash value insurance or annuity contract). Accordingly, such companies would not be treated as FFIs or NFFEs and would not be subject to FATCA.

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