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FATCA – Should We Be Worried?

CRCA 2012 Conference

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Hyatt Regency

Trinidad

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Agenda

- **The Road to FATCA**
- **FATCA Highlights and Guidance to Date**
- **Alternative Regime to FATCA**
- **The Proposed FATCA Regulations**
- **Timelines**
- **Should We Be Worried?**
- **Q&A**



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FATCA: The Road to FATCA

The Problem: Insufficient Information Reporting/Disclosure

The U.S. federal income tax system relies on voluntary compliance by taxpayers in computing, reporting and remitting their tax liability each year

This process is augmented by third-party information reporting, enabling IRS verification of taxpayer compliance

U.S. Congress believes that taxpayers have achieved sophisticated means of investing offshore, making possible a way to avoid third-party reporting and U.S. taxation

It is estimated that this unchecked process causes tax evasion by U.S. persons in annual losses to the U.S. Treasury in billions of dollars annually

The Intended Solution: FATCA

The Foreign Account Tax Compliance Act was enacted on March 18, 2010.

FATCA introduces a new reporting regime aimed at the disclosure of U.S. persons with offshore accounts and investments.

This disclosure is accomplished by a new withholding regime (Chapter 4), that works in tandem with the current withholding regime (Chapter 3).

Chapter 4 imposes a penal withholding tax on withholdable payments made to foreign financial institutions and other foreign entities that fail to comply with the disclosure requirements.

FATCA highlights

- **The goals of FATCA are to identify U.S. persons and have their investment information provided to the Internal Revenue Service (IRS)**
- **Under FATCA, payments to Foreign Financial Institutions (FFIs) are potentially subject to punitive 30% withholding rate on the “withholdable payments”**
- **An FFI can avoid the punitive 30% withholding by entering into an agreement with the IRS and becoming a “Participating” Foreign Financial Institution’s (PFFI)**

FATCA highlights (continued)

- **The FFI Agreement will require the FFI to identify U.S. accounts and report them to the IRS annually**
- **FATCA will also requires punitive 30%withholding to withholdable payments made to nonfinancial foreign entities (NFFEs). An NFFE is any entity that is not an FFI. To avoid this withholding, the NFFE must:**
 - Provide a certification to the withholding agent that it does not have any U.S. substantial owners
 - Provide the name, address, and TIN of any U.S. substantial owners to the withholding agent
 - The withholding agent will then report to the IRS

FATCA – Fantasy vs. Reality

Fantasy

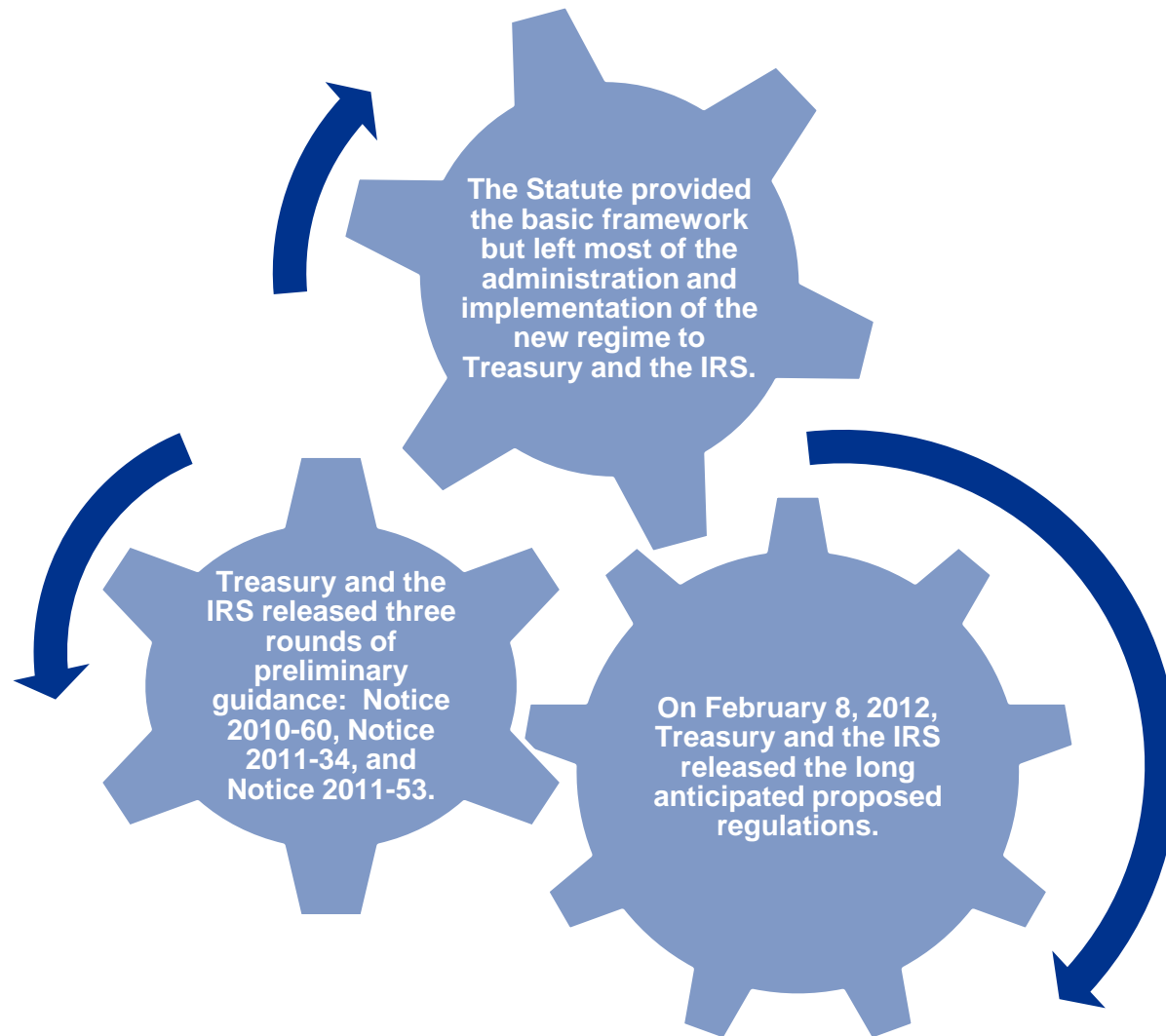
FATCA doesn't apply to us.
Only organizations with U.S. accounts are impacted.

Reality

FATCA will apply to any U.S. person/entity
that makes withholdable payments.

An FFI may have a customer base comprised
solely of non-U.S. individuals, but if it receives
and/or makes withholdable payments,
it will need to prove that these customers are not U.S.

Guidance To Date



FATCA – Fantasy vs. Reality

Fantasy

Since the rules aren't final, we can wait to address FATCA.

Reality

While it is true that the rules aren't final, your firm and KPMG understand it takes significant time to develop business requirements and build solutions.

It is critical to identify gaps between your firm's business processes and the proposed regulations and get to work on building solutions.

Alternative Regime to FATCA: Intergovernmental Approach

- U.S., France, Germany, Italy, Spain, UK issued joint statement
- Expressed support for FATCA goals but identified legal restrictions
- U.S. open to adopting intergovernmental approach to FATCA where:
 - Common approach reached between countries (FATCA partners)
 - FFIs would report FATCA information to their own country
 - FATCA partner would report the FATCA information to U.S.
 - U.S. commits to reciprocity in collecting & reporting to FATCA partner
 - Alternative regime based on automatic exchange authorized in existing bilateral tax treaties
- Where the U.S. & FATCA partner have entered into an agreement, FFIs would:
 - Not enter into FFI agreement with IRS
 - Report on U.S. accounts through their local government
 - Eliminate penal withholding requirement on recalcitrant account holders and FFIs in countries that have entered in an agreement with U.S.

Intergovernmental Approach: The Devil is in the Detail

- **At first glance, all affected parties like the Intergovernmental Approach as it appears to eliminate FATCA**
- **In a closer look, one realizes that may not be the case**
- **Camille Thommes, Director General of the Association of the Luxembourg Fund Industry, said the Joint Statement had introduced “some reliefs” but “in essence FATCA remains in place.”**
- **Mr. Thommes stated further: “It is important to stress that these are high level discussions between countries,” he added. “The devil is in the detail and we must look at the details of the agreements. In my opinion it would be a bit ambitious to say FATCA is off the table.”**

Source:

FT Adviser: “Ireland and Luxembourg support European FATCA deal”, February 17, 2012

FATCA – Fantasy vs. Reality

Fantasy

Our country intends to become a FATCA Partner in the new Intergovernmental Approach, therefore we do not need to be concerned about FATCA.

Reality

The length of time to create such an alternative regime is likely to be lengthy, and in the meantime, FATCA will become effective and FFIs will potentially be caught short.

In addition, compliance with many of FATCA's requirements will still be necessary by covered FFIs in either approach. All organizations must plan to deal with this complex set of compliance requirements.

Alternative Regime: Questions and Concerns

- **What about countries not in the named 5?**
- **Can a country that does not have a tax treaty with the US participate in this approach?**
- **What is the process to becoming a participating country?**
- **Would the IRS have the ability to seek additional information?**
- **How is it envisioned that a FFI would indicate it is participating in one vs the other regime under FATCA?**



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FATCA:

**The Proposed
Regulations**

Sections of the Proposed Regulations

- **Section 1471-1:** Scope of Chapter 4 of the IRC provisions & definitions
- **Section 1471-2:** Requirement to deduct and withhold tax on withholdable payments to certain FFIs
- **Section 1471-3:** Identification of payee
- **Section 1471-4:** FFI agreement
- **Section 1471-5:** U.S. accounts, financial accounts, U.S. owned foreign entity, FFI, FI, deemed-compliant FFIs, recalcitrant account holders, passthru payments
- **Section 1471-6:** Payments beneficially owned by exempt B/Os
- **Section 1472-1:** Withholding on NFFEs
- **Section 1473-1:** Withholdable payment, substantial U.S. owner, specified U.S. person, withholding agent
- **Section 1474-1:** Liability for withheld tax
- **Section 1474-2:** Adjustments for over/under withholding of tax
- **Section 1474-6:** Coordination of Chapter 4 of the IRC with other withholding provisions



Key FATCA Definitions and Notices

Withholdable Payment

Proposed Regulations - Section 1473(1)

- **Any payment of interest, dividends, rents, salaries, wages, premiums, annuities, compensations, remunerations, emoluments, and other fixed or determinable annual or periodical gains, profits, and income (FDAP income), if such payment is from sources within the United States;**

AND

- **Any 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**

Withholdable Payment Exclusions

Proposed Regulations - Section 1473-1(a)(4)

- **Certain short-term obligations: A payment of interest or original issue discount on short-term obligations**
- **Effectively connected income: Income is effectively connected with the conduct of a U.S. trade or business and is includible in the beneficial owner's gross income for the taxable year**
- **Ordinary course of business payments: Payments made in the ordinary course of business for nonfinancial services, goods, and the use of property**
 - Specifically: wages, office and equipment leases, software licenses, transportation, freight, gambling winnings, awards, prizes, scholarships, and interest on outstanding accounts payable arising from the acquisition of nonfinancial services, goods and other tangible property
- **Payments on obligations outstanding on 1st January 2013 are excluded from the definition of withholding payment and passthru payment**
- **Gross proceeds from sales of excluded property**

Definition: Foreign Financial Institution (FFI)

- **A financial institution is defined as any entity that meets at least one of the following:**
 - Accepts deposits in the ordinary course of business
 - Is in the business of holding financial assets for others
 - Is primarily engaged in the business of investing, reinvesting, or trading in securities, partnership interests, commodities, or any interest in such instruments

Deemed compliant FFIs

Proposed Regulations - Section 1471-5(f)

- **FFIs with relaxed requirements and are not required to enter into an FFI Agreement with the IRS**
- **Deemed compliant with the requirements and exempt from withholding**
- **Categories of deemed-compliant FFIs**
 - Registered deemed-compliant FFIs: Required to register with the IRS to declare status as deemed-compliant and to attest to the IRS that it satisfies certain procedural requirements.
 - Certified deemed-compliant FFIs: Not required to register with the IRS, but must certify to withholding agent that it meets the requirements of its certified deemed-compliant category on Form W-8

Types of Registered Deemed Compliant FFIs

- **Local FFI**
- **Qualified Collective Investment Vehicles**
- **Non-reporting members of participating FFI Group**
- **Restricted Fund**

Types of Certified Deemed Compliant FFIs

- **Non-registering Local Banks**
- **Retirement Funds**
- **Non-Profit Organizations**
- **FFI with Low-Value Accounts**

Owner Documented FFIs

- Upstream withholding agent must be USFI or PFFI and agree to report
- FFI does not maintain deposit or custody accounts and is not an insurance company
- FFI has no NPFFI owners and does not issue debt that is considered a financial account in excess of \$50,000
- Provides all requisite documentation to withholding agent

Definition: Financial account

Proposed Regulations - Section 1471-5(b)

The proposed regulations refine the definition of financial accounts to focus on traditional bank, brokerage, money market accounts, and interests in investment vehicles, and to exclude most debt and equity securities issued by banks and brokerage firms, subject to an anti-abuse rule.

Included:

- Any depository account
- Any custodial account
- Any equity or debt interest in an FFI, other than interests that are regularly traded on an established securities market
- Any cash value insurance contract and annuity contract issued or maintained by a financial institution

Excluded from Definition of Financial Account

- **Certain savings accounts (including both retirement and pension accounts and nonretirement savings accounts) that meet certain requirements with respect to tax treatment and the type and amount of contributions**
- **Any account held solely by one or more exempt beneficial owners or by nonparticipating FFIs that hold the account as intermediaries solely on behalf of one or more such owners.**
- **Debt or equity that is regularly traded on an established securities market**
- **Insurance contracts that provide pure insurance protection (such as term life, disability, health, property and casualty insurance contracts)**
- **Account held by an exempt beneficial owner**

Exempt Beneficial Owners

Foreign governments

International organizations

Foreign central banks of issue

Governments of U.S. possessions

Foreign retirement funds

- Treaty residents that are generally exempt from income tax in the fund's country of residence and satisfies any applicable LOB provision.
- Funds that receive contributions from government, employer or employee that are limited by reference to earned income where no one beneficiary has a right to more than 5% of the fund's assets, and investment income earned by the fund is exempt from income tax in its country of residence or 50 percent or more of the contributions are made by the government or employer.

Definitions: U.S. account and related definitions

U.S. Account: Proposed Reg's - Section 1471-5(a)(2)

Any financial account maintained by an FFI that is held by one or more specified U.S. persons or U.S. owned foreign entities

Specified U.S. Person: Proposed Reg's - Section 1473-1(c)

Any U.S. person other than the listed 12 types (which are U.S. exempt recipients)

U.S. Owned Foreign Entity: Proposed Reg's - Section 1471-5(c)

Any foreign entity that has one or more substantial U.S. owners

Definitions: Substantial U.S. Owner

Proposed Regulations - Section 1473-1(b)

- Non-U.S. corporation, partnership or trust where a specified U.S. person owns 10 percent, directly or indirectly
- Investment vehicles –Any U.S. ownership is a substantial U.S. owner

Definition: Recalcitrant account holder

Proposed Regulations - Section 1471-5(g)

- **An account maintained by a participating FFI (PFFI) that:**
 - Fails to comply with the PFFI's request for documentation or information to establish whether the account is a U.S. account
 - Fails to provide a valid Form W-9 upon PFFI's request PFFI
 - Fails to provide a correct name and TIN upon request after the PFFI receives notice from the IRS indicating a name/TIN mismatch
 - Fails to provide a valid and effective waiver of foreign law if foreign law prevents reporting with respect to the account holder by the PFFI
- **Exceptions:**
 - Account meets exception for U.S. accounts with deposit accounts with a balance of \$50,000 or less
 - Qualifies for documentation exceptions for preexisting accounts

Definition: Passthru Payment

Proposed Regulations - Section 1471-5(h)

- Any withholdable payment and any foreign passthru payment
- The proposed regulations reserve on the definition of a foreign passthru payment

Definition: Expanded affiliated group

Internal Revenue Code Section 1504(a)

- An expanded affiliated group means an affiliated group as defined in section 1504(a), determined by substituting “more than 50 percent” for “at least 80 percent each place it appears; and without regard to paragraphs (2) and (3) of section 1504(b).
- Partnerships and other entities shall be treated as a member of an expanded affiliated group if such entity is controlled (within the meaning of section 954(d)(3) by members of such group (including any entity treated as a member of such group by reason of this sentence).

Expanded affiliated group responsibilities

- **Members of the group are determined where they are at least 50% owned by the same parent, whether owned directly or indirectly**
- **Each entity will be assigned its own FFI EIN and will assume sole responsibility for its compliance, including the compliance of its global branches**
- **Each expanded affiliated group will appoint a lead FFI to complete applications and execute agreements with IRS**
- **A single member may be appointed as the “Compliance FFI” and will be responsible for drafting and ensuring FATCA compliant policies and procedures are adopted throughout the group**
- **Each affiliate in the group must be a participating FFI or registered deemed-compliant FFI, unless limited branch or limited FFI rules apply**

Transition Relief: Limited FFI

- **Transition rule for FFIs in expanded affiliated groups located in countries with legal prohibitions that restrict ability to comply**
- **Applies where FFI in group cannot:**
 - 1) report and close account or transfer account; or
 - 2) withhold and block account, close account or transfer account
- **Permits other FFIs in group to become PFFI and DCFFIs**
- **Limited FFI must agree to account identification requirements**
- **Limited FFI is treated as a NPFFI for purposes of penal withholding on withholdable payments**
- **Limited FFI must agree to not open new U.S. accounts or accounts for NPFFI**

Relief ends December 31, 2015



FFI Agreement

General Comments

- **Model will be set forth in a Revenue Procedure**
- **Will incorporate the definitions and requirements relevant to participating FFIs**
- **Intended timing:**
 - Publish a draft model FFI agreement in early 2012
 - Publish a final model FFI agreement, incorporating comments received, in the fall of 2012

FFI Agreement Provisions

- **Identification and documentation of account holders**
- **Waiver**
- **Withholding**
- **Reporting**
- **Expanded affiliated group**
- **Verification**
- **Requests for additional information**
- **Event of default**



Identification and Due Diligence

Identification by Account Type

PFFI / Registered Deemed Compliant FFI (DCFFI)

- Withholding certificate and verification of FFI-EIN

Certified DCFFI

- Withholding certificate and other verification, depending on claim---financial statement, organizational document, letter from counsel, etc.

Owner Documented FFI

- Withholding agent agreement, owner documentation (auditor can verify if agree to provide documents)

Publicly Traded Nonfinancial Foreign Entity (PT NFFE)

- Withholding certificate and name of exchange

Active NFFE

- Withholding certificate and verification (SIC, organizational document, credit report, etc.)

Passive NFFE

- Withholding certificate and written certification regarding owners (none or required data on U.S. persons)

FFI Due Diligence Requirements

Manual review for pre-existing accounts not required if certain data is maintained electronically

- Nationality and/or residence status, current residence and mailing addresses, current telephone number(s), whether there are any standing instructions, whether there is only an “in care of” address or “hold mail” instruction, and if there are any power of attorney (POA) or signatory authorizations.

Where paper search is required; defined scope

- Current customer master file; and any of the following if obtained within past five years:
 - Most recent: documentary evidence, account opening contract, AML documentation
 - Any POA or payment instruction currently in effect

De minimis threshold for pre-existing entity accounts is \$250,000

- If de minimus threshold is met (50K or 250K), no need to apply due diligence procedures until account balance reaches 1M—unless identified as U.S. account.

FFI Account Identification Requirements: Pre-Existing Individuals

- If already documented as U.S., then treat as U.S. (unless deposit account with balance \$50,000 or less)
- If not excluded in step above, can exclude all accounts \$50,000 or less. Once excluded, no requirements until balance exceeds 1M
- Electronic Search for U.S. indicia for accounts over \$50,000
- Must obtain W-9 and waiver (if needed) or cure if U.S. indicia is discovered (Within 2 years for regular accounts and within 1 year for those subject to the enhanced review)
- If balance is > 1M, must also perform “Enhanced Review.” Account manager inquiry and paper search
- Paper search of Current Customer Master file AND most recent (within last 5 years) documentary evidence, AML and other regulatory documentation, POA or signatories in effect and any standing instructions

FFI Account Identification Requirements: Pre-Existing Entity

- **Non-profit Organization**

- Letter from tax authority supporting claim or organizational document (same country as account and charitable purpose), TIN by that tax authority, and reporting as tax exempt to that country

- **Owner Documented FFI**

- New Withholding Certificate and FFI reporting statement with requisite owner information and agreement to provide documentation upon request. (Or has collected all documentation for each owner under AML rules within 4 years of payment date)

- **FFI w/Low Value Accts**

- New withholding certificate and financial statement/like document supporting claim (50M or less assets)

FFI Account Identification Requirements: Pre-Existing Exempt Beneficial Owners

- **Governments**
 - Generally know or name indicates government
- **International Organization**
 - Name is one that is designated as an international organization by executive order (on the list)
- **Foreign Central Bank**
 - Name and surrounding facts support claim
- **Retirement Funds**
 - Generally known as such in FFI's country and documentary evidence establishing qualification in country where organized.
- **Wholly Owned Entity**
 - New Withholding certificate, reporting statement, and documentation for every exempt beneficial owner.

FFI Account Identification Requirements: New Individuals

- IRS Form W-9 or W-8 or documentary evidence
- Review of all account opening documents for US indicia
- 90 days: Obtain W-9/waiver (if needed) or cure if U.S. indicia is discovered.

Validity Periods:

- Forms W-8: Same as Chapter 3 but Form W-8IMY for nonregistering local bank, FFI with low dollar accounts, and Owner-documented FFI will have same validity period of W-8BEN.
- Documentary Evidence: Same as Form W-8BEN. However, if document has expiration date, it is that date (even where the date is earlier than the 3+ validity period).

FFI Account Identification Requirements: New Entity

- **Non-profit Organization**

- Letter from counsel concluding entity meets the requirements or letter from counsel indicating entity was organized for such purpose and organizational document (same country as account and charitable purpose), TIN by that tax authority, and reporting as tax exempt to that country

- **Owner Documented FFI**

- New Withholding Certificate, documentation for all direct and indirect owners, and FFI reporting statement with requisite owner information. (If no US owners, documentation can be reviewed by external auditor. Annual statement must be provided.)

- **FFI w/Low Value Accts**

- New withholding certificate and financial statement/like document supporting claim (50M or less assets).

FFI Account Identification Requirements: Exempt Beneficial Owners

- **Governments**
 - Written statement that payee is government and beneficial owner
- **International Organization**
 - Withholding certificate or name is one that is designated as an international organization by executive order (on the list)
- **Foreign Central Bank**
 - Written statement that payee is foreign central bank of issue and beneficial owner
- **Retirement Funds**
 - Written statement, signed under penalties of perjury, that entity meets requirements and documentary evidence establishing qualification in country where organized
- **Wholly Owned Entity**
 - New Withholding certificate, reporting statement, and documentation for every exempt beneficial owner



Timelines

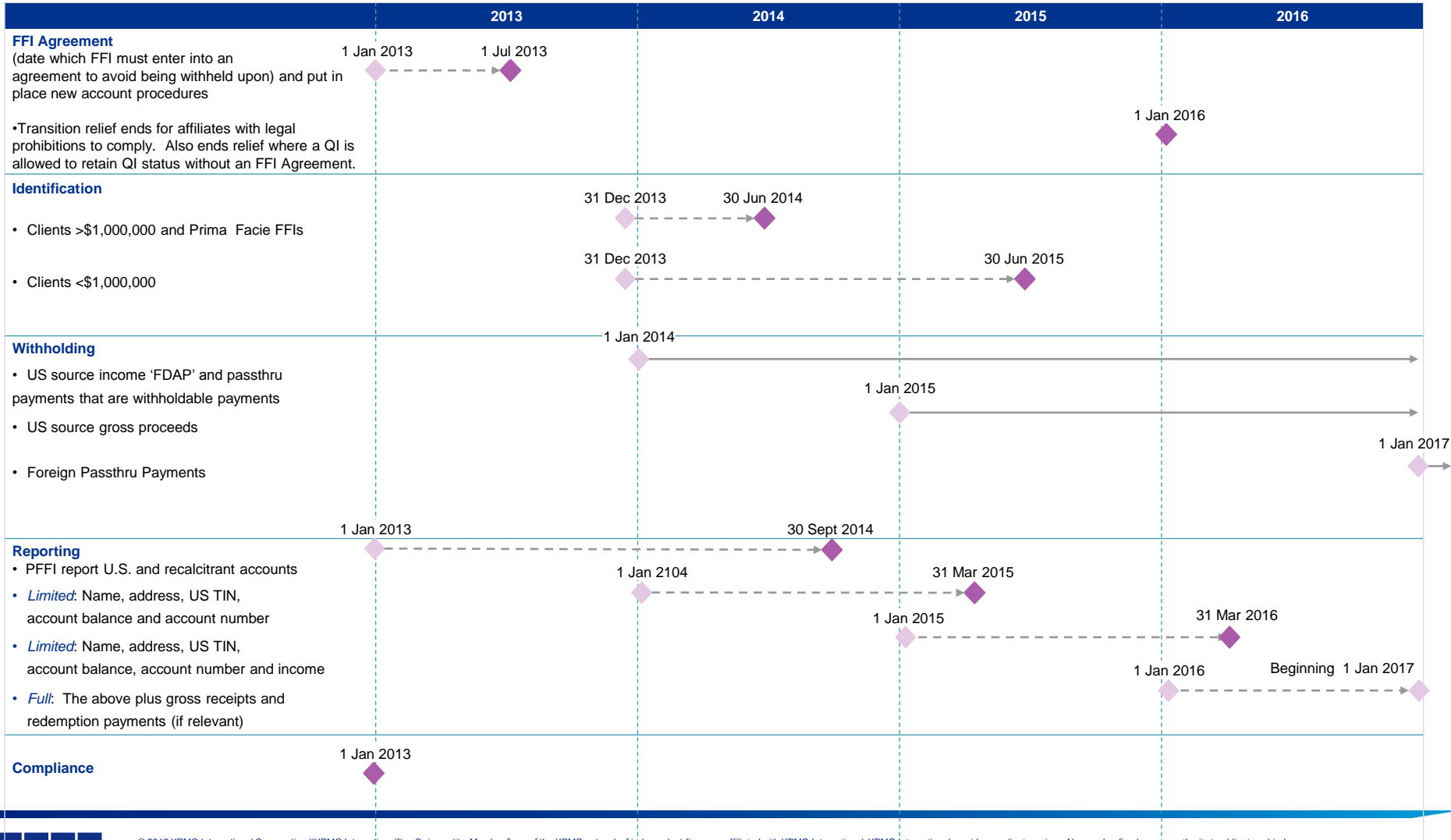
Schedule for Updates

- **First Half of 2012: Draft FFI Agreements**
- **Summer 2012: Draft Reporting Forms**
- **Year End 2012: Final Regulations**
- **Beyond: Intergovernmental Approach**

Foreign Account Tax Compliance Act (FATCA) Compliance Milestones



FATCA Milestones





Business Implications and Challenges

FATCA Impacts Within the Organization

FATCA Impacted Business Functions	Impacted Functional Groups						
	<i>Tax</i>	<i>Legal</i>	<i>Reg. Compl.</i>	<i>Acctg</i>	<i>Customer Relations</i>	<i>Ops</i>	<i>IT</i>
Product design, development and implementation	√	√	√		√		
Marketing, Sales & Distribution	√	√	√		√		
Onboarding		√	√		√	√	√
KYC/AML		√	√		√	√	√
Tax Documentation	√				√	√	√
Account Holder Communications					√		
Cash Distributions				√		√	√
Tax Withholding	√			√		√	√
Tax Reporting	√			√		√	√
Regulatory Compliance			√			√	√

Should We Be Worried?

Key Challenges

- **FATCA ownership within the organization**
- **Intergovernmental Approach**
- **Legal entity analysis**
- **AML/KYC procedures**
- **Existing account information; access to customer data**
- **Analyze and understand potential impact on business**
- **Determine impact to IT system(s)**
- **Internal/external education**
- **Time to develop a plan and mobilize**



Questions

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Thank You