



client alert

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FATCA SOMEWHAT RELAXED FOR 2014 AND 2015

On the afternoon of Friday May 2nd, 2014, the IRS unexpectedly announced that the years 2014 and 2015 will be a transition period for purposes of enforcement and administration of the Foreign Account Tax Compliance Act, or FATCA, but only for those financial institutions making a good faith effort to comply with the regime. In furtherance of this transition period, the IRS is extending certain transitional aspects of the due diligence requirements.

While this transition concept will be welcomed, it also adds some complexity to the already moving target of FATCA deadlines and procedures.

BACKGROUND

The Foreign Account Tax Compliance Act ("FATCA"), enacted in 2010, generally requires financial institutions outside of the United States ("FFIs") to disclose offshore accounts belonging to U.S. taxpayers to the U.S. Internal Revenue Service ("IRS") as a means of combating U.S. tax evasion. Failure by an FFI to participate in the FATCA system will result in a penalty tax of 30% being withheld from certain U.S. source income.

Final regulations implementing FATCA were released in January 2013 and then updated in February 2014. They require FFIs to register and sign an agreement with the IRS in which they undertake specified due diligence, information reporting, and, in some cases, withholding with respect to their accounts. However, to implement FATCA worldwide, and to address certain local law conflicts with FATCA such as privacy laws, the U.S. Treasury Department has been negotiating "intergovernmental agreements" ("IGAs") regarding FATCA with countries across the globe.

As of May 1, the U.S. Treasury has signed 30 IGAs, including with France on November 14, 2013, and has agreement in substance with 29 additional countries. Importantly, a compliant FFI resident in an IGA country generally will not be subject to the FATCA 30% penalty withholding tax. However, it generally must register with the IRS and undertake due diligence on its accounts, but any reporting will be to its home government tax authorities.

NOTICE 2014-33 (THE "NOTICE")

The Notice explains that the transition period is being provided in order to facilitate an orderly transition for withholding agents and FFIs to comply with the FATCA requirements. The Notice flags that amendments to the Final Rules will be issued in furtherance of this new transition period, including changes which impact the due diligence procedures and timing provided in the Final Rules and in the Annex I to the IGAs.

The IRS will ease its enforcement of FATCA through 2015 for entities, including, inter alia, participating FFIs, deemed compliant FFIs (which include those covered by an IGA), sponsored FFIs, and withholding agents, if they have made good faith efforts to comply with FATCA. Evidence of good faith efforts includes reasonable efforts during the transition period to modify account opening procedures to document the FATCA status of payees, and good faith efforts to identify and facilitate the registration of all FFI members of an expanded affiliated group. No further information is available yet as to what specifically constitutes such good faith efforts.

The Notice warns that an entity that has not made good faith efforts to comply with FATCA will not be given any relief from IRS enforcement during the transition period.

Changes affecting due diligence procedures center on the definition of a "pre-existing account" held by an entity. The revised rules will permit a withholding agent or FFI to treat an obligation (including an account) held by an entity as "pre-existing" for purposes of required due diligence if it is opened, executed, or issued on or after July 1, 2014, and before January 1, 2015, thereby effectively extending the pre-existing term by six months. The change is valuable because the due diligence required with respect to pre-existing entity accounts is less onerous than that required for new accounts (although accounts opened during this period will not benefit from the \$250,000 threshold exception applicable to accounts opened prior to July 1, 2014).

Until now, the deadline for most FFIs to implement new account opening procedures for entities was July 1, 2014, the date marking when an account could no longer be considered pre-existing. Many had voiced concern that this deadline was impractical, noting that the IRS has yet to even issue instructions for new forms that are critical to the due diligence process, like the new W-8BEN-E for entities to certify their FATCA status, which was released on March 30, 2014, but remains without instructions. The change signifies a continued effort by the IRS to address practical concerns of the industry regarding implementation of FATCA.

Importantly, the Notice clarifies that the courtesy extension for pre-existing accounts applies only to entity accounts and not to individual accounts because the procedures for documenting individual accounts are less complex. Furthermore, the Form W-8BEN for individual documentation was published with instructions on March 3, 2014. While this distinction makes sense, the staggered dates for pre-existing entity accounts versus pre-existing individual accounts, as well as other nuances set out in the Notice, risk increasing complexity to a degree that may undermine the usefulness of the extended period for pre-existing entity accounts.

The Notice confirms the application of this change to FFIs in IGA countries, noting that the IGAs contain a "most favorable terms" clause permitting an IGA nation to benefit from more favorable terms issued later in time, including relating to the procedures under Annex I regarding due diligence. It is expected that Annex I of future IGAs will include a new due diligence procedure for an entity account opened on or after July 1, 2014 and before July 1, 2015.

The Notice also sets out certain other changes, including modifications to the requirements for reasonable explanation supporting a claim of foreign status by an individual, and clarifications about how expanded affiliate groups with FFIs and branches that are prohibited by their home countries from fully complying with FATCA can manage the group's FATCA compliance.

Gide will continue to review the Notice and all other relevant developments, including following the implementation of the France IGA in France.

Please do not hesitate to contact any of us for further information. ■

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