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FATCA - Which Financial Institutions Are Caught?

1. Introduction

The FATCA regime entered into force from 1st July 2014.

As of that date:

- All financial institutions must have identified whether they have any “US account holders”;
- Financial institutions will have to start recording details of any payments that they make to any new US account holders, or to account holders who are “non-compliant”. This information will then be reported on an annual basis either directly to the IRS, or to the financial institutions local revenue authority (depending on what jurisdiction the financial institution is in); and
- Payments of US source income (and in future years capital gains) to non-compliant account holders will be subject to 30% US withholding tax.

In order to be compliant with their obligations under FATCA, banks, investment funds and investment managers have, therefore, been carrying out a review of all of their clients in order to identify where they might have US account holders. The definition of a “financial institution” for the purposes of the FATCA rules is much broader than expected. It includes, for example:-

- Professional trustees (other than individuals);
- Trusts;
- Family offices; and
- Nominees

There are two types of entity for the purposes of FATCA:

- **Foreign Financial Institutions (FFIs)** – this includes not only obvious types of non-US financial institutions such as banks, investment funds and investment managers, but also any entity that holds, manages, administers or invests money or financial assets on behalf of other people if either:
 1. the entity carries on this activity as its business; or
 2. even if the entity is not “in business”, the entity or its assets are managed by another financial institution. There are multiple sub-categories of FFI.

- **Non-Financial Foreign Entities (NFFE)** – this category covers all entities which are not within the definition of an FFI. There are only two sub-categories of NFFE:
 - **“Active” NFFEs** – these, broadly, are NFFEs that are carrying on a trading business. There is no need to identify any US owners of an active NFFE; and
 - **“Passive” NFFEs** – these are all other types of NFFE. It will be necessary for a passive NFFE to be able to identify whether it has any US owners.

The principal difference between a FFI and a NFFE is that a FFI will, in theory, have reporting obligations under FATCA, whereas a NFFE will not (it merely needs to be able to identify any US owners it might have).

Exactly what the reporting obligations of an FFI will be depends on what sub-category of FFI it falls into. For example, the following types of FFI do not need to file annual reports under FATCA:

- FFIs that are exempt from any reporting obligations – this includes government entities, regulated pension funds and similar; and
- FFIs that are deemed compliant with FATCA without having to undertake any reporting – this includes charities (who have no reporting obligations), but also includes certain categories of FFI that are only deemed compliant with FATCA because another financial institution has taken on the FATCA reporting obligation on their behalf.

Some of the more common entity types and their FATCA classification and reporting obligations are set out below.

2. Trustees

Trustees may be financial institutions for the purposes of FATCA, but only if they are “entities” and they are “in business”.

An individual acting as a trustee, whether or not in a professional capacity is not an “entity” and will not therefore be a financial institution. As such, the individual will have no reporting obligations under FATCA (although he may have to report on behalf of the trust of which he acts as trustee – see below).

Trustees that are entities, on the other hand, will be financial institutions if they are “in business” as trustees (i.e. if they charge for their services, and that is primarily what their business involves). Such trustees will therefore have reporting obligations under FATCA.

3. Trusts

A trust is considered to be a separate entity from its trustees for the purpose of FATCA.

The trust is an entity and is therefore capable of being a financial institution if, broadly:-

- It holds a majority of “financial assets” (broadly stocks, shares, financial instruments etc.); and
- Either the trust, or its assets, are professionally managed by an entity which is itself a financial institution (e.g. a professional trust company, or a discretionary investment manager).

A small family trust could, therefore, be a financial institution for the purposes of FATCA, and therefore have FATCA reporting obligations.

4. Nominees

Subject to certain exemptions regarded as low risk, some Accounts which are maintained by a Financial Institution will be deemed Financial Accounts and will have reporting obligations under FATCA. A person, other than a Financial Institution, that holds a Financial Account for the benefit of another person, e.g. as an agent or nominee is not treated as an account holder though with respect to such account for the purposes of the Agreement.

5. Family offices

Where a family office assists in the management or the administration of financial assets on behalf of others, it will be a financial institution, and will therefore have reporting obligations under FATCA.

6. What does being a Foreign Financial Institution mean?

The first step is to assess whether or not the FFI needs to register with the IRS in order to obtain a global intermediary identification number or GIIN. Any financial institution which will be undertaking FATCA reporting on its own behalf will need to obtain a GIIN, whether or not it has any US accounts to report.

This is done via the IRS portal at: <http://www.irs.gov/Businesses/Corporations/FATCA-Registration>

The deadline for registering with the IRS in time to obtain a GIIN by 1st July 2014 (when the FATCA rules came into force) was 5th May 2014.

However, there was some breathing room for FFIs who are in jurisdictions which have entered into Model 1 inter-governmental agreements (IGAs) with the US such as the UK (as below). FFIs in these jurisdictions do not need a GIIN until 1st January 2015 and the deadline for registration was 25th October 2014:

1. Australia	10. France	19. Italy	28. Netherlands
2. Belgium	11. Germany	20. Jamaica	29. New Zealand
3. British Virgin Islands	12. Gibraltar	21. Jersey	30. Norway
4. Canada	13. Guernsey	22. Latvia	31. South Africa
5. Cayman Islands	14. Honduras	23. Liechtenstein	32. Spain
6. Costa Rica	15. Hungary	24. Luxembourg	33. Slovenia
7. Denmark	16. Ireland	25. Malta	34. United Kingdom
8. Estonia	17. Isle of Man	26. Mauritius	
9. Finland	18. Israel	27. Mexico	

7. Can I appoint someone else to do this?

All trusts in the territories listed above (in addition to Austria, Bermuda, Chile, Japan and Switzerland) which have one or more trustee that is itself a financial institution (i.e. a professional trust company) will automatically qualify as a trustee documented trust and the FATCA reporting obligation falls on the trustees not the trust. The trust will not need to obtain a GIIN or register with the IRS.

However, all other types of financial institution will only be able to appoint a third party to report on their behalf if:

- They appoint a “sponsor”. The sponsor must be another financial institution which is:
 1. Already engaged in the management of the first financial institution or its assets (e.g. its trustee or discretionary investment manager or another person authorised to enter into contracts on behalf of the financial institution, so not including a custodian);
 2. Registered as a sponsoring entity with the IRS; and
 3. Willing to act as sponsor for the financial institution in question.

- They engage an unconnected third party financial institution to report on their behalf as an “owner documented FFI” (which requires the financial institution in question to provide the unconnected third party financial institution with all necessary information to enable it to make the appropriate reports).

8. What do I have to report?

The FATCA reporting requirements are that the identity of any “new US account holders”, (US persons – which includes any US citizen – and certain US entities) and the value of their “accounts” (and, in the future, details of any profits in these “accounts”) must be reported, either direct to the IRS or to the financial institution’s local revenue authority, i.e. HMRC, in the case of the UK.

Where an “account holder” is an entity then the question becomes: what type of entity is it?

- Financial institution – if the account holder is a financial institution that is FATCA compliant (i.e. it either does not have to undertake FATCA reporting, or it satisfies its FATCA reporting requirements) then no report needs to be made. However, if the account holder is a financial institution that is not FATCA compliant, then this needs to be reported.
- NFFE – if the account holder is an active NFFE then no report needs to be made. However, if the account holder is a passive NFFE, then a report needs to be filed if the NFFE has any US owners or “controlling persons”. This will include:-
 - Where the NFFE is a trust – any US settlor, trustee, beneficiary (generally only if they have a greater than 10% interest – direct or indirect – in the trust assets although this threshold may be higher depending on the jurisdiction) or protector.
 - Where the NFFE is a partnership – any US person with a greater than 10% interest – direct or indirect – in the partnership (this threshold may be higher depending on the jurisdiction).
 - Where the NFFE is a company – any US person with a greater than 10% interest – direct or indirect – in the company (this threshold may be higher, depending on the jurisdiction).

9. I have no US account holders. Does this mean I do not have to file any reports under FATCA?

That depends. In the UK, according to the UK domestic legislation any reporting financial institution needs to file an annual FATCA return with HMRC, even if they have no US accounts to report. It seems practice may vary from jurisdiction to jurisdiction.

10. I have US account holders. What do I need to report?

The first FATCA report filing deadline is 31st March 2015 (31st May 2015 in the UK). Reporting must be done annually.

The information that needs to be reported includes the name, address and US taxpayer identification number of the account holder, as well as certain details of the account.

11. What are the penalties for non-reporting?

Non-compliance with FATCA will result in 30% withholding tax on US source payments with effect from 1st July 2014. It may also from 2017 result in 30% withholding on payments from non-US sources that are made by payers in receipt of US source income or gains.

There are also penalties for reporting FFIs that are in breach of their reporting obligations under FATCA. These may vary from jurisdiction to jurisdiction.

12. Summary

FATCA is global in its reach and even those FFIs, NFFEs or individuals with no US assets and no US connections are affected by it.

Where a FFI has no US account holders, compliance with FATCA should not be particularly onerous. Registration with the IRS in order to obtain a GIIN is relatively easy, and any annual reporting requirements should be easily satisfied if there are no US account holders to report.

FATCA should not be ignored and professional advice should be sought where necessary.

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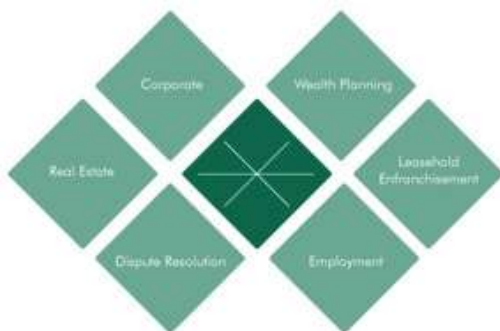
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