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Foreign Account Tax Compliance Act: The Most Revolutionary Piece of Tax Legislation Since the Introduction of the Income Tax

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Foreign Account Tax Compliance Act: The Most Revolutionary Piece of Tax Legislation Since the Introduction of the Income Tax

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ABSTRACT

With taxation of income being the most significant source of revenue, most national governments consider tax evasion prevention to be one of the priorities of their tax agencies. In the United States, tax evasion has been a significant concern of the Internal Revenue Service ever since the modern income tax was instituted with the passing of the Sixteenth Amendment in 1913. Over the following century, Congress enacted numerous measures aimed at curbing the illegal practice, but, as often is the case, both individuals and institutions desiring to not abide by the law found new ways to outsmart the tax authorities. However, the recently introduced Foreign Account Tax Compliance Act (FATCA), the most complex piece of tax legislation in modern times, will make tax evasion much more difficult, if not quite impractical. Through a system of reporting requirements and severe penalties, the law aims to discourage the unlawful practice, while at the same time it significantly amplifies the powers of the IRS. FATCA will thus revolutionize the American tax regime and also serve as a significant step toward the introduction of a global tax system in the future.

**Foreign Account Tax Compliance Act:
The Most Revolutionary Piece of Tax Legislation
Since the Introduction of the Income Tax**

I. Introduction

As the federal government expanded over the course of the twentieth century, the increasing need for financial resources necessitated the creation of an efficient and comprehensive taxation system. Throughout that time the tax code evolved to address the changing socioeconomic environment due to the forces of globalization, which made investment banking increasingly interconnected and foreign markets easier to access. Recognizing this new capability, certain taxpayers began to take measures to protect themselves from taxation by hiding their income in low tax jurisdictions. Since citizenship rather than residence determines tax liability for Americans, these tax evasion efforts naturally constitute criminal activity, which has led the government to repeatedly take preventative measures to ensure proper compliance. Another important step in this long history of regulation took place in 2010 when Congress passed the Foreign Account Tax Compliance Act (FATCA). Designed to improve upon the existing system of foreign financial account reporting, the legislation sets forth a framework of cooperation between the IRS, and foreign financial institutions as well as governments. While the mandates of the law ultimately focus on increasing tax revenue, they will inadvertently revolutionize the way taxation works on an international scale. However, to understand this potential significance of FATCA for the twenty-first century, it is necessary to examine how tax evasion became such an unyielding global concern for governments throughout the world.

II. Taxation and Tax Evasion

A. Background

While taxation in the United States extends as far back as the American Revolution, it was not until the turn of the nineteenth century that the modern tax system began to take shape. The passing of the Sixteenth Amendment in 1913 settled all former controversies regarding the constitutionality of the federal government's power to levy income taxes. Previously, both federal and state governments have taxed their residents' incomes as most prominently seen with

the Revenue Act of 1861 during the Civil War. However, the explicit inclusion of the power to collect taxes in the Constitution and the subsequent creation of the Bureau of Internal Revenue made taxation of income an undisputable and permanent reality. With changing budgetary needs over the following decades, the tax system underwent many changes such as the numerous revisions of tax brackets or the introduction of payroll withholding. These changes as well as the transformation of the IRS into a more efficient agency through deep restructurings made the American tax system a source of contention for certain individuals desiring to limit their tax burden.¹ In theory, taxpayers around the world can easily shelter their income by moving it to low tax jurisdictions through the use of various legal and accounting procedures, thereby preventing their country of origin from having a claim to those taxes. However, individuals having ties to the United States either through citizenship or residence cannot as easily accomplish the same objective, since the American tax system substantially differs from its foreign counterparts in its taxation approach.

B. Residence vs. Citizenship-based Taxation

Except the U.S. and the small African country of Eritrea, countries around the world impose income taxes based on geographical location rather than legal status of the taxpayers. Known as residence-based taxation (RBT), this concept holds that only the income of both citizens and resident aliens living within the borders of a given country can be taxed.² Taxpayers from RBT countries who live in foreign tax jurisdictions can control how much tax they pay by choosing where they reside and pay taxes. The system assumes that expatriates receive government benefits exclusively in their chosen country of residence and, therefore, their country of origin has no valid claim to the taxes on their income. This claim does not hold true when these taxpayers receive income from sources like financial securities or realty in the country of origin, because special rules might apply depending on the circumstances of each individual. However, RBT fundamentally prevents the double taxation of income, which

¹ “IRS at Work: IRS History.” TRAC IRS. Syracuse University, n.d. Web. 15 August 2015. <<http://trac.syr.edu/tracirs/atwork/current/irsHistory.html>>.

² “A Guide To Relinquishing or Renouncing U.S. Citizenship.” RenunciationGuide.com. RenunciationGuide.com, n.d. Web. 9 December 2015. <<http://www.renunciationguide.com/citizenship-taxation-and-expatriation-background-and-history/citizenship-based-taxation-international-comparison/>>.

subsequently results in its perception as a fair and equitable tax regime when compared to citizenship-based taxation (CBT).³

On the other hand, CBT countries tax their citizens and permanent residents regardless of where they choose to live. In the United States, Congress levies the personal income tax equally on their worldwide income avoiding double taxation with foreign tax credits and foreign earned income exclusions. As opposed to individuals in jurisdictions employing RBT, American taxpayers theoretically cannot move abroad to limit their tax payable to the IRS, because they are obligated by law to report all of their income regardless of its source. This complexity has created unfavorable tax circumstances for many individuals, who in some cases resorted to tax evasion or renunciation of their citizenship to protect their wealth.⁴ By employing various accounting and legal procedures to transfer their income to offshore locations with low tax rates and limited financial transparency, they can evade U.S. taxes. Despite the power of the American legal system, neither the IRS nor the courts have much influence when dealing with these nations, because their existence and status essentially depends on the dubious services provided to these taxpayers.⁵

C. Tax Havens

With the financial services provided in offshore tax havens guaranteeing secrecy, taxpayers have the capability to move their income generating sources to these locations. Their main incentive for this comes through the disparity between the minimal tax rates found in these offshore jurisdictions and the regular rates in their country of citizenship. In addition to the favorable tax regimes, tax havens generally have strong financial secrecy laws, which make it difficult for tax authorities to identify the taxpayers who use these services. With the financial institutions in these local jurisdictions being legally shielded from cooperating with tax agencies by virtue of these laws, the reporting requirement implicitly falls on the individual taxpayers, who will not cooperate when their assets are already protected. The difficulty with uncovering

³ “Residence-Based Taxation: A Necessary and Urgent Tax Reform.” American Citizens Abroad. American Citizens Abroad, 1 March 2013. Web. 15 August 2015.

<<https://americansabroad.org/files/9613/6302/0825/rbtmarch2013.pdf>>.

⁴ Wood, Robert W. “Many Americans Renounce Citizenship, Hitting New Record.” Forbes. Forbes, 7 August 2014. Web. 9 December 2015. <<http://www.forbes.com/sites/robertwood/2014/08/07/many-americans-renounce-citizenship-hitting-new-record>>.

⁵ “The 2011 Global Executive: Individual Tax, Social Security and Immigration.” Ernst & Young. Ernst & Young, 1 August 2011. Web. 15 August 2015.

<[http://www.ey.com/Publication/vwLUAssets/Global_Executive_2011/\\$FILE/GE_2011_Global_Executive.pdf](http://www.ey.com/Publication/vwLUAssets/Global_Executive_2011/$FILE/GE_2011_Global_Executive.pdf)>.

foreign asset holdings comes from the ability of accountants and lawyers to use the secrecy laws of multiple tax havens to create overlapping shell corporations across the globe. Because the local law protects these entities, it is difficult to determine the ownership chain throughout these different jurisdictions. Ultimately, tax authorities have no legal leverage over these individuals if they do not have evidence that they engaged in tax evasion in the first place.

Switzerland, the Cayman Islands, and more recently cities in the Far East such as Hong Kong have established a reputation as the tax jurisdictions of choice for wealthy individuals. While Switzerland's banking industry has turned into one of the country's specializations over the past century, the tax havens in developing regions have resorted to financial secrecy for economic growth. By deliberately creating laws designed to limit transparency and financial oversight, these jurisdictions attract foreign capital from wealthy individuals, spurring economic growth. With their national economies primarily consisting of the finance industry, these jurisdictions gain at the expense of other governments and through their sovereignty are legally protected from any repercussions. While the list of declared tax havens might be surprisingly short, most of the recent studies estimate that at least \$20 trillion of capital is being held offshore in these jurisdictions.⁶ Because the income generated by this capital is typically taxed at a low rate, governments have started to look more closely at others ways to put a stop to the practice.

D. Previous Attempts to Curtail Tax Evasion

By definition, tax evasion consists of breaking the law by way of intending to deliberately deprive the authorities of the taxes they have a legal right to collect.⁷ Because personal income taxes represent almost half of federal tax revenue, this unlawful act has repeatedly drawn the attention of the U.S. government, resulting in a series of legislation aimed at decreasing the tax gap estimated to be \$385 billion for the 2006 tax year.⁸ Starting with the passing of the Bank Secrecy Act (BSA) in 1970, Congress aimed to curtail money laundering and fraud by requiring the cooperation of financial institutions with the detection and reporting of suspicious transactions. Additionally, this legislation also established the foundation for the prevention of tax evasion by mandating both natural persons and legal entities to declare their

⁶ "Oxfam: Tax on \$18.5 offshore trillions could end world poverty." Tax Justice Network. Tax Justice Network, 22 May 2013. Web. 17 August 2015. <<http://taxjustice.blogspot.ch/2013/05/oxfam-tax-on-offshore-trillions-could.html>>.

⁷ "Tax Evasion." Cornell University Law School. Cornell University Law School, n.d. Web. 9 December 2015. <https://www.law.cornell.edu/wex/tax_evasion>.

⁸ Sahadi, Jeanne. "Tax gap: IRS comes up \$385 billion short." CNN. CNN, 6 January 2012. Web. 9 December 2015. <http://money.cnn.com/2012/01/06/news/economy/tax_gap/>.

foreign assets through the Report of Foreign Bank and Financial Accounts (FBAR).⁹ The annual filing of FinCEN Form 114, as the document is officially known, with the Financial Crimes Enforcement Network has been primarily intended for providing leads to track down illegal activity based on the financial records used in these transactions.¹⁰ Although the purpose of the BSA is to uncover financial fraud, the IRS uses the FBAR information in its efforts to prevent tax evasion.

While the BSA forms the basis of the strategy of stopping tax evasion, the IRS has other methods to encourage proper compliance. IRC §1441 obligates the withholding of 30% of U.S. source income in the form of wages, interest, dividends or royalties paid out to nonresident aliens. This mechanism prevents individuals, who neither have American citizenships nor declared permanent residency in the U.S. from receiving income that would otherwise go untaxed. The code section further stipulates that financial institutions based abroad can act as Qualified Intermediaries by keeping records of transactions from U.S. payers in order to accurately report income of the payees to the IRS and withhold taxes where necessary as mandated by the code.¹¹

In 2003, the IRS also started the Offshore Voluntary Compliance Initiative to allow taxpayers to become compliant by paying back taxes on their unreported income as well as any applicable interest and penalties. The ability to avoid criminal prosecution for willful tax evasion incentivized some individuals to cooperate with this amnesty program. While this only applied to taxpayers who used foreign issued credit and debits cards to access their offshore bank accounts, this IRS initiative enabled the agency to recover unpaid taxes, but also to get a new perspective on the state of tax evasion perpetrated by American taxpayers.¹²

E. Recent Developments

⁹ “Bank Secrecy Act.” Internal Revenue Service. Internal Revenue Service, 1 October 2015. Web. 10 October 2015. <<http://www.irs.gov/Businesses/Small-Businesses-&-Self-Employed/Bank-Secrecy-Act>>.

¹⁰ “Taxpayers with Foreign Assets May Have FBAR and FATCA Filing Requirements in June.” Internal Revenue Service. Internal Revenue Service, 10 June 2015. Web. 17 August 2015. <<http://www.irs.gov/uac/Newsroom/Taxpayers-with-Foreign-Assets-May-Have-FBAR-and-FATCA-Filing-Requirements-in-June>>.

¹¹ “26 CFR 1.1441-1 - Requirement for the deduction and withholding of tax on payments to foreign persons.” Cornell University Law School. Cornell University Law School, n.d. Web. 9 December 2015. <<https://www.law.cornell.edu/cfr/text/26/1.1441-1>>.

¹² “IRS Unveils Offshore Voluntary Compliance Initiative; Chance for ‘Credit-Card Abusers’ to Clear Up Their Tax Liabilities.” Internal Revenue Service. Internal Revenue Service, 14 January 2003. Web. 18 August 2015. <<https://www.irs.gov/uac/IRS-Unveils-Offshore-Voluntary-Compliance-Initiative;-Chance-for-%E2%80%98Credit-Card-Abusers%E2%80%99-to-Clear-Up-Their-Tax-Liabilities>>.

While the efforts of the U.S. government to curb tax evasion were only successful to a certain extent, two prominent controversies involving Swiss banks exposed the magnitude of the problem and explained why the U.S. government needed legislature such as FATCA. Switzerland has been the source of interest to American and European tax authorities, because of its emphasis on confidentiality in individuals' banking affairs. An FBI investigation in 2008, however, revealed that UBS AG, the largest bank in the country, sought American clients by offering to shield their assets from the IRS.¹³ A similar investigation took place in 2014 when Credit Suisse AG was found guilty of having assisted U.S. taxpayers in the filing of false income tax returns and consequently illegally avoiding the proper payment of taxes.¹⁴ Ultimately, both banks settled with the Justice Department for a cumulative sum of \$3.6 billion. The cases of UBS and Credit Suisse further illustrate that tax evasion is a crime not committed by dubious unknown banks controlled by criminal organizations, but by well-regarded multinational financial institutions. These prominent banks deliberately sought to assist American citizens in the breaking of American law and hoped for financial secrecy laws to protect them from legal scrutiny. While U.S. government representatives undoubtedly knew the extent of the illegal activities before the investigations took place, these circumstances reveal why tax evasion needed to be dealt with in a more powerful and concentrated effort through FATCA.

F. Introduction of the Legislation

Recognizing the need for a new approach to combat tax evasion, the American government decided to prepare new legislation aimed at obtaining more complete information about taxpayers and recovering a portion of the lost tax revenue. The Foreign Account Tax Compliance Act (FATCA), was introduced in Congress on October 27, 2009 by Senator Max Baucus and Representative Charles Rangel (D-NY). Ultimately, FATCA was added to the Hiring Incentives to Restore Employment (HIRE) Act, which was the first step to push the U.S. out of the recession. The purpose behind the inclusion was to raise revenue through FATCA's recovery of unpaid taxes to fund the stimulus portion of the legislation. Although FATCA was subject to much congressional debate, the bill was approved by Congress with several amendments and

¹³ Browning, Lynnley. "UBS Tax Evasion Case Sheds Light on Swiss Secrets." Newsweek LLC. Newsweek LLC, 6 November 2014. Web. 18 August 2015. <<http://www.newsweek.com/ubs-tax-evasion-case-shed-light-swiss-secrets-282637>>.

¹⁴ "Credit Suisse Pleads Guilty to Conspiracy to Aid and Assist U.S. Taxpayers in Filing False Returns." Department of Justice. Department of Justice, 19 May 2014. Web. 20 August 2015. <<http://www.justice.gov/opa/pr/credit-suisse-pleads-guilty-conspiracy-aid-and-assist-us-taxpayers-filing-false-returns>>.

signed by President Obama on March 18, 2010. While a lot of progress has been made since the time of its inception, the legislation has stirred up quite a lot of controversy surrounding its rigorous and highly complex reporting requirements as well as its severe penalties for non-compliance.¹⁵

III. Mechanism of FATCA

A. Objectives of the Legislature

While the reporting requirements present in FATCA resemble those found in the FBAR compliance process, legislators designed the law with the primary intent of collecting reliable and complete information about the foreign accounts of American taxpayers. Because the U.S. tax system relies on voluntary compliance by the taxpayers, the IRS could not confirm the information presented on the FBAR without auditing the individuals. By engaging financial institutions with the task, the agency ensures that it receives notice of all accounts belonging to American taxpayers even if some are unreported or have underreported values on the FBAR. Additionally by discouraging these financial institutions based in other countries from non-compliance through a series of strict penalties, the IRS guarantees that the provided information can be relied upon with a high degree of certainty. With this two pronged approach of individual and institutional reporting, the agency can cross-reference the provided information to identify inconsistent reporting. By securing the involvement of foreign governments, the U.S. also ensures its capability to reduce tax evasion by bringing together a collective of cooperating states under its program that ultimately will lead to the creation of a global tax reporting system.

B. Reporting by Individual Taxpayers

Expanding on the individual reporting requirements set forth by the Bank Secrecy Act of 1970, FATCA creates additional provisions that U.S. taxpayers have to abide by in order to avoid significant penalties. For every year in which the taxpayer files an income tax return, he or she must also file Form 8938 listing all specified foreign financial assets, which for the purposes of the law include pensions, stocks, partnership interests and financial accounts held overseas. However, only when the cumulative value of these assets exceeds the designated limit for the filing category does the taxpayer need to comply with the requirements of this law. For a single filer residing in the U.S., the reporting requirement takes effect if the assets are valued at \$50,000

¹⁵ Chudy, James. "President Signs HIRE Act, Including FATCA Provisions Combating Offshore Tax Evasion." Pillsbury Law. Pillsbury Law, 18 March 2010. Web. 20 August 2015. <<http://www.pillsburylaw.com/siteFiles/Publications/DABAB60873CF5F730C54F8CE26B549B2.pdf>>.

or more at the end of the tax year or \$75,000 at any other time during the year with the account values correspondingly doubled for married filers. As previously mentioned, FATCA's primary aim is to identify domestic taxpayers with foreign accounts and take action against those trying to evade tax. Therefore, the legislators imposed thresholds, which are less restrictive for taxpayers filing a U.S. tax return, but currently living outside of the United States. For the same taxpayer filing as single, the account values essentially quadruple to \$200,000 and \$300,000, respectively.¹⁶

While both the FBAR and FATCA Form 8938 essentially serve the same purpose, differences between the two laws, as shown in Exhibit A, demonstrate the complexity of how U.S. legislators combat tax evasion. Although the FBAR filing process resembles the reporting procedure required for Form 8938, it is filed electronically with the Department of Treasury by the last day in June with no extensions available. The filing of the FBAR is administered separately from the annual tax return sent to the IRS, but the agency still uses that information to pursue taxpayers with illicit offshore operations. The BSA does not consider the current residence of the taxpayers and sets a minimal \$10,000 account value filing threshold, thus targeting more taxpayers than FATCA. Therefore, circumstances where an individual has to report financial accounts on an FBAR, but does not have to file FATCA Form 8938 can occur. This difference in reporting requirements illustrates that FATCA was designed to identify wealthy individuals for whom tax evasion protects a substantial amount of income from taxation.¹⁷

This new approach to reducing tax evasion would not be as effective without penalty provisions that discouraged taxpayers from improper compliance with the reporting rules. To fairly administer the punishment, the FBAR makes the distinction between non-willful and willful negligence; up to \$10,000 for non-willful negligence and up to the greater of \$100,000 or half of the account balances for willful negligence. These penalties are administered per account per person with signature authority, which means that a penalty is assessed for each account unreported by one individual and that multiple taxpayers can be penalized for the same

¹⁶ "Do I need to file Form 8938, "Statement of Specified Foreign Assets"?" Internal Revenue Service. Internal Revenue Service, 19 November 2014. Web. 20 August 2015. <<http://www.irs.gov/Businesses/Corporations/Do-I-need-to-file-Form-8938-Statement-of-Specified-Foreign-Financial-Assets>>.

¹⁷ "Comparison of Form 8939 and FBAR Requirements." Internal Revenue Service. Internal Revenue Service, 2 February 2015. Web. 19 August 2015. <<http://www.irs.gov/Businesses/Comparison-of-Form-8938-and-FBAR-Requirements>>.

unreported account.¹⁸ Whereas the penalty structure for FBAR compliance carries strict penalties, the FATCA equivalent does not put as much strain on the taxpayers. However, since noncompliant individuals likely will be subject to penalties imposed under both laws, the double penalties encourage compliance with the law. Noncompliance with FATCA carries a simple \$10,000 penalty for each undisclosed account as well as another \$10,000 for each thirty day period of non-filing after being notified by the IRS for a maximum total penalty of \$60,000. The IRS, in addition to imposing criminal penalties, also reserves a non-expiring right to audit the noncompliant individual if the form is not filed by the due date of the tax return causing the statute to remain open indefinitely. Although the combined FBAR and FATCA penalties should make taxpayers hesitant about filing a false tax return, the main component of FATCA places the reporting mandate as well as the penalties on both foreign and domestic financial institutions.¹⁹

C. Reporting by Foreign Financial Institutions

To ensure the truthfulness of the information provided by individual taxpayers, lawmakers decided to institute a major provision into FATCA that provides the authorities with another source of obtaining financial records. The law stipulates that certain types of entities in the finance industry, collectively termed as foreign financial institutions (FFI), have to enter into a cooperation agreement with the IRS to identify American taxpayers among its account holders and disclose certain information about them. This reporting mandate only falls on institutions which perform ordinary banking services, hold financial assets for other persons, engage in trading or investing in various financial instruments or are insurance companies with cash value products or annuities. While this definition encompasses the majority of common financial institutions, most governmental entities, non-profit organizations, some retirement entities and certain smaller local financial institutions are exempt from cooperating with the IRS. Although the cooperation agreement with the IRS is voluntary, the list of FFIs, which registered with the IRS and have started to report information about their account holders, is quite exhaustive,

¹⁸ “FBAR Penalties.” Internal Revenue Service. Internal Revenue Service, 1 July 2008. Web. 21 August 2015. <http://www.irs.gov/irm/part4/irm_04-026-016.html#d0e529>.

¹⁹ “Summary of FATCA Reporting for U.S. Taxpayers.” Internal Revenue Service. Internal Revenue Service, 8 October 2015. Web. 14 October 2015. <<http://www.irs.gov/Businesses/Corporations/Summary-of-FATCA-Reporting-for-U.S.-Taxpayers>>.

because they would rather complete the additional reporting than face the penalties imposed by the IRS.^{20 21}

Following registration with the IRS as an FFI, the agreement obligates these entities to fully cooperate with the agency in matters pertaining to account holders deemed to be American taxpayers. Additionally, the IRS requires that financial accounts of foreign legal entities in which U.S. interest either directly or indirectly represents more than 10% of the stock have to be included in the reporting process. After identifying such individuals or entities, FFIs must annually report account information including investment volume and income paid by the account holder. While the identification and reporting procedures may seem trivial, the law requires the financial institutions to comply with verification, due diligence and investigation procedures. The obligations of FFIs do not stop at identification and reporting, because FATCA also requires them to take punitive measures against U.S. persons or non-participating FFIs who fail to comply with the law. In such circumstances, participating FFIs have to impose a 30% withholding tax on payments of U.S. source income or gross proceeds from sale of investment vehicles that create U.S. source income. This withholding tax is levied on non-participating FFIs not exempt from the program, individuals not willing to comply with the identification process and foreign entities which do not sufficiently disclose the identities of its U.S. owners. Thus, FFIs are in the position of either losing their institutional sovereignty by conforming to a foreign agency's rules or facing the extensive penalties in case of non-compliance with the law.^{22 23}

D. Reporting by Domestic Financial Institutions

Just as foreign financial institutions have agreed to cooperate with the IRS under FATCA, their domestic counterparts have been obligated with a set of withholding responsibilities that make the law so daunting for non-compliant foreign institutions. With the IRS having more authority domestically than abroad to administer the law, the agency tasked U.S. financial institutions (USFIs) into acting as the primary withholding agents for the penalties

²⁰ "FATCA Information for Foreign Financial Institutions and Entities." Internal Revenue Service. Internal Revenue Service, 02 June 2015. Web. 23 August 2015. <<http://www.irs.gov/Businesses/Corporations/Information-for-Foreign-Financial-Institutions>>.

²¹ "The widespread reach of FATCA: How will it affect your business?" PwC. PwC, 1 August 2013. Web. 23 August 2015. <<http://www.pwc.com/us/en/financial-services/publications/fatca-publications/assets/pwc-fatca-non-fs-mnecs.pdf>>.

²² "FATCA: A Brief Introduction." PwC. PwC, n.d. Web. 23 August 2015. <<http://www.pwc.lu/en/fatca/docs/pwc-fatca-brief-introduction.pdf>>.

²³ "Summary of Key FATCA Provisions." Internal Revenue Service. Internal Revenue Service, 6 November 2014. Web. 24 August 2015. <<http://www.irs.gov/Businesses/Corporations/Summary-of-Key-FATCA-Provisions>>.

levied on non-compliant FFIs. Because the USFIs essentially control the inflow and outflow of funds in the American financial markets, they possess the unique ability to assist the IRS with administering the integral penalty component of the law. FFIs, which do business in the United States and use USFIs to gain access to American markets, would not be able to circumvent the penalties without giving up their American business interests. While FFIs decided to cooperate to avoid the penalties of the IRS, non-participating foreign institutions have to face severe penalties that make it practically impossible to remain financially operational. In a time when the United States is one of the central financial centers, every transaction taking place around the globe at some point passes through American markets or involves the U.S. dollar. Therefore, operating entirely outside of American influence is very difficult for any sizable FFI that aims to remain profitable. Recognizing the impact that such circumstances would have on most investment banks, the IRS decided to use the USFIs to get FFIs to participate in its identification and reporting program.^{24 25}

While the majority of financial institutions opted to comply with the FATCA regulations, non-participating FFIs have to face the significant penalty the IRS deemed necessary to make non-compliance a bad choice. The agency instituted a 30% withholding penalty on passthru payments of U.S. source income made to non-compliant FFIs. These withholdable payments include periodic payments such as interest and dividends, gains from disposition of property that produce U.S. source income and deposit interest paid by American banks and their foreign branches. When considered in the context of global financial operations, any FFI involved in American markets would be faced with an automatic 30% that could not be mitigated with careful tax planning through the use of international treaties. Since such a significant reduction in income would, as expected, negatively impact the financial results of these institutions, the vast majority of FFIs decided to cooperate with the IRS and undertake the additional reporting procedures mandated by FATCA. While the requirements of the law primarily focus on FFIs to

²⁴ Buetow, Bob. "Foreign Account Tax Compliance Act: What Domestic Financial Institutions Need to Know!" Wipfli LLP. Wipfli LLP, 1 March 2014. Web. 24 August 2015. <<http://www.wipfli.com/resources/images/40411.pdf>>.

²⁵ "FATCA Information for U.S. Financial Institutions and Entities." Internal Revenue Service. Internal Revenue Service, 29 May 2015. Web. 23 August 2015. <<http://www.irs.gov/Businesses/Corporations/FATCA-Information-for-United-States-Entities>>.

assist with combating tax evasion, the government has also created treaties with foreign nations to assist with the reporting process on a national scale.²⁶

E. International Cooperation

With each country having its own unique set of confidentiality and banking secrecy laws, FFIs in some of these jurisdictions could not cooperate with the IRS without breaking the those national laws. While the financial institutions obviously could not disregard them and definitely wanted to cooperate to avoid the penalties, the FATCA lawmakers realized that they would have work with foreign governments into making the reporting requirement legal. By getting governments proactively involved in the process, Congress was able to eliminate all obstacles once FATCA mandates became national responsibilities. As such, the Department of Treasury partnered with numerous foreign governments including some tax havens to combat tax evasion through treaties called inter-governmental agreements (IGA).

While the signing of treaties has been a commonplace resolution to a variety of global tax issues, the IGAs present in FATCA set a new precedent for international cooperation. They establish the grounds necessary for governments to exchange information about individual taxpayers and combat their tax evasion efforts through a network of allied states. Since some foreign nations have laws expressly prohibiting the disclosure of private information, it was necessary for them to amend their laws to incorporate the FATCA mandates. There are two different models of the cooperation agreements in which both IGAs necessitate that foreign governments will require FFIs operating within their jurisdictions to cooperate with the IRS. With the identification and reporting requirement becoming part of the national legal system, these financial institution do not possess any other options that to cooperate unless they have exempt status. As such, non-compliance with FATCA carries the 30% withholding penalty on U.S. source income and also includes the penalties associated with breaking the laws of the local jurisdiction.²⁷

Under the Model 1 IGA, the FFIs identify American accounts in accordance with FATCA's due diligence rules and report that information to the appropriate authority of the

²⁶ "The road ahead: An in-depth analysis of the temporary and Final FATCA Regulations incorporating Notice 2014-33." Deloitte. Deloitte, n.d. Web. 25 August 2015. <<http://www2.deloitte.com/content/dam/Deloitte/us/Documents/Tax/us-tax-FATCA-incorporating-notice-012215.pdf>>.

²⁷ "Foreign Account Tax Compliance Act (FATCA)." Out-Law. Pinsent Masons, 1 November 2014. Web. 1 September 2015. <<http://www.out-law.com/sectors/financial-services1/banks/foreign-account-tax-compliance-act-fatca/>>.

partner government, which then passes that information along to the IRS on an automatic basis. Whereas this involves the foreign authorities in the information exchange, Model 2 stipulates that FFI have to report the taxpayers' information directly to the IRS without the need for any other parties to be involved in the process. While under both Model 1 and Model 2 the FFIs are obligated by their local law to cooperate with the FATCA reporting procedures, Model 1 sets up the stage for international cooperation in developing a worldwide tax reporting system.²⁸

While the reported information has value to the IRS, the widespread international cooperation creates a network of allied nations that is more efficient in reducing tax evasion. The Department of Treasury has signed over 70 IGAs and reached an agreement in substance with almost 40 additional foreign governments. With the notable exceptions of Austria, Bermuda, Hong Kong, Japan and Switzerland among others, the vast majority of foreign tax authorities opted to cooperate with the IRS under the Model 1 IGA. Cooperation under this particular IGA is especially advantageous for these nations, because the United States agreed to a reciprocal version termed Model 1A that enables the U.S. to share information about the taxpayers of the partner country. This reporting reciprocity incentivizes foreign nations to cooperate with the U.S., because they can institute their own tax evasion prevention programs similar to FATCA with access to the account information from the U.S. Since countries that are traditionally opposed to U.S. global initiatives such as Russia or China, and renowned tax havens such as Cayman Islands or Hong Kong decided to cooperate with the Americans, there do not exist many other places with the necessary laws and accounting standards to make tax evasion a viable alternative for certain taxpayers. With their options for offshore banking now limited, potential tax evaders either have to come up with new schemes or comply with the IRS.²⁹

While FATCA relies on international cooperation to prevent tax evasion by individual taxpayers, it is not the first program to address proper tax compliance on a global level. The Organisation for Economic Co-operation and Development (OECD), an international body primarily composed of Western countries, has been working to address the problem of Base Erosion and Profit Shifting (BEPS). On October 5 2015 the OECD finished its action plan that identified 15 key areas that need to be addressed to prevent multinational corporations from

²⁸ "FATCA Information for Governments." Internal Revenue Service. Internal Revenue Service, 6 April 2015. Web. 1 September 2015. <<http://www.irs.gov/Businesses/Corporations/FATCA-Governments>>.

²⁹ "Intergovernmental Agreement." Thomson Reuters. Thomson Reuters, 16 July 2014. Web. 5 September 2015. <<http://fatca.thomsonreuters.com/about-fatca/intergovernmental-agreement/>>.

manipulating global tax loopholes to avoid paying tax. Since the release, leaders of G-20 countries have endorsed the program and agreed to take the first steps to enact its precepts by 2017. While this program focuses on tax avoidance by multinational corporations, it shows that international cooperation is an effective tool that can have a positive impact to correct taxation issues.³⁰

F. Implementation

While FATCA represents years of cumulative efforts by legislators to combat tax evasion, the mandates of the law have only gradually been coming into effect over the past four years. The implementation of the law has been occurring in separate stages designated for domestic and foreign financial institutions with different deadlines for the registration, reporting and withholding components. According to Exhibit B, in 2014 the IRS opened its systems for FFIs to register and receive a Global Intermediary Identification Number (GIIN). Although the deadline for registration was May 5, FFIs in jurisdictions with Model 1 IGAs with the U.S. received more time to complete this part due to the involvement of their local governments in the process. With the first monthly Registered FFI list published on June 2, the penalty component by the withholding agents came into effect only a month later on July 1. Because the deadline to register with the IRS already passed, the 30% withholding tax applied to any FFIs not listed in the agency's monthly list. This first stage of the process was intended to establish the cooperation of governments and FFIs before the actual reporting could happen. 2014 marked the implementation of the reporting requirement with information from FFIs in non-IGA jurisdictions and FFIs in Model 2 IGA jurisdictions due on March 31 and that from FFIs in Model 1 IGA jurisdictions six months later on September 30. The required information at the beginning of the process included only the basic account information already required on the FBAR such as the owner's name, address, account number and balance. However, starting in 2016, all FFIs will also be required to individually report any income paid to the account, which will form the basis of how much tax the account holders will have to pay to the IRS that year.³¹ While this gradual implementation of FATCA prevents its financial effects from being promptly

³⁰ Cohn, Michael. "G20 Leaders Endorse OECD BEPS Tax Reforms." Accounting Today. Accounting Today, 17 November 2015. Web. 9 December 2015.

<<http://www.accountingtoday.com/news/tax-practice/g20-leaders-endorse-oecd-beps-tax-reforms-76442-1.html>>.

³¹ "Summary of FATCA Timelines." Internal Revenue Service. Internal Revenue Service, 13 April 2015. Web. 4 September 2015. <<http://www.irs.gov/Businesses/Corporations/Summary-of-FATCA-Timelines>>.

recognized, the law will bring about significant long-term changes to both American and global taxation.

IV. Significance of FATCA

A. Importance for Global Taxation

While ultimately the primary intent of FATCA was to increase the tax revenue collected by the IRS, its less obvious effects definitely eclipse the financial significance of the law for the federal government. Chief among those is that it represents the first step necessary for the creation of a global tax system based on cooperation of nations focused on eliminating tax evasion and enforcing proper tax compliance. While it may at first seem that the mandates of the law create excessive burden for foreign financial institutions, the mandatory cooperation with the IRS ensures that the process of international tax system convergence actually takes place. As opposed to a voluntary initiative through which some countries could decide against participating, FATCA's compulsory nature ensures that uncooperative nations do not defeat the practicality of the project. If this global tax system were to originate as a multinational effort of like-minded governments, existing tax havens would feel no need to comply and tax evasion would continue just as freely as before. However, since the success of the project depends upon complete global cooperation, the existence of tax havens in their current form remains difficult in the future under the mandates of FATCA. With the possibility of sanctions on their local financial institutions or the prospect of information reciprocity, these jurisdictions recognize that cooperation inherently represents the more beneficial alternative in the long run. While this may seem like policing the world through a carrot or stick approach, the U.S. is simply the only world power capable of ensuring the cooperation of other nations through its unrivaled economic and financial infrastructure.³²

Because the success of a global tax system is contingent upon the cooperation of all countries across the world, FATCA is the first step in the creation process of such a system. With over 100 countries guaranteeing their cooperation with the IRS under the reciprocity directives of the IGAs, the overwhelmingly positive response indicates that foreign governments recognize the benefits associated with being part of this new initiative. Even though FATCA places the FFIs within the control of the IRS, these governments decided to partake in the information

³² "FATCA Frequently Asked Questions (FAQs)." Deloitte. Deloitte, n.d. Web. 18 November 2015. <<http://www2.deloitte.com/content/dam/Deloitte/us/Documents/Tax/us-tax-fatca-faqs-2013-43-081213.pdf>>.

exchange, since they can increase their tax revenues as well as obtain information about their taxpayers living in the U.S. While the cooperation of Western nations could have been reasonably expected, FATCA's global reach becomes more impressive once it is recognized that countries such as Russia or China have already signed up for the program. These nations do not typically contribute to multilateral initiatives by the U.S. and its allies, and in some situations even try to publicly undermine those efforts. However, in the case of taxation, all nations, regardless of their alliances, have a common goal of preventing tax evasion and recognize that working together with other nations will make that goal more attainable. Subsequently, all governments desiring to limit what revenue they lose to tax haven abuse will naturally support the creation of a global tax system, which is the only way of effectively accomplishing such an objective. As follows, the existing tax havens would have no choice but to agree to the program under the increasing pressure just as Switzerland and the Cayman Islands have already done.³³

While the mandates of FATCA will only come into full effect starting in 2016, there already exists a framework for a more formal and automatic process of exchanging information among countries. Introduced on October 29, 2014 as the Automatic Exchange of Information on Financial Accounts, the agreement builds on FATCA's policies and procedures to make the exchange process not so centered on the U.S. It creates a single global standard referred to as the Common Reporting Standard (CRS) through which information can be exchanged automatically between countries and not just upon request in cases of criminal investigations involving taxation. Aside from the modified international structure, the mechanism behind the law remains largely similar to the one already developed for the benefit of the United States in FATCA. The comparable account and information requirements in the two laws are very comparable, but withholding penalties for non-compliance are obviously absent from the CRS. While it may seem that CRS is a voluntary initiative that cannot succeed, it can be thought of as both a continuation and extension of FATCA, which created the environment necessary for such an agreement to be reached among those nations in the first place. While the exchange of information under the CRS will begin in 2017 among the starting 56 jurisdictions, the program will expand in 2018 to encompass more than 100 countries. Because FATCA demonstrates the

³³ "Swiss banks suddenly preach transparency in U.S. tax evasion endgame." Financial Post. Financial Post, n.d. Web. 18 November 2015. <<http://business.financialpost.com/news/fp-street/swiss-banks-suddenly-preach-transparency-in-u-s-tax-evasion-endgame>>.

benefits of cooperation, the CRS most likely will gain momentum in the future by involving even more countries.³⁴

B. Importance for Domestic Taxation

Tax code reform has become a major aspect of the political debate with some individuals even going as far as to call for a complete abolishment of the IRS. Although the great variety of reform proposals from both the liberals and conservatives always target the simplification of the code, increased regulation through laws such as FATCA makes it clear that the objective should not be to make the code simple, but rather to make it more efficient and effective. By increasing the rules for individual reporting of income, FATCA ensures an increase in the extent of compliance with the tax code and guarantees that the government receives its appropriate share of taxes. While the law specifically focuses on collecting taxes only from individuals with certain foreign accounts, the principles as well as the procedures from this one tax area can help to revamp the code for dealing with other types of taxpayers. Therefore, claims that FATCA unnecessarily complicates the already highly complex tax code do not consider the basis from which this piece of legislation can help the reform process in the future.

Although some provisions of the law might indeed seem redundant or too liberal in scope, one cannot argue that the framework for increasing compliance is not far superior to the system that it was designed to improve upon. Over the last century the policy regarding taxation of taxpayers with foreign assets has systematically become more complex with introduction of new laws and compliance only became more effective with each iteration. As such, the introduction of FATCA, while groundbreaking in several distinct areas, can nonetheless be considered as the modern update to the code in this continuous process of improvement. Similarly, reform proposals for the entire tax code should be broken down into sections, which focus on solving specific problems like FATCA does to the ones persistent in taxation of foreign accounts.

Since FATCA introduces several additional components into the taxation of foreign accounts, the IRS's proper administration of the reporting program with FFIs will be crucial to the law's success. The agency performs a crucial role in the administration of the tax regime and

³⁴ "Automatic Exchange of Information on Financial Accounts." TheBanks.eu. TheBanks.eu, 3 November 2014. Web. 19 November 2015. <<https://thebanks.eu/articles/automatic-exchange-of-information-on-financial-accounts>>.

will only expand once FFIs across the world begin reporting the accounts of American taxpayers. This stream of information will need to be efficiently processed and appropriate steps will have to be taken by the IRS to deal with tax evading individuals. Therefore, the integral role of the IRS in this process will increase the scope of the agency's actions and will most likely necessitate additional resources from the federal budget. Since the improvement in the quality of information will undoubtedly increase tax return examinations conducted by the agency, enforcement of the tax code will become a more substantial endeavor that will need more attention by the IRS. In the scope of FATCA itself, the IRS receives more authority on an international basis by being able to request more information from FFIs as well as require their cooperation with any potential investigations. With the emergence of CRS, the tax authorities of participating countries including the IRS will play a more significant role in how their respective governments conduct their operations. Therefore, due to its experience with the provisions of FATCA, the IRS can serve as model for foreign tax agencies, which will need to implement its own reporting and enforcement frameworks.³⁵

IV. Criticism of FATCA

While FATCA became law without significant legislative setbacks due to the Democratic control of Congress, the law has been consistently facing severe criticism from its opponents. Some individuals have started to question whether the cost of the entire reporting procedure is worth the incremental increase in tax revenue for the government, because the program necessitates the creation of additional administrative functions that will add to the burden on the federal budget. Critics claim that the any additional revenue in the short term would be offset by the increased expenditures, leading the law to provide no net tax benefit. Additionally, these critics also say that if FATCA does not undergo amendment, the U.S. financial markets will lose capital due to foreign investors withdrawing their funds from the reach of the IRS. Capital flight is possible, but due to America's position as the center of the business world, it seems unlikely that foreign investment would move elsewhere solely due to changes in the tax code. However, other critics have taken a more theoretical approach by claiming that FATCA's intrusive nature constitutes a violation of rights for Americans taxpayers. They believe that with the additional

³⁵ "Offshore Financial Activity Creates Enforcement Issues for IRS." United States Government Accountability Office. United States Government Accountability Office, 17 March 2009. Web. 20 November 2015. <<http://www.finance.senate.gov/imo/media/doc/031709mbtest1.pdf>>.

reporting mandate by FFIs, American expatriates living and working abroad will be subject to unfavorable treatment due to the reporting obligations of institutions doing business with U.S. taxpayers. Certain taxpayers have started to report that due to FATCA's additional compliance costs for FFIs, they either had their financial accounts closed or experienced substantial difficulty opening new ones. This discrimination, caused indirectly by the actions of the U.S. government, has even forced some individuals to take the extreme step of renouncing their citizenship to forever limit their exposure to the far-flung reach of the IRS. While FATCA's mandates do not go into effect until 2016, in 2014 3,415 former U.S. taxpayers have decided to separate their ties with their native land.³⁶ In light of these drawbacks, the Republican National Committee in the U.S. and the Alliance for the Defence of Canadian Sovereignty (ADCS) in Canada have made efforts to obstruct the approval of FATCA over the last few years. These actions, however, have not achieved much success in their respective legal systems, because the law remains on course to take effect in its original form as originally scheduled.^{37 38}

While overall it may seem that these drawbacks of FATCA make it impractical, they have to be compared to the law's positive long-run effects when evaluating its utility. With the reporting and withholding requirements beginning in 2016, it might take some time to notice FATCA's ability to decrease tax evasion. The law builds the foundation on which a global tax system will develop that will limit tax evasion on a worldwide basis through inter-governmental cooperation. If the CRS succeeds at eliminating the majority of tax evasion schemes currently found in tax havens, it will not only return to governments their tax revenue, but also to a certain extent make it substantially more difficult for criminal organizations to conduct their illegal operations. With efforts to eradicate drug dealing, human trafficking or arms trading clearly not having the desired approach when battled directly, perhaps the introduction of FATCA and the CRS represent an appropriate opportunity to finally change the approach. Ultimately, the negative effects of

³⁶ "Taking the IRS to Court." The Wall Street Journal. The Wall Street Journal, 20 August 2015. Web. 20 November 2015. <<http://www.wsj.com/articles/taking-the-irs-to-court-1440114086>>.

³⁷ Temple-West, Patrick. "Republican Urge Congress to Repeal Anti-Tax Dodging Law." Huffington Post. Reuters, 26 March 2014. Web. 20 November 2015. <http://www.huffingtonpost.com/2014/01/24/rnc-anti-tax-evasion-law_n_4661102.html>.

³⁸ Wood, Robert W. "Canadians File Suit To Block FATCA And Prohibit Handover Of U.S. Names To IRS." Forbes. Forbes, 12 August 2014. Web. 20 November 2015. <<http://www.forbes.com/sites/robertwood/2014/08/12/canadians-file-suit-to-block-fatca-and-prohibit-handover-of-u-s-names/>>.

FATCA are a small price to pay compared to benefits of limiting of tax evasion in addition to fostering cooperation between governments in the long-run.

V. Conclusion

After decades of efforts aimed at limiting revenue losses stemming from tax evasion, the federal government finally came up with a solution that is its best opportunity to eradicate the illegal activity. While FATCA can be criticized for being too complex and burdensome, the many benefits of the law that will come to their full potential in the future undoubtedly make it a net positive initiative to prevent tax evasion. While undoubtedly new tax evasion schemes will emerge in the future, FATCA's mandates bring the world of global taxation into a new era of international cooperation. The convergence of taxation systems worldwide signifies that governments are changing their approach toward how they collect tax revenue in face of challenges of the modern time. Since inevitably the Common Reporting Standard will gain momentum once FATCA takes firm hold, the evolution of global taxation will continue to progress with new significant improvements taking effect along the way.

Exhibit A – Comparison of FATCA Form 8938 and FinCEN Form 114

	Form 8938, Statement of Specified Foreign Financial Assets	FinCEN Form 114, Report of Foreign Bank and Financial Accounts (FBAR)
Who Must File?	Specified individuals, which include U.S. citizens, resident aliens, and certain non-resident aliens that have an interest in specified foreign financial assets and meet the reporting threshold	U.S. persons, which include U.S. citizens, resident aliens, trusts, estates, and domestic entities that have an interest in foreign financial accounts and meet the reporting threshold
Does the United States include U.S. territories?	No	Yes, resident aliens of U.S. territories and U.S. territory entities are subject to FBAR reporting
Reporting Threshold (Total Value of Assets)	\$50,000 on the last day of the tax year or \$75,000 at any time during the tax year (higher threshold amounts apply to married individuals filing jointly and individuals living abroad)	\$10,000 at any time during the calendar year
When do you have an interest in an account or asset?	If any income, gains, losses, deductions, credits, gross proceeds, or distributions from holding or disposing of the account or asset are or would be required to be reported, included, or otherwise reflected on your income tax return	Financial interest: you are the owner of record or holder of legal title; the owner of record or holder of legal title is your agent or representative; you have a sufficient interest in the entity that is the owner of record or holder of legal title.
What is Reported?	Maximum value of specified foreign financial assets, which include financial accounts with foreign financial institutions and certain other foreign non-account investment assets	Maximum value of financial accounts maintained by a financial institution physically located in a foreign country
How are maximum account or asset values determined and reported?	Fair market value in U.S. dollars in accord with the Form 8938 instructions for each account and asset reported Convert to U.S. dollars using the end of the taxable year exchange rate and report in U.S. dollars.	Use periodic account statements to determine the maximum value in the currency of the account. Convert to U.S. dollars using the end of the calendar year exchange rate and report in U.S. dollars.
When Due?	By due date, including extension, if any, for income tax return	Received by June 30 (no extensions of time granted)
Where to File?	File with income tax return pursuant to instructions for filing the return	File electronically through FinCEN's BSA E-Filing System. The FBAR is not filed with a federal tax return.
Penalties	Up to \$10,000 for failure to disclose and an additional \$10,000 for each 30 days of non-filing after IRS notice of a failure to disclose, for a potential maximum penalty of \$60,000; criminal penalties may also apply	If non-willful, up to \$10,000; if willful, up to the greater of \$100,000 or 50 percent of account balances; criminal penalties may also apply

Source: <https://www.irs.gov/Businesses/Comparison-of-Form-8938-and-FBAR-Requirements>

Exhibit B – Summary of FATCA Timelines

Withholding (by withholding agents)

2014

July 1 30% U.S. withholding tax will apply to payments of certain U.S. source income (e.g., dividends, interest, insurance premiums) made to non-U.S. financial institutions (FFIs) ... **UNLESS** FFI establishes **by registration** it is

- A participating FFI, including FFIs in Model 2 IGA,
- An FFI in a jurisdiction with a Model 1 IGA treated as in effect, or
- A low-risk FFI

2019

January 1 30% U.S. withholding tax will apply to any gross proceeds from the sale or other disposition after December 31, 2018 of any property of a type that can produce the U.S. source income described above.

TBD U.S. withholding tax will apply to foreign passthru payment to a recalcitrant account holder or a nonparticipating FFI that is made after the later of December 31, 2018 or the date of the publication of final Treasury Regulations defining the term foreign passthru payment.

Exception: Certain smaller and more local FFIs and exempt beneficial owners (primarily government-owned entities and international organizations) can avoid withholding if they provide the withholding agent with documentation about their status.

Registration (by financial institutions)

2013

August 19 Registration website available for testing purposes only

2014

January 1 Official opening date to register and obtain Global Intermediary Identification Number (GIIN)

May 5 Final day to register for guaranteed inclusion on first registered FFI list (to avoid withholding)

June 2 First Registered FFI list published – updated monthly thereafter

2016

January 1 All limited FFI and limited branch registrations will be placed in registration incomplete status on their online FATCA account after December 31, 2015. Limited FFIs and limited branches that seek to continue such status during the 2016 calendar year must edit and resubmit their registrations after December 31, 2015, on the FATCA registration website.

December 31 Sponsoring entities must register their sponsored investment entities and sponsored controlled foreign corporations (CFCs) covered by Annex II of a Model 1 IGA on or before the later of December 31, 2016, and the date that is 90 days after a U.S. reportable account is first identified.

Sponsoring entities must register their sponsored investment entities and sponsored CFCs covered by Annex II of a Model 2 IGA on or before December 31, 2016.

2017

January 1 Sponsoring entities must register their sponsored registered deemed-compliant FFIs and sponsored direct reporting NFFEs by January 1, 2017. Sponsoring entities should consider registering to obtain GIINs well in advance of January 1, 2017, in order to give withholding agents sufficient time to complete the verification requirement.

Exhibit B (Continued) – Summary of FATCA Timelines

Withholding (by withholding agents)

2014

July 1 30% U.S. withholding tax will apply to payments of certain U.S. source income (e.g., dividends, interest, insurance premiums) made to non-U.S. financial institutions (FFIs) ... **UNLESS** FFI establishes **by registration** it is

- A participating FFI, including FFIs in Model 2 IGA,
- An FFI in a jurisdiction with a Model 1 IGA treated as in effect, or
- A low-risk FFI

2019

January 1 30% U.S. withholding tax will apply to any gross proceeds from the sale or other disposition after December 31, 2018 of any property of a type that can produce the U.S. source income described above.

TBD U.S. withholding tax will apply to foreign passthru payment to a recalcitrant account holder or a nonparticipating FFI that is made after the later of December 31, 2018 or the date of the publication of final Treasury Regulations defining the term foreign passthru payment.

Exception: Certain smaller and more local FFIs and exempt beneficial owners (primarily government-owned entities and international organizations) can avoid withholding if they provide the withholding agent with documentation about their status.

Registration (by financial institutions)

2013

August 19 Registration website available for testing purposes only

2014

January 1 Official opening date to register and obtain Global Intermediary Identification Number (GIIN)

May 5 Final day to register for guaranteed inclusion on first registered FFI list (to avoid withholding)

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January 1 All limited FFI and limited branch registrations will be placed in registration incomplete status on their online FATCA account after December 31, 2015. Limited FFIs and limited branches that seek to continue such status during the 2016 calendar year must edit and resubmit their registrations after December 31, 2015, on the FATCA registration website.

December 31 Sponsoring entities must register their sponsored investment entities and sponsored controlled foreign corporations (CFCs) covered by Annex II of a Model 1 IGA on or before the later of December 31, 2016, and the date that is 90 days after a U.S. reportable account is first identified.

Sponsoring entities must register their sponsored investment entities and sponsored CFCs covered by Annex II of a Model 2 IGA on or before December 31, 2016.

2017

January 1 Sponsoring entities must register their sponsored registered deemed-compliant FFIs and sponsored direct reporting NFFEs by January 1, 2017. Sponsoring entities should consider registering to obtain GIINs well in advance of January 1, 2017, in order to give withholding agents sufficient time to complete the verification requirement.

Source: <https://www.irs.gov/Businesses/Corporations/Summary-of-FATCA-Timelines>

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