U.S. Foreign Account Tax Compliance Act (FATCA) and Non-U.S. Long-Term Benefits Programs

February 2014

Briefing Agenda

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FATCA Background

U.S. Congressional Action:

- The U.S. taxes worldwide income (absent a specific exemption or tax treaty provision, U.S. persons are taxed on income arising in a foreign country)
- Individual U.S. taxpayers must file an income tax return annually regardless of where they reside
- Congress was concerned that U.S. taxpayers were not fully reporting income from foreign financial assets
- As a result, FATCA was enacted in 2010 as Chapter 4 of Subtitle of the Internal Revenue Code

What FATCA does:

- Requires U.S. taxpayers who have financial assets offshore to report such assets
- Requires non-U.S. “financial institutions” to provide information for the Internal Revenue Service that identifies U.S. owners of “foreign financial accounts”
- “Encourages” compliance by means of a 30% withholding tax on certain income from U.S. sources

Focus of FATCA:

FATCA largely focuses on **Foreign Financial Institutions** (FFIs):

- Funds (including fund management entities)
- Banks, investment managers and brokerage accounts
- Insurance companies (and captive insurers)
- Other intermediaries including custodians and insurance brokers

FATCA Background

FATCA's Goal:

FATCA's goal is to set up and operate a process to require U.S. taxpayers to report their specified foreign financial assets, verified by the relevant FFIs, by:

- expanding the U.S. domestic "two-strand" tax reporting process globally; and
- persuading other countries to join the U.S. (and reduce global tax "leakage")

FATCA Two-Strand Reporting:

FATCA requires reporting:

- Individual Strand—U.S. taxpayers report their foreign financial accounts and financial assets
- Program Strand—FFIs report the non-U.S. financial accounts of their U.S. taxpayer clients (or non-U.S. entities where U.S. taxpayers hold a substantial ownership interest)

Impact on Multinational Corporations' (MNCs') Long-Term Benefit plans:
Non-U.S. Long-Term Benefits programs are potentially subject to FFI reporting:

- Retirement and savings programs plus deferred compensation and bonus programs
- Cash-value life insurance benefits and annuities (immediate and/or deferred)
- Certain other Long-Term Benefits (e.g., non-U.S. stock programs and long-term incentive programs)

FATCA Background

<u>Non-U.S. Long-Term Benefits programs of MNCs may be subject to FFI reporting</u>
(irrespective of whether they include any participants who are U.S. taxpayers)

- A non-compliant (i.e., non-exempt and not registered) FFI will be subject to **withholding tax at the rate of 30%** on U.S.-source investment income
- In order to avoid/minimize this substantial tax on U.S. investments, MNCs should **check the FATCA status** of their benefits programs (including financing vehicles and service providers)
- Tax withholding under FATCA becomes effective **July 1, 2014**. The current deadline for registration with the IRS (if required) is April 25, 2014. A timely registered FFI will not be subject to the 30% withholding tax, nor will any program that qualifies as exempt under FATCA

Inter-Governmental Agreements (IGAs) with the USA

An IGA is an agreement between the USA and a local “partner” country, as to how FATCA is to apply in the local “partner” country.

An IGA...

- ...is a supplement to (and may provide more specificity than) the general regulatory guidance under FATCA
- ...helps to reduce the burden of FATCA reporting for FFIs in the local country
- ...addresses legal/ data protection constraints that may exist regarding sharing financial information with the IRS

There are two different models for IGAs:

- **Model 1** IGA—The local taxing authority will gather information from local non-exempt FFIs and will deliver it to the IRS (The local authority may receive reciprocal information from the IRS)
- **Model 2** IGA—Each local non-exempt FFI is authorized to report information directly to the IRS

22 IGAs have been finalized: UK, Denmark, Mexico, Ireland, Switzerland, Norway, Spain, Germany, Japan, France, Costa Rica, Cayman Islands, Guernsey, Isle of Man, Jersey, Netherlands, Malta, Bermuda, Mauritius, Italy, Hungary and Canada

Bermuda, Japan and Switzerland are Model 2. The other IGAs are Model 1.

IGAs are being negotiated between the U.S. and additional countries.

FATCA Regulations—FFI Exclusions for Non-U.S. Benefits Plans

The following Non-U.S. Benefits Plan categories are excluded from FFI reporting:

1. **Retirement Savings Accounts—A retirement account that satisfies <u>all</u> of the following:**
   - Subject to regulation as a personal retirement account or is part of a regulated retirement plan.
   - Tax-favored in the local country.
   - Annual information reporting is required to the local tax authorities.
   - Withdrawal of benefits only on reaching a specific age or event (death/disability). Penalties otherwise apply.
   - Per person annual contributions limited to $50,000 (or a lifetime limit not exceeding $1,000,000).

   May also include rollovers

2. **Non-Retirement Savings Accounts—An account that satisfies <u>all</u> of the following:**
   - Subject to regulation as a savings vehicle for purposes other than retirement.
   - Tax-favored in the local country.
   - Withdrawals from the account are conditioned on meeting specific criteria related to the purpose of the account (e.g., health care costs or tuition costs). Penalties otherwise apply.
   - Per person annual contributions limited to $50,000.

   May also include rollovers

FATCA Regulations—FFI Exemptions for Non-U.S. Benefits Plans

The following Non-US Retirement Plans are exempt from FFI reporting:

Exempt Beneficial Owners—six categories:

1. Treaty-qualified retirement funds—entitled to tax exemption on U.S.-source income under a U.S. Double Tax Agreement
2. Broad participation retirement funds—no beneficiary owns >5%of plan assets and the plan is government-regulated with annual information reporting on its beneficiaries provided to local tax authorities, plus one of the following needs to apply:

   i) The plan is generally exempt from tax on investment income due to its status

   ii) The plan receives at least 50% of its total contributions (other than transfers of assets from other plans) from its sponsoring employers

   iii) Distributions or withdrawals from the plan are allowed only upon specified events related to retirement, disability, or death. Penalties apply to distributions or withdrawals made beforehand

   iv) Contributions (other than certain permitted make-up contributions) for employees are limited, based on the employee's earned income and do not exceed U.S. $50,000 annually

FATCA Regulations—FFI Exemptions for Non-U.S. Benefit Plans

The following Non-US Retirement Plans are exempt from FFI reporting:

3. Narrow participation retirement funds—fund has fewer than 50 participants if <u>all of the following</u> apply:
   - i) plan is not sponsored by investment entities or passive NFFEs
   - ii) plan provides retirement, disability, or death benefits to current or former employees of one or more employers
   - iii) employee and employer contributions to the plan (other than qualifying rollovers) are limited by reference to earned income and compensation of the employee
   - iv) no more than 20% of participants are resident offshore
   - v) plan is government-regulated with annual information reporting on its beneficiaries provided to local tax authorities
4. Investment vehicles that are exclusively available to exempt retirement funds
5. Funds that would qualify under IRC Section 401(a) except that they are based outside the U.S.
6. Retirement plans of governments or international organizations

FATCA U.S. Reporting & Disclosure

IRS Forms for FATCA compliance:

- Form W-9—Request for Taxpayer Identification Number and Certification
- Form W-8BEN—Certificate of Foreign Status of Beneficial Owner for United States Tax Withholding and Reporting (Individuals)
- Form W-8BEN-E—Certificate of Status of Beneficial Owner for United States Tax Withholding and Reporting (Entities)
- Form W-8EXP—Certificate of Foreign Government or Other Foreign Organization for United States Tax Withholding and Reporting
- Form 8957—Foreign Account Tax Compliance Act (FATCA) Registration
- Form 1042— Annual Withholding Tax Return for U.S. Source Income of Foreign Persons
- Form 1042-S—Foreign Person's U.S. Source Income Subject to Withholding

Beyond the retirement program analysis, including proper documentation and filings, employers should ensure and employ a successful internal system to identify global employees meeting the definition of U.S. persons under U.S. tax law.

W-8BEN-E Certificate of Status of Beneficial Owner for United States Tax Withholding (Entities)

May 23, 2013: IRS publishes new Form W-8BEN-E (in draft form)

- **The Form serves as a certification of filer's status as beneficial owners or payees of a payment for withholding tax purposes and also as to their status under the FATCA provisions as either payees or account holders of an FFI.**

- **Form Requirements & Representations**
  - Establishes that the entity receiving the payment (payee) is the beneficial owner of certain income as well as establishes the status of the beneficial owner
  - Addition of sections designed specifically for disregarded entities and branches receiving payments and the expected change to a capacity check box to match the Form W-8ECI and W-8EXP
  - Filers must select a "FATCA Status" out of 28 options
  - Signed under penalties of perjury

In order to obtain proper documentation, FFIs will likely request a copy of the documentation regarding status (e.g., Form W-8BEN-E). Employers, in turn, will likely request the FFI's GIIN number (to ensure they have documented verification of proper registration status with the IRS for those third-party providers).

FATCA Program-level Reporting

Due Diligence Required of a Reporting FFI

1. Existing accounts

- Electronic records check of existing accounts as of June 30, 2014, for any US indicia*(low-value accounts may be excluded).
- For high-value accounts ($1 million+), an additional paper records check is required.

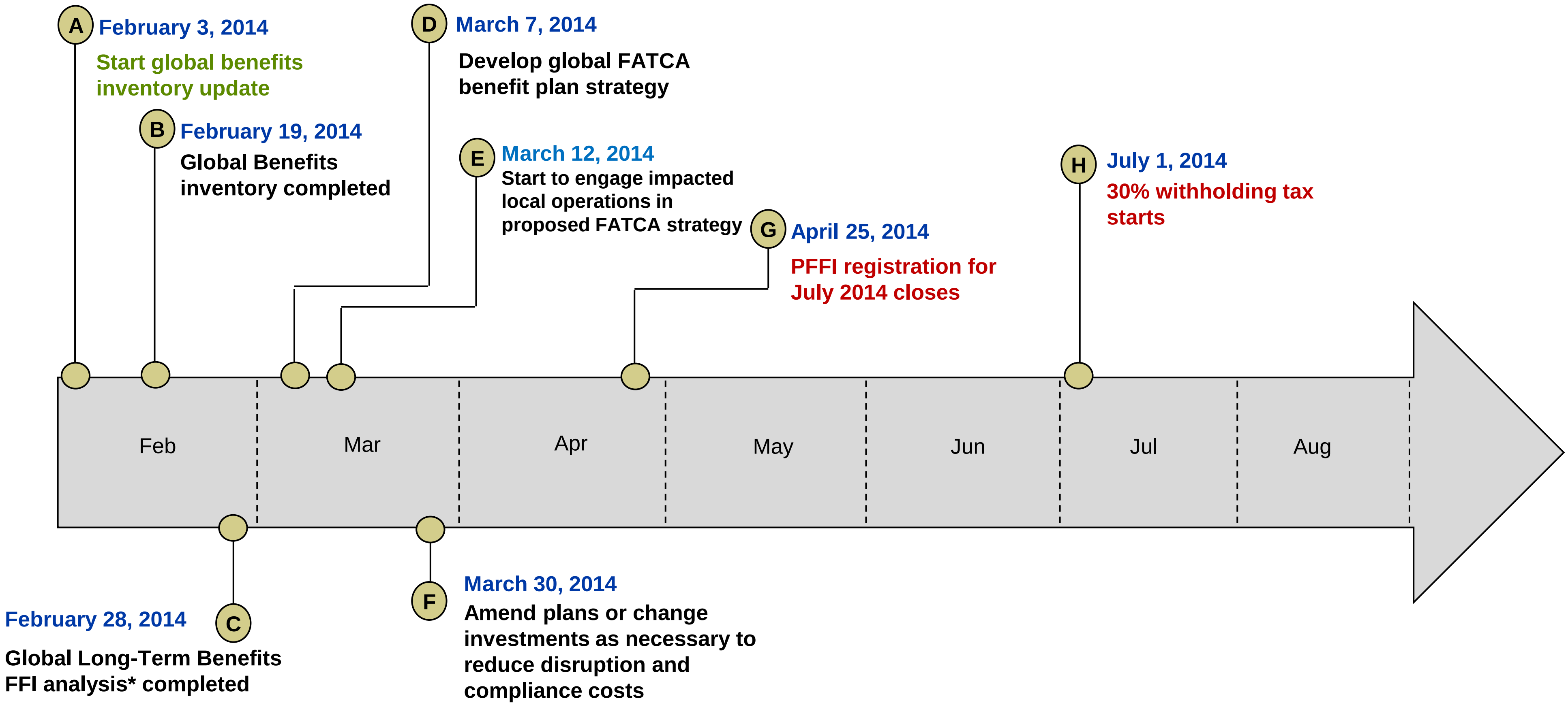
2. New accounts on or after July 1, 2014:

- Request information on U.S. taxpayer status at time the account is established.

*** An account holder has US indicia if he/ she:**

1. *Is known to be a U.S. citizen or a U.S. permanent resident (green card holder)*
2. *Was born in the U.S.*
3. *Has a current U.S. residence or mailing address*
4. *Has a current U.S. telephone number*
5. *Has provided standing instructions to transfer funds to a U.S.-based account*
6. *Has granted power of attorney over the account to a person with a U.S. address*
7. *Has a U.S. "care of" or hold mail address that is the sole known address of the account*

Sample FATCA Compliance Timeline for Benefits



*Analysis is:

1. Exempt/ non-reporting/ excluded?
2. Status currently uncertain —monitor/further analysis
3. Definitely non-exempt?

Recommended Actions

Issue	Detail	Recommendations
Determine and implement FATCA Benefits compliance strategy for employer-controlled entities, trusts etc.	The wide sweep of FATCA may include employer-sponsored long-term benefit plans, financing vehicles etc. in each jurisdiction outside the U.S.	▪ Make high-level analysis of benefit plans subject to FATCA ▪ Develop draft FATCA Benefits strategy (organize plans according to level of exposure) ▪ Finalize FATCA Benefits strategy (for sign-off by external advisors) and implement
Review FATCA compliance of service providers	To the extent that plan service providers are not FATCA-compliant, U.S.-source investment income is potentially subject to 30% withholding tax	▪ Implication on asset performance of benefit plans. ▪ Review/revise service provider agreements to address FATCA compliance
Individual-level reporting by U.S. expatriates (and executives) of non-U.S. accounts may be of concern to employer	Employer may wish to ensure that individual-level reporting requirements are complied with by its U.S. expatriates and any U.S. executives	▪ Employer should consider supporting expatriates and executives with regard to their individual reporting requirements

FATCA and Long-Term Benefit Plans–Suggested Compliance Process

Gather and review high-level information on long-term benefits plans worldwide

- Gather information on and create a comprehensive inventory of long-term benefits programs globally
- Categorize programs according to degree of exposure to FATCA
- Review the content of any applicable IGAs
- Analyze applicability of relevant regulatory exemptions and exceptions
- Assess FATCA exposure and whether an exemption/exclusion is applicable

Develop an optimal strategy for FATCA Benefits compliance

For each long-term benefit plan potentially subject to FFI reporting, determine:

- Expected FATCA status—exempt/excluded versus non-exempt
- If non-exempt, are there investments exposed to 30% withholding tax?
- If non-exempt, are there design changes to achieve exempt status or investment changes to minimize FATCA impact?
- If a plan needs to register, who will register the program on the IRS portal?

Secure assistance as necessary during the implementation process

- If a plan is exempt, prepare confirming documentation—(e.g., Form W-8BEN-E)—for each plan
- If a plan is to be redesigned, implement design changes
- If the investment options of a plan must be changed, determine other options
- If a plan needs to register with the IRS, go through the IRS registration process and prepare for IRS reporting
- Review consistency of individual reporting for U.S. expatriates and executives