

Global IRW Newsbrief

Information reporting and withholding (IRW)

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HM Treasury and HMRC release details outlining the implementation of FATCA in the UK

On 31 May 2013, HM Treasury and HMRC released the *International Tax Compliance (United States of America) Regulations 2013* ("UK Regulations") to implement the Agreement to Improve International Tax Compliance and to Implement FATCA and simultaneously released updated *Guidance Notes*.

The UK Regulations and Guidance Notes provide more clarity in respect of the legislation "*Draft Clauses & Explanatory Notes for the Finance Bill 2013*" published on the 11th December 2012 and what financial institutions within the UK will need to do in order to comply with the UK Regulations and in particular to identify and report 'specified US persons' from 1 January 2014.

This Newsbrief identifies key changes from the draft UK Regulations released in December and highlights relevant aspects of the associated Guidance Notes.

Background

The recent release follows a series of announcements which began with the joint announcement by the United States, France, Germany, Italy, Spain and the United Kingdom in February 2012 to intensify their co-operation in combating international tax evasion.

- 12 September 2012, the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the United States of America signed an *Agreement to Improve International Tax Compliance and to Implement FATCA (the "UK-US IGA")*.
- 18 September 2012, HMRC issued a consultative document to seek comments to enable legislation to be drafted which could be operated in the most efficient way by affected businesses.
- On 11th December 2012, HMRC published legislation as part of the *Draft Clauses & Explanatory Notes for the Finance Bill 2013*
- 18 December 2012, HM Treasury and HMRC released the draft *International Tax Compliance (United States of America) Regulations 2013* ("UK Draft Regulations") to implement the UK-US IGA and simultaneously released *draft guidance notes* and a *summary of responses to the consultation* which sought views on how the Government intends to legislate to deliver the commitments made in the UK-US IGA.

Key elements of the UK Regulations

1. Definition of a reporting Financial Institution

The UK Regulations generally retain the definitions of a UK reporting financial institution (“Reporting UK FI”) included in the draft UK Regulations with refinements in respect of the definition of a depository institution.

Based on the UK Regulations, HMRC will regard a person carrying out an activity that is a regulated activity for the purposes of the Financial Services and Markets Act 2000 by virtue of Article 5 of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (accepting deposits) or a person who is within paragraphs (a) to (e) or (h) to (j) of the definition of “electronic money issuer” in regulation 2(1) of the Electronic Money Regulations 2011 as a Depository Institution.

This definition includes entities regulated in the UK as a savings or commercial bank, a credit union, industrial and provident societies, building societies and pre-paid credit card as well as electronic issuers where credit balances can exceed \$50,000.

The Guidance Notes state that insurance brokers and solicitors would not be expected to be engaged in banking or similar business. However entities that solely provide asset based finance services or that accept deposits solely from persons as collateral or security pursuant to either a:

- sale or lease of property
- loan secured by property
- similar financing arrangement

between such entity and the person making the deposit with the entity, will not be considered a deposit institution. The UK regulations also clarify that the completion of a money transfers by instructing agents to transmit funds are not seen as accepting deposits.

The UK Regulations add holding companies directly or indirectly related to certain UK financial institutions (“Holding Company”), treasury companies of financial groups (“Treasury Companies”) and an entity that is managed by a financial institution and meets the financial assets test to the definition of a Reporting UK FI.

The Guidance Notes also address the inclusion of Trusts, Partnerships, a Central Securities Depository, Personal Investment Companies and Securitisation Vehicles within the definition of a Reporting UK FI.

PwC Observation: *The UK Regulations acknowledge that accepting deposits on its own does not meet the definition of a Depository Institution, the UK Regulations base the definition of a depository institution on the regulated activity of accepting deposits under the Financial Services and Markets Act 2000 but extend the definition to include certain pre-paid credit card and electronic money issuers who are exempt from the definition of a depository provider for the purposes Electronic Money Issuers Regulations 2011.*

The inclusion of an entity that is managed by a financial institution and meets a financial assets test in the investment entity definition is intended to clarify the fact that entities whose assets consist of non-debt direct interests in real property, even if managed by another investment entity would not be classified as a Reporting UK FI under the UK Regulations.

The Guidance Notes clarify the fact that:

- *a holding company, whose primary activity includes holding (directly or indirectly) all or part of the outstanding stock of one or more related entities that are Financial Institutions other than Holding Companies and Treasury Companies, is a Reporting UK FI; and*
- *treasury companies whose primary activity includes entering into hedging and financing transactions with or for Related Entities that are Financial Institutions are classified as Reporting UK FI while other treasury companies are non financial foreign entities (“NFFEs”).*

However, the inclusion of the UK-US IGA definition of an investment entity in the UK Regulations may conflict with the other definitions of an investment entity set out in the UK Regulations and Guidance Notes in respect of entities whose assets consist of non-debt direct interests in real property, Holding Companies and Treasury Companies.

Trusts are addressed in the Guidance Notes and will be dealt with under the investment entity definition with those that are managed by a Reporting UK FI being classified as a Reporting UK FI. Trusts which are not managed by an investment entity will be classified as a passive non financial foreign entity (“Passive NFFE”) with an obligation to identify controlling persons.

Partnerships and Personal Investment Companies will need to consider whether they are within the definition of an investment entity.

A Central Securities Depository (“CSD”) such as Euroclear UK & Ireland Limited is not required to undertake any reporting required by the UK-US IGA. Members of the CSD or the Reporting UK FI that accesses the CSD on their behalf are responsible for any reporting any securities held by means of CSD.

The Guidance Notes clarify the fact that the classification principles should be applied to each entity within a securitisation structure to determine whether or not an entity is a Reporting UK FI.

A securitisation structure may include an issuing entity, funding entity, seller, mortgage trustee and other counterparties. The expectation is that issuing entities are likely to be classified as Investment Entities on the basis of their activities, Trusts should be classified in accordance with the Trust principles set and holding and funding entities are likely be Financial Institutions in their own right. A securitisation vehicle that is a Financial Institution will need to consider if it has any Financial Accounts that may be reportable and if not, a nil return is required

It is important to note that the UK regulations incorporate various categories of deemed compliant and excepted FFI as set out in the US FATCA Regulations. This is achieved through the definition of a non reporting UK FI which includes the registered deemed compliant, certified deemed compliant and owner documented financial institution categories from the US FATCA Regulations.

In circumstances where an entity is classified as a registered deemed compliant FFI, the entity will be required to register with the IRS and in accordance with the UK-US IGA was classified as a non reporting UK FI. However, the UK Regulations stipulate that a non-reporting UK FI qualifies as a reporting financial institution where it is a registered deemed compliant financial institution and accordingly, has reporting obligations in respect of both Financial Accounts and payments to NPFFIs.

2. Financial Accounts and account holders

Under the UK-US IGA, Reporting UK FIs must provide information to HMRC on an annual basis in relation to Financial Accounts held by Specified US Persons or by a non-U.S. entity with one or more Controlling Persons that is a Specified U.S. person. In the UK-US IGA these are referred to as US Reportable Accounts. The categories of Financial Account are Depository and Custodial Accounts, Cash Value Insurance and Annuity Contracts or Equity and Debt Interests.

The UK Regulations retain the definition of a US Reportable Account maintained in the UK from the UK Draft Regulations together with the various exceptions in respect of accounts not required to be reviewed, identified or reported in accordance with the UK-US IGA.

The Guidance Notes also set out circumstances in which a Reporting UK FI needs to consider the type of account and the capacity in which it is held. For trusts, estates and partnerships, the Financial Account is held in the name of the respective trust, estate or partnership. In certain circumstances where a person other than a financial institution holds an account for the benefit of another person, agent, custodian, nominee, signatory, investment advisor or intermediary, then the person on whose behalf the account is held is the account holder.

The Guidance Notes clarify that intermediary accounts held by a Reporting UK FI for a non-Financial Intermediary (such as a firm of solicitors or estate agents) and established for the purposes of either, a court order, judgement or other legal matter on which the non-Financial Intermediary is acting on behalf of their underlying client or a sale, exchange, or lease of real or personal property subject to certain conditions are not Financial Accounts

The Guidance Notes provide clarification as to whether certain of types of collateral arrangement give rise to Financial Accounts. In particular, the Guidance Notes state that transactions which include the collection of margin or collateral on behalf of counterparty may fall within the definition of a Custodial Account. They also state that the Custodial Accounts definition includes arrangements pursuant to which an obligation exists to return cash or assets to another.

The inclusion of equity or debt interests within the definition of a Financial Account in an Investment Entity, Holding or Treasury Company is addressed in the Guidance Notes. The Guidance Notes also clarify the exemption from the definition of a Financial Account for debt or equity interests regularly traded on an established securities market.

The Guidance Notes provide rules around the treatment of cash value and annuity contracts as financial accounts.

Accounts held solely in the capacity as a personal representative of an estate, to fulfill the terms of an order or judgment made in legal proceedings, held to provide security for the performance of a party's obligation under a contract for the sale, exchange or lease of real or personal property in certain circumstances and escrow accounts have also been excluded from the definition of a US Reportable Account.

The treatment of undesignated, segregated and fully disclosed clearing and settlement arrangements is addressed in the Guidance notes.

The election in respect of those accounts not required to be reviewed, identified or reported under various thresholds has been amended to be a positive election to treat such accounts as not being reportable accounts.

The requirement to aggregate account balances in order to apply the various thresholds and to apply the currency conversion provisions of the UK-US IGA continue to apply.

PwC Observation: The inclusion in the Guidance Notes of circumstances where a person other than a financial institution holds an account for the benefit of another person, is intended to clarify the UK-US IGA definition of the account holder. The UK-US IGA definition of the account holder is the person listed or identified as the holder of a Financial Account by the Financial Institution that maintains the account. The clarification reflects the terms of the updated Model 1 IGA requiring Reporting UK FIs to look through certain entities.

The treatment of debt or equity interests as regularly traded on an established securities market as those listed on the London Stock Exchange, AIM and PLUS represents a significant simplification from the measurements required under the US FATCA Regulations.

The exclusion of accounts held in respect of estates, court orders, certain collateral arrangements and escrow accounts from the definition of a Reportable Account adds to the exemptions in respect of retirement accounts and products and certain other tax favoured accounts.

The Guidance Notes recognise the fact that the classification of collateral will depend on the legal terms under which the collateral is provided. However, further clarification may be required to confirm when margining arrangements and obligations to redeliver assets give rise to Custodial Accounts.

For example, stock lending transactions typically involve an obligation to redeliver “equivalent securities” at the end of the term of the transaction, with full title over the “loan securities” passing to the borrower for the term of the loan. Margin posted as collateral is usually held by counterparties for their own benefit as security under these arrangements. In both circumstances it is not clear on what basis such arrangements would meet the definition of a Custodial Account.

Responsibility for undesignated, segregated and fully disclosed clearing and settlement arrangements aligns with the principle that responsibility for the identification of the account holder rests with the party responsible for the anti money laundering and know your customer due diligence procedures.

The amendment from an election to forego the various threshold exceptions to a positive election to treat the accounts as not being Reportable Accounts is intended to resolve the potential conflicts of such an election with Data Protection legislation. The ability to make an election to treat the accounts as not being Reportable Accounts is a matter which should be considered by each Reporting UK FI and must be made on or before the reporting date for the calendar year in question. The form and rules in respect of such an election have yet to be clarified.

Reporting UK FIs should continue to pay careful attention to the rules that determine the way in which accounts must be aggregated for the application of various due diligence thresholds. These rules still require the aggregation accounts maintained by a Reporting UK FI and its related entities to the extent that computerised systems link the accounts by reference to a data element and allow the amounts to be aggregated. Accordingly, there is a potential requirement for aggregation to apply to accounts maintained by related entities outside the UK.

3. Collective Investment Vehicles

The UK Regulations provide that a collective investment vehicle includes an investment trust and a venture capital trust, unless the fund vehicle is not a “person” or is constituted as a “trust”. The Guidance Notes clarify that the only Financial Accounts that are relevant to the UK-US IGA are the Equity and Debt Interests in collective investment schemes including examples of platforms, nominees and advisory only distributors.

PwC observation: *A collective investment scheme that is not constituted as a person refers to legal persons and would include arrangements such as a Unit Trust. Accordingly, any reporting responsibilities in relation to the interests a collective investment scheme constituted as a person will be those of the collective investment scheme.*

The reporting responsibilities in relation to the interests a collective investment scheme not constituted as a person constituted as a person will be those of the manager or operator of the collective investment scheme.

4. Identification obligations for reportable accounts

The UK Regulations generally follow the identification provisions of the UK-US IGA and have been amended to accommodate the election to apply the relevant thresholds and to treat certain accounts as not being reportable accounts.

The UK Regulations include provisions to require a Reporting UK FI to maintain arrangements that are designed to establish the territory in which any account holder or controlling person is resident for income tax or corporation tax purposes or for the purposes of any tax imposed by the law of the territory that is of a similar character to either of those taxes, to retain evidence, to treat new accounts as pre existing accounts in certain circumstances and to share documentation.

The UK Regulations have replaced the provision in the Draft UK Regulations to allow the use of documentary evidence in situations where self-certification is required with an election for a Reporting UK FI to obtain evidence of a person’s US status. However, the Guidance Notes appear to conflict with the UK Regulations and offer an alternative for New Individual Accounts whereby documentary evidence may be used as an alternative to self certification.

PwC Observation: *The detailed requirements in respect of any self certification or similar agreed form to replace Forms w-9 or W-8 remain key considerations for the implementation process.*

The requirement to obtain documentation and the ambition to ensure that the information collected will support potential multi lateral information reporting need to be balanced with the customer experience in designing the customer due diligence processes. The inclusion of provisions in respect of the treatment of new accounts for pre existing account holders and documentation sharing may allow Reporting UK FIs to develop more efficient account holder documentation processes as opposed to following an account by account approach.

The election to obtain evidence of a person’s US status provides Reporting UK FIs with the ability to apply an indicia based approach limiting self certification to cases where US indicia are identified. The form of this election has yet to be determined.

5. Reporting obligations

The general reporting requirements in the UK Regulations follow the requirements set out in the UK-US IGA and have been amended to include reporting of the Reporting UK FI's Global Intermediary Identification Number ("GIIN"). The due date for reporting is 31 May of the year following the calendar year to which the return relates except for 2013 for which the due date is 31 March 2015.

PwC Observation: HMRC have retained the 31st May reporting deadline with a phased implementation in 2015 requiring reporting in respect of 2013 by 31 March 2015. The absence of any details in respect of the method of transmission and the format of the data to be transmitted is an area of considerable uncertainty in the UK Regulations and HMRC have stated that these are areas of ongoing discussion.

The requirement to report the GIIN indicates that Reporting UK FIs will be required to register through the IRS FATCA portal but it remains unclear what that process will entail. The portal is expected to open on 15 July 2013 and there is a significant amount of work required in order to obtain the registration information in respect of each Reporting UK FI and to identify sponsoring or lead FFIs for related FFI entities.

6. Reporting of 'Payments' to NPFFIs

The UK Regulations retain the requirement set out in the UK-US IGA for a Reporting UK FI to establish and maintain arrangements that are designed to identify payments which are made to a non-participating financial institution in the calendar year 2015 or 2016, whether the payment is made to a non-participating financial institution as an account holder or otherwise. The UK Regulations incorporate the reporting of amounts credited to a NPFFI and retain the exclusion from the definition of a payment any consideration given by the Reporting UK FI for the provision of goods or non-financial services to it.

PwC Observation: The exclusion of consideration given for the provision of goods or non-financial services means the payments to be reported are:

- a) non-US source interest paid on a Financial Account held by a NPFFI;
- b) non-US source dividends paid on a shareholding held in a Financial Account held by a NPFFI;
- c) payments to an NPFFI in connection with a securities lending transaction, sale-repurchase transaction, forward, future, option, swap, or similar transaction which are directly or indirectly contingent upon or determined by reference to, the payment of interest or a dividend from US sources; and
- d) non-US source payments, to a NPFFI, that are the proceeds or benefits of a cash value insurance contract or annuity contract.

Payments that do not need to be reported include payments:

- 1) for services, the use of property, office and equipment leases, software licenses, transportation, freight, gambling winnings, awards, prizes, scholarships, and interest on outstanding accounts payable arising from the acquisition of goods or services;

- 2) *where the Reporting UK FI has only a passive role in the payment process and so, alternatively either no knowledge of the facts that give rise to the payment or no control over the payment or no custody of the property which relates to the payment or does not have custody of property which relates to the payment;*
- 3) *capital markets payments in c) above that are not directly traceable to a US source; and*
- 4) *payments where the Reporting UK FI does not hold documentation to identify the payee as a NPFFI, unless the payee is a prima facie FFI.*

The requirement to report payments made to a NPFFI as an account holder or otherwise remains a significant challenge.

Further clarification may be required in respect of the payments to be reported. For example, the exclusion for capital markets payments appears to be restricted to certain types of transaction such that brokerage fees in connection with the purchase of shares may be reportable.

The inclusion of a prima facie FFI test in respect of payees where the Reporting UK FI does not hold documentation requires careful consideration in respect of the way in which a prima facie FFI will be identified.

It is also unclear whether reporting applies only to the direct recipients of payments or the concept of payee should be applied, for example where an NPFFI is a partner in a partnership receiving a payment.

Some actions to think about

With a little over a month until registration and 7 months until new account holders need to be taken on in a FATCA compliant fashion, stakeholders need to be working towards the implementation of FATCA compliant processes and procedures.

It appears that further changes will be forthcoming to both the UK Regulations and Guidance Notes with clarification still required in respect of any registration process, the method of transmission of data and the format of data to be reported while the details of account holder self certification are for the Reporting UK FI to determine. However, the scoping and due diligence obligations have been defined and decisions around the associated compliance approach need to be made in order to ensure that the implementation of those compliance procedures can proceed.

While any UK FATCA compliance regime or consideration of the Responsible Officer regime as set out in the proposed US FATCA Regulations has been excluded from the UK Regulations, Reporting UK FIs will still need to establish the process by which they will ensure that all in scope entities are compliant. This needs to be achieved in a way that ensures that costs and disruption to operations and customers are kept to a minimum.

For more information, please contact your usual PwC contact or any the following persons:

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