
Treasury and IRS provide additional extension to fully implement FATCA

September 22, 2015

In brief

With certain Foreign Account Tax Compliance Act (FATCA) transitional and reporting deadlines set to expire on September 30, 2015, December 31, 2015, and December 31, 2016, the Department of the Treasury (Treasury) and the Internal Revenue Service (IRS) published Notice 2015-66 (Notice) announcing their intention to provide additional time for withholding agents and foreign financial institutions (FFIs) to comply with certain aspects of FATCA. In addition to extending certain transition rules, the Notice describes the compliance timeline for jurisdictions that have signed or agreed in substance to a Model 1 intergovernmental agreement (IGA), but have not yet brought the IGA into force.

Specifically, Treasury and the IRS intend to amend the regulations under Chapter 4 (Sections 1471-1474) of the Internal Revenue Code by extending:

- The date for when withholding on gross proceeds and foreign passthru payments will begin;
- The period on the use of limited branches and limited FFIs; and
- The deadline for a sponsoring entity to register its sponsored entities and document such entities with withholding agents.

Finally, Treasury and the IRS also intend to modify the regulations for the treatment of collateral under the grandfathered obligation rule. The Notice specifies that taxpayers may rely on its provisions prior to Treasury and the IRS amending the regulations.

Observation: *The Notice specifically mentions the purpose of these provisions is to facilitate an orderly transition for withholding agents and FFIs regarding FATCA compliance. This approach has been followed by the government since the 2010 enactment of FATCA and it is expected that these extensions will come as welcome relief to many areas of the financial services industry.*

In detail

During the first three quarters of 2015, withholding agents have been busy implementing their FATCA documentation, due diligence, and reporting obligations. Many challenges associated with FATCA

reporting have been identified and resolved. However, there has been much anticipation of the guidance for registering sponsored FFIs, reporting requirements in IGA jurisdictions without current guidance, and the general approach and path forward

for requirements with January 1, 2016 effective dates. The Notice is welcome guidance for taxpayers and withholding agents working to comply with FATCA.

Issues related to IGAs that have not been brought into force

The Notice addresses situations where a partner jurisdiction has signed an IGA or reached an agreement in substance to enter into an IGA, but has not implemented local legislation and regulations to bring the agreement into force. In these situations, Treasury intends to treat FFIs covered by the incomplete IGA as compliant and not subject to FATCA withholding, so long as the partner jurisdiction demonstrates firm resolve to bring their respective IGA into force. The due date for these jurisdictions to report information under the IGA on September 30, 2015 has been extended to September 30, 2016, at which time all information related to both 2014 and 2015 is reportable.

Observation: Many stakeholders have been seeking guidance regarding the status of an IGA partner jurisdiction that did not collect FATCA reporting from local financial institutions (FIs) and provide this information to the US by September 30, 2015.

Sponsored FFIs

The current FATCA regulations requires sponsored FFIs to obtain their own global intermediary identification number (GIIN) prior to January 1, 2016. The Notice provides an additional transition year and permits withholding agents to rely upon withholding certificates provided by sponsored registered deemed-compliant FFIs (RDCFFIs) and sponsored direct reporting nonfinancial foreign entities (NFFE) that include only the sponsoring entity's GIIN until January 1, 2017.

For payments made after this date, withholding agents must obtain the GIIN of the RDCFFI or sponsored direct reporting NFFE in one of two

ways. One is by obtaining a new withholding certificate from the payee that includes its GIIN. The second permits a withholding agent that has a withholding certificate that includes the GIIN of the sponsoring entity to obtain oral or written confirmation of the payee's GIIN (such as by e-mail), which will be incorporated into withholding certificate. In either situation, the withholding agent will have 90 days from the date it obtains the GIIN to verify its accuracy against the published IRS FFI list.

In late 2015, the IRS expects to publish a user guide and unveil its streamlined process for sponsoring entities to register their sponsored entities on the IRS FATCA FFI registration website. Given that there are only three months remaining in 2015, the regulations will be amended to extend to January 1, 2017 the date for sponsoring entities to register their sponsored RDCFFIs and sponsored direct reporting NFFEs. Sponsored investment entities and sponsored controlled foreign corporations covered by Annex II of a Model 1 IGA will maintain their deemed-compliant status as long as they are registered by the sponsoring entity on or before the later of December 31, 2016 or the date that is 90 days after a US reportable account is first identified.

Observation: This extension follows guidance provided in August 2015 regarding the reporting schema to be used to complete bulk uploads of information. The asset management industry in particular utilized the sponsored entity status to manage the registration process. As a result, many (thousands) entities must be registered. Without the announced extension, these entities would need to be registered in a little over 90 days. Since the IRS has yet to release the guidance to register, additional time is welcome. With just over a year to complete the registration (based on

the revised timeline), the IRS must release guidance quickly in order to give withholding agents sufficient time to complete this requirement and avoid FATCA withholding.

Extension of time for withholding on gross proceeds and foreign passthru payments

FATCA's withholding requirements are being phased in over a number of years. Withholding on withholdable payments that are US source fixed, determinable, annual, or periodical (FDAP) income commenced on July 1, 2014 (with limited exceptions). Withholding on gross proceeds from the sale or other disposition of property that can produce US source interest or dividends was scheduled to commence on January 1, 2017 and withholding on foreign passthru payments was scheduled to commence no sooner than January 1, 2017. The Notice indicates that the start date of withholding on gross proceeds will be extended two years to January 1, 2019. The Notice also indicates that a participating FFI (PFFI) will not be required to withhold on a foreign passthru payments before the later of January 1, 2019 or the date of publication in the Federal Register of final regulations defining the term foreign passthru payment.

Observation: While the original start date for withholding on gross proceeds was over a year away, many stakeholders had begun to turn their attention from FATCA reporting to FATCA withholding. The additional time will not only benefit industry, but allows the IRS time to draft the guidance necessary to provide rules on withholding in situations such as partnerships and other flow-through entities.

Treatment of collateral under the grandfathered obligation rule

Regulations currently provide that a grandfathered obligation includes an agreement requiring a secured party to make a payment with respect to collateral posted to secure a grandfathered obligation. Regulations further provide that where collateral secures both grandfathered and non-grandfathered obligations, the collateral posted to secure the grandfathered obligation must be determined by a pro rata allocation. In an effort to reduce the compliance burden associated with the pro rata allocation of collateral among grandfathered and non-grandfathered obligations, the Notice indicates the regulations will be amended to provide that the pro rata allocation method will not be mandatory. Under this approach, a secured party will be permitted to withhold on all collateral or to apply the pro rata approach with respect to such collateral.

It is common in industry to have collateral rehypothecated such that the secured party generally is not able to determine which collateral was

rehypothecated and which collateral has been retained. As such, Treasury and the IRS intend to amend the definition of grandfathered obligations to include obligations that give rise to substitute payments created as a result of a payee posting collateral that is otherwise treated as a grandfathered obligation.

Extension of limited branch and limited FFI statuses to January 1, 2017

Regulations currently provide that an FFI that is a member of an expanded affiliated group (EAG) may obtain the status of a PFFI or RDCFFI, so long as each FFI that is a member of its EAG has the status of a PFFI, RDCFFI, or exempt beneficial owner. If a member of the EAG operates in a jurisdiction that prevents it from becoming a PFFI or RDCFFI, it may become a limited FFI or limited branch. Although limited FFIs and branches will not taint the status of other members of its EAG, these statuses are transitional (i.e., they are scheduled to terminate on January 1, 2016). In an effort to allow additional time for FFIs and other stakeholders to determine whether to continue operating in

jurisdictions where limited branches or limited FFIs exist, the regulations will be amended to extend the availability of limited branch and limited FFI statuses to January 1, 2017.

The Notice indicates that, after December 31, 2015, all limited FFIs and limited branches will be placed in “registration incomplete” status on their online IRS FATCA account. Limited FFIs and limited branches will be required to edit and re-submit their registrations after December 31, 2015 on the IRS FATCA registration website to continue their limited status during 2016.

Observation: *Where the status of limited FFIs or branches changes such that they are able to comply with the terms of an FFI agreement, these entities should immediately amend their registration to reflect the modified status.*

Recap of changes

Taxpayers may rely on the provisions of the Notice prior to the issuance of the amendments it describes.

		Existing rule	Notice 2015-66 updates
Limited branch and limited FFI status	Status classification	Terminates on January 1, 2016	Terminates on January 1, 2017 with updated registration
Withholdable payments	Definition	US source FDAP income and, beginning in 2017, gross proceeds from the sale or other disposition of property of a type that can produce interest or dividends that are US source FDAP income	US source FDAP income and, for sales or other dispositions occurring after December 31, 2018, any gross proceeds from the sale or other disposition of any property of a type that can produce interest or dividends that are US source FDAP income

		Existing rule	Notice 2015-66 updates
Withholding	Gross proceeds	January 1, 2017	January 1, 2019
	Passthru payments	January 1, 2017	The later of January 1, 2019 or the date of publication in the Federal Register of final regulations defining the term “foreign passthru payment”
Grandfathered obligations	Collateral securing both grandfathered and non-grandfathered obligations	Mandatory pro rata approach for FATCA withholding	May apply FATCA withholding to entire amount or apply the pro rata approach
	Definition		Addition that any obligation that gives rise to substitute payments and that is created as a result of the payee posting collateral that is otherwise treated as a grandfathered obligation
Due date for sponsoring entities to register	<ul style="list-style-type: none"> RDCFFIs Sponsored direct reporting NFFEs 	January 1, 2016	January 1, 2017
	<ul style="list-style-type: none"> Model 1 IGA covered sponsored investment entities Model 1 IGA covered sponsored controlled foreign corporations 	Maintain deemed-compliant status as long as they are registered by the sponsoring entity on or before the later of December 31, 2015 or the date that is 90 days after a US reportable account is first identified	Maintain deemed-compliant status as long as they are registered by the sponsoring entity on or before the later of December 31, 2016 or the date that is 90 days after a US reportable account is first identified
Transitional rule on providing GIINs	Withholding certificates for sponsored RDCFFIs and sponsored direct reporting NFFEs that include only the sponsoring entity’s GIIN	Reliable for payments made prior to January 1, 2016	<ul style="list-style-type: none"> Reliable for payments made prior to January 1, 2017 For payments made after this date, withholding agents must obtain the GIIN of a payee that is a sponsored RDCFFI or a sponsored direct reporting NFFE
IGA	Expiration of IGAs treated as in substance	So long as the partner jurisdiction demonstrates firm resolve to bringing their respective IGA into force by December 31, 2014, and exchange information by September 30, 2015	So long as the partner jurisdiction demonstrates firm resolve to bringing their respective IGA into force and that any information reportable under the IGA on September 30, 2015 is exchanged by September 30, 2016, together with any information that is reportable under the IGA on September 30, 2016

The takeaway

While the constant state of flux on due dates and requirements challenge even the most sophisticated FIs, the additional time provided in the Notice should be welcome because it allows for the orderly implementation of FATCA. While certain stakeholders in larger organizations may be eager to fully implement FATCA, especially in light of the requirement to implement the Common Reporting Standard in many jurisdictions, the need for full implementation may need to be tempered with the permitted additional time being granted and the requirement for more guidance from Treasury and the IRS. FIs in IGA jurisdictions also will need to consider the requirements in their jurisdiction despite the additional time being granted by Treasury and the IRS as certain provisions may not be adopted by partner jurisdictions.

Let's talk

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