

FATCA Compliance: Preparing for the Challenges Ahead

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NAVIGANT

Agenda

- Introduction
- Presentation
- Questions and Answers — (anonymous)
- Slides — now available on front page of Securities Docket
 - www.securitiesdocket.com
- Wrap-up

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The Basics of the Foreign Account Tax Compliance Act (FATCA)

Presented to Securities Docket

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I. FATCA overview

A. Ongoing criminal tax matters

After UBS entered into a deferred prosecution agreement with the DOJ, and thousands of individuals disclosed their previously secret offshore accounts to the IRS, the U.S. Government introduced FATCA, likely the most far-reaching tax statute in our lifetime.

B. FATCA's effective date

FATCA generally goes into effect on January 1, 2013.

C. FATCA's affect on foreign and U.S. financial institutions

FATCA generally mandates that foreign financial institutions ("FFIs") identify U.S. taxpayers with accounts or suffer a 30% withholding on withholdable or passthru payments. To avoid the withholding tax, FATCA requires FFIs obtain and report information to the IRS on its accounts held by one or more specified U.S. persons or U.S. owned foreign entities.

FATCA also affects United States financial institutions ("USFIs") by requiring USFIs to identify whether their entity account holders are U.S. persons, FFIs, NFFEes or excepted from FATCA compliance. FATCA also requires USFIs to withhold when appropriate.

II. Top 10 things you need to know about FATCA

A. The Top 10 list

10. FATCA affects almost everyone
9. Steep penalties for non-compliance
8. Conducting a diligent review (review of individual accounts)
7. The certifying officer
6. Analyzing the financial institution's entity account holders
5. Foreign jurisdiction privacy laws and the right to an account
4. Passthru payments
3. Does the financial institution have the IT capabilities to comply?
2. Will lobbying the Government still help?
1. What are financial institutions currently doing?

II. Top 10 things you need to know about FATCA

B. Detail of Top 10 list

10. FATCA affects almost everyone

a. According to FATCA, a financial institution is an entity that:

- i. Accepts deposits in the ordinary course of a banking or similar business, such as savings banks and commercial banks.
- ii. Holds financial assets for the account of others as a substantial portion of its business such as broker-dealers, clearing organizations and custodial banks.
- iii. Is engaged (or holding itself out as being engaged) primarily in the business of investing, reinvesting, or trading in securities, partnership interests, or commodities or any interest (including a futures or forward contract or option) in such securities, partnership interests, or commodities such as mutual funds, funds of funds, hedge funds and private equity and venture capital funds.

II. Top 10 things you need to know about FATCA

10. FATCA affects almost everyone

b. USFIs

- i. USFIs will be required to withhold 30% of withholdable payments to non-participating FFIs and recalcitrant account holders.
- ii. USFIs will be required to follow certain documentary procedures, as described in Notice 2010-60, to determine how to classify entities. For pre-existing entity accounts, USFIs will likely have to search “electronically searchable information,” which is stored in the form of an electronic database against which standard queries in programming languages can be run.

II. Top 10 things you need to know about FATCA

10. FATCA affects almost everyone

c. FFIs will have to:

i. Comply with verification and due diligence procedures with respect to the identification of U.S. accounts.

(a) A diligent review for U.S. indicia is necessary for private banking accounts and individual accounts with year-end balances or values in excess of \$500,000;

(b) Electronically searchable information must be searched for U.S. indicia for all other individual pre-existing accounts.

II. Top 10 things you need to know about FATCA

10. FATCA affects almost everyone

c. FFIs will have to:

- ii. Report annually certain information with respect to U.S. accounts maintained by such FFI;
- iii. Deduct and withhold 30% from any passthru payment made to a recalcitrant account holder or any non-participating FFI;
- iv. Comply with any other requests made by the IRS for additional information about U.S. accounts and
- v. Obtain a waiver from the account holder when foreign law would prevent disclosure of information to the IRS.

II. Top 10 things you need to know about FATCA

9. Steep penalties for non compliance

a. 30% withholding

FATCA mandates a 30% withholding on withholdable and passthru payments to recalcitrant account holders and non-participating FFIs.

b. Recalcitrant account holders:

- i. Do not supply information requested.
- ii. Do not agree to waive any applicable restrictions on the reporting of their information to the IRS.

c. Non-participating FFIs:

- i. Do not sign an FFI Agreement with the IRS and do not fall under an exception.
- ii. The IRS will publish a list of all participating FFIs and deemed compliant FFIs to which it will provide an FFI EIN.

II. Top 10 things you need to know about FATCA

8. Conducting a diligent review

a. Accounts necessitating a diligent review

For all private banking accounts, as well as other types of individual accounts that have a year-end balance or value of \$500,000 or more, FFIs must conduct a “diligent review” of paper and electronic account files and other records for each account to identify indicia of a U.S. account. Diligent review is not defined by the Treasury or IRS.

II. Top 10 things you need to know about FATCA

8. Conducting a diligent review

b. Private banking accounts

The definition of a private banking account is broader than as defined by the USA PATRIOT Act. The definition of private banking accounts under Notice 2011-34 generally includes accounts:

- i. Serviced by a department at the FFI referred to as private banking, wealth management or similar department;
- ii. Where the FFI focuses on servicing accounts or the investments for high net worth individuals;
- iii. That are considered private banking accounts under the bank's AML/KYC requirements or
- iv. In which some or all of the FFI's employees: (a) ordinarily provide personalized services or (b) gather information about individual clients' personal, professional and financial histories in addition to the information ordinarily gathered with respect to the FFI's retail customers.

II. Top 10 things you need to know about FATCA

8. Conducting a diligent review

c. Indicia of U.S. status for private banking accounts includes:

- i. U.S. citizenship or lawful permanent resident (green card) status;
- ii. U.S. birthplace;
- iii. U.S. residence address or a U.S. correspondence address (including a U.S. P.O. Box);
- iv. Standing instructions to transfer funds to an account maintained in the U.S. or directions regularly received from a U.S. address;
- v. An “in care of” address or a “hold mail” address that is the sole address with respect to the client or
- vi. Power of Attorney or signatory authority granted to a person with a U.S. address.

d. The bank’s responsibility if U.S. indicia are present

If U.S. indicia are present, the FFI has to request a Form W-9 or Form W-8BEN and other documentation as necessary from the client, possibly including a waiver when foreign law would prevent disclosure of information to the IRS.

II. Top 10 things you need to know about FATCA

7. The certifying officer

The responsibilities of the certifying officer

- a. The Chief Compliance Officer or equivalent level officer has to certify that between the Notice 2011-34 publication date (either April 8 or May 9, 2011) and the effective date of the FFI Agreement, FFI management personnel did not engage in any activity, or have any formal or informal policies and procedures in place, directing, encouraging, or assisting account holders with respect to strategies for avoiding identification of their U.S. accounts.
- b. The certifying officer will further be required to certify that the FFI had written policies and procedures in place as of the effective date of the FFI's FFI Agreement prohibiting its employees from advising U.S. account holders on how to avoid having their U.S. accounts identified.
- c. The certifying officer must also certify when the FFI has completed the procedures relating to the analysis of its pre-existing individual accounts, including the search for U.S. indicia in "electronically searchable information" for pre-existing individual, non-private banking accounts (Notice 2011-34 was silent on entity accounts).

II. Top 10 things you need to know about FATCA

6. Analyzing the financial institution's entity account holders
 - a. USFIs and FFIs generally have similar requirements when reviewing their pre-existing entity account holders.
 - b. When analyzing pre-existing entity accounts the goal is to be able to categorize your entity accounts as one of the following:
 - i. U.S. Account;
 - ii. Participating FFI;
 - iii. Deemed Compliant FFI;
 - iv. Non-participating FFI;
 - v. Entities described under § 1471(f);
 - vi. Excepted NFFE or
 - vii. NFFE with substantial U.S. owners.
 - c. Substantial U.S. ownership

FATCA generally defines substantial U.S. ownership as ownership of more than 10% of an entity by a U.S. person. This may be a lower ownership threshold than the bank's current process for identifying beneficial ownership via its KYC/CDD procedures.

II. Top 10 things you need to know about FATCA

5. Foreign jurisdiction privacy laws and the right to an account

a. Foreign jurisdiction privacy and legal requirements

FFIs around the globe will have to contend with foreign jurisdictions’:

- i. Data privacy and bank secrecy laws;
- ii. Laws that effectively make it illegal to withhold foreign taxes and
- iii. Laws relating to the discrimination of persons of American nationality.

b. Potential solutions

- i. Individual waivers by account holders and
- ii. Governmental exchanges of information.

II. Top 10 things you need to know about FATCA

4. Passthru payments

a. The potential broad application of passthru payments

A passthru payment, as calculated in Notice 2011-34, is very broad and the mathematical formula could effect various types of payments from a FFI to a non-participating FFI or recalcitrant account holder.

- i. Passthru payment: Any withholdable payment or other payment to the extent attributable to a withholdable payment.
 - ii. Passthru payment calculation: (i) the amount of the payment that is a withholdable payment; plus (ii) the amount of the payment that is NOT a withholdable payment multiplied by the passthru payment percentage.
 - iii. Passthru payment percentage: generally determined by dividing the sum of the FFI's U.S. assets as of the last 4 quarterly testing dates by the sum of the FFI's total assets as of those same dates.
- b. Help from the FFI's Treasury, Controllor, Finance or other group may be required to determine the passthru payment percentage.

II. Top 10 things you need to know about FATCA

3. Does the financial institution have the IT capabilities to comply?
 - a. FFIs and USFIs are going to have to determine what “electronically searchable information” they currently maintain on their clients across the world.
 - b. The most useful information in terms of searching for U.S. indicia is likely to reside within databases of:
 - i. Client on-boarding and financial crimes platforms (customer watch list monitoring and transaction monitoring) and
 - ii. Client transactions and payments.

II. Top 10 things you need to know about FATCA

3. Does the financial institution have the IT capabilities to comply?
 - c. A structured approach to inventory the reports, fields, feeds, and capabilities that currently exist as part of your current customer watch list monitoring efforts is a valuable first step.
 - d. Many FATCA requirements may be met by leveraging existing systems and service functions that already exist and can be dual purposed.

An example is the ability to use the customer screening platform(s) that are part of your financial crimes or AML systems infrastructure, comparing customer names against various sanctions and other lists on a nightly basis. By enriching the current data feeds, and adding new detection checks, these platforms may be used to satisfy part of the requirement to search electronic information for U.S. indicia for FATCA purposes.

II. Top 10 things you need to know about FATCA

2. Will lobbying the Government still help?
 - a. The Treasury and IRS have generally been receptive to lobbying efforts by the industry.

Based on lobbying efforts the Treasury and IRS:

- i. Changed the methodology to analyze the bank's pre-existing individual accounts;
 - ii. Limited the definition of electronically searchable information and
 - iii. Limited the requirement to aggregate account values across all affiliated FFIs.
 - b. The Treasury and IRS have met with industry groups and financial institutions.
 - c. Foreign Governments are discussing FATCA with the Treasury and IRS as well.
 - d. Potentially useful future lobbying steps could relate to:
 - i. Passthru payments and
 - ii. Delaying the date withholding starts.

II. Top 10 things you need to know about FATCA

1. What are financial institutions currently doing?
 - a. Establishing the FATCA Task Force and Project Management Office;
 - b. Identifying the impact FATCA will have on each of their entities and business lines;
 - c. Quantifying the number of accounts for review, specifically private banking accounts and accounts with balances or values in excess of \$500,000 that require a diligent review;
 - d. Researching foreign laws that could pose a conflict with FATCA reporting requirements;
 - e. Identifying policies and procedures across the world that will have to be updated, specifically on-boarding policies and procedures;
 - f. Inventorying the number of relevant IT systems and reports, fields, feeds and capabilities of those systems and
 - g. Estimating the budget and resources necessary to comply with FATCA.

Questions?

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For Attending This Webcast

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