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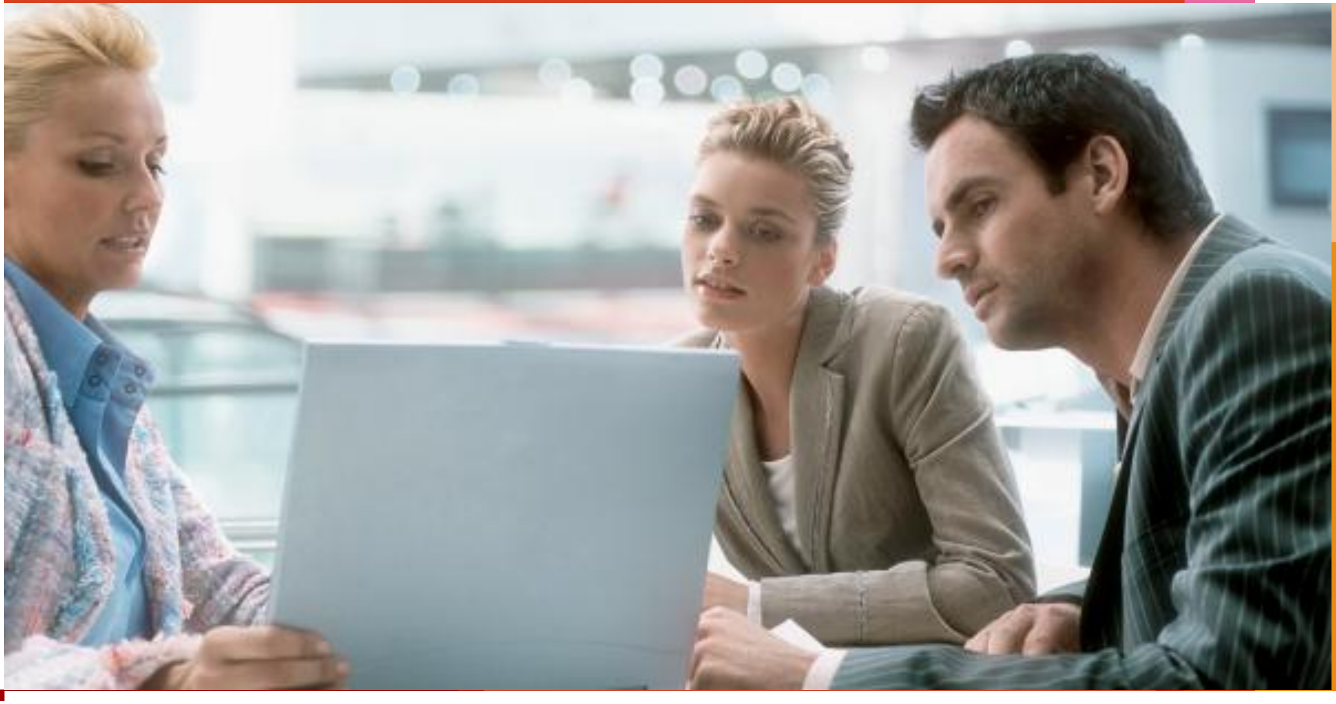
Foreign Account Tax Compliance Act (FATCA)

Key Considerations for the KBA (Kenya Bankers Association)



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Agenda – KBA Presentation

- Section 1: The Basics of FATCA
- Section 2: Inter-Governmental Agreements
- Section 3: South Africa's Approach to their IGA
- Section 4: PwC's Recommendations

Section 1: The Basics of FATCA

- ❑ An overview
- ❑ The 3 pillars of FATCA
- ❑ Who does FATCA affect?
- ❑ The FATCA timelines

An Overview
Background

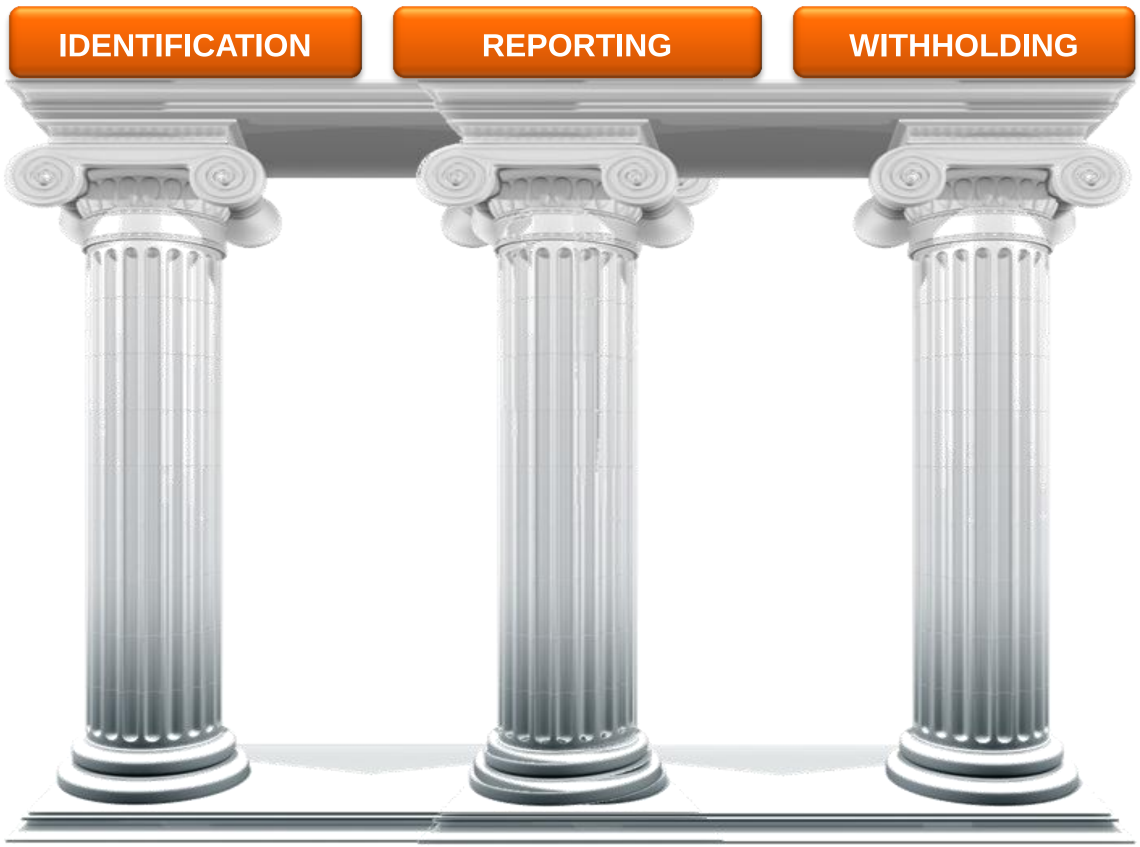
- The Foreign Account Tax Compliance Act provisions which were included in the Hiring Incentives to Restore Employment ("HIRE") Act passed in March 2010 (generally referred to as "FATCA")
- Provide the Internal Revenue Service ("IRS") with increased ability to detect U.S. tax evaders hiding their money in foreign accounts and investments
- Provisions aimed at certain payments made to non-U.S. persons to compel compliance and not meant to collect significant tax
- Created new "Chapter 4" of the Internal Revenue Code ("IRC" or "Code") (Provides limited grandfathering exemptions)
- Impacts Foreign Financial Institutions ("FFI") and Non-Financial Foreign Entities "NFFE"), while imposing new burdens on U.S. withholding agents
- Generally, withholding does not apply to "withholdable payments" until July 1, 2014 with transitional relief for payments of gross proceeds and passthru payments

An Overview
FATCA's Objective and Purpose

- The **objective** of FATCA is to "detect, deter and discourage offshore tax evasion" by US citizens or residents.
- *Major functions impacted:*
  - Client identification (on-boarding)
  - Tax reporting
  - Tax withholding
  - Governance

- The **purpose** is to create greater transparency by strengthening information reporting and compliance with respect to US accounts.

Three Pillars of FATCA



1. Identification

Identification

- **New customers** (individuals and/ or entities) and
- **Pre-existing customers**: need to understand which customers are:
  - U.S. individuals and/ or entities
  - For entities, which are FFIs or NFFEs
- Counterparties (approved and status monitoring)
- De minimus rules

2. Reporting

Identification → **Reporting**

- New customers
- Pre-existing customers

- **A specified U.S. Person**, the name, address and taxpayer identification number (TIN)
- **A U.S. owned foreign entity**, the name, address, and TIN (if any) of the U.S. owned foreign entity and name, address, and TIN of each substantial U.S. owner
  - The account number
  - Account balance or value
  - Gross receipts, withdrawals or payments from the account
- Other information includes:
  - The account number of U.S account holders; the account balance or value; gross receipts, withdrawals or payments from the account; recalcitrant account holders; and NPFFI's (Non-Participating Foreign Financial Institutions)

3. Withholding - 30 % tax withholding

Identification → Reporting → **Withholding**

Identification
- New customers
- Pre-existing customers

Reporting
- Specified U.S. Person
- A U.S. owned foreign entity

Withholding
- **Withholdable payments** defined as:
  - Any US source FDAP income, including interest, dividends, rents, salaries, wages, premiums, annuities, compensations, remunerations, and emoluments
  - Any gross proceeds from the sale of any property that could produce US source dividends or interest
  - Interest on deposits at foreign branches of US banks is US source income
  - Excludes income effectively connected with a US trade or business

Who does FATCA Affect?

A FFI is a foreign entity that either:	Examples:	
▪ Accepts deposits in the ordinary course of a banking or similar business; or	▪ Commercial banks ▪ Savings and Loan Associations	▪ Credit unions ▪ Co-operative banking institutions
▪ Holds financial assets for the account of others, as a substantial portion of its business; or	▪ Broker Dealers ▪ Clearing Organisations ▪ Trust Companies	▪ Custodial banks ▪ Custodian of Employee Benefit Plan
▪ Entity primarily conducts as a business one or more of the following activities or operations for or on behalf of a customer: 1. trading in certain financial products 2. individual or collective portfolio management 3. investing, administering or managing money or financial assets on behalf of others . 4. entities that hold themselves out as collective investment vehicles, mutual funds, private equity funds, etc. ; or	▪ Mutual Funds ▪ Funds of Funds ▪ ETF ▪ Hedge Funds ▪ Private Equity Funds ▪ Venture Capital Funds	▪ Sovereign Wealth Funds ▪ Commodity Pools ▪ Managed Funds ▪ Collective Investment Vehicles

An NFFE is any foreign entity which is not an FFI

Who does FATCA Affect?

A FFI is a foreign entity that either:	Examples:
▪ is a company regulated as an insurance company in its country of operation, ▪ has gross income arising from insurance, reinsurance, and annuity contracts that exceeds 50 percent of gross income, or ▪ has assets associated with insurance, reinsurance, and annuity contracts that exceeds 50 percent of gross assets; or ▪ An entity that is a holding company or treasury center that: 1.is part of an expanded affiliate group (EAG) that includes other financial institutions, or 2.if formed in connection with investment vehicles such as private equity funds, mutual funds, hedge funds, etc.	▪ Life Insurance companies/products

An NFFE is any foreign entity which is not an FFI

What is a NFFE?

Non-Financial Foreign Entity (NFFE)

- Foreign entities which are not FFIs.
- Excepted NFFE's are:
  - Corporations (and certain affiliated entities) that are regularly traded on an established securities market;
  - Foreign governments, any political subdivision of a foreign government, or any wholly owned agency or instrumentality;
  - International organizations or wholly owned agency or instrumentality; or

FATCA Timeline For non IGA countries, as at 12 July 2013

(For FFI Agreements Effective on 30 Jun, 2014)

	2012	2013	2014	2015	2016	2017/ 2018
FFI Governance		**August 19 2013** – IRS FATCA registration portal available (Note 1)	**Apr 25 2014** – Last day to register for inclusion on the Jun 2, 2014 IRS list of PFFIs and RDCFFIs **Jun 2 2014** – First IRS list of PFFIs and RDCFFIs to be published **Jun 30 2014** – Earliest effective date of an FFI Agreement		**Jan 1 2016** - Expanded affiliated group transition period ends for Limited FFIs and Limited Branches **Feb 29 2016** - Responsible officer must be able to certify completion of identification and review for all preexisting individual and entity accounts (Note 2)	**Jan 1 2017** - Interests previously issued in bearer form must be redeemed or immobilized **Jun 30 2017** - First Certification of Compliance and Effective Controls required **Dec 31 2016** - Last day for qualification as Limited Life Debt Investment Entity **Dec 31 2016** - End of first compliance certification period
Due Diligence for Pre-Existing Accounts			**Dec 31 2014** – Complete identification and review of preexisting entity account holders that are prima facie FFIs	**Jul 1 2015** – Complete identification and review of preexisting high value individual accounts	**Jul 1 2016** – Complete identification and review of all remaining preexisting individual and entity accounts (Note 3)	
Procedures for New Accounts			**Jul 1 2014** – Enhanced account opening procedures must be in place to establish the FATCA status of new individual and entity accounts			
Withholding			**Jul 1 2014** – Cut-off date for grandfathered obligations (Note 4) **Jul 1 2014** – Begin FATCA withholding on US source FDAP income for all new accounts and NPFFIs **Dec 31 1 2014** – Begin FATCA withholding on preexisting entity account holders that are undocumented prima facie FFIs	**Jan 1 2015** – Begin FATCA withholding on any undocumented individual preexisting high value account	**Jan 1 2016** – Begin FATCA withholding on remaining undocumented preexisting accounts	**Jan 1 2017** – Begin FATCA withholding on gross proceeds. FATCA withholding is also expected to begin for foreign passthru payments.
Reporting				**Mar 15 2015** – Begin FATCA reporting on Form 1042-S for US source FDAP income for calendar year 2014 **Mar 31 2015** – Limited FATCA reporting on Form 8966 for calendar year 2014 for US accounts (Note 5) **Mar 31 2015** – Begin aggregate FATCA reporting on Form 8966 for recalcitrant accounts	**Mar 15 2016**– Form 1042-S reporting must include foreign reportable amounts paid to NPFIs during calendar year 2015 (also applies to calendar year 2016) **Mar 31 2016** – Limited FATCA reporting on Form 8966 for calendar year 2015 includes income payments	**Mar 31 2017**– Full FATCA reporting on Form 8966 begins for calendar year 2016 **Mar 15 2018**– Begin FATCA reporting on Form 1042-S for US gross proceeds and potentially foreign pass thru payments for calendar year 2017

(1) The IRS has committed to making the FATCA registration portal available no later than July 15, 2013. This, it could be available earlier.

(2) As part of the certification, FFI must also certify that it did not have any procedures in place from August 6, 2011 that would assist account holders in the avoidance of FATCA.

(3) Certain de minims thresholds and retesting rules may apply.

(4) Generally applies to obligations that can produce a withholdable payment. Grandfathered obligations also include: (1) any obligation that gives rise to a withholdable payment solely because the obligation is treated as giving rise to a dividend equivalent pursuant to section 871(m) and the regulations thereunder, provided that the obligation is executed on or before the date that is six months after the date on which obligations of its type are first treated as giving rise to dividend equivalents; (2) with respect to foreign passthru payments, any obligation that is executed on or before the date that is six months after the date on which final regulations defining the term foreign passthru payment are filed with the federal register; and (3) any agreement requiring a secured party to make a payment with respect to, or to repay, collateral posted to secure a grandfathered obligation.

(5) Limited reporting includes name, address, TIN, account number, and account balance of each specified US person who is an account holder. For account holders that are treated as US owned foreign entities and owner-documented FFIs for reporting purposes, report name, address and TIN (if any) of such entity and each substantial US owner of such entity or specified US person.

FATCA Timeline for FFIs under Model I IGA (Note 1)

	2012	2013	2014	2015	2016	2017/ 2018
FFI Governance		**August 19 2013** IRS FATCA registration portal available	**Jun 30 2014** – Earliest date that an FFI can be a Partner Country FI	**Jan 1 2015** – Obtain GIIN from the IRS		
Due Diligence for Pre-Existing Accounts				**Dec 31 2014** – Complete identification and review of preexisting high value individual accounts (Note 3)	**Dec 31 2015** – Complete identification and review of all remaining preexisting accounts (Note 4)	
Procedures for New Accounts			**Jul 1 2014** – Enhanced account opening procedures must be in place to establish the FATCA status of new accounts (Note 3 & 5)			
Withholding			**Jul 1 2014** – Begin FATCA withholding on US source FDAP income for NPFIs (Note 4)			
Reporting				Prior to Sep 30, 2015 – Reporting FATCA Partner FI will need to provide required information to FATCA Partner prior to IGA deadlines in order for FATCA Partner to be able to meet corresponding deadlines (Note 6)	2016 – Reporting FATCA Partner FI to report to FATCA Partner Country the name and the aggregate amount of payments made in 2015 and 2016 to NPFE (Note 6)	2017 – Reporting FATCA Partner FI to obtain and report TIN of each specified US account holder for preexisting accounts (Note 6)

(1) IGA: Intergovernmental Agreement
(2) Certain de minimis thresholds and retesting rules may apply.
(3) Withholding applies to US source income paid to nonparticipating financial institutions by reporting FATCA Partner financial institutions acting as a withholding QI, withholding foreign partnership or withholding foreign trusts. Other reporting FATCA Financial Institutions must provide information necessary to allow an immediate payor to withhold.
(4) Dates for withholding on gross processed and passthru payments are highly speculative and will be worked out between the US and FATCA partner countries in the next two years.
(5) Dates will be provided under legislations issued by FATCA Partner tax authorities.

Section 2: Inter-Governmental Agreements (IGA)

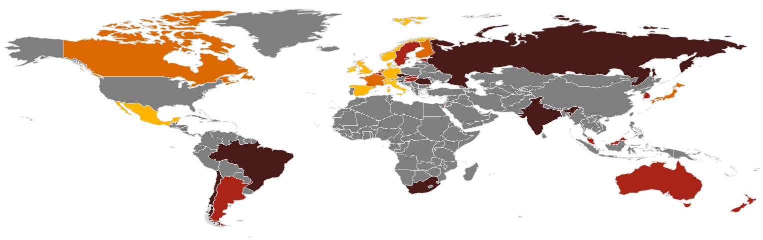
- ❑ What is an IGA?
- ❑ A global IGA update
- ❑ Key attributes and benefits of an IGA
- ❑ The role of the regulator

What is an IGA?

The primary purpose of a IGA is to assist with the legal impediments that exists around privacy laws and barriers. The aim is to better enable FATCA compliance and ease the transition.

Intergovernmental Agreement	
Definition	The IGA is an agreement between a country and the US IRS, whereby it is agreed that: 1. the FATCA regulations will not apply (in its entirety) to the financial entities in that country; 2. local financial entities report specific information to their local regulatory authority, who in turn provide the information to the IRS; with the IRS obligated to provide reciprocal information in certain cases (Model I) OR; 3. local financial entities report specific information to the IRS directly, with the consent of their local tax authorities (Model II); 4. there is no requirement for entities to withhold on recalcitrant account holders.

A Global IGA Update



Concluded an IGA

Denmark (1), Germany (1), Ireland (1), Japan, Mexico (1), Norway (1), Spain (1), United Kingdom (1), Japan (2), Switzerland (2), France (1)

→ Signed and released IGAs

Process of finalizing an IGA

- Bahamas, Canada, Cayman Islands, Finland, Guernsey, Isle of Man, Italy, Jamaica, Jersey, Malta, Netherlands
- IRS' negotiations with these countries to be completed soon

Actively engaged in dialogue of concluding an IGA

- Argentina, Australia, Belgium, Cyprus, Estonia, Hungary, Israel, South Korea, Liechtenstein, Luxembourg, **Malaysia**, New Zealand, Slovak Republic, **Singapore**, **South Africa**, Sweden
- US Treasury expects to be able to conclude negotiations with several of these countries in the coming months

Exploring options for an IGA

- Bahrain, Bermuda, **Brazil**, the British Virgin Islands, Chile, Curacao, Czech Republic, Gibraltar, **India**, Lebanon, Mauritius, Romania, Russia, Seychelles, Saint Martin, Slovenia, Taiwan
- No expectations or timelines were provided for these discussions

Model I Inter Governmental Agreements (IGAs)

- Under this agreement, Foreign Financial Institutions who enter into IGAs will be able to report information on U.S. account holders and accounts directly to their national tax authorities, who in turn, will report to the IRS.
- **Two options exist**
  - 1a: reciprocal
  - 1b: non-reciprocal
- **IGA highlights and benefits**
  - Reciprocity (in Model 1a)
  - Current KYC rules and percentages apply
  - Retirements plans excluded
  - Increased clarity around due diligence with country specific provisions

Model II Inter Governmental Agreements (IGAs)

- Model II IGA was designed to address potential conflicts of national and local laws that would make it difficult, for Financial Institutions in some jurisdictions, to comply with FATCA.
- The most notable difference between Model I and Model II IGA's is that in the latter, financial institutions will report information directly to the IRS rather than their local jurisdictions

Key Attributes and Benefits of an IGA

RELAXED COMPLIANCE REQUIREMENTS

An IGA will also benefit a group of small financial institutions if the Partner country can successfully negotiate specific exemptions from FATCA

CONTROLLED INFORMATION FLOW

An IGA will allow for better control over flow of information without flouting banking data protection and privacy laws

REDUCED COMPLIANCE COST

An IGA would reduce compliance cost as the compliance requirements are less stringent e.g. Definition of a qualifying US entity will be based on the local AML requirements as against 10% defined for non-IGA countries. FFIs in IGA Partner countries; do not have withholding responsibilities, can explore the possibility of product carve-outs etc.

RECIPROCITY AND INCREASED TAX REVENUE

Automatic exchange of information between countries (model specific) and possible increase in tax revenue following the identification of qualifying US and Kenyan citizens

PROVIDES A FRAMEWORK FOR THE NEW TAX INTEGRATED SYSTEM

The information requirements of the IGA enable the tax authority to be proactive in the design of the new integrated tax system in line with global trends

The Role of the Regulator/ KBA

Promulgate regulations and guidelines

Ensure compliance

Reduce the cost of compliance

Minimise the negative impact on the consumer

Liaise with the US IRS

Coordinate the process

Section 3: South Africa's Approach to their IGA

- ❑ Background
- ❑ Workstream setup
- ❑ Current status
- ❑ PwC's involvement

SA's IGA - Background

- South Africa announced its intention to enter into an IGA in December 2012;
- Through the Banking Association of South Africa, working groups have been established for all FI's to participate in;
- The purpose of these working groups are to provide the South African Revenue Services (SARS) with the required industry information, specifically on:
    - Issues - to be resolved by SARS;
    - Suggestions – like product carve outs;
    - Decision taken at a industry level; and
    - To formulate a common understanding and procedure where possible.

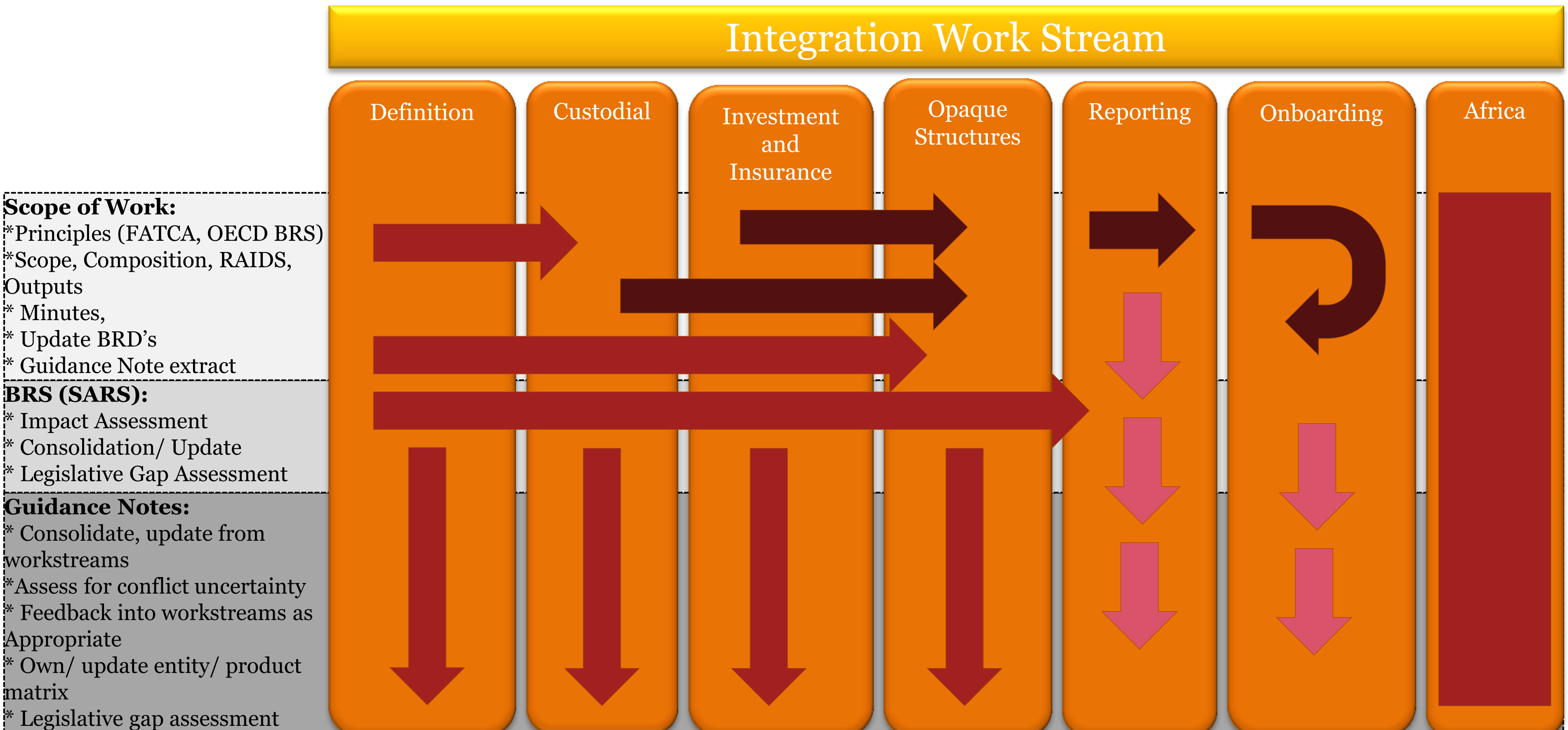
SARS

national treasury

Department:
National Treasury
REPUBLIC OF SOUTH AFRICA

SA's IGA – Workstream Setup

- The current setup of the working groups is depicted in the below figure.



SA's IGA – Current Status

- The status:
  - Industry meetings are still in progress;
  - FATCA requirements have been extended to accommodate the Automatic Exchange of Information (OECD);
  - Certain key decisions have been agreed between industry and SARS, such as: The minimum and maximum amount of TINS to collect, the additional questions to be included on the customer application forms, due diligence procedures for High Value Account Holders with regards to reporting and screening, de minimus thresholds, reporting timelines, the procedure for reporting for a branch or subsidiary in Africa, etc;
  - Due to the IRS shut down, negotiations have been slow;
  - SARS has released a Business Requirements Specification document to test the reporting mechanisms with industry;
  - Other circulars have been sent for FATCA awareness purposes.

SA's IGA – PwC's Involvement

- PwC is involved in 4 of the 8 working groups, namely:
  - Reporting;
  - Onboarding;
  - Africa; and
  - Integration.
- Services provided include:
  - Advisory;
  - Documentation and collation of industry comments, actions, issues, risks and decisions;
  - Input into the guidance notes;
  - SARS support in terms of actions; and
  - Owner of the document for the industry comments on the SARS BRS.

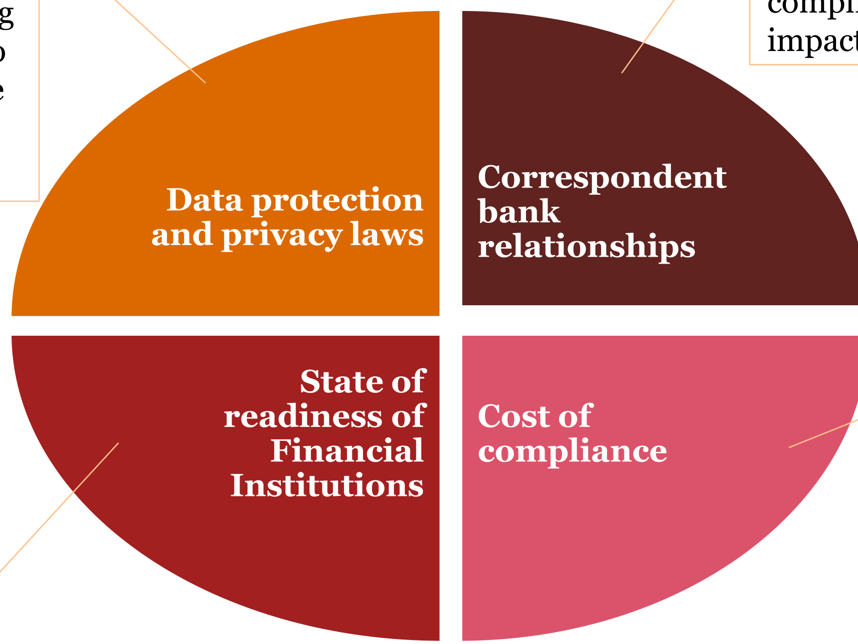
Section 4: PwC’s Recommendations

- ❑ Summary of Concerns for FFI’s
- ❑ PwC’s Approach to the IGA
- ❑ Other items to consider
- ❑ Question and Answer Session
- ❑ Contact Details

Summary of Concerns for FFI's (Foreign Financial Institutions)

There are significant legal barriers **(e.g. data protection and privacy laws)** which prevent institutions from sharing customer information and entering into FFI agreements, which will result in the punitive 30% withholding on all US Source income.

Impairment of **relationships with correspondent banks**; foreign banks may rationalize relationships with non-compliant local banks. This will impact FI customers.



With the new **FATCA requirements** placed on customer identification (on boarding processes and procedures), withholding mechanisms and reporting procedures, Financial Institutions may need to **exert significant effort** in order to become FATCA compliant. Many feel lost and not well prepared for these changes.

FATCA creates a **significant operational and due diligence obligation** on financial institutions. It will require developing/unlocking of additional systems capabilities and modification of existing operational processes with a resultant increase in overall compliance cost.

These concerns necessitates the involvement of key regulators and associations.

PwC's Approach to FATCA
High level Roadmap

CURRENT STATE ASSESSMENT

Mobilisation

Classify Legal Entities and Map Business Units

Analyse Business Entities:
Existing Account Holders,
High-Level Processes,
Supporting Systems,

Assess Impact

FUTURE STATE DEVELOPMENT

Define Compliance Strategy

Registration and IGA Sign up

Define Target Operation Model:
Organisational
Process
System

Develop Business Case & Funding Request

Develop Implementation Roadmap

IMPLEMENTATION

Compliance Governance

Remedied Accounts

Revised Processes & Procedures

Revised Systems

Revised Roles & Responsibilities

FATCA Compliance

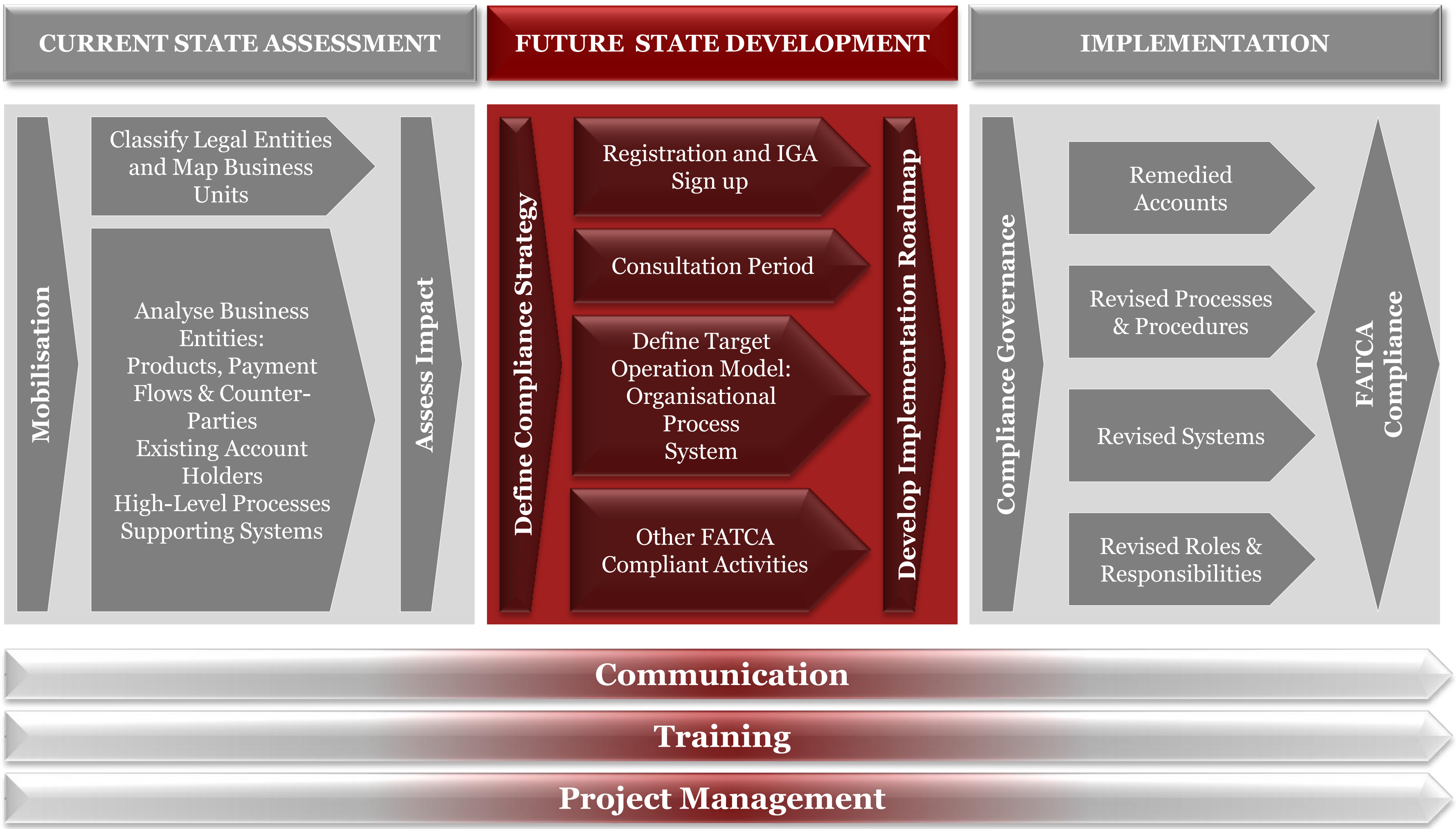
Communication

Training

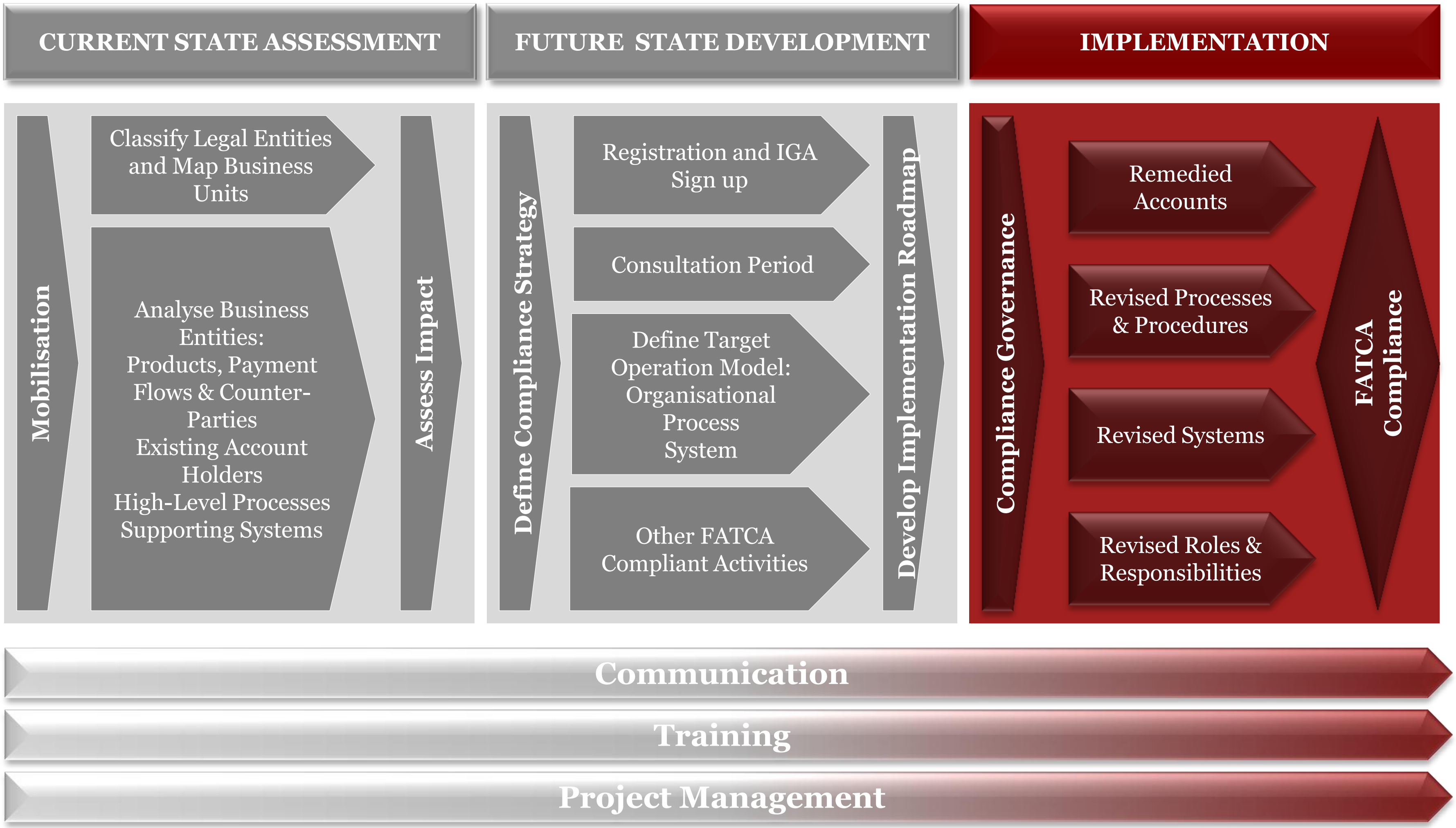
Project Management

PwC's Approach to FATCA

High level Roadmap



PwC's Approach to FATCA
High level Roadmap



PwC's Approach to IGA's is Practical and Flexible

	Phase 1	Phase 2	Phase 3
Phases	**Workstream Setup and Industry Consultation** (Establish the workstreams for Kenya's approach to the IGA, taking into consideration domestic uniqueness)	**IGA Negotiation and Sign-up** (Negotiate and enter into IGA with IRS)	**Implementation Support** (Define framework for monitoring FATCA compliance and IGA progress)
Key Activities	• Stakeholder mapping and orientation • FATCA requirements analysis • Current legal and regulatory framework • Benchmarking • Analysis of Model choices	• Finalise product carve outs • Finalise Industry comments and concerns • Enter into IGA Negotiation • IGA signing • Arrangements with FFIs • Detailed roadmap	• FATCA Compliance Monitoring Framework • Periodic FATCA/IGA updates • Stakeholder sessions • Amendment of reporting systems (if Model 1) • OECD requirements

Project Management Support & Stakeholder Engagement

Relevant Updates /Industry Knowledge

From our experience, the approach should be; transparent, easily understood and structured into defined work-streams, each with a clear set of objectives and milestones.

Other Items to Consider

FATCA is not the only regulation to be imposed on Kenya…

- OECD Requirements: The Automatic Exchange of Financial Account Information
  - *Purpose*: to have in place a common standard on reporting and due diligence for financial account information;
  - Extends certain FATCA requirements, such as indicia and reporting;
  - A Model Competent Authority Agreement will have to be entered into (in order to exchange information with member country);
  - No BRS document has formally been released and FFI's must prepare for the OECD requirements, not just FATCA.

For further information on how we can support you on this journey, please contact any of the persons indicated below

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Question and Answer Session