

Tax Alert

New Guidance Sets Forth Delayed Timelines for Due Diligence and Other Requirements Under FATCA

October 31, 2012

The Internal Revenue Service (IRS) issued Announcement 2012-42 (available [here](#)), which delays the timelines during which withholding agents and foreign financial institutions (FFIs) will be required to implement and complete due diligence and other requirements under the Foreign Account Tax Compliance Act (FATCA). These delayed timelines will be incorporated into the final FATCA regulations, which are expected to be released by the Department of the Treasury and the IRS before the end of the year.

Announcement 2012-42 is important to investment managers, including managers of onshore and offshore hedge funds, private equity funds and other alternative investment vehicles. In particular, Announcement 2012-42 delays the implementation of due diligence requirements by withholding agents when they open new accounts (such as an onshore fund that admits a foreign investor) until January 1, 2014. Prior to the issuance of Announcement 2012-42, withholding agents were supposed to have new account opening procedures in place by January 1, 2013. Although the required implementation of due diligence for withholding agents has been delayed, investment managers should continue to collect the proper Forms W-9 and Forms W-8 from their investors in both onshore and offshore vehicles and may consider beginning to undertake what are likely to be FATCA-compliant due diligence procedures with respect to new and preexisting accounts.

BACKGROUND

FATCA, which was enacted on March 18, 2010, generally requires withholding agents to withhold 30 percent of certain payments to an FFI unless the FFI has entered into an agreement (an FFI agreement) with the IRS under which the FFI agrees, among other things, to obtain and report certain information with respect to the direct and indirect owners of its accounts. Although the purpose of FATCA is to identify U.S. persons who may be investing through accounts in foreign institutions, the compliance procedures will require that withholding agents and FFIs obtain certain identifying information with respect to all accounts, whether or not they are actually owned by U.S. persons. Since the enactment of FATCA, the IRS has released several notices and proposed regulations regarding the implementation of FATCA (prior coverage is available [here](#)) and has delayed the implementation of FATCA beyond the statutory effective date of January 1, 2013, with respect to both the information reporting and the withholding obligations of withholding agents and FFIs.

ANNOUNCEMENT 2012-42

Treasury and the IRS have determined that the FATCA status of entity account holders may change during 2013 as FFIs enter into FFI agreements, and that, as a result, withholding agents that implement new account opening procedures by January 1, 2013 (as required by previous guidance), could be required to undertake duplicative



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efforts to verify an FFI's status under FATCA and whether such withholding agent is required to withhold on payments made to such FFI. Thus, in order to reduce significantly the administrative burden associated with implementing due diligence procedures by withholding agents and FFIs, Announcement 2012-42 provides delayed timelines for withholding agents and FFIs to implement and complete due diligence and other requirements under FATCA.

Announcement 2012-42 also states that Treasury and the IRS intend to expand the scope of "grandfathered" obligations and provide further guidance regarding "grandfathered" derivatives transactions in the final FATCA regulations. Finally, Announcement 2012-42 notes that withholding on "gross proceeds" under FATCA will be delayed by two years, so that such withholding is now scheduled to begin on January 1, 2017 (prior to the issuance of Announcement 2012-42, withholding on gross proceeds was scheduled to begin on January 1, 2015). Withholding on U.S.-source interest and dividends, among other types of income, is still anticipated to begin on January 1, 2014.

DUE DILIGENCE TIMELINES

Announcement 2012-42 provides the following new due diligence timelines for withholding agents and FFIs, which begin no earlier than January 1, 2014 —

- Withholding agents (other than participating FFIs and deemed-compliant FFIs) must fully implement new account opening procedures for new individual and entity accounts by January 1, 2014.
- Withholding agents (other than participating FFIs and deemed-compliant FFIs) must complete the review and documentation of all preexisting accounts of *prima facie* FFIs by June 30, 2014, and all preexisting accounts of entities other than *prima facie* FFIs by December 31, 2015. To coordinate the due diligence timeline with the effective date of withholding under FATCA, a withholding agent will not be required to withhold on payments made to a *prima facie* FFI with respect to a preexisting obligation prior to July 1, 2014, unless the withholding agent has documentation establishing the payee's status as a nonparticipating FFI.
- Withholding agents that are participating FFIs must fully implement new account opening procedures for new individual and entity accounts by the later of January 1, 2014, or the effective date of the FFI agreement.
- Withholding agents that are participating FFIs must complete the review and documentation of all preexisting accounts of *prima facie* FFIs by the later of June 30, 2014, or six months after the effective date of the FFI agreement, and all preexisting accounts of entities other than *prima facie* FFIs by the later of December 31, 2015, or two years after the effective date of the FFI agreement (special rules apply to preexisting accounts of individuals, which would be required to be complied with no earlier than December 31, 2014).
- Withholding agents that are registered-deemed compliant FFIs must fully implement new account opening procedures for new individual and entity accounts by the later of January 1, 2014, or the date of their registration.
- The final FATCA regulations will provide that a participating FFI will be required to file information reports with respect to the 2013 and 2014 calendar years no later than March 31, 2015.

Announcement 2012-42 emphasizes that although the final FATCA regulations will provide a reasonable period of time to allow withholding agents to review and document all preexisting accounts — as outlined above — the final FATCA regulations will make clear that once a particular account has been documented, withholding or

reporting, as appropriate, must begin with respect to that account even though the time period for completing the identification and documentation of all preexisting accounts may not have expired.

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