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Management Alert

Deadline Approaching for Foreign Retirement Plans to Comply with FATCA

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Beginning July 1, 2014, any foreign retirement plan that invests in the United States will face a potential 30% withholding tax on income derived from US investments unless the plan is able to demonstrate that it is either exempt from, or in compliance with, the Foreign Account Tax Compliance Act (FATCA). Moreover, plans that are not otherwise exempt from FATCA must register with the IRS by April 25, 2014.

Accordingly, any multinational employer that sponsors non-US retirement plans that invest in the US should be reviewing all of its plans to make sure they comply with FATCA prior to the deadline.

What is FATCA?

FATCA was enacted in 2010 to insure that US taxpayers properly report, and pay tax on, their income earned overseas. Part of FATCA is focused on "foreign financial institutions", or FFIs, which are defined as foreign entities that hold financial assets for the account of others. An FFI, unless it satisfies an exemption, must be able to document the extent to which the beneficiaries of its assets are US taxpayers, or be subject to a 30% withholding tax on its US income.

IRS regulations have confirmed that funded foreign retirement plans are classified as FFIs, and therefore potentially subject to the 30% tax on their US income unless they qualify for an exemption from, or can demonstrate compliance with, FATCA. It is important to note that the 30% tax applies to all of the noncompliant plan's US source income, not just the portion that is attributable to US taxpayers who participate in the plan.

Although the focus of this Management Alert is on the FATCA obligations of foreign retirement plans, it should also be noted that FATCA (and the parallel requirements under the Foreign Bank Account Report requirements, or FBAR) also impose filing requirements on individual US taxpayers who have an interest in overseas assets, with stringent potential penalties including criminal liability. Companies whose employees regularly work overseas may wish to provide support for those employees to make sure they comply with their FATCA and FBAR obligations. For more information on the reporting requirements of individual US taxpayers, see our client alert *here*.

Which Plans are Exempt from FATCA?

Although all funded foreign retirement plans are potentially classified as FFIs subject to FATCA, there are a number of exemptions that will apply to most plans. The IRS has entered into "inter governmental agreements", or IGAs, with a number of foreign countries, and these IGAs typically identify certain types of plans that have a low potential for abuse, and accordingly are exempt from FATCA reporting. For example, the IGA with Canada provides that most types of "registered" retirement and savings plans (which is roughly the equivalent of a "qualified" plan in the US), are exempt.

Accordingly, the first step taken by a company that sponsors foreign retirement plans should be to determine which plans are located in countries that have entered into IGAs that provide that the type of plan involved is exempt from FATCA. There will be no further concerns under FATCA with these plans, regardless of whether they currently invest in the US or begin to do so in the future.

If a foreign plan is not covered an IGA, there are six other classes of plans that are exempt from FATCA compliance under the IRS regulations, including plans that are covered by certain tax treaties, certain plans that provide for broad participation, certain small plans with no more than 50 participants, and plans that would qualify under Code §401(a) if they were organized in the US. However, all of these exemptions include a number of technical requirements that will require some degree of investigation into the terms of the plan, and at least in the short run companies will want to restrict this analysis to non-IGA plans that actually invest in the US.

How Does a Non-Exempt Plan Comply with FATCA?

If a foreign plan is not exempt from FATCA, either under an IGA or one of the six exemptions, and the plan invests in the US, it will need to become a "reporting FFI." The deadline for registering as a reporting FFI, in order for a plan to be exempt from withholding beginning July 1, 2014, is April 25, 2014. The registration itself is a complex process, and must be done through an IRS maintained web site. Once a plan registers as a reporting FFI, it must undertake a review of its records to identify all accounts that have various "indicia" indicating that they may be owned by a US taxpayer (such as a mailing address or phone number within the United States), and commit to ongoing review of its accounts in the future. If a company has any plans that are not exempt, and that currently invest in the US, it is important that this process begin as soon as possible to insure that registration may be completed by the April 25 deadline.

Next Steps

Each company with overseas operations should take the following steps to insure that its plans are not subject to the 30% FATCA withholding tax:

- Identify all retirement or savings plans maintained outside of the United States
- Determine which plans are covered by an IGA.
- For plans that are not covered by an IGA, and that currently invest in the US, determine whether they are covered by one of the six FATCA exemptions.
- Register any plans that are not exempt and that currently invest in the US as reporting FFIs not later than April 25, 2014.

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