The Implications to Clients of Mainland China, Taiwan and Hong Kong Reaching Agreement with US on FATCA

The US Foreign Account Tax Compliance Act commonly referred to as FATCA officially went into effect on July 1st 2014. The purpose of FATCA is to help the US government combat offshore tax evasion by US persons. These include US citizens, green card holders, or persons who are otherwise tax residents under US law. Clients of banks, trust companies (including PTCs – private trust companies), who are US persons should be aware that their identities and financial information will be made available to the US IRS.

FATCA requires US persons, including those living outside the US, to report to the US tax authorities their financial accounts held in other jurisdictions, and requires foreign financial institutions ("FFI") to report the identity of their US customers and their financial information.

Under FATCA, the definition of "FFI" is very broad and encompasses a number of entities generally not considered to be financial institutions. It is crucial that US persons determine whether the non-US entity they are dealing with is a FFI or not for FATCA purposes.

Governments around the world have entered into intergovernmental agreements ("IGA") with the US to implement the access to information required under FATCA. There are several types of IGA models which have been developed: Model 1A (Reciprocal), Model 1B (Nonreciprocal), Model 2 (with or without a preexisting TIEA or Tax Information Exchange Agreement.)

Just four days before FATCA became effective, China reached an agreement in substance with the US on June 26th 2014 on the terms of a Model 1A IGA to implement FATCA in China. Although China and the US have not officially signed the IGA but only "initialed" it, the US will treat China as equivalent to having an IGA in effect until the end of 2014.

Under a Model 1A agreement, FFIs (foreign financial institutions) in China have to report the relevant information on U.S. taxpayers to the Chinese government, which will then provide the information to the US government. Conversely, the Chinese government will also be able to receive information regarding Chinese taxpayers based in the US.

Three days before China initialed its IGA with the US, on June 23rd 2014, Taiwan agreed in substance and initialed a Model 2 IGA with the US.

Even earlier, on May 9th 2014, Hong Kong, like China and Taiwan, agreed in substance to enter into an IGA with the US. Similarly, Hong Kong has only "initialed" the IGA with the US but has not officially signed it yet. That will presumably take place later in 2014. The US will treat Hong Kong as equivalent to having an IGA in effect until the end of 2014.

While the IGA which China has agreed to enter into with the US is a Model 1A IGA, the one Hong Kong has agreed to enter into is a Model 2 IGA, with a pre-existing TIEA. Under the Model 2 IGA, financial institutions in Hong Kong will need to register and conclude separate individual agreements with the US IRS. Under these agreements, the institutions will seek consent of their account holders who are US taxpayers to report their account information to the IRS on an annual basis. The operation of the Model 2 IGA will be supplemented by exchange of information at the

government level on a need basis and upon request pursuant to the TIEA signed between Hong Kong and the US (see prior coverage in our March 2014 newsletter as attached).

The essential difference between China's Model 1A IGA and Hong Kong's Model 2 IGA is as follows. In China, financial institutions have to report account information of US taxpayers to the Chinese government, which will transmit such information to the US IRS. In Hong Kong, on the other hand, financial institutions have to report the relevant account information of US taxpayers to the US IRS directly.

The Taiwan IGA is different from both the China's IGA and the Hong Kong IGA. Taiwan has initialed a Model 2 IGA without a preexisting TIEA. Therefore, while financial institutions in Taiwan, like those in Hong Kong, have to report the relevant account information of US taxpayers to the US IRS directly, there is no mechanism to provide additional information by Taiwan to the US at the government level since Taiwan does not have a TIEA in place with the US. In practice, despite the lack of a TIEA, it is quite possible that informal exchange of information may take place between the two governments, so that additional information is provided by Taiwan to the US.

As of July 1st 2014, a total of thirty nine countries have finalized and signed IGAs with the US. Fifty nine countries have "initialed" but not yet signed off on the IGAs. Three countries are "in dialogue", that is, in the middle of negotiations, with another three "exploring options" of entering into IGAs with the US. Out of these jurisdictions, besides China, Hong Kong and Taiwan, the other Asian jurisdictions are: Australia ("signed" Model 1A IGA), Japan ("signed" Model 2 IGA), Korea ("initialed"), Malaysia ("initialed"), New Zealand ("signed" Model 1A IGA) and Singapore ("initialed").

Below is the current IGA status of selected jurisdictions:

Jurisdiction	**Status**	**Model**	**Date signed / initialed**
Bermuda	Signed	Model 2 with preexisting TIEA or DTC *	12/19/2013
BVI	Signed	Model 1B - Nonreciprocal with preexisting TIEA or DTC	6/30/2014
Cayman Islands	Signed	Model 1B - Nonreciprocal with preexisting TIEA or DTC	11/29/2013
Cyprus	Initialed	Model 1A – Reciprocal	4/22/2014
Guernsey	Signed	Model 1A - Reciprocal	12/13/2013
Isle of Man	Signed	Model 1A – Reciprocal	12/13/2013
Jersey	Signed	Model 1A - Reciprocal	12/13/2013
Liechtenstein	Signed	Model 1A - Reciprocal	5/19/2014
Singapore	Initialed	Model 1A – Reciprocal	5/5/2014
Switzerland	Signed	Model 2 – with preexisting TIEA or DTC	2/14/2013
Turks & Caicos Islands	Initialed	Model 1A – Reciprocal	5/12/2014

* DTC refers to double tax convention

While each financial institution may have their own questionnaire for customers so as to determine whether the customer is a US person, the US IRS generally requests that financial institutions use a Form W8-BEN for individuals to declare that they are non-US persons for US tax purposes. For

entities (that is, not individuals) who wish to claim they are non-US for tax purposes, Form W8-BEN-E is used instead. Recently, Form W8-BEN-E has been revised and expanded to 8 pages in length. It has been speculated that a more detailed version of Form W8-BEN is being planned by the US IRS to replace the current version. Presumably, the new Form W8-BEN will require more questions to be answered in order for an individual to claim non-US tax status.

While most of the large banks and financial firms have been anticipating and preparing for compliance with FATCA since the law was enacted a couple of years ago, many of the smaller size firms and individuals are still relatively unprepared for FATCA. This is especially true for individuals who have established trusts which use holding companies to own and manage assets. Because of the broad sweep of FATCA's definition of a FFI, most holding companies used within a trust structure will find themselves classified as a FFI. Therefore, it is important for both financial firms (including companies holding assets on behalf of a trust) and individuals involved with trust structures to understand clearly what the implications to them are under the newly effective FATCA.

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