Houston Business & Tax Law Journal

2015

Houston Business and Tax Law Journal

15 Hous. Bus. & Tax L.J. 300

LENGTH: 13551 words

CONTENT: DESPERATE TIMES CALL FOR DESPERATE MEASURES: THE COST TO MULTINATIONAL CORPORATIONS OF IMPLEMENTING FATCA

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I.

Welcome to Gotham City, U.S.A.

Every seemingly immortal super hero has an equally appalling, yet brilliant, villain: Superman and Lex Luthor, Professor Xavier and Magneto, Batman and Joker ... Tax Evasion and FATCA? Or is it FATCA and Tax Evasion? The problem with determining which is the hero and which is the villain is a matter of perspective. For the United States government, the officers of whom have grown tired and weary from losing billions of dollars to tax evasion strategies employed by multinational corporations, the Foreign Account Tax Compliance Act (FATCA) is nothing short of a knight in shining armor. [n1] However, for multinational corporations facing an unattractive and uncompetitive international taxation system, FATCA is nothing but an additional thorn in an already-wounded side.

This note will explore (1) the background upon which the FATCA legislation was enacted, (2) the heroic efforts the United States government expects from FATCA with regards to tax evasion, (3) the villainous results multinational corporations will be forced to contend with as a result of FATCA, and (4) alternative approaches to reaching mutually-agreeable results.

II.

Evolution of the Corporate Climate: Change Is Not Reserved For the X-Men

The Foreign Account Tax Compliance Act was enacted to combat specific tax evasion issues that are rampant in the corporate world. [n2] This section is intended to provide a basic understanding of the United States' currently-enacted system of taxation, as well as an overview of the overarching issue of tax evasion.

A.

Worldwide Taxation

The United States is one of the few first world countries to retain a worldwide system of taxation. [n3] Under the worldwide [*302] system of taxation, as opposed to a territorial regime, [n4] domestic corporations are taxed on revenues "from whatever source derived." [n5] The foreign earnings of a multinational corporation are taxed upon repatriation of those earnings into the United States, allowing for a temporary deferral of tax liability. [n6] Certain forms of foreign earnings however, are taxed immediately under the Internal Revenue Code Subpart F rules. [n7]

In an effort to mitigate the double taxation of revenue that is inherent in this system of worldwide taxation, the Code provides both direct and indirect credits to corporations for taxes paid to foreign jurisdictions. [n8]

To illustrate, assume Corporation P is a United States multinational corporation with a wholly owned subsidiary, Corporation S, incorporated in Canada. Corporation P has a tax liability of 10x in the United States, based on its income earned globally. During the year, Corporation S paid Corporation P a dividend and incurred a withholding tax of 2x on the dividend in Canada. The 10x tax liability of Corporation P in the United States is reduced by the already-paid 2x withholding tax in Canada, as Corporation P is deemed to have paid the Canadian withholding tax under Code section 901(a), leaving Corporation P [*303] with a 8x tax liability in the United States. [n9]

B.

The Opportunity to Evade

The United States' system of taxation is based on voluntary self-assessment and compliance. [n10] Taxpayers are expected to openly and honestly disclose all relevant annual income, as dictated by the Code, on an annual income tax return; failure to do so provides the Government with the opportunity to impose penalties and fines for any omission. [n11] If only all taxpayers were so open and honest in their annual disclosures! [n12]

As expected, this is not so. The system of voluntary compliance opens the floodgates to tax evasion opportunities. In an effort to more effectively understand the issue, the Internal Revenue Service (Service) performs calculations to estimate the "tax gap", or the amount of tax liability owed by taxpayers that is not paid in a timely manner. [n13] The latest released study in 2012, which includes statistical data for the year 2006, estimates the tax gap to be $ 385 billion. [n14] While the tax gap is composed of three components, non-filing, underreporting of tax owed, and underpayment, [n15] "the largest component of the tax gap is underreporting." [n16] In 2006, the Service estimated that $ 285 billion of the $ 290 billion tax gap related to tax year 2001 was [*304] attributable to underreporting. [n17]

The unfavorable nature of the United States' system of worldwide taxation, combined with an influx in the global investment climate, has led high-income tax payers, as well as multinational corporations, to shelter revenues in accounts outside of the United States, thereby avoiding taxation on foreign revenues. [n18] Recognizing the significance of this issue, the Senate's Permanent Subcommittee on Investigations conducted extensive research in 2008 to quantify the amount of offshore tax abuse. [n19]

According to the Subcommittee's report, "the United States loses an estimated $ 100 billion in tax revenues due to offshore tax abuses" each year. [n20] The investigation showcased multinational corporations using effective tax saving strategies that included housing large sums of money and assets in foreign shell companies and offshore trusts. [n21] Thus, allowing the assets to remain out of the United States and out of the hands of United States taxation authorities. [n22] Without a drastic move to undercut these tax evasion techniques, the United States seemed destined to lose billions of dollars each year to offshore accounts and clever cults of tax accountants and attorneys.

III.

It's a Bird, It's a Plane, It's ... FATCA?

On March 18, 2010, Congress enacted the Hiring Incentives to Restore Employment Act, colloquially known as the HIRE Act. [n23] Sections 501 through 541 of the HIRE Act represent the substantive portion of the Foreign Account Tax Compliance Act, or FATCA. [n24] The following discussion in this section is intended to provide a basic overview of the FATCA legislation, including the intended consequences of the legislation, the expected reporting requirements to comply with the legislation, the withholding tax penalty, and the obligatory collaboration with foreign governments.

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A.

Purpose and Intended Consequences

FATCA represents portions of the HIRE Act that add new Code sections aimed at combating the problem of tax evasion via the use of offshore accounts. [n25] The purpose of FATCA is plainly stated in the summary to the final FATCA regulations:

To prevent [...] abuse of the U.S. voluntary tax compliance system and address the use of offshore accounts to facilitate tax evasion, it is essential in today's global investment climate that reporting be available with respect to both the onshore and offshore accounts of U.S. taxpayers. This information reporting strengthens the integrity of the U.S. voluntary compliance system by placing U.S. taxpayers that have access to international investment opportunities on an equal footing with U.S. taxpayers that do not have such access or otherwise choose to invest within the United States. [n26]

It is clearly the intent of Congress to use FATCA as a primary means of combating tax evasion - FATCA aims to combat tax evasion by manipulating the voluntary compliance aspect of the taxation regime. [n27] While the FATCA regulations cast a broad net, "the Treasury and IRS have narrowed the scope of FATCA withholding to apply to specific types of entities identified in the legislation and those persons that pose a significant risk of tax evasion." [n28] Given this purpose and these [*306] strong assumptions, it is necessary to analyze the reporting requirements that are thrust onto taxpayers as a result of FATCA.

B.

The Basic Reporting Requirements

Generally, the FATCA regulations impose a thirty percent withholding penalty on certain fixed United States source payments not meeting the basic reporting requirements of the legislation. [n29] By threatening to penalize institutions that do not report their offshore revenue and assets through FATCA, the government assumes withholding agents will be exponentially more likely to comply voluntarily with the reporting requirements. [n30] At its most simplistic, FATCA provides institutions with three basic options: annually report certain account holder information to the Service, [n31] deduct and withhold a tax equal to thirty percent of applicable payments to account holders not meeting the annual reporting requirements, [n32] or close accounts with account holders that subject an institution to annual reporting. [n33]

Institutions upon which these reporting requirements have been thrust include both foreign financial institutions (FFIs) [n34] and non-financial foreign entities (NFFEs). [n35] In order to meet the annual reporting requirements, FFIs and NFFEs must enter into information sharing agreements with the Secretary of the Treasury (Secretary), whereby the institution agrees to provide the requisite information to the Secretary, as set forth in Code [*307] sections 1471 and 1472. [n36] The agreement is registered with the Service and commits the institution to withholding the penalty tax on noncompliant account holders and nonparticipating FFIs. [n37]

The information required to be provided to the Secretary, while similar for FFIs and NFFEs, varies slightly. FFIs must obtain and report the name, address, tax identification number, account number, and account balance or value of every United States account and/or account holder. [n38]

NFFEs are required to provide either a certification that the beneficial owner [n39] of the payment does not have any United States owners or, in the case of a beneficial owner with United States owners, the name, address, and tax identification number of each substantial United States owner. [n40]

Graciously, Congress has provided several exceptions to account reporting. [n41] FFIs are excluded from reporting account information for account holders with aggregate account balances less than $ 50,000. [n42] To prevent duplicative reporting, FFIs are not required to report account information if another FFI will be reporting the information to the Service. [n43] Additionally, withholdable payments outstanding on January 1, 2014, for which an FFI or NFFE does not have the appropriate documentation, are excludable from the penalty tax as grandfathered obligations. [n44] Lastly, and perhaps most importantly, the final regulations provide circumstances whereby an NFFE can be excepted from the withholding penalty. [n45] A NFFE that is both traded on a public stock exchange and participates actively in a trade or business, is not subject to the withholding penalty if it is the beneficial owner of a withholdable payment. [n46]

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C.

Certainty to Penalty

The 1940's brought significant changes to the American taxation system, necessitated by years of war and depression. [n47] The Revenue Act of 1942 [n48] greatly increased the amount of tax revenue collected and the number of Americans subject to income taxation. [n49] The Current Tax Payment Act, enacted in 1943 on the heels of the 1942 Revenue Act, did much more - it established the withholding tax structure that is still in force today. [n50] In summation, the costs of World

War II far exceeded the federal tax revenues being generated in the United States. n51 As a result, the Revenue Bill of 1942 imposed the Victory Tax, a five percent income tax on all individuals, in an attempt to generate greater tax revenue. n52 The Victory Tax was later repealed by the Income Tax Act of 1944. n53

The new FATCA thirty percent withholding changes the purpose of the withholding tax by using the payment as a penalty for noncompliance rather than as a tool for the preemptive collection of taxes.

Fortunately, the final regulations provide some relief for failures to withhold. n54 Under the final regulations, an entity that is required by FATCA to withhold and remit any withholding tax but fails to do so becomes liable for the tax owed. n55 In the same breath, an entity that does withhold amounts under FATCA when acting as a withholding agent is indemnified against the recipient for any claim based on the FATCA withholding. n56

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D.

Mitigating Factors Available to Foreign Countries

1.

Intergovernmental Agreements

As succinctly stated by the IRS, "in cases in which foreign law would prevent an FFI from complying with the terms of an FFI agreement, the Treasury Department has collaborated with other governments to develop two alternative intergovernmental agreements (IGAs) that facilitate FATCA implementation and further reduce burdens on FFIs in partner jurisdictions." n57

The Model 1 IGA was released by the Treasury Department on July 26, 2012. n58 The model was based on discussions already in process between the United States and partner countries. n59 The Model 2 IGA was released by the IRS on November 14, 2012, n60 and, while largely similar to the Model 1 IGA, the Model 2 IGA has two significant differences. n61 FFIs within a jurisdiction operating under a Model 2 IGA are required to report the required FATCA information directly to the IRS rather than reporting the information to their local government as dictated by the Model 1 IGA. n62 While this provision takes unwanted pressure off local governments, the cost of securely sending the required information directly to the IRS increases the cost of compliance to the reporting entity. n63 Lastly, under a Model 2 IGA, reciprocal reporting by the United States to the foreign jurisdiction is not mandatory, but optional. n64

Secrecy law waivers

A problem still exists, however, for reporting entities in jurisdictions that have not entered into IGAs with the United States. n65 The secrecy laws of tax havens n66 are what make these [*310] jurisdictions attractive to those looking to bypass United States taxation. n67 The FATCA provisions are written to prevent this behavior. n68 Under Code section 1471(b)(1)(F), if foreign law prevents a reporting entity from complying with FATCA, the reporting entity must attempt to obtain a "valid and effective [*311] waiver" of the secrecy law from each account holder. n69 If the waiver is not obtained, the reporting entity is required to close the account. n70

Unfortunately, there appear to be few options for reporting entities unless the local government chooses to enter into an IGA with the United States. As a result, the United States government is ensuring the policy reasons for enacting FATCA are met, either via compliance by reporting entities, collaboration with foreign jurisdictions, or refusing to do business with noncompliant account holders.

IV.

Faster Than a Speeding Bullet: FATCA's Wounding of Multinational Corporations

A large focus has been placed on the impact of FATCA to individual taxpayers, including those high-profile taxpayers that have rescinded their United States citizenship as a result of the legislation. n71 While the effect of FATCA to individual taxpayers is great, the effect of FATCA to corporate taxpayers is equally astounding. This two-part section surveys how multinational corporations are pulled within the reach of FATCA and what cost exists to corporations as a result of complying with the legislation.

A.

How Multinational Corporations Become Involved

While FATCA was enacted to purposefully target taxpayers guilty of tax evasion, the wide net cast by FATCA pulls in additional entities, including large multinational corporations. [n72] Without significant research or the assistance of a well-trained tax firm, FATCA can become a trap for the unwary: multinational corporations may be in violation of the FATCA requirements without knowing the reporting requirements apply. [n73] There are, primarily, three avenues by which multinational corporations are required to participate in FATCA: [*312] (1) if an entity within the structure is a FFI, (2) if an entity makes withholdable FDAP payments, and (3) if an entity receives withholdable payments. [n74]

1.

Foreign Financial Institution

While the name foreign financial institution may lead to a conclusion that nonfinancial businesses are exempt from the FATCA reporting requirements, the broadly-written definition encompasses more forms of business than one may expect. [n75]

At its most simplistic, foreign financial institutions are foreign entities with a substantial portion of business dedicated to holding financial assets for others or investing and trading securities. [n76] Do not assume that the definition of an FFI is so narrow as to only include banks. Several forms of FFIs are hidden in corporate structures like sleeping giants. [n77] These types of FFIs include non-United States retirement funds, [n78] treasury centers, [n79] holding companies [n80], and captive finance companies. [n81] The complex organizational structures of multinational corporations provide the perfect breeding ground for these [*313] beasts. [n82]

2.

Withholdable Payments

FATCA generally imposes on an entity an obligation to withhold thirty percent of payments qualifying as FDAP made to FFIs and NFFEs. [n83] As a result, the cumbersome reporting requirements imposed by FATCA are thrust upon entities that happen to make payments of FDAP income to includable entities. [n84] Multinational companies making withholdable payments to both third parties and intercompany parties must ensure the recipients are either FATCA compliant, or exempt entities under the final Regulations. [n85]

3.

Non-financial Foreign Entities

Foreign entities receiving withholdable payments may be subject to FATCA reporting requirements as well. [n86] Code section 1472 covers withholding issues with regards to non-financial entities. [n87] Under Code section 1472(a), a withholding agent is required to deduct and withhold thirty percent of a withholdable payment made to an entity that is itself a NFFE or has a beneficial owner that is a NFFE. [n88] NFFE's are able to meet certain requirements to waive the withholding requirement by withholding agents. [n89] However, this of course imposes the complex FATCA reporting requirements on these non-financial foreign entities receiving withholdable payments. [n90]

B.

The Cost of Compliance

Now that a cursory discussion of the complex requirements of FATCA has been concluded, a discussion of the cost of complying with those requirements can commence. The costs of complying to a large multinational corporation are not only financial, but are also denominated in reputation, talent, and time. [n91] A first step in complying with FATCA is classifying all business entities within the corporate structure according to the [*314] FATCA Regulations and guidance. [n92] Multinational corporations must consider how to engage in more transparent communication with counterparties, while also training employees to understand, and comply with the FATCA Regulations. [n93] A last hurdle for multinational corporations is to set reasonable expectations for both counterparties and internal parties regarding changes in payments and processes as a result of the withholding and compliance. [n94]

1.

Classifying Business Entities

To determine where companies are vulnerable to FATCA, a study must be conducted to identify and classify all business entities within the corporate structure under the FATCA Regulations. [n95] As previously discussed, multinational corporations with FFIs and NFFEs within the corporate structure are likely subject to FATCA reporting. [n96] But how does one practically determine whether an entity is a FFI or NFFE?

A business activity analysis is the collection of information to identify and document the functions and primary transactions of entities in an attempt to create a fluid understanding of business processes. [n97] A study completed by the Massachusetts Institution of Technology [n98] surveyed the various techniques for collecting data to understand and analyze work processes. [n99] The study suggests a mix of three approaches to most thoroughly analyze business activities and approaches: (1) conducting semi-structured interviews, (2) observing, and (3) independently verifying the information received. [n100] The cost and time to a multinational corporation to undertake this form of business analysis depends upon multiple factors including available staffing, number of entities, placement of foreign entities, and the like.

A company that has classified all entities according to the FATCA Regulations is not yet finished with compliance [*315] procedures. Entities deemed to be FFIs should be registered with the Service in order to avoid being withheld upon. [n101] FFIs wishing to avoid the hassle of the withholding penalty are required to enter into FFI agreements with the Service to allow the entity to be treated as a participating FFI. [n102] The Service provides two methods by which an entity may register with the Service: online and paper. [n103] From this registration process, the Service publishes a list of participating FFIs to alert withholding agents of the excepted status of the FFIs. [n104]

Once a company has undertaken the painstaking process of classifying the business entities, and has subsequently registered the participating FFIs with the Service, there is one practical consideration left - the level of exposure and impact of classifying an entity incorrectly. It is possible the mislabeling of an entity as a NFFE that is actually a FFI will push the participating FFIs within an affiliated group into non-participating status. Regardless of the consequence, corporations must be aware that failure to categorize entities with reasonable prudence could potentially be costly.

2.

Transparent Communications with Counterparties

The previous subsection explored the costs associated with classifying a corporation's own entities; however, the FATCA structure pairs entities together according to payor and recipient. A corporation making withholdable payments to another entity, be it intercompany, intracompany, or third party, must determine whether or not the payee is an entity exempt from withholding.

The final FATCA Regulations address the required documentation to identify the status of a payee in Regulations section 1.1471-3. [n105] Generally, the payee of a withholdable payment is the entity to whom the payment is remitted [n106], regardless of whether or not the entity is the beneficial owner of [*316] the payment. [n107] The more complicated determination, however, is not who the payee is, but whether or not the payee is an exempt entity.

The Service has provided that a withholding agent must determine a payee's status on "documentation that the withholding agent can reliably associate with such payment." [n108] Generally, a corporation can associate a payment with the appropriate documentation if: (1) the documentation is received prior to the payment, (2) it can be determined from the documentation how much of the payment relates to the piece of documentation, and (3) the corporation has no reason to believe the documentation is incorrect. [n109] Forms of documents acceptable to determine the status of the payee include withholding forms and certificates already in use by corporations. [n110]

The dominant cost of implementing this step is the request and maintenance of the proper documentation for all payees and withholdable payments. A corporation's staff will likely spend a significant amount of time communicating with counterparties to obtain the appropriate documentation for each withholdable payment. Additionally, the documentation must be organized and maintained for audit purposes for a set number of years. [n111] These costs will vary depending upon the number of withholdable payments a corporation makes and the number of counterparties with which an entity does business.

3.

Training individuals

To understand and execute new reporting procedures, employees must be well versed on the requirements of FATCA. A 2011 study estimated that corporations spend an annual average of $ 1,182 per employee to train those employees. [n112] That figure [*317] projects out to a large $ 156.2 billion in organizational training costs. [n113] Unfortunately, the generic organizational and leadership training received by employees does not cover the broad requirements of FATCA, requiring companies to create and execute specified training programs for FATCA alone.

a)

Documentation Collection and Review

A corporation making withholdable payments is required to obtain documentation from payees to determine the FATCA status of the payee, as discussed above. [n114] Meaning, the employees must know, and understand, how to review the documentation for reliability and completeness. [n115] Final Regulations section 1.1471-3(e) discusses in great detail the standards of knowledge an individual must use when reviewing documentation received. [n116] The broad standard of knowledge announced by the Service is as follows:

A withholding agent shall be considered to have reason to know that a claim of chapter 4 status is unreliable or incorrect if its knowledge of relevant facts or statements contained in the withholding certificates or other documentation is such that a reasonably prudent person in the position of the withholding agent would question the claims made. [n117]

This reasonably prudent person standard announced in the final Regulations is a common standard across legal disciplines, and it creates a hypothetical prudent person in the same or similar circumstances against whom the individual should [*318] compare his actions. [n118] In addition to the general standard of knowledge, withholding agents to new accounts opened after January 1, 2014 are deemed to know whether or not documentation is reliable when comparing the documentation to new customer files. [n119] With regards to the foreign status of a foreign individual or entity, however, a withholding agent is only charged with knowledge where the agent receives an indication of domestic status to the contrary. [n120]

Specific standards of knowledge relate to each form of reliable documentation as well. [n121] Perhaps most importantly is the requirement that a withholding agent relying on the review and maintenance of documentation by an agent is considered to know or have reason to know the facts within the knowledge of the agent. [n122]

The final Regulations also provide for an allowable reliance on reasonable presumptions rather than on documentation, when the documentation received is not reliable or when the proper documentation is not available. [n123] Generally, where the required documentation is available, the withholding agent may rely upon certain presumptions to determine the status of the payee, including status as a domestic or foreign entity, and status as a participating or non-participating FFI. [n124] A withholding agent that is unable to determine that particular form of FFI applying to a payee must assume the payee is a non-participating FFI for reasons of conservatism. [n125]

The lack of appropriate training for employees applying this [*319] presumption clause opens corporations to the possibility of negative repercussions. [n126] On one hand, a withholding agent that withholds on a withholdable payment because of presumptions made, and later determines the payee to be an exempt entity, is not liable for the withheld amount. [n127] Conversely, if a withholding agent fails to withhold because of presumptions made, the withholding agent is liable for all tax, interest, and penalties associated with the payment. [n128]

Finally, reviewers are able to rely on documentation obtained from a variety of additional sources, including shared databases [n129] and third-party providers. [n130] When relying upon these sources of data, withholding agents are still held to the same general standards of knowledge as applied to the documentation. [n131]

b)

When to Withhold

Employees that are trained to identify the appropriate FATCA characterization of payees by obtaining and maintaining the appropriate documentation have only completed half of the process. Once it has been determined that an entity is not exempt from FATCA withholding, employees must determine when and how to enforce the Regulations through the withholding mechanism.

Corporations that had previously not been required to withhold on certain payments will require new payment processes and payment software systems. New software programs alone cost corporations thousands of dollars. [n132] Each employee using the software must be given a license to use the software, which can cost thousands of dollars per user. [n133] [*320] Additionally, new software also requires training for employees that will be using the software, as well as consultants to configure and implement the software. [n134] The costs build quickly with no appreciable gain to the corporation.

The new withholding measures have the ability to affect several corporate departments. New contracts that are negotiated between corporations should include language speaking to FATCA requirements, including the possibility of contractually requiring the payee to provide the required documentation to the withholding agent to avoid withholding. The structure of a large corporation will likely be drastically impacted by the advent of FATCA.

In conclusion, a large cost to corporations of complying with FATCA will inevitably be the cost of training employees to implement and enforce the FATCA requirements in such a way as to avoid additional liability to the corporation.

4.

Relaying Reasonable Expectations

A corporation that is not exempt from FATCA is likely to fall within one of two situations: (1) the corporation will receive payments that are thirty percent less than expected, or (2) the corporation will make payments to counterparties that are thirty percent less than expected by the payee. Either way, certain measures must be taken to relay these expectations to either a Board of Directors or a customer for possible underpayment as a result of the thirty percent withholding.

a)

Financial Statement Impact

Growth and certainty are two key drivers behind financial forecasting. [n135] While, historically, the Securities and Exchange Commission (SEC) banned financial projections from publishing in an effort to protect against over-reliance by investors, the SEC now views the financial projections of corporations as valuable data. [n136] Regardless of this history, it is without question that a corporation has a duty to shareholders, future investors, and employees to accurately forecast and publish financial results upon which those same individuals may rely. [n137]

Financial projections become reality in the form of a [*321] corporation's Form 10-K filing. [n138] The Form 10-K is an annual filing with the SEC by corporations to report actual financial results for the previous year. [n139]

Because the Form 10-K is a public document, once the document has been published, shareholders, future investors, and employees are able to compare the actual reported financial results of a corporation to the previously forecasted financial speculations. [n140] While the publication of financial forecasts requires corporations to qualify the results as purely speculative in nature, [n141] it is not unreasonable for shareholders, future investors, and employees to lose faith in a corporation that reports results significantly lower than previously anticipated.

The enforcement of FATCA brings to light new forecasting issues for corporations. Entities within a corporation's organizational structure that will have withholding deducted from payments will experience a reduction in overall revenue. Additionally, as previously stated, entities that are characterized incorrectly for purposes of FATCA are still liable for the withholding that would have previously been deducted. [n142] If corporations do not plan for the reduction as a result of withholding in the financial forecast, the likelihood of overstating prospective income is great.

b)

Customer Relations Impact

The imposition of FATCA also has the potential to wreak havoc on the relationships corporations have with customers and counterparties. Corporations requesting documentation have the displeasure of working with recalcitrant account holders. [n143] Additionally, corporations are tasked with setting reasonable expectations for customers with regards to the receipt of less payment as a result of withholding. Each of these issues potentially leads to a loss of customers or business, both issues with which corporations should be extremely concerned.

FATCA requires entities to provide a significant amount of [*322] confidential or identifying information to withholding agents in an attempt to prove the status of an entity for withholding purposes. [n144] It is reasonable that customers and third parties act cautiously when withholding agents request confidential information; however, these account holders risk having the account closed for lack of compliance. [n145] As corporations are forced to close accounts with more customers for lack of compliance, corporations will have a more difficult time finding third parties with whom to do business.

An important practical question that must be answered by corporations is how many times should the corporation try to collect the documentation from a payee before characterizing the payee as recalcitrant? The Service has provided temporary relief from recalcitrant account holders by allowing withholding agents to maintain accounts with these recalcitrant account holders as long as payments to the account holders are withheld upon. [n146] Maintaining accounts with recalcitrant account holders requires additional steps be taken by the withholding agent. [n147] Corporations maintaining accounts with recalcitrant account holders are required to report the number of recalcitrant account holders and the balance of those accounts each year to the Service, creating additional time and documentation expenditures. [n148]

Similar to setting reasonable expectations with shareholders, corporations must set reasonable expectations with customers. Recalcitrant account holders may not be aware that in failing to comply with the documentation requirements, they will be penalized with the thirty percent withholding. [n149] Customers receiving less payment than was previously discussed or contracted can sour a business relationship quickly. Additionally, customers who provide documentation that cannot be reliably associated with the payment in question may also be penalized with the thirty percent withholding for lack of proving exempt status. [n150] In order to provide notice to these customers of the potential for withholding, corporations must implement and [*323] enforce a transparent system of communication with the customers.

FATCA not only changes the way corporations conduct business, but also requires significant financial outlay and the possibility of an erosion to the corporations' customer base. The costs of complying with FATCA are far more than financial: it hits the heart of a corporation - the investors, the employees, and the customers.

V.

Avoiding Kryptonite: A Search for FATCA Alternatives

The problems of tax avoidance and evasion are not new ones. [n151] A study performed in 1987 detailed the role corporations play in the tax evasion problem. [n152] At that time, corporate noncompliance with tax regulations represented over 25% of the tax gap issue. [n153] To promote compliance with tax regulations while also fostering the global business market, several attempts have been made to enact measures to further both goals. A discussion of previously enacted, and ineffective, measures will first be undertaken in this section, followed by a discussion of currently in-process measures, with a look to how the measures compare against FATCA.

A.

Been There, Done That: The Ineffectiveness of Previously-Enacted Measures

The two most prominent attempts at curbing tax evasion while attempting to foster global trade are (1) the usage of tax treaties and (2) the enactment of bank secrecy laws. As evidenced in the discussion that follows, however, these two measures stand in direct contravention with the FATCA legislation, making them, in effect, moot.

1.

In-Force Tax Treaties

Prior to the enactment of FATCA, the United States fostered information sharing between countries via income tax treaties [*324] and tax information exchange agreements. [n154] Conflicts between FATCA and treaty provisions will be resolved by allowing FATCA to override beneficial in-force tax treaties. Generally, Article 26 of the United States Model Income Tax Treaty [n155] requires countries entering into a tax treaty to exchange relevant tax information as required by the treaty itself or local country laws. [n156] In addition to the dozens of tax treaties that are currently in-force between the United States and partner countries, roughly twenty tax information exchange agreements (TIEAs)have also been executed. [n157]

The United States Model Income Tax Treaty necessitates that each country a party to the treaty exchange all information required to carry out the tax provisions of the partner country. [n158] The lack of specificity regarding the particular information required to be exchanged, mixed with the absence of any penalty for noncompliance, makes the tax treaty an ineffective means of curtailing tax evasion. [n159]

More to this point, dozens of tax treaties have been negotiated between the United States and partner countries, however, with regards to FATCA, the work has essentially been for nothing. In terms of superiority, any conflicting provision in a tax treaty is overridden by the corresponding FATCA provision. [n160] This has effectively made Article 26 of any negotiated tax treaty moot.

Unfortunately TIEAs provide little assistance to end the problem of tax evasion. TIEAs are often narrowly written as to only cover the production of tax information between countries when a criminal matter is involved. [n161] More frustrating is the common requirement that the issue falling under the TIEA be criminal in both jurisdictions, which is hardly ever the case when dealing with tax haven countries. [n162] In short, the TIEAs do little to aid the United States government's effort in preventing and prosecuting cases of tax evasion.

[*325] In summation, the shortcomings of the current agreements between the United States and partner countries in the form of tax treaties and TIEAs have prompted the need for a more comprehensive sharing arrangement.

2.

Bank Secrecy Laws

Agreements between the United States and partner countries have an added layer of complexity in the form of bank secrecy. Bank secrecy is a way for foreign banks to assist United States taxpayers in committing tax evasion by opening bank accounts in the names of corporate entities. [n163] These foreign banks, protected by secrecy laws in their own countries, are unable to disclose the confidential information of their account holders, thereby perpetuating the opportunity to evade United States taxes. [n164] In acknowledging the harmful impact of bank secrecy on the ability of countries to enforce compliance with tax reporting, the Organization for Economic Cooperation and Development (OECD) supported a movement to reduce bank secrecy by publishing a "blacklist" of tax haven [n165] countries. [n166] Countries are eligible for removal from the blacklist once the country's government agrees to reduce the local secrecy laws. [n167]

A promise to reduce secrecy laws is not enough to combat tax evasion. Under TIEA's, the information exchange agreement is limited to information that is legally obtainable in the normal course of administration of the requested country and does not include trade secrets. [n168] Due to this limitation, banking secrecy [*326] rules may excuse production of information under these agreements. [n169] This banking secrecy intertwines with FATCA in that foreign laws prohibiting the reporting of information required by FATCA will result in corporations closing accounts in those countries. Clearly, an attempt at reducing bank secrecy has not been an effective deterrent to the overall problem of tax evasion.

The lack of currently enforceable FATCA alternatives come up short in preventing tax evasion, proving FATCA to be the strongest deterrent available to the United States government at this time.

B.

Alternatives "In The Works"

While few options to FATCA exist that are currently enacted, several prospective options are in the proverbial legislative "pipeline". The repeal of the "check-the-box" regulations, in addition to a movement to a territorial tax regime, are both viable alternatives to FATCA.

1.

Repeal of "Check-the-Box" Regulations

The "check-the-box" regulations are a set of mechanical regulations that allow corporations to choose the tax treatment for all entities within the organizational structure. [n170] Under the regulations, corporations are able to choose to treat certain entities as disregarded for United States taxation purposes. [n171] This disregarded treatment allows corporations to flow profits into low-tax jurisdictions rather than having the earnings taxed in high-tax jurisdictions, thereby avoiding tax liability. [n172]

In 2009, the Obama administration included in a budget proposal the decision to repeal the "check-the-box" regulations. [n173] [*327] The proposal cited that the repeal would increase United States tax revenue by a net $ 86.5 billion. [n174] As imagined, however, this proposal to repeal the regulations found little love in the corporate community, [n175] and the proposal was removed from the final budgetary analysis. [n176] If repealed, corporations would be forced to restructure entire organizations, and tax planning mechanisms would be ineffective. [n177] Because this article focuses on minimizing cost to corporations, unless the repeal of the "check-the-box" regulations costs less than the cost of complying with FATCA, it will be deemed as an unreasonable alternative.

2.

Moving to a Territorial Regime

A last available alternative to FATCA is the movement to a territorial taxation regime, rather than the current worldwide system of taxation. As suggested in the President's Advisory Panel in 2005, a movement to a territorial system of taxation would increase taxation revenues and remove the disincentive to repatriate profits back to the United States. [n178] As a result, the movement to a territorial regime would be more cost effective than the current system of worldwide taxation, and would also eliminate the problem of tax evasion, as the United States would be concerned with profits derived in the United States only. [n179] In terms of cost to corporations, it would appear the movement to a territorial system of taxation would be the most effective means of balancing the interests of corporations against the interests of the government.

VI.

Caped Crusader or Menacing Maniac?

In an already unfavorable corporate tax climate, the burdensome reporting requirements under FATCA outweigh the benefit that is being generated for the government. When comparing the benefit the government is deriving from the [*328] legislation against the corporations' costs of complying with the legislation, the scale is tipped toward viewing FATCA as a terrible menace rather than as a prominent power. At least one alternative exists to FATCA: a movement to a territorial system of taxation. The movement would support the interests of both the United States government and large corporations by largely eliminating the problem of tax evasion while also reducing the costs of complying for corporations.

Legal Topics:

For related research and practice materials, see the following legal topics:
International LawAuthority to RegulateTaxationTax LawState & Local TaxesAdministration & ProceedingsTax Avoidance & EvasionTax LawState & Local TaxesIncome TaxCorporations & Unincorporated AssociationsGeneral Overview

FOOTNOTES:

n1. See U.S. S. Permanent Subcomm. on Investigations, 110th Cong., Tax Haven Banks and U.S. Tax Compliance (Comm. Print 2008) [hereinafter S. Investigations].

n2. T.D. 9610,78 Fed. Reg. 5874-01, 5874 (2013) [hereinafter FATCA Regs].

n3. See S. Republican Policy Comm., 113th Cong., Territorial vs. Worldwide Taxation (Comm. Print 2013) (John Barrasso) (stating that "among G-7 countries, only the U.S. has a worldwide tax system. [...] Eight OECD nations have worldwide systems, including the U.S., Greece, Ireland, South Korea, and Mexico. The other OECD nations with worldwide tax systems have top tax rates far below the top U.S. corporate tax rate.").

n4. The principle feature of a territorial system of taxation is the taxation of only income that is purely domestic. Several large territorial systems of taxation in which the United States conducts business provide exemptions of foreign income that meet certain requirements rather than a complete exemption of all foreign income. Staff of the Joint Comm. on Taxation, 112th Cong. Background and Selected Issues Related to the U.S. International Taxation System and Systems that Exempt Foreign Business Income (Comm. Print 2011).

n5. I.R.C. ß 61(a) (2014).

n6. See I.R.C. ß 951(a)(2014) (discussing the taxation of certain types of income of controlled foreign corporations).

n7. See generally I.R.C.ßß952 - 956 (2014). The subpart F rules of the Code seek to tax currently the otherwise deferred earnings of a controlled foreign corporation, depending upon the nature of the income. See I.R.C. ß 951. The general categories of subpart F income include passive-type income (interest, rents, royalties, dividends), insurance income, foreign base company sales and services income, foreign investments in United States property, illegal bribes and kickbacks, and income derived in a foreign country to which Code section 901(j) applies. I.R.C. ß 952(a). Subpart F income is treated as a deemed distribution in the current year and creates previously taxed income for the controlled foreign corporation. Id.

n8. I.R.C. ß 901(a). Code section 902(a) provides that a domestic corporation receiving a deemed dividend from a foreign corporation, of which it owns more than 10 percent, receives a credit on its against its United States tax for the same proportion of the foreign corporation's foreign income taxes. I.R.C. ß 902(a)(2014). Additionally, Code section 901(j) disallows any foreign tax credit for taxes paid to certain countries as identified by the Secretary of State. I.R.C. ß 901(j)(1)(A), (2)(A). As of December 2012, the countries for which credit is disallowed are as follows: Cuba, Iran, North Korea, Sudan, and Syria. Internal Revenue Service, Instructions for Form 1118, IRS.gov (Rev. 2014), http://www.irs.gov/pub/irs-pdf/i1118.pdf.

n9. I.R.C. ß 902(a).

n10. Helvering v. Mitchell, 303 U.S. 391, 399 (1938). See also Rev. Rul. 2007-20, 2007-14 I.R.B. 863 (discussing whether or not the system of tax compliance is truly voluntary - while taxpayers are allowed to calculate and report the appropriate amount of tax liability, the taxpayers are not allowed to determine whether or not the laws apply to them).

n11. Rev. Rul. 2007-20, 2007-14 I.R.B. 863.

n12. Revenue Ruling 2007-20 acknowledges and discusses taxpayer dependence upon the holding in Flora v. United States to not report and pay taxes. Rev. Rul. 2007-20, 2007-14 I.R.B. 863 (citing Flora v. U.S., 362 U.S. 145, 176 (1960)). In Flora, the Supreme Court reiterates that the United States' system of taxation is based upon "voluntary assessment and payment". Id.

n13. I.R.S. News Release FS-2012-6 (Jan. 2012), available at http://www.irs.gov/uac/IRS-Releases-2006-Tax-Gap-Estimates (explaining that the statistical analysis of the tax gap is undertaken only every few years due to the complex scope and breadth of the analysis).

n14. Id.

n15. See Eric Toder, What Is The Tax Gap?, Tax Notes, October 22, 2007, http://www.taxanalysts.com/www/freefiles.nsf/Files/TODER-28.pdf/$ file/TODER-28.pdf ("The non-filing gap is the tax not paid on time by taxpayers who have a legal requirement to file a tax return, but do not file on time. The underreporting gap is the tax owned by taxpayers who file returns on time, but underreport the amount of tax they owe. The underpayment gap is the loss of revenue owed by taxpayers who file returns on time, but do not pay their reported tax due on time.").

n16. Id.

n17. Id.

n18. FATCA Regs, supra note 2, at 5874.

n19. S. Investigation, supra note 1, at 4.

n20. Id. at 46.

n21. Id. at 46-47.

n22. Id. at 27.

n23. Hiring Incentives to Restore Employment Act, Pub. L. No. 111-147, 124 Stat. 71 (2010)[hereinafter HIRE Act].

n24. While the HIRE Act includes the promulgation of legislation surrounding other federal issues, the FATCA sections of the HIRE Act comprise a significant portion of the legislation. HIRE Act ßß501-541.

n25. FATCA Regs, supra note 2, at 5874.

n26. Id.

n27. Id. Congressional representatives and lobbyists have previously entered into discussions regarding appropriate alternatives to the worldwide taxation regime, assuming that the problem of tax evasion is in part due to the complicated and uncompetitive international taxation structure of the United States. The numerous discussions and bills have proven unsuccessful, as Congress has chosen to enact

FATCA over a move to a territorial taxation regime. See, e.g., H. Ways and Means Comm., 112th Cong., 1st Sess., Technical Explanation of the Ways and Means Discussion Draft Provisions to Establish a Participation Exemption System for the Taxation of Foreign Income, (Comm. Print 2011); Nat'l Comm. on Fiscal Responsibility and Reform, The Moment of Truth, 32-33 (2010); President's Econ. Recovery Advisory Board, Rep. on Tax Reform Options: Simplification, Compliance, and Corporate Taxation, 89 (2010).

n28. PricewaterhouseCoopers, LLP, The Widespread Reach of FATCA: How Will It Affect Your Business? (2013) (discussing the risk that companies with complex business structures and aggressive tax planning strategies pose to the problem of tax evasion). Following the enactment of the HIRE Act, several documents with preliminary guidance were published. Proposed Regulations were established by the Department of Treasury on February 15, 2012, followed by a period allowing for public commentary on the proposed regulations. Prop. Treas. Reg.ßß1.1471 - 1.1474, 77 Fed. Reg. 9022, 9022 (Feb. 15, 2012). In addition, several I.R.S. Notices (now, collectively known as the FATCA Notices) provided preliminary guidance. See, e.g., I.R.S. Notice 2010-60, 2010-37 I.R.B. 329; I.R.S. Notice 2011-34, 2011-19 I.R.B. 765; I.R.S. Notice 2011-53, 2011-32 I.R.B. 124. The Department of Treasury promulgated Final Regulations related to FATCA on January 28, 2013. FATCA Regs, supra note 2.

n29. Deloitte Tax, LLP, The Road Ahead: An In-Depth Analysis of the Final FATCA Regulations (2013).

n30. Frederic Behrens, Using a Sledgehammer to Crack a Nut: Why FATCA Will Not Stand, 2013 Wis. L. Rev. 205, 214 (2013).

n31. I.R.C. ß 1471(b)(1)(A)-(C)(2010).

n32. Id. at (D).

n33. Id. at (F)(ii).

n34. A foreign financial institution is defined as "any financial institution which is a foreign entity." A financial institution, by definition, is any entity that ordinarily accepts deposits, holds financial assets for other entities as "a substantial portion of its business", or is engaged in the trading or investing of securities. Id. at (d)(4)-(5).

n35. A nonfinancial foreign entity is defined as "any foreign entity which is not a financial institution" pursuant to Code section 1471(d)(5). I.R.C. ß 1472(d)(2012).

n36. I.R.C. ß 1471(b)(1).

n37. Treas. Reg. ß 1.1471-4 (1)(2012).

n38. I.R.C. ß 1471(c)(1)(A)-(D).

n39. The definition of beneficial owner for purposes of FATCA legislation is the same as that set forth in Regulations section 1.1441-1(c)(6): "the term beneficial owner means the person who is the owner of the income for tax purposes and who beneficially owns that income." Treas. Reg. ß 1.1471-1(b)(8) (citing Treas. Reg. ß 1.1441-1(c)(6)(2012)).

n40. I.R.C. ß 1472(b)(1)(A)-(B).

n41. I.R.C. ß 1471(d)(1)(B) (2012).

n42. Id. at (B)(ii).

n43. Id. at (d)(1)(C).

n44. Treas. Reg. ß 1.1471-2(b)(2012).

n45. Treas. Reg. ß 1.1472-1(c)(2012).

n46. Id. at (c)(1)(i). An NFFE is deemed active if less than 50% of the gross income of the NFFE for the previous year is comprised of passive income, including interest, rents, royalties, and dividends. Additionally, an entity must have a weighted average percentage of assets less than 50% of which give rise to passive-type income. This asset test is conducted on a quarterly basis. Id. at (c)(1)(iv).

n47. See, e.g., Jerry Tempalski, Revenue Effects of Major Tax Bills, 2-3 (U.S. Dep't of Treasury OTA, Working Paper 81, 2006).

n48. Revenue Bill of 1942, 56 Stat. 234, ß 450 (1942).

n49. Tempalski, supra note 47, at 4.

n50. Id. at 10.

n51. Id. at 2.

n52. Id. at 9.

n53. See Income Tax Act of 1944, 58 Stat. 234, ß 6 (1944).

n54. I.R.C. ß 1471(a) (2012).

n55. Id. ("Every person required to deduct and withhold any tax under this chapter is hereby made liable for such tax and is hereby indemnified against the claims and demands of any person for the amount of any payments made in accordance with the provisions of this chapter.").

n56. Id. at (a), (b)(3)(B)-(C).

n57. I.R.S. Notice 2013-69, 2013-46 I.R.B. 503.

n58. Model FATCA Intergovernmental Agreement ("IGA") Released, Investment Company Institute, 2012, available at http://www.ici.org/ops/fund_dist/memo2634 4#_ftn2.

n59. Id. A joint statement was released by the United States, France, Germany, Italy, Spain, and the United Kingdom, stating the intention to enter into intergovernmental agreements. Id.

n60. deloitte Tax, LLP, Comparison of IGA Model Agreements to Final Regulations, (2013), available at http://hb.betterregulation.com/external/Comparison %20of%20the%20final%20FATCA%20regulations%20to%20the%20model%20 IGAs%20-%2004%20Feb%2013.pdf [hereinafter Comparison of Models].

n61. Id.

n62. I.R.S. Notice 2013-69 at 2. See also Comparison of Models, supra note 59.

n63. Comparison of Models, supra note 59.

n64. Id.

n65. Unfortunately for the United States government, several G-20 countries have yet to enter into IGAs with the United States. The G-20 countries and the respective status of an IGA between the country and the United States are as follows:

Argentina	3	India	4	Saudi Arabia	5
Australia	3	Indonesia	5	South Africa	3
Brazil	4	Italy	1	Turkey	5
Canada	2	Japan	1	United Kingdom	1
China	5	Republic of Korea	5	United States	
France	1	Mexico	1	European Union	EU states monitored separately
Germany	1	Russia	4		

Legend

1	Agreement signed
2	Final negotiations underway
3	Actively engaged in a dialogue
4	Working to explore options
5	Dialogue not yet begun

G20 Members, 2013, available at http://www.g20.org/about_g20/g20_members (listing the current members of the G-20 group of countries); Intergovernmental agreement (IGA) monitor, PricewaterhouseCoopers, LLP, 2013, http://www.pwc.com/us/en/financial-services/publications/fatca-publications/intergovernmental-agreements-monitor.jhtml.

n66. A tax haven is recognizable via four key factors: (1) the country imposes no or nominal taxes on income; (2) the country has in place laws or administrative practices that give individuals and corporations the benefit of strict secrecy rules; (3) the country has a lack of transparency into the legislative, legal, and administrative processes; (4) the country does not require corporations or individuals to be engaged in active business activity. Organization for Economic Co-operation and Development, Countering Offshore Tax Evasion: Some Questions and Answers (2009).

n67. Jane G. Gravelle, Cong. Research Serv., R40623, Tax Havens: International Tax Avoidance and Evasion (2013).

n68. FATCA Regs, supra note 2, at 5874.

n69. I.R.C. ß 1471(b)(1)(F) (2012).

n70. Id.

n71. In 2011, approximately 1,780 United States expatriates denounced their United States citizenship as compared to the 280 citizens that did the same in 2008. Giles Broom, Rich Americans Give Up Their Passports, Bloomberg Businessweek, May 1, 2012. Among these citizens are celebrities such as billionaire co-founder of Facebook Inc. Eduardo Saverin. Aggressive politicians, such as Democratic Senator Jack Reed, are calling for these individuals to be banned from re-entry into the United States. Kathleen Hunter, Schumer Proposed Tax on People Like Facebook's Saverin, Bloomberg Businessweek, May 17, 2012.

n72. PricewaterhouseCoopers, LLP, supra note 28.

n73. Id.

n74. Id. See also Deloitte Tax, LLP, FATCA Frequently Asked Questions (FAQs) (2011).

n75. PricewaterhouseCoopers, LLP, supra note 28.

n76. I.R.C. ß 1471(d)(4)-(5) (2012).

n77. See Treas. Reg. 1.1471-5(5)(e)(1)(i) (2012).

n78. Several broad exemptions exist to allow leniency to non-United States retirement funds under the final regulations, however, companies should still be well-versed in the exemption requirements to ensure specific retirement funds are exempted from FFI status. Treas. Reg. ß 1.471-6(f).

n79. According to the final Regulations, a treasury center is an entity whose primary activity is "to enter into investment, hedging, and financial transactions with or for members of its expanded affiliated group." Treas. Reg. ß 1.1471-5(e)(5)(i)(D). Certain specific nonfinancial treasury centers within an organizational structure are excepted from inclusion as a FFI if they meet the definition of a treasury center (as defined above), are not a depository institution or custodial institution, and do not hold themselves out as an investment vehicles. Id. at (e)(5)(i)(A).

n80. A holding company is an entity whose primary activity consists of directly or indirectly holding any portion of the stock of a member of the expanded affiliated group of the entity. Treas. Reg. ß 1.1471-5(e)(5)(i)(C). As with the excepted treasury center, a holding company that is a nonfinancial entity by virtue of meeting the requirements of the final Regulations is not classified as a FFI. Id. at (e)(5)(i)(A).

n81. A captive insurance company is an entity whose primary activity is "to enter into financing [...] or leasing transactions with or for suppliers, distributors, dealers, franchisees, or customers of such entity or of any member of such entity's expanded affiliated group that is an active NFFE." Treas. Reg. ß 1.1471-5(e)(5)(i)(E). As with treasury centers and holding companies, a captive insurance company that is nonfinancial in nature and meets the requirements as defined in the final Regulations is excepted from FFI status. Id. at (e)(5)(i)(A).

n82. See id. at (e)(2)(E)(iii).

n83. Jennifer Wheater, FATCA and Funds - Where Are We Now?, 13 No. 2 Bus. L. Int'l 143, 145 (2012).

n84. Id. at 152.

n85. Id. at 146-52.

n86. FINAL FATCA REGULATIONS AMPLIFY BROAD SWEEP OF LEGISLATION FOR SECURITIES AND BANKING INDUSTRY (February 2013), 2013 WL 2319472.

n87. I.R.C. ß 1472 (2012).

n88. I.R.C. ß 1472(a).

n89. I.R.C. ß 1472(b).

n90. Id.

n91. PricewaterhouseCoopers, LLP, supra note 28, at 8.

n92. PricewaterhouseCoopers, LLP, supra note 28, at 2.

n93. PricewaterhouseCoopers, LLP, supra note 28, at 9.

n94. PricewaterhouseCoopers, LLP, supra note 28, at 8.

n95. PricewaterhouseCoopers, LLP, supra note 28, at 9.

n96. PricewaterhouseCoopers, LLP, supra note 28.

n97. Step B Analysis of Business Activity, New South Wales Government: State Records, http://www.records.nsw.gov.au/recordkeeping/dirks-manual/step-by-step-through-dirks/step-b/content-and-scope-of-step-b (last visited Dec. 5, 2013).

n98. Brian T. Pentland, et. al., Useful Descriptions of Organizational Processes: Collecting Data for the Process Handbook, Mass. Inst. of Tech. (1999).

n99. Id. at 1.

n100. Id. at 5.

n101. Treas. Reg. ß 1.1471-4(a) (2012).

n102. Treas. Reg. ß 1.1471-4(a). See also I.R.S. Notice 2013-69, 2013-46 I.R.B. 503.

n103. Rev. Proc. 2014-12, 2014-3 I.R.B. 1.

n104. The final regulations have named the list the "IRS FFI list" and expect the list to contain the names and identification numbers for all "participating FFIs, registered deemed-compliant FFIs, and reporting Model 1 FFIs." Treas. Reg. ß 1.1471-1(b)(67).

n105. Treas. Reg. ß 1.1471-3.

n106. Several exceptions exist with regards to foreign agents receiving payments. If the foreign agent is an NFFE, participating or deemed-compliant FFI, a flow-through entity, a United States intermediary or agent of a foreign person, territory financial institution, or disregarded entity, that entity will not be considered a payee for withholding purposes. Treas. Reg. ß 1.1471-3(a)(3)(2012).

n107. Treas. Reg. ß 1.1471-3(a)(1).

n108. Treas. Reg. ß 1.1471-3(b).

n109. Treas. Reg. ß 1.1471-3(c)(1). Appropriate levels of knowledge with regards to the review of documentation received from payees is discussed in subsection iii below.

n110. Types of acceptable forms of documentation include Form W-9, Form W-8BEN (Withholding certificate of a beneficial owner), Form W-8IMY (Withholding certificate of an intermediary, flow-through entity, or United States branch), Form W-8EXP (Certificate for exempt status), Form W-8ECI (Certificate for effectively connected income). Treas. Reg. ß 1.1471-3(c)(3). Each form has its own set of requirements for validity, most including a statement of withholding given under penalty of perjury. Id.

n111. Treas. Reg. ß 1.1471-3(c)(6)(iii). The final regulations specifically address record retention by providing that a withholding agent is required to keep the withholding documentation for as long as the documentation is relevant to the withholding agent's tax liability. Id. Additionally, the withholding agent has the option of keeping original or copied versions of the documentation. Id.

n112. Laurie Miller, American Society for Training & Development, State of the Industry Report: Organizations Continue to Invest in Workplace Learning (2012).

n113. Id.

n114. Treas. Reg. ß 1.1471-3(b) (2012).

n115. The final regulations require a withholding agent to review each withholding statement, owner reporting statement, withholding certificate, written statement, and all documentary evidence and "must verify that the information contained on the withholding certificate, written statement, and documentary evidence is consistent with the information on the withholding statement or owner reporting statement." Treas. Reg. ß 1.1471-3(e)(4)(vi)(A)(1)-(2).

n116. Treas. Reg. ß 1.1471-3(e). The penalty for not withholding when a certain standard of knowledge is obtained by the corporation can have severe consequences for the corporation: "A withholding agent shall be liable for tax, interest, and penalties to the extent provided under section 1474 and the regulations under that section if it fails to withhold the correct amount despite knowing or having reason to know the amount required to be withheld. A withholding agent that cannot reliably associate the payment with documentation and fails to act in accordance with the presumption rules set forth in [...] this section may also be liable for tax, interest, and penalties." Id. at (e)(1).

n117. Id. at (e)(4).

n118. The prudent person, synonymous with the reasonable person, is defined as "[a] hypothetical person used as a legal standard, especially to determine whether someone acted with negligence; specifically, a person who exercises the degree of attention, knowledge, intelligence, and judgment that society requires of its members for the protection of their own and of others' interests." Black's Law Dictionary 1380-81 (9th ed. 2009).

n119. Treas. Reg. ß 1.1471-3(e)(4)(2012).

n120. Id.

n121. The most common piece of documentation is the withholding certificate, which requires, "[a] withholding agent has reason to know that a withholding certificate provided by a person is unreliable or incorrect if the withholding certificate is incomplete [...], contains any information that is inconsistent with the person's claim, the withholding agent has other account information that is inconsistent with the person's claim, or the withholding certificate lacks information necessary to establish entitlement to an exemption from withholding [...]." Treas. Reg. ß 1.1471-3(e)(4)(ii). Less common specific standards of knowledge for written statements, documentary evidence, and documentation received from flow-through entities and intermediaries are detailed in sections 1.1471-3(e)(4)(iii), (iv), and (vi). Id. at (e)(4)(ii)-(vi).

n122. Treas. Reg. ß 1.1471-3(e)(4)(ii).

n123. Treas. Reg. ß 1.1471-3(f).

n124. Id. at (f)(1).

n125. Id. at (f)(4).

n126. Id. at (f)(9).

n127. Id.

n128. Id.

n129. Databases include the electronic collection and maintenance of documentation by an agent of the withholding agent. The database may be a shared database, meaning it services more than one withholding agent, as long as the information is readily available to all withholding agents when needed, and the time at which the data was input or transmitted must be easily discernable from the database deliverable. Treas. Reg. ß 1.1471-3(c)(9)(i)(2012).

n130. Strict requirements apply to data provided by a third-party data provider. Generally, the third-party data provider must be in the business of credit or business reporting and have reviewed the documentation prior to providing it to the withholding agent. Id. at (c)(9)(ii).

n131. Id. at (c)(9)(i-ii).

n132. Oracle Technology Global Price List, Oracle Corporation, (Sept. 2013), available at http://www.oracle.com/us/corporate/pricing/price-lists/business-intelligence-price-list-071347.pdf.

n133. Id.

n134. Id.

n135. Tony Vadasz, Accurate Forecasting: A Fundamental Part of Financial Management, Sarbanes-Oxley Compliance J. (2005).

n136. See John Poole, Improving the Reliability of Management Forecasts, 14 J. Corp. L. 547, 548-49 (1989).

n137. Id. at 555 (citing Beecher v. Able, 374 F. Supp. 341, 348 (S.D.N.Y. 1974)).

n138. Form 10-K, U.S. Sec. & Exch. Comm'n, available at http://www.sec.gov/about/forms/form10-k.pdf.

n139. Id.

n140. Id.

n141. See Poole, supra note 139, at 555 (citing Sawyer v. Prickett, 86 U.S. 146, 157 (1875); Moser v. New York Life Ins. Co., 151 F.2d 396, 397 (9th Cir. 1945); McElrath v. Elec. Inv. Co., 114 Minn. 358, 361, 131 N.W. 380, 381 (1911).)

n142. I.R.C. ß 1471(a) (2012).

n143. Recalcitrant account holders are those individuals or entities that refuse to provide the documentation that has been requested for purposes of determining the individual or entity status for FATCA. I.R.C. ß 1471(d)(6).

n144. Treas. Reg. ß 1.1471-3(b) (2012).

n145. Treas. Reg. ß 1.1471-5(g)(2).

n146. It is stressed that allowing accounts to remain open with recalcitrant account holders is temporary relief only. Long-term recalcitrant accounts should be closed after a reasonable period of time. This reasonable period is not further defined with any specificity. I.R.S. Notice 2011-34, 2011-19 I.R.B. 765.

n147. Treas. Reg. ß 1.1471-4(d)(6)(i).

n148. Id.

n149. I.R.S. Notice 2011-34, 2011-19 I.R.B. 765.

n150. I.R.C. ß 1471(a) (2012).

n151. There is a fine line between tax avoidance and tax evasion. Tax avoidance is the calculation of lower tax liability as a result of aggressive tax positions. Tax avoidance is legal as long as the positions taken are legal. Tax evasion is the willful attempt to avoid the payment of additional tax when the additional tax is due. While tax evasion requires knowledge of evasive behavior, it does not require a malicious motive. Mark Turner, Build An Awareness of Unlawful Tax Evasion to Ensure Avoidance, Thomson: Practical Tax Strategies (2008).

n152. I.R.S., Pub. 1415, Net Tax Gap and Remittance Gap Estimates (1990).

n153. Id.

n154. See Hearing on Banking Secrecy Practices and Wealthy American Taxpayers Before the H. Comm. on Ways and Means, 111th Cong. (2009) [hereinafter Secrecy Hearings].

n155. I.R.S., U.S. Model Income Tax Convention of Nov. 15, 2006 (2006).

n156. Id.

n157. Secrecy Hearings, supra note 157 (statement of Patrick J. Tiberi).

n158. I.R.S., U.S. Model Income Tax Convention of Nov. 15, 2006 (2006).

n159. Id.

n160. Foreign Bank Account Reporting and Tax Compliance: Hearing Before the Subcomm. on Select Revenue Measures of the H. Comm. on Ways and Means, 111th Cong. (2009) (statement of Dirk Suringa).

n161. Secrecy Hearings, supra note 157 (statement of Reuven S. Avi-Yonah).

n162. Id.

n163. S. Investigation, supra note 1. The Department of Homeland Security's investigation brought to light the fraudulent banking practices of two large foreign banks: LGT Bank in Liechtenstein and UBS AG. As part of the investigation, the Subcommittee reported the following insight regarding bank secrecy and the connection with tax evasion: "From at least 2000 to 2007, LGT and USB employed banking practices that could facilitate, and have resulted in, tax evasion by their U.S. clients, including assisting clients to open accounts in the names of offshore entities; advising clients on complex offshore structures to hide ownership of asset; using client code names; and disguising asset transfers into and from accounts." Id. at 16.

N164. U.S. S. Permanent Subcomm. on Investigations, 109th Cong., 2nd Sess., Tax Haven Abuses: The Enablers, The Tools and Secrecy (Comm. Print 2006).

n165. Organization for Economic Co-operation and Development, Countering Offshore Tax Evasion: Some Questions and Answers (2009).

n166. See Organization for Economic Co-operation and Development, 2000 Progress Report: Towards Global Tax Co-operation: Progress in Identifying and Eliminating Harmful Tax Practices 17 (2000). See also David Crawford, Tax Havens Pledge to Ease Secrecy Laws, Wall St. J., Mar. 13, 2009, at A1.

n167. See also David Crawford, Tax Havens Pledge to Ease Secrecy Laws, Wall St. J., Mar. 13, 2009, at A1.

n168. Susan Morse, Tax Compliance and Norm Formation Under High-Penalty Regimes, 44 Conn. L. Rev. 675, 707 (2012).

n169. Id.

n170. The regulations are promulgated in the Regulations sections 301.7701-1 to 301.7701-4. Treas. Reg.ßß301.7701-1 to -4 (2012).

n171. Jane G. Gravelle, International Corporate Income Tax Reform: Issues and Proposals, 9 Fla. Tax Rev. 469, 483-84 (2009).

n172. The following example provides a clear picture of how these regulations foster tax evasion:

Loans from an affiliate in a tax haven to an affiliate in a high-tax country can generate interest deductions in the high-tax country, but not lead to taxation under Subpart F for the interest income paid to the tax haven because, from the point of view of the U.S. tax authorities, the two affiliates are one company.

Id.

n173. Ryan J. Donmoyer, Obama Seeks End of Corporate Tax Break to Raise $ 190 Billion, Bloomberg.com (May 9, 2009), http://www.bloomberg.com/apps/news?pid=new sarchive&sid=a4.7CIfqd5h0.

n174. Id.

n175. Id. See also Alston & Baird, LLP, Check the Box Proposal Raises Hackles (2009).

n176. Kevin Drawbaugh & Andy Sullivan, Insight: How Treasury's Tax Loophole Mistake Saves Companies Billions Each Year, Reuters Online (May 30, 2013), http://www.reuters.com/article/2013/05/31/us-usa-tax-checkthebox-insight-idUSBRE94T17K20130531.

n177. Jane G. Gravelle, Cong. Research Serv., R40623, Tax Havens: International Tax Avoidance and Evasion (2013).

n178. President's Advisory Panel on Federal Tax Reform, Simple, Fair, and Pro-Growth: Proposals to Fix America's Tax System (2005).

n179. Gravelle, supra note 174, at 491.