**EXPLANATORY MEMORANDUM TO**

**THE INTERNATIONAL TAX COMPLIANCE (UNITED STATES OF AMERICA) REGULATIONS 2014**

**2014 No. 1506**

**1.** This explanatory memorandum has been prepared by HM Treasury and is laid before the House of Commons by Command of Her Majesty.

This memorandum contains information for the Select Committee on Statutory Instruments.

2. **Purpose of the instrument**

2.1. These Regulations replace the International Tax Compliance (United States of America) Regulations 2013 (S.I. 2013/1962, 'the 2013 Regulations'), which are revoked.

2.2. The instrument implements the Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the United States of America to Improve International Tax Compliance and to Implement FATCA, signed on 12 September 2012 ("the Agreement"), as that Agreement has effect from time to time. The Agreement was amended by an Exchange of Notes between the two governments dated 3rd of June and 7th June 2013.

2.3. The Agreement, as amended will come into force when the necessary internal procedures for entry into force have been completed and written notification is provided to the other party.

**3. Matters of special interest to the Select Committee on Statutory Instruments**

3.1. The 2013 Regulations were reported for doubtful vires by the Select Committee on Statutory Instruments in the Third Report of Session 2013 -2014 as the regulations adopted revised timelines in implementing the treaty although the treaty had not been formally amended.

3.2. Article 7 of the Agreement grants the UK the benefit of any more favourable terms in any equivalent Inter-Governmental Agreement between the US and other Partner Jurisdictions when the agreement containing the beneficial clause has been brought into force. The more favourable terms apply automatically as if they were specified in the Agreement.

3.3. Since the 2013 Regulations came into force, other jurisdictions (the Cayman Islands and Mexico) have entered into, and brought into force, equivalent agreements with the US which contain the revised later start date of 30 June 2014. Article 4 of these

agreements also contains provisions permitting the use of definitions in relevant US Treasury Regulations in place of corresponding definitions in the treaty. These agreements can be found at http://www.treasury.gov/resource-center/tax-policy/treaties/Pages/FATCA.aspx.

3.4. Therefore, under the terms of the Agreement the UK is now able to properly reflect the revised timelines and other relevant provisions in the US Treasury Regulations in these Regulations implementing the Agreement.

## 4. Legislative Context

4.1. The Agreement provides for mutual exchange of tax information between the tax authorities of the two States. (The UK has agreed to provide the US with certain information about the accounts of US taxpayers who hold accounts in UK financial institutions, and about certain payments made by UK financial institutions to financial institutions in other jurisdictions that do not have an agreement with the US).

4.2. Further, in relation to UK financial institutions within the scope of the Agreement, the US has agreed not to impose a withholding tax that it would otherwise seek to apply to UK financial institutions with US source income. Those institutions would, absent the Agreement, be required to supply the IRS with certain information about account holders who are US taxpayers, or otherwise be subject to withholding tax. However the Data Protection Act 1998 would preclude financial institutions within the UK's jurisdiction from supplying such information directly to the US.

4.3. The instrument implements the Agreement, by enabling HM Revenue & Customs (HMRC) to obtain from UK financial institutions the information the UK has agreed to provide to the US, and so ensures that UK will receive reciprocal exchange of tax information from the US.

4.4. Information passed by UK financial institutions to HMRC under this instrument will, as required by the Agreement, be automatically exchanged annually with the United States Internal Revenue Service (IRS) as envisaged by Article 27 of the Convention between the United Kingdom of Great Britain and Northern Ireland and the Government of the United States of America for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and Capital Gains.

4.5. This instrument, pursuant to the UK's obligations in the Agreement, obliges UK financial institutions to pass to HMRC information about US taxpayers and so includes a requirement to put in place arrangements to obtain details of the country of tax residence of account holders. This allows financial institutions to introduce systems for collecting and maintaining information whilst also enabling compliance with data protection rules.

4.6. This requirement will relate only to accounts opened on or after the date that these Regulations come into force.

4.7. The Agreement include provisions that certain procedures and definitions set out in US Treasury Regulations (the US Treasury Regulations Relating to Information Reporting by Foreign Financial Institutions and Withholding on Certain Payments to Foreign Financial Institutions and Other Foreign Entities) may be adopted in implementing the Agreement. Provisions equivalent to the US Treasury Regulations have therefore been adopted in relation to the rule relating to currency translation and the rule relating to modification of due diligence requirements.

## 5. Territorial Extent and Application

5.1. This instrument applies to all of the United Kingdom.

## 6. European Convention on Human Rights

6.1. As the instrument is subject to negative resolution procedure and does not amend primary legislation, no statement is required.

## 7. Policy background

- What is being done and why

7.1. The Foreign Account Tax Compliance Act (FATCA), which is part of the US Hiring Incentives to Restore Employment Act of 2010, aims to combat tax evasion by US tax residents using foreign accounts.

7.2. It includes certain provisions on withholding taxes and requires financial institutions outside the US to pass information about their US customers to the US tax authorities, the Internal Revenue Services (IRS). Failure to meet these new reporting obligations would result in a 30 per cent withholding tax on any US source income held by the financial institutions. Draft US regulations setting out the implementation details were published in February 2012.

7.3. The FATCA provisions potentially imposed new and substantial burdens on UK businesses in identifying US taxpayers, and registering and reporting information to the IRS. Significantly for UK institutions the Data Protection Act precludes financial institutions from passing on such information.

7.4. The UK Government (along with France, Germany, Italy, and Spain) and with the support of the European Commission took part in joint discussions with the US Government to explore an intergovernmental approach to FATCA, supporting the overall aim to combat tax evasion, while reducing risks and burdens on financial institutions. A model intergovernmental agreement (IGA) was developed and published

in July 2012.

7.5. The UK and the US subsequently signed an agreement based on the IGA – the 'UK-US Agreement to Improve International Tax Compliance and to Implement FATCA' - in September 2012 (the "Agreement").

7.6. On 9 April 2013 the Government - along with France, Germany, Italy and Spain - also announced an agreement to develop and pilot multilateral tax information exchange based on the Model Intergovernmental Agreement to Improve International Tax Compliance and to Implement FATCA. The model will therefore form the basis of a new international standard of automatic exchange of information.

7.7. Since the UK and the US signed the Agreement, the US's domestic legislation has been the subject of some revisions. The US has formally announced by Notice a change to the implementation time line, and this is reflected in the coming into force date of these Regulations.

7.8. The Regulations make provisions in relation to imposing penalties for breach of obligations under the Regulations, including the imposition of daily penalties which where were not dealt with in the 2013 Regulations

- Consolidation

7.9. These Regulations revoke and replace the 2013 Regulations. In addition to the changes noted above, these Regulations contain further changes to clarify and simplify some parts of the 2013 Regulations, for example by setting out due diligence requirements in a tabular format.

## 8. Consultation outcome

8.1. These Regulations have not been subject to consultation as they make relatively minor changes to the effect of 2013 Regulations which were subject to extensive consultations. The changes clarify and simplify the 2013 Regulations and new provisions closely follow the International Tax Compliance (Crown Dependencies and Gibraltar) Regulations 2014 (S.I. 2014/520) which were also subject to extensive consultation.

## 9. Guidance

9.1. Working with business and advisers HMRC has produced guidance in relation to the 2013 Regulations which is accessible at http://www.hmrc.gov.uk/fatca/index.htm. HMRC will amend the relevant guidance to reflect changes made by these Regulations at the next update.

## 10. Impact

10.1. The impact on business, charities or voluntary bodies of these changes is negligible.

10.2. The impact on the public sector of these changes is negligible.

10.3. A Tax Information and Impact Note covering the 2013 Regulations was published on 31 May 2013 alongside a draft of those Regulations and is available on the HMRC website at http://www.hmrc.gov.uk/thelibrary/tiins.htm. It remains an accurate summary of the impacts that apply to this instrument.

## 11. Regulating small business

11.1. The legislation applies to small business.

11.2. To minimise the impact of the requirements on firms employing up to 20 people, HMRC are taking steps to deliver eased reporting requirements and, through negotiation with the US, have effectively removed the smallest financial institutions (for example Credit Unions and Community Investment Companies) from reporting completely. Sole traders are not affected.

11.3. Affected businesses have confirmed that these exemptions will reduce the impact on small business, carving out certain products that are typical to these financial institutions (for example ISA's) and reducing the level of reporting for those at lower risk of having access to evasion.

11.4. However the size of the business is not in itself a key determinant of the risk of tax evasion. As such any financial institution can be a reporting entity if it has US account holders of its products. For example a large "business" can have many financial institutions within its structure as reporting is on an entity by entity basis and large UK banking groups will have potentially thousands of financial institutions to report on within their business.

11.5. Therefore each financial institution may be a small entity, but the business in which they sit may not.

## 12. Monitoring & review

12.1. HMRC and HM Treasury will continue to liaise with stakeholders from time to time to discuss the implementation of the Regulations as part of continuing engagement with industry.

## 13. Contact

Fiona Hay or Wayne Strangwood at HM Revenue and Customs Tel: 03000 585 882 / 03000 585 493 or email: Fiona.hay@hmrc.gsi.gov.uk / wayne.a.strangwood@hmrc.gsi.gov.uk can answer any queries regarding the instrument.