Hong Kong signs Model 2 IGA under FATCA

Hong Kong and the United States signed an intergovernmental agreement (IGA) on 13 November 2014 that will facilitate compliance with FATCA by financial institutions in Hong Kong.

The US Foreign Account Tax Compliance Act ("FATCA") is a US law designed to combat tax evasion by US citizens and residents through the use of offshore accounts and investments. Generally, FATCA requires the identification and reporting of US taxpayers by Foreign Financial Institutions ("FFIs") outside of the US to the US Internal Revenue Service ("IRS"). In certain instances, FATCA withholding at the rate of 30% may also apply to certain types of US sourced income.

Within Asia Pacific, only Australia, New Zealand, Hong Kong and Japan have signed IGAs with the US Treasury to-date, thereby defining their obligations and exemptions under FATCA and/or local law. In particular, the Hong Kong IGA covers certain exemptions for financial institutions or products, including Mandatory Provident Fund schemes, registered financial institutions with a local client base, certain investment advisers and investment managers established in Hong Kong.

While the Hong Kong IGA largely mitigates the need for FATCA withholding, there still will be cases where FATCA withholding could apply, i.e. where withholdable payments (US source income or proceeds from the sale of property that generates US source income) are made to overseas Non-Participating FFIs.

Under the IGA, FFIs in Hong Kong may rely on a set of streamlined due diligence procedures to screen and identify US indicia in order to locate US accounts and clients for reporting purposes. For example, in determining whether a new individual account is a US account based on a customized self-certification received from the applicant, rather than more esoteric procedures under FATCA regulations, such as the use of US-centric withholding certificates. FFIs are required, however, to confirm the reasonableness of such certification which can be accomplished by reference to other documents obtained during the account opening process.

FFIs are required to report the relevant account information of US taxpayers directly to the IRS under the Model 2 IGA adopted by Hong Kong. This is supplemented by group requests made by the IRS to the Hong Kong Inland Revenue Department for exchange of information on relevant US taxpayers at a government level on a need basis. We expect that local authorities will only be involved by exception.

One of the largest misconceptions about FATCA is that FFIs without US customers will not be impacted. While the reporting aspects of FATCA are reduced when there are no US customers, the primary responsibility conferred upon FFIs is to be able to identify US customers through the new client due diligence process as well as through pre-existing client remediation.

Furthermore, companies that are not normally considered financial institutions may still be considered FFIs under the Hong Kong IGA (i.e. under the headings of custodial institution, depository institution, investment entity or specified insurance company) and may have due diligence and reporting requirements under FATCA.

Link to the Hong Kong IGA:
http://www.treasury.gov/resource-center/tax-policy/treaties/Documents/FATCA-Agreement-Hong%20Kong-11-13-2014.pdf

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