



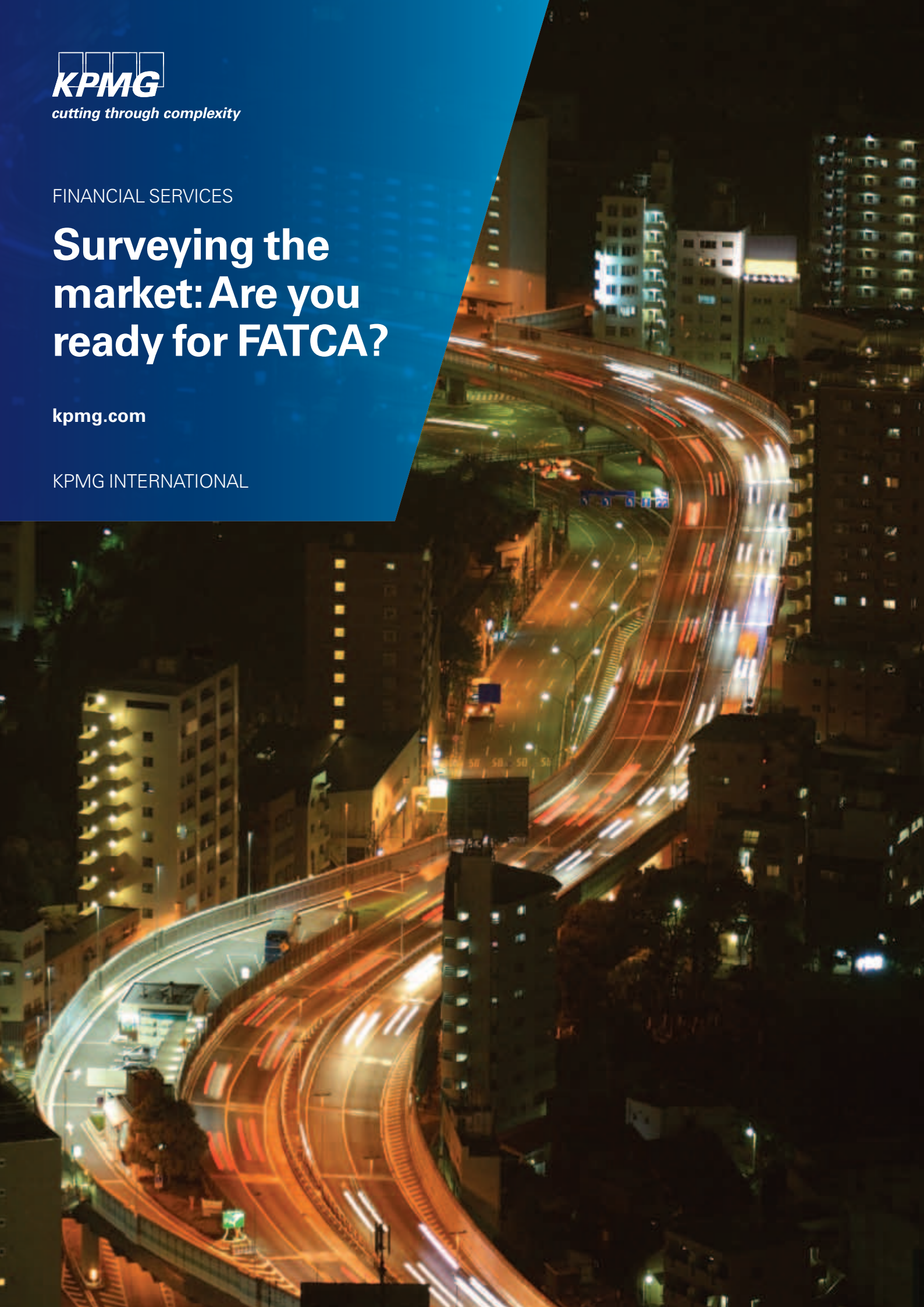
cutting through complexity


FINANCIAL SERVICES

Surveying the market: Are you ready for FATCA?

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Executive summary

Despite the name, the Foreign Account Tax Compliance Act (FATCA or the “Act”) is not simply a tax issue. Rather, compliance with the Act demands financial institutions adopt a cross-functional approach that incorporates their compliance, operations, tax, legal and information technology departments.

Furthermore, recent developments have confused what was already a thorny issue. Delays in publishing the final rules, and the emergence of potentially transformative intergovernmental agreements (IGAs), all of which are still being negotiated except for the IGAs with the United Kingdom and Denmark, have left financial institutions unable to fully define their FATCA-compliance projects, despite the imminent deadlines.

With the industry hobbled by so many uncertainties, KPMG’s Global FATCA professionals conducted a global survey of global and regional banks, insurance companies and various other financial institutions to assess participants’ awareness, attitudes and actions regarding FATCA: what steps have they taken thus far, what resources are they allocating to the task, how much time will compliance require, where do the key challenges lie?

By leveraging these responses, organizations will be equipped with practical benchmarking tools they can use in the development of their own FATCA compliance programs.

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Key survey findings include:

- **Status:** Most organizations have started to tackle FATCA compliance but are at various stages of preparedness. The majority (59 percent) say they have completed or are undertaking an impact assessment.
- **Project sponsor:** Tax (25 percent) and Compliance (24 percent) groups are the leading project sponsors within institutions.
- **Participants:** Half say all groups (compliance, operations, tax, legal and information technology) are participating in their FATCA compliance programs.
- **Impact:** Operations is expected to be the single area most impacted by the Act.
- **Implementation plan:** 86 percent of organizations intend to adopt some form of centralized implementation plan, as opposed to taking a purely decentralized approach by country or region.
- **Professional assistance:** Majority (57 percent) of organizations are using or plan to use a professional services firm(s) to assist with implementation.
- **People involved:** Majority (63 percent) estimate 10 or more people will be involved in FATCA planning and implementation, of which 18 percent say they will use more than 100 people.
- **Budget:** Median budget allocation is approximately US\$250,000, although there are wide disparities in the amount organizations plan to spend, ranging from less than US\$100,000 to more than US\$100 million.
- **Timescale:** Two-thirds anticipate FATCA implementation will take somewhere between six and 18 months, while 23 percent forecast it will require 18 months or more.
- **Readiness:** Less than half (45 percent) would have been able to meet the FATCA requirements by the original 1 January 2013 deadline for US Financial Institutions (USFI) and Foreign Financial Institutions (FFIs). Since the survey was conducted, Announcement 2012-42, issued by the US Department of the Treasury and Internal Revenue Service (IRS) on 24 October 2012, has extended the deadline for withholding agents to implement new account opening procedures until 1 January 2014.
- **IGA awareness:** More than half (56 percent) were not aware of any governments in the countries in which they operate intending to enter into an intergovernmental agreement with the IRS to maintain domestic reporting. The US Treasury Department subsequently announced on 8 November 2012 that it is discussing the development of IGAs with more than 50 countries, which should raise awareness of the issue.
- **Process revision:** Almost all organizations (92 percent) feel their client on-boarding, customer identification or documentation processes will need to be revised as a result of FATCA.
- **Greatest compliance challenge:** Account identification requirements emerge as the top-ranked FATCA-related compliance challenge, followed by documentation requirements and systems changes.
- **Existing program leverage:** Four-fifths of organizations plan to leverage their AML/KYC compliance programs to help satisfy the FATCA requirements.

As the FATCA deadlines approach, it is crucial that financial institutions focus their efforts on the most pressing issues, such as identification of US withholding agents (USWAs) and FFIs, and conducting a detailed inventory of their existing processes and systems. To avoid the prospect of undertaking

significant rework, organizations should wait to implement other FATCA-related changes, such as drafting new client on-boarding procedures and revising systems, until there is greater clarity on the final requirements.



Introduction

Contrary to popular perception, FATCA is not merely a tax issue. While the Act, which will be phased in from January 2014, is designed to prevent offshore tax abuses by US citizens and residents, the withholding tax and reporting obligations have implications for affected institutions' business models and product, market and distribution strategies.

To comply, FFIs will have to review and leverage Know Your Customer (KYC) and Anti-Money Laundering (AML) procedures, and may have to change the way new customers are approved and documented. In some cases, institutions are faced with updating their IT infrastructures to ensure they have the tools to withhold tax on applicable payments and report the requisite information to the IRS.

The planning and implementation programs needed to achieve compliance will be complex and far-reaching. Yet considerable confusion over what will be required remains. The final regulations – which are expected to differ markedly from the draft proposals – are not due out until the end of 2012 and possibly the beginning of 2013. Furthermore, ongoing IGA negotiations are set to affect how the rules are applied in different jurisdictions.

FATCA at a glance

- Provisions apply to a wide range of institutions, including banks, insurance companies that issue cash value products, and an array of collective investment vehicles.
- FFIs are subject to FATCA if the company either has US clients or holds US assets in any form.
- Imposition of 30 percent withholding tax on all “withholdable payments” from US sources unless the FFI enters into a disclosure agreement with the US Treasury.
- To comply with the regime, FFIs must:
 - Identify direct and indirect owners of their accounts to determine if they are US investors.
 - Disclose their US accounts to the IRS annually, or to appropriate domestic tax authorities where an IGA is in place.
 - Where appropriate, deduct and withhold 30 percent from any payment made to inadequately documented investors.
- US Withholding Agents – i.e. entities that have “control, receipt, custody, disposal, or payment of any item of income of a foreign person that is subject to withholding” – have also been drawn into the FATCA regime. To meet their requirements, affected US institutions will have to identify non-US account holders and investors, and report relevant account details to the IRS.



Intergovernmental Agreements

Two IGA approaches have emerged to date.

The “Model 1” IGA – pioneered by France, Germany, Italy, Spain, and the United Kingdom – transforms the responsibilities and risks FFIs face. Under the agreement, FFIs in IGA jurisdictions will report to their local tax authorities, rather than the IRS, with the local authority (e.g. HM Revenue & Customs in the United Kingdom) relaying the requisite information to the IRS. Some IGAs also bring reciprocity into play, with USWAs now having to report details of non-US account holders and investors to the IRS, which in turn will pass the information to the relevant jurisdiction’s tax authority. The US Treasury Department released the Model 1 reciprocal agreement on 25 July 2012.

On 14 November 2012, the US Treasury Department published its “Model 2” IGA template, which Switzerland, Japan and various other countries that are constrained by local laws from implementing a Model 1 IGA are expected to adopt.

Under Model 2, FFIs in that jurisdiction will have to register with the IRS by 1 January 2014 and comply with the terms of an FFI Agreement (i.e. meet the client identification, disclosure and withholding responsibilities set out by FATCA). Where local laws require, FFIs must request consent from account holders for the institution to report information on their US accounts. Where consent is granted, FFIs will report the relevant customer information directly to the IRS. Where consent is not given, FFIs will have to provide the IRS with aggregate information on their non-consenting account holders. The IRS may subsequently request further detailed information on these accounts and obligations from the jurisdiction’s government, which will have six months to provide it.

The United Kingdom’s Model 1 IGA was signed in mid-September. Royal Assent to the Finance Bill, which will contain the IGA implementing provisions legislation, is expected by summer 2013.

The United States and Denmark followed suit on 15 November 2012, with the signing of a bilateral agreement based on the US Treasury Department’s Model 1 reciprocal agreement. The agreement, which will “enter into force on the later of 1 January 2013, or the date of the later of such notifications,” requires both nations to collect relevant information on reportable accounts from their respective financial institutions.

Other countries’ IGA negotiations are further behind, and it could take years to finalize all the agreements.

Market survey results

Despite FATCA's impending roll-out, uncertainty resulting from the lack of firm rules is complicating organizations' understanding of their roles under the new regime, and thus their planning and implementation efforts.

Against this backdrop, KPMG conducted a survey between May and August 2012 of 129 executives at financial institutions that will be caught in the FATCA net, of which 57 percent are headquartered in the United States and 43 percent are headquartered in other jurisdictions. The respondents comprised of global banks (32 percent), insurance companies (22 percent), regional banks (19 percent), asset management companies (9 percent) and other organizations (18 percent) such as global investment banks and broker/dealers, securities companies and transfer agents. The survey participants answered a number of questions, focused mainly on non tax technical issues, to ascertain what planning and implementation actions they are taking in readiness for FATCA, the resources they are committing, and the challenges they face.

Survey Respondents



Source: KPMG International

Preparedness

The FATCA provisions will affect a broad swathe of the financial sector. Almost all the organizations surveyed (93 percent) believe the Act will apply to their company. Most of these (89 percent) have started taking some sort of steps towards achieving compliance.

However, the level of preparedness varies. To date, action has centered primarily on undertaking an impact assessment. Some organizations have gone further, with 11 percent in the process of revising policies, procedures and systems, and 10 percent building an operating model. By contrast, 12 percent are waiting for release of the final regulations before committing to further action.

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Time frame pressures

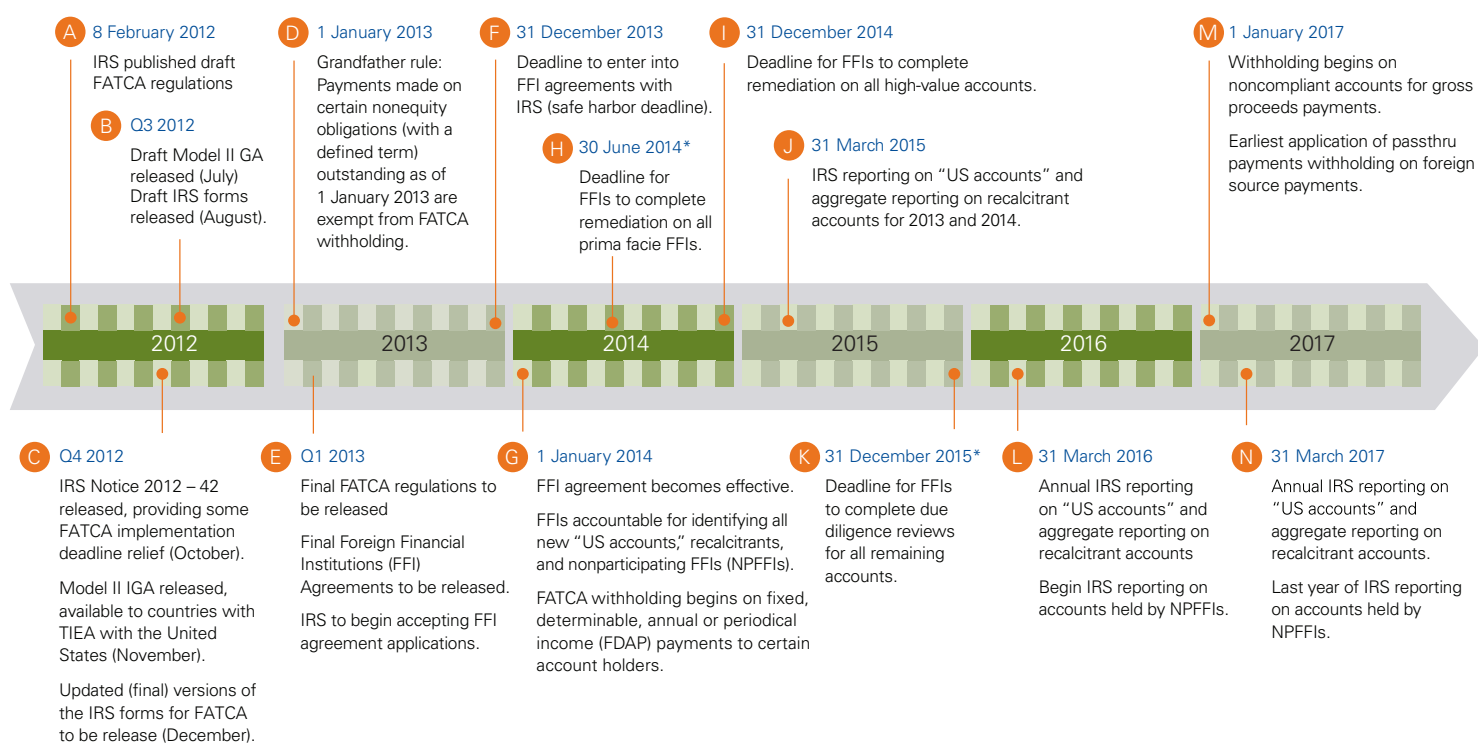
With the final regulations not expected until the end of 2012 and possibly the beginning of 2013, the lack of concrete rules has prevented organizations from fully defining their FATCA compliance projects. Nevertheless, the roll-out deadlines are looming.

The time pressures become even more apparent in light of the survey respondents' predicted implementation schedules:

- **Two-thirds** anticipate FATCA implementation projects will take somewhere between six and 18 months.
- Almost a **quarter** (23 percent) expect implementation to take 18 months or more.
- Only 9 percent think implementation will require less than six months.

The complexity of responsibilities and time required to achieve compliance meant less than half of respondents (45 percent) were confident of meeting the FATCA requirements by the original 1 January 2013 deadline for USWAs and for FFIs. Since the survey was conducted, the US Treasury Department and IRS have issued Announcement 2012-42, extending the deadline for withholding agents to implement new account opening procedures until 1 January 2014. While the extension changes what was an impossible implementation schedule into something more feasible, the time frames remain challenging.

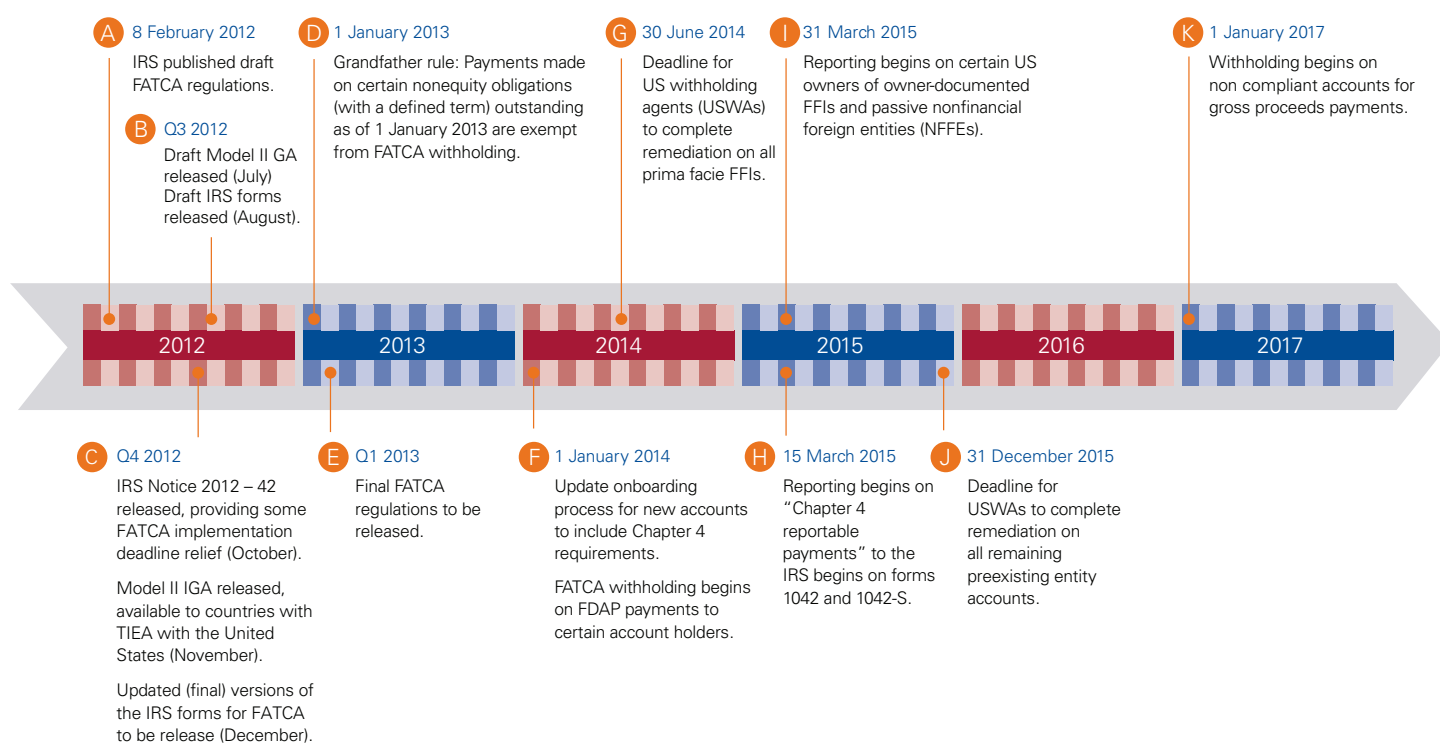
FATCA Timeline for Foreign Financial Institutions



* These dates assume that the FFI's PFFI agreement is approved by the IRS and is effective on 1 January 2014.



FATCA Timeline for US Withholding Agents



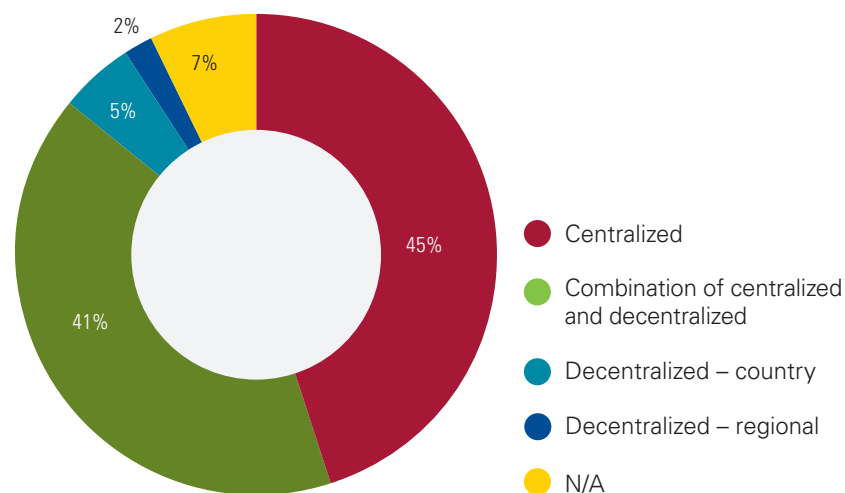
Sponsorship roles and responsibilities

With the clock ticking, ensuring your organization drives forward with its project planning and implementation program is crucial. But where should responsibility lie for leading the effort?

Considering the global impact of FATCA and the many business and functional areas it affects, most organizations (86 percent) are pursuing a centralized implementation plan in some form, be it driven purely from the center or with a combination of centralized and decentralized management. Only 7 percent are taking a decentralized approach.

As for which group within the institution is taking responsibility as project sponsor for their FATCA compliance program, the survey results proved more mixed.

Centralized implementation



Source: KPMG International



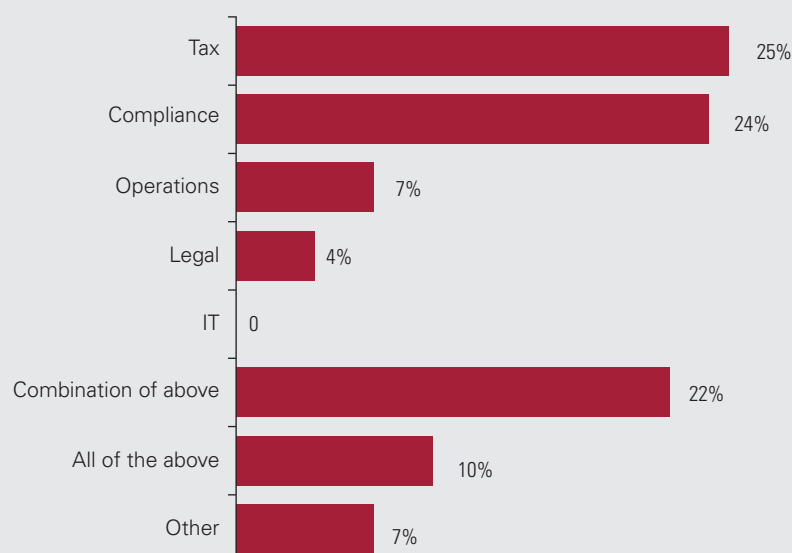
The picture that emerges is that there is no one right way for institutions to tackle their FATCA preparations. For some institutions, it makes sense for Compliance to assume the sponsorship mantle, since they may have already led a lot of their organization's work on AML – an area of significant overlap with FATCA compliance.

Others may prefer their planning and implementation project to sit in operations, as this is the area organizations cite as being most impacted by FATCA.

Crucially, FATCA compliance is an interdepartmental issue – one that almost 80 percent of the organizations surveyed think will require participation by all or a combination of their compliance, operations, tax, legal and IT departments. What is important, therefore, is to determine the most appropriate approach for your particular institution based on consultation with the relevant departments, and to ensure those groups continue to talk to each other throughout the project planning and implementation phases, and beyond.

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Project sponsor



Other responses include:

- Account Management
- Business risk
- CFO
- Corporate Planning
- Group Corporate Centre (Group Finance)
- Head office driven except US branches
- Risk
- Special project team

Source: KPMG International

Resource allocations

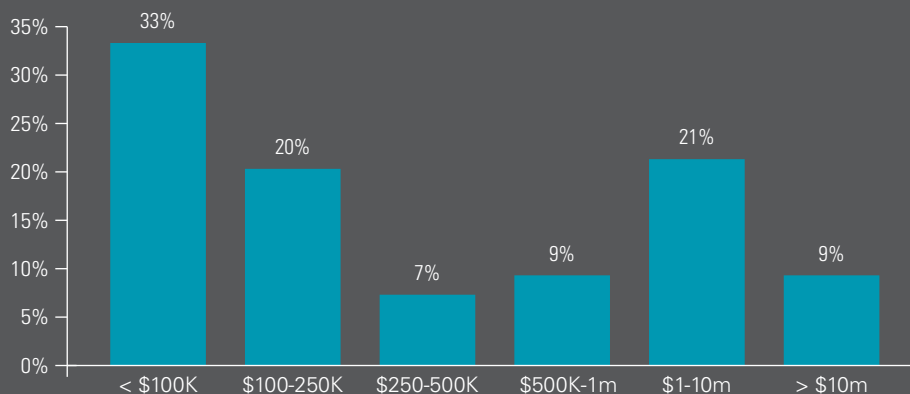
The scale of the challenge organizations face in achieving FATCA compliance should not be underestimated. However, the amount of resources our survey respondents are dedicating to the task varies enormously, which is likely a reflection of the location, size and scope of the institutions' businesses.

- 63 percent estimate that 10 or more people will be involved with their FATCA implementation project, with 18 percent signaling more than 100 people will take part.
- 36 percent expect to use less than 10 people.

Similarly, while the median budget among the survey respondents was approximately US\$250,000, the figure hides a wide disparity in companies' actual or planned allocations. For example, USWAs with no or limited exposure to the IGA requirements will have a relatively light FATCA compliance burden, and thus need to make only limited investments. By contrast, a global bank operating in multiple regions and subject to a web of IGAs will have to undertake a significant retooling of processes and systems.

So while more than half (53 percent) of the survey participants have allocated or will allocate less than US\$250,000 to FATCA, 21 percent (the second largest single group) have budgeted for between US\$1 million and US\$10 million. At the top end of the scale, a small number of institutions (4 percent) are devoting US\$100 million or more to their compliance efforts.

Budget allocations



Source: KPMG International

By contrast, a global bank operating in multiple regions and subject to a web of IGAs will have to undertake a significant retooling of processes and systems.

IGA implications

The amount and complexity of work involved in FATCA compliance will depend to a large extent on the number and types of jurisdictions in which an organization operates. In particular, the emergence of the IGAs means different countries are formulating alternative FATCA compliance arrangements, which will have an enormous bearing on institutions' obligations and workloads.

For instance, the IGAs contain several important simplifications compared to the proposed FATCA regulations, such as eliminating withholding on recalcitrants. However, the agreements introduce logistical complexities for companies as well, as with the new definition of an investment entity, country-to-country differences in Annex 2, which lists the entities, plans, and products that are to be excluded from FATCA reporting, and that partner countries will be left to determine much of the detail on specific obligations (e.g. on the issue of self-certification). Organizations with cross-border operations falling under different regimes (i.e. partially IGA Model 1, IGA Model 2, FFI and USWA) face particularly complex implementation and ongoing compliance requirements.

US Withholding Agents

Under the reciprocity obligations introduced by the Model 1 IGA, US withholding agents will have to report details of their foreign account holders and investors to the IRS. This reporting burden did not exist in the initial FATCA proposals and will add substantial work and operational complexity to the lives of USWAs.

Model 1 IGA

By contrast, the Model 1 IGA – the first of which was signed with the United Kingdom in mid-September – is a welcome simplification for those FFIs captured by the agreements.

Firstly, it eliminates the requirement for FFIs to withhold tax on gross proceeds, and potentially on "passthru" payments as well. In addition, a responsible officer will no longer be held accountable for certifying their institution is meeting its compliance obligations (although as-yet undefined local country certification requirements may be introduced).

As a result, the commercial, legal, and reputational risks previously associated with FATCA have been reduced significantly. Furthermore, by making the client on-boarding process less onerous and removing the need for institutions to build a withholding engine, the IGAs effectively drive down the cost of compliance.

Model 2 IGA

The Model 2 template, published by the US Treasury Department on 14 November stipulates that FFIs in the applicable jurisdictions will have to register with the IRS by 1 January 2014 and comply with the terms of an FFI Agreement (i.e. meet the client identification, disclosure and withholding responsibilities set out by FATCA). Where appropriate consent from account holders is granted, FFIs will report the necessary



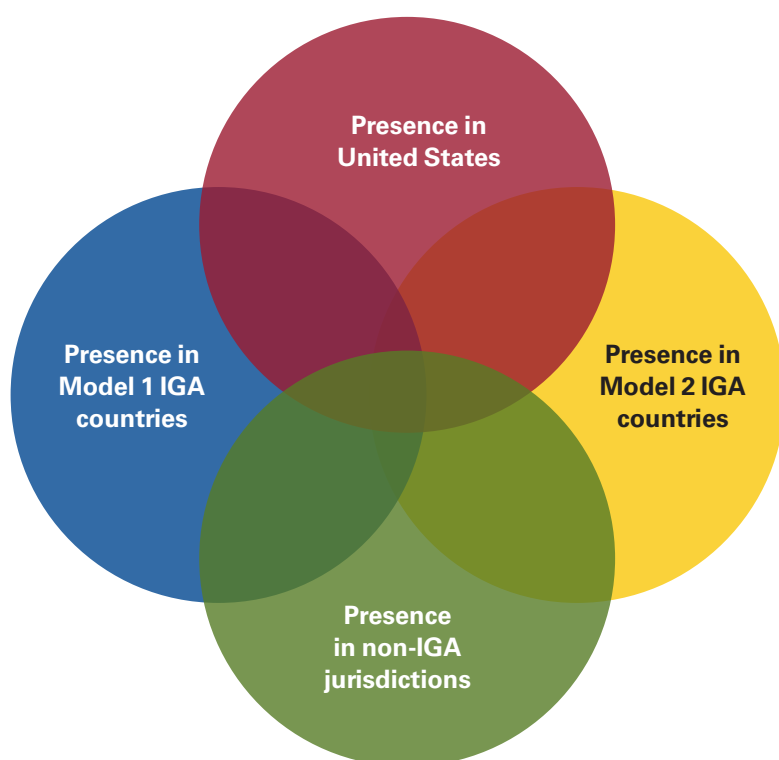
information on their customers directly to the IRS. Where consent is not given, FFIs will have to provide the IRS with aggregate information on their non-consenting account holders. The IRS may subsequently request further detailed information on these accounts and obligations from the jurisdiction's government, which will have six months to provide it. Having to report directly to the IRS in this way will likely make the process more complex for FFIs, with potentially greater commercial, legal and reputational risks than under the Model 1 framework.

Non-IGA jurisdictions

The current model IGAs are premised upon a requirement that the country entering into the IGA have either a tax treaty or tax information exchange agreement (TIEA) with the

United States. Some notable jurisdictions, for example Hong Kong and Singapore, do not have these agreements with the US, and would have been presumed ineligible to enter into an IGA. However, on 8 November 2012, the US Treasury Department released a notice stating they are discussing the development of IGAs with more than 50 countries, including Singapore, which indicates that not having a tax treaty or a TIEA will not hinder jurisdictions from entering into an IGA. Yet despite their potentially game-changing impacts, our survey revealed the majority of respondents (56 percent) either did not know or were unsure whether any governments in the countries in which they operate intend to enter into an intergovernmental agreement with the United States. Treasury's November announcement should raise companies' awareness with this issue.

Complexity of a multi country presence



Trouble spots

So where do the greatest compliance challenges lie?

According to the survey respondents, meeting FATCA's account identification requirements poses the biggest problem. Other notable areas with which financial institutions are wrestling include achieving compliance with the documentation requirements, having the right systems in place and having the ability to generate and send the requisite reports.

Considering the onus FATCA puts on pinpointing financial institutions' US clients and asset holdings, almost all companies (92 percent) feel their client on-boarding, customer identification and/or documentation processes will need to be revised. But despite the operational burden compliance

brings, 81 percent of respondents have no intention of terminating customer relationships to sidestep the requirements.

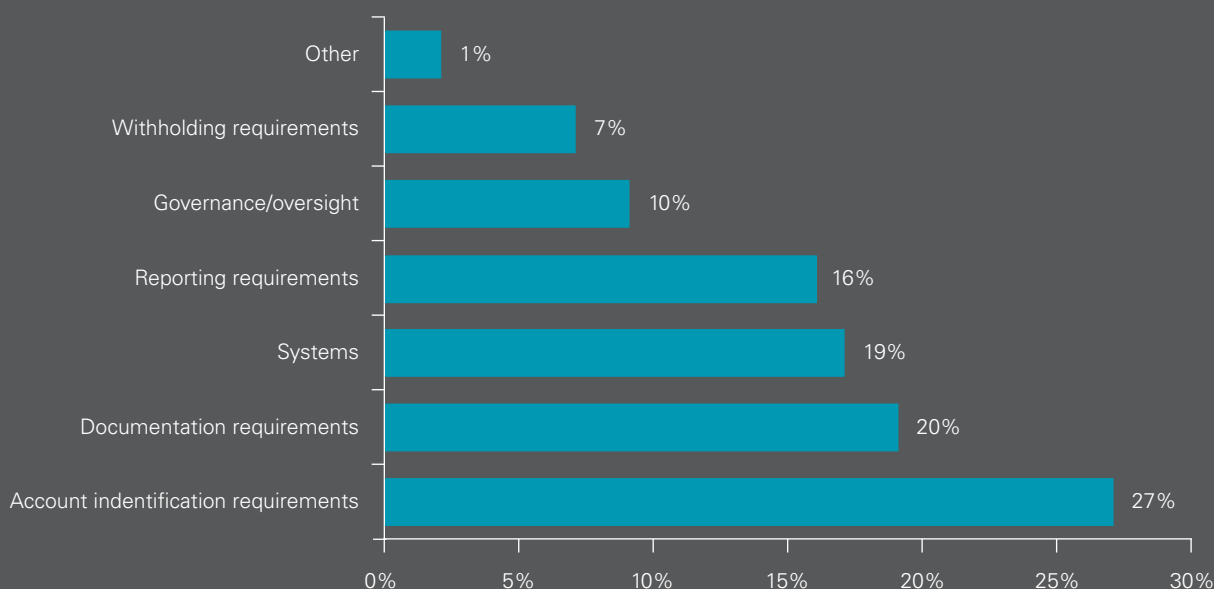
The good news is organizations do not necessarily need to start from scratch. Rather, four-fifths of the institutions surveyed plan to leverage their existing AML/KYC compliance programs to help satisfy the FATCA requirements.

Nevertheless, it is important to bear in mind that, despite the fact AML/KYC can be leveraged to help satisfy FATCA customer identification and documentation requirements and possibly assist with the entity classification process, there may be gaps in existing AML/KYC programs that need to be addressed, including systems enhancements. For instance,

most existing KYC programs are based on money laundering risk. Hence, more due diligence information is available on a customer considered high risk than on one who is low risk. In sum, there should not be an expectation on the FATCA front that customer KYC information will be equally available for all customers.

Perhaps not surprisingly, given the compliance workload involved and how much is at stake, the majority of organizations (57 percent) are using or planning to use a professional services firm(s) to assist with their FATCA implementation program, with another 29 percent considering doing so.

Biggest challenges



Source: KPMG International

Client on-boarding, customer identification and/or documentation processes may need to be revised.

Action steps

As noted, lack of clarity surrounding the final rules and how various countries' IGA negotiations will alter the landscape make it difficult for institutions to properly plan and implement fully fledged FATCA programs. In this environment, therefore, organizations should seek to extract maximum value from the FATCA work done to date, and minimize the need to undertake significant rework by not implementing changes that try to second guess the eventual framework outcome.

To this end, the first step should be to conduct a detailed inventory of existing processes and systems. Organizations will then be better placed to reformulate new client on-boarding procedures and revise applicable systems once the final requirements become clear.

Ensuring your preparedness for the most immediate effective deadline is another priority. This requires organizations to identify their FFIs and either sign up with the IRS or register them under an IGA scheme as appropriate.

Where possible, leveraging existing projects and processes that contain elements of FATCA, such as current AML and KYC programs, is likely to be the most effective way to jumpstart your program. By contrast, there is no point focusing on remediation, withholding, reporting, etc. when the final rules – which will presumably deviate substantially from the initial proposals – are yet to be announced.

At an organizational level, good communication is crucial. By enrolling all relevant parties into the FATCA program to see and understand their specific requirements, the complexity of compliance can be reduced dramatically. Similarly, it is important to identify key external stakeholders impacted by the potential changes and develop an effective communication plan with them.

Ultimately, because FATCA touches an entire organization, achieving compliance requires the review and assessment of every legal entity and business unit within the institution. While this forensic scrutiny brings significant challenges, approached the right way the work involved can also uncover various opportunities, such as ways to streamline your organizational structure, enhance processing efficiencies or realign your business model.



Ensuring your preparedness for the most immediate effective deadline is another priority. This requires organizations to identify their FFIs and either sign up with the IRS or register them under an IGA as appropriate.

Action required

Despite the lack of clarity surrounding the final FATCA framework, USWAs and FFIs caught within the regime need to take action now to prepare for compliance:

1. Identify your expanded affiliate group (e.g. USWAs, FFIs and Non-Financial Foreign Entities (NFFE)).
2. Review client on-boarding processes and procedures.
3. Collaborate with Compliance, Operations, Tax, Legal and IT stakeholders internally to understand their specific requirements.
4. Communicate with external stakeholders to cooperate on prospective areas of change.



The survey results also demonstrate a widespread consensus about where the focus of work will lay, with almost all respondents stating client on-boarding, customer identification and/or documentation processes will need revising, and with most planning to leverage existing AML/KYC compliance programs to help satisfy their FATCA requirements. Meanwhile, the majority of organizations are adopting some form of centralized plan to drive their implementation projects, rather than delegating responsibility to their regional or country businesses.

Conclusion

Uncertainty surrounding exactly what will be required of institutions in the post-FATCA world is complicating the industry's compliance readiness efforts. This is especially true for institutions with a broad global footprint, which may become subject to an array of reporting and withholding tax arrangements.

Nevertheless, it is clear from our survey that a high level of awareness about FATCA exists among industry participants and that the vast majority of organizations have kick started their compliance projects in some form.

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Yet wide divergences in approaches and opinions are evident too. The survey reveals a broad spectrum of responses in terms of the number of people and size of budget organizations are dedicating to FATCA compliance, the time they expect project implementation to take, and whether they will be ready for the upcoming deadlines.

At this stage, with the final rules and international agreements still in flux, focusing your efforts on well-defined areas that enable your organization to meet the most immediate deadlines, while minimizing the risk of undertaking work that subsequently proves redundant, should be the priority.



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