Identifying the Path Forward with Foreign Taxpayer Identification Number Requirements

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In this article, the authors discuss foreign taxpayer identification number requirements.

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Navigating foreign taxpayer identification number (FTIN) requirements has made 2017 a roller coaster ride for the information reporting and withholding community. The ride took off abruptly with a simple sentence included in the IRS's December 30, 2016, publication of final and temporary regulations under Chapter 3:

> For withholding certificates associated with payments made on or after January 1, 2018, if an account holder does not have a foreign TIN, the account holder is required to provide a reasonable explanation for its absence (e.g., the country of residence does not provide TINs) in order for the withholding certificate not to be considered invalid.

With the publication of that new requirement, the U.S. Department of Treasury finally made good on commitments undertaken in the 100-plus intergovernmental agreements negotiated to facilitate the implementation of the Foreign Account Tax Compliance Act. As part of the IGAs, Treasury committed to establishing rules by January 1, 2017, requiring U.S. financial institutions to collect and report FTINs for holders of reportable accounts. This supports the idea that FATCA is delivering reciprocal information to foreign governments on their own residents because a name without a TIN is a difficult prospect for a government to tax.

While the FTIN requirement has existed in concept since the 2014 launch of FATCA-compliant Forms W-8, the requirement to collect an explanation for the lack of the FTIN and, more importantly, the lack of a phased approach to gather this information, had taken many U.S. financial institutions by surprise. Before this new requirement, an account holder completing a Form W-8 was required to provide an FTIN unless the account holder's country of tax residence did not issue TINs or account holders were not required to obtain a TIN locally. In practice, withholding agents were stuck with no way to know if the beneficial owner completing the form met one of these two criteria or just decided not to provide the FTIN. The OECD learned from this gap, requiring an explanation for the lack of an FTIN as part of the common reporting standard (CRS).

This rocky beginning began to smooth out over the summer as it became increasingly apparent that the IRS was planning to issue some level of transitional relief. Guidance was finally published on September 25 as part of Notice 2017-46, 2017-41 IRB 1. The notice includes plenty of good news for withholding agents such as a phased approach to manage FTIN solicitation for Forms W-8 signed before January 1, 2018; a whitelisting of countries not issuing FTINs; the ability for withholding agents to associate the FTIN or explanation with the account holder's withholding certificate; and the elimination of domestic backup withholding on gross proceeds for failure to provide an FTIN.

Specifically, Forms W-8 signed in 2015 and 2016 will expire on the earlier of their natural expiration date or when a change in circumstance invalidates the form. Forms W-8 signed in 2017 are potentially going to require remediation, as absent

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an FTIN, these will expire on the earlier of December 31, 2019, or when a change in circumstance invalidates the form. Importantly, the collection of the FTIN outside of a Form W-8 works only for tax forms signed before January 1, 2018; after that, the FTIN must be provided on the Form W-8 itself, presumably to manage previous IRS concerns that the FTIN would be provided under penalties of perjury.

In response to concerns raised by retail banking intuitions, the IRS also confined the FTIN requirement to account holders in jurisdictions with which the U.S. has an information exchange agreement in effect. That said, time will tell if this is a true victory. Making sure FTINs are captured for additional accounts as new countries are added to this list could prove more challenging for institutions managing annual reviews. This and several other operational complexities mean withholding agents are not going to be able to coast smoothly into 2018.

Reviewing Annual Re-Solicitation Processes

U.S. financial institutions either have started or will soon commence their annual fall re-solicitation processes for expiring Forms W-8. In the wake of Notice 2017-46, withholding agents need to decide how to manage Forms W-8 signed in 2017, as these will not naturally expire before the December 31, 2019, cutoff date. Should these be re-solicited now, or is it worth waiting in the hope that these customers will be conditioned to provide this information a year or two down the road? There is also going to be pressure for withholding agents to repaper expiring Forms W-8 before December 31. This is the cutoff for withholding agents being able to solicit a separate statement to collect the FTIN versus requiring the FTIN to be included on the Form W-8. Chasing an account holder for an updated form, especially when a client has just provided one, is expensive and time-consuming and potentially introduces new validation errors into the process.

Mapping to Existing Reporting Processes

Withholding agents need to spend time now deciding how to operationalize FTIN requirements. Generally speaking, account masters were built pre-FATCA and possibly even before the Chapter 3 regulations. While there may have been an upgrade or two to add FATCA or CRS-relevant fields, most account masters lack multiple TIN fields. If an account holder has provided a U.S. TIN to support a treaty claim or refund request, the single TIN field may already be in use. There are also some systems that maintain the FTIN in a free text field that may not easily map into existing reporting processes. It is also worth reviewing the parameters for the fields selected to maintain FTINs. At a minimum these should be alphanumeric, be capable of holding special characters, and allow for at least 30 characters. Effectively managing this information as it is collected and, even more importantly, determining how it will be exported for reporting purposes, will be key to avoiding issues later.

In developing a written explanation template, financial institutions should work with the end goal in mind — obtaining a valid Form W-8. The IRS instructs that a valid explanation is a statement that the beneficial owner is not legally required to obtain a TIN in its country of tax residence. This is not the time to get creative! Financial institutions should stick very close to this preapproved language in developing their templates. Absent actual knowledge that a beneficial owner has an FTIN that it has not provided, an explanation that an account holder is not legally required to obtain a TIN is sufficient and does not create validation concerns.

What if There Is No FTIN to Report?

However, what happens if an institution publishes a template including an option for the country of tax residence that does not issue TINs? Arguably, most people had picked up on the fact that the Cayman Islands does not issue TINs, and the white list announced in Notice 2017-46 confirms this, but what if that explanation is provided for Germany or the United Kingdom? The IRS has been clear that U.S. institutions are not required to validate this information against the TIN data that the OECD has been assembling, but what if another account holder from that jurisdiction provides a TIN? This raises several interesting questions that can be avoided by keeping the written explanation template as simple as possible.

Many intriguing questions will arise with respect to validation requirements. For example,

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under Australian law, providing a TIN is not required. Reciprocal data provided by Treasury would therefore not require an Australian TIN. Rather, U.S. institutions would report the taxpayer's date of birth. Would this explanation suffice if an Australian taxpayer refused to provide a TIN? Notice 2017-46 clearly requires withholding agents to determine whether an explanation is reasonable when it veers from the safe harbor language that the account holder is not legally required to obtain a TIN in its country of tax residence.

It's also important to keep in mind that there are withholding requirements for new accounts without a valid FTIN or explanation beginning January 1, 2018. Following the publication of Notice 2017-46, gross proceeds withholding is off the table. However, withholding agents will still be required to update withholding processes and grapple with the scenario of an otherwise valid Form W-8 meeting the requirements to avoid withholding on bank deposit interest yet not meeting requirements to avoid backup withholding on dividend income given the lack of an FTIN or reasonable explanation. It remains to be seen whether withholding agents will be able to manage multiple statuses for account holders depending on type of income or will be forced to default the account status in accordance with the presumption rules.

Finally, withholding agents already struggling to monitor for changes in circumstance should note the new requirements. A change in permanent residence country is also a trigger for knowing that the FTIN or reasonable explanation is now incorrect. Automated processes for monitoring changes will be critical to timely capturing these changes and updating documentation.

Back to Basics in Building Compliance

Finally, this is a good opportunity to remember the fundamentals: written policies, procedures, and training. When carrying out the same processes every day, it is easy to defer updating policies and procedures to focus on more urgent responsibilities. However, updated policies and procedures are a cornerstone of compliance, not to mention one of the first requests the IRS will make on audit. Furthermore, it does no good to spend time developing policies and procedures if those responsible for execution are not trained. With the advent of these changes around the FTIN and myriad other tax requirements, it is crucial that new procedures be documented and communicated.

There is no doubt Treasury is trying hard to meet its commitments under the IGAs. However, it should not be forgotten that no matter how broadly an IGA is drafted, it still does not require the same level of information exchange as is required by the CRS. U.S. institutions should begin to wonder if this is the first step in moving toward a combined CRS-FATCA regime. Nevertheless, for now the focus should remain on operationalizing requirements and soliciting FTIN statements for forms dated in 2017 to take advantage of the supplemental statement provisions. While the roller coaster does not have a tranquil path to the new year, Notice 2017-46 has smoothed some of the previous twists and turns. ■

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