

April 20, 2012

Information Reporting – Interest Paid to Non-U.S. Individuals on U.S. Bank Deposits

IRS and the Treasury Department Issue Final Regulations Requiring the Reporting of Interest or Original Issue Discount (“OID”) Paid to Nonresident Alien Individuals on Bank Deposits

SUMMARY

On April 17, the IRS and Treasury Department released final regulations (the “Final Regulations”) that require banks to annually report to the IRS the amount of interest earned on U.S. bank deposits held by nonresident alien individuals residing in countries with which the U.S. has in effect an income tax treaty or other convention or bilateral agreement providing for the exchange of information. Such reporting is currently only required for interest earned on the bank deposits held by U.S. citizens or residents, and nonresident alien individuals who reside in Canada. The Final Regulations are more limited than the regulations proposed in January, 2011 (the “Proposed Regulations”), which would have extended such reporting to all nonresident alien individuals regardless of their country of residence.¹

The IRS also released Revenue Procedure 2012-24, which lists the countries with which the United States is treated for this purpose as having in effect an income tax treaty or other convention or bilateral agreement providing for the exchange of information.

This new reporting requirement is aimed at combating tax evasion, in part by bolstering the IRS’s efforts to increase the mutual exchange of tax information with other jurisdictions. In particular, the implementation of FATCA will rely in part on information exchange agreements entered into with other jurisdictions and information provided to the IRS pursuant to such agreements.

On the same day that the Final Regulations were released, bills were introduced in the Senate and the House of Representatives that would block the implementation of the Final Regulations.

The Final Regulations are effective for payments made on or after January 1, 2013.

DISCUSSION

Under current law, U.S. banks are not required to withhold on payments of bank deposit interest² paid to a nonresident alien individual³ on an account maintained in the United States if the account is not effectively connected with a U.S. trade or business. In addition, under current law, while bank deposit interest on deposit accounts is excluded from the information reporting requirements otherwise generally applicable to interest payments made to nonresident aliens, interest payments on such accounts held by Canadian residents are subject to information reporting.⁴

The Final Regulations extend this reporting requirement applicable to Canadian residents to all U.S. bank deposit accounts held by residents of countries with which the U.S. has in effect an income tax treaty or other convention or bilateral agreement pursuant to which the United States agrees to provide, as well as receive, information. The specific list of such countries was published on April 17 as Revenue Procedure 2012-24 (the "Revenue Procedure").⁵ The IRS has stated that it will update this list periodically. The limitation of reporting to the listed countries narrows the scope of reporting somewhat from the Proposed Regulations, which required reporting for bank deposit interest paid to all nonresident alien individuals.⁶ The Final Regulations provide that bank payors may nevertheless elect to report all interest paid to all nonresident alien individuals irrespective of whether they are residents of a country listed in the Revenue Procedure. This election is made by reporting all such interest.

For purposes of determining the identity and residence of a nonresident alien individual, the bank payor is permitted to rely on the individual's valid Form W-8BEN and the permanent residence address provided on that form, unless the payor knows or has reason to know that this documentation is not correct or is unreliable.

Under the Final Regulations, the bank deposit interest paid to a nonresident alien individual is reportable on Forms 1042 and 1042-S, which are the forms used generally to report payments of U.S. source interest income to nonresident aliens. Reporting under the Final Regulations is required for all payments made on or after January 1, 2013.

The purpose of extending the reporting requirement beyond Canadian residents, according to the preamble to the Final Regulations (the "Preamble") is to assist in combatting tax evasion, primarily by ensuring that the IRS can exchange information relating to tax enforcement with other jurisdictions when necessary and can participate in international agreements relating to the exchange of tax information. In particular, the Preamble notes that providing such information to other jurisdictions is key to ensuring reciprocity of information sharing: "A jurisdiction's willingness to share information with the IRS to combat offshore tax evasion by U.S. taxpayers depends, in large part, on the ability of the IRS to exchange information that will assist that jurisdiction in combating offshore tax evasion by its own residents." Such

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agreements include information exchange agreements that are entered into as part of implementing FATCA,⁷ including the FATCA partnership agreements that the IRS has indicated will allow financial institutions in FATCA partner countries to report information to their own governments rather than the IRS.⁸ The Preamble also notes that under the international standard for transparency and exchange of information, the exchange of tax information between countries cannot be limited simply because a country's domestic laws do not require banks to report the required information. Finally, the Preamble states that the regulations will directly enhance U.S. tax compliance by making it more difficult for U.S. taxpayers to fraudulently claim to be nonresident alien individuals in order to avoid reporting on bank deposit interest paid to them.

One of the major concerns raised in response to the Proposed Regulations, according to the Preamble, was that the information collected might be misused by the foreign countries with which the IRS shares the information collected. The Preamble discusses these concerns, and states that the Treasury Department and the IRS believe sufficient safeguards are in place to address these issues, including the following:

- Section 6103 of the Internal Revenue Code, which imposes confidentiality rules for return information, and allows the IRS to share return information with a foreign government only under an information exchange agreement;
- Established international standards which provide that parties to information exchange agreements must agree to treat and protect information received as secret and not to use it for law enforcement purposes other than the administration, collection and enforcement of taxes covered by the agreement;
- Treasury Department and IRS policies with respect to the standards applied to review a foreign jurisdiction's legal framework for maintaining confidentiality of taxpayer information before entering into an information exchange agreement; and
- IRS policies
 - to not exchange information on deposit interest specifically with any country if the IRS determines the country is not complying with obligations to protect confidentiality of information, and
 - to not exchange this information with any country that does not tax such deposit interest income, because such information could not be used for the enforcement of tax laws in that country.⁹

The Preamble discusses the distinction between IRS agreements with foreign countries to exchange information on an automatic basis and the exchange of information upon request. Currently, Canada is the only country with which the U.S. has an automatic exchange of deposit interest income information. The Preamble states that for all countries with which the IRS may exchange information upon specific request, the IRS evaluates the requesting country's current practices with respect to confidentiality and requires the requesting country to "explain the intended permitted use of the information and justify the relevance of that information to the permitted use." The Preamble also states that the IRS would evaluate the practices and policies of any country before entering into an automatic exchange agreement.

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On the same day that the Final Regulations were released, Representative Bill Posey (R-FL) and Senator Marco Rubio (R-FL) introduced bills that would block the implementation of the Final Regulations.¹⁰

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ENDNOTES

- ¹ A discussion of the Proposed Regulations can be found in the S&C Publication "[Information Reporting – Interest Paid to Nonresident Alien Individuals on Bank Deposits](#)" (January 7, 2011) which may be obtained by following the instructions at the end of this publication.
- ² Bank Deposits include amounts held with persons carrying on the banking business and savings institutions, as well as amounts held by insurance companies under an agreement to pay interest thereon. IRC Sections 6049(b)(5) and 871(i)(2).
- ³ A nonresident alien individual is defined in IRC Section 7701(b)(1)(B), that is, an individual that is neither a citizen of the United States nor a resident of the United States. Under Treas. Reg. § 1.6049-4(d)(4) and Treas. Reg. § 1.6049-1(a)(3), the person to whom interest is paid is the person whose identifying number is required to be included on an information return with respect to the interest. Under Treas. Reg. § 1.6049-4(b)(5) and Treas. Reg. § 1.6049-8, interest and OID on deposits paid to residents of Canada is subject to reporting. The Final Regulations extend these provisions to any nonresident alien individuals who are resident in the listed countries.
- ⁴ Generally, payments to non-U.S. individuals are subject to reporting on Forms 1042 and 1042-S; prior to the Final Regulations, interest on deposit accounts (other than interest paid to Canadian residents) was excluded from this reporting. IRC Sections 6049(b)(2) and (b)(5). With respect to payments to recipients that are not individuals, under Treas. Reg. § 1.6049-4(c) no information return is required with respect to any payment to (i) a corporation, (ii) a tax exempt organization, (iii) an individual retirement plan, (iv) the United States government and any wholly-owned agency or instrumentality, or any state, the District of Columbia, or possession of the U.S., (v) a foreign government, (vi) an international organization, (vii) a foreign central bank of issue, (viii) a securities or commodities dealer, (ix) a real estate investment trust, (x) an entity registered under the Investment Company Act of 1940, (xi) a common trust fund, (xii) a financial institution, (xiii) certain charitable trusts, (xiv) a nominee or custodian, (xv) a broker, or (xvi) a dealer in notional principal contracts.
- ⁵ Notable exclusions from the list in the current Revenue Procedure include Argentina, Brazil (with which the United States currently has a tax exchange information agreement pending), Colombia, Hong Kong, Saudi Arabia and the UAE. The Revenue Procedure is attached as an Annex to this publication.
- ⁶ Another difference from the Proposed Regulations is that the Final Regulations do not require banks to provide a statement to nonresident alien individuals that informs them that the information may be furnished to the government of the country where the nonresident alien resides. The Preamble states that this information will be available in the Revenue Procedure, and states that this change is in response to comments received in response to the Proposed Regulations.
- ⁷ The provisions of the Hiring Incentives to Restore Employment Act of 2010 that require foreign financial institutions to identify U.S. accounts and report information to the IRS are commonly referred to as "FATCA".
- ⁸ Such information exchange agreements were discussed in a joint statement issued by the Treasury Department along with the governments of France, Germany, Italy, Spain and the United Kingdom. The joint statement outlined these countries' intention to "intensify their co-operation in combating international tax evasion" and to explore common approaches to implementing FATCA. The joint statement outlined a possible framework for FATCA implementation based on reciprocal reporting between the U.S. and a country with which the U.S. signs an agreement.
- ⁹ The Preamble states that while no information would actually be shared with any country with which the U.S. does not have in effect an information exchange agreement, the Final Regulations further address this concern by also not requiring the provision of information with respect to bank deposit interest paid to residents of those countries.
- ¹⁰ The Posey Bill is H.R. 2568, and the Rubio bill is S. 1506.

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Part III

Administrative, Procedural, and Miscellaneous

26 CFR 1.6049.00-00 Returns Relating to Payments of Interest
(Also: 1.3406.07-00 Exceptions to Backup Withholding)

Implementation of Nonresident Alien Deposit Interest Regulations

Rev. Proc. 2012-24

SECTION 1. PURPOSE

Sections 1.6049-4(b)(5) and 1.6049-8 of the Income Tax Regulations, as revised by TD 9584, require the reporting of certain deposit interest paid to nonresident alien individuals on or after January 1, 2013. The purpose of this revenue procedure is to list, in Section 3, the countries with which the United States has in effect an income tax or other convention or bilateral agreement relating to the exchange of information within the meaning of section 6103(k)(4) pursuant to which the United States agrees to provide, as well as receive, information and under which the competent authority is the Secretary of the Treasury or his delegate, as described in §1.6049-8(a). As discussed in the preamble to the regulations, even when such an agreement exists, the Internal Revenue Service (IRS) is not compelled to exchange information, including information collected pursuant to the regulations, if there is concern regarding the use of the information or other factors exist that would make exchange inappropriate. This revenue procedure also identifies in Section 4 the countries with which the Treasury Department and the IRS have determined that it is appropriate to have an automatic exchange relationship with respect to the information collected under the regulations. This revenue procedure will be updated as appropriate.

SECTION 2. BACKGROUND

The regulations provide that in the case of reportable interest aggregating \$10 or more paid to a nonresident alien individual (as defined in section 7701(b)(1)(B) of the Internal Revenue Code), the payor shall make an information return on Form 1042-S for the calendar year in which the interest is paid. Reportable interest is interest described in section 871(i)(2)(A) that relates to a deposit maintained at an office within the United States, and that is paid to a nonresident alien individual who is a resident of a country identified, in an applicable revenue procedure (see §601.601(d)(2) of this chapter) as of December 31 prior to the calendar year in which the interest is paid, as a country with which the United States has in effect an income tax or other convention or bilateral agreement relating to the exchange of information within the meaning of section

6103(k)(4) pursuant to which United States agrees to provide, as well as receive, information and under which the competent authority is the Secretary of the Treasury or his delegate. This revenue procedure constitutes the revenue procedure referenced in §1.6049-8(a) and will be updated by subsequent revenue procedures as appropriate.

SECTION 3. COUNTRIES OF RESIDENCE WITH RESPECT TO WHICH THE REPORTING REQUIREMENT APPLIES

The following are countries with which the United States has in effect an income tax or other convention or bilateral agreement relating to the exchange of tax information within the meaning of section 6103(k)(4) pursuant to which the United States agrees to provide, as well as receive, information and under which the competent authority is the Secretary of the Treasury or his delegate:

Antigua & Barbuda
Aruba
Australia
Austria
Azerbaijan
Bangladesh
Barbados
Belgium
Bermuda
British Virgin Islands
Bulgaria
Canada
China
Costa Rica
Cyprus
Czech Republic
Denmark
Dominica
Dominican Republic
Egypt
Estonia
Finland
France
Germany
Gibraltar
Greece
Grenada
Guernsey
Guyana
Honduras
Hungary

Iceland
India
Indonesia
Ireland
Isle of Man
Israel
Italy
Jamaica
Japan
Jersey
Kazakhstan
Korea (South)
Latvia
Liechtenstein
Lithuania
Luxembourg
Malta
Marshall Islands
Mexico
Monaco
Morocco
Netherlands
Netherlands island territories: Bonaire, Curacao, Saba, St. Eustatius and
St. Maarten (Dutch part)
New Zealand
Norway
Pakistan
Panama
Peru
Philippines
Poland
Portugal
Romania
Russian Federation
Slovak Rep.
Slovenia
South Africa
Spain
Sri Lanka
Sweden
Switzerland
Thailand
Trinidad and Tobago
Tunisia
Turkey
Ukraine

United Kingdom
Venezuela

SECTION 4. COUNTRIES WITH WHICH TREASURY AND THE IRS HAVE DETERMINED THAT AUTOMATIC EXCHANGE OF DEPOSIT INTEREST INFORMATION IS APPROPRIATE

The following list identifies the countries with which the automatic exchange of the information collected under §§1.6049-4(b)(5) and 1.6049-8 has been determined by the Treasury Department and the IRS to be appropriate:

Canada

SECTION 5. EFFECTIVE DATE

This revenue procedure is effective for interest paid on or after January 1, 2013.

SECTION 6. DRAFTING INFORMATION

The principal author of this revenue procedure is Kathryn T. Holman of the Office of Chief Counsel International (International). For further information regarding this revenue procedure contact Kathryn T. Holman on (202) 622-3840 (not a toll free call).