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Alleviating the Compliance Burden of US FATCA on Nigeria's Financial Services Industry: A Case for Government Intervention

The additional compliance cost imposed on FFIs has the potential of growing to unimaginable proportions should the revenue agencies of other countries with substantial economic clout seek to follow the example of the US IRS

In March 2010, the United States' Government enacted the Foreign Account Tax Compliance Act (FATCA), which is aimed at curbing offshore tax evasion and aggressive tax avoidance by United States (US) nationals and US controlled companies.

The Act which came into full effect on 1 January 2013 mandates foreign financial institutions (FFI) and non-financial foreign entities (NFFEs) to enter into agreements with the US Internal Revenue Service (IRS), which will require them to report certain financial information of US nationals and companies that maintain bank accounts with them to the IRS.

The obligations imposed by FATCA on FFIs and NFFEs include the following, among others:

- identify customer account holders who are US citizens
- comply with verification and due diligence procedures and instructions issued by IRS
- make annual reports to IRS on the identified US accounts
- comply with any other additional IRS reporting requests
- withhold penalty at 30% from payments into the accounts of US nationals or companies who fail to comply with reasonable requests for information under the Act

It is necessary to note that US subjects it nationals and companies to taxes based on their worldwide income. As a result, enactment of FATCA is in a bid by the US Government to mitigate its loss of tax revenue, which the IRS estimated to be about US$304 billion and US$305 billion in 2009 and 2010, respectively.

As noted above, the Act imposes a 30% withholding penalty on any US sourced payments accruing to US account holders, FFIs and NFFEs who fail to comply with the requirements of the Act or directives of IRS. The withholding penalty would apply to any fixed or determinable annual or periodical (FDAP) payment made on or after 1 July 2014, while it would apply to FDAP gross proceeds from 1 January 2015. In addition, pass-thru payments would be subject to withholding effective from 1 January 2015.

Upon registration and acceptance by IRS, FFIs and NFFIs are assigned Global Intermediary Identification Numbers (GIIN). As at 23 December 2014, about 143,110 FFIs from about 226 jurisdictions have registered with IRS and have been assigned GIINs for identification purposes. About 83 Nigerian financial institutions had registered with the IRS in compliance with the FATCA requirements as at 31 October 2014.

The widespread reach of FATCA and the disclosure requirements under the Act raises various thorny issues, which include data privacy and confidentiality matters. While it is acknowledged that data protection laws and regulations are usually overridden by public interest considerations, the extraterritorial imposition of US domestic national laws with the threat of financial sanctions, appears to be overreaching.

In order to address some of these concerns, the US Treasury Department developed two alternative models of intergovernmental agreements (IGAs). The IGA is aimed at facilitating effective and efficient implementation of FATCA information reporting in a manner that removes foreign law impediments, fulfills the information reporting objectives of the Act and reduces compliance burden imposed on FFIs

Some countries have already opted to sign IGAs with the US IRS in order to mitigate some of the concerns associated with FATCA compliance above. There are two categories of IGAs that are currently being implemented, namely:

Model 1 regime: FFIs that sign up to this IGA are required to report details of US account holders to the respective governments of their jurisdictions, which will in turn pass them on to the US IRS. 5 out of the G7 countries (i.e. Canada, France, Germany, Italy and United Kingdom), as well as Australia, China, Brazil, South Africa, Mexico, France and the Netherlands are some of the jurisdictions that have signed up for this class of IGA. About 39 countries have signed up for this category in total.

Model 2 regime: Under this regime, financial institutions report details of US account holders directly to the IRS. Japan is the only G7 country that signed up for this category of IGA. Other jurisdictions that have opted for this category are Chile, Switzerland, Bermuda and Austria.

Another version of Model 1 IGA is Model 1B, which is available to jurisdictions like Nigeria that do not have Tax Information Exchange Agreement or Double Taxation Agreement with the US. It places an obligation on the government of such a country to obtain the information required under FATCA with respect to all US' reportable accounts and to annually exchange this information with the US on an automatic basis. It also accords such a country's government the right to determine the amount and characterization of payments that will be covered by FATCA in that country. This version of Model 1 IGA does not include a reciprocity clause applicable under a Model 1A IGA

Nigeria is currently a net importer of foreign aid. She relies heavily on foreign direct investment (FDI). Nigerian financial institutions are expected to comply with FATCA by either registering with IRS or indicating to IRS that they do not maintain accounts for US nationals or companies. They are also expected to modify their internal control systems and processes in order to ensure compliance with the reporting requirements of FATCA.

This additional compliance cost imposed on FFIs has the potential of growing to unimaginable proportions should the revenue agencies of other countries with substantial economic clout seek to follow the example of the US IRS.

In view of these concerns, the bilateral IGAs introduced by IRS is a welcome development and the Nigerian Government and Federal Inland Revenue Service (FIRS) are urged to fully exploit the option in order to reduce the high regulatory compliance burden and additional cost of doing business in Nigeria, which customers (i.e. Nigeria taxpayers) of financial institutions in Nigeria will be forced to bear. And this would be consistent with both the letter and the spirit of the National Tax Policy. No valuable time should be wasted in unproductive analysis on the extra-territorial application of FATCA given the realities of global financial services industry (FSI). The FATCA train has left the station. Proactivity in managing its impact and implications for Nigeria's FSI is what is required.

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Oluseye Arowolo
Partner | Tax & Regulatory Services
oarowolo@deloitte.com

Yomi Olugbenro
Partner | Tax & Regulatory Services
yolugbenro@deloitte.com