

The IGA – FATCA's New Ally as Respects Brazil

Enacted on March 18, 2010, the U.S. Foreign Account Tax Compliance Act (commonly referred to by its acronym, "FATCA") targets U.S. taxpayer non-compliance via the holding of assets through offshore accounts or foreign companies. Since the initial frenzy at the time of its introduction, FATCA has not been on the Brazilian radar – until recently.

FATCA requires that all foreign financial institutions ("FFIs") report U.S. citizen account-related information to the U.S. Internal Revenue Service ("IRS"). It imposes considerable gross withholding penalty for those that are non-adherent. FFIs that do not adhere – or are not exempt under FATCA regulation – may have payment of U.S. source income made to them withheld at a rate of up to 30%.

The consequence to FFIs imposed by FACTA for non-adherence is burdensome. The effectiveness of application of the act might be limited, however, as some foreign institutions may be legally prohibited from disclosing information to the IRS by local legislation.

On September 23, 2014, an intergovernmental agreement ("IGA") for the exchange of information was signed between the U.S. and Brazil towards establishing the framework for the application of FATCA to Brazilian FFIs and as part of a global effort led by the Group of Twenty – G20 intended to prevent tax evasion.

The IGA – based on the Tax Information Exchange Agreement ("TIEA") signed between the U.S. and Brazil on March 20, 2007, and published in Brazil for legal effect within the country under Decree No. 8.003, dated March 15, 2013 is intended to improve international tax compliance.

Under the IGA, Brazilian financial institutions will report information on U.S. taxpayer-held assets in Brazil to the Secretariat of the Federal Revenue of Brazil ("SFR"), which will then transmit said information to the IRS. In exchange, the IRS will provide Brazilian authorities with information on Brazilian taxpayer financial operations on U.S. soil.

A reporting financial institution is defined by the IGA as comprising not only banks accepting deposits, but also custodial institutions holding third party assets and certain insurance companies. The definition includes as well investment entities that trade in securities and derivatives, such as investment banks and brokerage houses, and individual and collective portfolio management structures such as investment funds.

The basic obligation of Brazilian financial institutions under the IGA is to report account information. Such reporting is to take place annually within nine months of each calendar year to which the information refers. The information to be provided by the Brazilian financial institutions to the SFR must at least include the name, address and tax identification number (TIN) of the account holder and the account's number and balance.

There are important exceptions to the reporting obligation, namely: i) individual-held accounts with balances not exceeding US\$ 50,000.00 need not be reported; ii) existing legal entity-held accounts held by legal entities with a balance that does not exceed US\$ 250,000.00 need not be reported until the account balance exceeds US\$ 1,000,000.00; iii) non-profit charities and sponsored retirement funds are excluded from reporting obligations; iv) financial institutions that do not solicit clients outside Brazil are exempt from reporting provided they: a) have at least 98% of their account value held by Brazilian residents and have proper procedures in place for the detection and notification of U.S. taxpayer-held accounts or b) do not have more than US\$ 175,000,000.00 in assets on their balance sheet.

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The IGA contains no prohibition or restriction against the keeping by banks of depository or investment accounts held by U.S. nationals living in Brazil, or U.S. controlled entities incorporated in Brazil, provided they are properly reported. Whereas it is true as noted that financial institutions that have 98% of their accounts held by Brazilian residents and do not solicit clients outside this country will avoid reporting obligations altogether, this does not justify any discriminatory treatment against U.S. nationals or residents alone. In fact under present local rules both U.S. nationals living in Brazil and U.S. controlled entities incorporated in Brazil would be considered Brazilian residents and thus would not lead to disqualification from the non-reporting benefit.

Brazilian financial institutions have the obligation to undertake fairly extensive due diligence of existing accounts to determine whether they are reportable. Such due diligence covers review of electronically searchable data for individual-held accounts the balance of which exceeds US\$ 50,000.00 and does not surpass US\$ 1,000,000.00 ("high value accounts"). For accounts with balances greater than US\$ 1,000,000.00, enhanced review procedures apply requiring possible review of paper documents and the obligation to have procedures in place to ensure relationship manager reporting of relevant account characteristic change. Such review procedures must be completed no later than June 30, 2015 for high value accounts, and June 30, 2016 for other accounts.

As concerns legal entity-held accounts, the Brazilian financial institution due diligence encompasses verification of documents kept for anti-money laundering/know-your-customer purposes in relation to reportable accounts, to determine whether the account holder is a U.S. legal entity, whether it is controlled by a U.S. resident or whether it is another Brazilian financial institution not properly reporting accounts, in which case the global amount of payments made to said institutions must be reported to the SFR.

The IGA should only enter into force after ratified by Brazilian Congress and published by Decree. Further, for it to become effective will require extensive regulation from authorities such as the SFR and financial regulators. This being said, the likelihood of said approval taking place in the short term is high and Brazilian financial institutions should start preparing to meet their obligations under what will be the new rules.

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