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FOREIGN ACCOUNT TAX COMPLIANCE ACT (FATCA) AND AGREEMENT WITH ROMANIA – A STEP IN THE FIGHT AGAINST INTERNATIONAL TAX EVASION

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Abstract

The study of the international tax evasion reveals a practice of setting up fictitious entities, whose purpose is to provide large amounts of money through fraud. They perform by means of dissimulative maneuvers and operational skills important profits while producing at the same time big losses to trading counterparties who are not cautious enough.

International tax evasion is truly endangered by a new regulation - Agreement of fulfilment of tax obligations on foreign accounts of US citizens (FATCA- Foreign Account Tax Compliance Act).

The article aims to present both FATCA and FATCA bilateral Agreement between Romania and the US.

Keywords:

The US Foreign Account Tax Compliance Act, the fight against tax evasion, FATCA bilateral Agreement between Romania and the US.

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1. Introductory notions about FATCA

The pressure of the economic crisis on the US federal budget and exponential growth of tax evasion abroad have led to the introduction in October 2009 of a new draft bill in the US Senate, which aimed at reducing tax evasion. By 2009 a similar program operated, established by the IRS, but which proved unworkable. Thus, in 2001, UBS banking group, registered in that program, agreed to pay 780 million dollars penalties for hiding information regarding accounts of US citizens. The inefficiency of the program and the estimates of the loss of about 100 billion dollars a year due to unpaid taxes were among the strongest arguments for change. This is how FATCA (*Foreign Account Tax Compliance Act*) appeared, enacted into law by US President on March 18, 2010[3].

FATCA (*The US Foreign Account Tax Compliance Act*) is a set of legislative measures adopted in March 2010 by the United States of America (USA) in order to prevent and reduce tax evasion generated by the border activity of US residents.

Principles of FATCA are:

- non-resident financial institutions in the US are required to identify and report annually to the US tax authorities, automatically, specific information related to accounts opened by US residents, foreign entities with substantial US ownership and customers classified as recalcitrant;
- refusal to disclose specific information about US residents by financial institutions non-resident in the US is punishable under US law by applying a 30% withholding tax on any payment such as interest, dividends, rents, premiums, annuities, compensations, remunerations, fees and other annual or periodic fixed or determinable gains, coming from the US. This rate is applicable if the financial institutions non-resident in the US refuse to disclose the identity and communicate information about their clients who are US residents.

FATCA is linked to preventing and combating what is considered to be unfair competition by creating private capital in a state, stored afterwards outside the state of origin. Even legally obtained, it is considered that this money is a source of evil for the economy where it was produced, as it does not return to the production circuit of the state

[3] http://www.arb.ro/aparitii-media/antifrauda.html

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of origin, but is outsourced. To have a record of this money, USA identified a necessary way from this point of view - FATCA.

In this context, FATCA legislative package requires non-US financial institutions, under an intergovernmental agreement or independently to provide the IRS information about customers who have American citizenship or tax obligations to the US and relating to their accounts on holder, addresses, balances or transactions carried out. Also, if these people do not meet their tax obligations, financial institutions can perform withholding for IRS

So, the agreement to fulfil tax obligations on foreign accounts of US citizens lays the foundations for a genuine tax reform.

FATCA regulation must be understood in the context of the two large-publicized cases in 2008[4], and of the extraordinary dimension of tax evasion.

If the first case recalled targeted tax evasion through accounts at LGT Bank in Liechtenstein owned by Germans, and by other Europeans; secondly, placed on adverse positions USA and Swiss Bank, USA accusing the Swiss bank of conspiracy as a result of causing a fraud on the US by helping American residents hide their ownership of large sums of money deposited in offshore accounts in Swiss banks.

In terms of the dimension of US tax evasion, US Senate, estimates that the federal budget lost $ 100 billion dollars through tax evasion acts[5].

The US regulation, which has a broad incidence - as it targets the financial system as a whole - FATCA (*Foreign Account Tax Compliance Act*) is the keystone of the Obama administration in the fight against tax evasion practiced by opening accounts outside the US state, and also a revolutionary moment for the international financial system. The target group of this regulation is the natural and / or legal persons (in the sense that the majority of shareholders / associates have American nationality or citizenship) considered rich who have an American nationality or citizenship, as appropriate, who keep their savings in accounts outside the US. From the FATCA provisions, it is considered that rich people are

[4] I., B., Grinberg. *FATCA: an evolutionary moment for the international tax system*, p. 7, available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1996752 (accessed on 25/01/2013).

[5] O.E.C.D. - Centre for tax policy, "Fighting tax evasion", available at http://www.oecd.org/ctp/fightingtaxevasion.htm (accessed on 02/09/2013).

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those people who opened accounts outside the US that exceed the threshold of $ 50,000.

FATCA requires a reporting obligation and a withholding tax system at the rate of 30% of all payments from US for foreign financial institutions that refuse to disclose the identity of their customers with tax residence in the US. The tax regime can be avoided only if these financial institutions enter into agreements with the US, under which they can conduct identification of customers, American natural or legal persons, reporting on them. Reporting covers both new customers and pre-existing ones.

Since FATCA faced the opposition of other countries, motivated by the fact that the disclosure of financial data on clients of financial institutions comes in conflict with the obligation of confidentiality of data on their customers, USA solved this problem by regulating two types of bilateral government agreements, the models of which have already been published. The first published model allows governments of states which enter into agreement with FATCA to substitute their own financial institutions, which are obliged to report to national governments, which shall afterwards report to the US tax authorities; the second model establishes an agreement of the foreign state to request its own financial institutions to cooperate with US tax authorities. A statistical achieved in this respect notes the preference for the model first mentioned[6].

On September 12, 2012, they concluded the agreement required between the US and the UK, and discussions were held with other fifty states. The process is in final stages in countries like: France, Germany, Italy, Spain, Japan, Switzerland (opted for the second option), Canada, Denmark, Finland, Guernsey, Ireland, Isle of Man, Jersey, Mexico, the Netherlands and Norway, plus Argentina, Australia, Belgium, Cayman Islands, Cyprus, Estonia, Hungary, Israel, Korea, Liechtenstein, Malaysia, Malta, New Zealand, Slovakia, Singapore and Sweden. Among the states that have opted to sign is and Romania, along with Bermuda, Brazil, British Virgin Islands, Chile, Czech Republic, Gibraltar, India, Lebanon, Luxembourg, Russia, Seychelles, Saint Maarten, Slovenia and South Africa.

[6] Christians Allison, What you give and what you get: reciprocity under a Model 1 Intergovernmental Agreement on FATCA, available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2292645 (accessed on 11.09.2013).

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To this end, in August 2013 they launched FATCA portal for registration of financial institutions which are required to make reports under that act, including of financial institutions in the State which concludes intergovernmental agreements with the US tax authorities under FATCA. The establishment of an online account is conditioned by the appointment of persons authorized by the financial institution to make reports. The completion of data inserted on FATCA portal will be made until January 1, 2014. Registration means receiving an identification number after the date mentioned above.

The provisions of the Act on fulfilment of tax obligations on foreign accounts of US citizens, as amended, set two deadlines for tax withholding at a rate of 30% for incomes obtained from US: January 1, 2014 - for income from dividends and interest obtained by non-participating foreign financial institutions, namely that do not conclude the agreement for providing information with the Treasury and Tax Authorities in the US, and January 1, 2015 for the other types of payments.

FATCA intends to create a much better collaboration between financial institutions globally. It involves both developed economies and emerging economies. Although announced as a special event the entry into force of FATCA regulations on January 1, 2014, was extended by six months, at least until July 1, 2014.

2. FATCA bilateral Agreement between Romania and the US

In order to eliminate barriers to reporting and tax withholding they suggest the conclusion by the State of residence of financial institutions to which FATCA provisions are applied of a FATCA bilateral agreement with the American tax authorities. In this respect, Romania has initiated such an agreement to facilitate the reporting process by Romanian financial institutions.

Financial institutions in Romania[7] which are targeted by the application of FATCA provisions are:

- credit institutions
- custodian institution
- investment entities
- insurance companies.

[7] http://www.mfinante.ro/acordfatca.html?pagina=domenii

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The term starting on which FATCA provisions are applied is July 1, 2014, and this is first term starting from which certain reporting requirements (eg, collecting information related to US residents, foreign entities with substantial US ownership and customers classified as recalcitrant) become applicable.

Later, a new registration deadline was established on the IRS website, namely May 5, 2014, being extended by 10 days to the original date of April 25, 2014 date by which financial institutions non-resident in the US could register on site on US Treasury as registered institutions that align to FATCA provisions.

Romanian and American tax authorities have started the process of negotiating the FATCA Agreement according to the standard Model 1A (with reciprocity).

Romania is on the list of countries with which the US authorities consider they have reached a substantive agreement, even if the Agreement was not actually signed as of April 2, 2014 and it will be maintained on the list until December 31, 2014 provided that FATCA Agreement is signed by the end of the year.

Regarding the registration deadline on the IRS website, in Romania's case, given that it is included in the list of countries with which the US authorities consider they have reached a substantive agreement, the provisions of the Note of US Treasury no.1 from 2014 shall be taken into account.

According to US Treasury Note no.2014 - 17 of April 2, 2014, until the signing of a FATCA Agreement, Romanian resident financial institutions are allowed to register on FATCA registration website, as registered deemed-compliant FFI. With this status, financial institutions will make all reports according to the provisions of standard Model 1A (with reciprocity). Also, they will be allowed to confirm this status to withholding agents and shall not be required to obtain a registration number (˝GIIN˝) before the date of January 1, 2015.

Conclusions

Internationally, efforts to combat tax evasion take the form of cooperation. One of the most common forms of combating international tax evasion takes the form of codes. Unfortunately, all these codes are only a sum of good intentions, being rather aspirational than operational.

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A proposal in 2007 aimed at developing such a Code, under the aegis of the United Nations[8], which contained provisions on cooperation in combating international tax evasion. The objectives are: assistance in developing international rules applicable to all nations in preventing the conduct of tax evasion deeds; identification of aggressive forms of tax evasion, which is different from common forms of tax evasion; to provide necessary support for civil society to prevent international tax evasion.

Given the global economic crisis that still persists, the fact the national budgets are still subject to strong pressures, the commitments signed to honour the new global regulations on taxes, there are enough signs that FATCA will be implemented internationally.

FATCA analysis highlights the main objective pursued consistently by still the first power of the world, USA, the erosion of bank secrecy, besides ensuring an unprecedented fiscal transparency. Americans' attempt to explain the positive effects of FATCA explain even the banking secrecy as one of the greatest evils in the world, considering it a violation of universal human rights[9]. Thus, starting from the fact that the UN Convention on Economic, Social and Cultural Rights recognizes and guarantees the right to adequate living conditions - food, clothing and housing (art. 11), the right to health insurance schemes, to drinking water (art. 12) and the right to education (art. 13) - banking secrecy (not covered by any international treaty or convention on human rights) and tax evasion come in conflict with human rights when, due to them, state governments are unable to meet the economic and minimalist rights and demands.

[8] M., McIntyre. *United Nations Code of Conduct of Cooperation in Combating International Tax Evasion*, Wayne State University Law School – Legal Studies Research Paper Seriesno. 08-12/2008, available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1118805 (accessed on 04.09.2013).

[9] S., Cohen. *Does Swiss bank secrecy violate international human rights?,* 2013, p. 4, available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2297020 (accessed on 04.09.2013).

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