

## HIRE ACT IMPOSES REPORTING, COMPLIANCE OBLIGATIONS ON FOREIGN FINANCIAL INSTITUTIONS

**T**hough most of the publicity generated by the Hiring Incentives to Restore Employment Act of 2010 (“the HIRE Act”) focused on its intent to create jobs, the bill will have significant tax ramifications as it incorporates provisions of the Foreign Account Tax Compliance Act, which was introduced in Congress last year.

The HIRE Act imposes significant new information reporting and compliance obligations on foreign financial institutions (and some other foreign persons). Perhaps most important, unless foreign financial institutions identify and disclose their U.S. account holders, payments to the institutions of U.S. source investment income and proceeds from certain equity and debt instruments of U.S. issuers will be subject to a new 30 percent withholding tax.

Key tax provisions of the HIRE Act include:

- The addition of a 30 percent withholding tax on any “withholdable payment” (which includes U.S. source investment income and also certain capital gain income) made to:
  - (a) a foreign financial institution unless the foreign financial institution agrees in writing with the IRS to take certain steps to disclose U.S. investors, or
  - (b) a “non-financial foreign entity” (e.g., a hedge fund or a private equity fund) unless the nonfinancial foreign entity provides certain disclosures with respect to its U.S. investors (or certifies that it has none) to the IRS.

Generally, these provisions are effective for payments made after December 31, 2012. However, payments on certain obligations will be “grandfathered.”

- The repeal of the portfolio debt exception as it applies to foreign targeted bearer bonds. The HIRE Act did not repeal the portfolio debt exception as it applies to “registered debt obligations.” Most portfolio debt falls into this latter category. Issuers and holders of portfolio debt obligations would be well advised to review the basis for qualification. This provision applies to obligations issued after March 18, 2012.
- The addition of new reporting rules requiring any U.S. individual who holds an interest in a “specified foreign financial asset” to report information about such asset on the individual’s tax return if the aggregate value of such assets is in excess of \$50,000. This reporting requirement also applies to entities formed or used to hold specified foreign financial assets (“SFFAs”). SFFAs include financial accounts maintained by a foreign financial institution and any stock or security issued by a non-U.S. person, any financial instrument or contract held for investment that has a non-U.S. issuer or counterparty, or any interest in a foreign entity. Failure to disclose the required information regarding SFFAs will result in a \$10,000 penalty. These provisions



apply to taxable years commencing after March 18, 2010. It seems clear that regulations or some other form of guidance will have to be issued to enable taxpayers to comply with these provisions.

- The addition of a 40 percent penalty for any underpayment attributable to any undisclosed SFFA and the extension of the statute of limitations to six years for any understatement attributable to any undisclosed SFFA. This provision applies to returns filed after March 18, 2010 as well as to previously filed returns where the applicable statute of limitations has not expired.

- An expansion of reporting requirements with respect to passive foreign investment companies. All shareholders of a passive foreign investment company now are required to file an annual report with respect to such investment. This provision is effective as of March 18, 2010 but is premised on such reporting “as the Secretary may require.” Therefore, compliance appears not to be required until regulations or some other form of guidance is issued as to what information must be reported.
- The imposition of a 30 percent withholding tax on certain “dividend equivalent” payments, absent a reduction in rate pursuant to an applicable U.S. tax treaty. This provision applies to certain “swap payments” that are contingent upon, or determined by reference to, the payment of a dividend. This provision is effective for payments made on or after September 14, 2010.
- Increased reporting requirements and penalties with respect to foreign trusts. The effective dates of these provisions are varied but generally are effective as of March 18, 2010.

The HIRE Act contains many other significant provisions that can affect international transactions. ■

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