To address the fiscal deficits created by the recent global financial crisis, many governments have opted to increase tax revenues by targeting individuals who are not fully disclosing their taxable income. With the US leading the way, the Foreign Account Tax Compliance Act became US legislation in March 2010. Detailed regulations were issued by the US Department of the Treasury on 17 January 2013 and the latest amendments were issued on 20 February 2014.

FATCA’s main objective is to combat off-shore tax invasion by US citizens and US companies through measures which increase transparency, enhance reporting and strengthen sanctions. These measures will almost certainly affect US tax payers, however, the greatest impact will be felt by the banks outside the US. Non-US banks will automatically be burdened with a 30% withholding on most US-linked income, unless they comply as follows:

**DOCUMENTATION**
- Obtain sufficient information from all account holders to properly identify US accounts
- Apply verification, due diligence and on boarding procedures

**WITHHOLDING**
- Withhold 30% from most US-linked income for non-compliant account holders
- From 31 December 2016, withholding 30% from US-linked proceeds for non-compliant account holders, and from payments to other non-US financial institutions to the extent the payments are “pass thru payments”

**REPORTING**
- For each US account, report the account details, holder details, balance and movements annually
- Provide additional info to the US Internal Revenue Service (IRS) as requested

For non-US banks to comply with FATCA, significant changes will need to be made to their internal systems, control frameworks, processes and procedures, which will be a time-consuming and costly exercise.

Additionally, with the compliance deadlines below, banks which have not yet made significant progress with the changes that need to be made to internal processes will risk being penalized:

<table>
<thead>
<tr>
<th>Date</th>
<th>Event Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>August 2013</td>
<td>IRS Registration Opened</td>
</tr>
<tr>
<td>June 2014</td>
<td>Final date for priority GIIN listing</td>
</tr>
<tr>
<td>July 2014</td>
<td>Documentation &amp; US Income Withholding</td>
</tr>
<tr>
<td>March 2015</td>
<td>Reporting</td>
</tr>
<tr>
<td>January 2017</td>
<td>Gross Proceeds and Passthru Withholding</td>
</tr>
</tbody>
</table>
**IGA implications**

The US and Indonesia have recently reached an agreement in substance and an Intergovernmental Agreement (IGA) is treated as “in effect” as of 4 May 2014 with the expectation that an actual IGA will be signed later this year. An IGA ultimately reduces the overall burden on financial institutions, simplifies due diligence requirements and broadens agreements between the Indonesian Tax Office (ITO) and the US Internal Revenue Service (IRS). Further, by signing an IGA, the Indonesia government will agree to enact domestic laws that mandates all financial institutions operating in Indonesia to participate with FATCA and comply with its core principles.

Additionally, the model applied by the IGA is Model 1, which has the following key implications:

- **Relaxed withholding requirements**: withholding is no longer required for recalcitrant accounts (accounts which are not providing the needed info for FATCA) and financial institutions operating in Indonesia (except for unresolved significant non-compliance)
- **Suspension of account closing requirements**: recalcitrant accounts are no longer required to be closed
- **Resolution of conflicts with domestic law**: the withholding and reporting requirements no longer conflict with local law
- **Reporting to the ITO**: reporting is done to the ITO (instead of to the IRS directly), which will in turn provide the information to the IRS

**FATCA reporting**

Since reporting is considered as the last step of the FATCA compliance chain, and IRS reporting requirements have just recently been finalized, there has been limited disclosure on this aspect. Since reporting forms an integral part of FATCA, financial institutions shouldn’t underestimate the amount of work required. Just as for other compliance regimes, there will be a need to have a robust reporting solution in place to manage the complexities relating to data quality, data security, automation, and analysis, whilst also being able to accommodate further regulatory change as FATCA evolves.

In order to accurately produce the FATCA reports, banks will ultimately need to have data and business rules available to:

- Identify **US accounts**: US citizens, US residents, US corporations, substantial US owners, etc.
- Identify **NPFFIs**: Non-Participating Foreign Financial Institutions – i.e. non-compliant entities
- Identify **recalcitrant accounts**: accounts which are not providing the needed info for FATCA
- Identify **US indicia**: links to the US, based on birth place, “in care of” address, power of attorney granted to a person with a US address etc.
- Report **account holder** details: name, address, Tax Identification Number, entity type, etc.
- Report **US owner** details: relevant details of US persons with “significant” company ownership
- Report **financial details**: account balance, interest, dividends, proceeds, redemption, etc.
- And more...

The figure below provides a snapshot of the data (which typically comes from disparate systems on different technical platforms and data models) that banks will need to consolidate for FATCA reporting:

Furthermore, the business rules will need to be sufficiently maintainable and extensible, not only to cope with inevitable FATCA changes, but also to comply with future Global FATCA (GATCA) requirements.
Current compliance status of banks in Indonesia

More than 350 financial institutions in Indonesia have now completed their registration via the IRS portal, and most Tier-1 banks in the Indonesia have been preparing for FATCA for the past 2 to 3 years by focusing on the following aspects:

- **On-boarding procedures**: analysis of existing procedures, and creation of new account opening and other procedures to ensure compliance with FATCA’s verification and due diligence requirements
- **Monitoring procedures**: creation of procedures which regularly validate information, such as account classification and customer circumstances

Many Tier-2 and Tier-3 banks, on the other hand, have made significantly fewer preparations; even though a majority of the smaller banks have made some FATCA progress, only a minority are expected to be fully compliant with every single documentation requirement (which has been in effect since 1 July 2014). Some smaller banks have actually decided to try and avoid FATCA by ceasing to make US-linked investments, and/or exiting US customers. As a practical matter this will be very difficult as FATCA does not rely on a bank actually having US clients. Non-complying banks may continue to be exposed to the impact of FATCA, particularly if they receive US source payments or deal with participating foreign financial institutions.

The main reason for the lack of preparation with the smaller banks is uncertainty; there is still a lack of clarity with IRA’s FATCA regulations, Indonesia’s final IGA as well as the future GATCA regime, which makes it challenging for banks to come up with a robust solution which not only meets the obvious requirements at hand, but also the ones yet to come.

With regards to FATCA reporting, many banks (including the bigger ones) have not made any progress at all, even though the March 2015 reporting deadline is looming in the horizon. According to a recent survey done by Wolters Kluwer Financial Services, more than half (54%) of respondents from over 60 financial institutions in Asia-Pacific said they still don’t know how they will meet next year’s submission requirements:

From another Wolters Kluwer Financial Services survey, a whopping 70% of more than 30 banks in the region agreed that the single most important challenge for regulatory reporting (including FATCA) is data management, which entails obtaining the correct data in the required state for onward reporting:

**What is your key challenge for regulatory reporting?**

If banks are having a hard time complying with today’s FATCA requirements, the 2015 reporting deadlines will be even more of a challenge for the industry.

Note that with the IGA now being imminent, withholding is less of an immediate concern for banks in Indonesia, and will only be applicable for rather exceptional cases.
Relaxed penalties for effort in good faith

With the US realizing that many banks in Indonesia and other parts of world are finding it challenging to comply with FATCA, the IRS issued a notice on 1 May 2014 to relax its penalties for the time being. Calendar years 2014 and 2015 will be considered as a transition period, and institutions deemed to be making efforts to comply with FATCA "in good faith" will not be subject to withholding tax penalties, even if they do not strictly meet the deadline.

However, "good faith" has not been clearly defined, nor were any concrete examples provided as part of the notice.

Achieving a competitive advantage

FATCA regulatory requirements will certainly be onerous for banks in Indonesia, however it also creates an opportunity to achieve competitive advantage for those banks that are able to implement in a manner that not only meets external compliance, but also generates greater transparency internally, allowing for reduction of regulatory risk and enhanced management information.

The success of this reform and the ability of banks to adopt them in a cost-effective and compliant manner will depend on the investment in an infrastructure which collects and automates the production of the required regulatory information. The best-positioned banks will be those that upgrade existing infrastructure to collect the additional information required by regulators, while simultaneously consolidating and centralizing this information with other data currently being used for internal and external purposes. A single data repository could then form the basis of all regulatory requirements, including FATCA reporting.