

Guidance Note

FATCA and CRS in the Cayman Islands

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Introduction

The regulatory framework in the Cayman Islands is increasingly complex and requires specialist legal support. Stuarts' funds attorneys regularly advise our clients on how to be compliant with their current regulatory obligations and in particular for FATCA and CRS.

US FATCA

The Foreign Account Tax Compliance Act ("**US FATCA**") was enacted in the United States in 2010 in order to reduce perceived offshore tax evasion by US persons holding assets through offshore accounts that were not subject to US information reporting to the Internal Revenue Service (the "**IRS**"). US FATCA requires a foreign entity that is a foreign financial institution ("**Financial Institution**" or "**FI**") either (i) to enter into an agreement with the IRS relating to such reporting or (ii) to comply with local laws that implement an intergovernmental agreement ("**IGA**"). If a Financial Institution does not comply with US FATCA, a 30% withholding tax is imposed on US source income of that Financial Institution. Financial Institutions are also required to close accounts where their US customers do not provide information to be collected by it.

UK FATCA

On 5 November 2013, the Cayman Islands government signed an intergovernmental agreement with the United Kingdom (the "**UK IGA**", and together with the US IGA, the "**IGAs**") aimed at improving international tax compliance which provides a framework for the implementation in the Cayman Islands of a UK tax residents reporting regime ("**UK FATCA**"), which is similar in scope to US FATCA.

Unless there is an available exemption, Cayman Islands based Financial Institutions which are subject to the IGAs will be required to identify **Financial Accounts**¹ held by United States or United Kingdom **Specified Persons**² (as the case may be) and report specified information about those accounts to the Cayman Islands Tax Information Authority (the "Cayman TIA"). The Cayman TIA would then pass this information on to the

¹ The term "**Financial Account**" means an account maintained by a Financial Institution, and includes: (i) in the case of an Entity that is a Financial Institution solely because it is an Investment Entity, any equity or debt interest (other than interests that are regularly traded on an established securities market) in the Financial Institution; (ii) in the case of a Financial Institution not described in subparagraph (i), any equity or debt interest in the Financial Institution (other than interests that are regularly traded on an established securities market), if [(i) the value of the debt or equity interest is determined, directly or indirectly, primarily by reference to assets that give rise to U.S. Source Withholdable Payments, and (ii)] the class of interests was established with a purpose of avoiding reporting in accordance with the [relevant] IGA; and (iii) any Cash Value Insurance Contract and any Annuity Contract issued or maintained by a Financial Institution, other than a noninvestment-linked, nontransferable immediate life annuity that is issued to an individual and monetizes a pension or disability benefit provided under an account that is excluded from the definition of Financial Account in Annex II. Notwithstanding the foregoing, the term "Financial Account" does not include any account that is excluded from the definition of Financial Account in Annex II of the relevant IGA.

² The term "**Specified Person**" means: (i) in respect of the US IGA, a U.S. citizen or resident individual, a partnership or corporation organized in the United States or under the laws of the United States or any State thereof, a trust if (i) a court within the United States would have authority under applicable law to render orders or judgments concerning substantially all issues regarding administration of the trust, and (ii) one or more U.S. persons have the authority to control all substantial decisions of the trust, or an

IRS (in relation to US accounts) and His Majesty's Revenue and Customs ("HMRC") (in relation to UK accounts) on an automatic basis annually.

CRS

On 16 October 2015, the Cayman Islands Tax Information Authority (International Tax Compliance) (Common Reporting Standard) Regulations, 2015 (the "**CRS Regulations**") were brought into effect. The CRS Regulations are the means by which the OECD Common Reporting Standard (the "**CRS**"), being due diligence and reporting standards for the global automatic exchange of information for tax purposes ("**AEOI**"), are to be implemented in the Cayman Islands. It is anticipated that the CRS Regulations will shortly be followed by further regulations which will deal primarily with enforcement of the CRS and penalties for non-compliance.

In many ways, the obligations under the CRS Regulations apply in the same manner as FATCA and, specifically, to Reporting Financial Institutions ("**Reporting FIs**"). A Depository Institution, Custodial Institution, Specified Insurance Company and an Investment Entity (which includes most funds) are all considered FIs for the purposes of the CRS Regulations and, again, the relevant definitions largely mirror those used in FATCA.

The requirements of the CRS Regulations are also similar to FATCA. They require:

- a. the establishment by Reporting FIs of policies and procedures designed to identify an account holder or controlling person that is tax resident in a jurisdiction that is participating in the implementation of the CRS (a "**Participating Jurisdiction**") and to apply the due diligence procedures set out in the CRS (commencing 1 January 2016 for new accounts);
- b. that due diligence information, and a record of the procedures taken to comply, must be retained for six years from the end of the year the information was obtained or the procedures were carried out;
- c. a Reporting FI with reporting obligations to electronically notify the TIA (through the TIA's online AEOI portal before 30 April of the first year the Reporting FI is required to comply with the reporting obligations) of the name and categorisation of the Reporting FI and the name, address designation and contact details of an individual authorised to be the principal point of contact of the Reporting FI; and
- d. a Reporting FI to electronically file a return (report) of Reportable Accounts with the TIA through the AEOI portal before 31 May of the year following the calendar year to which the report relates. Accordingly, the first reporting year under the CRS Regulations is 2016 with reports due by 31 May 2017.

It is important that a Reporting FI ensures that its systems can identify account holders (and their 'know your client' information) in each of the Participating Jurisdictions from

an estate of a decedent that is a citizen or resident of the United States, subject to certain exceptions set out in the US IGA; and (ii) in respect of the UK IGA, a person or Entity who is resident in the United Kingdom for tax purposes, and includes a person or Entity who is resident in both the United Kingdom and the Cayman Islands, under the respective domestic law of country, subject to certain exceptions set out in the UK IGA.



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1 January 2016. In this regard, the Ministry of Financial Services has published self-certification forms that the industry may use which were developed by the FATCA/CRS Working Group, for compliance with the CRS, and US and UK FATCA. They may be used as is, or modified, as necessary. Please let us know if you require a copy of these self-certification forms.

The Ministry of Financial Services has advised that Self-certifications should be obtained and validated as part of financial institutions' account opening procedures. If it is not possible to obtain a self-certification on 'day one' of the account opening procedures, it should be obtained and validated as quickly as possible and in any event, no later than 90 days after the account has been opened. If a financial institution fails to obtain a self-certification within 90 days, it must report the account to the Cayman Islands Department for International Tax Cooperation ("DITC") as undocumented. Financial institutions with a disproportionate number of undocumented accounts may be subject to DITC compliance reviews, once the review regime has been developed. In practice, it is expected that FIs will seek to obtain information on all of its account holders and not just those who are tax resident in a Participating Jurisdiction. Each Reporting FI should also have its own documented set of policies and procedures for international tax compliance. We recommend that such Reporting FIs update their existing FATCA policies and procedures manuals to include the CRS by **1 January 2016**.

The TIA has published a list of [Participating Jurisdictions](#) pursuant to the CRS Regulations.

The OECD has published official commentary on the CRS, which the CRS Regulations acknowledge is an integral part of the CRS and accordingly applies for the purposes of the AEOI under the CRS Regulations. In addition, the OECD has published a CRS Implementation Handbook which, although not part of the CRS, provides a practical guide to implementing the CRS to both government officials and FIs and includes a comparison between the CRS and FATCA. The commentary and CRS Implementation Handbook can be found on the OECD website (www.oecd.org/tax/automatic-exchange/).

The Ministry of Financial Services anticipates that CRS Guidance Notes will be published in Q1 2016, following consultation with the FATCA/CRS Working Group. The Working Group is currently considering issues related to CRS implementation, and its guidance notes will be limited to practical aspects of the CRS that are specific to Cayman.

Read more on the [Implementation of the OECD Common Reporting Standard in the Cayman Islands](#).

Who is Affected by FATCA and CRS?

The IGAs and the FATCA Regulations apply to all Cayman Islands Financial Institutions ("CFIs"), regardless of whether they hold any Financial Accounts for Specified Persons. Some action will be required of all CFIs that maintain Financial Accounts. The extent of that action will depend on a number of factors including whether account holders are Specified Persons and the value and nature of the Financial Account.

FATCA can also have an impact on entities which are not Financial Institutions. Any non-US entity under the US IGA and non-UK entity under the UK IGA that is not a FI will be



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considered a Non-Financial Foreign Entity (“**NFFE**”) under US or UK FATCA. There are two categories of NFFE (i) an **Active NFFE**³ or (ii) a Passive NFFE. A NFFE, whether Passive or Active, has no obligations itself under the IGAs and FATCA Regulations but may have to confirm its status and provide details of **Controlling Persons**⁴ to another Financial Institution if requested to do so by the Financial Institution. A CFI may also have reporting obligations in respect of Financial Accounts it maintains for a Passive NFFE with Controlling Persons who are Specified Persons.

The FATCA Regulations and Guidance Notes assist Cayman Islands entities in determining their status as a Financial Institution or NFFE including whether it would be an Active or Passive NFFE.

Is the Cayman Islands Entity a Financial Institution?

The first step to be undertaken by a Cayman Islands entity is to establish whether, for the purposes of the IGAs, the entity is a Financial Institution. This, together with establishing the type of Financial Institution it is, will determine the extent of the obligations that need to be undertaken.

A CFI is any Financial Institution organised under the laws of or resident in the Cayman Islands. For these purposes, organised under the laws of the Cayman Islands means the following:

- for a company, if the company is incorporated in the Cayman Islands;
- for trusts, if any of the trustees are incorporated, registered or licensed in the Cayman Islands; and
- for partnerships, if the partnership is established in the Cayman Islands.

Having established that an entity is a Cayman Islands entity (for FATCA purposes), it should be determined whether it is a Financial Institution. Under the US IGA, the term Financial Institution applies to non-US entities which fall within any, or more than one, of the below categories. Under the UK IGA, the term applies to non-UK entities in the same categories. These are:

- Custodial Institution - any entity that earns a substantial portion (at least 20 percent) of its gross income from the holding of financial assets for the accounts of others and from related financial services.
- Depository Institution - broadly any entity that is engaged in a banking or similar business.
- Investment Entity - an entity that conducts as a business, or is managed by an entity that conducts as a business, one or more of the following activities, for or on behalf of a customer, trading in:

³ An “**Active NFFE**” is essentially an entity that conducts an actual business activity other than holding assets that produce investment income such as interest, dividends etc. and less than 50% of that entity’s gross income for the preceding year is passive income (i.e. income other than trading income) and less than 50% of its assets are assets that produce passive income. A Passive NFFE is any NFFE that is not an Active NFFE.

⁴ “**Controlling Person**” means a natural person who exercises direct or indirect control over an entity. For this purpose, a 25% ownership threshold applies for companies, partnerships, trusts and foundations.



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- money market instruments (cheques, bills, certificates of deposit, derivatives etc.)
- foreign exchange
- exchange, interest rate and index instruments
- transferable securities and commodity futures trading
- individual and collective portfolio management
- otherwise investing, administering or managing funds or money on behalf of other persons



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In practice, when applying this definition, an entity that is professionally managed will generally be an Investment Entity, by virtue of the managing entity being an Investment Entity.

- Specified Insurance Company - an insurance company is a Specified Insurance Company when the products written are classified as Cash Value Insurance or Annuity Contracts or if payments are made with respect to such contracts.

The definitions of the entities above are as provided by the IGAs, however, the FATCA Regulations and Guidance Notes provide that it is open for a CFI to choose to use a definition of Financial Institution set out in the US FATCA Treasury Regulations relating to US FATCA (the “US Treasury Regulations”). Whether that would be beneficial to a particular entity will need to be assessed on a case by case basis.

A subsidiary or branch of a non-Cayman Islands entity (including a US entity) carrying on a business, as a Custodial Institution, a Depository Institution, an Investment Entity, or a Specified Insurance Company in the Cayman Islands, will also be a Reporting Cayman Islands Financial Institution.

The FATCA Regulations and Guidance Notes assist Cayman Islands entities in determining whether it falls within one of the above categories and therefore whether it is a Financial Institution. In practice, most investment funds in the Cayman Islands (including hedge and private equity funds) will be considered an ‘Investment Entity’ and therefore a Financial Institution.

Read more on [How does US and UK FATCA Apply to Cayman Islands Entities.](#)

How Stuarts Can Help?

Stuarts can help clients with the full spectrum of FATCA and CRS compliance. The following is an overview of services provided by our experienced and dedicated regulatory compliance team:

AEOI service	Fees Per Entity/LP	Fees Per GP
Classification	US\$2,000 to \$3,000 (one-off)	US\$2,000 to \$3,000 (one-off)
IRS Registration/DITC Notification	US\$1,200 (one-off).	Included in the below fees
Annual Reporting to cover all US FATCA and CRS reports	US\$2,000 (per annum)	\$1,000 per entity
Annual CRS Compliance Form	US\$500 per entity (per annum)	N/A
Preparing CRS Policies and Procedures	US\$3,950 for the first entity and \$750 for each additional entity (one-off);	\$750 for each additional entity (one-off)
FI Deactivation	\$600 per entity (one-off)	\$600 per entity (one-off)

Guidance

This publication is for general guidance and is not intended to be a substitute for specific legal advice. Specialist advice should be sought about specific circumstances. If you would like further information, please contact:

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Stuarts Humphries is a leading Cayman Islands legal practice with international reach. Offering a full range of corporate and commercial legal advice together with a constant client focus, our experienced attorneys assist our clients on their most significant and challenging commercial transactions, structures, liabilities and obligations.

Our proven track record in advising leading international Law Firms, Investment Managers, Investment Companies and High-Net-Worth individuals is a result of the deep understanding of our markets.

At Stuarts, we strive to build and maintain enduring relationships with our clients through the combined legal expertise and business acumen of our practice groups and by providing outstanding service.



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