Corporate Tax Alliance

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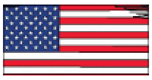
FATCA *by Marc Schwartz & Paul Tadros*



Many taxpayers around the world have heard of the US' infamous Foreign Account Tax Compliance Act ("FATCA"). This law has proven to be onerous and has caused aggravation globally, including the US.

FATCA created an entirely new chapter in the US Internal Revenue Code with the objective of ensuring US tax compliance. The IRS has focused specifically on US persons through the use of offshore accounts.

> "FATCA created an entirely new chapter in the US Internal Revenue the use of offshore accounts"

Unless strict and oftentimes burdensome reporting requirements are met, FATCA imposes a 30% withholding tax on certain payments to "Foreign Financial Institutions" ("FFIs") and "Non-Financial Foreign Entities ("NFFEs").

Two important definitions play a significant role in the application of the FATCA provisions: (a) "U.S. Account" i.e., Any foreign account maintained by a foreign financial institution that is held by one or more specified U.S. persons or U.S. owned foreign entities. In addition to the traditional types of bank accounts, a "foreign account" as defined above includes, inter alia, cash value insurance contracts and annuity contracts issued by and maintained by an insurance company, a holding company or financial institution; and (b) foreign financial institution.

- **Withholdable Payments**" include payments of interest, dividends, rents, royalties, salaries, wages, annuities, licence fees, gains and profits where such payment is from sources within the U.S. Withholdable Payments also include the gross proceeds from the sale of U.S. property (including U.S. stocks and securities) that is capable of producing interest or dividends.
- "**FFIs**" include non-U.S. entities that:
  - -Accept deposits in the ordinary course of banking or similar business ("**Depository Institutions**");
  - -As a substantial portion of their business, hold financial assets for the account of others, in a custodial capacity. The portion of its business is "substantial" where the entity earns over 20% of its gross income from such activities during the 3 year period ending on 31 December of the year in which the determination is made, or since incorporation, if shorter ("**Custodial Institutions**");
  - -Are engaged primarily in the business of investing, reinvesting or trading in securities e.g. funds, securitisation vehicles, trusts, corporate trustees and fiduciaries. The "primarily" threshold is met if 50% of the entities' gross income for the 3 year period ending on 31 December of the year in which the determination is made, or since incorporation if shorter, is attributable to such activities ("Investment Entities").
  - -Insurance companies.
- "**NFFEs**" are entities which do not fall into the definition of FFI above but nonetheless hold U.S. assets or have U.S. investors.

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Avoiding the 30% withholding tax obligation

Payment of the 30% withholding tax penalty on all U.S. source "withholdable payments" may be avoided by FFIs by either:

- Becoming a "Participating FFI". This involves entering an agreement with the U.S. Department of Treasury to:

  A Identify and report to the IRS information on certain U.S. persons (including U.S. controlled foreign entities) that directly or indirectly hold depository and custodial accounts with the FFI or equity or debt issued by the FFI. Information to be forwarded includes:

    -The name, address and TIN of each U.S. account holder;
    -The account number or designation;
    -The account balance or value;
    -The gross receipts and gross payments or withdrawals from the account.

  The FFI will also be required to comply with any due diligence or verification procedures requested by the relevant U.S. authorities in respect of their U.S. accounts holders.

  B Withhold on "passthru" payments made to "recalcitrant" account holders and account holders that are "Non Participating FFIs".

  C In some cases, close accounts with respect to which reporting is not permitted.

- Complying with any Intergovernmental Agreement (IGA) entered into by the FFI's local jurisdiction.

Similarly, NFFEs will not find themselves liable to the 30% withholding tax where they identify each substantial U.S. person that owns a direct or indirect interest, or where they certify that there are no substantial U.S. owners.

Methods of implementation of FATCA

Methods of implementation of FATCA will vary from jurisdiction to jurisdiction. As mentioned above, many jurisdictions are opting to enter **Intergovernmental Agreements ("IGAs")** with the U.S. Government.

Model intergovernmental agreements

The U.S. Department of Treasury has published model IGAs which follow two approaches.

- Under **Model 1**, financial institutions in the partner country report information about U.S. accounts to the tax authority of the partner country. That tax authority then provides the information to the U.S. Model 1 comes in a reciprocal version (Model 1A) under which the U.S. will also share information about the partner country's taxpayers with the partner country, and a non-reciprocal version (Model 1B
- Under **Model 2,** partner country financial institutions report directly to the U.S. Internal Revenue Service and the partner country agrees to lower any legal barriers to that reporting.

FFIs in Model 1 IGA jurisdictions will be governed by the laws enacted in their own countries while those in Model 2 IGA jurisdictions will follow the final FATCA regulations.

In order to signal to other countries that the U.S. will cooperate in tax matters, Congress passed legislation requiring all U.S. banks to report to the IRS interest paid to non-residents of the U.S. notwithstanding that such interest is exempt from U.S. withholding tax. It is anticipated that the IRS will share that information with the tax authorities of the countries in which the individuals are resident. Currently (and for a number of years), the U.S. and Canada have been routinely sharing such information. For example, if a U.S. person receives interest income from a bank in Canada, the Canada Revenue Agency automatically shares that information with the IRS and vice versa.

FATCA implementation dates

FATCA became effective 1 January 2013; however, regulations phased in reporting and withholding obligations over a number of years beginning 1 January 2014. The regulations, in essence, progressively increased the compliance burden for FFIs and other affected entities. Over time it is anticipated that additional intergovernmental agreements will be signed, increasing the global flow of financial data both to and from the U.S. Global investors can expect continued transitional guidance from the U.S., in addition to FATCA-like legislation in their home jurisdictions.

As a side note, there is a push by many in the US Congress (the national legislative branch of government) to remove FATCA as a law due to its extensive requirements and its potential negative impact on global investment.

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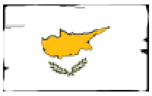
The benefits of setting up a Cyprus International Trust

by Aspen Trust Group



The use of a Trust as a vehicle for international tax planning and business structuring is becoming increasingly popular. In 2012 the law governing the Cyprus International Trust (CIT) was modernised with the aim of providing incentives for the establishment and administration of trusts in Cyprus by non-residents, creating one of the most attractive trusts legal frameworks in the world. Cypriot Trusts can be very effective vehicles for channelling income to and from companies in different jurisdictions.:

If its terms so provide, the law applicable to an International Trust can be changed to a foreign law, provided that the new law recognises the validity of the Trust and the respective interests of the beneficiaries (a Trust established in a foreign jurisdiction may, by its terms, select Cypriot law, provided that the foreign law itself recognises such a change). No law, Cypriot or foreign, relating to inheritance or succession affects any transfer or disposition in favour of the Trust in any way, nor may it affect its validity.

The same person can be the settlor, the Trustee (through a Cyprus IBC in which he/she can be the sole director and he/she can be the only beneficial owner of the shares), and also a beneficiary (i.e. an individual could have absolute control and ownership of the Trust fund).

Types of Trusts
Depending on the circumstances of the settlors and his/her objectives, different types of Trusts can be set up in Cyprus. These include:

- Discretionary Trust
- Fixed Trust
- Fixed and Descretionary Trust
- Trading Trust
- Purpose Trust

> “all of the Trust’s funds may be invested in any investment anywhere”

Benefits of Cyprus International Trust
An international Trust may form a Cyprus international business company, partnership or branch and obtain the benefits available to them and carry out business in Cyprus subject to the laws of the country which are imposed on the beneficiaries and not on the Trust itself. It is good to note at this point that an International Trust is exempt from registration under any law. In addition, there are no reporting requirements in Cyprus for International Trusts nor are there any time limitations for its existence –an International Trust can exist in perpetuity. Moreover, an International Trust can accumulate income for its entire duration.

All or any part of the Trust’s funds may be invested in any investment anywhere, so long as the Trustee exercises the diligence and prudence that a reasonable person would be expected to exercise making the investments. Trust capital received in Cyprus by a foreigner (resident or retired in Cyprus) from Trusts not resident in Cyprus is not taxable on the Trustee and dividends, interest or royalties received by an international Trust from a Cyprus international business company are not taxable and not subject to any withholding tax. Further, an International Trust is not subject to any Capital Gains Tax in Cyprus on the disposal of assets (except immovable property in Cyprus).

Finally, general tax benefits in Cyprus also affect the Cyprus Interantional Trusts, such as:

- Income, gains and profits are exemted from income tax, capital gains tax, special contribution or any other taxes in Cyprus.
- No estate duty or inheritance tax in Cyprus.
- Dividends, interest or other income received from a Cyrus Company are not subject to any withholding tax.

Conclusion
The Cyprus International Trust, whether used to protect assets from claims, to determine inheritance shares, minimise tax burden, or for a combination of reasons, is an invaluable tool for flexible and effective estate and tax planning.

The provisions under the International Trusts Law, coupled with the advantages of the island’s strategic location, its international reputation as a financial centre, and excellent taxation and formation benefits, allows Cyprus to compare favourably to most estate planning and tax minimisation jurisdictions in the world.

Provided that sound professional advices is sought, a Trust can maximise the various benefits of prudent investors and organise their business matters in a way which best suits their particular circumstances and needs.

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