

Foreign Account Tax Compliance Act (FATCA) Impact for captive managers in Guernsey

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Introductions



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Objectives of the session

- ▶ Background to FATCA and its objectives
- ▶ Timeline for implementation and key dates
- ▶ The impact of the FATCA regulations on captive insurers
- ▶ Practical considerations

Warning – Jargon ahead

FATCA contains multitudes of acronyms and plenty of jargon – we will refer to these in this presentation but all are defined in the FATCA Glossary at the end of your pack.

A rectangular box with a thin black border containing several acronyms and terms. The text is arranged as follows:

- Top left: FFI
- Top center: PFFI
- Top right: *NPFFI*
- Middle left: W-8BEN-E
- Middle center: **W-9**
- Middle right: IGA
- Bottom left: NFFE
- Bottom center: GIIN
- Bottom right: FDAP

FATCA overview

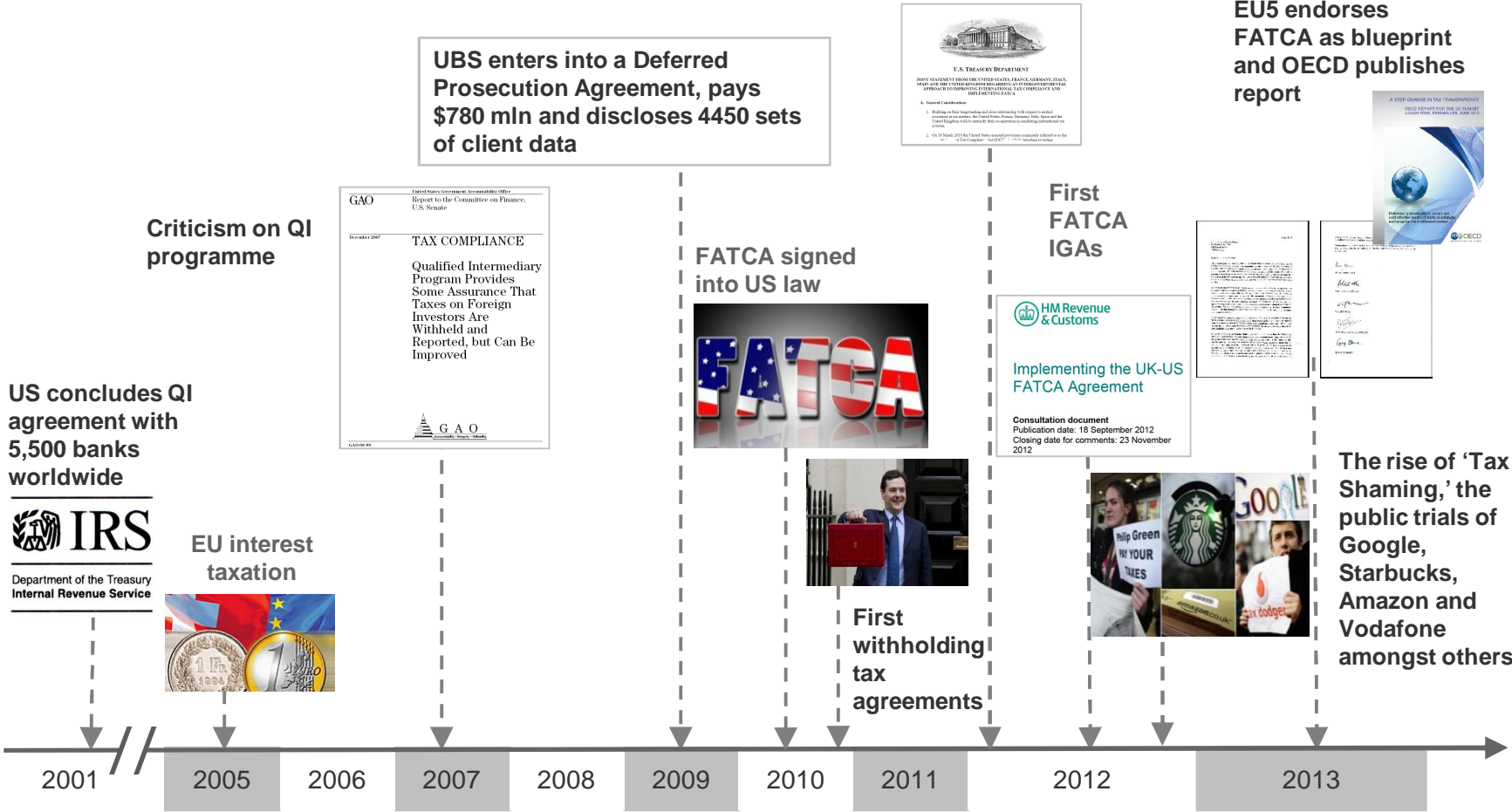
- ▶ Foreign Account Tax Compliance Act (FATCA) is US tax law designed to prevent US taxpayers from avoiding tax by investing through non-US financial institutions and investment vehicles and concealing their assets from IRS.

- ▶ FATCA introduces a 30% withholding tax on certain payments made to Non Participating Foreign Financial Institutions (NPFPI) and Non Financial Foreign Entities (NFFE) if they fail to comply.
 - ▶ Withholding applies on or after 1 July 2014.

- ▶ Participating Foreign Financial Institutions (FFIs) will report the investments of US persons (and other information) which the IRS can assess alongside the individual's tax return to calculate their correct tax liability.
 - ▶ First reports will be made on or before 31 May 2015.

- ▶ **The US wants information – the purpose is not the collection of withholding tax.**

The road to FATCA and beyond



How big is the problem?

Recent press articles confirm the US still has a problem:

The billionaire creator of Beanie Babies toys could face up to five years in prison after agreeing to admit a charge of tax evasion.

Federal prosecutors said that Ty Warner "went to great lengths" to hide more than \$3m (£1.9m) of income in a secret Swiss bank account.

Mr Warner's lawyer said his client had agreed to pay a \$53m fine.

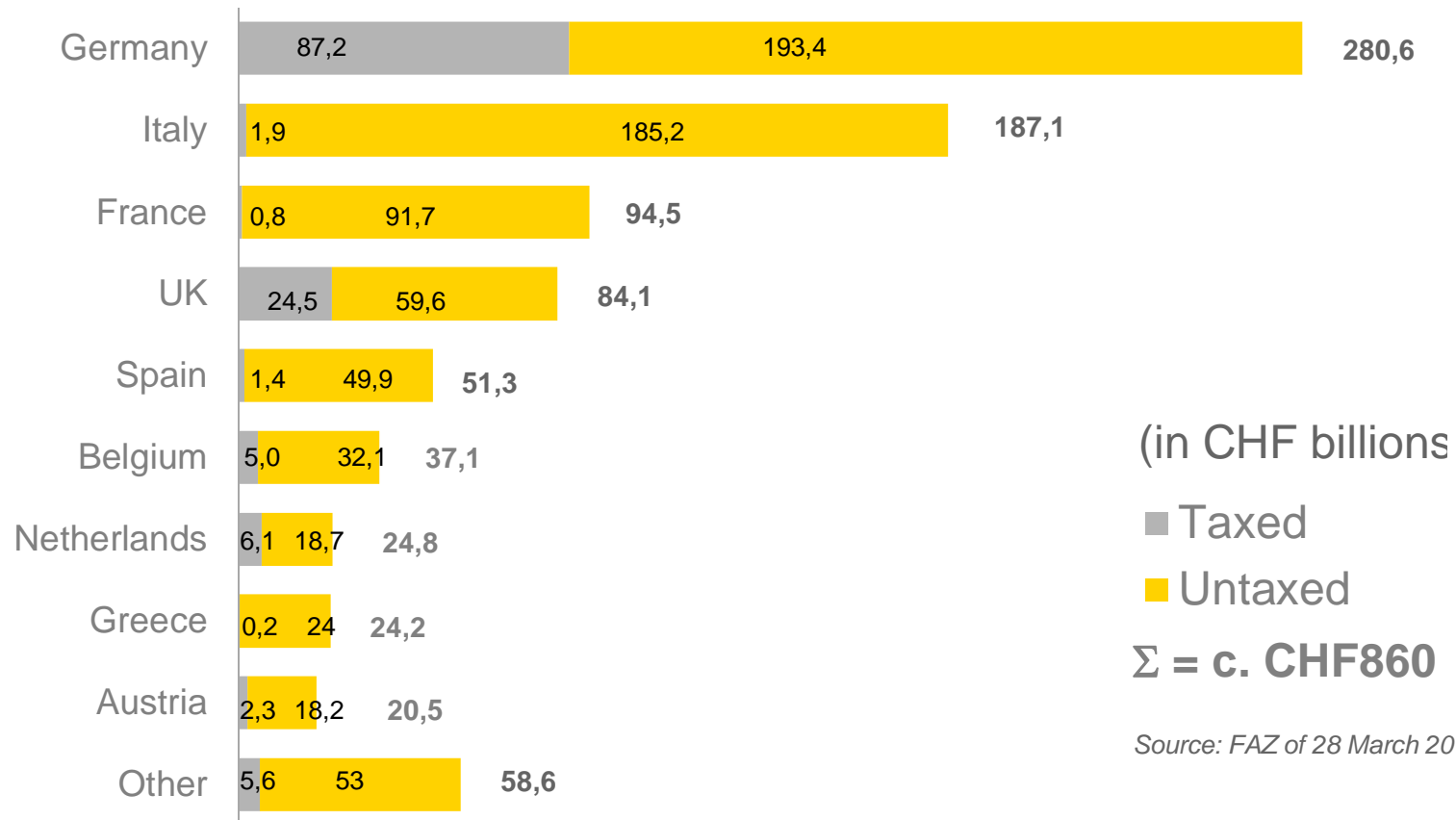


Beanie Babies were particularly popular in the 90s

Source: BBC news 19 September 2013

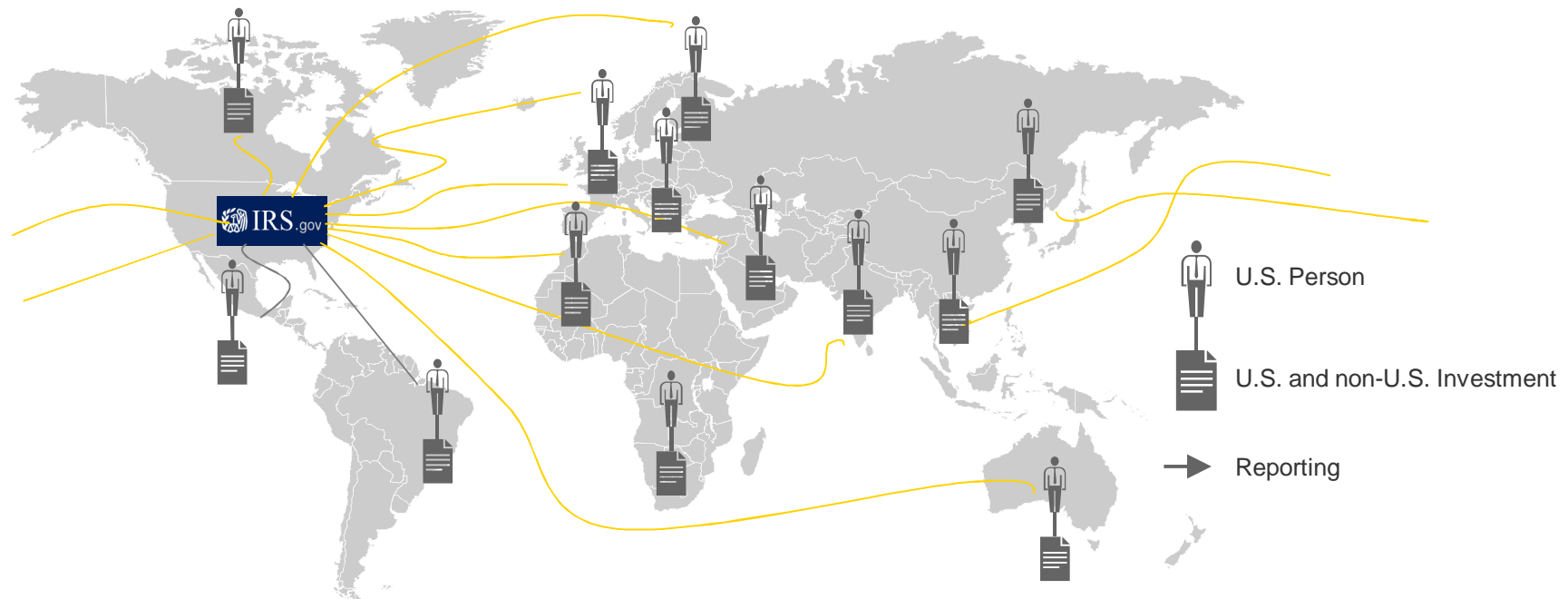
How big is the problem?

Statistics on EU monies held in Swiss bank accounts would suggest the EU has the same problem:



How the IRS will collect this information

- ▶ All revenues and proceeds from investments by a U.S. person will eventually need to be reported to the IRS under FATCA, generally irrespective of the type of holding and where it is held in the world.



Foreign Financial Institutions (FFI)

- ▶ For the purposes of FATCA, companies classified under the following definitions will be FFIs and will be required to meet FATCA FFI reporting requirements.

Depository institution	Custodial institution	Investment institution	Specified insurance institution
<p>An entity that accepts deposits in a banking or similar business where deposits are accepted in the ordinary course of its business with customers</p> <p>OR</p> <p>Is a holding company of such an institution</p>	<p>An entity that holds financial assets on the account of others for a substantial part of its business.</p> <p>Substantial is measured as 20% or greater of the entity's gross income</p> <p>OR</p> <p>Is a holding company of such an institution</p>	<p>An entity:</p> <ul style="list-style-type: none"> ▶ Investing, administering or managing funds or money on behalf of other persons ▶ Trading in money market instruments ▶ Conducting FX trades ▶ Trading in interest rate/index instruments ▶ Trading in transferrable securities and commodity futures <p>OR</p> <p>Is a holding company of such an institution</p>	<p>An insurance company that issues or is obliged to make payments with respect to a cash value insurance or annuity contract</p> <p>OR</p> <p>Is a holding company of such an institution</p>

- ▶ We expect many offshore insurance groups not to be FFIs, unless they have activities such as Life insurance, employee benefits or wealth management elsewhere in their group.

The FFI Agreement IRS registration process

- ▶ The online FATCA registration portal for Financial Institutions opened on 19 August 2013. The diagram below illustrates the registration process:

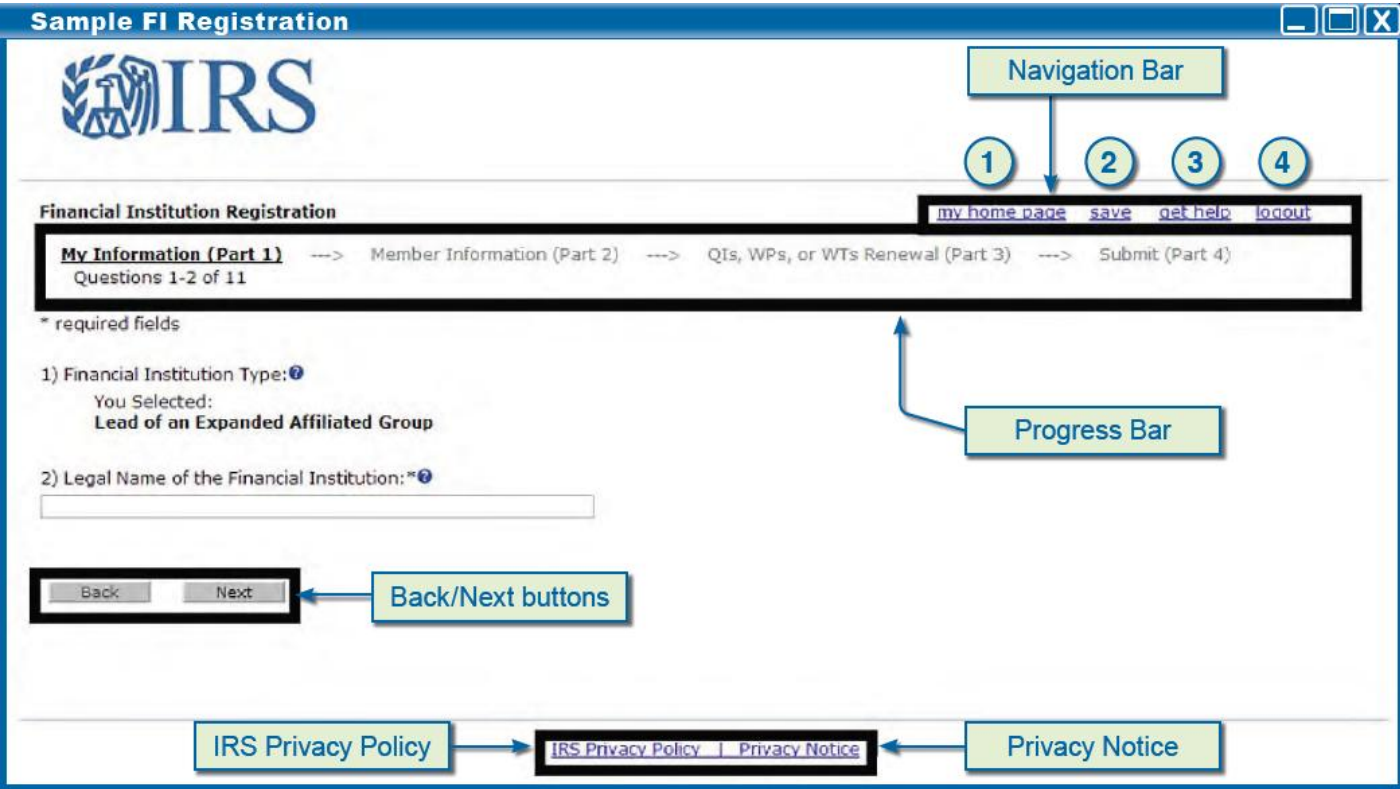


(Source: IRS: Foreign Account Tax Compliance Act (FATCA) user guide)

The FFI Agreement

The FATCA portal

- ▶ The registration process is expected to take 20 – 30 minutes per entity.
- ▶ Groups must register their lead FFI, Responsible Officer, Point of Contacts and all Foreign Financial Institutions with the correct classification.



(Source: IRS: Foreign Account Tax Compliance Act (FATCA) user guide)

The Global Intermediary Identification Number (GIIN) Identifying FFIs as FATCA compliant

- GIIN**
- The GIIN will be a unique alpha-numeric sequence providing the following :
 - Identifies a financial institution as FATCA compliant to potential U.S. withholding agents.
 - Allows for identification of a financial institution’s FATCA type, category, and country.
 - Associates each entity with other affiliates/branches in the same affiliated group.
 - Allows for identification of an entity on the IRS FFI List.

39AEF1.00000.FI.724

FI FATCA ID	FI Type	Category Code	Country
<i>This field contains the FATCA ID, which will be a randomly generated alphanumeric sequence</i>	<i>This field indicates the type of institution (Lead, Member, or Single) and allows for a sequencing of members under a lead</i>	<i>This field indicates the financial institution or branch category type</i>	<i>This field contains the ISO numeric country code for the location of the financial institution</i>

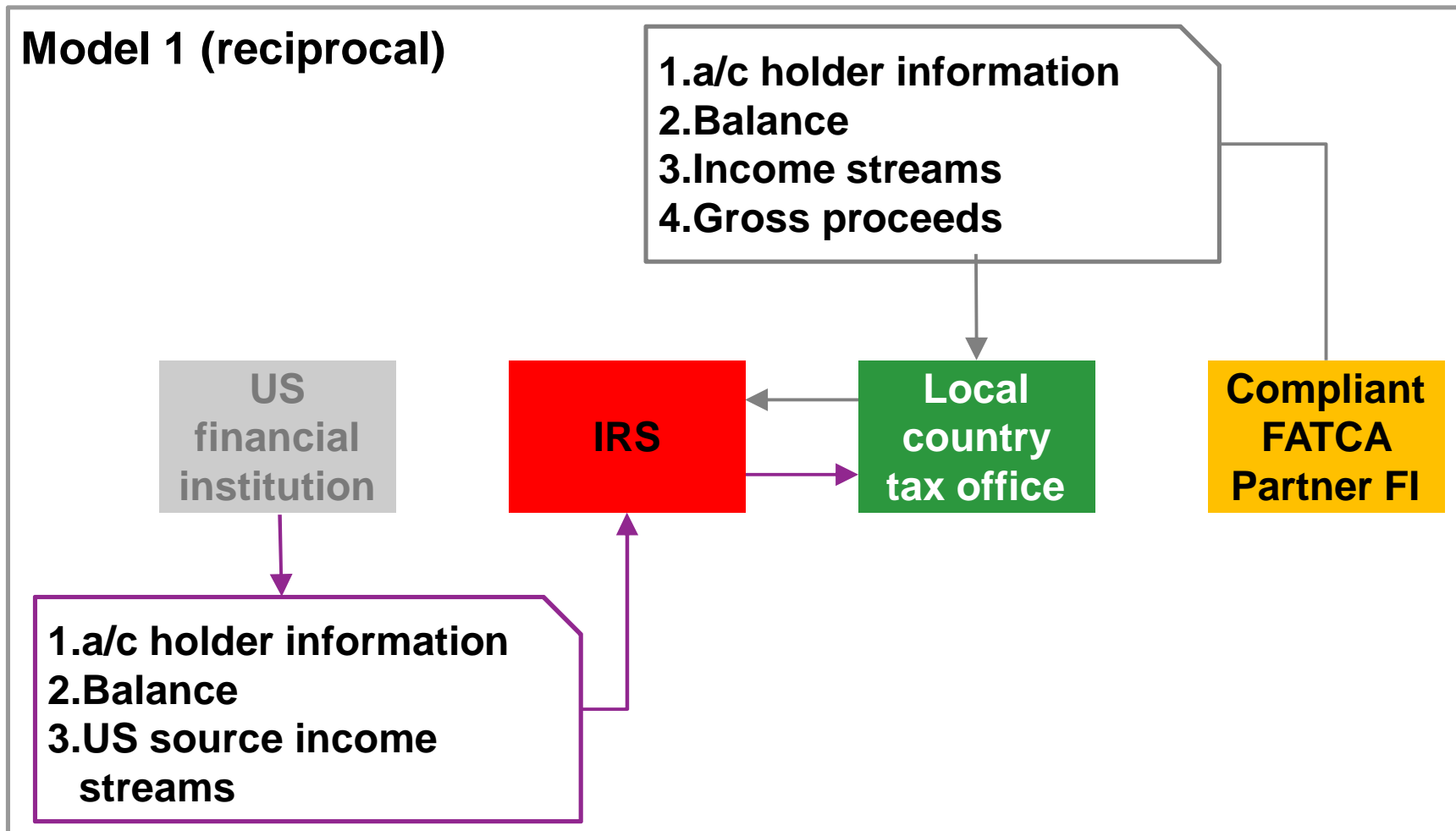
(Source: IRS)

Inter-Governmental Agreements (IGAs)

- ▶ Bipartite agreement between the US and a host country.
- ▶ Facilitates the transmission of information for the benefit of the FFI and the IRS.
- ▶ The FFI receives a more straightforward route to compliance (Model I).
- ▶ The IRS receives information without data protection issues causing legal restrictions to compliance.

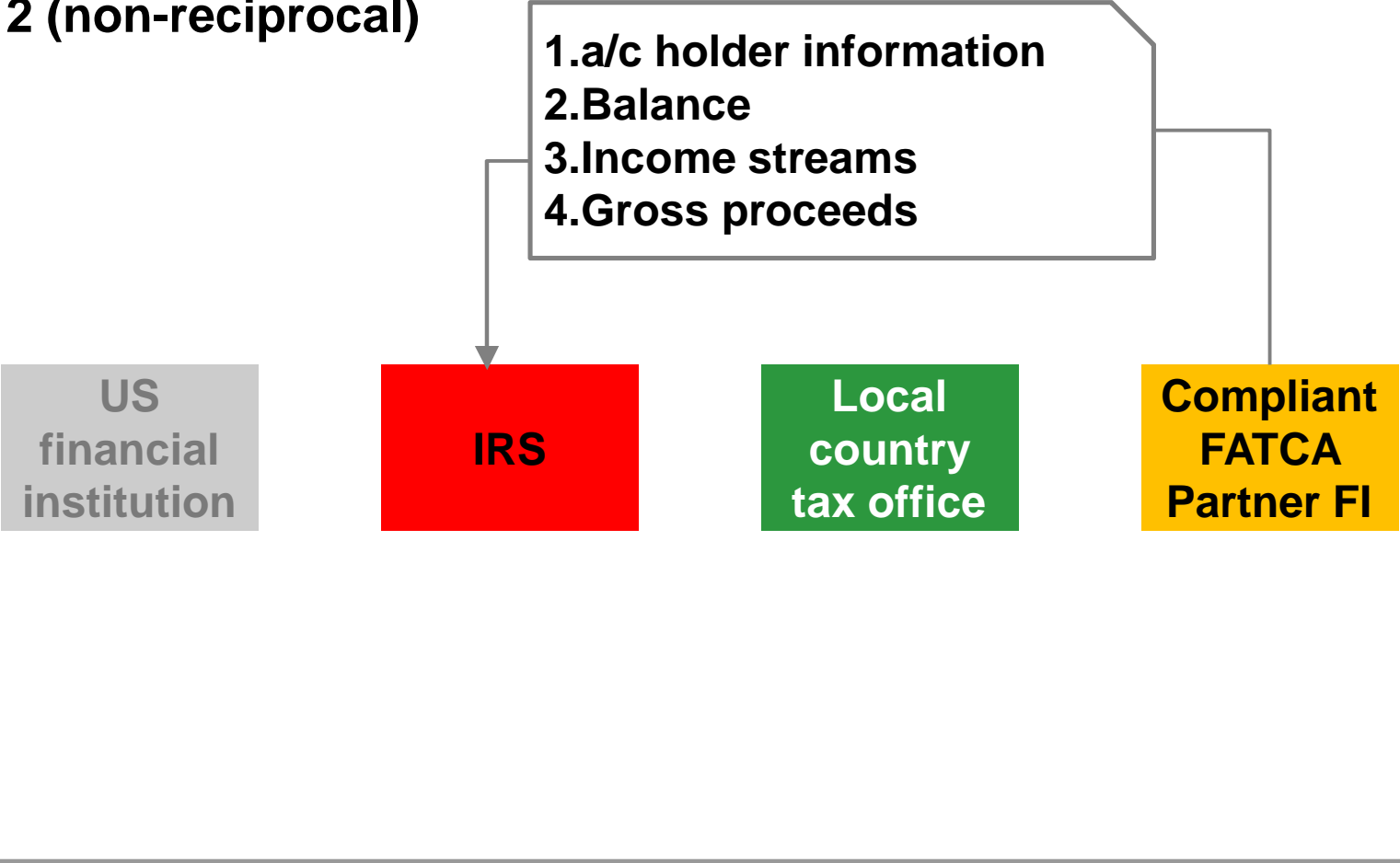
IGA – The two models

Guernsey is widely expected to sign a Model 1 IGA before 31 December 2013 which permits information to be provided to local tax authority.



IGA – The two models

Model 2 (non-reciprocal)

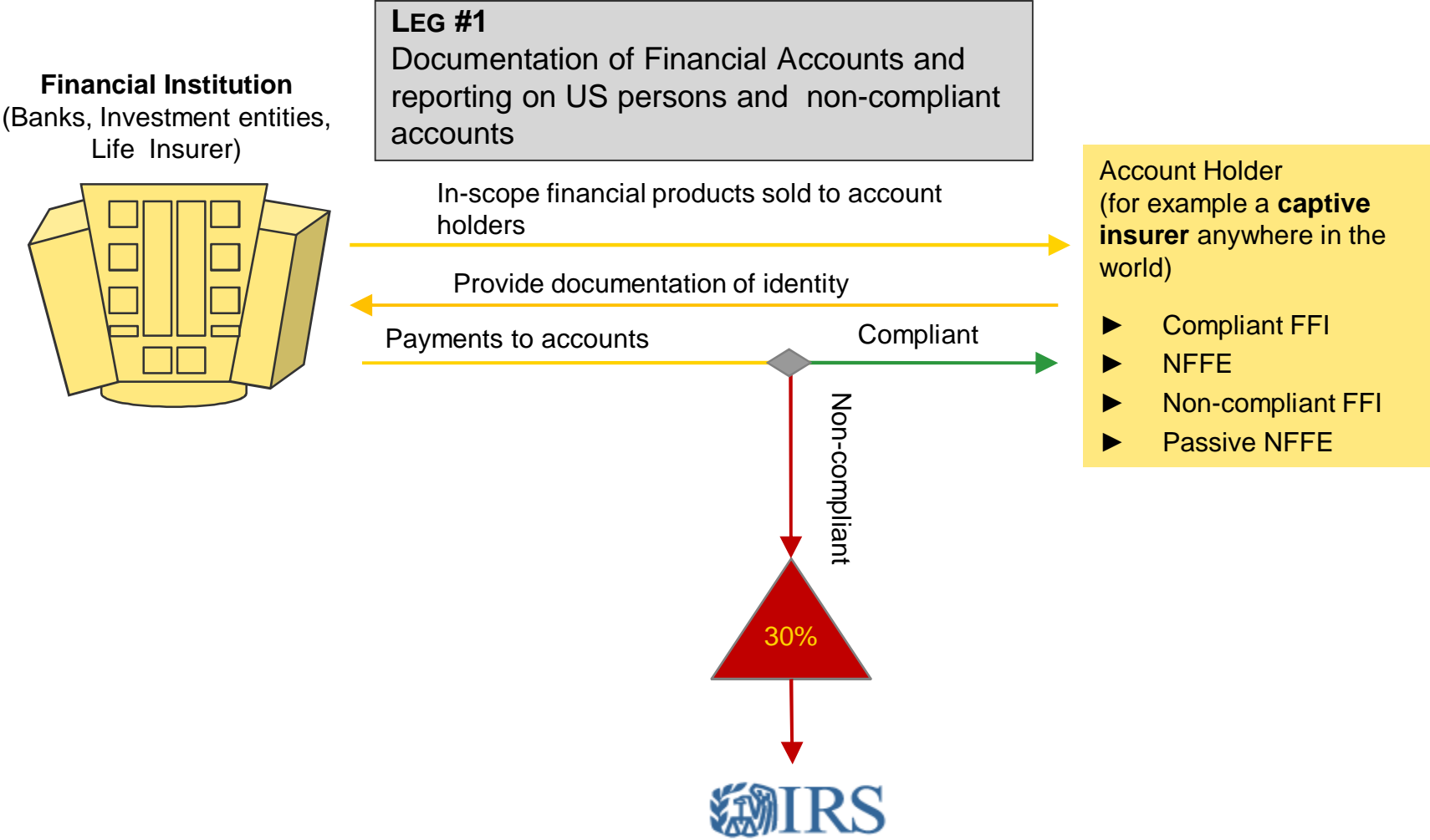


The impact of the FATCA regulations on captive insurers

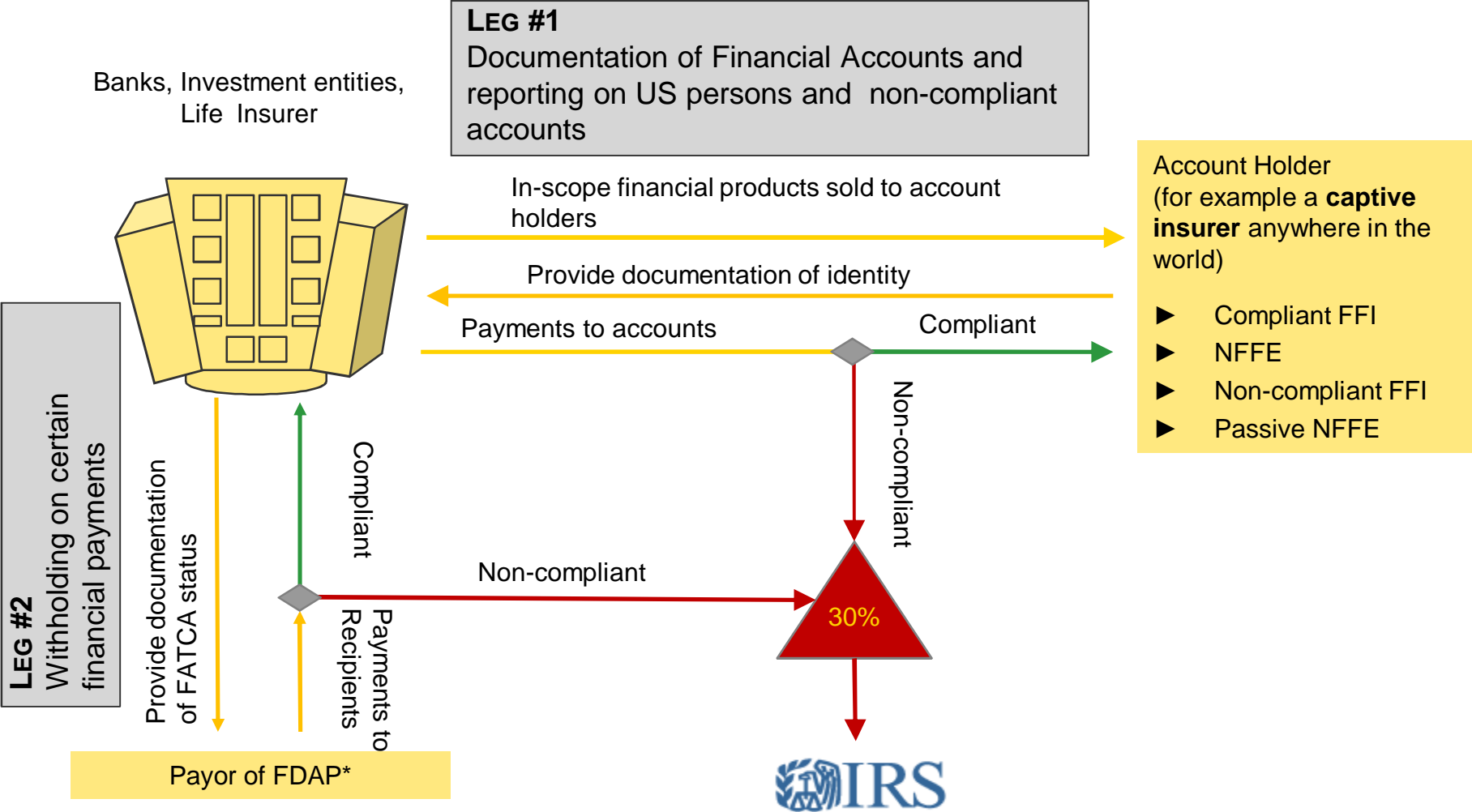


The two legs of FATCA

Leg#1 – The “due diligence” leg



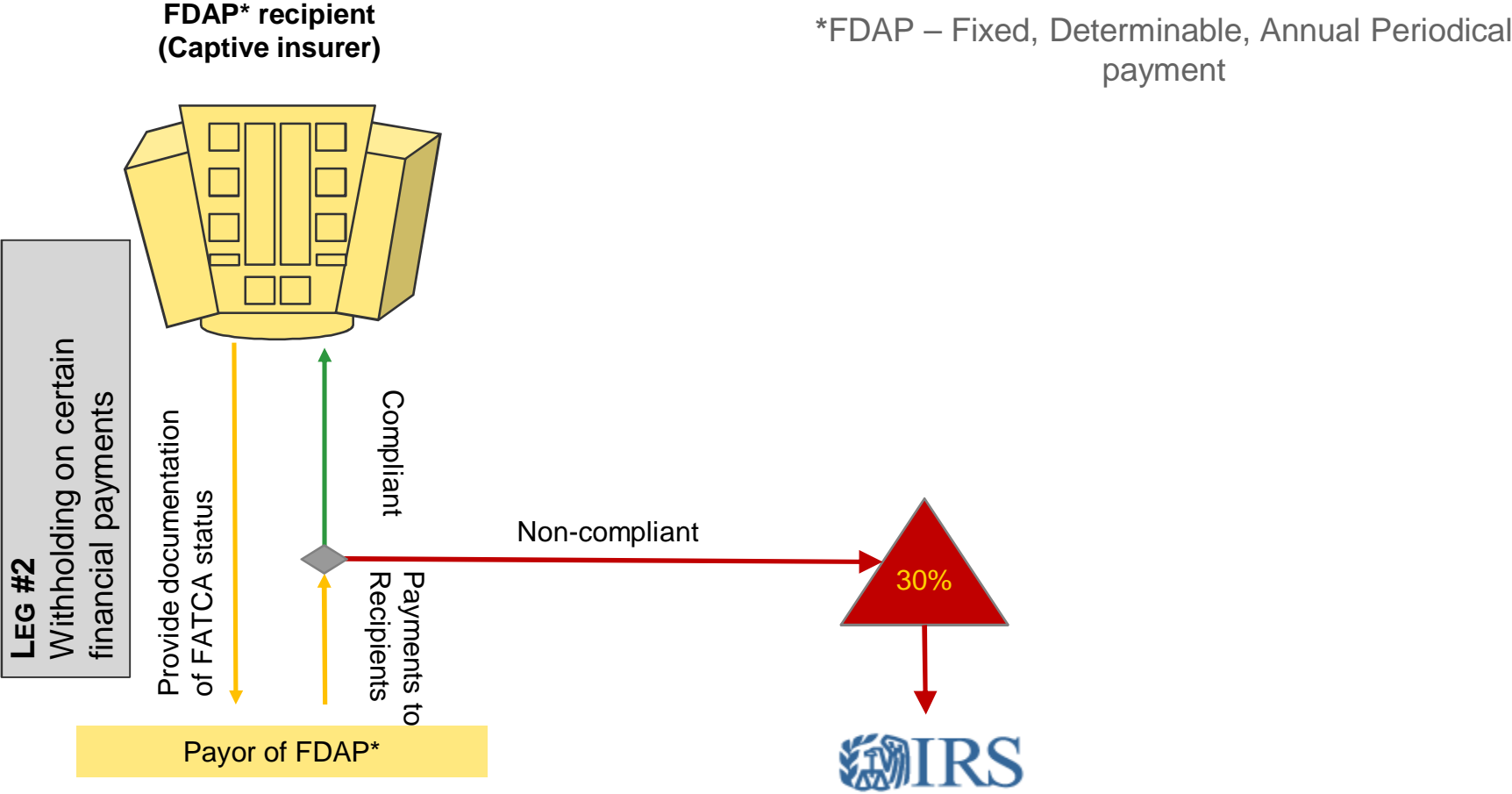
The two legs of FATCA



* FDAP – Fixed, Determinable, Annual Periodical

The two legs of FATCA

Leg#2 – The “FDAP” leg



FDAP and insurance premiums

Fixed, Determinable, Annual Periodical (FDAP) income includes:

- ▶ Insurance and reinsurance premium in respect of US source risk.
- ▶ Payable in respect of an offshore obligation entered into on or after 1 July 2014.

Fixed, Determinable, Annual Periodical income (FDAP)

Insurance premium in respect of US source risk

- ▶ 1473-1(a)(2) of the FATCA regulations defines US source as *“income treated as derived from sources within the United States under sections 861 through 865 ...”*

- ▶ 861 states:
“Amounts received as underwriting income (as defined in section 832(b)(3)) derived from the issuing (or reinsuring) of any insurance or annuity contract:
 - (A) in connection with property in, liability arising out of an activity in, or in connection with the lives or health of residents of, the United States,”

Fixed, Determinable, Annual Periodical income (FDAP)

Payable in respect of an offshore obligation entered on or after 1 July 2014

- ▶ The term offshore obligation means any contract that is maintained and executed at any location outside of the United States.

- ▶ There are grandfathering rules for policies that are put in place before 1 July 2014.

- ▶ Withholding should not be applied to annual policies for calendar year 2014 unless:
 - ▶ the terms of the contract are not certain or there are material elements of coverage that remain to be agreed on or after 1 July 2014; or
 - ▶ there is a material modification to an existing obligation on or after 1 July 2014.

The timing of withholding on FDAP

FATCA withholding

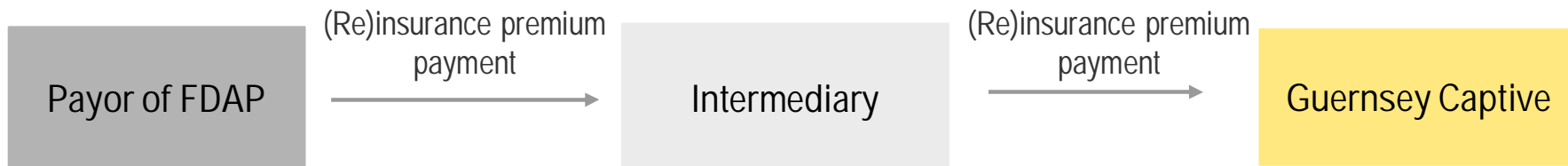
- ▶ Payers of FDAP to non-compliant entities will be required to withhold 30%.
- ▶ However the timing of when withholding obligations arise depends on whether the payment is made via an intermediary.
- ▶ Direct FDAP payments for offshore obligations are not subject to withholding until 1 January 2017.



The timing of withholding on FDAP

FATCA withholding

- ▶ However FDAP payments for offshore obligations payable via an intermediary are withholdable payments effective 1 July 2014.



Recap captive insurers impact

Captive insurers are specifically impacted by FATCA, as follows:

- ▶ From 1 July 2014, FATCA will impact insurance premiums payable for US source risk which are paid to an offshore insurance company via an intermediary such as an insurance broker.
- ▶ These premium payments will be treated as a withholdable FDAP payments.
- ▶ US source risk includes domestic US P&C risk and risk related to US citizens.

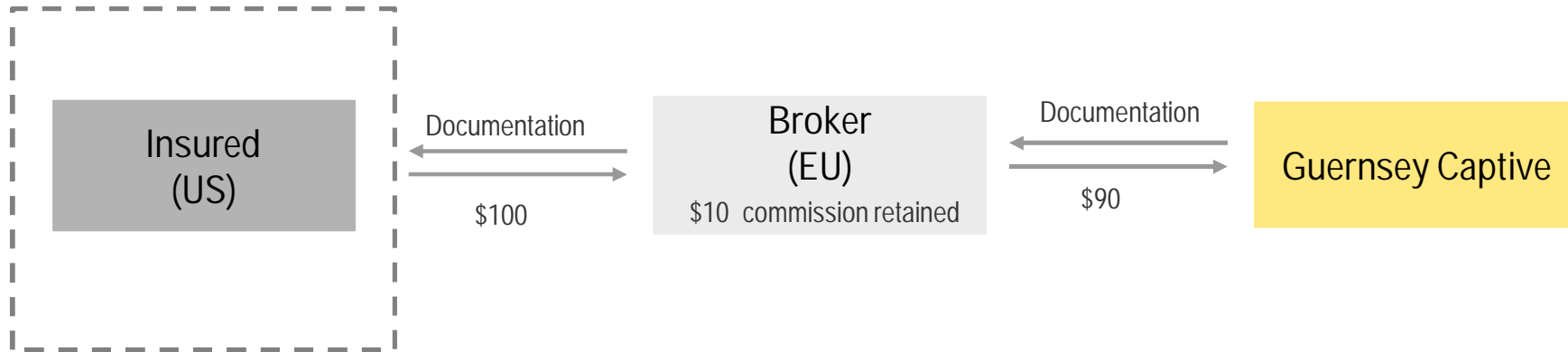
Example impact of FATCA



Background

- ▶ Insured pays \$100 premium payment to Broker. Broker pays \$90 to Guernsey Insurance Captive, retaining \$10 commission.
- ▶ Generally, Insured is aware that a portion of the premium paid constitutes commission retained by the Broker.
- ▶ From a documentation standpoint, the broker serves as intermediary.

Example impact of FATCA



A) Insured Party - Documentation and Reporting Obligations

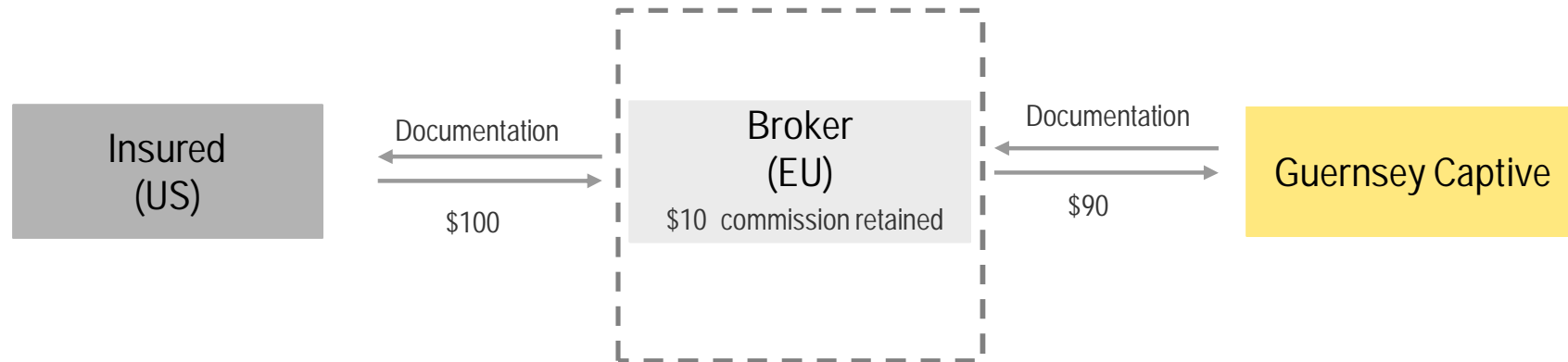
Documentation to be provided

- ▶ N/A.

Reporting Requirement

- ▶ Form 1042-S to Guernsey Captive as beneficial owner of premium payment
- ▶ Copy of Form 1042-S sent to Broker in its capacity as intermediary.
- ▶ Form 1042-S to Broker in its capacity as beneficial owner for the commission.

Example impact of FATCA



B) Broker - Documentation and Reporting Obligations

Documentation to be provided from Broker to Insured

- ▶ Form W-8IMY to Insured. The following are attached:
 - ▶ Broker: W-8BEN-E or other documentation sufficient to establish FATCA status for portion of premium that constitutes commission.
 - ▶ Guernsey Captive: W-8BEN-E or other documentation sufficient to establish FATCA status for the remainder of the premium.
 - ▶ Withholding statement allocating \$10 to Broker for commission, and \$90 to Captive.

Reporting Requirement

- ▶ None.

Example impact of FATCA



C) Guernsey Captive - Documentation and Reporting Obligations

Documentation to be provided from Guernsey Captive to Broker

- ▶ Form W-8BEN-E to Broker.

Reporting Requirement

- ▶ None.

Additional scenarios to consider

- ▶ US broker in place of non US broker
- ▶ Captive as a US corporation instead of non US corporation
- ▶ Insured is non US
- ▶ Onward reinsurance by the Guernsey Captive

Practical considerations



Practical considerations for FATCA compliance

- ▶ Captives and their managers should consider the following:
 - ▶ Analyse each captive's FATCA status and complete Form W-8BEN-E;
 - ▶ Review third party agreements to determine where FDAP is paid via an intermediary and will be subject to accelerated withholding;
 - ▶ Educate the necessary employees and captive owners on the impact of FATCA; and
 - ▶ Embed a process to ensure that a W-series Form is provided or requested whenever required.

Self certifying the captive as FATCA compliant using Form W-8BEN-E

Chapter 4 Status (FATCA status) (Must check one box only unless otherwise indicated). (See instructions for details and complete the certification below for the entity's applicable status.)

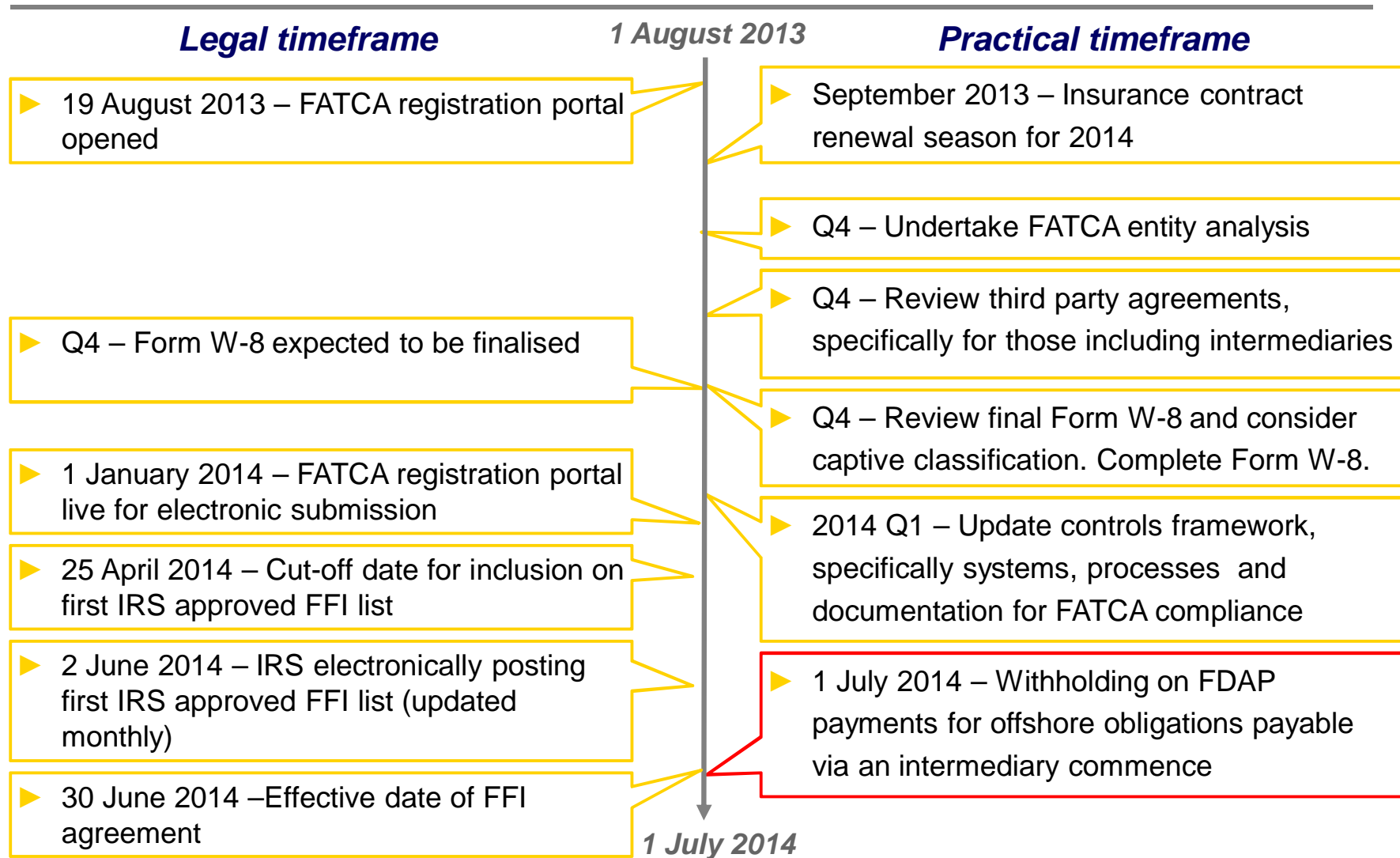
- | | |
|---|---|
| <input type="checkbox"/> Nonparticipating FFI (including a limited FFI or limited branch). | <input type="checkbox"/> International organization. Complete Part XIII. |
| <input type="checkbox"/> Participating FFI. | <input type="checkbox"/> Exempt retirement funds. Complete Part XIV. |
| <input type="checkbox"/> Reporting Model 1 FFI. | <input type="checkbox"/> Entity wholly owned by exempt beneficial owners. Complete Part XV. |
| <input type="checkbox"/> Participating FFI in a Model 2 IGA jurisdiction. | <input type="checkbox"/> Territory financial institution. Complete Part XVI. |
| <input type="checkbox"/> Registered deemed-compliant FFI (other). | <input type="checkbox"/> Excepted nonfinancial group entity. Complete Part XVII. |
| <input type="checkbox"/> Sponsored FFI that has not obtained a GIIN (only for payments made prior to January 1, 2016). Complete Part IV. | <input type="checkbox"/> Excepted nonfinancial start-up company. Complete Part XVIII. |
| <input type="checkbox"/> Certified deemed-compliant nonregistering local bank. Complete Part V. | <input type="checkbox"/> Excepted nonfinancial entity in liquidation or bankruptcy. Complete Part XIX. |
| <input type="checkbox"/> Certified deemed-compliant FFI with only low-value accounts. Complete Part VI. | <input type="checkbox"/> 501(c) organization. Complete Part XX. |
| <input type="checkbox"/> Certified deemed-compliant sponsored, closely held investment vehicle. Complete Part VII. | <input type="checkbox"/> Nonprofit organization. Complete Part XXI. |
| <input type="checkbox"/> Certified deemed-compliant limited life debt investment company (only for payments made prior to January 1, 2017). Complete Part VIII. | <input type="checkbox"/> NFFE that is publicly traded or affiliate of a publicly traded NFFE. Complete Part XXII. |
| <input type="checkbox"/> Owner-documented FFI. Complete Part IX. | <input type="checkbox"/> Excepted territory NFFE. Complete Part XXIII. |
| <input type="checkbox"/> Restricted distributor. Complete Part X. | <input type="checkbox"/> Active NFFE. Complete Part XXIV. |
| <input type="checkbox"/> Nonreporting IGA FFI. Complete Part XI. | <input type="checkbox"/> Passive NFFE. Complete Part XXV. |
| <input type="checkbox"/> Foreign government, Government of a U.S. possession, or foreign central bank of issue. Complete Part XII. | <input type="checkbox"/> Not receiving withholdable/passthru payment.
Must enter code: <input type="text"/> |

(N.B. This is an extract of the draft Form W-8BEN-E. *Source: www.irs.gov/pub/irs-dft/fw8bene--dft.pdf*)

Future expectations

- ▶ Brokers will be setting out their documentation requirements over the next few months
- ▶ Publication of FATCA forms including the all important W-8BEN-E and instructions
- ▶ A small set of changes to the main US regulations expected to be published
- ▶ More IGAs to be signed by end of 2013
- ▶ Those with FFIs within their groups under US FATCA will also need to be ready for CDOT exchange of information agreements from 1 July 2014
- ▶ Further delay?

FATCA timeline up to 1 July 2014



Further reading

- ▶ [http://www.irs.gov/Businesses/Corporations/Foreign-Account-Tax-Compliance-Act-\(FATCA\)](http://www.irs.gov/Businesses/Corporations/Foreign-Account-Tax-Compliance-Act-(FATCA))
- ▶ www.ey.com/FATCA
- ▶ <http://www.giia.gg/>

Questions



Glossary

Abbreviation	Term
AML	Anti Money Laundering
EAG	Expanded Affiliated Group
EIN	Employer Identification Number
FATCA	Foreign Accounting Tax Compliance Act
FI	Financial Institution
FFI	Foreign Financial Institution
GIIN	Global Intermediary Identification Number
IGA	Intergovernmental Agreement
IRS	Internal Revenue Service (the US federal tax authority)
KYC	Know Your Customer
NFFE	Non Financial Foreign Entities
PFFI	Participating Foreign Financial Institution
NPFFI	Non Participating Foreign Financial Institution
TCF	Treating Customers Fairly
TIN	Tax Identifying Number
USWA	US Withholding Agent

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