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Cayman Islands Government Announces FATCA Intergovernmental Agreement

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The Cayman Islands government announced on August 13, 2013 that it has concluded negotiations with the US government on a “Model 1” intergovernmental agreement (“IGA”) with respect to the US Foreign Account Tax Compliance Act (“FATCA”) and a new tax information exchange agreement (“TIEA”). Both countries have initialed the agreements and stated that the official signing will be held as soon as possible. Like the IGAs the US government has signed with other foreign governments, the Cayman Islands IGA is intended to streamline FATCA information reporting and reduce compliance burdens for Cayman Islands financial institutions.

Background

FATCA (contained in Sections 1471 through 1474 of the Internal Revenue Code) was enacted 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”). FATCA generally requires a foreign payee that is a foreign financial institution (an “FFI”) either (1) to enter into an agreement with the IRS relating to such reporting (an “FFI Agreement”, and such an FFI, a “Participating FFI”) or (2) to comply with local laws that implement an IGA. If an FFI does not satisfy these requirements (and is not otherwise exempt), withholdable payments made to such FFI will be subject to withholding under FATCA at a rate of 30%. FATCA information reporting and withholding requirements generally do not apply to FFIs that are treated as “deemed-compliant” because they present a relatively low risk of being used for tax evasion or are otherwise exempt from FATCA withholding.

Cayman Islands IGA

IGAs allow foreign governments to implement FATCA in a manner that removes legal impediments to compliance in the relevant foreign country (e.g., bank secrecy laws) and that reduces compliance burdens on FFIs. The Treasury Department has developed two alternative IGA models in collaboration with foreign governments: the Model 1 IGA and the Model 2 IGA.

The IGA with the Cayman Islands will be a Model 1 IGA. FFIs located in Model 1 IGA countries (other than those not subject to reporting) generally are required to identify US accounts pursuant to due diligence rules adopted by the IGA partner country and to report specified information to the relevant governmental authorities of the IGA partner country. This information will be automatically exchanged by the IGA partner country with the IRS, and FFIs in Model 1 IGA countries are not required to enter into FFI Agreements with the IRS. In contrast, FFIs in Model 2 IGA countries (other than those not subject to reporting) are not relieved from the requirement to enter into an FFI Agreement to avoid FATCA withholding.

Under the Cayman Islands IGA, Cayman Islands FFIs will not be required to enter into FFI Agreements with the IRS to avoid withholding under FATCA. Instead, Cayman Islands FFIs will be required to provide certain information about their US account holders to the Cayman Islands Tax Information Authority, which will share that information with the IRS. A Cayman Islands FFI that complies with Cayman Islands due diligence and reporting requirements established in accordance with the Cayman Islands IGA will be eligible to be treated as a registered deemed-compliant FFI for FATCA purposes. Once signed, the Cayman Islands IGA should streamline FATCA information reporting and reduce compliance burdens for Cayman Islands FFIs. The text of the Cayman Islands IGA and the new TIEA will be made public once the official signing occurs.

FFI Registration Process

Most Cayman Islands FFIs will still have to register with the IRS and obtain a global intermediary identification number (“GIIN”) to avoid FATCA withholding. The IRS announced on August 19, 2013 that the online registration system is now open for registration. The system is accessible at: [http://www.irs.gov/Businesses/Corporations/Foreign-Account-Tax-Compliance-Act-\(FATCA\)](http://www.irs.gov/Businesses/Corporations/Foreign-Account-Tax-Compliance-Act-(FATCA)). As registrations are finalized and approved by the IRS, registering FFIs will receive notices of registration acceptance and will be issued GIINs.

Beginning in June 2014, the IRS intends to publish a monthly electronic “IRS FFI List” of Participating FFIs and registered deemed-compliant FFIs (including reporting FFIs in Model 1 IGA countries) to allow withholding agents to verify payees’ GIINs. Although the first IRS FFI List was originally scheduled to be published in December 2013, issuance of the list has been postponed until June 2014 in connection with the extension to the timeline for initial implementation of FATCA that the Treasury Department and the IRS recently announced in Notice 2013-43. As discussed in our client publication dated July 15, 2013 (available at <http://www.shearman.com/timeline-for-initial-fatca-implementation-extended-07-15-2013/>), Notice 2013-43 generally extended the timeline for initial implementation of FATCA from January 1, 2014 to July 1, 2014. Consistent with the revised timeline, an FFI generally should finalize its registration with the IRS no later than April 25, 2014 (instead of October 25, 2013) to be included in the first IRS FFI List. As a result of the Cayman Islands IGA, however, Cayman Islands FFIs will have additional time to register with the IRS and obtain GIINs as compared to FFIs located in non-IGA countries. For an FFI located in an IGA country, verification of a GIIN by a withholding agent (and, accordingly, FATCA withholding) will not be required for withholdable payments made prior to January 1, 2015.

Other IGAs

The US government has signed Model 1 IGAs with Denmark, Germany, Ireland, Mexico, Norway, Spain and the United Kingdom, and has signed Model 2 IGAs with Japan and Switzerland. If you wish to receive information on another IGA or aspect of FATCA, you may contact your regular Shearman & Sterling contact person or any contact person listed in this publication.

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