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HOW WILL FATCA AFFECT YOUR TRUST?

Portia J. Nicholson

Now that The Bahamas is treated as having a FATCA Model 1 (non-reciprocal) Intergovernmental Agreement (IGA) in effect, you may be wondering how this will affect your trust. The legal treatment of trusts under FATCA may be quite different than they would normally receive. A trust formed under Bahamian law is not a legal entity. Nor would it be considered a financial institution. It is an arrangement whereby one person, a trustee, holds assets for the benefit of another. And a settlor who is not a beneficiary would have divested his interest in the assets of the trust. But when considering FATCA rules, leave your preconceptions at the door.

The purpose of FATCA is to enable the United States (US) Internal Revenue Service (IRS) to increase tax compliance by identifying US Persons who hold financial accounts outside of the US. To accomplish this goal, FATCA requires all foreign financial institutions (FFIs) to register with the IRS and obtain a Global Intermediary Identification Number (GIIN). Each financial institution also has the responsibility of carrying out the due diligence procedures set forth in Annex 1 to the IGA in order to identify accounts held, or being opened, by US Persons. Under a Model 1 IGA, these accounts are known as US Reportable Accounts and must be reported by the FFI to the Competent Authority (in the case of The Bahamas, the Ministry of Finance), which must arrange for automatic transmission of the information to the IRS.

Under the IGA, a trust is an entity and will be treated as a US Person if (i) a US court would have jurisdiction to render orders or judgments concerning substantially all issues regarding its administration, and (ii) a US citizen or permanent resident or US corporation has authority to control its decisions. A trust not conforming to that description is a foreign trust, and its treatment under the IGA will depend on whether it falls within the definition of an FFI or a Non-financial Foreign Entity (NFFE).

A non-US trust will be classified as an FFI if it is an Investment Entity or if, as a substantial part of its business (twenty percent or more of its average gross income over a three year period or during its existence, if shorter) it holds financial assets for the account of others. A trust used as collective investment vehicles will undoubtedly be categorised as an FFI. But other trusts may also be caught given the broad definition contained in the IGA. Since Bahamian law trusts actually do not hold assets of any kind, the assets being held instead by trustees, nor do they conduct business, since they do not have legal capacity, these definitions give rise to conceptual problems, which are likely

to be resolved by treating the assets and activities of the trustee as those of the trust.

If the trust is considered an FFI, any debt or equity interest in the trust (other than interests that are regularly traded on an established securities market) will be a financial account and may therefore be subject to reporting and withholding under FATCA. An equity interest is considered to be held by the settlor, the beneficiaries and any other natural person exercising ultimate effective control over the trust, which may include a protector.

"...all trust stakeholders must ensure that they understand where they fall within FATCA, the obligations it imposes on them and what they need to do in order to comply."

A trust that is an FFI must either register on the IRS portal and obtain a GIIN or be registered by a Lead FFI as a member of an Expanded Affiliated Group or by a Sponsoring FFI as a Sponsored FFI unless, in the case of a Bahamian law trust, its trustee is a Reporting USFI or FFI and reports all information required under the IGA with respect to the reportable accounts of the trust.

Trusts that are not FFIs are not required to register for a GIIN. However, if the trust is an NFFE and one or more of its Controlling Persons (the settlor, trustees, protector, beneficiaries and other natural persons exercising ultimate effective control over the trust) are Specified US Persons, its accounts must be reported to the Competent Authority for further automatic disclosure to the IRS. A trust that has no US Controlling Persons should take all steps necessary to ensure that it is in a position to self-certify its status. This may be done by completion and presentation of appropriate US Treasury Forms in the W-8 series and by other evidence (such as a non-US passport and certificate of loss of US nationality). If the trust has Controlling Persons who are US Persons, the trustees should obtain their Taxpayer Identification Number and have them complete the appropriate W-9 or other Treasury Form evidencing their tax compliance.

Ultimately, trusts categorised as FFIs and other trusts holding financial accounts may become subject to 30% withholding on their "withholdable payments" if they fail to comply with FATCA regulations. This means that 30% can be deducted from their US-source fixed or determinable annual or periodic income (FDAP) and from the gross proceeds of any sale or other disposition of the type of property that can produce US-source FDAP. It is therefore essential that trustees and other parties to a trust take steps to determine their FATCA categorisation and the implications that may arise therefrom.

The treatment of trusts under FATCA gives rise to several conceptual difficulties and questions but this much is clear: all trust stakeholders must ensure that they understand where they fall within it, the obligations it imposes on them and what they need to do in order to comply. While there is widespread resentment of FATCA as an unwarranted imposition on persons who have no US tax liability, prudence dictates that trustees and others follow the advice of former Speaker of the US House of Representatives, Nancy Pelosi, who said, "Organize, don't agonize".

Portia J. Nicholson is a Partner in the Ocean Centre office and is a member of a number of practice groups including:- Commercial Transactions, Litigation, Real Estate & Development, Financial Services and Intellectual Property.

THE FACTS ON THE ENACTMENT OF FATCA

Tom Mylott

On 1 July, 2014 the much anticipated Foreign Account Tax Compliance Act (FATCA) will begin to have a practical impact as withholding will begin to be imposed on certain income payments to non-participating Foreign Financial Institutions (FFIs) and account holders who do not provide the required information.

On 2 July, 2014 the United States (US) Internal Revenue Service (IRS) is expected to publish its first FFI List, which will contain the names of all the institutions which will not be subject to withholding due to them registering through the FATCA website before the 5 May, 2014 deadline. So, for those institutions that have not yet registered, is it all too late?

"Financial Institutions within Cayman and The Bahamas now turning their minds to the FATCA application process will also need to consider under which of the four categories they will be required to register..."

Fortunately, further guidance has been published which extends the deadline for registration until 31 December, 2014 for FFIs within jurisdictions which have signed an Intergovernmental Agreement (IGA) with the US. Up until that point, these FFIs can self certify their status and enjoy temporary immunity from withholding.

Once the registration application has been processed and completed, the FFI will receive a global intermediary identification number (GIIN) which essentially gives withholding agents confirmation that withholding should not be imposed on the FFI. As of 1 January, 2015 FFIs in jurisdictions which have signed an IGA will need to provide their GIIN as evidence of compliance so as to avoid withholding being imposed.

There is still some uncertainty concerning the role of the "Responsible Officer", who is the person appointed by the financial institution to run its FATCA compliance programme. Recent guidance by the Cayman Islands Ministry of Finance (Ministry of Finance) indicated that the Responsible Officer will function principally as the point of contact with the Tax Information Authority of the Cayman Islands (TIA), the body to which all FFIs within the Cayman Islands (Cayman) will need to submit information on account holders.

It is clear from the registration process with the IRS that the name of the Responsible Officer is to be given to the IRS when registering, leaving open the question whether the Responsible Officer will be subject to direct scrutiny by the IRS. Again the Ministry of Finance has given a helpful indication that the role of the Responsible Officer will not be imported into the Cayman legislation and we await confirmation of this when the draft legislation is released.

Financial Institutions within Cayman and The Bahamas now turning their minds to the FATCA application process will also need to consider under which of the four categories they will be required to register, whether this be Single, Lead, Member or Sponsoring Entity, all of which we will now consider below:

A Single FFI is an FFI that does not have any Member FFIs. A Single FFI may also include a foreign branch of a United States Financial Institution (USFI) treated as a Reporting FFI under a Model 1 IGA or that has in effect a Qualified Intermediary Agreement.

A Lead FFI is an FFI that will initiate the FATCA registration process for each of its Member FFIs and is authorized to carry out most aspects of its Members' FATCA registrations. A Lead FFI is not, however, required to act as a Lead FFI for all Member FFIs within an Expanded Affiliated Group (EAG). Thus, an EAG may include more than one Lead FFI that will carry out FATCA registration for a group of its Member FFIs.

"As can be seen by these definitions, compliance with FATCA is fairly technical and requires significant planning within financial institutions to ensure that the necessary steps have been taken."

A Member FFI is an FFI that is registering as a member of an EAG that is not acting as a Lead FFI. A Member FFI will need to obtain its FATCA Identification (FATCA ID) from its Lead FFI. The FATCA ID is used to identify the member FFI for purposes of registration but it should be noted that the FATCA ID is not the same number as the GIIN. A GIIN is issued to FFIs after the FATCA registration is submitted and approved.

A Sponsoring Entity will perform the due diligence, withholding, and reporting obligations of one or more sponsored investment entities or controlled foreign institutions (Sponsored Entities). An FFI that will also act as a Sponsoring Entity for one or more Sponsored Entities is required to submit a second registration to act as a Sponsoring Entity. The Sponsoring Entity will receive a separate Sponsoring Entity GIIN and should only use that GIIN when it is fulfilling its obligations as a Sponsoring Entity.

As can be seen by these definitions, compliance with FATCA is fairly technical and requires significant planning within financial institutions to ensure that the necessary steps have been taken. Most recently, the TIA issued draft guidance notes on both the US and United Kingdom IGAs. The guidance provides a useful comparison of the rules imposed under each. Among other matters, the guidance notes confirm that Cayman FFIs will be able to apply definitions from the US regulations in place of the IGA definitions and addresses some common entity classification concerns for captive insurance companies and insurance managers. Also, it is made clear that reporting Cayman FFIs with no US Reportable Accounts are required under the Regulations to report that fact to the TIA. Industry comments and feedback were invited until June 6, 2014 but the guidelines provide a useful summary of what FFIs will need to do in order to be compliant as the deadline for implementation within Cayman approaches.

Tom Mylott is a Senior Associate in the Cayman Islands. He is a member of the Private Clients & Wealth Management group specialising in trusts, tax planning and wills.

PROBATE & ADMINISTRATION ACT UPDATE

Lisalette T. Gibson

The Probate and Administration of Estates Act (the Act) which came into effect on 1st June 2011 brought about some noteworthy changes to the Bahamian regime for administration of estates.

These changes will be applicable to any estate falling within the jurisdiction of the Supreme Court of The Bahamas (the Court), which arises when a deceased person was ordinarily resident in The Bahamas or where the estate of a deceased person consists of property in The Bahamas.

"The Act also addresses a situation where a minor is the sole executor who has no interest in the residuary estate of the deceased."

Among the significant changes brought about by the Act are revisions to the provisions relating to minors. Where a minor would be the only person entitled to probate, pursuant to section 13 of the Act, a grant of letters of administration with the Will annexed may be granted "for the use and benefit of the minor" until he attains the age of eighteen years, to the following persons in order of priority:

- to the parents of the minor jointly,
- to the statutory or testamentary guardian of the minor, or
- to any guardian appointed by a court of competent jurisdiction.

The Act also addresses a situation where a minor is the sole executor who has no interest in the residuary estate of the deceased. In this case unless the Court directs otherwise, administration is granted to the person entitled to the residuary estate for the use and benefit of the minor.

If a minor has been appointed co-executor to act jointly with an adult executor, the adult executor will be granted probate with power reserved to the minor executor until he attains the age of eighteen years, when he will be entitled to apply.

If, however, the adult executor renounces, refuses to accept or fails to make an effective application for a grant, the appointment may be made in accordance with section 13 of the Act as outlined above.

Where the Court is satisfied that a person entitled to a grant is by reason of mental incapacity (incapable of managing his affairs), section 15 of the Act provides that the Court may make a grant of representation for the use and benefit of that person until further representation is granted or until the Court directs otherwise. The grant will be issued to the following persons in order of priority:

- to the person authorized by the Court in accordance with any other law to apply for a grant,
- where there is no person so authorized to act, to any person entitled to the residuary estate of the deceased, or
- to such other person or persons as the Court may by order direct.

The Court will not issue a grant, however, until it is satisfied that all persons equally entitled with the incapable person have been cleared off. This means that if two other persons were equally entitled to make an application for the grant, each person would have to either renounce his right or consent to another person falling

within one of the above categories applying on behalf of the incapable person.

The Court upon application, will reseal foreign grants of representation from a court in any member state of the Commonwealth and any state in the United States as well as any other country specified by Order by the Attorney-General.

"The Act also makes provisions for small sums of money forming part of the deceased's estate to be available prior to a grant of representation."

Where a trust corporation has been appointed executor of a Will whether solely or jointly with another person, in accordance with section 38 subsection (1) of the Act, before the Court issues the grant of representation, the trust corporation must file a resolution authorizing it to serve as executor.

The Act also makes provisions for small sums of money forming part of the deceased's estate to be available prior to a grant of representation. Any authorized officer of a bank can now pay up to $2,500 from funds held to the credit of a deceased person, to any person for funeral expenses, without a grant of probate or letters of administration. However, the recipient of the funds must complete a declaration in accordance with section 8 of the Oaths Act (*Ch. 60*) and provide satisfactory proof of the death of the deceased person as well as any additional evidence required by the authorized officer of the bank.

Similarly, where an employee (other than a holder of any public office or contract officer) is entitled to funds from his employer, he can arrange prior to his death to have such funds paid to a specific person after his death by executing a document under oath specifying to whom the funds should be paid. The employer may rely on a certified copy of the employee's death certificate to disburse the funds, without a grant of probate or letters of administration being obtained. The employer will not be liable for such disbursement of funds, nor will such funds form part of the deceased employee's estate or be subject to his debts.

For small estates whose assessed value, including real and personal property, does not exceed $10,000, application for a grant of representation may be made directly to the Probate Registry, without going to Court.

Testators may deposit their Will for safekeeping with the Registrar of the Supreme Court for a fee. The Will is recorded by the Registrar and is under the control and direction of the Chief Justice. The Will can be withdrawn or substituted at any time by the testator for a fee. It is available for inspection during the lifetime of the testator or upon proof of death by the personal representative named in the Will or his attorney or by any beneficiary named in the Will or his attorney. The Will must be in a sealed envelope bearing:

- the name and address of the testator as it appears in the Will,
- the name and address of any executor as it appears in the Will,
- the date of the Will, and
- the name of the person who deposits the Will.

The deposit of a Will does not create the presumption that it is the last Will and Testament of the testator.

Lisalette T. Gibson is an Associate in the Ocean Centre office. She is a member of the Private Clients & Wealth Management group specialising in trusts, tax planning and wills.

TERRALEX INSOLVENCY MEETING HOSTED IN THE CAYMAN ISLANDS

L-R: Tara Cooper Burnside, Tara A. Archer, Premier of the Cayman Islands, Gina M. Berry, Country Managing Partner in Cayman.

Higgs & Johnson's Cayman office hosted the TerraLex Insolvency North American Practice Group Meeting. TerraLex is one of the world's leading international legal referral networks. With approximately 160 leading, independent law firms and 15,000 attorneys in 100 countries, TerraLex members provide the legal resources and expertise needed to conduct successful business worldwide.

Partners of the Bahamian Litigation practice group, Tara Archer and Tara Cooper Burnside, participated in this meeting in addition to representatives from several law firms in the USA, Canada and Turks & Caicos.

One highlight of the meeting was a visit from the Premier of the Cayman Islands, the Hon. Alden McLaughlin, MBE, JP, MLA. Attorneys had the opportunity to meet with him during an informal breakfast meeting that took place.

Mark Benedict, Partner in the firm Husch Blackwell, noted his appreciation as follows: 'The Insolvency Practice Group meeting was a resounding success. The Higgs & Johnson team did a fantastic job and has set the bar quite high for any future meetings. The benefit of these meetings to me is the connections and relationships that can be built.'

Higgs & Johnson's Country Managing Partner in Cayman, Gina Berry, stated: 'We are thrilled that everything fell into place and that it was time well spent. The level of connection amongst participants and impact achieved firmly support the TerraLex mission; and we were glad to be part of this positive experience.'

FIRM A SPONSOR AT THE STEP CARIBBEAN CONFERECENCE HELD IN THE BAHAMAS

L-R: Nadia J. Fountain and Tara Frater

Higgs & Johnson was a luncheon sponsor of the 2014 STEP Caribbean Conference held in The Bahamas. Under the theme, "Exploring the Possibilities" the conference considered the prospects that accompany the notion that Caribbean IFC's will continue to grow and leverage their respective strengths in a world where change is the norm.

The conference tackled a myriad of issues facing the trust practitioner including the changing face of the client, dealing with complexities of running a trust business locally, regionally and globally as well as the increasing impact of technology. The STEP Caribbean Conference continues to attract a cadre of world class speakers and provide the latest in professional development and learning while creating an opportunity for discussion, dialogue and networking.

L-R: Earl A. Cash, Aliya Allen (BFSB CEO & Executive Director) and Theo Burrows

Nadia J. Fountain, Partner was a co-presenter with Tara Frater, Senior Associate at Lex Caribbean's Barbados office. They presented on the topic 'Trustees as Shareholders'. Nadia highlighted the standard of care, risks, limitations and due diligence requirements that are associated with this particular dynamic.

L-R: Theo Burrows and Lisalette T. Gibson

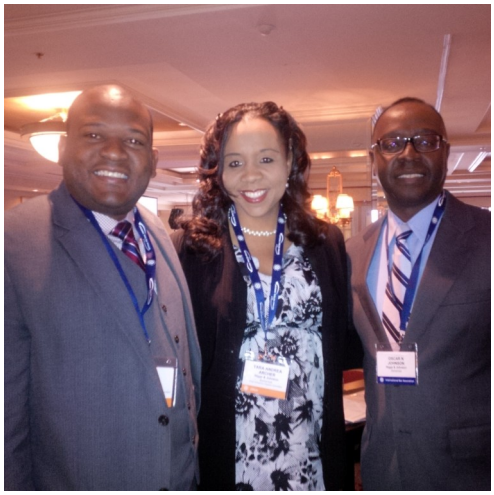
In her capacity as a board member of STEP Bahamas, Nadia noted "I was proud to be a part of the STEP Bahamas Branch as we featured our jurisdiction at this year's conference. Through events such as these, The Bahamas is able to showcase the importance of the financial services industry in this jurisdiction and also highlight the depth of our expertise with a large number of local trust professionals participating and representing our world class talent pool."

Firm Booth

Chair of the Private Clients & Wealth Management group, Dr. Earl A. Cash attended along with Senior Associate Tom Mylott (Cayman Office) and Associates Theo Burrows and Lisalette Gibson, who had responsibility for manning the Higgs & Johnson booth.

ATTORNEYS ATTEND IBA'S BAR LEADERS CONFERENCE

(L-R) Audley D. Hanna Jr., Tara A. A. Archer, Pierre J. Dalphond, Justice of the Quebec Court of Appeal, Alexander De Zordo of Borden Ladner Gervais and Oscar N. Johnson, Jr.



Managing Partner, Oscar N. Johnson, Jr., Partner, Tara A. A. Archer and Associate, Audley D. Hanna Jr., attended the IBA Litigation Committee and the IBA Corporate Counsel Forum - International Litigation Conference entitled "Crossing the Great Divide" held in Montreal, Canada.

The IBA is the world's leading organization of international legal practitioners with more than 50,000 individual lawyers and over 200 bar associations and law societies, spanning all continents, among its members. The IBA provides unparalleled networking and development opportunities through quality conferences, publications and other media, and has a wealth of experience in providing assistance to the global legal community.

The Conference highlighted a number of topics including:- "Discovery Around the World – Comparative Approaches and Strategic Choices"; "Strategies for Controlling the Costs of Discovery across Borders"; and "Obtaining Evidence Abroad – A Comparative Jurisdictional Study". Focus was also had on planning for the upcoming annual IBA Conference, which will be held in Tokyo, Japan this year.

Mrs. Archer noted, "The Bahamas' increasing involvement in the global marketplace necessitates a keen understanding of all areas of cross-border litigation. The Conference was profoundly enlightening on matters relating to obtaining evidence from one jurisdiction for use in another and highlighted how different the process can be from one jurisdiction to another".

PARTNERS ATTEND TERRALEX GLOBAL MEETING

Partners, Dr. Earl A. Cash and Surinder Deal from The Bahamas along with Cayman Country Managing Partner, Gina M. Berry attended the TerraLex Global meeting held in Indianapolis. Ms. Deal is currently a Director.

Dr. Cash (pictured) had the opportunity to meet with the Mayor of the City, Greg Ballard (pictured) during one of the luncheons.