



Common Reporting Standard considerations for FATCA-compliant trusts



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Introduction

The Foreign Account Tax Compliance Act (FATCA) is in full swing. Non-US financial institutions have completed reporting of US account holders for tax year 2014 and will soon begin compiling details for their 2015 FATCA reports. Just as international families and their advisers are getting used to myriad requests for FATCA Form W-8 certification forms, more than 90 other countries have indicated that they wish to address tax evasion through a global exchange of financial information by implementing the Common Reporting Standard (CRS) which, like FATCA, will affect non-US trusts and their trustees.

FATCA for trustee-documented trusts and sponsored investment entities

Many wealthy international families use succession planning structures that include offshore trusts and holding companies. A professional trust company is often engaged as trustee. Under FATCA, those trust companies have generally registered with the Internal Revenue Service (IRS) as reporting foreign financial institutions (FFIs) and have been issued a global intermediary identification number (GIIN). The trustee has addressed requests for FATCA documentation from financial institutions with regard to accounts in the name of the trust by providing Form W-8BEN-E for a non-grantor trust. In the case of a grantor trust, the trustee has provided Form W-8IMY along with the non-US grantor's Form W-8BEN or, in some situations, the US grantor's Form W-9. Generally, where the trust has been established in a jurisdiction that now has a FATCA intergovernmental agreement (IGA) with the IRS, the appropriate Form W-8 will indicate that the trust's Chapter 4 FATCA status is non-reporting IGA FFI as a trustee-documented trust under the relevant IGA.

Many professional trust companies have also registered to act as FATCA sponsoring entities and have been issued a separate sponsoring entity GIIN. Thus, where the non-US trust owns a non-US company that is an investment entity for FATCA purposes, the company and the trustee may have entered into a sponsoring entity agreement. This enables the company to provide Form W-8BEN-E to requesting financial institutions showing a Chapter 4 FATCA status of non-

reporting IGA FFI as a sponsored investment entity or sponsored closely held investment vehicle. An underlying company that has made a US check-the-box election to be disregarded is to provide the Form W-8 for its single foreign owner, the trust.

Both the trust and the underlying company are deemed compliant for FATCA purposes under the relevant IGA. The trustee has filed a FATCA report for tax year 2014 to report a US settlor, if any, and any US beneficiaries that received distributions from the trust. The 2015 FATCA report will generally be due by March 31 2016.

CRS beginning in 2016

International families and their advisers may soon hear from their trustees about expanded reporting obligations known as the CRS developed by the Organisation for Economic Cooperation and Development (OECD). Where FATCA imposes obligations for financial institutions to report US account holders, the OECD CRS expands a financial institution's reporting obligations to residents of CRS 'participating jurisdictions' – that is, jurisdictions with which an agreement is in place pursuant to which the financial institution is obliged to provide the CRS information. More than 90 jurisdictions have endorsed the CRS, but participating jurisdictions must still enact legislation and implement a tax information reporting programme.

Modelled on FATCA, the CRS requires financial institutions in participating jurisdictions to report account holder information to their own tax authorities, which will then exchange that information with the tax authorities of the participating jurisdictions in which the account holders are tax resident. At least 75 countries have signed a multilateral competent authority agreement that commits them to implement the CRS. So-called 'early adopters' – such as Bermuda, the Cayman Islands, the British Virgin Islands, Jersey, Guernsey, Colombia and the EU member states – began compliance from January 1 2016, with initial reporting for the 2016 calendar year in 2017. The Bahamas, Switzerland, Brazil, Canada, Israel, Panama and the other 'late adopters' have agreed to start exchanging information in 2018.

CRS for trustee-documented trusts and sponsored investment entities

Trustee-documented trusts

The CRS is not very different from FATCA from an administrative standpoint. Under the CRS, a 'non-reporting financial institution' includes a trust to the extent that the trustee is a reporting financial institution and reports all information required to be reported under the CRS with respect to all reportable accounts of the trust. This fits neatly with the definition of 'trustee-documented trust' under the IGAs.

A trust structure that is FATCA compliant as a trustee-documented trust can provide the necessary CRS self-certification to any requesting financial institution. However, its trustee now needs to turn its attention to all individuals – not just US persons – who are considered to have so-called 'equity interests' in the trust. If any of those individuals are resident in a CRS partner jurisdiction, their interest in the trust may be reportable.

In the case of a trust that is a financial institution, an equity interest is considered to be held by any person treated as a settlor or beneficiary of all or a portion of the trust, or any other natural person exercising ultimate effective control over the trust. If that equity interest holder is a 'reportable person', then a CRS report will be submitted reporting the individual's name, address, jurisdiction(s) of residence, tax identification number, date and place of birth. A reportable person will be treated as being a beneficiary of a trust if such reportable person has the right to receive, directly or indirectly (eg, through a nominee), a mandatory distribution or may receive, directly or indirectly, a discretionary distribution from the trust.

Underlying sponsored investment entities

An underlying holding company that is an investment entity, and thus a financial institution for the purposes of FATCA, generally has the same classification under the CRS. The company can provide a self-certification stating that it is a financial institution. Reportable persons under the CRS do not include:

- corporations whose stock is traded publicly;
- corporations related to such public companies;

- government entities;
- international organisations;
- central banks; or
- financial institutions.

The bank or other investment custodian where the underlying investment entity has an account need not file a CRS report because the company is not a reportable person. As regards the holding company itself, its equity interest is held by the trust, which is also an investment entity and thus a financial institution. Therefore, the company need not file a CRS report because its equity holder, the trust, is not a reportable person. As with FATCA, the CRS reporting in this situation takes place at the trust level by the trustee.

Under the CRS, the underlying holding company is a financial institution rather than a non-reporting financial institution because the non-reporting financial institution classification under the CRS does not include a sponsored investment entity (unless a participating jurisdiction chooses to define it as such under domestic law). Nevertheless, the CRS participating jurisdiction may provide in its implementing legislation for investment entity financial institutions to appoint a person as the entity's agent to carry out the duties and obligations imposed on the entity by the CRS. Thus, the trustee – as both the FATCA sponsoring entity and the CRS agent for the underlying holding company – can coordinate due diligence and certification.

Investment entity not resident in CRS participating jurisdiction

If the trust or underlying company is not resident in a CRS participating jurisdiction, the requesting bank or other financial institution is required, pursuant to its applicable CRS regulations, to treat the trust or company as a passive non-financial entity. This means that the requester must obtain information regarding the entity's 'controlling persons', and any controlling person tax resident in a CRS participating jurisdiction must be reported. Most commonly used offshore jurisdictions – such as Bermuda, the British Virgin Islands, the Bahamas and the Cayman Islands – have indicated that they will implement the CRS, but it must be determined whether the requesting financial institution's applicable CRS regulations have identified the particular country on a published list of jurisdictions with which it is participating. If the United States is ultimately considered not to be a participating jurisdiction, this will affect non-US accounts in the name of US companies controlled by individuals in CRS jurisdictions.

Awaiting implementing legislation

One particularly difficult aspect of the CRS is that a complete analysis will depend on the final details of the implementing legislation and tax authority practice in each particular jurisdiction. For example, the family adviser must check the local CRS regulations to determine whether the equity interest of a trust beneficiary will be limited to the value of a distribution in the relevant reporting year, so that discretionary beneficiaries who do not receive a distribution will not be reportable account holders for that year. If provision is made for CRS commentary (which is any explanatory material made and published by the OECD for the purposes of assisting with the interpretation of the CRS) to be an integral part of the jurisdiction's implementing legislation, then commentary in the OECD *Common Reporting Standard Implementation Handbook* will be relevant. For example, Paragraph 214 of the handbook provides that when identifying the financial accounts of a trust that is a financial institution, a discretionary beneficiary will be treated as an account holder only in the years in which that beneficiary receives a distribution from the trust.

CRS self-certification

Trust settlor

As regards the trust's settlor, it will be necessary for the settlor to provide a self-certification that allows the trustee to determine the settlor's residence for tax purposes and to confirm the reasonableness of such self-certification based on information obtained by the trustee in connection with the establishment of the relationship, including any documentation collected pursuant to anti-money laundering or know your client procedures. If the self-certification

establishes that the settlor is resident for tax purposes in a reportable jurisdiction, the trustee will need to obtain the settlor's tax identification number with respect to such reportable jurisdiction and make the settlor aware that CRS reporting is required. The settlor must inform the trustee if his or her tax residence changes.

The settlor or his or her adviser should discuss with the trustee exactly what is to be reported and the amount. Even where the settlor has retained no powers and no interests in the trust property, the settlor's equity interest is to be reported. The settlor and his or her adviser must consider the home country ramifications of such reporting.

Discretionary beneficiaries

As regards the trust's discretionary beneficiaries, the relevant local CRS regulations should be reviewed to confirm that only beneficiaries resident for tax purposes in a reportable jurisdiction who have received a distribution from the trust are to be reported. The self-certification for each such beneficiary will indicate his or her tax home and tax identification number if that home is a reportable jurisdiction. The family adviser should ensure that if a discretionary beneficiary has no knowledge of the trust and the intent of the settlor is that he or she should not have knowledge until a later date, that beneficiary should not be contacted for a self-certification. Instead, the settlor or protector can provide the necessary due diligence information; since the beneficiary has not received a distribution, no CRS report is required. When the time comes to make a distribution to such a beneficiary, the trustee can seek the self-certification and the tax identification number from the beneficiary directly before releasing any funds.

Peripatetic individuals

Because countries other than the United States levy tax based on residency, which may not be acquired until an individual spends a certain number of days in the country, it is possible for a non-US individual not to be tax resident anywhere. Generally, the individual will have multiple homes in different countries, none of which are the country of which he or she is a citizen. The trustee's review of account opening statements plus know your customer and anti-money laundering due diligence will include indicia such as mailing addresses and telephone numbers, instructions to transfer funds to an account in a particular jurisdiction or the location of an agent or attorney in fact that establish a connection to one or more countries. The individual will need to discuss with the trustee the fact that he or she is not subject to tax in any country and likely provide documentary evidence establishing his position of non-residence for tax purposes. Without adequate documentation, the trustee must treat the individual as a resident for tax purposes of each jurisdiction for which an indicium is identified.

Comment

Financial institutions all over the world are beginning to request CRS self-certification documentation, along with FATCA documentation, even though implementing legislation may not be finalised. Although questions raised by the uncertainty surrounding the CRS can be frustrating, advisers to international families should take a practical approach, work with their trust companies and ensure that each family member has considered where he or she is tax resident. Statements regarding tax residency should be consistent on all documentation and reporting. Advisers should begin to discuss with the trust company who and what will be reported.

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