BRIEFING NOTE

November 2015

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The Common Reporting Standard - Setting the benchmark for global information exchange

Background

The OECD (Organisation for Economic Co-operation and Development) Common Reporting Standard (CRS) is a big step towards a globally co-ordinated approach to disclosure of income earned by individuals and organisations. As a measure to counter tax evasion, it builds upon other information-sharing legislation such as FATCA (the US Foreign Account Tax Compliance Act often referred to as US FATCA), the European Union (EU) Savings Directive and The Crown Dependencies and Gibraltar Regulations (often referred to as UK FATCA). In recent years, governments and financial institutions have become much more aware of the large amounts of undisclosed wealth held in offshore accounts. Governments see a big opportunity to boost revenue by collecting tax relating to these accounts – but only if sufficient data can be obtained from financial institutions around the world.

Individuals in particular find it relatively easy to hold and manage investments through financial institutions outside of their country of residence, without any income being visible to their domestic tax authorities, unless the taxpayer actually discloses it. Consequently, international bodies such as the G20 (Group of 20 Twenty Leaders and Finance Ministers and Central Bank Governors) and the OECD have started co-ordinated efforts to gain a truer picture of income and assets worldwide. Initiatives such as the EU Savings Directive and US FATCA both required greater disclosure, and provided a foundation from which to develop a global standard for exchange of information.

Traditional arrangements for exchanging information have been bilateral, based around tax treaties for avoiding double taxation, as well as tax information exchange agreements. However, the multilateral Convention on Mutual Administrative Assistance in Tax Matters allows in principle for unilateral, bilateral and multilateral exchange. Automatic Exchange of Information (AEOI) is not new – a recent survey conducted by the OECD shows widespread use of this practice – but it is only recently that the push has become more comprehensive and global in scope.

AEOI involves the systematic transmission of large amounts of information (such as investment income) from the tax administration where the account is held to the tax administration where the taxpayer is resident. The resident tax administration can then verify whether the taxpayer has accurately reported his or her income. While the main focus is on exchanging information about financial accounts, many types of income and other information may be relevant including employment income, pensions, and changes of residence or sales and purchases of real estate.

CRS

AEOI has also attracted significant political interest and US FATCA has inspired a number of countries to explore the possibilities of developing similar arrangements. In April 2013, the G20, which had already been calling for a global approach for a number of years, endorsed the concept of the CRS as a new global standard drawing extensively on the intergovernmental approach to implementing US FATCA. The OECD published the text of this single global standard in February 2014.

The G20 has called on all countries to adopt the CRS. In principle, there are no restrictions. According to the joint statement dated 19 March 2014, 44 countries (including the UK) had indicated that they would be prepared to implement the new standard by 31 December 2015.[1]

CRS and US FATCA

The CRS is modelled after US FATCA and requires jurisdictions to exchange information obtained from all their financial institutions. This automatic exchange of information will involve regular transmission of bulk taxpayer information concerning different types of income and asset information, such as information on dividends, interest, royalties, salaries, pensions amongst others.

Where the CRS differs from US FATCA is that CRS is based on residence and does not refer to citizenship. Furthermore, the US FATCA withholding tax which introduces additional features into the reporting process are not needed when implementing the CRS. Owing to the different focus of the CRS, there are by necessity, differences in the information collected and exchanged and it is envisaged these differences will cause implementation difficulties for institutions already struggling with US FATCA data collections.

Whilst the CRS is primarily aimed at tax evasion by individuals, in common with US FATCA, the information exchange is automatic and takes no account of the fact an individual may not be required to disclose the information in his country of tax residence or that due to their particular tax status they are fully compliant. This contrasts with information sharing legislation such as UK FATCA where there is an opt out for UK Resident/Non Domiciled individuals.

[1] Those signing as Early Adopters in the 19 March 2014 Statement are : Argentina, Belgium, Bulgaria, Colombia, Croatia, Cyprus, the Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Iceland, India, Ireland, Italy, Latvia, Liechtenstein, Lithuania, Malta, Mexico, the Netherlands, Norway, Poland, Portugal, Romania, Slovakia, Slovenia, South Africa, Spain, Sweden and the United Kingdom; the UK's Crown Dependences of Isle of Man, Guernsey and Jersey; and the UK's Overseas Territories of Anguilla, Bermuda, the British Virgin Islands, the Cayman Islands, Gibraltar, Montserrat and the Turks & Caicos Islands.

What's Next?

From 1st January 2016, the CRS will set the benchmark for global information exchange. This provides for a framework for financial institutions to share client data with tax authorities around the world. More than 90 countries are committed to adopting the CRS and it will eventually replace many existing AEOI Agreements. Financial data will be collated from 1st January 2016 and reporting will take place from September 2017. Consequently, the CRS will co-exist with other agreements for some time, most notably US FATCA. It is clear the CRS will be adopted without delays and the risk of discovery for those with undisclosed assets overseas continues to gather pace.

To ensure HMRC get the most out of international tax agreements, such as the AEOI Agreements and the CRS, they are continuing to increase the number of tools available to tackle offshore evasion. The four consultation documents on tackling offshore evasion published on 16 July 2015 which invited comments from interested parties until 8 October 2015 are an indication of HMRC's serious intentions in this regard. The proposed measures would increase penalties for offshore issues, sanction those who enable others to commit offshore evasion and contemplate the introduction of a strict liability offence with a potential prison term. In tandem with this individuals are being encouraged to take advantage of the Disclosure Facilities, such as the Liechtenstein Disclosure Facility ("LDF") to declare previously undisclosed foreign assets in a reduced penalty environment.

What will be reported?

As indicated above, similar information must be reported under the CRS as under US FATCA, i.e. the identity and residence of financial account holders (including certain entities and their controlling persons), account details, reporting entity, account balance/value and income/sale or redemption proceeds. There is a broad definition of what constitutes a financial account. There will be no exclusion for non-UK domiciliaries' accounts.

Who will do the reporting (reporting entities)?

Financial institutions (as defined in keeping with the definition under US FATCA Agreements and including depository institutions, custodial institutions, investment entities, trustees and specified insurance companies, unless they present a low risk for being used for evading tax and are excluded from reporting) will be responsible. Certain entities will be treated as exempt from reporting such as Governmental entities, international organisations, central banks, certain retirement funds and exempt collective investment vehicles. The reporting obligations for trustees of family trusts are expected to be much broader than under US FATCA.

Who will be reported (reportable persons)?

These include any individual identified by a reporting entity in one country as resident for tax purposes in a reportable country (i.e. a country with which the participating country has, in effect, an AEOI agreement), as well as certain entities, including trusts and foundations.

A beneficiary of a trust will be treated as a reportable person if such a person has the right to receive a mandatory distribution from the trust. This distribution can be received either directly or indirectly, for example through a nominee or if that person receives a discretionary payment from the trust. Again, this receipt can be either directly or indirectly from the trust.

Status and timing

Financial data will be collated from 1st January 2016 with reporting taking place from September 2017. Reporting must be maintained annually.

Conclusion and Recommendations

The G20 charged the OECD with developing the CRS, the primary goal of which was to facilitate automatic tax information exchange between non-US countries. In short, the CRS is intended to be a standardised, cost effective long-term model for the bilateral automatic exchange of tax information (including creating common due diligence procedures). The transparency created by the CRS is intended to be another deterrent to taxpayers' use of offshore financial accounts (held directly or indirectly) to avoid domestic tax liabilities.

Once fully established and operational, it is the intention that CRS will replace the reporting under UK FATCA but run in parallel with US FATCA.

UK taxpayers need to ensure that:

1. The correct information is held by their financial institutions so that this can be forwarded to HMRC or other relevant tax authorities.
2. All relevant issues have been correctly disclosed to HMRC. HMRC are committed to increasing their investigation into offshore activities with a view to securing more prosecutions.
3. Any offshore arrangements should be correctly documented and stand up to scrutiny. Any clients with tax irregularities need to use the existing Facilities, particularly the LDF, before they close on 31 December 2015 to avoid the harsher regime to follow.

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For further information on any of the issues raised in this Briefing Note, or for help on any disclosure matters, please contact a member of the Rooks Rider Solicitors Wealth Planning Team.

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