Privacy: What's Left?

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A seismic change in the international private wealth arena is under way. Over 90 jurisdictions have committed to automatically exchange comprehensive financial information on an annual basis under the OECD's Common Reporting Standard (CRS). The CRS will start in 2016 in over 55 jurisdictions.

This article comments on the CRS and, in particular, on certain practical implications arising from the CRS for private wealth and estate planning. We also summarise other international developments on transparency. These developments, together with the CRS and FATCA, have resulted in the triumph of transparency over privacy as the emerging global standard.

UK Public Registers

Legislation providing for a public register of beneficial owners of UK companies received royal assent on March 26, 2015. Commencing in April 2016 self-reported data on the ultimate individual owner and controlling persons for private UK companies will appear in the Companies House register and will be available for government and public (including media) access.

Offshore Central Registers?

The UK is demanding that its Crown Dependencies and Overseas Territories similarly adopt central registers of corporate beneficial owners available to tax authorities and law enforcement.

EU Central Registers

The EU adopted the 4th Anti-Money Laundering Directive on May 20, 2015. The directive requires central registers of beneficial owners of legal entities. Public access will be permitted for those who can show "legitimate interest" (e.g., potentially including the media). Trusts are also included where the trust generates local tax consequences, though there are no provisions for public access. EU Member States have two years to implement the directive in national law.

Public Registers of Directors

The Financial Action Task Force (FATF) published new guidance on transparency and beneficial ownership on October 27, 2014. This requires countries to ensure that basic information on companies is obtained and recorded by the company registry, including a public register of company directors.

OECD Common Reporting Standard

Objectives and Obligations

The FATCA-inspired CRS is designed to tackle international tax evasion by establishing the annual automatic transmission of bulk taxpayer information. Financial institutions are required to (i) conduct due diligence on financial accounts to identify account holders who are tax resident in participating jurisdictions; and (ii) report information on these accounts to their domestic tax authority which will then automatically transmit that information directly to the tax authorities of participating jurisdictions where account holders are tax resident.

From FATCA to CRS

51 "early adopter" jurisdictions signed a Multilateral Competent Authority Agreement in October 2014. Some 40 other countries have also undertaken to adopt the CRS. Financial institutions will need to identify account holders in over 90 countries, not simply US persons in the context of FATCA.

2016 Start Date for CRS

Financial institutions in early adopter jurisdictions will need to begin tracking accounts from January 1, 2016 and exchanging information on those accounts beginning in 2017. Other participating countries will join a year later, tracking accounts from 2017 and exchanging information on those accounts from 2018. A list of participating jurisdictions and their start date is available on the OECD's website.

Broad Application

The CRS applies to a broad range of financial institutions (e.g. banks, custodians, brokers, certain collective investment vehicles and insurance companies). Trusts, companies, partnerships and foundations may be investment entities and therefore financial institutions if managed by a professional trustee or service provider. The financial information to be reported is unprecedented in breadth and includes taxpayer identification numbers (TIN), account balances (or values) and sales proceeds from financial assets. Disclosure of account balances goes beyond the information required on domestic tax returns in most countries, which are normally designed to disclose income and capital gains to determine taxable income. The CRS also requires looking through passive non-financial entities to report on the individuals that ultimately control these entities.

Cross-Border Application

The CRS is designed to raise tax revenue arising in foreign structures. It is not aimed at domestic structures.

What is a Financial Account?

A financial account includes equity or debt interests in investment entities. Professionally managed trusts, personal holding companies, foundations and partnerships may be investment entities. The shares of a company or a partner's interest in a partnership are financial accounts for the shareholder and partner, respectively. Similarly, settlors, beneficiaries and other individuals exercising ultimate effective control over a trust (or foundation) are treated as having a financial account in the trust (or foundation). However, a discretionary beneficiary will only be treated as having a financial account in a trust if the beneficiary receives a distribution in the calendar year (see paragraph 70 of the OECD's Commentary on Section VIII of the CRS).

What should clients do?

1. Clients should review their wealth structures to consider the scope of information that will be automatically disclosed to their home country and whether that information can be limited.
2. Clients should be responsive to due diligence requests from their bank. If a bank has conflicting information suggesting that a client resides in two jurisdictions and is unable to confirm a single jurisdiction of tax residence, the bank may be required to disclose information to both jurisdictions (through their tax authority).
3. Clients should proactively regularize non-compliant arrangements including through amnesties and disclosure programs. This will likely be more favorable than being audited.
4. Clients should confirm the tax efficiency of, and reporting obligations in respect of, their wealth structure.

Please do not hesitate to contact us if you wish to discuss these matters.