

STEP's comments on the UK implementation of disclosure of cross-border tax planning arrangements under *EU Directive 2018/822 (DAC6)* and HMRC guidance published in its *International Exchange of Information Manual* on 1 July 2020 – trusts and estates-related points.

About Us

STEP is the worldwide professional association for those advising families across generations. We help people understand the issues families face in this area and promote best practice, professional integrity and education to our members.

Today we have over 22,000 members in over 100 countries and over 8,000 members in the UK. Our membership is drawn from a range of professions, including lawyers, accountants and other specialists. Our members help families plan for their futures: from drafting a will or advising family businesses, to helping international families and protecting vulnerable family members.

We take a leading role in explaining our members' views and expertise to governments, tax authorities, regulators and the public. We work with governments and regulatory authorities to examine the likely impact of any proposed changes, providing technical advice and support and responding to consultations.

The purpose of this note

Given the nature of the services provided by STEP's members, they are most likely to need to consider whether reporting is required under DAC6 in relation to trust/company structures with which they are involved. However, this paper also address a few issues related to wills and estates. The guidance published in July 2020 (the HMRC guidance), which forms part of the *International Exchange of Information Manual (IEIM)*, does not deal with many of the issues which arise in relation to trusts, wills and estates.

STEP's views on the relevant issues surrounding the implementation of DAC6 as a result of statutory instrument 25/2020, *The International Tax Enforcement (Disclosable Arrangements) Regulations 2020* (the Regulations) and the HMRC guidance, in the context of trusts and trust structures are set out in the remainder of this paper.

Caveat

It should be noted that although HMRC has seen this document and have had the opportunity to comment on it, HMRC has not endorsed the views set out in it and the document should not be taken as representing HMRC's views.

The views set out in the document reflect the views of the STEP committee members involved in its preparation. They are intended to assist professional advisors in considering the issues, but do not constitute advice and are not a substitute for consideration of the issues by a professional advisor in each client's specific context.

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Where relevant, references have been made to pages/paragraphs of the HMRC guidance, identified by IEIM numbers.

(A) Cross-Border Arrangements

1. Meaning of 'concerning': general (IEIM630040)

- 1.1 The expression 'cross-border arrangement' is defined at Art 3(18) of DAC6. Before considering whether a particular hallmark applies to an arrangement, it is necessary to consider whether the arrangement is a cross-border arrangement. To be a cross-border arrangement:¹

¹ Defined as an arrangement concerning either more than one Member State or at least one Member State and a third country, where certain further conditions apply, namely that:

- (a) not all of the participants in the arrangement are resident for tax purposes in the same jurisdiction;
- (b) one or more of the participants in the arrangement is simultaneously resident for tax purposes in more than one jurisdiction;
- (c) one or more of the participants in the arrangement carries on a business in another jurisdiction through a permanent establishment situated in that jurisdiction and the arrangement forms part or the whole of the business of that permanent establishment;
- (d) one or more of the participants in the arrangement carries on an activity in another jurisdiction without being resident for tax purposes or creating a permanent establishment situated in that jurisdiction; or
- (e) such arrangement has a possible impact on the automatic exchange of information or the

- (a) the arrangement must 'concern' either more than one Member State or at least one Member State and a third country; and
- (b) it must be the case that either:
 - (i) one of the tests in (a) to (d) of Art 3(18) is satisfied by reference to the 'participants' in the arrangement; or
 - (ii) the arrangement will, if implemented, have a possible impact on the automatic exchange of information (AEOI) or the identification of beneficial ownership.

1.2 In the definition of 'cross-border arrangement', there is no definition of the word 'concerning'. The guidance at IEIM630040 says that for an arrangement to 'concern' a country, that country must be 'of some material relevance' to the arrangement. It is not clear whether the factors to be taken into account when looking at whether an arrangement 'concerns' a particular country, and the application of the material relevance test, depend on which of the hallmarks might potentially apply, should the arrangement be a cross-border arrangement. However, this appears to be the inference from IEIM630050.

1.3 This is relevant to the question of whether an arrangement that potentially engages Hallmark D1 qualifies as a cross-border arrangement (see 2 below).

2. Meaning of 'concerning': arrangements that are potentially within Hallmark D1

2.1 Hallmark D1 is any 'arrangement which may have the effect of undermining the reporting obligation under the laws implementing Union legislation or any equivalent agreements on the automatic exchange of Financial Account information, including agreements with third countries, or which takes advantage of the absence of such legislation or agreements'. The Common Reporting Standard (CRS), relating as it does to the automatic exchange of financial account information, is clearly relevant.²

2.2 For the purposes of the CRS, in relation to a trust, a reportable person would include:

- (a) the settlor;
- (b) the trustees;
- (c) the beneficiaries (subject to certain carve-outs; see 2.3 below);

identification of beneficial ownership. See also IEIM630020.

² See IEIM645010 (Hallmark D1 – Undermining reporting obligations).

- (d) the protector; and
- (e) any natural person exercising effective control.

For CRS purposes, a trust will arguably 'concern' a jurisdiction where any of the above persons are resident for tax purposes in that jurisdiction.

2.3 However, we note that for the purposes of the CRS it should not be necessary to consider the residence status of the following beneficiaries, on the basis that none of these beneficiaries are reportable for the purposes of CRS:

- (a) a discretionary beneficiary falling within a defined class who has not received a distribution from the trust in the calendar year; or
- (b) any contingent beneficiary who can only benefit on the happening of a particular event, e.g. attaining a specified age, the death of another beneficiary or the termination of a trust (until the contingency is satisfied and the beneficiary receives a benefit).

2.4 For the purposes of Hallmark D1, therefore, we consider that an arrangement consisting of the creation/funding of a trust will 'concern' a jurisdiction if any of the following persons is tax resident in that jurisdiction at the time the arrangement is made available:

- (a) a trustee;
- (b) the settlor;
- (c) any protector;
- (d) any named current discretionary beneficiary;
- (e) any discretionary beneficiary falling within a defined class:
 - (i) who has, in the calendar year in which the arrangement is made available, received a distribution from the trust; or
 - (ii) to whom, at the time the arrangement is made available, the trustees intend to make a distribution in the reasonably foreseeable future
- (f) any fixed interest beneficiary, e.g. a life tenant; and
- (g) any natural person exercising effective control over the trust.

2.5 This definition would therefore exclude any discretionary beneficiary falling within a defined class who receives a distribution from the trust in that part of the calendar year after the arrangement is made available, provided the

trustees did not intend, at the time that the reporting trigger would have been reached, to make a distribution to the beneficiary.

- 2.6 If, at the time of the relevant arrangement, it is clear that there is an intention to make distributions to a particular member of the class of beneficiaries, we would consider that the arrangement would also concern the country of residence of that beneficiary. For example, consider a trust which has the descendants of numerous branches of a family listed as classes of discretionary beneficiaries. If in practice the trust is expected to benefit only the first descendant in one of those classes in the reasonably foreseeable future, the residence of that potential beneficiary only need be considered.
- 2.7 We also consider that an arrangement ‘concerns’ a particular jurisdiction if the arrangement involves an asset situated or held in that jurisdiction, or which will become situated or held in that jurisdiction as an immediate result of the arrangement, provided that the asset is of material relevance to the arrangement.
- 2.8 We consider that if another hallmark is potentially relevant, the identity of the persons or the other factors that need to be considered in determining whether the arrangement is a cross-border arrangement may be different. For example, the country in which the protector is resident may be of no material relevance to the arrangement.

3. **Meaning of ‘participant’**

- 3.1 There appears to be no section in the guidance regarding the definition of a participant.
- 3.2 We consider that ‘participant’ must be given its natural meaning, which does not include advisors. It means, essentially, a party to the arrangement in the legal sense, i.e. a person entering into the arrangement.
- 3.3 We consider that a ‘participant’ in connection with a trust should include:
- (a) on the formation of the trust, the settlor, the trustees and the protector (if any) appointed on the formation of the trust; and
 - (b) in relation to any other arrangement concerning the trust:
 - (i) the trustees;
 - (ii) any natural person exercising effective control (within the guidance given in the FATF *Guidance for a Risk-Based Approach for Trust & Company Service Providers (TSCPs)*,³ which may include a

³ See <http://www.fatf-gafi.org/media/fatf/documents/reports/RBA-Trust-Company-Service->

protector if the protector has the relevant degree of 'control') but only if they participate in the arrangement within its natural meaning; and

(iii) any other party to the arrangement.

- 3.4 In our view, unless a beneficiary of a trust is a party to an arrangement (for example the beneficiary's participation is required for that particular arrangement) or the beneficiary's involvement amounts to 'effective control' within the meaning of the FATF guidance referred to at 3.3(b)(ii) above, the beneficiaries of a trust (whatever their status) should not be treated as 'participants' for this purpose. Although the beneficiaries of a trust have interests and rights, they are not normally parties.
- 3.5 Accordingly, the question of whether any arrangement affecting a trust is a 'cross-border arrangement' for the purposes of conditions (a) to (d) of art. 3(18)⁴ should not generally be affected by where the beneficiaries are resident. However, for the purposes of art. 3(18) para. (e), in cases where Hallmark D1 is potentially engaged, it will be necessary to consider the residence status of the beneficiaries (subject to the carve-outs for discretionary and contingent beneficiaries discussed at 2.3 above) to determine whether the arrangement is a cross-border arrangement.

(B) The Main Benefit Test

4. The meaning of 'tax advantage' (IEIM641000 - IEIM641050)

- 4.1 An arrangement otherwise falling within Hallmark A, Hallmark B and certain parts of Hallmark C will only be caught if it satisfies the main benefit test. This is only met if it can be established that the main benefit or one of the main benefits which, having regard to all relevant facts and circumstances, a person may reasonably expect to derive from the arrangement is the obtaining of a tax advantage.⁵

[Providers.pdf](#). Annex 1 of that document says this about 'Natural person exercising effective control':

'For these purposes "control" means a power (whether exercisable alone or jointly with another person or with the consent of another person) under the trust instrument or by law to:
i. dispose of or invest (other than as an investment manager or adviser) trust property; ii. direct, make or approve trust distributions; iii. vary or terminate the trust; iv. add or remove a person as a beneficiary or to or from a class of beneficiaries and or; v. appoint or remove trustees.'

⁴ See footnote 1.

⁵ Tax advantage' is defined for the purpose of the UK Regulations in Regulation 2(4) as including:

- (a) relief or increased relief from tax;
- (b) repayment or increased repayment of tax;
- (c) avoidance or reduction of a charge to tax or an assessment to tax;

- 4.2 Accordingly, a tax advantage does not arise for these purposes where the tax consequences of the arrangement are entirely in line with the policy intent of the legislation upon which the arrangement relies.
- 4.3 The test looks at whether a tax advantage (as defined in the Regulations) was one of the main benefits that a person could reasonably expect to obtain from the arrangement. The HMRC guidance⁶ states that 'it does not matter if the person was seeking a tax advantage from the arrangement, or what other reasons they might have had for entering into the arrangement, what matters is whether the arrangement is such that a tax advantage is the main benefit or one of the main benefits that a person may reasonably be expected to derive from the arrangement'.
- 4.4 However, we consider that this does not mean that subjective intentions and expectations are completely irrelevant for this test. One of the factors which must be relevant in deciding whether obtaining a tax advantage was one of the main benefits which someone may reasonably have been expected to derive from the arrangement, must be whether or not that person did in fact intend to obtain a tax advantage. The intentions of those implementing an arrangement may therefore offer a good indication as to whether the arrangement would reasonably be expected to have generated a tax advantage.
- 4.5 The UK tax legislation contains specific provisions that apply to the taxation of trusts with a cross-border element (e.g. a non-UK resident trust settled by a UK resident but non-domiciled settlor is subject to specific statutory regimes for income tax, capital gains tax and inheritance tax). The statutory rules in this area, many of which have recently been overhauled, mean that a trust which is a cross-border arrangement may be entirely in line with the policy intent of the relevant legislation. In our view, therefore, setting up and managing a structure which will be subject to the UK tax regime applicable to non-resident trusts should not be considered as satisfying the main benefit test, provided that the structure is subject to taxation in a way that is in line with the policy intent of the relevant legislation.
- 4.6 The application of some of the tax rules relating to offshore trusts depends upon whether tax avoidance was one of the purposes or one of the main purposes of the arrangements. If the taxpayer is able to establish that tax avoidance was not one of the main purposes of the arrangements, it would normally be reasonable

(d) avoidance of a possible assessment to tax;
(e) deferral of a payment of tax or advancement of a repayment of tax; and
(f) avoidance of an obligation to deduct or account for tax,
where the obtaining of the tax advantage cannot reasonably be regarded as consistent with the principles on which the relevant provisions that are relevant to the reportable cross-border arrangement are based and the policy objectives of those provisions.

⁶ At IEIM641010.

to assume that obtaining a UK tax advantage was not the main benefit (or one of the main benefits) which they expected to derive from the arrangement. However, if there is some feature of the arrangement which takes it outside the policy intent of the relevant legislation, the main benefit test may be satisfied.

(C) Relevant Hallmarks

5. Hallmark A3: standardised documentation and structures (IEIM642030)

5.1 Hallmark A3 applies to a cross-border arrangement if it has 'substantially standardised documentation and/or structure and is available to more than one relevant taxpayer without a need to be substantially customised for implementation', and the main benefit test is satisfied.

5.2 The HMRC guidance⁷ states: 'the use of precedent documents in the production of legal documentation would not normally trigger this hallmark as the documents are commonly subject to detailed consideration of the clients' circumstances and can be customised accordingly'.

5.3 Trust documentation and wills containing trust provisions are typically drafted in standard format, based on precedents which are then amended and tailored to the specific requirements of the settlor.

5.4 The use of a standard precedent as a basis for the purpose of drafting a trust (or other similar arrangement, including, for example a partnership or company articles of association etc.) would not, by itself, therefore mean that the formation of a trust (or other similar arrangement) falls within Hallmark A3. It is very unusual for a precedent document to be used without any changes at all. It is simply there as a starting point and the final document will be tailored to the needs of the particular situation.

6. Hallmark B2: conversion of income into capital (IEIM643020)

6.1 We do not intend to comment on this hallmark generally. In relation to trusts we take the view that where trustees decide to accumulate income so that it thereafter forms part of the capital of the trust fund, and later exercise their powers to make a capital distribution to a beneficiary, this should not be regarded as engaging Hallmark B2 in a UK tax context.

6.2 This hallmark can only be engaged where the main benefit test is met. Accumulation of income is part of the normal operation of a discretionary trust, and UK resident and non-UK resident trusts are subject to a range of anti-avoidance provisions in the UK tax code, under which trust income may be taxed on the trustees and/or the settlor and/or beneficiaries who receive

⁷ At IEIM642030.

distributions. Generally, the accumulation of income will not give rise to any discernible tax benefit, as the income will be taxed under one or the other of these anti-avoidance provisions. In the event that the income is not taxed on the trustees or the settlor and the distribution of accumulated income is not taxed on the recipient beneficiary, this can only be because, as a matter of policy, a tax charge is not intended to arise in the particular circumstances of the case. Either way, there is no tax advantage, as that expression is construed in the context of the main benefit test (see 4 above). We therefore take the view that, in a UK tax context, the main benefit test cannot be satisfied by an arrangement that involves trust income being accumulated and later paid out as capital.

- 6.3 The position may be otherwise in the event that income is accumulated and a capital distribution is made to a beneficiary who is resident in an EU Member State. If so, consideration will need to be given to the issue of whether the tax outcome for that beneficiary is consistent with the policy behind the tax legislation of the country where the beneficiary is resident.

7. Hallmark D1: undermining reporting obligations (IEIM645010)

- 7.1 An arrangement will fall within Hallmark D1 if it may have the effect of undermining the reporting obligation under the laws implementing European Union legislation or any equivalent agreements on the automatic exchange of financial account information, including agreements with third countries, or which takes advantage of the absence of such legislation or agreements. It is stated that arrangements which will be caught by Hallmark D1 include the use of legal entities, arrangements or structures that eliminate or purport to eliminate reporting of one or more account holders or controlling persons under the automatic exchange of financial account information.
- 7.2 One important issue raised by the wording of Hallmark D1 is whether the test is purely objective (and capable of applying regardless of whether the participants in the arrangement intend to undermine CRS) or whether an intention to undermine CRS is required.
- 7.3 The HMRC guidance states at IEIM645010 that the test in Hallmark D1 is an objective one, but that in determining whether an arrangement has the effect of undermining the CRS the intent of those involved will be relevant, as it will offer a good indication as to whether the arrangement may have the relevant effect.
- 7.4 In our view the word 'undermine' carries an implication of deliberate subversion, and a distinction needs to be made between arrangements which have the effect of causing CRS reporting obligations to fall away (but where there is no deliberate subversion of such obligations) and arrangements where there is deliberate subversion.

- 7.5 In reality, therefore, we consider that there is a subjective aspect to the test. Whether Hallmark D1 applies depends on whether the arrangements have a purpose of circumventing CRS reporting, contrary to the policy behind CRS, or whether they result in non-reporting as a natural consequence of some other purpose, which is consistent with the policy. We consider that the relevant subjective intent (to undermine CRS should normally be viewed from the point of view of the participants to the arrangement. However, this may not always be apparent, for example, if the arrangement is a marketable arrangement and therefore there are, as of yet, no participants in the arrangement. In such circumstances, it would be appropriate to consider the intention of the intermediary in designing and marketing the arrangement. For example, where an intermediary promotes an arrangement on the basis that CRS reporting would not be required, this would indicate that arrangements have a purpose of circumventing CRS reporting, and therefore the hallmark would be met, even though it is not possible to identify the purpose of any particular participant.
- 7.6 The mere fact that an arrangement results in there being no reporting under CRS legislation does not, of itself, we consider, mean that the CRS legislation has been circumvented within the meaning of this Hallmark. The Hallmark requires deliberate undermining.
- 7.7 The correctness of this interpretation is clear from Recital (13) to DAC6, where it is stated that 'A specific hallmark should be introduced to address arrangements designed to circumvent reporting obligations involving automatic exchanges of information.' The wording 'designed to circumvent' makes it clear that the objective of this Hallmark is to catch arrangements where there is deliberate subversion of CRS reporting.
- 7.8 There is also support for this interpretation in the *Model Mandatory Disclosure Rules for CRS Avoidance Arrangements and Opaque Offshore Structures* approved by the OECD (the Model MDRs) and the commentary on the Model MDRs. It is expressly stated in Recital (13) to DAC6 that the Model MDRs and the commentary may be used as an aid in interpreting the parts of DAC6 that are concerned with CRS avoidance arrangements.
- 7.9 The Model MDRs describe a CRS avoidance arrangement as 'any arrangement where it is reasonable to conclude that it has been designed to circumvent or has been marketed as or has the effect of circumventing CRS legislation'.
- 7.10 As noted above, 'designed to circumvent' indicates that intent is required. The wording 'or has the effect' might suggest that the concept of a CRS avoidance arrangement is wider than this. However, according to the Model MDRs, 'an Arrangement is not considered to have the effect of circumventing CRS Legislation solely because it results in non-reporting under the relevant CRS Legislation, provided that it is reasonable to conclude that such non-reporting

does not undermine the policy intent of such CRS Legislation'. This undermining of policy intent is key, and intent is implied by the word 'undermining'.

- 7.11 For example if a business transaction is entered into, without any intent to undermine CRS reporting, but non-reporting under CRS legislation is a natural consequence of the arrangement, this will not be caught by Hallmark D1 because there was no intention to undermine the CRS. The conclusion would be different if a business transaction was deliberately structured in a particular way with the objective of causing CRS reporting not to apply, in a manner contrary to the policy behind the CRS legislation.
- 7.12 If a gift of funds to an individual or a trust is made and the result of that gift is that CRS reporting ceases to apply to those funds, and that is a natural consequence of the gift, and the gift is not motivated by an intention to avoid CRS reporting, in our view this should not be caught by Hallmark D1. Our interpretation appears to be consistent with the example of the French bank account in the HMRC guidance IEIM 645010.
- 7.13 If an intermediary advises the trustees on the reorganisation of a trust structure to simplify or streamline reporting obligations under the CRS, we consider that this should not be reportable under DAC6 where the CRS reporting after the reorganisation reflects both the economic reality of the position and the persons who exercise effective control at that time. Examples of this include:
- (a) rationalising a trust structure so that all relevant parties (for example, settlor, trustees, beneficiaries, protectors) and underlying entities are tax resident in the same CRS participating jurisdiction (ongoing reporting will still occur in accordance with the CRS but will be made to the tax authority in one jurisdiction rather than in multiple jurisdictions);
 - (b) restricting a class of beneficiaries of a trust to include only some of those who have previously received benefits, no further economic benefit arising to those who have been removed from the beneficial class;
 - (c) varying the provisions of the trust to remove protectors and other natural persons exercising effective control. However, if the removal of an individual as a protector (or other individual having effective control over the trust) is part of an arrangement whereby such person retains effective control over the trust through other means, but as a result of such removal is not subject to reporting under CRS, this is likely to be inconsistent with the policy behind the CRS legislation and then their removal may be a reportable arrangement.
- 7.14 It is not uncommon for the tax residence of a trust to be changed as a result of the appointment of trustees resident in a different jurisdiction which may be a

non-CRS-participating jurisdiction, for example the US. Similarly, assets may be transferred from a trust established in a CRS-reporting jurisdiction to a US trust where, for example, there is a US settlor. In neither case is this usually carried out for the purposes of circumventing CRS. In relation to the US, the CRS reporting may be different, on the basis that the trust is likely to be treated as a Passive non-financial entity (NFE) rather than a Reporting Financial Institution (FI). However, we consider that this does not undermine the policy intent of the CRS which specifically provides for entities established in non-participating jurisdictions to be treated as Passive NFEs. In these circumstances, the Financial Institution would instead be required to report the controlling persons of the Passive NFE assuming they are located in a reportable jurisdiction.

- 7.15 Suppose trustees ask an advisor to advise them on a proposed restructuring of a trust and, for completeness, the advisor sets out the extent to which the proposed restructuring would have the effect of causing CRS reporting obligations to be reduced in scope or to fall away entirely. Suppose the advisor has finalised the design of the restructuring such that the arrangement could be considered to have been 'made available for implementation' (see 10 below) but the trustees decide not to implement the restructuring arrangement (which could be for a variety of reasons, including the wish not to be considered to be undermining CRS). We consider that the fact that the trustees, having sought advice on a proposed restructuring, decide not to pursue the restructuring could indicate, subject to any evidence to the contrary, that they do not have the subjective intention of circumventing CRS reporting or undermining the policy intent of the CRS legislation, so that Hallmark D1 is not engaged.

8. Hallmark D2: obscuring beneficial ownership (IEIM645020)

- 8.1 Hallmark D2 applies to an arrangement involving a 'non-transparent legal or beneficial ownership chain' with the use of persons, legal arrangements or structures:
- (a) that do not carry on a substantive economic activity supported by adequate staff, equipment, assets and premises; and
 - (b) are incorporated, managed, resident, controlled or established in any jurisdiction other than the jurisdiction of residence of one or more of the beneficial owners of the assets held by such persons, legal arrangements or structures;
 - (c) where the beneficial owners of such persons, legal arrangements or structures, as defined in *Directive (EU) 2015/849*, are made unidentifiable.

It is clear that for Hallmark D2 to be engaged, all four elements of this test must be satisfied. There has to be a 'non-transparent legal or beneficial ownership

chain' that involves persons, arrangements or structures meeting the conditions set out in paras. (a), (b) and (c).

8.2 Paragraph (a): passive vehicles

- (a) The type of entity described in para. (a) is termed a 'passive vehicle' in the Model MDRs. It is to be distinguished from 'active vehicles', i.e., entities carrying on a substantive activity which are supported by adequate staff, equipment, assets and premises.
- (b) The commentary to the Model MDRs notes that a combination of these four elements (staff, equipment, assets and premises) must be directly connected to the activities of the entity itself and not to the activities of another party, in order for an offshore vehicle to be treated as active (and therefore outside the scope of Hallmark D2). Many offshore jurisdictions require resident companies to have sufficient 'substance' in accordance with rules introduced by the EU. Many trusts have underlying companies based in such offshore jurisdictions which are used to hold assets. In our view, where a company satisfies the 'substance' requirements in the relevant jurisdiction for the purpose of that legislation, this should be sufficient to ensure that the company is not to be treated as satisfying the conditions of para. (a); provided that the relevant jurisdiction's rules on economic substance are in line with international standards and are adequately enforced in the relevant jurisdiction.

8.3 Paragraph (b): jurisdiction of residence of the beneficial owners

- (a) For the purposes of para. (b) we consider that, in relation to a trust:
 - (i) The term 'beneficial owner' includes:
 - (1) the settlor (whether or not the settlor can benefit from the trust);
 - (2) the trustees;
 - (3) beneficiaries with current fixed interests in the trust;
 - (4) current discretionary beneficiaries who are named or who fall within a defined class and who have received a distribution from the trust;
 - (5) any protector; and
 - (6) any other natural persons exercising effective control.
 - (ii) However, the term 'beneficial owner' does not include:

- (1) a discretionary beneficiary falling within a defined class who has not received a distribution from the trust; or
- (2) any contingent beneficiaries who can only benefit on the happening of a particular event, e.g. attaining a specified age, the death of another beneficiary or the termination of the trust (unless or until the contingency is satisfied and the beneficiary receives a benefit).

8.4 Objective or subjective test?

- (a) Hallmark D2(c) at first sight looks like a purely objective test. However, we consider that it must be construed in accordance with the policy aim of the hallmark, which is surely to require reporting where arrangements are entered into with the purpose of subverting AML rules on the identification of beneficial owners.
- (b) There is support for this view in the Model MDRs which, as noted above, may be used as an aid to interpreting Hallmarks D1 and D2. The Model MDRs state that 'in general terms, a Passive Offshore Vehicle will fall within the scope of this hallmark where the ownership of that vehicle has been structured so as to not allow the accurate determination of the identity of natural person(s) with ultimate effective control over that vehicle'. This wording indicates that intent is required, i.e., the participants must intend to make the beneficial owners unidentifiable through the arrangement.
- (c) For example, assume that a UK intermediary advises a UK resident but non-domiciled settlor on the formation of a trust for the benefit of the settlor, the settlor's children and remoter issue. The children and remoter issue are not individually named in the trust deed and some are resident outside the UK. The trust is formed in a CRS-reporting jurisdiction so that information regarding the settlor and any beneficiary who receives a distribution who is resident in a reporting jurisdiction will be reported under CRS. The trust is not reported on any trust register because there is no requirement to do so. There is no intention on the part of the intermediary or the settlor to seek to obscure the beneficial owners of the trust. We consider that such an arrangement should not be disclosable. This would also be the case if the trustee was resident in the US so that the trust was a Passive NFE for CRS purposes.

8.5 Informal control arrangements

- (a) The commentary to the Model MDRs addresses a concern with what it terms 'informal control arrangements', meaning arrangements which allow natural persons to indirectly control an offshore vehicle under informal

arrangements with persons who have direct control over that vehicle. It is stated that such arrangements do not allow the accurate identification of the beneficial owner, either by making it difficult to identify the natural persons with direct or indirect control or by creating the appearance that the person with such control is the beneficial owner whereas, in reality, effective control rests with a third party or parties.

- (b) The commentary gives the example of a trustee of a trust who habitually acts on the instructions of another person. We agree that for a trustee to act on the instructions of another person is normally impermissible as a matter of trust law, and may be indicative of what the commentary calls 'informal control arrangements'. However, it should be noted that it is common and indeed normal for a trustee to take account of the wishes and views of other persons, who may include the trust's settlor, protector and beneficiaries. This is obviously not a situation in where the beneficial ownership of the structure is made unidentifiable.
- (c) We consider that in order to satisfy this test, it should be necessary to demonstrate that the other person as a matter of fact exercises effective control over the relevant entity, i.e., is closer to a 'shadow' trustee or protector on the basis that (similar to the 'shadow director' test) that person is a person on whose instructions or directions the actual director or protector is accustomed to act. Where such a person who exercises effective control is, in fact, reported under CRS (as should be the case with a natural person exercising effective control), the arrangement should not be reportable under DAC6.

8.6 Beneficiaries named or identified by membership of a class (IEIM 645020)

- (a) In relation to trusts, the HMRC guidance states that 'where the beneficiaries are named, or identified by class, the beneficiaries would not be considered to be made unidentifiable. For example, a trust where the beneficiaries were Ms X and her future lineal descendants would not automatically meet this hallmark. Similarly, where there is the possibility of beneficiaries being added to a trust in the future, this would not necessarily trigger this hallmark, unless people were deliberately excluded from the trust temporarily to try to avoid being identified'.
- (b) The creation of a trust will not therefore be reportable under Hallmark D2 where the beneficiaries are:
 - (i) named (even as contingent, substitutionary or default beneficiaries);
 - (ii) defined as a class with reference to kinship to a specified individual (or with reference to marriage to, or civil partnership with, members of that class);

- (iii) defined as a class with reference to employment with a named employer.
- (c) The mere existence of a power to add beneficiaries would not trigger Hallmark D2 unless it has been included in the trust instrument in order to obscure the identity of the intended beneficial owner(s) of the trust.

(D) Miscellaneous Points

9. Other persons likely to be affected

9.1 Para. 14(h) of art. 8ab of DAC6 requires the identification of 'any other person in a Member State likely to be affected by the reportable cross-border arrangement'.

9.2 Say a UK intermediary advises a non-EU trustee on an arrangement falling within Hallmark D. The UK intermediary is required to make a report. The trustees will be disclosed as the client of the UK intermediary. We consider that arguably:

- (a) the settlor;
- (b) the protector;
- (c) any natural person exercising effective control; and
- (d) the beneficiaries (i.e., beneficiaries with fixed interests, named discretionary beneficiaries and discretionary beneficiaries described by reference to a class who have received a distribution)

are potentially disclosable in the report as 'other person[s] in a Member State likely to be affected by the reportable cross-border arrangement' but only if, as a matter of fact, the cross-border arrangement does affect the information required to be disclosed under CRS with respect to such persons.

9.3 Where a UK intermediary advises a non-UK company owned by a trust on an arrangement entered into by the company, and the UK intermediary is required to make a report, the company will be disclosed as the client of the UK intermediary. The UK intermediary will also be required to disclose in the report 'any other person in a Member State [who is] likely to be affected by the reportable cross-border arrangement'. However, we consider that provided that there is no direct, material impact of the arrangement on: (i) the tax position of other persons, (ii) the information required to be disclosed under the CRS with respect to other persons, and (iii) the identification of other persons as beneficial owners, then there is no requirement to make such disclosure of other persons. Assuming that these conditions are met, there is no requirement

to disclose in the report persons such as the trust's settlor, its trustees, its beneficiaries and any protector.

10. Meaning of 'made available' (IEIM651010)

10.1 IEIM651010 makes it clear that normally the design of an arrangement must be final before the arrangement can be said to be made available for implementation. The guidance refers to the following hypothetical situation:

- (a) An advisor, in response to a request from a client, provides a high level outline of five different possible solutions to a problem but a lot of the details are not yet known, and would depend on the client's particular circumstances and a more detailed analysis of the relevant laws and regulations to ensure the arrangement works as intended.
- (b) Subsequently, the advisor works with the client to tailor the arrangements to the client's particular circumstances and carries out further analysis of the legal position, but the full tax analysis from the other jurisdiction has not yet been completed. The manual says it is reasonable to conclude that there may still be material changes to the proposed arrangements depending on the outcome of that analysis.

IEIM651010 says that at neither of these points have the arrangements been made available to the client for implementation, as there are still material factors that are still subject to change.

10.2 In the example in IEIM651010 it is only when the client commissions the advisor to finalise the 'designs' and the advisor identifies two viable options and presents those options to the client, that the arrangement is considered to be made available for implementation, as the client could now pick an option and proceed to implement it.

10.3 Suppose that in response to a request from trustees with regard to the restructuring of a trust, an advisor drafts a document (for example an instrument of appointment) which, if executed, would have the effect of reducing reporting obligations under AEOI obligations, but the trustees have not yet been given advice on one or more material factors (e.g., tax, trust law, reporting or other implications of the document). By analogy with what is said at IEIM651010, the advisor cannot, in our view, be said to have made the arrangement available to the trustees for implementation as there is still material advice which has not yet been given (tax, trust law, reporting or other implications of the document) and which, when advised upon, may result in material change to the arrangement.

10.4 In any event, in the above example, even after the point where the restructuring arrangement is considered to have been made available to the trustees for implementation (i.e., after all material advice has been given), we consider that,

as referred to in para. 7 (and subject to para. 7.5), it is only where the participants in the arrangement (the trustees in the above example) form an intention to circumvent or undermine CRS reporting obligations that Hallmark D is engaged, such that the arrangement becomes a reportable cross border arrangement.

11. Will and will trusts

11.1 A will, will trust (also known as a testamentary trust) and other legal arrangement in a will comes into being only after the death of the testator. Before death, the testator may decide to revoke the will completely or to amend it and may decide not to include the trust (or other legal arrangement) provisions at all or to change the terms of the will trust. For this reason, a will and any will trust or other legal arrangement contained in the will should not be considered to be an 'arrangement' for the purposes of DAC6 unless, and until, the death of the testator and the implementation of the provisions of the will.

11.2 We note also that in setting out whether an arrangement is a 'cross-border arrangement' the conditions (a) to (d) of art. 3(18) use the present tense (e.g., 'not all of the participants in the arrangement are resident..' and 'such arrangement has a possible impact on the automatic exchange of information or the identification of beneficial ownership') and that will trusts and other legal arrangements to be set up by will are only intended to take effect at some point in the future.

11.3 The death of the testator and the existence of the terms of the trust or other legal arrangement in the will should neither mean that an arrangement is made available for implementation nor that the first step in the implementation of the reportable cross-border arrangement has been made. The trigger for disclosure would be when the first step in the implementation of the will trust or other legal arrangement is actively made, which could, for example, be that the will trustees agree to act or the design of the trust is finalised. However, we do not consider that the will trust need actually be funded for the first step to occur.

12. Intermediaries and service providers (IEIM621010)

12.1 The definition of intermediary also means any person who, having regard to the relevant facts and circumstances and based on available information and the relevant expertise and understanding required to provide such services, knows, or could be reasonably expected to know, that they have undertaken to provide, directly or by means of other persons, aid, assistance or advice with respect to designing, marketing, organising, making available for implementation or managing the implementation of a reportable cross-border arrangement (otherwise known as a 'service provider'). However, a person can provide evidence that they did not know and could not reasonably be expected to know

they were involved in a reportable cross-border arrangement. For this purpose, they may refer to all relevant facts and circumstances as well as available information and their relevant expertise and understanding. See IEIM621050 and 621060.

- 12.2 The HMRC guidance at IEIM621050 states that 'a person who subsequently becomes aware of an arrangement, for example if an auditor, examining a company's accounting records, identifies a transaction which is reportable' would not be an intermediary (as long as that person did not do anything else so as to fall within the intermediary category).
- 12.3 It seems consistent with this guidance therefore that, for example, a person who begins providing advisory or other services in relation to the exercise of trustees' powers and discretions or the administration or taxation of the trust, after it has been set up, will not need to consider whether the arrangement that resulted in the setting up of the trust was a reportable cross-border arrangement or (if it was) whether a report was made.
- 12.4 When advising clients in relation to trusts and company structures the advisor will usually be acting for the client directly. However, in some cases the advisor may be instructed by an agent of the client e.g., a family office. Where a person acts as an agent of a client in obtaining advice for the client and passes that advice on to the client, and that agent does not provide advice in relation to the arrangement or aid or assistance in relation to the arrangement other than acting as agent, that person should not be regarded as an intermediary for the purposes of DAC6. For example, if a family office collates third-party advice and passes it on to the client, the family office would not be an intermediary. However, if the family office collates advice and provides a recommendation, the family office could be an intermediary.

13. Ongoing monitoring/reporting requirement? (IEIM653000)

13.1 The aid, assistance or advice needs to be given with respect to the implementation of a reportable cross-border arrangement. Suppose a UK law firm provides services with respect to the creation of the trust and, at the time of creation of the trust, there is no reporting obligation under DAC6 because:

- (a) neither the settlor nor the trustee are resident outside the UK (i.e., the participants are all resident in the same country); and
- (b) none of the beneficiaries are resident outside the UK

So there is no AEOI from one country to another and as the arrangement does not 'concern' more than one Member State, or a Member State and another country, it is not a cross-border arrangement.

13.2 Suppose the UK law firm continues to provide services to the trust after it has been set up and circumstances change (e.g., the settlor or one of the beneficiaries becomes resident outside the UK) and the trust now 'concerns' a Member State and another country. We consider that the UK law firm does not have an obligation to report the trust arrangement merely due to this change in circumstances which arose after the trust was set up. However, the UK law firm would need to consider going forwards whether any new arrangement entered into by the trust was a reportable cross-border arrangement on the basis that the trust now 'concerns' a Member State and another country.

14. Relevant taxpayers in relation to trusts (IEIM622000-IEIM622020)

14.1 A 'relevant taxpayer' means any person to whom a reportable cross-border arrangement is made available for implementation, or who is ready to implement a reportable cross-border arrangement or has implemented the first step of such an arrangement (art. 3(22) of DAC6). A relevant taxpayer is only potentially under a reporting obligation if there is no intermediary, or legal professional privilege is available and precludes reporting by any intermediary.

14.2 A typical trust structure has various entities through which it holds assets and a number of people involved in terms of control and/or beneficial interest. The intermediary may act, for example, for one or more of:

- (a) the trustees;
- (b) the settlor;
- (c) the protector;
- (d) any natural person exercising effective control;
- (e) the beneficiaries; or
- (f) a company or other holding vehicle owned by the trust.

14.3 We consider that the definition of relevant taxpayer encompasses any person who is the client of the intermediary or who otherwise implements the arrangement as a party to it. In a trust context, relevant taxpayers may include the settlor (if a party to the arrangement, for example on the creation of the trust), the trustees, and any protector whose consent is required for the implementation of the arrangement. We consider that the definition of relevant taxpayer does not, however, include the beneficiaries, any protector, or any other person where, with regard to each of those persons, that person's involvement is not required for implementation of the arrangement. A beneficiary who is a party to the arrangement, for example on the basis that the beneficiary needs to give their consent for the arrangement to be effected or who exercises effective control over the trustees, will be a relevant taxpayer,

but a beneficiary will not be a relevant taxpayer in the case where they are not a party to the arrangement. Even where a beneficiary is not a relevant taxpayer, they could be a person 'likely to be affected by the reportable cross-border arrangement' within the meaning of para. 14(h) of art. 8ab of DAC6 (see para. 9 above).

- 14.4 Where the arrangement is entered into solely by the trustees, we consider that the settlor, beneficiaries, protector or natural person exercising effective control should be not treated as a relevant taxpayer. This is on the basis that the advice was given to, and the arrangement made available to and implemented by, the trustees.
- 14.5 Where the arrangement is entered into by the company or holding vehicle owned by the trust and the consent of the trustees as shareholder is not required for the purpose of entering into the arrangement, we consider that the company or holding vehicle should be treated as the relevant taxpayer and the trustees (or other parties identified in paras. 14.2(a) to 14.2(e) above) should not be treated as a relevant taxpayer.

15. **Meaning of 'associated enterprise'⁸ in a trust context**

- 15.1 For the purposes of the associated enterprise test, we consider that a beneficiary of a trust should not normally be treated as having a 'right of ownership' (as referred to in art. 3(23)(c) of the Directive) in underlying property held by the trustees nor as having an entitlement to the profits of an entity in

⁸ Under Art 3(23) DAC6, an 'associated enterprise' is defined as a person who is related to another person in at least one of the following ways:

- (a) a person participates in the management of another person by being in a position to exercise a significant influence over the other person;
- (b) a person participates in the control of another person through a holding that exceeds 25% of the voting rights;
- (c) a person participates in the capital of another person through a right of ownership that, directly or indirectly, exceeds 25% of the capital;
- (d) a person is entitled to 25% or more of the profits of another person.

If more than one person participates, as referred to in points (a) to (d), in the management, control, capital or profits of the same person, all persons concerned shall be regarded as associated enterprises.

If the same persons participate, as referred to in points (a) to (d), in the management, control, capital or profits of more than one person, all persons concerned shall be regarded as associated enterprises.

For the purposes of this point, a person who acts together with another person in respect of the voting rights or capital ownership of an entity shall be treated as holding a participation in all of the voting rights or capital ownership of that entity that are held by the other person.

In indirect participations, the fulfilment of requirements under point (c) shall be determined by multiplying the rates of holding through the successive tiers. A person holding more than 50% of the voting rights shall be deemed to hold 100%.

An individual, his or her spouse and his or her lineal ascendants or descendants shall be treated as a single person.

which the trustees may have an interest (as referred to in art. 3(23)(d) of the Directive). This is, however, subject to the specific terms of the trust.

- 15.2 In circumstances where the same corporate trustee of a number of unrelated trusts has shares in a company and, as trustee of each trust, owns less than 25 per cent of the shares of the company (but together the trustee holds more than 25 per cent of the shares) we consider that for the purpose of calculating the 25 per cent test, it is not necessary to combine the voting rights held by the trustee with respect to each trust; unless part of the arrangement involved dividing up the voting rights among separate trusts for the purpose of ensuring that the 25 per cent test is not met.

STEP Technical Committee, 12 November 2020