FATCA: practical examples

This guidance is relevant for all UK trusts and trustees, whether or not they have any known US connections.

All UK trusts are entities; their status under FATCA needs to be determined. The status can either be that the entity is a Financial Institution or it’s not. UK trusts will have to declare their status to any Financial Institution with which they have dealings. Whether a UK trust is a Financial Institution or not depends on a number of different factors; importantly this is not based on the US connections of the settlor, beneficiaries or on the ownership of any US assets by the trust.

Working through the FATCA guidance (issued jointly by The Law Society, ICAEW and STEP) will assist UK trusts in determining their FATCA Status. The guidance below is to run through some common examples of UK trusts that practitioners may come across in practice.

The numbering in each of the examples below corresponds with the questions posed in the FATCA flowchart and include:

- Question 1: Is the trust a UK tax resident?
- Question 2: Is the trust a charitable trust?
- Question 3: Is the trust acting for customers and is more than 50 per cent of the trust’s gross income attributable to trading in money market instruments, portfolio management or the investment and administration of funds?
- Question 4: Is the trust ‘managed’ by an entity which acts for customers and where more than 50 per cent of gross income is attributable to trading in money market instruments, portfolio management or the investment and administration of funds?
- Question 5: Is more than 50 per cent of the trust’s income attributable to investing, reinvesting or trading in financial assets?

1. ‘£10’ Pilot trusts

For sensible wealth planning reasons, a wealthy client of your firm created a series of pilot trusts. These trusts are all of a standard discretionary nature with three family members as lay trustees and a pool of beneficiaries drawn from the client’s wider family. Each trust was constituted with a £10 note, which was stapled to the relevant deed and placed in your firm’s vaults.

Q1. These trusts are UK tax resident and therefore subject to UK Intergovernmental Agreement (IGA) reporting; a determination of status under FATCA must be made by the trustees.

Q2. These trusts are not charitable trusts and therefore the charitable trust exemption does not apply.

Q3. These trusts are family trusts; as such they are not undertaking activities on behalf of a customer.
Q4. These trusts are not managed as the trust property (the ‘£10’ note) is stapled to the trust deed. The trustees are lay family members and therefore not Financial Institutions themselves and no other management of assets takes place.

Q5. No income arises to these trusts and therefore the trust status under FATCA is that they are Non-Financial Foreign Entities (NFFEs). The trust does not need to register or report to the IRS.

A note of this outcome should be placed with each trust deed. A note must be made to review the FATCA status of each trust when circumstances change. It is not until each trust receives more assets (for example lump sums that are payable either under a pension scheme or under a company’s death in service scheme) that it becomes necessary to review each trust’s circumstances and therefore status under FATCA.

2. Nil-rate band discretionary trust established after a first death of a couple

Prior to the creation of the transferable nil-rate band, clients of your firm created wills with nil-rate band discretionary trusts within them as part of estate planning with the aim of reducing liability to inheritance tax (IHT) on the death of a surviving spouse. The trusts were created with lay trustees and a pool of beneficiaries including the surviving spouse and the deceased’s wider family. One of the clients has subsequently died and these trusts have been constituted following the first death with various assets up to the available nil-rate band. Three main possibilities exist for the type of assets used to fulfil the available nil-rate band: i) a debt/charge scheme; ii) cash; and iii) land/property.

Q1. These trusts are UK tax resident and therefore subject to UK IGA reporting; a determination of status under FATCA must be made by the trustees.

Q2. These trusts are not charitable trusts and therefore the charitable trust exemption does not apply.

Q3. These trusts are family trusts; as such they are not undertaking activities on behalf of a customer.

Q4. Each of the three main asset classes should be looked at in turn:

i. a debt/charge scheme is not managed as the trust property (the debt/charge) is only the right to receive or recover the debt. Typically interest is not charged and trustees have the right to waive the payment of interest. The trustees are lay family members and therefore not Financial Institutions themselves and no other management of assets takes place;

ii. where the cash equivalent of the nil-rate sum is held by the trustees, they must ensure that trust property is properly invested and therefore it is unlikely to be left as cash in a bank account. If it was just placed and left on deposit at a UK bank, however, then it is not managed, as UK bank accounts are exempt and are not reportable under FATCA (other exempt products include National Savings and Investments products and Premium Bonds).

iii. land/property held in the name of the deceased (typically a half-share of the jointly owned property) that has been transferred into the name of the trustees; the trustees under the terms of the trust allow the surviving joint owner to reside in the property rent free. These trusts are not managed. The trustees are lay family members and therefore not Financial Institutions themselves and no other management of assets takes place.

Q5. No income arises to these trusts and therefore the trusts’ status under FATCA is that they are all NFFEs. These trusts do not need to register or report to the IRS.

A note of this outcome should be placed with each trust deed. A note must be made to review the FATCA status of each trust when circumstances change, typically when the death of the survivor
occurs. When the surviving spouse passes away it becomes necessary for the trustees to review each trust’s circumstances and therefore the trust’s status under FATCA.

3. **Trusts of land**

Your firm acts for a number of clients who own property in England & Wales jointly as co-owners. Trusts of land arise where ownership of land is by more than one person whether the co-owners are beneficial joint tenants or tenants in common.

Q1. These trusts are UK tax resident and therefore subject to UK IGA reporting; a determination of status under FATCA must be made by the trustees.

Q2. These trusts are not charitable trusts and therefore the charitable trust exemption does not apply.

Q3. These trusts are arrangements between co-owners; as such they are not undertaking activities on behalf of a customer.

Q4. These trusts are not managed, the asset is usually non-income-producing. The trustees are the co-owners and therefore not Financial Institutions themselves and no other management of assets takes place.

Q5. No income arises to these trusts and therefore the trusts’ status under FATCA is that they are all NFFEs. These trusts do not need to register or report to the IRS.

4. **Legacy trusts held on an age contingency**

Your firm acts on behalf the executors of a deceased estate that is near completion. A legacy of £1,000 is due to a beneficiary upon attaining 18. The beneficiary is currently 16. An account is opened with a bank in the name of the personal representatives as trustee for the beneficiary and the £1,000 deposited in the account.

Q1. The trust is UK tax resident and therefore subject to UK IGA reporting; a determination of status under FATCA must be made by the trustees.

Q2. The trust is not a charitable trust and therefore the charitable trust exemption does not apply.

Q3. This is a purpose trust; as such it is not undertaking activities on behalf of a customer.

Q4. UK bank accounts for this purpose are exempt and are not reportable under FATCA. The trustees are lay family members and therefore not Financial Institutions themselves and no other management of assets takes place.

Q5. Although income may arise to the trust, it is not attributable to investing and therefore the trust status under FATCA is a NFFE. The trust does not need to register or report to the IRS. The trust will be reported upon by the bank as a Financial Institution.

5. **Family trust invested with a discretionary fund manager**

Your firm acts for a number of wealthy UK-based families who hold significant assets within trust structures. The assets are invested on behalf of the trustees with a discretionary fund manager at a prestigious financial institution.

Q1. These trusts are UK tax resident and therefore subject to UK IGA reporting; a determination of status under FATCA must be made by the trustees.
Q2. These trusts are not charitable trusts and therefore the charitable trust exemption does not apply.

Q3. These trusts are family trusts; as such they are not undertaking activities on behalf of a customer.

Q4. The trust funds are managed by a discretionary fund manager who is, for the purposes of the FATCA Regulations, a Financial Institution. The trust is therefore a Financial Institution. The trustees can either register and report the trust themselves to the IRS or the trustees can seek that the discretionary fund manager sponsors the trust and undertakes the FATCA compliance on behalf of the trust.

6. **Scenarios 1 to 5, but with a US-connected settlor/trustee/beneficiary**

   Under the FATCA rules, trusts are included within the definition of foreign entity. The trust can be classified as a Financial Institution or NFFE. The classification under scenarios 1 to 5 does not alter whether or not the trust has US connections.

7. **Scenarios 1 to 5, but with a corporate trustee**

   Under FATCA, where trusts with corporate trustees exist the trustees will need to register and report on the trust. This is the case even if the outcome above was that the trust fell into the NFFE category. All trusts under scenarios 1 to 5 are Trustee Documented Trusts, the corporate trustee registers and reports on the trust; the individual trusts do not need to register or report.