FATCA – GUIDANCE TO MEMBERS
ACTION REQUIRED

August 2014

1. INTRODUCTION

This paper summarises the key aspects of the Foreign Account Tax Compliance Act (FATCA) and alerts members of professional firms to the action needed at various points over the coming months to ensure that your firm, its partners and its associated entities are properly meeting their obligations under the new rules and that you are able to discuss them with your clients. A timetable of key dates is included in Appendix I.

Who is affected?

• Any person who acts as a trustee.
• Any firm which is a Foreign Financial Institution referred to hereafter as a Financial Institution (FI) (there is a wide definition of this, see Section 2).
• Any accountant or lawyer who is or has clients who are in these categories.

What is FATCA?

FATCA is part of a larger piece of legislation (Hiring Incentives to Restore Employment Act) introduced in the United States in 2010 to ensure that that country’s citizens are fully disclosing their worldwide income to the Internal Revenue Service (IRS). It has spawned a number of international agreements being adopted primarily in the Crown Dependencies and Overseas Territories, while the Organisation for Economic Cooperation and Development (OECD) is also working on an international disclosure process. There will be further developments in this area of disclosure but in this Guidance Note we concentrate on FATCA.

The key point to be clear about is that as a result of the UK-US intergovernmental agreement (IGA), the legislation is now part of UK law through s222 Finance Act 2013 and the regulations issued under that section. There are consequences for default – both financial and reputational.

Even if you have no US clients there is action that you need to take now.
How does it work?

The IRS is unconvinced that ‘recipient based’ measures such as Foreign Bank Account Reporting (FBAR) are enough to protect their tax base. FATCA has been introduced to put a reporting burden on the payer of monies.

All UK entities are subject to the UK rules and you will find that you will be asked for your FATCA status with the usual anti-money laundering and client identification processes when dealing with other institutions such as banks, etc. and will need to be familiar with the detailed requirements. Failure to comply may mean you are not able to open or operate bank accounts, etc.

The effect of the legislation is to place an obligation on Financial Institutions (FIs) to inform the IRS when any sums are paid to or for a US person, regardless of where in the world the payment is made. Additionally, the IRS must be assured that the FI has adequate systems in place to identify and record US Persons. If there is a failure to report or any other non-compliance with the regime the payer will be in default. It is understood that penalties may be imposed and any sums paid to the FI will be subject to penal rates of withholding taxes (30 per cent), which the FI may have to bear, rather than the underlying client.

The major impact of FATCA will fall on banks and investment houses but it is essential to understand that firms such as yours are directly affected, even if you only have UK clients.

As partners (or as directors, administrators and trustees) you have direct UK legal obligations that must be met if you are to avoid financial (and reputational) penalties. The full guidance is available at http://www.hmrc.gov.uk/drafts/uk-us-fatca-guidance-notes.pdf. This is referred to as the UK guidance in the remainder of this Guidance Note, which attempts to distil the key elements into an overview.

This note cannot be comprehensive and you should ensure that you understand and meet your particular obligations. It will be in your interest to ensure that your clients are aware of their obligations as well.

So what do I have to do?

- Identify and classify the entities comprising your practice and the client entities with which you are connected such as trusts;
- Register any FI for a Global Intermediaries Identification Number (GIIN);
- Review your practice systems and implement any necessary changes to:
  1) engagement letters
  2) client take-on process
  3) client identification
  4) establishing reportable transactions
  5) effecting the report
  6) client communications;
- Make the appropriate reports to HMRC.

The deadline is October 2014, by which time you need to register any FIs with the IRS as an FI. At that time you will also need to demonstrate that you have adequate systems in place to identify and record US Persons. The first reporting will be for the calendar year...
2015, but systems will need to be put in place now. The mechanics of reporting, which will be to HMRC, are not yet known.

The remainder of this note provides more information on these points.

2. DETAILED CONSIDERATIONS

Entity Classification

Entities will be either FIs or Non-Financial Foreign Entities (NFFE).

An entity is an FI if it is one of the following:

- A Depository Institution – one that accepts deposits in the ordinary course of a banking or similar business.
- A Custodial Institution – holds financial assets on behalf of others as a substantial portion of its business (more than 20 per cent of gross income). Some trust companies and nominees are included in this category.
- An Investment Entity – either trading in financial assets or ‘otherwise investing administering or managing money or funds on behalf of other persons’ (more than 49 per cent of gross income) or acting as an investment advisor. In addition entities managed by an FI or whose assets are managed by FIs may be Investment Entities. Some family trusts and some trust companies will fall into this category.
- Specified Insurance Companies – one that issues cash value insurance or annuity contracts.
- Holding Companies and Treasury Centres – ones where the primary activity is holding the stock of at least one entity that is an FI.

If the entity is not an FI it is a NFFE. FIs are further divided into reporting and non-reporting institutions (not to be confused with the UK income tax concept of reporting and non-reporting funds).

You will need to apply these definitions to each element of your practice and clients with which you are associated. In particular, you should note that under the HMRC guidance family trusts are usually investment entities for these purposes. The particular rules for trustees are covered in Section 3.

In all cases, this guidance is concerned with UK resident entities. In most cases this will be readily apparent, but where it is not clear, the UK definition of tax residence determines the matter. Non-UK resident subsidiaries and branches are outside the scope of the UK agreement. UK permanent establishments of non UK entities are within the UK agreement.

Entities are related if they are under common control (direct or indirect ownership of more than 50 per cent of vote and value). Related entities can be relevant if there are any Non-Participating Financial Institutions (NPFI) in the group. A NPFI is one which is an FI but chooses not to comply or is unable to, as a result of the jurisdictions in which it operates. There are numerous issues surrounding NPFI that cannot be covered here but are explained in the UK guidance.
If an entity is an FI then it will need to carry out the required reporting and compliance, whereas a NFFE will certify its status to the FI with which it has a relationship (using a form W-8BEN), which will in turn undertake the reporting and compliance. This distinction is particularly important when considering the issue of trusts.

**Registration**

Having established which of your practice entities is an FI and also if there are any clients (particularly trusts) that are FIs, it will be necessary to register them for a GIIN.

Registration with the IRS is carried out online by completing Form 8957 [http://www.irs.gov/pub/irs-ut/f8957.pdf](http://www.irs.gov/pub/irs-ut/f8957.pdf). The GIIN is issued and then needs to be supplied to other institutions as evidence that you are compliant. This is the reference number that you will report under. Guidance on completion of the form is available at the same link but you should be aware that this is an IRS form and IRS guidance is written from an American perspective. You should ensure that you understand fully the questions being asked and the correct response for a UK entity, bearing in mind the UK guidance.

Banks and financial institutions have already started to write to clients and their advisors about FATCA. In some instances they have erroneously written to UK advisors about trusts and companies that are resident outside the UK. The IGA between the UK and US may not be relevant to these clients; these entities may well be governed by a similar agreement between the US and the government of the jurisdiction in which they are either resident or administered.

Financial institutions will ask for GIINs (where the entity is an FI) or confirmation (using a W-8BEN form) that the entity is a NFFE. Banks and other institutions will ultimately be unable to operate accounts for any trust or client without this. The first tranche of registrations has to be submitted by 5 May 2014 with the list of registered entities being published in June 2014. This is an optional registration date, but all FIs must be registered on the list to be published at 31 December 2014 so that withholdings will begin at 1 January 2015. To ensure that the registration has been processed in time for inclusion on that list the **last practical date for registration is 25 October 2014**.

**Practice management**

Overall responsibility will be given to a Reporting Person and that individual will carry the primary burden of reporting.

Essentially you will have to fulfil the following aims:

1) Identify and record US Persons
2) Identify and record payments to or for those persons
3) Report the items in 2) to the authorities.

You need to note the definition of a US person and be familiar with the concept of US indicia (see below) and use this to establish whether there are any US Persons as clients or as beneficiaries or settlors of trusts.
This has a number of ramifications and you should consider the following as a bare minimum, although there may well be further adaptations to consider depending on your particular circumstances.

1) Engagement letters – it will be important to ensure that your engagement letters set out clearly the ambit of your work. If you are acting for a trust or other FI client, you should be clear as to any FATCA compliance work you are assuming for them or whether there will be none at all. You should also set out that the client will be responsible for advising you of any changes in their FATCA status or if there are any changes in their US connections.

The engagement letter will also need to deal with data protection issues as it may be necessary for you to share the client’s FATCA status and GIIN with other financial institutions and make appropriate reports to HMRC.

2) Client take-on – in addition to the usual know-your-client information, you will need to determine if your client has any US connections and record the information carefully. As similar agreements are entered into with other jurisdictions, it is recommended that procedures are put in place now to record any foreign connections. You will be required to ensure you have current valid ID for each client so you will also need to consider how this can be monitored. Changes of circumstance may have consequences for FATCA status or the information to be reported. You will also need to establish and record tax residence status. Accountants should carry out an annual check as part of the tax return or accounts preparation process, but lawyers may need to put different systems in place.

3) Client identification – whether or not a person is a US person will be determined by the use of so-called US indicia. These include the following:

- US citizenship or lawful permanent resident (green card) status;
- A US birthplace;
- A US residence address or a US correspondence address (including a US PO box);
- Standing instructions to transfer funds to an account maintained in the United States, or directions regularly received from a US address;
- An ‘in care of’ address or a ‘hold mail’ address that is the sole address with respect to the client; or
- A power of attorney or signatory authority granted to a person with a US address.

Having one of these indicia does not mean that the account is owned by a US person, only that it must be given closer scrutiny. If a US person is found, there is prescribed documentation to be held as follows:
### US Indicia Documentation Required

Having established those of your clients which are US Persons under this definition, you need to ensure that your take-on and monitoring systems are updated on a regular basis. You should also be aware that if you have a computer searchable database the integrity of the database could be examined in compliance checks. The professional bodies consider that staff training similar to that currently dealing with money laundering should be carried out. Staff must be educated on take-on procedures and the need to ensure that information is up to date.

**Example**

You have a client who sells a business and is minded to create a trust for his adult children. A partner of your firm is trustee. In a subsequent year one of the adult children marries a US citizen. The terms of the trust may automatically include the new spouse as a beneficiary or they may be specifically added. Any grandchildren born to that marriage will be US Persons. You need systems that are reliable enough to identify such events and possibilities.

Any distributions made to those grandchildren will be FATCA reportable by the trustees. If the trustees are your clients, you could be negligent if you do not advise them of their reporting obligations.

If there is no computer database, paper records such as copy passports, etc., must be maintained. However, in an advance from money laundering records, and as noted above, the supporting document must be in date and valid at all times. Thought will need to be given as to a workable system of recording, monitoring and taking action at expiry dates.

Reporting the actual payment will need to be considered in due course and further information can be issued once the UK reporting process has been established and guidance published by HMRC.

<table>
<thead>
<tr>
<th>US citizenship or lawful permanent resident</th>
<th>Obtain W-9</th>
</tr>
</thead>
<tbody>
<tr>
<td>US birth place</td>
<td>Obtain W-9 or W-8BEN; and non-US passport or similar documentation establishing foreign citizenship; and written explanation regarding US citizenship</td>
</tr>
<tr>
<td>US address (residence, correspondence, or PO box)</td>
<td>Obtain W-9 or W-8BEN; and non-US passport or similar documentation establishing foreign citizenship</td>
</tr>
<tr>
<td>Instructions to transfer funds to US accounts or directions regularly received from a US address</td>
<td>Request W-9 or W-8BEN; and documentary evidence establishing non-US status</td>
</tr>
<tr>
<td>Only address on file is 'in care of' or 'hold mail' or US PO box</td>
<td>Request W-9, W-8BEN; or documentary evidence establishing non-US status</td>
</tr>
<tr>
<td>Power of Attorney or signatory authority granted to person with US address</td>
<td>Request W-9, W-8BEN; or documentary evidence establishing non-US status</td>
</tr>
</tbody>
</table>
Documents relating to the due diligence process for each client must be retained for six years following the end of the year in which the status was established.

3. Particular rules relating to trusts

Firms’ trust clients will broadly fall into two categories:

1. Those where either a principal or a trust company owned by the firm is a trustee.
2. Clients of the firm where no principal or subsidiary is a trustee.

In the first situation, the firm or principal will be required to take responsibility for FATCA matters. In the second case, although their FATCA status, monitoring and reporting will be a matter for the Trustees, firms advising such clients will need to be clear as to the extent of their obligation and ability to do so.

Registration requirements

All trusts are caught by FATCA irrespective of whether or not they have US Persons as settlors, trustees or beneficiaries, or US assets.

As with firms themselves, the starting point will be to determine the FATCA status of each trust and where the trust is a FI register and obtain a GIIN.

The requirement to do so will depend on the nature of the trust, the composition of the trustees, the underlying assets and who manages the assets. A flow-chart is attached in Appendix II that will provide some guidance. Appendix III sets out some common scenarios with an illustrative FATCA analysis but it is important to recognise that every trust will need to be considered and a note of the examination and conclusion should be retained.

The fact that a trust has a US-connected settlor or trustee or beneficiary does not alter the categorisation for FATCA purposes. It may, however, alter the reporting requirements and in the case of a US trustee, there may be more of a question over the residence of the trust.

Corporate trustees

Where there is a corporate trustee, it registers and reports on the trust; the individual trusts do not need to register or report. It may be worth considering whether there is merit in appointing a corporate trustee in place of or in addition to the individual trustees to eliminate the need for the individual trust to register and report. The responsibility for doing so is passed to the corporate trustee. In this situation the trust itself becomes known as a Trustee Documented Trust.

Where the firm or its principal acts as a trustee, the practice management issues raised in Section 2, are of particular importance.
Owner documented trusts

Instead of registering it may be possible for trustees to opt for owner documented status. They can only do so without challenge if they have enough regular information to prove that all owners (beneficiaries who receive one or more distributions) are and remain non-US Persons.

They will also have to recertify their status every three years via form W8-BEN-E and if at any time the trustees become aware that an owner has become a US person, they will have to register with the IRS and report to HMRC in the normal way. Further, they will need to appoint a withholding agent. It is understood that banks and investment businesses, which already act as Qualifying Intermediaries for US tax purposes, are currently considering whether they will be prepared to offer this service. The current indications are that they will do so.

Trustees must notify withholding agents of any change in status within thirty days. They will need to have systems and procedures in place to ensure that this is adhered to.

Creation of new trusts

The current regulations are unclear as to the deadline for obtaining a GIIN or otherwise regulating the FATCA status of trusts created after October 2014, i.e. once the first set of registration is completed. Taking into account the requirements of banks and other institutions to be able to operate accounts, the advice must be that FATCA status, and registration as necessary, should be an integral part of the process for creating any new trust and completed as soon as practicable.

There is a particular point of concern surrounding executors. Executors themselves are not entities within FATCA and will therefore be reported upon as usual. There is one exception in that the accounts of deceased persons are not reportable accounts as long as the FI concerned is in possession of the death certificate. However, it is not uncommon for executors to become the trustees of a will trust and the point of transition between the two can be difficult to identify with precision. Practitioners will need to be alert for this circumstance and ensure that the appropriate steps are taken in good time, including whether a corporate trustee should be appointed, and align with the records at banks and investment managers etc.
APPENDIX I
FATCA IGA TIMETABLE

**FIs registration with IRS**

<table>
<thead>
<tr>
<th>Year</th>
<th>Date</th>
<th>Event</th>
</tr>
</thead>
<tbody>
<tr>
<td>2014</td>
<td>5 May</td>
<td>Deadline for registrations to appear on initial list of FIs to be published in June</td>
</tr>
<tr>
<td></td>
<td>2 June</td>
<td>Initial list of registered entities published</td>
</tr>
<tr>
<td></td>
<td>25 October</td>
<td>Likely last practical date for registration to meet 1 January 2015 deadline*</td>
</tr>
<tr>
<td>2015</td>
<td>1 January</td>
<td>Withholding begins</td>
</tr>
</tbody>
</table>

*While the IRS has not published a firm final date by which FIs must register, FIs in Model 1 IGA jurisdictions such as the UK must be able to confirm GIINs by 1 January 2015 to avoid withholding.

**We would therefore recommend registration by 25 October 2014.**
<table>
<thead>
<tr>
<th>Reporting Year</th>
<th>In respect of</th>
<th>Information to be reported</th>
<th>Reporting date to HMRC</th>
</tr>
</thead>
<tbody>
<tr>
<td>2014</td>
<td>• Each Specified US Person either holding a Reportable Account Or • as a Controlling Person of an Entity Account</td>
<td>• Name • Address • US TIN (where applicable or DoB for Pre-existing Accounts) • Account number or functional equivalent • Name and identifying number of Reporting Financial Institution • Account balance or value</td>
<td>31 May 2015</td>
</tr>
<tr>
<td>2015 As 2014, plus the following:</td>
<td>• Custodial Accounts</td>
<td>• The total gross amount of interest; • The total gross amount of dividends; • The total gross amount of other income paid or credited to the account</td>
<td>31 May 2016</td>
</tr>
<tr>
<td></td>
<td>• Depository Accounts</td>
<td>• The total amount of gross interest paid or credited to the account in the calendar year or other reporting period</td>
<td></td>
</tr>
<tr>
<td></td>
<td>• Other Accounts</td>
<td>• The total gross amount paid or credited to the account including the aggregate amount of any redemption payments made to the account holder during the calendar year or other appropriate reporting period</td>
<td></td>
</tr>
<tr>
<td>2016 As 2015, plus the following:</td>
<td>• Custodial Accounts</td>
<td>• The total gross proceeds from the sale or redemption of property paid or credited to the account</td>
<td>31 May 2017</td>
</tr>
<tr>
<td>2017 onwards</td>
<td>• All of the above</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

APPENDIX II
UK TRUSTS UNDER THE UK/USA INTERGOVERNMENTAL AGREEMENT (IGA)

See flowchart associated with this text at:


Section A: Is the trust a Financial Institution or an NFFE?

Question 1:

Is the trust UK tax resident?
If ‘yes’, go to Question 2.
If ‘no’, the trust is not subject to the UK IGA but may be subject to reporting either under US FATCA regulations or under an another IGA. Only UK tax resident trusts fall under the UK/US IGA.

‘If all the trustees are resident in the UK for tax purposes then the trust is UK resident. Where some of the trustees, but not all are UK tax resident then the trust is to be treated as UK resident if the settlor is both resident and domiciled in the UK for tax purposes.’ (UK Guidance, p11)

Residence is to be determined in accordance with established UK principles. HMRC guidance on trustee residence can be found at:

http://www.hmrc.gov.uk/manuals/tsemmanual/attachments/tsem1461_appendix1.doc
and
http://www.hmrc.gov.uk/cnr/nr_trusts.htm#1

Question 2:

Is the trust a charitable trust?
If the answer is ‘no’, go to Question 3.
If ‘yes’, the trust is a Deemed Compliant Financial Institution. The trust is categorised as a Non-Reporting United Kingdom Financial Institution and does not need to register or report under FATCA.

This applies to:

‘a. Any entity registered as a charity with the Charity Commission of England and Wales
b. Any entity registered with HMRC for charitable tax purposes
c. Any entity registered as a charity with the Office of the Scottish Charity Regulator.’

(UK Regulations Annex II.II.A

The UK Regulations are silent on the issue of charities regulated by the Charity Commission for Northern Ireland.
Question 3:
Does the trust carry on business in the UK and is 50 per cent or more of the trust’s gross income attributable to trading in money market instruments, etc., portfolio management or the investment and administration of funds?

If the answer is ‘no’, go to Question 4. Family trusts will generally not be carrying on business, so most will pass on to Question 4.

If the answer is ‘yes’ the trust is an Investment Entity and therefore a Financial Institution. The trust may need to register with the IRS as a Foreign Financial Institution and report (see Section B).

‘The term ‘Investment Entity’ means any entity that conducts as a business (or is managed by an entity that conducts as a business) one or more of the following activities or operations for or on behalf of a customer:

(1) trading in money market instruments (cheques, bills, certificates of deposit, derivatives, etc.); foreign exchange; exchange, interest rate and index instruments; transferable securities; or commodity futures trading;

(2) individual and collective portfolio management; or

(3) otherwise investing, administering, or managing funds or money on behalf of other persons.’


An Investment Entity ‘conducts as a business’ in this context ‘if the entity’s gross income attributable to such activities is equal to or exceeds 50 per cent of the entity’s gross income during the shorter of:

- The three-year period ending on 31 December of the year preceding the year in which the determination is made; or
- The period during which the entity has been in existence.’ (UK Guidance, Section 2.28 http://www.hmrc.gov.uk/fatca/130814-guidance.pdf)

Question 4:
Is more than 50 per cent of the trust’s income attributable to investing, reinvesting or trading in financial assets?

If the answer is ‘no’, the trust is a Non-Financial Foreign Entity (NFFE). See Section C.

If the answer is ‘yes’, the trust may be an Investment Entity subject to the answer to Question 5.

UK Guidance highlights that a trust ‘whose assets consist of non-debt direct interests in real property or land, even if managed by another Investment Entity, would not be an Investment Entity’. (UK Guidance, Section 2.28, p40)

Question 5:
Is the trust ‘managed’ by an entity carrying on business in the UK where more than 50 per cent of gross income is attributable to a business trading in money market instruments, etc., portfolio management or the investment and administration of funds.

If the answer is ‘no’, the trust is a Non-Financial Foreign Entity (NFFE). See Section C below.
If the answer is ‘yes’, the trust is an Investment Entity and therefore a Financial Institution and may need to register with the IRS. See Section B.

‘Managed’ is undefined in the UK regulations, but the US Regulations (§1.1471-5(e)(4)(v) Example 5) indicate that any financial institution undertaking the activities of an investment entity on behalf of the trust, typically either as a trustee or as discretionary fund manager, will be deemed to be a manager of the trust in this context. UK Guidance suggests that with regard to trusts, ‘professionally managed’ ‘would typically be where the trustees have appointed a discretionary fund manager to manage the trust’s assets’. UK Guidance also confirms that a trust will not become an investment entity if ‘it simply holds a Depository Account with a Financial Institution where that Financial Institution does not manage the account.’ (UK Guidance, Section 2.36)

Section B: Trusts that are Financial Institutions
Dependent on the nature of the trustee, trusts that are Financial Institutions may have to register and report directly under the IGA or have the option to appoint a third party to fulfil their requirements under the IGA. In some circumstances, however, the trustee is required to register and report on the trust.

Question 6:
Does the trust have a ‘Reporting Financial Institution’ as trustee?
If ‘yes’ the trust is a ‘Deemed Compliant Financial Institution’ and is regarded as a ‘Trustee Documented Trust’. This is defined as:

‘A trust established in the United Kingdom to the extent that the trustee of the trust is a Reporting US Financial Institution, Reporting Model 1 FFI, or Participating FFI and reports all information required to be reported pursuant to the Agreement with respect to all US Reportable Accounts of the trust.’ (UK Regulations Annex II, II.D http://www.official-documents.gov.uk/document/cm86/8656/8656.pdf)

Any corporate entity acting as a trustee may be an FI under the IGA. In these circumstances, the trustee will need to register and report on the trust. The trust itself, however, is a Non-Reporting UK Financial Institution and does not need to register or report.

If the answer to Question 7 is ‘no’, the trust will need to either register with the IRS as a Foreign Financial Institution and report directly or if preferred it can appoint a third party to fulfil its reporting obligations; or the trust can opt to become a Sponsored Investment Entity, a Sponsored Closely Held Investment Entity or an Owner Documented Financial Institution.

Registration
The IRS registration portal can be found at:

This gives instructions, a user guide (http://www.irs.gov/pub/irs-pdf/p5118.pdf) and other materials to assist with FATCA registration.

On or after 1 January 2014, each FI will be expected to finalise its registration information by logging-in to its online account on the FATCA registration website, making any necessary additional changes, and submitting the information as final. Once registration is finalised and approved, registering FIs will receive a notice of registration acceptance and will be issued a Global Intermediary Identification Number (GIIN). The GIIN will enable the trust to interact with other Financial Institutions.
The IRS will electronically post the first IRS Foreign Financial Institution (FFI) List by 2 June 2014. To ensure inclusion in the June 2014 IRS FFI List, an FI will need to finalise its registration by 25 April 2014. The list will be updated monthly, but to ensure a smooth transition it may be prudent to ensure that relevant trusts are registered in time to appear on the first list. To meet the regulations, however, FIs do not need to be on the list until 1 January 2015 (prior to which date they can self-certify as an FI). To ensure inclusion on the January 2015 IRS FFI List, however, an FI must finalise its registration by 25 October 2014.

**Third party service providers**

Trusts that are categorised as Investment Entities may wish to consider using third-party service providers to meet their reporting obligations, although it is clear that all reporting obligations remain ultimately with the trust.

‘Each Party may allow Reporting Financial Institutions to use third-party service providers to fulfil the obligations imposed on them by a Party, as contemplated in this Agreement, but these obligations shall remain the responsibility of the Reporting Financial Institutions.’


**Sponsored Investment Entity**

A Sponsored Investment Entity is a Registered Deemed Compliant Financial institution and will need to obtain, or have its sponsor obtain on its behalf, a GIIN from the IRS and submit annual returns to HMRC. (N.B. Following changes to US Regulations, it is anticipated that these provisions may well be changed to require registration only after a US reportable account has been identified).

A Sponsored Investment Entity is an entity that has a contractual arrangement for its due diligence and reporting responsibilities to be carried out by a sponsoring entity. The Sponsoring Entity is an entity that is authorised to manage the sponsored Financial Institution and to enter into contracts on behalf of the sponsored Financial Institution. This option may of interest, for example, to a trust whose investments are managed on a discretionary basis by a fund management group. In these circumstances the trust would be an Investment Entity, but it could delegate its reporting under the IGA to the fund management group if the fund management group was prepared to be its sponsor.

A sponsor must register with the IRS as a sponsoring entity, and must, where a Sponsored Entity has reportable accounts, register each of the funds it manages with the IRS as ‘Sponsored Entities’. A Sponsored Entity will remain liable for any failure of its Sponsoring Entity to comply with IGA reporting obligations on its behalf.

The requirements for both Sponsored Investment Entities and Sponsoring Entities are outlined in US regulations:


An Investment Entity can be a Sponsored Investment Entity provided that it is an Investment Entity that is not a Qualified Intermediary (QI), Withholding Foreign Partnership (WP), or Withholding Foreign Trust (WT) and an entity has agreed to act as a sponsoring entity.

The Sponsoring Entity must:

1) Be authorised to act on behalf of the Sponsored Entity to fulfil the requirements of the FFI agreement.
2) Be registered with the IRS as a Sponsoring Entity.
3) Have registered the Sponsored Investment Entity with the IRS by the later of 1 January 2016, or the date that the Sponsored Entity identifies itself as qualifying.
4) Agree to perform, on behalf of the Sponsored Entity, all due diligence, withholding, reporting, and other requirements that the Sponsored Entity would have been required to perform if it were a participating Financial Institution.

5) Identify the Sponsored Entity in all reporting completed on the Sponsored Entity’s behalf.

**Sponsored Closely Held Investment Vehicles**

This category is similar to a Sponsored Investment Entity, which renders the trust a Registered Deemed Compliant Financial institution, but Sponsored Closely Held Investment Vehicles are instead certified Deemed Compliant Financial Institution and as such they do not need to register either directly or via their sponsor.

To qualify, the trust must be an Investment Entity that is not a US Qualified Intermediary, Withholding Foreign Partnership or Withholding Foreign Trust. The trust must also have a contractual arrangement with a Sponsoring Entity that is a Participating Financial Institution, Reporting Model 1 Financial Institution or US Financial Institution that is authorised to manage the Financial Institution and enter into contracts on its behalf under which the Sponsoring Entity agrees to all due diligence, withholding and reporting responsibilities that the Financial Institution would have if it were a Reporting Financial Institution.

Crucially, Sponsored Closely Held Investment Vehicles must not hold themselves out as an investment vehicle for unrelated parties and must have 20 or fewer individuals that own debt and equity interests (disregarding interests owned by Participating Financial Institution, Deemed Compliant Financial Institutions and an equity interest owned by an entity that is 100 per cent owner and itself a Sponsored Closely Held Investment Vehicle).

If these criteria are met, the Sponsoring Entity will have to register with the IRS as a Sponsoring Entity but it does not need to register the sponsored entities. The Sponsoring Entity will, however, be required to report on the Sponsored Entity.

**Owner Documented Financial Institution**

Owner Documented Financial Institutions are Certified Deemed Compliant Financial Institutions and as such are not required to register with the IRS and obtain a GIIN. UK Guidance states that this classification is ‘intended to apply to closely held Passive Investment Vehicles that are Investment Entities, where meeting the obligations under the Agreement would be onerous given the size of the entity.’

A trust may only be treated as an Owner Documented Financial Institution for payments received from and accounts held with a ‘Designated Withholding Agent’. A Designated Withholding Agent is a reporting Financial Institution that has agreed to undertake relevant due diligence and reporting. To qualify as an Owner Documented Financial Institution, the entity must:

1) Be a Financial Institution solely because it is an Investment Entity.
2) Not be owned by or in an expanded affiliated group with any Financial Institution that is a depository institution, custodial institution, or specified insurance company.
3) Not maintain a financial account for any non-participating Financial Institution.
4) Provide the Designated Withholding Agent with the necessary documentation and agree to notify the withholding agent if there is a change in circumstances.
5) Secure the agreement of the Designated Withholding Agent to report the relevant information with respect to any specified persons.

The Designated Withholding Agent will need the following information (US Regulations 1.1471-3(d)(6)(iv)):
1) The name, address, TIN (if any), and ‘Chapter 4 status’ (i.e. position under FATCA) of ‘every individual and specified US person’ that owns a direct or indirect equity interest in the owner documented FI (looking through all entities other than specified US Persons).

2) The name, address, TIN (if any), and chapter 4 status of every ‘individual and specified US person’ that owns a debt interest in the owner documented FI (including any indirect debt interest) in excess of USD50,000 (disregarding all such debt interests owned by ‘participating FFIs, registered deemed-compliant FFIs, certified deemed-compliant FFIs, excepted NFFEs, exempt beneficial owners, or US persons other than specified US Persons’).

3) Any other information the withholding agent reasonably requests in order to fulfil its obligations under FATCA.

As an alternative to the process outlined above, the Owner Documented Financial Institution can opt to provide an ‘auditor’s letter substitute’ (US Regulations, 1.1471-3(d)(6)(ii)). This requires the Owner Documented Financial Institution to provide a letter from an auditor or an attorney that is licensed in the US or whose firm has a location in the US, signed no more than four years prior to the date of the payment, that certifies that the firm or representative has reviewed the Owner Documented Financial Institution’s documentation with respect to all of its owners and debt holders described in that the Owner Documented Financial Institution meets the necessary requirements. The Owner Documented Financial Institution must also provide an owner reporting statement and a Form W-9, with any applicable waiver, for each specified US person that owns a direct or indirect interest in the Owner Documented Financial Institution or that holds debt interests. A withholding agent may rely upon the auditor’s letter substitute if it does not know or have reason to know that any of the information contained in the letter is unreliable or incorrect.

Section C: Trusts that are NFFEs

Trusts that are NFFEs must determine if they are ‘Active’ or ‘Passive’ NFFEs. The definition of a ‘Passive NFFE’ is simply any NFFE that is not an ‘Active NFFE’ (UK Regulations, Annex I.IV. B.3).

To be an active NFFE, a trust must meet one of a variety of criteria. The two most relevant for trusts are likely to be:

‘Less than 50 percent of the NFFE’s gross income for the preceding calendar year or other appropriate reporting period is passive income and less than 50 percent of the assets held by the NFFE during the preceding calendar year or other appropriate reporting period are assets that produce or are held for the production of passive income’ (UK Regulations, Annex I. IV.B.4.a);

or ‘Substantially all of the activities of the NFFE consist of holding (in whole or in part) the outstanding stock of, and providing financing and services to, one or more subsidiaries that engage in trades or businesses other than the business of a Financial Institution, except that an NFFE shall not qualify for this status if the NFFE functions (or holds itself out) as an investment fund, such as a private equity fund, venture capital fund, leveraged buyout fund or any investment vehicle whose purpose is to acquire or fund companies and then hold interests in those companies as capital assets for investment purposes’ (UK Regulations, Annex I. IV.B.4.e).

‘Passive income’ is not defined within the IGA agreement, but under the terms of the IGA can be assumed to have the same meaning as under UK law. This would suggest that it includes dividends, interest and royalties. While a UK trust can hold parent company and subsidiary shares among its assets, it cannot itself have a subsidiary.
It is worth noting, however, that the US FATCA regulations give a rather wider definition of ‘Active NFFE’, focusing on ‘related persons’ rather than ‘subsidiaries’. In particular, it defines as active income:

‘Any income from interest, dividends, rents, or royalties that is received or accrued from a related person to the extent such amount is properly allocable to income of such related person that is not passive income. For purposes of this paragraph (c)(1)(iv)(B)(1), the term ‘related person’ has the meaning given such term by section 954(d)(3) determined by substituting ‘foreign entity’ for ‘controlled foreign corporation’ each place it appears in section 954(d)(3)’ (1.1472-1(c)(1)(iv)(B)(1))

UK Guidance (p8) indicates that ‘where a Financial Institution identifies an alternative element of the US Regulations or alternative element of a different Intergovernmental Agreement that it feels it would like to apply then it should contact HMRC to discuss the issue’.
APPENDIX III
COMMON TRUST SCENARIOS

All UK trusts are entities; their status under FATCA needs to be determined. The status can either be that the entity is an FI or it is not. UK trusts will have to declare their status to any bank etc. with which they have dealings. Whether a UK trust is an FI 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.

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?

‘£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 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 trusts’ status under FATCA is that they are all 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 trusts circumstances and their status under FATCA.

**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 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. Many of 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 FIs 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, however, if it was just placed and left on deposit at a UK bank then it is not managed, as UK bank accounts are exempt and are not
reportable under FATCA (other exempt products include National Savings & Investment 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 FIs 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 status under FATCA.

**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 FIs 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.

Note the distinction here that even if the trust only holds property – the family home – and has no accounts. If it has family trustees it is an NFFE but will not be reported on or required to report as above, however, if it has a corporate trustee it will be an FI, a trustee documented trust, and will need to be reported on by the trustees.

**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 FIs 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.

**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 an FI. The trustees can either register and report the trust themselves to the IRS, or the trustees can appoint a withholding agent and opt for deemed compliant status. Alternatively, the existing trustees may consider appointing a corporate trustee, which is an FI, as an additional or replacement trustee, thus avoiding the need to register and transferring responsibility for reporting to that trustee.

Some typical categories of trusts can be summarised as follows:

*The trust is a registered charity*. The trust is exempt from the registration and reporting requirements imposed by FATCA.
The trust is a FURBS. Although there is an exemption for pension schemes, FURBS and other similar unapproved retirement benefit schemes do not qualify as exempt financial institutions and may therefore be required to register.

At least one of the trustees is a company that is empowered to act as a trustee. The corporate trustee is subject to registration and reporting requirements. It will register in its own right as an FI and will carry out all reporting requirements in respect of the appointments that it holds. The individual trusts of which it is a trustee will not therefore be required to register or to submit annual returns.

All of the trustees are individuals and the trust’s sole or main asset comprises a portfolio of investments managed by an investment advisor. The trust itself is an FI, which is required to register with the IRS and will have to submit an annual return to HM Revenue & Customs.

The trustees are all individuals and the only asset comprises an interest in real property (land and buildings). The trustees will not be required to register with the IRS.

The trustees are all individuals and the sole asset is an insurance policy secured on the life of a living person. Whilst the insured is still alive, there is no requirement to register.
APPENDIX IV
GLOSSARY

The regulations, forms and guidance introduce a number of new terms and a proliferation of acronyms. Much of the terminology is technically detailed and written from a US perspective so it is important to be sure of the interpretation of each phrase when applying it to the circumstances under consideration.

A comprehensive glossary is not possible within the scope of this guidance note but clarification can be found in the HMRC guidance and on the instructions to complete form 8957. Informal definitions for some of the most important terms used in this note are set out below.

CONTROLLING PERSON – a natural person who exercises control over an entity. In the case of a trust this can include a settlor, beneficiary, trustee or protector or member of a class of such persons or ‘any other person exercising ultimate effective control’. This definition is intentionally wide but is a specific example where in the ordinary course of advising trustees, a UK practitioner would not regard a protector or a member of a class of beneficiaries as having control so there is the potential to make an inadvertent error in reporting or identification. The term controlling person is relevant for determining what needs to be reported under FATCA.

FATCA – derived from the title of the Foreign Account Tax Compliance Act, this is the umbrella term for the law and practice in this area and used as shorthand to indicate the requirements for registration or the nature of an entity’s status under these provisions.

FFI/FI – a Foreign Financial Institution is an entity with registration and reporting requirements under FATCA. The word foreign is by reference to the USA and as such for simplicity this note refers only to UK resident Financial Institutions. Whether an entity is a FI is primarily determined as set out in part 1 of this guidance but reference should be made to the HMRC guidance and underlying regulations if in doubt. The status will be certified by provision of the GIIN to other institutions which require it and provision of form W8-BEN-E

FORM W8-BEN-E – the form certifies that a person or entity is not a US person. The form for individuals is known as a W-8BEN.

FORM 8957 – the form used to register as an FI with the IRS. The process is generally electronic submission.

FORM W9 – a form identifying a US person and disclosing their US taxpayer identification number (TIN)

GIIN – Global Intermediary Identification Number is a 19 character number issued to the FI on registration with the IRS. It is then used as a reference for all reporting and will need to be disclosed on FATCA status supporting documentation.

IGA – intergovernmental agreement. This is a treaty negotiated between the US and other countries to apply the US FATCA rules globally. There are two formats of the agreement:
• **Model 1** in which domestic law is enacted and under which reporting is undertaken to the domestic authority. The UK has a Model 1 agreement so that these regulations are UK law and reporting will be done through HMRC. The only interaction with the Internal Revenue Service of the USA will be the initial registration and obtaining of a GIIN.

• **Model 2** in which the country concerned agrees to the principles of FATCA but the governing law and reporting is directly to the USA. Reporting is enabled irrespective of any data protection or bank secrecy laws in the jurisdiction concerned. Switzerland and Japan for example, have Model 2 IGAs.

**NFFE** – a Non-Financial Foreign Entity is any entity which is not a FI. Status as a NFFE will be by certification or provision of a form W9 or W8-BEN-E. There are two forms of NFFE; active and passive.

An active NFFE is engaged in a non-financial business. A passive NFFE is one that is not engaged in a business and it will usually be required to identify its owners to the FI with which it has a relationship and in particular whether it is owned by any US Persons.

**NPFI or RNFFE** – these are respectively a Non-Participating Financial Institution and a Recalcitrant Non-Financial Foreign Entity. They are used to indicate those entities which do not comply with FATCA whether through wilful non-compliance or because they are unable to do so in the jurisdiction in which they are resident. Penalties can vary but in the first instance there will be 30 per cent withholding tax on any payment of US source income or proceeds from the sale of US securities. It may not be possible to operate financial accounts for NPFI or RNFFEs.

**OWNER DOCUMENTED ENTITY** – this is an entity delegating its FATCA reporting to a depository bank. The Entity will have to ensure the bank is content to take on the role. It is understood that many banks will be unable to do so.

**SPONSORED ENTITY** – this is an entity delegating its FATCA responsibilities to a third party or sponsor. The Sponsored entity may not have more than 20 owners or will have to register itself. It is unclear which institutions will be able to offer services as a sponsor.

**TRUSTEE DOCUMENTED TRUST** – a trust with a corporate or professional trustee which is, itself, registered as an FI. In this case the corporate trustee undertakes the FATCA compliance and the trust itself need not register for a GIIN.

**US PERSON** – any person including US citizens by birth or naturalisation including dual citizens, any lawful US resident; any green card holder, any US corporation or partnership or trust subject to the jurisdiction of the US courts. To assist in identifying US Persons, the FI is required to have regard to US indicia which include: US place of birth; citizenship; a green card; US address or telephone number; standing instructions to correspond with the US such as a power of attorney or mail collection address; regular payments to or from a US bank account.