

# THE COMMON REPORTING STANDARD – A GLOBAL F.A.T.C.A.?

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## STANDARD FOR AUTOMATIC EXCHANGE OF FINANCIAL ACCOUNT INFORMATION IN TAX MATTERS

The Standard for Automatic Exchange of Financial Account Information in Tax Matters (also known as the “Common Reporting Standard” or “C.R.S.”)<sup>1</sup> is a global system of automatic exchange of information for tax purposes (“A.E.O.I.”). As of January 1, 2016, financial institutions (“F.I.’s”) in jurisdictions that have signed up as members of the Early Adopters Group (“E.A.G.”)<sup>2</sup> of the C.R.S. are obligated to gather identification and residence information from new account holders to pass it to their jurisdictions’ reporting authority in order to enable reporting of the accounts. By 2018, the 96 jurisdictions<sup>3</sup> that have adopted the C.R.S. will be exchanging information on those account holders identified as reportable between their respective reporting authorities. F.I.’s and tax authorities still need to work through all the details, but below is a brief introduction to the system, how it is expected to work, and some potential pitfalls.

### What Countries Does It Affect and When?

Those jurisdictions that have adopted the C.R.S. include most of the world’s major economies and financial centers, with the notable exception of the U.S. The earliest date for information exchange under the C.R.S. will be 2017<sup>4</sup> (for information gathered in 2016) for the 56 jurisdictions that make up the E.A.G. The remaining 40 jurisdictions are committed to commence exchange by 2018. The process starts with F.I.’s collecting information on new account holders and then expands to include information on relevant existing account holders. The system was developed by the Organization for Economic Co-operation and Development (“O.E.C.D.”) and the Global Forum on Transparency and Exchange of Information for Tax Purposes (“Global Forum”) to combat tax evasion in response to a request by the G-20. The aim was to build on the systems and agreements put in place to comply with the Foreign Account Tax Compliance Act (“F.A.T.C.A.”) and to create a comprehensive global standard for A.E.O.I.

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<sup>1</sup> [“Standard for Automatic Exchange of Financial Information in Tax Matters.”](#) O.E.C.D. Automatic Exchange Portal - Common Reporting Standard (C.R.S.). July 21, 2014.

<sup>2</sup> [“Joint Statement by the Early Adopters Group.”](#) O.E.C.D. October 1, 2014.; [“CRS by Jurisdiction.”](#) O.E.C.D.: C.R.S. Implementation and Assistance.

<sup>3</sup> [“A.E.O.I.: Status of Commitments.”](#) O.E.C.D. Global Forum on Transparency and Exchange of Information for Tax Purposes.

<sup>4</sup> [“C.R.S. by Jurisdiction.”](#) O.E.C.D.: C.R.S. Implementation and Assistance.

The U.S. is already receiving information on U.S. persons ahead of these C.R.S. deadlines. The first information exchange under its own A.E.O.I. system took place at the end of September 2015.<sup>5</sup> Under the U.S. system – operating under F.A.T.C.A. – the U.S. Internal Revenue Service (“I.R.S.”) is provided with information on financial accounts of U.S. persons, either from F.I.’s directly or from the relevant tax authority of those foreign tax jurisdictions that have appropriate Intergovernmental Agreements (“I.G.A.’s”) with the U.S. The U.S. has committed to implement a level of reciprocity under the Model 1 I.G.A.’s rather than signing up to participate in the C.R.S., but political stalemate has prevented the legislative changes necessary to make that work in practice. Among other consequences, if a jurisdiction participating in the C.R.S. deems the U.S. as non-participating, then most U.S. trusts, as well as F.I.’s that are investment entities (e.g., a managed investment entity like a mutual fund), with accounts in the participating jurisdiction will have to provide information on their controlling persons, which otherwise is only required for more limited types of F.I.’s in participating jurisdictions.

### **How Does It Work?**

The C.R.S. sets out the information that reporting authorities in participating jurisdictions should gather from F.I.’s located in those jurisdictions and that should be automatically exchanged on an annual basis with other participating jurisdictions. This information broadly consists of details of financial assets that are held by the F.I.’s on behalf of taxpayers that are resident in other participating jurisdictions, provided that the reporting authority has in place an agreement for the exchange of tax information. F.I.’s report to the reporting authority in the participating jurisdiction in which they are located. The consequences of non-compliance are left to the participating jurisdictions to specify in domestic legislation.

### **The Documentation**

The system is made up of components. First, there is the ‘Model’ Competent Authority Agreement (“C.A.A.”)<sup>6</sup> (a bilateral and reciprocal agreement based on the F.A.T.C.A. Model 1 I.G.A.), which provides the international legal framework<sup>7</sup> for A.E.O.I. under the C.R.S. The Common Reporting and Due Diligence Standard<sup>8</sup> sets out the reporting and due diligence requirements, and is known as the Common Reporting Standard or “C.R.S.” This can cause confusion because the acronym C.R.S. is also commonly used to refer to the Common Reporting Standard as a whole. Finally, there is a “User Guide”<sup>9</sup> for the C.R.S. XML Schema and Commentaries.<sup>10</sup> The Schema may need to change in the future as the system evolves. To overcome the potential legal difficulties this would create, in December 2015, the O.E.C.D. agreed on a plan to work out a system for adopting future changes (see below).



<sup>5</sup> The first information exchange under reciprocal I.G.A.’s, took place by the September 30, 2015 deadline.

<sup>6</sup> “[Commentaries on the Common Reporting Standard.](#)” O.E.C.D.

<sup>7</sup> “[The C.R.S. Multilateral Competent Authority Agreement.](#)” O.E.C.D.: International Framework for the CRS.

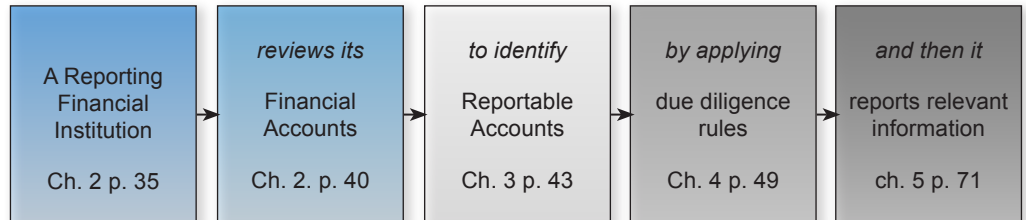
<sup>8</sup> “[Commentaries on the Common Reporting Standard.](#)” O.E.C.D.

<sup>9</sup> “[Common Reporting Standard User Guide and Schema.](#)” O.E.C.D.

<sup>10</sup> “[Commentaries on the Common Reporting Standard.](#)” O.E.C.D.

## What Is Required of F.I.'s?

The A.E.O.I. process for the C.R.S. is set out in the component documents above, but the O.E.C.D. has also prepared the C.R.S. *Implementation Handbook*<sup>11</sup> (the “Handbook”), which explains the basics simply and clearly in “Part II: Overview of the C.R.S. and Due Diligence Rules.”<sup>12</sup> Put simply, F.I.’s in jurisdictions that participate in the C.R.S. will need to follow the steps in the diagram below.



Guidance on exactly how to implement these steps may be found at each chapter of the Handbook referenced in the diagram above, with step-by-step flow charts on identifying Reporting Financial Institutions, Financial Accounts, and Reportable Accounts as well as the various due diligence rules to be applied depending on the nature of the account as new or pre-existing (open before January 1, 2016) and the nature of the holder as an entity or individual.

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F.I.’s should advise clients and account holders that they must provide their details to the F.I. and that data will be made available to tax authorities in the client’s jurisdiction of residence. While there is considerable overlap between F.A.T.C.A. and the C.R.S., information, systems, and processes that F.I.’s have established to comply with F.A.T.C.A. will need to be adapted if they are to be used for the C.R.S. The C.R.S. covers more accounts and entities than F.A.T.C.A., and there is some flexibility on which accounts are included (e.g., individual jurisdictions can define which accounts are low-risk) so there is a real possibility of jurisdictional variations for reporting. Also, jurisdictions are free to decide the format by which F.I.’s will report information. Although the Handbook suggests jurisdictions use the C.R.S. Schema (which is virtually identical to the F.A.T.C.A. XML Schema) to avoid the need for significant additional investment on the part of governments or F.I.’s, it is not mandatory and F.I.’s will need to confirm the approach taken by the appropriate jurisdiction.

### Timetable

F.I.’s in E.A.G. countries will have prepared their I.T. and administrative systems to deal with the requirements for new account-opening procedures from January 1, 2016. For E.A.G. jurisdictions, the timetable is as follows:

1. F.I.’s will be required to have account-opening procedures in place to record tax residence for all new accounts opened from January 1, 2016.
2. Pre-existing accounts are those already open on December 31, 2015.
3. Due diligence identifying high-value, pre-existing individual accounts must be

<sup>11</sup> [“The C.R.S. Implementation Handbook.”](#) O.E.C.D.

<sup>12</sup> *Id.*, p. 34.

complete by December 31, 2016.

4. Due diligence for low-value, pre-existing individual accounts and entity accounts must be complete by December 31, 2017.
5. First reporting of information gathered in 2016 is expected in 2017.

As an example of the preparations being made in E.A.G. countries, in the author's jurisdiction of the Cayman Islands (which is a founding member of the E.A.G.) the Cayman Islands Department of International Tax Co-operation of the regulatory authority, the Cayman Islands Monetary Authority, has introduced regulations<sup>13</sup> and set up an A.E.O.I. Portal<sup>14</sup> to allow F.I.'s to monitor progress.

For jurisdictions that are not in the E.A.G., the timetable for collecting the same information is extended through 2017, with reporting scheduled to commence in 2018.

### **What Is the Domestic Legal Basis of the C.R.S.?**

To create any global standard, the information gathering and exchange mechanisms need to be incorporated into the legal system of each participating country. This means that the jurisdictions that have signed up to participate in the C.R.S. have been bringing in new or adapting existing legislation to ensure that F.I.'s report the required information on the relevant financial assets that are held. The four core requirements for governments to implement the C.R.S. are as follows:

1. Translating the reporting and due diligence rules into domestic law, including rules to ensure their effective implementation (including penalties and sanctions)
2. Selecting a legal basis for the automatic exchange of information
3. Putting in place I.T. and administrative infrastructure and resources
4. Protecting confidentiality and safeguarding data

The approach to protecting the confidentiality and integrity of the data being exchanged may differ for each jurisdiction. There is non-mandatory guidance offered by the O.E.C.D. in its guide *Keeping it Safe*<sup>15</sup> from July 2012. In it, the O.E.C.D. sets out best practices and gives practical guidance (including a checklist) on what steps jurisdictions should take to protect the confidentiality of tax information. This protection is important, as jurisdictions can withhold information based on the fact that they consider it will not be safe in the destination jurisdiction.

### **What Is the International Legal Basis?**

To reduce the number of F.I.'s providing information to the I.R.S. directly, the U.S.

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<sup>13</sup> [“The Tax Information Authority \(International Tax Compliance\) \(Common Reporting Standard\) Regulations, 2015.”](#) Cayman Islands Department for International Tax Cooperation. October 16, 2015.

<sup>14</sup> [“AEOI News & Updates.”](#) Cayman Islands Department for International Tax Co-operation.

<sup>15</sup> [“Keeping It Safe: The O.E.C.D. Guide on the Protection of Confidentiality of Information Exchanged for Tax Purposes.”](#) O.E.C.D.

developed Model I.G.A.'s, which allowed governments to collect information from the F.I.'s that is then provided to the U.S. in bulk. The C.R.S. provides for an alternative to multiple bilateral tax information exchange agreements. The O.E.C.D. and Global Forum drafted a Multilateral Convention on Mutual Administrative Assistance in Tax Matters ("M.A.C.") that jurisdictions may sign. This provides a legal gateway for the exchange of tax information between all countries and jurisdictions that have signed up for the C.R.S. As of October 29, 2014, 51 jurisdictions signed the Model C.A.A. for A.E.O.I. based on Article 6 of the M.A.C. – there are now 89 jurisdictions covered by the M.A.C. and 74 by the Model C.A.A.<sup>16</sup> To help F.I.'s understand how far along a jurisdiction is in the implementation of the C.R.S., the O.E.C.D.'s A.E.O.I. Portal has an overview of the current state of implementation for all committed G-20/O.E.C.D. member countries, which is contained in a single table.<sup>17</sup>

### **Future Changes to the C.R.S. XML Schema**

On December 1, 2015, the O.E.C.D. agreed<sup>18</sup> to plan to consider, review, and adopt future changes to the C.R.S. XML Schema that would allow it to evolve over time. This came after the European Commission asked for the inclusion of three additional fields and a value in the C.R.S. XML Schema, which highlighted the potential legal issues involved in making such a change (e.g., changes to the C.A.A.). The plan is for a substantive review of the experiences of tax authorities during the first exchange and use of the C.R.S. information in 2017 and 2018 (as well as the early exchanges of information under the F.A.T.C.A. I.G.A.'s) in order to see what other technical changes to the C.R.S. XML Schema might be needed.

### **So, Is It Really Any Different from F.A.T.C.A.?**

The C.R.S. was designed to build on the agreements and systems put in place by governments and F.I.'s to comply with F.A.T.C.A. The goal was to create an effective new international standard at a minimal cost to F.I.'s and governments.

However, F.A.T.C.A. is U.S.-specific and its I.G.A.'s were unsuitable for a global standard, so changes were made.<sup>19</sup> The use of citizenship as an indication of tax residence and references to U.S. domestic law were changed, as were approaches that were more suited to the bilateral context of F.A.T.C.A. I.G.A.'s rather than the multilateral context of the C.R.S. The use of F.A.T.C.A. regulation definitions in the C.R.S. should help those working with both systems, but not all definitions are the same. This will create practical problems and operational challenges for F.I.'s. These include identifying which entities need further investigation for the C.R.S. and reporting entities with controlling persons that have a different tax residency than the entity.

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<sup>16</sup> “Statement of Outcomes.” O.E.C.D.: Global Forum on Transparency and Exchange of Information for Tax Purposes. October 30, 2015.

<sup>17</sup> “C.R.S. by Jurisdiction.” O.E.C.D.: C.R.S. Implementation and Assistance.

<sup>18</sup> “Statement of Outcomes by Working Party No. 10 on the EU Proposal on the Addition of Fields to the CRS XML Schema.” O.E.C.D. December 1, 2015.

<sup>19</sup> The Handbook offers detailed comparisons at p. 84, “Part III: The Standard compared with F.A.T.C.A. Model 1 I.G.A.,” and p. 22, ¶36, “Differences to F.A.T.C.A.”

holding below which due diligence by F.I.'s is not required. Regarding non-compliance, the F.A.T.C.A. threat of withholding from a non-compliant F.I.'s own money does not apply, but each participating jurisdiction will legislate its own non-compliance penalties.

The C.R.S. covers accounts held by individuals and entities, including trusts and foundations, and the information it covers includes balances, interest, dividends, and sales proceeds from financial assets. Some C.R.S. due diligence procedures will require manual checks to confirm information with paper-based documentary evidence. Without an agreed, standard form of self-certification, each jurisdiction is free to ask F.I.'s for more information than the minimum, causing duplication in the preparation of information on account holders in order to meet the information and presentation requirements of different jurisdictions.

### **Further Help from the O.E.C.D. and Global Forum**

To back up the formal documentation of the C.R.S., the O.E.C.D. recently launched a new A.E.O.I. Portal<sup>20</sup> to give tax administrations and F.I.'s the information and legal, administrative, and I.T. tools that may be needed. It has published detailed F.A.Q.'s<sup>21</sup> and a second edition of its *Offshore Voluntary Disclosure Programmes*<sup>22</sup> with updated guidance on the design and implementation of voluntary disclosure programs based on the practical experience of 47 countries, including the views of private client advisers. The Global Forum has also been monitoring how jurisdictions that have signed up for the C.R.S. are implementing the commitments they have undertaken.

### **Beneficial Ownership Registers and the C.R.S.**

There has been much discussion of beneficial ownership public registers, and it is significant that the Global Forum will include in its next round of peer reviews the examination of a jurisdiction's ability to provide beneficial ownership information.<sup>23</sup> This is not something that arises from the C.R.S. In fact, the C.R.S. does not actually refer at all to beneficial ownership, but rather to controlling persons. There is nothing in the C.R.S. that requires the setting up of a register, public or otherwise, for any of the information collected by F.I.'s and passed to the relevant reporting authority.

The driver for establishing beneficial ownership registers comes from the G-20 High-Level Principles on Beneficial Ownership Transparency,<sup>24</sup> which includes the provision that

<sup>20</sup> [“A.E.O.I. Portal.”](#) O.E.C.D.

<sup>21</sup> [“C.R.S.-related F.A.Q.'s.”](#) O.E.C.D.

<sup>22</sup> [“Update on Voluntary Disclosure Programmes: A Pathway to Tax Compliance.”](#) O.E.C.D. August 1, 2015.

<sup>23</sup> [“Statement of Outcomes.”](#) O.E.C.D.: Global Forum on Transparency and Exchange of Information for Tax Purposes. October 30, 2015.; [“Global Forum on Tax Transparency Pushes Forward International Co-operation against Tax Evasion.”](#) O.E.C.D. Newsroom. October 30, 2015.

<sup>24</sup> [“G20 High-Level Principles on Beneficial Ownership Transparency.”](#) G-20.: 2014.; [“Update to Article 26 of the O.E.C.D. Model Tax Convention and Its Commentary.”](#) O.E.C.D. July 17, 2012.



*“A global system of A.E.O.I. to attempt to defeat tax evasion is an ambitious idea, which goes far beyond F.A.T.C.A.”*

[c]ountries should ensure that competent authorities (including law enforcement and prosecutorial authorities, supervisory authorities, tax authorities[,] and financial intelligence units) have timely access to adequate, accurate[,] and current information regarding the beneficial ownership of legal persons. Countries could implement this, for example, through central registries of beneficial ownership of legal persons or other appropriate mechanisms.

The Global Forum is the premier international body for ensuring the implementation of the internationally agreed upon standards of transparency and exchange of information in tax matters. Through an in-depth peer review process, it monitors its members to ensure that they fully comply with the standard of transparency and exchange of information to which they have committed. This monitoring covers C.R.S. compliance as well as other commitments, such as those under a Tax Information Exchange Agreement (“T.I.E.A.”). Under T.I.E.A.’s, there is an exchange of information on request (“E.O.I.R.”) mechanism. At a meeting<sup>25</sup> held at the end of October 2015, the Global Forum created a new framework for the second round of Phase 2 peer reviews on exchange of information. The new 2016 terms of reference<sup>26</sup> include a requirement that

[j]urisdictions should ensure that ownership and identity information, including information on legal and beneficial owners, for all relevant entities and arrangements is available to their competent authorities.

The U.K. and the E.U. have chosen to meet their commitment to ensure “timely access to adequate, accurate[,] and current information regarding the beneficial ownership of legal persons” by implementing public registers. Other countries, such as the Cayman Islands, meet the same obligation by ensuring their regulatory bodies have the information available from the formation of the relevant entities, and valid requests for such information can be, and are, responded to in a timely fashion. The C.R.S. will not require any change to this commitment or the way it is met by participating jurisdictions. It will, in fact, require assessment of slightly different criteria to identify controlling persons for some entities.

## CONCLUSION

A global system of A.E.O.I. to attempt to defeat tax evasion is an ambitious idea, which goes far beyond F.A.T.C.A. It remains to be seen whether, and how, the dual F.A.T.C.A. and C.R.S. systems for A.E.O.I. will continue on their parallel paths. It will be interesting to see whether or not the two systems will gradually converge, and how the fact that the U.S. is not a participating C.R.S. country and isn’t legally able to require U.S.-based F.I.’s to collect the relevant information on account holders will play out in practice.

With 96 jurisdictions committed to A.E.O.I. through the C.R.S. system, it is a certainty

<sup>25</sup> [“Statement of Outcomes.”](#) O.E.C.D.: Global Forum on Transparency and Exchange of Information for Tax Purposes. October 30, 2015.; [“Global Forum on Tax Transparency Pushes Forward International Co-operation against Tax Evasion.”](#) O.E.C.D. Newsroom. October 30, 2015.

<sup>26</sup> [“Tax Transparency 2015: Report on Progress.”](#) O.E.C.D.: Global Forum on Transparency and Exchange of Information for Tax Purposes. 2015, p. 33.

that F.I.'s will be asking their clients for more information in order to establish the clients' residence and then report their account information to the tax authority of their residence (through the F.I.'s tax authority). This will happen in every jurisdiction where the client has a reportable account and, as what is asked may differ slightly from jurisdiction to jurisdiction, it will be difficult to apply a "one size fits all" approach to due diligence/"know your client" requirements. These are early days for the C.R.S., but like F.A.T.C.A., it is here to stay in one form or another, and it is already operating in E.A.G. jurisdictions. Even though the U.S. is not a participating jurisdiction, the C.R.S. will still have an impact on some F.I.'s located there and it must still be taken into account.