THE U.K. TRUST REGISTRATION SERVICE: IMPACT FOR TRUSTEES

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E.U. DRIVE TOWARDS TRANSPARENCY

The past few years have seen a steep increase in trust reporting obligations in the context of F.A.T.C.A. and the Common Reporting Standard ("C.R.S."). Trustees must now come to terms with a new set of record keeping and disclosure obligations introduced by the U.K. Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 (the "Regulations"), which came into force from June 26, 2017 to enact the E.U. Fourth Money Laundering Directive (E.U. 2015/849).

These obligations are potentially wide-ranging and onerous, but importantly, there are straightforward ways in which non-U.K. trustees can fall outside the regime.

From the trustee's perspective, the main impact of the Regulations is the introduction by HM Revenue & Customs ("H.M.R.C.") of a new Trust Registration Service ("T.R.S."). T.R.S. achieves two goals. The first is to digitize the registration of trusts for the purposes of filing U.K. tax returns in cases where trustees are required to pay U.K. income or capital gains tax. The second is to meet H.M.R.C.'s obligation under E.U. law to maintain a register of certain prescribed information by requiring the trustees of "taxable relevant trusts" to provide information on their settlors, beneficiaries, "power holders," and assets.

This information is, in some respects, significantly wider than the information that must be disclosed in other contexts (*e.g.*, C.R.S.) and arguably goes beyond what is required from the U.K. under E.U. law. The good news, however, is that – unlike the rules in other jurisdictions[1] – the Trust Register is not open to public inspections.

In addition to the Trust Register, the trustees of "relevant trusts" are obliged to maintain extensive internal written records relating to the trust's beneficial owners and potential beneficiaries. On request, this information must be shared with law enforcement authorities and other bodies that have anti-money laundering ("A.M.L.") client due diligence obligations.

On October 9, 2017, H.M.R.C. published guidance in the form of a series of FAQs, which sets out their interpretation of the relevant parts of the Regulations and explains how they intend the T.R.S. to work in practice. However, there were several areas of uncertainty and contradiction, and H.M.R.C. has had to engage in significant subsequent correspondence with interested professional bodies to clarify or amend their position (and amended FAQ's on December 6, 2017).

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1 *E.g.*, Germany. See, in detail, "The New Transparency Register in Germany," *Insights* 10 (2017).

KEY TERMS: WHICH TRUSTS DOES THIS AFFECT?

All relevant trusts fall within the new record keeping obligations introduced by the Regulations.

A "relevant trust" will include all U.K.-resident express trusts and any non-U.K.-resident express trust that has U.K.-source income arising at the trust level (*e.g.*, on assets held through a tax transparent entity for U.K. purposes) or that directly holds U.K. assets at the trust level.

An "express" trust is a trust established deliberately by a settlor. Consequently, it does not include a statutory trust, a resulting trust, or a constructive trust, each of which acknowledges a trust as a matter of law or equity, rather than intent. It also arguably does not include certain types of revocable trusts common in U.S. estate planning, which are more akin to bare trusts under English law, although each trust must be examined on its terms.

A trust will be U.K. resident if all the trustees are U.K. resident, or if there is at least one U.K. resident trustee and the settlor is resident or domiciled in the U.K. at any time when the funds are added to the trust. Trustees of non-U.K.-resident trusts should be aware of the potential for the trust to become inadvertently U.K. resident at the time assets are transferred to an existing trust.

A relevant trust is a "taxable relevant trust" in any year in which the trustees are liable to pay any of the following taxes on any U.K.-source income or directly held U.K. assets (referred to collectively as the "relevant taxes"):

- Income tax
- Capital gains tax
- Inheritance tax
- Stamp duty land tax ("S.D.L.T.," which is payable on purchases of U.K. real estate interests)
- Stamp duty reserve tax ("S.D.R.T.," which is a tax payable on purchases of U.K. securities made via a clearing house)
- Land and buildings transaction tax in Scotland

It is important to note that the U.K. tax liability must fall on the trustees directly and/or that taxable U.K. assets must be held directly. This means that the following scenarios will not create taxable relevant trusts:

- A trust that would have had a U.K. tax liability but for a relief (*e.g.*, hold-over relief on otherwise chargeable capital gains, business property relief from U.K. inheritance tax, or relief claimed under a double tax treaty)
- A trust that is taxable in respect of U.K. assets held through a non-U.K. holding company (including U.K. residential property held through a non-U.K. company) that is not "look-through" entity for U.K. tax purposes

•	A circumstance in which a U.K. tax liability is attributed to someone other than the trustees (*e.g.*, a beneficiary under a life interest trust where income is mandated directly by the trustee to the life tenant so that the trustees do not receive the income in their bank account first and thus the trustees have no further U.K. tax liability for the year in relation to directly held assets)

"Non-U.K. trusts can fall inside or outside of the T.R.S. regime depending on when the relevant U.K. tax liability arises."

•	A trust that only has a liability to U.K. Value Added Tax ("V.A.T.") in any year (as this is not a relevant tax)

•	A charitable trust – unless it has incurred a liability to pay any of the relevant taxes, which would normally only apply to a charity that owns a company engaged in business or that receives other non-exempt income (nevertheless, all relevant charitable trusts now have an obligation to keep written records in relation to the charity's beneficial owners)

•	A bare trust

•	A trust with a *de minimis* U.K. tax liability (less than £100 tax on bank or building society interest income)

Non-U.K. trusts can fall inside or outside of the T.R.S. regime depending on when the relevant U.K. tax liability arises. For example, a non-U.K. trust that directly holds a non-income producing U.K. asset will only be a taxable relevant trust for a year in which an inheritance tax, decennial charge,[2] or exit charge[3] arises under the periodic charge regime – known as the "relevant property regime" – that applies to trusts for inheritance tax purposes. It will, however, still be a relevant trust for as long as it holds that asset and will have ongoing internal record keeping obligations.

Since the FAQs were first published, H.M.R.C. has confirmed that the holding of U.K. assets through a nominee would not prevent the trust from being a taxable relevant trust even though legal ownership of the assets is not direct, because the tax liability arising from the U.K. asset falls on the trustees directly.

Trustees should be particularly careful if they have made loans to any person in the U.K., as this could be a U.K. asset and, if interest bearing, produce U.K.-source income.

It seems that if a non-U.K. trust directly purchased U.K. shares it would be required to register using the T.R.S. even if the only foreseeable U.K. tax nexus for the trust is the S.D.R.T. payable on the transaction (which would normally be deducted automatically). Take, for example, a non-U.K. trust with no U.K.-resident beneficiaries and U.K. assets valued below the inheritance tax exempt nil rate band so that no inheritance tax liability arises under the relevant property regime. The trust would remain on the Register, but the information would not need to be updated unless, and until, another relevant U.K. tax charge arises for the trustees.

Importantly, this analysis should not apply where chargeable securities are purchased by a custodian because the liability then falls on the custodian as legal

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[2] Inheritance tax is charged at each ten-year anniversary of the trust on the net value of any relevant property in the trust on the day before that anniversary.

[3] Inheritance tax is charged up to a maximum of 6% on assets – such as money, land, or buildings – transferred out of a trust. This is known as an "exit charge" and applies to all transfers of relevant property.

purchaser (who would then recoup the liability through its fees) and the trustees would have no further reporting or payment obligations in relation to the purchase. We expect this to be confirmed by H.M.R.C. in due course.

RELEVANT DATES

As has always been the case, trustees must register to file U.K. tax returns the first time they have a U.K. income tax or capital gains tax liability. However, they are now required to use the T.R.S. rather than the old paper system. For non-U.K. trusts, this will normally only be the case if the trustees receive U.K.-source income and at least one beneficiary of the trust is resident in the U.K.

The registration deadline for self-assessment has not changed and falls six months after the end of the tax year in which the U.K. tax liability first arises (*e.g.*, for the tax year ended April 5, 2017, the deadline would normally be October 5, 2017). For this year only, the deadline has been extended to January 5, 2018, to allow all parties to get used to the new system (to which agents were only given access on October 17, 2017).

The deadline for populating the Trust Register with beneficial ownership information falls on January 31 following each year in which a relevant tax liability arises. The first relevant year is 2016/17, so the first deadline for providing the prescribed information would be January 31, 2018, but H.M.R.C. have extended the deadline to March 5, 2018, for this year only.

However, if a trust already registered for self-assessment with H.M.R.C. but has been wound up since April 6, 2017, it does not need to be included on the Register. A trust that was wound up since April 6, 2017, but was first liable to U.K. tax in 2016/17 must still register for self-assessment, but it seems it will not be required to populate the Trust Register if it does not exist on March 5, 2018.

By January 31 following the close of each tax year, taxable relevant trusts must update the Register with any changes or confirm that no changes occurred in the preceding year. However, changes can be made to the Register at any time, and in practice, trustees should ensure that their internal records are up to date at all times. Note that trusts that are not taxable relevant trusts for the year do not need to update the Register.

The relevant dates can be summarized as follows:

January 5, 2018	Deadline for trusts with a U.K. income tax or capital gains tax liability for the first time in 2016/17 to register for self-assessment using the T.R.S.
March 5, 2018	Deadline for all taxable relevant trusts with a relevant tax liability in 2016/17 to provide prescribed information on beneficial owners using the T.R.S.
October 5, 2018 (and later years)	Deadline for trusts with a U.K. income tax or capital gains tax liability for the first time in 2017/18 (and later years) to register for self-assessment using the T.R.S.

January 31, 2019 (and later years)	Deadline to notify H.M.R.C. of any changes (or confirm no changes) on the T.R.S. if the trust had a relevant tax liability in 2017/18 (and later years)

WHAT INFORMATION MUST TAXABLE RELEVANT TRUSTS PROVIDE ON THE TRUST REGISTER?

The full list of information required is beyond the scope of this article. Recently published FAQs have shed additional light on some of these categories.

One of the purposes of the T.R.S. is to identify the "beneficial owners" of taxable relevant trusts. These are considered to be

- the settlor(s),
- the trustees,
- the beneficiaries and potential beneficiaries, and
- any individual who has control over the trust, which could include a protector or anyone who has the power to change the trustees.

The first point to note is that information must be current and up to date, so if there are changes between now and the relevant registration or updating deadline, the outdated information can be disregarded (including where a trust has been wound up). For example, if a trustee or beneficiary is removed or added in the interim period, only the current trustees and beneficial class at the date of registration must be disclosed. When the Register is updated each year, any former beneficiaries and trustees will be removed from the record and will no longer appear on the Register.

IDENTIFYING BENEFICIARIES INDIVIDUALLY OR BY CLASS

This has perhaps been the most controversial area of the T.R.S. for trustees, as when first published, the H.M.R.C. guidance appeared to be wider than the disclosure obligations under other regimes, such as the C.R.S. The scope has since been narrowed by a change in approach by H.M.R.C.

The Regulations refer to "the beneficial owners of the trust and any other individual referred to as a potential beneficiary."

It is clear under the FAQs that any individual named in a trust deed or in a related document written by the settlor (*e.g.*, a letter of wishes) as a potential beneficiary must be disclosed, even if their prospects of actually benefitting are remote. However, if the settlor names a beneficiary subject to a contingency (*e.g.*, contingent on the deaths of all other named beneficiaries), that beneficiary need only be named if and when the contingency is fulfilled. H.M.R.C. have indicated that third-party reports of the settlor's wishes, such as a solicitor's attendance note, would not be considered as a "document written by the settlor" for these purposes.

Where there is a class of beneficiaries such as the settlor's descendants, the initial FAQs included seemingly contradictory examples. Does the requirement extend to identifying all individual members of a class who are in existence and providing information on each of them, or is it sufficient to describe the class and to identify only those individuals who have actually received a benefit? Since the publication of the FAQs, H.M.R.C. vacillated in their approach but have now confirmed their view that individual members of a discretionary class need only be disclosed if they actually receive a financial or non-financial benefit from the trust after June 26, 2016 – the commencement of the Regulations.

H.M.R.C.'s change in approach likely goes to the fact that their guidance, as initially published, went further than the Regulations require. It is stated in the Regulations that where the beneficial owners include "a class of beneficiaries, not all of whom has been determined" (emphasis added) then only a description of the class must be provided, and there is a specific carve-out from providing information on individual beneficiaries in these circumstances.

"Any individual named in a trust deed or in a related document written by the settlor (e.g., a letter of wishes) as a potential beneficiary must be disclosed."

This interpretation would also be in line with the wider guidance on concepts of beneficial ownership in similar A.M.L. contexts. For example, the recommendations published by the Financial Action Task Force in relation to beneficial ownership in the context of client due diligence suggest that it should be adequate for financial institutions to establish the identity of a beneficiary at the time of a pay-out or when the beneficiary intends to exercise vested rights. This would seem to be a proportionate obligation in light of the purpose of the Regulations to combat tax evasion and other forms of money laundering.

In this context, it is worth noting that personal data obtained by H.M.R.C. or any other relevant person for the purposes of the Regulations may only be processed for the purpose of preventing money laundering or terrorist financing. This supports the argument that the Regulations should be interpreted in a narrower sense.

DISCLOSURE OF TRUST ASSETS

The details of assets that have been added to the trust, including the addresses of any U.K. real estate, must be reported on the Register alongside a valuation of the assets when first contributed to the trust. This obligation extends to all added assets, not just those that have triggered a U.K. tax consequence, but does not extend to providing details of reinvested assets (unless otherwise reportable as triggering a U.K. tax liability).

It seems that H.M.R.C. are taking a pragmatic approach to valuation (as they did under the old regime) and will not expect formal valuations to be obtained. If a valuation has already been provided on first registration under the old regime, the exercise need not be repeated.

DETAILS OF ADVISERS

H.M.R.C. have clarified that the obligation to report the identity of "all advisers who are being paid to provide legal, financial, tax or other advice to the trustees" extends only to details of the agent (if any) who is notified to H.M.R.C. (under Form 64-8) as acting on the trustees' behalf in relation to these registration requirements.

RECORD KEEPING OBLIGATIONS

All relevant trusts are required to maintain accurate and up-to-date written records relating to the trust's beneficial owners and potential beneficiaries (reflecting the information required to be disclosed on the Trust Register), which they must share on request from law enforcement authorities and other bodies who have A.M.L. client due diligence obligations (*e.g.*, investment managers, law firms, and banks). Records are to be kept for five years from the final distribution and, in general, may be deleted thereafter. Anyone to whom this information is communicated in a business context must be notified of any changes within 14 days.

This means that all relevant trusts must maintain internal records even when they have no U.K. tax liability to report.

WHO CAN ACCESS THIS INFORMATION?

Under the Regulations, access may only be given to named law enforcement agencies in the U.K. and other E.E.A. countries through the National Crime Agency.

Some parties have expressed concern that "persons with a legitimate interest with respect to money laundering, terrorist financing . . . [etc.]" – N.G.O.'s or investigative journalists would be examples – could challenge the scope of the Regulations as this wording is included in the original E.U. Directive. Indeed, under the draft Fifth E.U. Money Laundering Directive currently being negotiated in the E.U. Parliament, the proposal is for all beneficial ownership registers to be made public.

This concern may be heightened in light of the recent "Paradise Papers" hack of 13.4 million documents from one of the leading firms in offshore finance, along with corporate registries in 19 tax jurisdictions. The papers reveal the financial dealings of politicians, celebrities, corporate giants, and business leaders. Journalists claim that investigation is in the public interest because such leaks and hacks from the offshore world repeatedly expose wrongdoing. Facilitating a global system of transparency and information exchange through such mechanisms as the T.R.S. and C.R.S. will likely be considered a way to tackle abusive offshore practices.

However, public demand for increased transparency should be balanced by domestic and European privacy and data protection rules. When a similar trust register was created in France, it was initially announced that this would be made public. However, public access to the information was held to be unconstitutional in a decision of the French Constitutional Court (Conseil Constitutionnel) on October 21, 2016. The court found that public access to the French trust register was a disproportionate breach of privacy rights for those individuals with trust arrangements. Consequently, the French government issued a new Ordinance, which transposes the E.U. Fourth Money Laundering Directive, limiting access to the French trust register to named law enforcement agencies.

It would seem unlikely that wider public access would be permissible under European data protection laws, especially once these are strengthened by the E.U. General Data Protection Regulation, which will be fully enforceable across the E.U. from May 2018.

PENALTIES FOR NONCOMPLIANCE

Trustees are expected to take "all reasonable effort and steps" to obtain and update the information requested and will be in compliance if they can show that they have acted in accordance with that standard. Record keeping will be all the more important in this context.

Both civil and criminal penalties may be imposed for noncompliance, including the imposition of "appropriate" financial penalties, public statements of censure, and up to two years of imprisonment. The details of these will be set out in the "near future," but H.M.R.C. have noted in the guidance that any civil penalty imposed must be proportionate to the offence committed and that there will be a robust appeals process.

Enforcement of such penalties against non-U.K. trustees in other jurisdictions may bring practical difficulties, but most trustees will be more concerned about reputational issues resulting from non-compliance and their continued ability to interact with other financial institutions. However, trustees in non-E.U. jurisdictions with strict privacy laws must consider how to balance these conflicting obligations and may require specific domestic legislation allowing them to make disclosures in these circumstances.

WHAT SHOULD TRUSTEES BE DOING NOW?

Trustees should review their assets and income to determine whether trusts they administer are relevant trusts and whether it would be appropriate to put corporate blockers in place before a tax charge arises. Trustees who incurred a U.K. income or capital gains tax liability for the first time in 2016/17 have relatively little time to register before January 5, 2018, although beneficial ownership information is not due until March 5, 2018.

Information should, in any event, be collected now in relation to relevant trusts for which internal record keeping obligations are current and ongoing.

Trustees should also consider – in conjunction with settlors and beneficiaries as appropriate – whether the beneficial class wording in the trust or in written documents from the settlor is suitably drafted. It may be prudent to include only those who have a real prospect of benefitting from the trust in order to reduce the due diligence, reporting, and record keeping burden on the trustees.

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