Trusts and FATCA: A New Reporting Regime

Aileen Keogan *Aileen Keogan Solicitor & Tax Consultant*

Background

The Foreign Account Tax Compliance Act (FATCA) was signed into US law in March 2010, effective from January 2013 as part of the US Hiring Incentives to Restore Employment (HIRE) Act 2010.[1] Its purpose is to increase revenue to the US Internal Revenue Service (IRS) by identifying offshore US accounts that could be used for tax evasion by US residents.[2] It requires institutions outside the US to pass information to the US tax authorities.

Although the legislation is controversial, it is being accepted by many countries.[3] The threat of the withholding of 30% tax on payments to institutions with investments in the US[4] and penalties for those institutions appears to have spurred its implementation outside the US.

Ireland concluded an inter-governmental agreement (IGA) with the US to facilitate the implementation of FATCA and to provide a reciprocal exchange of information regarding US financial accounts held by Irish residents. This IGA was imported into Irish law under Finance Act 2013.[5] It is based on a model[6] whereby institutions are required to report information directly to the Irish Revenue Commissioners rather than to the IRS, with Ireland then automatically exchanging information with the US annually in respect of reportable accounts. However, financial institutions, as defined, must have registered with the IRS directly to obtain a global intermediary identification number (GIIN)[7] before the IRS list is published on 31 December 2014. To ensure that the financial institution is on this list, registration should have been completed before 24 October 2014. This was the last practical date to meet that deadline.

---

1 The FATCA provisions are contained in the US Internal Revenue Code, ss1471–4.
2 This is now extended to all US citizens who have not availed of treaty relief.
3 All of the G7 countries, 42 countries that hold IGAs and 59 countries that have reached agreements in substance. Model 1, which Ireland has adopted, is reciprocal, whereby the US will also share information with the partner country. However, Latin America, the Middle East and China have not yet complied and may resist. Russia has not signed an IGA but has permitted its institutions to report directly to the US.
A fall-out is that many institutions are refusing to do business with known US citizens because of the compliance costs and enhanced risks. There is also the huge administrative cost associated with compliance.
More recently, a constitutional challenge has been taken against the IGA between Canada and the US, based on the Canadian Charter of Rights and Freedoms (privacy, search and seizure) and sovereignty issues, including the division of federal and provincial powers in Canada.
4 FATCA obliges all US paying agents to withhold tax of 30% from payments of US-source income that are made to any non-US financial institution unless that institution has entered into an agreement with the US IRS to report directly certain information on account holders who are US persons. Under the IGA, Irish financial institutions will not be subject to the 30% withholding tax on US-source income, provided that they comply with the requirements of the Irish legislation.
5 Section 104 FA 2013.
6 Model IGA, published on 26 July 2012: Model 1, similar to the model adopted by the UK, Denmark and Mexico.
7 Using IRS Form 8957.

In May 2013 the Irish Revenue Commissioners circulated draft Guidance Notes on the implementation of FATCA in Ireland and draft Financial Accounts Reporting Regulations 2013. These were updated in January 2014, again in draft form, with observations and comments invited, and the formal Guidance Notes were issued on 1 October 2014. Reporting Regulations were published in June 2014 to implement FATCA in Ireland, with effect from 1 July 2014.[8]

Summary for Trusts

FATCA has implications for trusts and estates, whether operating within or outside the US. In the case of trusts, for the purposes of the legislation, they will likely be either a "foreign financial institution" (FFI, also known as an FI) or a "non-financial foreign entity" (NFFE). The category into which a trust falls depends on both the nature of the trust assets and the nature of the trustees. The category will determine the level of reporting, who needs to report for the trust and whether registration is required for either the trust or the trustee.

> The status of a trust depends on various factors but not on whether the trust has US connections to the settlor or beneficiaries or the ownership of US assets.

As a trust will need to declare its status to any financial institution with which it has dealings (banks, stockbrokers etc.), it will need to determine its own status and then claim exemption, register as a financial institution (and then report itself) or self-certify that it is an NFFE.

As a trust will need to declare its status to any financial institution with which it has dealings (banks, stockbrokers etc.), it will need to determine its own status and claim exemption, register as a financial institution (and then report itself) or self-certify that it is an NFFE.

If a trust is a financial institution, it must register, obtain a GIIN and use this number as evidence for other financial institutions that it is FATCA compliant. It must then complete due diligence on the composition of its trust and either file annual returns detailing information about any US residents/citizens who are beneficiaries or control the trust or, if there are no US connections as beneficiaries or controllers, file a "nil" return annually.

If it is not a financial institution, it must determine whether it is a "passive NFFE" as defined and self-certify this on a US Form W-8 for giving to financial institutions with which it holds accounts to avoid those institutions withholding 30% tax.

If the trust does not hold a financial account, this should be noted on the trust file to explain why the trust has not either registered as a financial institution or self-certified as a passive NFFE.

Once the trust has determined its status, a note of this should be kept with the trust deed. The status can change if circumstances change.

> As a trust will need to declare its status to any financial institution with which it has dealings (banks, stockbrokers etc.), it will need to determine its own status and claim exemption, register as a financial institution (and then report itself) or self-certify that it is an NFFE.

The Formal Details

Various questions must be asked of the trust/estate entity to determine whether it requires registration, reporting or self-certification or need do nothing at all other than note its position on the file.

Is the entity Irish resident?

The IGA applies to trusts resident in Ireland.

Revenue has confirmed that "normal residence rules for trusts apply for the purposes of FATCA". However, different criteria apply in determining the residence of a trust under various tax heads. It had been assumed that the CGT test of residence under s54 TCA 1997 would be the relevant criteria to use in the context of the IGA, and Revenue has indicated in correspondence that, in the case of some trustees being resident outside Ireland, in effect some of the CGT tests apply. However, unusually the residence of the settlor appears to apply in the case of professional trustees.[9]

> If the trust is not Irish resident, it is not subject to Irish IGA reporting but may still need to report under the US FATCA regulations or under another IGA.

8 SI 292 of 2014.
9 Per Revenue correspondence with STEP Ireland: If all trustees are Irish resident, the trust is Irish resident. If some trustees are non-Irish resident, the trust is Irish resident if the effective administration of the trust is in Ireland. For professional trustees, the residence of the settlor at the time that the trust is established is attributed to the trust.

Is it a financial institution?

A financial institution is defined as a custodial institution, depository institution, investment entity or specified insurance company. In the case of trusts and estates, it is likely that the category "investment entity" will apply. This category includes an entity that is managed by an entity that conducts as a business one or more of various activities on behalf of a customer ("account holder"), including individual and collective portfolio management, and investing, administering or managing funds or money on behalf of other persons. If the entity's gross income from such activities equals or exceeds 50% of its entire gross income during the shorter of two periods,[10] it is deemed to be an investment entity.

Therefore a trust will be an investment entity if it engages another financial institution, such as a stockbroker, to manage the trust or its financial assets on its behalf on a discretionary basis. This is not, however, entirely clear, and the Irish Revenue Guidance Notes do not clarify what is meant by these professionally managed trusts. The latest update to the UK Guidance Notes, on the UK's similar position, is therefore helpful, stating that:

> "a trust is professionally managed
>
> › where trustees have appointed a financial institution to carry out the day to day functions of the trust beyond just the managing of investments; or
>
> › where the financial institution manages the financial assets and manages the investment strategy."

Therefore if the trust merely holds a financial account and there is no participation by the financial institution holding that account, the trust itself is not a financial institution.[11]

Is it a reporting financial institution or exempt/deemed compliant?

The financial institution then must decide if it is a "reporting financial institution" or a "non-reporting financial institution". An Irish reporting financial institution is any Irish-resident financial institution that is not exempt from FATCA reporting or deemed compliant for FATCA purposes under Annex II of the IGA or under US Regulations.

Exemption from reporting is categorised under Annex II, Part I, and includes the National Treasury Management Agency, the National Asset Management Agency, the Central Bank, Irish offices of EU institutions and of the European Investment Bank, and certain retirement funds.

"Deemed compliant" entities include sporting and charitable bodies, pension trusts, financial institutions with a local client base and certain collective investment vehicles, all listed in Part II of Annex II, which are categorised as "self-certified deemed compliant" financial institutions. These entities in general need not register with the IRS, nor will they have any reporting obligations in relation to any financial accounts on which they may have claimed the exemption in the first place.[12]

Charitable trusts would fall into this category and therefore not require registration or reporting nor have to carry out due diligence in relation to their accounts.

Other trusts that are already established under the above criteria to be investment entities, and therefore financial institutions, are treated as reporting financial institutions.

If the trust is a reporting financial institution because it is managed by a financial institution, but that financial institution is not the trustee, the trust will be required to register as an investment entity unless the trust is able to take advantage of the "sponsored investment entity" or the "owner-documented financial institution" category.[13]

Does the financial institution hold a financial account?

A "financial account" is an account maintained by a financial institution, including equity/debt interests in an investment entity. A financial institution does not, however, automatically have financial accounts.

Therefore if the trust is a financial institution, it needs to assess whether it holds any financial accounts. Likewise, if the trust is not a financial institution but holds an account with a financial institution, that financial institution must assess whether the trust account is a financial account. For example, if the financial institution is acting as an executing broker (e.g. acting not on a discretionary basis but only

10 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.

11 Unless the trustee itself is a financial institution. The Guidance Notes state that where a trustee is a financial institution or the trustee engages a financial institution to manage the trust or the financial assets of the trust, the trust itself is a financial institution. If the trust is not professionally managed, it is an NFFE.

12 See Revenue Guidance Notes, 1 October 2014, app. 1, para. 3, which states that "unless specifically stated", a self-certified deemed compliant financial institution will not have to register or submit returns or carry out due diligence under FATCA. If the entity has US-source income, it should supply the US payor with self-certification to avoid US FATCA withholding tax on that income.

13 See Revenue Guidance Notes, app. 1, para. 3H.

on an advisory basis), that facility will not be treated as a financial account.

In relation to the accounts of deceased persons, if the death is noted by the financial institution (e.g. the death certificate is noted on the account), the account will not be treated as a financial account and so it will not be reportable by the estate in the year of death or subsequently.

There may still be a need to identify the controlling person of the trust or estate (if the entity is a passive NFFE) by virtue of the self-certification route (see below).

An account held by a financial institution for a non-financial intermediary (e.g. a solicitor or estate agent) established for the purposes of:

- a court order, judgment or other legal matter where the solicitor/estate agent is acting on behalf of his or her client or
- a sale, lease, exchange of real or personal property with various conditions applying for compliance purposes

is not a financial account. It is an "intermediary account (escrow account)". A person, other than a financial institution, holding a financial account for another person is not treated as an account holder. This applies for nominees, agents, signatories, intermediaries and custodians. Where a parent opens an account for a child, the child (not the parent) is the account holder unless it is an intermediary account (escrow account).

Exempt accounts are listed in Annex II of the IGA and generally relate to pension-type accounts, profit-sharing schemes and employee share ownership trusts. If the account is an exempt account, it is not a financial account.

Where the account is not a financial account, it would appear that it is not reportable, nor is there a requirement for registration or for a "nil" return.

Does the financial institution hold a reportable financial account?

A "reportable financial account" is a financial account that is not exempt, is held by one or more specified US persons or by a passive NFFE with one or more controlling persons that are specified US persons, and is maintained by a reporting financial institution.

Where an account holder fails to respond to the financial institution's request for self-certification or other documentation to verify the account holder's status, the financial institution must treat the account as a reportable financial account.

Where the financial account is not a reportable financial account, as the account holder is not a specified US person, the reporting financial institution must make "nil" return.

What Should Be Reported and How?

The reportable information for financial institutions that maintain financial accounts includes:

- the name, address and US tax identification number (TIN) of each account holder who is a specified US person,
- the account number,
- the name and identifying number of the reporting Irish institution,
- the account balance or value and
- the amounts paid or credited to the account holder.

If it has been established that an account holder is a US person, the financial institution must obtain a US TIN for that person. There are various provisions in relation to pre-existing and new accounts in this respect. The accounts are reportable, if they are not exempt, for all subsequent years unless the account holder ceases to be a US person. There are certain de minimis amounts that are exempt from reporting (e.g. USD50,000 for deposits).

Where a trust or an estate is listed as the holder of a financial account, the trust, rather than the owner or beneficiary, is to be treated as the account holder.

In the case of a trust that is a financial institution, unless it avails of the sponsored investment entity or the owner-documented financial institution category, it will need to report in respect of persons who are the beneficial owners of all or a portion of the trust, persons who are beneficiaries entitled to mandatory distributions from the trust (directly or indirectly) and persons who are beneficiaries and who receive discretionary distributions from the trust in the reporting period.

This information must be reported to Revenue within six months of the year-end to which the information relates: 2014 information is to be reported by 30 June 2015. It is anticipated that the majority of the reporting will be carried out through ROS (Revenue On-line Service). Otherwise, the financial institution is not FATCA compliant and is categorised as a "non-participating financial institution". In the case of Irish financial institutions, this will apply to those that do not comply with the guidelines and legislation.

It is possible for a trust that is a financial institution to provide a "designated withholding agent"[14] with all relevant information and arrange that this agent reports to the IRS/Irish Revenue on behalf of the trustee.

The identification of the account holder may become an issue, as the financial institution is expected to apply due diligence procedures to identify the account holder and ascertain whether he/she/it is a "specified US person".[15]

A person is a US person if he/she/it is resident in the US or is a US citizen. A trust is a US person if:

- a court in the US would have authority under applicable law to render orders or judgments concerning substantially all issues regarding the administration of the trust and
- one or more US persons have the authority to control all substantial decisions of the trust, or an estate of a decedent who is a citizen or resident of the US.

The due diligence process requires that:

- the financial institution identify certain defined US indicia linked to an account holder[16] or
- the account holder self-certify his/her/its status to the financial institution.

Financial institutions can rely on self-certification in the following circumstances. Typically this is done on a US form known as the IRS Form W-8 or W-9.

Individual account holders

For new accounts, a person may confirm that he or she is not resident in the US and not a US citizen by using the financial institution's existing anti-money-laundering "know your customer" (KYC) procedures. If the confirmation is seen to be reasonable and is checked against other records of that person, this is acceptable. For existing accounts, if indicia suggest that the account holder is a US person, further inquiries are required to establish the veracity of the self-certification, and this also depends on the level of funds in the account (referring to low-value and high-value accounts).

Entity account holders

If the entity is identified as a specified US person, the account is reportable unless self-certification determines it is not such a person. Generally, there is no *de minimis* amount for this.

If the financial entity is not an Irish financial institution (or one of another recognised State), the financial institution needs to establish whether the entity is a certified deemed compliant financial institution (as mentioned above), an exempt beneficial owner or an excepted foreign financial institution. If the entity is a passive NFFE, the financial institution must obtain self-certification from the account holder to establish its status unless information is publicly available or already in its possession whereby it can be reasonably determined to be an active NFFE. If the trust is identified as a passive NFFE, the financial institution must consider whether any of the controlling persons of that entity are US citizens or tax resident in the US and in this regard can rely on KYC information already gathered for those accounts holding less than USD1m or, in the case of accounts exceeding that, the account holder or the controlling person can self-certify.

Non-financial foreign entity

Where a trust is not a financial institution and holds a financial account with a financial institution, it will be a "non-financial foreign entity" (NFFE).

In such cases the trust is required to prove self-certification to the financial institution in relation to its status as a passive or active NFFE, as applicable, so that the financial institution with which the trust holds a financial account can carry out due diligence for that NFFE.

A "passive NFFE" is an NFFE that is not active. An "active NFFE" is any NFFE that meets one of the various criteria, including that less than 50% of the NFFE's gross income for the preceding calendar year (or other appropriate reporting period) is passive income and less than 50% of the assets held by the NFFE during the preceding calendar year (or other appropriate reporting period) are assets that produce

---

14 Such as a participating financial institution that agrees to undertake the additional due diligence and reposting required under the US Regulations to treat the financial institution as an "owner-documented financial institution", and so the entity itself need not register with the IRS. If a financial institution relies on a third-party service provider to fulfil its obligations under FATCA, the obligations remain those of the financial institution.

15 As set out in Chapters 7–10 of the Revenue Guidance Notes.

16 Indicia include: identification of the account holder as a US resident or citizen, an unambiguous indication of a US place of birth, a current US mailing or residence address, a current US telephone number, a standing instruction to transfer funds to an account maintained in the US, a current effective power of attorney or signatory authority granted to a person with a US address, a "care of" or "hold mail" address (where a review of paper records will then need to be carried out).

or are held for the production of passive income. For FATCA purposes, income received on assets used as capital in a general insurance business should be treated as active rather than passive income. "Passive income" is defined as including gross income consisting of dividends, interest, rents, royalties and excess gains over losses on sales of certain property or on foreign currency exchange.[17]

Where a passive NFFE has controlling persons or beneficiaries that are US persons, its accounts will be reportable accounts, but it is the financial institution that holds these accounts that will be required to report on the accounts. The trust will need to provide the details to the financial institution.

Practical Approach

It is expected that most Irish family trusts would be either:

› financial institutions (where the trust fund is managed by a financial institution on a discretionary basis) or

› passive NFFEs (as the greater part of the income will be passive).

On this basis, the following checklist would be useful for practitioners dealing with trusts.[18]

› Is the trust resident in Ireland?

  › If not, this is not of concern under the Irish IGA but may be under the FATCA Regulations that pertain to the place of its residence.

  › If it is Irish resident, then continue to the next question.

› Is the trust resident in Ireland?

  › If not, this is not of concern under the Irish IGA but may be under the FATCA Regulations that pertain to the place of its residence.

  › If it is Irish resident, then continue to the next question.

› Is the trust a charity? If so, it is exempt and does not need to register or report under the Irish IGA. It is likely to need to self-certify its status to financial institutions with which it deals.

› If the trust is a financial institution, it should register and report directly or appoint a third party to report for it.

› How is it determined that the trust is a financial institution?

  › Is the trust managed by professional trustees?[19] If so, it is a financial institution.

  › Does the trust have financial assets whereby more than 50% of its income comes from investing, reinvesting or trading in such investments? If not, it may not be a financial institution. If the income has reached this threshold, the trust is a financial institution.

  › Does the trust engage an adviser to manage its funds on a discretionary basis? If so, even if the trust does not derive more than 50% of its income from its investments, it is a financial institution.

  › Does the trust have a corporate trustee which is itself a reportable financial institution? If so, the corporate trustee should report on behalf of the trust (where the trust itself does not register or report). The corporate trustee must also register and report as a financial institution itself. This trust itself is then an owner-documented trust.

› If the trust is not a financial institution, it is an NFFE and does not need to register or report. However, it will need to self-certify on a Form W-8 that it is a passive NFFE or consider whether it is an active NFFE.

Conclusion

All Irish trusts and trustees, whether or not they have any known US connections, need to consider their status under the Ireland–US IGA. If they are required to register, they must have done so by 25 October 2014. Otherwise, there will be withholding tax from 1 January 2015 and potential penalties.

Financial institutions with which the trusts hold funds will be expecting each trust to produce a GIIN indicating that the trust is registered before 1 January 2015 or produce a certificate that confirms its status. It is likely that these procedures will arise as part of the

17 See the Revenue Guidance Notes, app. 2, para. 9.
18 STEP UK has provided a very useful flowchart for the UK–US IGA, which is very similar to the Ireland–US IGA, as well as practical examples and a guide; see http://www.step.org/fatca.
19 An entity carrying on business in Ireland where more than 50% of its gross income is attributable to trading in money market instruments, portfolio management or the investment and administration of funds.

financial institutions' KYC procedures (either on their review of their procedures for existing accounts or on the initial set-up of the accounts).

Failure to confirm the trust's status will leave financial institutions (including, potentially, the trusts themselves) open to penalties and will leave trusts vulnerable to withholding tax as payees.

Practitioners should identify and classify the entities comprising their practice and the client entities, such as trusts, with which they are connected. The terms of engagement for a practice should be amended to reflect the fact that practitioners will need to consider FATCA and any necessary reporting on behalf of the trust as a client in respect of any dealings with that trust. If you are acting for trusts, you will need to advise your clients, the trustees, of their reporting requirements, including future reporting in a change of circumstances. If practitioners themselves or their partners are trustees, they need to be aware of what reporting requirements a trustee has immediately and on an ongoing basis.

Practitioners should identify and classify the entities comprising their practice and the client entities, such as trusts, with which they are connected. The terms of engagement for a practice should be amended to reflect the fact that practitioners will need to consider FATCA and any necessary reporting on behalf of the trust as a client in respect of any dealings with that trust.

Any entities that are identified as financial institutions should have been registered for a GIIN from the IRS before 24 October 2014.

Practitioners should put in place adequate systems to identify and record US persons – this identification is required now, even if reporting is not required until 2015. Such reporting will be to the Irish Revenue Commissioners if the trust is a financial institution or on the Form W-8 to the financial institution with which the trust has dealings. There will either be a "nil" return filed or a return detailing the US persons who are beneficiaries or control the trust.

An entity that is identified as a passive NFFE will be asked by financial institutions in due course to confirm that it is an NFFE using a Form W-8, so that the financial institution can operate the account for that entity. In such a case, the Form W-8 will allow the entity to list the US persons relevant to the trust.

Any changes to the status of the trust, the trustees or the beneficiaries will need to be notified to Revenue directly or via the financial institution with which the trust has dealings, as appropriate.

This additional layer of regulation for practitioners and trusts may appear excessive and not necessarily productive, given the extensive exchange-of-information facilities in double taxation agreements; however, this time it is hitting the financial institutions directly and could be said to be akin to the third-party returns that practitioners file in Ireland. It remains to be seen what level of exchange of information will be forthcoming to the Irish authorities from the US by way of reciprocity, and indeed whether the US will be able to filter sufficiently the level of worldwide reporting that will be made to it under these arrangements. This new regime is being monitored by other governments to see if it is an effective method of identifying non-compliant offshore funds of their countries' taxable persons, and it has been indicated that other countries may follow the US lead in requiring reporting. Hopefully, if this is to occur, it can be done in a manner consistent between countries following a model promoted by an internationally recognised body such as the Organisation for Economic Co-operation and Development, similar to the way in which double taxation agreements are applied, so that practitioners will not have to follow different rules for different jurisdictions. It is also regrettable that the current forms that must be filed originate from the US and are not Irish-sourced forms, as the terminology of the US forms are very different and not entirely clear to us: although many of the questions on these forms will not be relevant for practitioners, there is a need to understand them all to assess their relevance.

This article is an adjusted extract from a recent lecture given by Aileen Keogan at the Annual STEP (Society of Trust and Estate Practitioners) Ireland/Law Society of Ireland Joint Conference and is reproduced with their kind permission.

Read more on TaxFind FATCA and the CRD: the Global Development of Financial Information Reporting, *Irish Tax Review*, Issue 2, 2014