

# Hiding in plain sight: how non-US persons can *legally* avoid reporting under both FATCA and GATCA

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## Abstract

This article addresses gaping holes in both FATCA and GATCA reporting when it comes to non-US persons. Holes where sensitive information can stay private and avoid prying eyes. Maybe these holes will close. But only if and when the USA—now, ironically, the greatest of all hiding places—chooses to do so.

Do not hold your breath.

Let me be very clear upfront: this article is *not* about how to avoid reporting to keep undeclared funds hidden from tax authorities. Avoiding reporting to evade taxes is illegal. As is assisting people in that unsavoury pursuit. People go to gaol for those activities.

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Fact is, there is no way to *legally* avoid reporting if the purpose is to evade taxes. Do not let your clients go there. And do not in any way assist clients who want to go there. Not only is assisting tax evasion illegal, but if your clients get caught, you will be the first person they do in.

No, this article is about how non-US persons who want to avoid reporting *for perfectly legitimate reasons*—reasons like privacy and personal security—can do so legally. Indeed, privacy is a basic human right.<sup>1</sup> Therefore, every person has the right to minimize the amount of data flowing to others, including to the government, provided doing so does not violate any laws. Including, of course, anti-avoidance laws.

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## Introduction

The article begins by addressing FATCA.<sup>2</sup> More specifically, the article describes the information the US promises to give its FATCA Partner Jurisdictions under the so-called ‘reciprocal’ FATCA Inter-Governmental Agreements (IGAs). Astonishingly little, as it turns out. And what scant information the USA does promise to give will prove virtually useless to its IGA partners. Put it this way: non-US persons who truly want to keep their financial

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1. See, eg, art 12 of the Universal Declaration of Human Rights and Section I, art 12 of the EU Convention of Human rights.

2. ‘FATCA’, of course, refers to the US’s Foreign Account Tax Compliance Act. FATCA was enacted as part of the Hiring Incentives to Restore Employment Act of 2010 (P.L. 111-147) on 18 March 2010. FATCA consists of five parts, only the first of which is relevant to this article. That part (Part I—Increased Disclosure of Beneficial Owners) is enacted as ss 1471–1474 of the US Internal Revenue Code. As used in this article, FATCA also refers to the final Treasury Regulations under the statute, additional IRS interpretive guidance, and the various model and country-specific IGAs designed to further FATCA’s ends.

information private under FATCA have no difficulty doing so legally. The article explains why. And how.

*Non-US persons who truly want to keep their financial information private under FATCA have no difficulty doing so legally*

The article next shows how reporting under GATCA<sup>3</sup> can be legally avoided. Again, easily: as long as the USA does not sign up for GATCA—a safe bet for the foreseeable future—one need to only move one's accounts to the USA. Welcome to the new Switzerland. Indeed, if, as some people have recommended, the USA is treated as a GATCA Participating Jurisdiction even though it does not actually sign up, then the assets will not even have to go to the USA—provided they are held in an appropriate structure.

The article then explains what type of trust can avoid both FATCA and GATCA reporting, including GATCA reporting if the USA is treated as a Participating Jurisdiction and the assets are not in the USA. Since this structure requires a US-resident trustee, the article explains how the trust should be structured to avoid US taxation.

The article concludes by examining FATCA's and GATCA's potentially pesky 'anti-avoidance' rules. Under FATCA, restructuring often will not be necessary to prevent disclosure of non-US persons. But even if it is, any restructuring will not violate any relevant FATCA anti-avoidance rules because, well, there are not any.

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Under GATCA, it is a little trickier, but it really depends on the specific anti-avoidance rules of the jurisdiction where the account is held. Even so, any restructuring that occurs before the anti-avoidance rules take effect will not be covered. One obviously has to check each specific country's rules to determine their effective date. Generally, however, it will not be before that country's general GATCA start date. For early adopters, that is 1 January 2016. For others, it is at least a year later. So, even for accounts in early-adopter countries, there should still be time to put in place strategies to legally avoid GATCA reporting.

## FATCA

As originally constructed, FATCA was a purely one-way street. Under the FATCA statute<sup>4</sup> and Treasury Regulations,<sup>5</sup> non-US financial institutions are required give the US data about US persons. The USA is not required to give anything in return.

This unilateral approach did not sit too well with some countries. After all, US taxpayers are not the only tax evaders in the world. Besides, FATCA's diktat was all well and good except for one inconvenient fact: it is illegal in most countries for local financial institutions to disclose client information to unauthorized persons, including to the US government. Therefore, in the absence of local FATCA

3. As used in this article, 'GATCA' is short for 'Global FATCA' and refers to the OECD's Standard for Automatic Exchange of Financial Account Information in Tax Matters, available at <<http://www.oecd.org/ctp/exchange-of-tax-information/standard-for-automatic-exchange-of-financial-information-in-tax-matters.htm>> accessed 3 October 2015. GATCA is based extensively on FATCA except that it extends the search for tax evaders beyond FATCA's aim (US taxpayers) to taxpayers from essentially every country. Many people, including the OECD, refer to GATCA as 'the Common Reporting Standard' or 'CRS' for short. That nomenclature is misleading. The Common Reporting Standard is but one part of FATCA and takes up just 33 pages of the entire 311-page document. GATCA comprises: (i) an Introduction (ii) a Model Competent Authority Agreement (MCAA), (iii) the Common Reporting Standard, (iii) extensive Commentaries on both the MCAA and the Common Reporting Standard, and (iv) various Annexes. The MCAA describes the data that Participating Jurisdictions agree to exchange. The Common Reporting Standard contains the due diligence and related rules Financial Institutions must apply to ensure that Participating Jurisdictions receive the relevant data. The CRS is, therefore, the very rough equivalent of Annex I of the FATCA IGAs, which contain FATCA's due diligence rules for FFIs in IGA countries. Therefore, using 'the Common Reporting Standard' or 'CRS' to refer to all of GATCA is the equivalent of using 'Annex I' to refer to all of FATCA. Moreover, the name 'Common Reporting Standard' is bland and non-descriptive in any event: It gives little indication of what GATCA is really about. 'Common' to whom? 'Reporting' what? 'Global FATCA' is much more helpful, especially to people who are already familiar with FATCA. So . . . 'as for me and my household' (Joshua 24:15) we will stick with 'Global FATCA', or 'GATCA' for short.

4. US Internal Revenue Code, ss1471–1474.

5. US Treasury Regulation ss 1.1471-1ff.

implementing legislation, the USA could demand all the data it wanted from non-US financial institutions, and it could threaten penalties in the form of withholding taxes (which it did), but it would not do the USA any good. The threat of withholding taxes by the mighty USA may be scary to financial institutions, but not as scary as the threat of sanctions for violating the law of the very jurisdiction where the financial institution is located. Thus, it was essential that other governments get on board with FATCA or it was going to be 'full of sound and fury, signifying nothing'.<sup>6</sup>

So, if FATCA was to mean anything at all, the USA had to entice other countries to play along. This did not prove difficult for two reasons. First, non-US financial institutions themselves wanted to be able to comply with FATCA so they would not be hit with its withholding-tax penalty. They lobbied their governments to allow FATCA reporting. Second, the governments themselves saw an opportunity: if they could convince the USA to reciprocate and provide information about their own taxpayers, FATCA would be win-win for both governments.

The USA agreed. Sort of.

True enough, the USA has subsequently entered into numerous FATCA IGAs, many of which are 'reciprocal'.<sup>7</sup> But reciprocal is as reciprocal does. Table I illustrates what data IGA partner countries must give the USA and, for those countries with reciprocal IGAs, what substantially less information the USA agrees to give in return.

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To summarize, the IRS will *not* give its 'reciprocal' FATCA partners any information about:

- Depository (ie cash) accounts held by entities, even entities resident in the FATCA partner country,
- Non-cash accounts, whether held by individuals or entities, even those that are resident in the FATCA partner country, *unless* the accounts earn *US source income*, or
- The controlling persons of any entities, whether the entities are from the reciprocal partner country or from third countries, and even if those entities are owned and controlled by residents of the reciprocal partner country

Thus, all a non-US individual has to do to avoid disclosure under a 'reciprocal' IGA with the USA is to hold the following accounts in a US financial institution:

- Cash Accounts:
  - Hold the account through an entity, or
- Non-Cash Accounts:
  - Block the account for assets that produce US-source income (eg US securities), or

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6. Macbeth, Act 5, Scene 5. The quote is part of Macbeth's morbid description of life:

Life's but a walking shadow, a poor player  
That struts and frets his hour upon the stage  
And then is heard no more.  
It is a tale told by an Idiot,  
Full of sound and fury, signifying nothing.

7. Some countries do not care to receive information from the USA about their residents and have therefore entered into 'non-reciprocal' IGAs. These countries include ones that either do not have any income tax (eg the Bahamas, Bermuda, the British Virgin Islands, and the Caymans Islands) or have only a territorial income tax (eg Hong Kong and Singapore).

For a full list of IGA countries, see: <<http://www.treasury.gov/resource-center/tax-policy/treaties/Pages/FATCA-Archive.aspx>> accessed 3 October 2015. The list is divided into several parts, specifically, (i) those with actual so-called 'Model 1' IGAs in place, (ii) those with actual so-called 'Model 2' IGAs in place, (iii) those that have 'reached an agreement in substance' on an IGA as of 30 June 2014, and (iv) those that have 'reached an agreement in substance' on an IGA as of 30 November 2014. These last two categories are treated as if they had an actual IGA in place (so-called 'deemed IGAs') and are also further subdivided between Model 1 and Model 2 IGAs. Only actual Model 1 IGAs can be reciprocal, though not all of them are. All actual Model 2 IGAs and all deemed IGAs (whether Model 1 or 2) are non-reciprocal. However, many countries with deemed Model 1 IGAs are expected to subsequently enter into actual Model 1 IGAs that are reciprocal.

Unfortunately, the list does not indicate which of the actual Model 1 IGAs are reciprocal and which are not—one must read the text of the relevant IGA to garner that information.

Table I

Type of account	IGA partner must give	Does USA reciprocate?
Depository (ie cash) accounts	Account balance or value	No
	If held by an <b>individual</b> :	
	• Gross interest paid	Yes, if the account earns \$10 or more of interest
	If held by an <b>entity</b> :	
	• Gross interest paid	No
Custodial	Account balance or value	No
	Gross interest and dividends	US <i>source</i> income only, but only if
		• already subject to reporting, and
		• only with respect to individuals or entities resident in the partner jurisdiction
	Other income generated with respect to assets held in the account	No
	Gross proceeds from the sale or redemption of property	No
Accounts <i>other than</i> Custodial and Depository Accounts	Account balance or value	No
	Gross amount paid or credited, including redemption payments	No
Accounts held by passive NFEs	Information on controlling persons	No

- If one wants to invest in US securities, then—just as with cash accounts above—hold the account through an entity<sup>8</sup>

Now, some words of warning about holding accounts through entities. Remember the UBS scandal. Under the Qualified Intermediary rules, as applied literally, accounts held by non-US entities are not disclosed to the USA even if they earn US source income and even if the owner or controller of the entity is a US person. UBS fully exploited this loophole by encouraging its tax-evading US clients to use non-US entities so that they could not only avoid disclosure but also invest in US securities (through these entities) while doing so.<sup>9</sup> These entities were, of course, mere shams, tools to facilitate tax

evasion. As such, they offered no protection at all, a point that UBS and its clients learned the hard way.

By the same token, entities held by non-US persons holding US accounts *in order to evade tax* should be treated as shams as well. But the same should not be true of entities that are used by *fully compliant taxpayers* who merely wish to minimize reporting for legitimate reasons and who respect all corporate formalities. Assuming, of course, they do not violate any anti-avoidance rules, which we will address later.

## GATCA

What about disclosure of non-US persons under GATCA? As is explained more fully below, provided the accounts and any entities through which they are

8. Note: if the entity is resident in a reciprocal IGA partner jurisdiction and the account earns US-source income, the entity itself will be reported. However, the beneficial owners of the entity will not be reported.

9. Lest the reader be wondering, your author was not involved in any way while an employee of UBS (or at any other time) in any of these activities.

held are located in the USA for GATCA purposes, disclosure will not be a problem as long as the USA does not enter into GATCA.

The USA isn't likely to enter into GATCA any time soon for at least two reasons. First, most of the data that GATCA requires to be exchanged is not currently reported to the IRS by US financial institutions. Naturally, the USA can't promise to give data it doesn't collect. Therefore, unless and until US law is changed to mandate GATCA-style reporting, the USA simply can't agree to the sort of comprehensive information exchange GATCA requires.<sup>10</sup>

Second, there is little likelihood that US law will be amended in the near future to allow the IRS to collect the required data. The USA already gets all the data it needs on US taxpayers via FATCA, so it does not need GATCA to find its own tax evaders. Moreover, the Republicans, who control both houses of Congress, do not want to hurt the US's banking industry.<sup>11</sup> It is no secret that US banks, particularly in Miami, are awash in undeclared Latin American money. Expanding data exchange would only drive this money offshore and destroy the US's current competitive advantage.<sup>12</sup> How ironic—no, how *perverse*—that the USA, which has been so sanctimonious in its condemnation of Swiss banks, has become the banking secrecy jurisdiction *du jour*.

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As long as the USA does not enter into GATCA, its financial institutions will not be reporting any non-US persons under that regime. So all one has to do to avoid reporting under GATCA is move one's assets to a financial institution resident in the USA for GATCA purposes. Now, one has to be careful if the assets are held through a client structure that is itself resident in a participating jurisdiction—in that case, even though the US financial institution (eg bank where the assets are booked) will not be reporting anything under GATCA, the client structure itself may be reporting, depending on whether it is a Financial Institution or Non-Financial Entity. As is explained later, however, a trust with a US-resident trustee but structured as a non-US trust for US tax purposes is ideally suited for this purpose, ie, it will avoid GATCA (and FATCA) reporting, while at the same time avoiding US taxation.

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Of course, if the USA did enter into GATCA, then all bets would be off. Or would they? The USA would still have an advantage over other jurisdictions

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10. Indeed, it is precisely because the data US financial institutions report to the IRS is so limited that the US's obligations under its 'reciprocal' FATCA IGAs are so narrowly drawn. Under current US law, US financial institutions report only the following to the IRS concerning accounts held by non-US persons: (i) interest in depository accounts held by individuals that earn \$10 or more of interest, and (ii) limited categories of US-source income earned on other accounts, whether held by individuals or entities. The US's obligations under 'reciprocal' IGAs faithfully track these limitations.

11. I do not mean to pick on Republicans. There are many Democrats who are equally staunch in their support of the US banking industry, but the Democrats do not control Congress. Even if they were to gain control of both houses and keep the White House in the next election (November 2016)—which is extremely unlikely—there is no guarantee Democrats would pass the necessary legislation. The US banking lobby has many friends on both sides of the aisle.

12. Indeed, in 2013, Republican Congressman Bill Posey, who represents Florida's Eight Congressional District, wrote to Jack Lew, Secretary of the Treasury, decrying even the reporting of interest earned on depository accounts by non-US persons. The letter is available at <[http://www.repealfatca.com/downloads/Posey\\_letter\\_to\\_Sec.\\_Lew\\_July\\_1,\\_2013.pdf](http://www.repealfatca.com/downloads/Posey_letter_to_Sec._Lew_July_1,_2013.pdf)> accessed 3 October 2015. Congressman Posey claimed that reporting interest on depository accounts 'would not bring one penny into the U.S. Treasury', 'would discourage investment in the United States', and 'would further impose costly compliance costs on American banks and credit unions, and their depositors and members'. The letter also railed against both the reciprocal IGAs' commitment to seeking legislative changes enabling fully equal levels of data exchange and the Obama administration's proposal to give the US Treasury Department authority to achieve just that. The resistance to data exchange is no less strong today in Congress than it was in 2013. Given the current political climate, there is little or no chance the USA will sign up to GATCA in the near term.

Table II

USA becomes a participating jurisdiction	USA remains a non-participating jurisdiction
US FIs do not have to treat IE FIs in Non-Participating Jurisdictions as Passive NFEs, ie, US FIs do not have to look through these entities and report their Controlling Persons (CPs) to the CPs' home countries	US FIs have no GATCA obligations
FIs in every other Participating Jurisdiction must treat IE FIs in Non-Participating Jurisdictions as Passive NFEs, ie, must look through these entities and report their CPs to the CPs' home countries	FIs in Participating Jurisdictions must treat IE FIs in Non-Participating Jurisdictions ( <i>this would include US IE FIs</i> ) as Passive NFEs, ie, must look through these entities and report their CPs to the CPs' home countries

courtesy of the OECD. Under GATCA, a so-called 'Investment Entity' Financial Institution (IE FI) resident in a Non-Participating Jurisdiction must be treated as a Passive Non-Financial Entity (Passive NFE) and looked through for its Controlling Persons.<sup>13</sup> The rule is designed to prevent client structures such as trusts and holding companies, which will generally be IE FIs, being established in Non-Participating Jurisdictions so as to hide otherwise reportable persons. Since the structures themselves would be in Non-Participating Jurisdictions, they would not be doing any reporting themselves. Pursuant to this rule, however, any Financial Institution that is in a Participating Jurisdiction that holds an account for such an entity will have to treat the structure as a Passive NFE and report its Controlling Persons to any partner jurisdiction where they reside. Unless, that is, the Financial Institution where the account is held is in the USA—if the USA does participate

in GATCA, its Financial Institutions would be exempt from this look-through rule.

The Introduction to GATCA provides that:

it is compatible and consistent with the CRS for the United States to not require the look through treatment for investment entities in Non-Participating Jurisdictions.<sup>14</sup>

The first column in Table II illustrates this form of American Exceptionalism. No other country is offered this preferential treatment.<sup>15</sup>

Note, though, that this 'out' for the USA does not mean that, if it remains a Non-Participating Jurisdiction, Financial Institutions in Participating Jurisdictions do not have to look through IE FIs resident in the USA. In other words, the exception for the USA represented by the first box below "USA becomes a participating jurisdiction" is not to be confused with

13. GATCA, 58 (the definition of 'Passive NFE' in art VIII, D.8 of the Common Reporting Standard).

14. GATCA, Introduction, para A.5 (bottom of page 10). The reasons the OECD gives for this position are unconvincing. The first is that 'the intergovernmental approach to FATCA is a pre-existing system with close similarities to the CRS'. Okay, but what does that have to do with exempting the USA from treating IE FIs in Non-Participating Jurisdictions as Passive NFEs and looking through them for their Controlling Persons? Nothing at all.

The second reason given by the OECD is 'the anticipated progress towards widespread participation in the CRS'. The gist here, I suppose, is that the more countries adopt CRS, the fewer Non-Participating Jurisdictions there will be, and therefore the fewer occasions there will be to treat IE FIs in Non-Participating Jurisdictions as Passive NFEs. Again, true enough. But how does that justify giving the USA—and only the USA—a pass on having to look through such structures, few as they might be?

No, the real reason the USA is given a pass here is that the IRS does not collect data on ownership or controlling interests in entities with financial accounts, so it could not enter into CRS if it had to provide data on such people. Every other country must change its law to ensure collection of this data (if not already collected), but that is a bridge too far for the USA. Might is right.

15. Interestingly, the exception given to the USA applies only to IE FIs in Non-Participating Jurisdictions that are treated as Passive NFEs. There is no similar exception for entities that are actual Passive NFEs, whether they be in Participating or Non-Participating jurisdictions. In other words, the OECD has not said that, if the USA joins GATCA, it will not have to look through actual Passive NFEs for Controlling Persons. Presumably, this was an oversight and the USA would be given an exception here as well.

It is also noteworthy that the OECD does not exempt the USA (if it becomes a Participating Jurisdiction) from any of the other requirements of GATCA. There are lots of data—not just data about Controlling Persons—that GATCA requires to be reported but that the IRS does not currently collect, eg, account balances, non-US-source income, and gross proceeds from the sale or redemption of property. US law would have to be changed to require collection of this data before the USA could join GATCA. But if the law could be changed to require collection of that data, why could not it also be changed to require collection of data about Controlling Persons? It is odd that the OECD would give the USA an exception for just the latter, and then only if the entity is an IE FI in a Non-Participating Jurisdiction, and not if it is an actual Passive NFE.

the rule expressed in the second box below “USA remains a non-participating jurisdiction”.

Now, some have suggested that, even if it does not participate in the GATCA, the USA should nevertheless be treated as a participating jurisdiction.<sup>16</sup> There is no principled basis for this position. However, given the US’s political muscle, one cannot rule out this possibility. If it did come to pass, the US’s already considerable competitive advantage over other jurisdictions would skyrocket. The result would be that entities such as US-resident funds and client structures that were IE FIs could book their assets anywhere—not just in the USA—and still avoid disclosure of their Controlling Persons. That would be an unrivalled and enviable position indeed: As long as the IE FI account holder itself were resident in the USA, it would be opaque and its Controlling Persons would be completely sheltered from scrutiny by offshore banks. Beat that, rest of the world!

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Pulling the above FATCA and GATCA analysis together leads to the conclusions in [Table III](#) based on these assumptions:

- The account holder is a non-US Person.
- The account holder is resident in a FATCA Reciprocal IGA Jurisdiction.

- The account holder is resident in a GATCA Participating Jurisdiction.
- All assets are booked in a US-resident bank.

The advantage of booking the assets in the USA are made stark when one compares the above conclusions to what would happen if the assets were booked outside the USA in a GATCA Participating Jurisdiction. In that case, there would be full GATCA reporting by the bank or, if the entity were a Financial Institution in a Participating Jurisdiction, by the entity itself. If the entity were an IE FI in a Non-Participating Jurisdiction, then the entity would not report anything, but the bank would treat the entity as a Passive NFE, would look through it, and would report its Controlling Persons.<sup>17</sup>

## Holding structures

As can be seen above, introducing an entity as the account holder complicates matters. Under a reciprocal FATCA IGA, the complication is minor: the USA will not report the entity’s Controlling Persons and will report the entity itself only if the entity is resident in the reciprocal IGA country (and even then, only if the entity invests in US securities). In other words, if the entity is, say, a British Virgin Islands (BVI) company, the entity will not be reported at all because the BVI does not have a reciprocal IGA with the USA. Therefore, fully tax-compliant non-US persons who are resident in a reciprocal IGA country but who wish to avoid disclosure for legitimate reasons can use a company in a non-reciprocal IGA country to hold the account (assuming, of course, all corporate formalities are observed). Piece of cake!

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16. See, eg, the comments attributed to Julia Tonkovich, attorney-adviser, Treasury Office of International Tax Counsel, in *US Position on Common Reporting Standard Problematic for US Trusts and Funds*, Kristen Parillo, 2015 World Tax Daily 154-2, Tax Analysts Doc 2015-18477, 11 August 2015: ‘CRS “would not have happened . . . were it not for FATCA” and “it wouldn’t make sense to put the U.S. in the same category as the five jurisdictions that have not yet committed to the CRS (Bahrain, the Cook Islands, Nauru, Panama, and Vanuatu)’. Compare those comments to the extremely non-committal ones of Pascal Saint-Amans, Director of the OECD Centre for Tax Policy and Administration, at a media briefing before the October 2014 Global Forum meeting, as cited in the above article. Saint Amans said that the USA is ‘more than an early adopter . . . ; it’s the driver, it’s the country that made [CRS] largely possible’ with FATCA. However, he added that the US’s special situation makes it difficult to classify its commitment to the CRS because it has the most advanced mechanism, has committed to some form of reciprocity that is not yet complete, and has developed the legislation that forms the basis for implementing the CRS.

The UK, for its part, does not list the USA as a Participating Jurisdiction in its FATCA and GATCA implementing regulations (Schedule I of the International Tax Compliance Regulations 2015). It will be interesting to see how other jurisdictions treat the USA in their GATCA legislation.

17. This is, unless the entity was resident in the USA but the USA was nonetheless treated as a Participating Jurisdiction even though it did not actually sign up to GATCA.

Table III

Account held by	USA does not enter into GATCA	USA does enter into GATCA
Individual	No FATCA or GATCA reporting by the US Bank provided (i) the assets are not in a Depository (ie cash) Account, and (ii) the account is blocked for US securities	i. No FATCA reporting provided by the US bank (a) the assets are not in a Depository (ie cash) Account, and (b) the account is blocked for US securities ii. Full GATCA reporting by the US bank
Entity	No FATCA reporting by the US bank provided the account is blocked for US securities No GATCA reporting by the US bank Full GATCA reporting by the entity if it is a Financial Institution No GATCA reporting by the entity if it is a Passive NFE	No FATCA reporting by the US bank provided the account is blocked for US securities If the entity is a Financial Institution: i. No GATCA reporting by the US bank ii. Full GATCA reporting by the entity If the entity is a Passive NFE: i. Full GATCA reporting by the US bank of the entity ii. No GATCA by the US bank reporting of the entity's Controlling Persons iii. No GATCA reporting by the entity

Things are different under GATCA if the entity is a Financial Institution in a Participating Jurisdiction. In that case, even if the assets are booked in the USA, the entity itself will report its own account holders, assuming they are resident in Participating Jurisdictions. Most client structures are Financial Institutions (typically, IE FIs). Therefore, the only practical way to avoid GATCA reporting with most client structures is to use an entity resident in a Non-Participating Jurisdiction. As mentioned previously, if the assets are booked outside the USA, that

will not work because the bank will treat the entity as a Passive NFE and report its Controlling Persons. But if the assets are booked in the USA, it will work. Problem is, there are going to be few Non-Participating Jurisdictions.<sup>18</sup> Other than the USA.

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18. Currently, only the following five of the 127 Global Forum members have not committed to implementing GATCA: Bahrain, Cook Islands, Nauru, Panama, and Vanuatu. OECD Secretary-General Report to G20 Finance Ministers, Istanbul, Turkey, February 2015, at page 20. (The complete list of Global Forum members is available on the following website: <<http://www.oecd.org/tax/transparency/membersoftheglobalforum.htm>>) accessed 3 October 2015 There are around 60 countries that are not members of the Global Forum, so Global Forum membership is by no means universal. Nevertheless, the political pressure to join GATCA is only going to increase on countries that have not yet committed, whether they be Global Forum members or not.

The Table listing the five Global Forum members who have not yet committed to GATCA contains two other lists as well, specifically, a list of Global Forum members that have undertaken to exchange information beginning in 2017 (these are the so-called 'early adopter' countries) and a list of members that have undertaken to exchange information the following year ('second wave' countries). There are more than 30 other Global Forum members that are not included in the early-adopters list, the second-wave list, or the list of five non-committed countries. Presumably, these 'missing' countries have committed to implementing GATCA, just not as soon as the early-adopters or second-wave countries—otherwise, they would join the five countries on the non-committed list.



Bingo! A US-resident entity account holder with a US account will not be reportable under GATCA or FATCA. But one has to be careful. If the entity is resident in the USA for US tax purposes, it will—like all US persons—be subject to worldwide income tax and US reporting obligations. Thus, the object would be to use an entity that is resident in the USA for GATCA purposes (and therefore will not report under GATCA as long as the USA does not sign up to GATCA) but that is not resident in the USA for US tax and reporting purposes (and therefore will not report non-US persons under FATCA and will not be subject to US tax or reporting obligations). The ideal candidate with which to thread this needle? A trust with a US trustee that is structured as a non-US trust for US tax purposes.

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*Bingo! A US-resident entity account holder with a US account will not be reportable under GATCA or FATCA*

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Putting aside ‘branches’, a concept not relevant to trusts, a ‘Participating Jurisdiction Financial Institution’ under GATCA is a Financial Institution that is ‘resident in’ a Participating Jurisdiction.<sup>19</sup> A trust is resident under GATCA where one or more of its trustees are resident, irrespective of whether the trust itself is resident for tax purposes in a Participating Jurisdiction.<sup>20</sup> Thus, a trust with a US-resident trustee is not a ‘Participating Jurisdiction Financial Institution’ and, as such, is not subject to GATCA’s constraints.

Based on the above, a trust with, say, a US trust company as trustee, would be out of scope for GATCA. The same would be true of a trust with a US-resident individual as trustee.

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*A trust with, say, a US trust company as trustee, would be out of scope for GATCA. The same would be true of a trust with a US-resident individual as trustee*

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Making such a trust not a US person, and therefore not subject to US tax on anything other than US-source income, is relatively easy. To be a US person, a trust must meet both the so-called ‘court’ and ‘control’ tests.<sup>21</sup> The simplest of these tests to fail is the ‘control’ test: just give one non-US person control over one ‘substantial decision’ of a trust and—Hey Presto!—the trust is a non-US trust.<sup>22</sup> For example, the control test will be flunked if a non-US-resident person (eg a protector) is given the power to make any one or more of the following decisions (this list is not exhaustive):

- Whether a receipt is allocable to income or principal.
- Whether to terminate the trust.
- Whether to compromise, arbitrate, or abandon claims of the trust.
- Whether to sue on behalf of the trust or to defend suits against the trust.
- Whether to remove, add, or replace a trustee.

So, it is easy—really easy—to take a trust both out of scope of GATCA with respect to non-US persons, and out of scope of worldwide US taxation. Just use a trust with a US-resident trustee—that takes it out of GATCA—but give a non-US person one of the above powers (or one of the others listed in US Treasury Regulation section 301.7701-7)—that makes it a non-US person for US income tax and FATCA purposes. Of course, all assets should be booked in the USA otherwise the non-US bank or other Financial Institution will have its own GATCA reporting obligations.<sup>23</sup>

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19. GATCA, 158, para 3 (Commentary on s VIII concerning Defined Terms).

20. *ibid* 159, para 4.

21. US Internal Revenue Code, s 7701(a)(30)(E).

22. US Treasury Regulation s 301.7701-7.

23. But see the later discussion of what happens if the US finagles its way into being treated as a GATCA Participating Jurisdiction even though it does not actually participate in GATCA.

*So, it is easy—really easy—to take a trust both out of scope of GATCA with respect to non-US persons, and out of scope of worldwide US taxation*

As for the following potential US reporting obligations, none poses an issue for a trust structured as recommended above, provided (i) the trust is formed under non-US law, and (ii) none of the beneficiaries lives in the USA.

### **FinCen Form 114, Foreign Bank Account Report (FBAR)**

FBARs are required only for non-US financial accounts, so are relevant only if a trust has an account outside the USA. Unless the USA ends up being treated as a GATCA Participating Jurisdiction (as addressed later), all accounts should be in the USA. If they are, the trust will have no FBAR filing obligations.

But even if an account is outside the USA, the trust will not have an FBAR filing obligation provided the trust is formed under non-US law. Only 'U.S. Persons' are required to file FBARs. A trust is a US Person for this purpose only if it is 'formed under the laws of the United States'.<sup>24</sup> The US tax status of a trust and of its trustee are irrelevant.<sup>25</sup> Therefore, if a trust is to hold an account outside the USA (eg, because, as discussed later, the USA is treated as a GATCA Participating Jurisdiction), the trust should be formed under non-US law. The law of any offshore jurisdiction will do for this purpose.<sup>26</sup>

### **Department of Commerce Form BE-10**

The purpose of a BE-10 is to 'secure current economic data on the operations of U.S. parent companies and their foreign affiliates'.<sup>27</sup> At first blush, the form has nothing to do with private-client structures. However, its Instructions are drafted very broadly and, in limited circumstances, the form can impact certain trusts with US connections.

Until this year, no-one in the private-client industry had ever heard of the BE-10. That is because, until this year, only US persons and entities who were specifically requested to do so by the Department of Commerce had to complete the form. That changed this year: for the first time, the form had to be completed by 'U.S. persons' that, at any point in 2014, had at least a 10 per cent interest in a 'foreign business enterprise'.<sup>28</sup>

Trusts are 'persons' for BE-10 purposes.<sup>29</sup> A 'U.S. person' is any person 'resident in the United States or subject to the jurisdiction of the United States'.<sup>30</sup> The BE-10 instructions define when an individual is resident in and subject to the jurisdiction of the USA.<sup>31</sup> Unfortunately, they do not do the same for trusts. Query, then, whether a trust with a US trustee that is structured as a non-US trust for tax purposes is a US person for BE-10 purposes. And query further whether it makes a difference if the trust is governed by US or non-US law.

One thing is clear, though: trusts with only individual beneficiaries none of whom is a 'U.S. person' for BE-10 purposes have no BE-10 obligations. Subject to limited exceptions, an individual is a US person for BE-10 purposes only if he or she is living in the USA or is outside the USA for less than one year.<sup>32</sup> Thus, the individuals that are the focus of this article, ie,

24. FinCen Form 114 Instructions, 5–6.

25. *ibid* 6.

26. The potential FBAR filing requirements of trusts with non-US accounts are not to be confused with the separate FBAR filing requirements of US-person trust beneficiaries or settlors. This article addresses only non-US persons so will not delve further into the filing requirements of US persons.

By the same token, a trust's FBAR obligations are distinct from those of any underlying entity. Thus, if a trust owns a US entity such as a Delaware LLC, the FBAR obligations, if any, of that entity must be considered separately from those of the trust itself.

27. Form BE-10 Instructions, 1.

28. *ibid* 1, 'Who must report'.

29. *ibid* 7, para J, Estates, trusts, and intermediaries, subpara 2.

30. *ibid* 5, para S, definition of 'U.S. person'.

31. *ibid* 5, para D, Determining country of residence or jurisdiction of individuals.

32. *ibid*.

non-US persons for US tax purposes, are non-US persons for BE-10 purposes as well. Consequently, any trusts of which such persons are beneficiaries will have no BE-10 reporting obligations even if the trustee is resident in the USA.

### **Form 8938, Statement of Specified Foreign Financial Assets**

US individuals must file this form to disclose their offshore financial assets. The 8938 is broader than the FBAR, which is limited to foreign financial ‘accounts’. Although the US Treasury has proposed requiring certain ‘specified domestic entities’, including trusts, to file form 8938, those proposals have not yet been enacted.<sup>33</sup> In any event, only trusts that are US trusts for tax purposes would be captured by the proposal. As previously mentioned, the trusts recommended in this article should be structured as non-US trusts for tax purposes. If that is done, the trust will have no Form 8938 filing obligation.

### **Anti-avoidance rules**

Both FATCA and GATCA contain anti-avoidance language designed to prevent persons from doing just what this article describes, ie circumventing their reporting rules. For example, the reciprocal FATCA IGAs contain the following provision:<sup>34</sup>

- **Prevention of Avoidance.** The Parties shall implement as necessary requirements to prevent Financial Institutions from adopting practices intended to circumvent the reporting required under this Agreement.

The above provision is rather narrow, prohibiting only financial institutions, not taxpayers, from trying to circumvent reporting.

GATCA goes even further. Section IX of the CRS requires jurisdictions to have rules and procedures to prevent any ‘Financial Institutions, persons or

intermediaries’ from adopting practices intended to circumvent GATCA’s reporting and due diligence procedures.

The UK, for example, has implemented this requirement in section 23 of its International Tax Compliance Regulations 2015, which apply to both FATCA and GATCA. Under these regulations, if ‘a person enters into any arrangements’ and ‘the main purpose, or one of the main purposes’ is to avoid any obligations under the regulations, the regulations ‘are to have effect as if the arrangements had not been entered into’.

This language is exceptionally broad. It is not limited to arrangements with a tax evasion motive—any arrangements whatsoever that are designed to avoid reporting obligations are caught. It does not matter that the person in question may be fully tax compliant and the reasons for avoiding reporting are purely legitimate.

How would the above provision apply to a non-US person arranging his or her affairs to avoid FATCA reporting—for example, by transferring assets to the USA or blocking a US account for US securities? It would not. Keep in mind that the FATCA reporting the section addresses is in UK regulations. Those Regulations do not cover reporting by *US Financial Institutions about UK residents*—they govern reporting by UK Financial Institutions about US persons. Put simply, US Financial Institutions have no ‘obligations under these [U.K] regulations’ to avoid. Similarly, UK resident individuals have no FATCA reporting or other obligations full stop—those obligations fall solely on Financial Institutions. Therefore, the above UK anti-avoidance rule simply does not apply to a UK resident who structures his or her affairs to avoid reporting under FATCA.

But surely the USA has a comparable anti-avoidance provision that would be violated if a UK person arranged his or her affairs to avoid FATCA reporting back to the UK? Nope. There are a number of anti-avoidance provisions in the US

33. Form 8938 Instructions, 1 ‘Who Must File’, US Treasury Proposed Regulation 1.6038D-6, and IRS Notice 2012-8.

34. See, eg, art 5.4, Model 1A IGA Reciprocal, Preexisting TIEA or DTC 6 June 2014.

FATCA regulations.<sup>35</sup> However, none of these anti-avoidance provisions address avoidance of a *US Financial Institution's* reporting obligations. So much for the US commitment in its reciprocal IGAs to 'implement as necessary requirements to prevent Financial Institutions from adopting practices intended to circumvent the reporting required under this Agreement'! No such anti-avoidance measures have been implemented by the USA. And none are likely in the current environment. Therefore, unless and until the USA does enact such measures, tax-compliant non-US persons can safely arrange or re-arrange their affairs to avoid FATCA reporting without violating either US anti-avoidance rules or ones comparable to the UK's rule cited above.

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*So much for the US commitment in its reciprocal IGAs to 'implement as necessary requirements to prevent Financial Institutions from adopting practices intended to circumvent the reporting required under this Agreement'! No such anti-avoidance measures have been implemented by the USA. And none are likely in the current environment*

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What about avoiding reporting under GATCA? Would a tax-compliant UK person trigger the above provision if, say, he or she moved an account to the USA from a Participating Jurisdiction with legislation similar to the UK? It is not clear. Is moving an account an 'arrangement'? Questionable. But even if it is, what is the result of the regulations applying 'as if the arrangement had not been entered into'? Would the bank continue to report the account? That would be the effect of treating 'the arrangement' as if it had not been entered into. But how would any bank know that an account holder's purpose, or one of his or her purposes, in moving an account to the USA was to avoid GATCA reporting? Should all banks these days assume

an avoidance-of-GATCA-reporting purpose for accounts moving to the USA until proven otherwise?

These are all tricky questions. Truth is, the real-world application of a broad anti-avoidance provision like the UK's is indeed hard to gauge.

However, a more fundamental point is this: no matter how broad the scope of any anti-avoidance rule, no law applies before its effective date. These UK regulations are effective on 1 January 2016 with respect to GATCA (including the EU's own implementation of GATCA as reflected in the EU Council Directive on Administrative Cooperation (DAC), 2011/16/EU as amended by EU Council Directive 2014/107).<sup>36</sup> Any arrangements entered into before that date, even if the sole purpose is to avoid GATCA reporting, are simply not captured.

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It is likely that other GATCA Participating Jurisdictions that have not yet enacted anti-avoidance rules will, like the UK, tie their effective date to their general GATCA go-live date. Obviously, though, one has to consider each country's specific rules. Fully tax-compliant persons who want to arrange (or re-arrange) their affairs to avoid GATCA reporting should act soon. Indeed, if they want to sidestep thorny interpretive questions about the scope of particular anti-avoidance provisions, they need to do so before those provisions come into effect. For early-adopter countries, that will likely be 1 January 2016, as it is for the UK. For others, it likely will not be before 1 January 2017. But bear this in mind: it is not just the rules where the person is resident that may be relevant—the laws of countries where accounts are currently held or where existing structures are located or managed from must also be considered.

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35. For example, a Responsible Officer of a Participating FFI must certify to the best of his or her knowledge after conducting a reasonable inquiry that the FFI did not have any formal or informal practices or procedures in place from 6 August 2011 to assist account holders in the avoidance of FATCA. US Treasury Regulation, s 1.1471-4(c)(7).

36. International Tax Compliance Regulations 2015, s 1(4).

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*It is not just the rules where the person is resident that may be relevant—the laws of countries where accounts are currently held or where existing structures are located or managed from must also be considered*

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## Conclusion

Avoiding reporting under FATCA and GATCA by fully tax-compliant persons for perfectly legitimate reasons such as personal safety and privacy is neither immoral nor illegal, provided one does not violate any applicable anti-avoidance rules. In contrast, avoiding reporting in furtherance of tax evasion is both immoral and (in most countries) illegal and should never be countenanced.

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*Avoiding reporting under FATCA and GATCA by fully tax-compliant persons for perfectly legitimate reasons such as personal safety and privacy is neither immoral nor illegal, provided one does not violate any applicable anti-avoidance rules*

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*Avoiding reporting in furtherance of tax evasion is both immoral and (in most countries) illegal and should never be countenanced*

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Given GATCA's impending 1 January 2016 starting date in early-adopter countries, and the fact that some GATCA anti-avoidance legislation is effective on that date, non-US person law-abiding clients must act quickly if they wish to arrange their affairs so as to avoid GATCA reporting. As explained above, one way of doing so is to move accounts to the USA and put them in a trust with a US-resident trustee. To avoid US tax and reporting obligations, the trust should

give a non-US person control over at least one 'substantial decision' of the trust.

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*Given GATCA's impending 1 January 2016 starting date in early-adopter countries, and the fact that some GATCA anti-avoidance legislation is effective on that date, non-US person law-abiding clients must act quickly if they wish to arrange their affairs so as to avoid GATCA reporting*

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That "giant sucking sound" you hear? It is the sound of money rushing to the USA to avoid GATCA reporting.<sup>37</sup> Unfortunately, much of that money will be undeclared. Some, however, will be fully taxed and will move (if it has not already done so) for perfectly honourable reasons.

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*That "giant sucking sound" you hear? It is the sound of money rushing to the USA to avoid GATCA reporting*

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What if the USA is successful, as some have suggested it should be, in being treated as a Participating Jurisdiction even though it does not actually participate in GATCA? You will hear another giant sucking sound but in the reverse direction—money will flow out of the USA to other countries but will remain in IE FIs that are US resident for GATCA purposes—those entities will not report because the USA will not be participating in GATCA, and the non-US banks where the entities have accounts will not report because they will not have to treat the entities as passive NFEs. Best of both worlds for the USA. The US fund and trust industries will be particularly tickled. The US bank industry, not so much.

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This article addresses just some ways in which FATCA and GATCA reporting can be avoided with

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37. The phrase "giant sucking sound" was popularised by Ross Perot during a 1992 presidential candidates' debate. Mr. Perot used the phrase to describe the sound of US jobs he said would be rushing to Mexico under the North American Free Trade Agreement (NAFTA). See <[https://www.youtube.com/watch?v=Rkgx1C\\_S6ls](https://www.youtube.com/watch?v=Rkgx1C_S6ls)> accessed 3 Oct. 2015. In the present context, of course, the "giant sucking sound" is in the opposite direction, ie into the USA. Mr. Perot would no doubt approve.

respect to non-US persons. It is by no means exhaustive. There are other avenues available as well. Unfortunately, discussion of those must wait for another day.

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