RESPONSE TO PUBLIC DISCUSSION DRAFT: MANDATORY DISCLOSURE RULES FOR ADDRESSING CRS AVOIDANCE ARRANGEMENTS AND OFFSHORE STRUCTURES

Dear Achim,

Business at OECD’s (BIAC’s) response to the public discussion draft regarding Mandatory Disclosure Rules (MDRs) for Addressing CRS Avoidance Arrangements and Offshore Structures is enclosed. To summarize very briefly:

- We strongly support the Standard for Automatic Exchange of Financial Account Information in Tax Matters (Common Reporting Standard or CRS). The CRS’ administrable procedures and detailed guidance make it a key tool for addressing the important and valid public policy concerns regarding tax evasion and money laundering.

- We also strongly support efficient and targeted mechanisms for addressing CRS avoidance arrangements, where these are shown to be necessary. Such mechanisms will ensure a fair and transparent financial system, and will benefit compliant firms.

- However, while we recognize that the rules must be crafted to stop abusive behaviour by “bad actors”, a number of our members have expressed concerns that introducing MDRs with immediate effect while CRS itself is still being implemented will result in unnecessary burdens. We suggest that either the scope of the immediately effective rules is reduced substantially to cover only scenarios where there is evidence of abuse, or the effective date is postponed pending full implementation of CRS and a more detailed review of its effectiveness in practice. We believe that this approach will not put CRS at risk, but will increase certainty and thereby reduce compliance burdens on low-risk taxpayers and financial institutions (FIs).

- Rules targeted to actual abuses will also prevent tax administrations from being overwhelmed with information, only some of which will be useful; a significant volume of extraneous or irrelevant information would inhibit enforcement efforts by making it harder to find abusive behaviour.

- Operationalizing these rules will be critical for FIs with extensive commercial activities and thousands of employees who service a large client base. Consequently, FIs will need:
  - clear and easy-to-understand rules;
Our specific, high-level, recommendations are that:

- an actual knowledge standard be applied;
- a main purpose test be applied;
- penalty protection be provided for reporting FIs (not acting as product developers/promoters) when they make a good faith effort to develop and implement effective policies and procedures; and
- protection from legal actions initiated by clients whose transactions have been reported under the MDRs be provided for reporting FIs and other tax intermediaries acting in good faith.

Finally, we recognize that achieving the correct balance—so that the rules are both effective and targeted—can be challenging. To that end, we would be pleased to discuss our comments with you in greater detail.

Sincerely,

Will Morris  
Chair BIAC Tax Committee

Keith Lawson  
Chair BIAC Business Advisory Group on CRS

Enclosure

cc: John Peterson  
Philip Kerfs
Chapter 1 – Definition of CRS Avoidance Arrangement

Comments on the Commentary:

Para. 13 – The generic definition of a “CRS Avoidance Arrangement,” for the reasons below, is overly inclusive. A more targeted approach would benefit both tax administrations and financial institutions (FIs) seeking to comply with these important rules.

We believe, for example, that it is “reasonable to conclude” that any transfer from a reportable depository account to any retirement account that is an Excluded Account “has the effect of” circumventing CRS information reporting requirements. That, combined with the definition of Relevant Services as offering any assistance with respect to the implementation of a CRS Avoidance Arrangement, could mean that every Reporting FI is required to report all such transfers.

Because we do not believe that all such transfers should be reportable under these rules, we recommend that a dominant purpose or similar standard be required for an arrangement to be a CRS Avoidance Arrangement. In determining purpose, the steps taken to achieve an outcome and whether feasible alternatives existed to achieve the same commercial goal should be considered.

In addition, as described in more detail below, we believe that the definition of Relevant Services should be limited to situations in which it is reasonable for the service provider to conclude that the intent of the arrangement is to avoid reporting under the CRS (and see also below our comments on Para. 16 regarding this test). The term Relevant Services should not include commercial relationships such as cash management, payment services, financing, or execution-only brokerage.

Para. 14 – It is unclear when an exchange by the United States under FATCA constitutes “the same Financial Account” information as would have been reported and exchanged under the CRS. In almost no circumstance would a Reporting Financial Institution be in a position to know whether a transfer to an account in the United States would meet this standard. Does this mean that no transfer to the United States is a CRS Avoidance Arrangement, or that every transfer to the United States is a CRS Avoidance Arrangement? Would other types of arrangements be implicated? If so, how?

Para. 15 – We believe that this paragraph should make clear that factual statements from FIs about CRS, how it works, etc. (without more) should not be evidence of marketing (similar to the legal opinion example).

Para. 16 – The “reasonable to conclude” standard appears to assume that an FI has knowledge of all relevant facts. This standard thus could be read to require detailed training across large segments of a financial institution. We recommend that the standard be applied based upon actual knowledge.
Under this revised standard, the question would be whether it is reasonable to conclude, based upon what the FI knows, whether the arrangement is an attempt to specifically avoid reporting under the CRS. This standard of knowledge would align with the CRS’ Relationship Manager Inquiry.

Para. 17 – Clarification is needed regarding the “core functionality” of a financial account and the “features” that are designed to take a financial product outside the definition of financial account.

Para. 17 – Without additional guidance, all e-money transactions and/or all derivatives transactions might be reported. This would result in reporting tens of millions of accounts and millions of transactions per day – which would make it harder for governments to identify abusive transactions.

Para. 17 – Any reporting will exacerbate client relationship difficulties as CRS avoidance has pejorative implications. Providing FIs with express immunity from litigation for good faith reporting will be necessary to enable the rules to function.

Para. 18 – Would transfers from a bank account to a retirement account or other form of nonreportable account be covered? If so, this “over-reporting” would make it harder for governments to identify abusive transactions. Does the FI need to check each time it transfers money cross border if the account holder would be reportable in the jurisdiction to which the money is moving to? If the account holder was not reportable in the first place, would there be a need to check? If the account holder would be reportable in that other jurisdiction, would there be a need to check if the transfer is to an exempt account (low risk product, etc.)?

In addition, we are confused by the reference to a $250,000 limitation at the end of paragraph 18, because there is no such limitation for new accounts.

Para. 19 – Paragraph 19 seems to state that a simple transfer (presumably from a reportable account to a non-reportable account) in itself would not be a CRS Avoidance Arrangement because it is not “an arrangement between the bank and the customer to circumvent CRS legislation.” We would very much welcome such a limitation, but we do not see a basis for it in the draft rules.

Consistent with the statement in Paragraph 19, a similar statement should be provided for collective investment vehicles (CIVs) when a CIV investor instructs the CIV (or its service provider) to transfer funds from the CIV investment to a bank account which may be outside the scope of CRS reporting.

Para. 26 – It seems the movement from a trust to a company will always be an avoidance scheme regardless of the reason for doing so. In addition to our suggestions above in relation to paragraphs 13 and 16, there should be a specific carve-out for widely held funds that might merge or migrate to another entity form.
Para. 30 – The definition of the term “Arrangement” captures legal arrangements that are (a) Institutional Investors or (b) owned by one or more Institutional Investors. A paragraph like Para. (3) of the Definition of Offshore Structure should be added.

Chapter 2 – Definition of an Offshore Structure

Comments on the text of the draft hallmark:

In section 1.4(a), it is typical that brokers will invest in shares on behalf of their clients “in street name” and not disclose the nominator to the fund or company that issues the shares. Under the CRS, the brokers would be disclosing these custodial accounts if maintained for non-residents. It would be helpful to have an example that excludes such Reporting Financial Institution brokers from the scope of this definition where they maintain financial accounts for the beneficial owners.

In section 1.4(d), we would recommend the creation of a list of jurisdictions, or the use of an existing list (e.g., the FATF high-risk and non-cooperative jurisdictions list), that meet one or more of the three criteria maintained by the OECD and agreed by all participating countries. To leave the decision to each FI would very likely result in each FI taking separate counsel and using different lists of jurisdictions that they believe meet one of the three criteria.

In section 1.4(e), the definition of what is “adequate” in terms of information collected and maintained by trusts is subjective. Is a name and address adequate without more? Is it adequate to use a risk based approach and only collect and maintain information on beneficial owners of more than 20% of the trust? We recommend, like above, that the OECD maintain a list agreed to by all Partner Jurisdictions.

Section 1.4(c) should not include the use of a Legal Arrangement if it is incorporated, resident, managed, controlled, or established, in a jurisdiction that does require the trustees (or functional equivalents) to obtain and hold the relevant information regarding the Legal Arrangement, even if it organized under the laws of a jurisdiction that does not do so.

Comments on the Commentary:

Para. 37 – A definition of the term “substantive economic activity” should be added. We also note that the definition of “passive” is different than under the CRS, so Reporting Financial Institutions may have no way of knowing whether this new standard is met.

Para. 39 – The definition of “offshore” is very broad (and would cover a family trust when one beneficiary moves to another jurisdiction). A more targeted definition (e.g., one that identified specific factors, such as bearer shares) would reduce overreporting. In addition, the definition of offshore structure in paragraph 39 does not seem to be consistent with the definition in section 1.2, which says that “offshore” is an entity set up in a jurisdiction “other than” the jurisdiction of one or more of the beneficial owners. Said another way, if the entity is set up in a jurisdiction of any of the beneficial owners, it will not be offshore. Additional clarity is needed.
Para. 41 – Text should be added to clarify that “obscure” is not the opposite of “fiscally transparent” (as used, e.g., in Article 1(2) of the OECD Model Tax Convention), but rather of “the lack of transparency regarding ownership.”

Should the “undisclosed nominee” in the penultimate sentence of paragraph 41 actually be an “undisclosed nominator” structure to be consistent with section 1.4(a)? Alternatively, should the phrase be changed to “where the nominator is undisclosed?” Perhaps, in lieu of an “undisclosed nominator,” should the commentary use the phrase “undisclosed beneficiary”?

Para. 42 – A definition of the term “beneficial ownership” should be added, even if it is (a) an open definition or (b) a definition by reference to the FATF Guidance on Transparency and Beneficial Ownership (October 2014), as (i) that term is a common law (as opposed to civil law) term and (ii) a domestic definition of that term may not exist in some civil law jurisdictions.

Para. 43 – We have the same question here as in paragraph 41. Specifically, should the phrase be changed to “where the nominator is undisclosed?” Perhaps, in lieu of an “undisclosed nominator,” should the commentary use the phrase “undisclosed beneficiary”?

Para. 46 – We would recommend that the review of options to be limited to those options that are not publicly traded, or those options written involving at least one publicly traded group affiliate. To do otherwise would likely result in a significant volume of reporting, which would raise privacy considerations and make identification of abusive transactions more difficult.

Para. 47 – The use of credit cards should also be included. We also would recommend making clear that the prepaid debit cards are not those of a particular merchant or those tied to a Financial Account at a Reporting FI. It may also be helpful to tie this into the overpayments on credit cards rules to eliminate those other prepaid debit cards with less than a certain balance. Please note that the review of all prepaid debit cards may cut against the access to banking goals for developing countries. We also are confused by the reference to interest free loans, as those are not financial accounts in the first instance.

New paragraphs – We recommend that the Commentary discuss Sections 1.4(d) and (e). A few clarification points are included in our comments, above, on the text of the draft hallmark.

Para. 48 – The relevant update, revision, or date, of the FATF Recommendations referred to in the definitions of the terms “Basic information” and “Beneficial Owner” should be explicitly included (as, e.g., in Para. 132 of the Comm. on Section VIII of the CRS). Moreover, the Commentary that “the guidance that has been developed in the FATF context can be used to interpret those terms” should be explicitly included in the text proper (i.e., Para. 33).

Para. 49 – The definition of the term “Institutional Investor” should also include a Legal Person or Legal Arrangement (a) that is regulated as a mutual fund, exchange traded fund, private equity fund, hedge fund, venture capital fund, leveraged buy-out fund, real estate investment trust, master limited partnership, or any similar investment vehicle (see, in such regard, Para. 20 of the Comm. on
Section VIII of the CRS); (b) the shares or interests of which are widely held (i.e., not only publicly traded); and (c) that is wholly owned by one or more of the foregoing. We also would suggest that the CRS-defined term “entities regularly traded on an established exchange” be used in lieu of “publicly traded entities.”

Chapter 3 – Disclosure Requirements on Intermediaries

Comments on the text of the draft hallmark:

**Section 5.2** – We would recommend adding the word “knowingly” before “providing assistance...” in the definition of Relevant Services. Adding the word “knowingly” will tie the definition of Relevant Services back to the definition of a CRS Avoidance Arrangement, which should require a full understanding of the terms and consequences of such an arrangement in order to make it reasonable to conclude one exists.

**Section 5.3** – We are struggling to understand how the certified or notarized copy of the most recent tax filing of a Reportable Taxpayer would work in practice, and recommend that it be eliminated. For example, does each government where the taxpayer is resident provide those certificates to give to the Intermediary? Is the Intermediary intended to study each tax filing and make that determination, or is the certification or notarization meant to be done by a third-party tax advisor at the expense of the Reportable Taxpayer? Is the Intermediary expected to collect and maintain them on an annual basis? How would the Intermediary evaluate whether the documents represented all relevant filings? What would a taxpayer resident in a country that does not levy income tax be expected to produce?

**Section 5.4** – We believe it would make the Service Provider definition clearer and more consistent to use the phrase “reasonable to conclude” in lieu of “reasonably be expected to know” and refer back to paragraph 16.

Comments on the Commentary:

**Para. 55** – A definition of the term “person” should be added, even if it is (a) an open definition or (b) a definition by reference to, e.g., Article 1(a) of the OECD Model Tax Convention, as the lack of definition may be exploited to avoid falling within the definition of the terms “Promoter” and “Service Provider”.

**Para. 57 et seq. Para. 73** – Additional guidance and examples are needed regarding the types of “advise or assistance” that constitute “relevant services” in respect of a scheme. A broadly-applied standard could lead to substantial overreporting.

**Para. 57 et seq** – “Reasonable person/reasonably expected to know” standards are problematic for large financial institutions (same comment in Chapter 1). Main (or dominant) purpose should be required.
Similarly, an Intermediary be required to have reasonable grounds for suspicion or know that there is a deliberate attempt to avoid CRS obligations (because there may be substantial legitimate reasons for implementing such structures).

Para. 62 – We believe the subjective aspect of the requirement – *i.e.*, which jurisdictions lack the globally accepted AML/KYC rules that could lead to obscuration of natural persons – could result in inconsistent application. Consequently, we restate our recommendation above to make available a globally agreed list of these countries.

Para. 64 – Usually, foreign Intermediaries do not offer their services to domestic clients “through a branch”, but do so *in situ* through, *e.g.*, visits, meetings (*in, e.g.*, an “office hotel”), *(international tax)* conferences, emails, and social media (*e.g.*, LinkedIn).

Para. 70 – It may be useful to deem the (properly defined) Relevant Services to have been provided if consideration has been paid, credited, or received, with respect to such Relevant Services.

Para. 74 – Reporting should not be required when the end users are not reportable.

Para. 75 – Standard that intermediary holds a “certified or notarized copy of the most recent tax filing that shows that the Reportable Taxpayer is compliant with its tax obligations” is so high as to make the exception essentially useless. How is the intermediary to know that the taxpayer is compliant if the tax return is in a foreign language and/or so complicated that compliance cannot be determined? *(Same comment provided for section 5.3 of the text of the draft hallmark)*.

**Chapter 4 – Information Reporting**

Comments on the text of the draft hallmark:

**Section 3.1** – When relying on another Intermediary’s disclosure, they will need to collect and maintain some sort of proof. A copy of the filing would contain PII of the Reportable Taxpayers, so how would this work in practice?

Comments on the Commentary:

Para. 77 – How are the details to be reported? Free form narrative or a checklist of items/categories? In addition, we believe that the sentence that states that information is within a person’s control if it can be obtained by asking for it creates a duty to investigate every non-reportable Financial Account and even transactions (*e.g.*, options) that are not Financial Accounts. We suggest that it be clear that this standard only applies for purposes of determining what information must be reported, not what information a Financial Institution is deemed to know.

Para. 77 – More guidance is welcome regarding when information can be obtained by “asking” for it. Is there any limit on how many inquiries (to the same or different persons) must be made?

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Para. 78 – We appreciate that the model rule information requirements are intended to reduce compliance burden. Nevertheless, as described in this submission, the Commentary must be modified and clarified in numerous respects for the compliance burden to be proportionate.

Para. 79 – The obligation to report on persons with whom the FI does not have a business relationship/contractual privity is problematic as the parties do not have a data protection agreement. If Intermediaries are intended to use the definition of “control” from paragraph 77, then is a web search for similar Arrangements or a review of government databases (if made available) also required? If so, what are the key terms or other data elements that should be searched?

Para. 87 – Duplicative reporting also can be prevented by not requiring reporting of transactions (a) for which suspicious activity reports have been filed or (b) that have been otherwise disclosed or reported (e.g., through a tax return).

If a second Intermediary relies upon the disclosure of the first Intermediary in a Partner Jurisdiction, how do the tax authorities identify the Arrangement when the second Intermediary only reports the Reportable Taxpayers and nothing else because it would be duplicative?

Para. 88 – We would strongly recommend a central database of Partner Jurisdiction relationships for Intermediaries to draw from.

Para. 91 – Disclosure by a taxpayer should not be required where disclosure would be limited by any (i.e., not only domestic) protections against self-incrimination (e.g., under international law or the laws of another jurisdiction).

Para. 91 – Disclosure by an Intermediary should not be required to the extent it would infringe that Intermediary’s privilege against self-incrimination (e.g., under domestic law, international law, or the laws of another jurisdiction).

Para. 93 – The expression “with the intention of” should be substituted, at least, by “and it is reasonable to conclude that it will.”

Para. 95 – An expectation that each jurisdiction will have a publicly-available list of Partner Jurisdictions should be added.
Chapter 5 - Penalties

Comments on the Commentary:

In General – We would recommend using the CRS penalties for non-filing that are already in place. If there is not already an account holder penalty in particular jurisdiction, then the FI penalty could be extended to the Reportable Taxpayer.

Para. 96 – Penalties should reflect relative degree of culpability. Promoters, for example, should suffer greater penalties than a large FI subject to a “reason to know” standard. A similar distinction should be made, for example, between “fraudulent” behavior and transactions based upon “equivalent” financial products.

Para. 96 – Penalty relief should be provided when an FI establishes appropriate policies and procedures that generally are followed. This standard would prevent penalties for inadvertent reporting errors.

Para. 97 – Consistency in implementation (i.e., not more or less than the OECD standard), penalty amounts, interpretation (i.e., guidance), and application, across jurisdictions will ensure a level playing field.

Para. 97 – The Commentary should state that certain jurisdictions should implement penalties in primary legislation.

Para. 99 – The Commentary should recognize that, in any case, penalties should be determined by each jurisdiction considering its circumstances (e.g., its constitutional rights and guarantees).

Para. 102 – The Commentary should recognize that a tax administration should not publicize names where contrary to obligations of confidentiality.