



## Preparing for the OECD Common Reporting Standard

The CRS calls for a redesigning of IT and business architecture. Here's a roadmap for compliance.

### Executive Summary

The Common Reporting Standard (CRS), an initiative by the Organization for Economic Cooperation and Development (OECD), aims to set a standard for exchanging information about taxpayers between different jurisdictions. Financial institutions (FIs) will have to modify existing processes and practices to comply with the additional requirements of CRS. The changes entail increased complexity in customer onboarding and due diligence procedures, enhanced data management systems and increased reporting. Global FIs will also have to take into account the variations in the interpretation of regulations across different jurisdictions.

FIs in the UK will have to be cognizant of two particular aspects of CRS. Firstly, the bilateral/multilateral agreements signed by the UK with different jurisdictions. Accounts related to all of these jurisdictions would have to be identified and reported. Currently, over 98 jurisdictions have publicly committed to CRS with nearly 55 (including the UK) committing to the first automatic exchange of information by Q3 2017. Secondly, FIs will have to keep tabs on Her Majesty's Revenue and Customs (HMRC) interpretations of the standard itself.

The OECD standard for automatic exchange of information is much broader in scope than previous tax compliance reporting regimes. Existing

tactical approaches cannot be upgraded directly. It calls for a redesigning of information technology (IT) and business architecture that can adapt to new countries coming on board. This white paper presents the considerations and challenges in complying with the CRS requirements, and offers a roadmap for the necessary transition.

### Overview

#### Automatic Exchange of Information

The recent Panama papers leak has underlined the need for cooperation between tax administrations in the fight against tax evasion and to protect the integrity of tax systems. Exchange of information is a key aspect of such cooperation. OECD Automated Exchange of Information (AEOI) and the CRS are built on previous regulations for sharing tax data, such as FATCA (U.S. Foreign Accounts Tax Compliance Act) and the EU Saving Directive. The automatic exchange of information enables countries to receive taxpayer information systematically and periodically from other countries.

The first exchange of information (under CRS) is scheduled for Q3 2017 (see Figure 1) by 55 countries including the UK, its crown dependencies of the Isle of Man, Guernsey and Jersey, and the UK's overseas territories of Anguilla, Bermuda, the British Virgin Islands, the Cayman Islands, Gibraltar, Montserrat, and the Turks and Caicos.



## CRS timeline

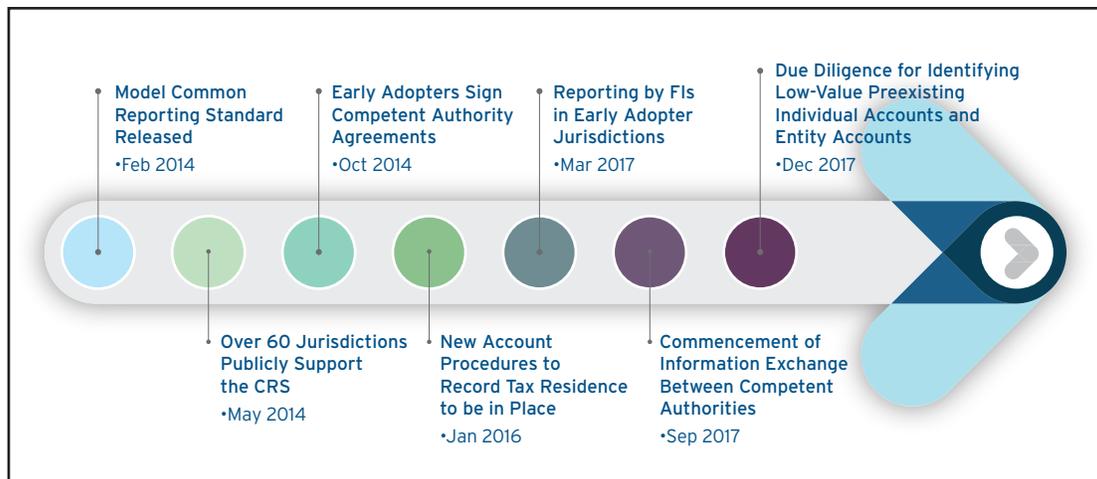


Figure 1

### CAA and CRS

The framework of AEOI is based on two components: CAA and CRS. The Competent Authority Agreement (CAA) is a model of an agreement between jurisdictions allowing for automatic exchange of financial account information. CAA provides the governance framework and each jurisdiction retains the right to revise the provisions of the agreement. CRS provides the standard for exchanging information and defines the reporting and due diligence standards for each jurisdiction.

OECD has modeled CAA and CRS on FATCA Model 1 Intergovernmental Agreement (Model 1 IGA). The principal changes include removal of U.S. specificities (to make it generic for multiple countries) and provisions concerning the withholding of taxes. It aims to provide national tax agencies with enhanced taxpayer information.

### CRS Requirements

#### Additional Due Diligence/Onboarding Requirements

CRS requires all in-scope account holders to be classified regardless of the balances in the accounts. This translates to changes in due diligence procedures to classify and identify the reportable individual and entity accounts. Self-certification of tax residency is to be used as a means for identifying indicia for all types of reportable accounts.

For individual accounts, tax residency will be determined by an enhanced review process that

includes: documentary evidence, indicia search and, in certain cases, paper record search and actual knowledge testing of the relationship manager. Any gaps in electronic searches would mandate the use of paper record search. All new individual accounts will go through the same due diligence procedure as preexisting individual accounts. There is no de-minimis threshold for individual accounts.

For entity accounts, individual jurisdictions can take a decision to exempt accounts below a de-minimis threshold. For new accounts, there is no de-minimis threshold, but the other requirements are similar to those for preexisting entity accounts.

### Reporting Requirements

Financial institutions will have to submit annual reports to the corresponding competent authority of the participating jurisdictions. Reportable information includes interest, dividends, account balance/value, income from certain insurance products, sales proceeds from financial assets and other income generated from assets held in the account or payments to the account.

The format/schema of CRS reporting in extensible mark-up language (XML) is presented in Figure 2 (next page). The CRS schema reuses the FATCA schema and elements of the OECD's Standard Transmission Format (STF). So there are some elements in the CRS schema that are not required for the purposes of reporting and exchange under CRS (e.g., pool report and nationality).

## CRS Reporting Schema

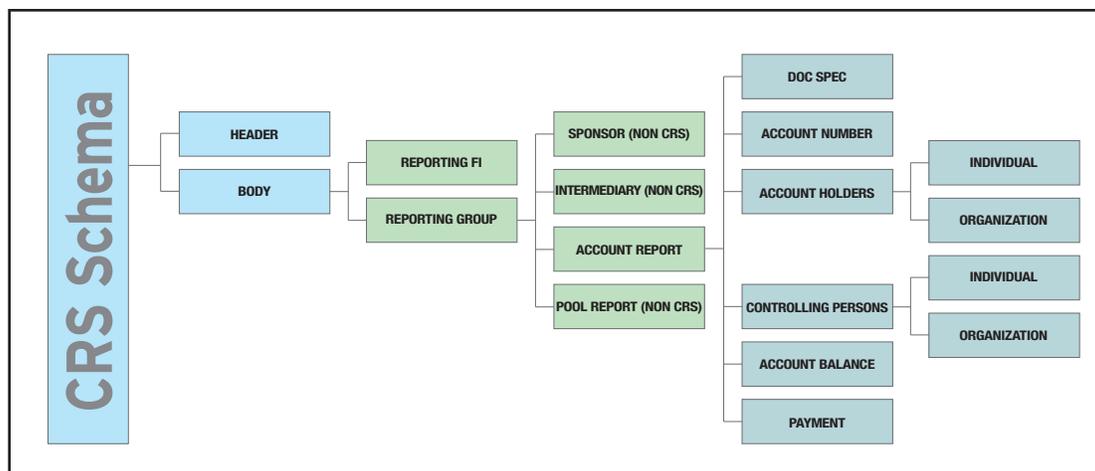


Figure 2

### FATCA and CRS

The scope of CRS is largely the same as that of U.S. Model 1 IGA across three key dimensions: financial information to be reported, financial institutions that are required to report and reportable accounts. The key differences have been highlighted in Figure 3.

In spite of the differences, the similarities allow partial leveraging of existing FATCA capabilities to support delivery. Figure 4 (next page) highlights areas of reusability of existing FATCA capabilities by financial firms.

### Comparison of CRS and FATCA

Key Differences	FATCA	CRS
<b>De Minimis Limits</b>	\$50,000 (all individual accounts) \$250,000 (preexisting entity accounts)	\$250,000 (preexisting entity accounts)
<b>Indicia</b>	Focused on U.S. citizenship and residency.	Focused on tax residency alone.
<b>Due Diligence</b>	Separate due diligence for preexisting and new accounts, and for individuals and entities. Significantly different processes between FFI agreement and model 1 IGA.	Due diligence modelled on IGA, but with a number of key differences.
<b>Definition of FI</b>	Most financial institutions, unless specifically exempted as being lower risk.	Similar to FATCA, but no exemption for local smaller entities excluded under FATCA.
<b>Account Scope</b>	Most banking products unless low risk; some insurance; most asset management.	Banking and asset mgmt. broadly similar, though regularly traded exemption removed for interest in investment entities. CRS has no back book exemption for insurance.
<b>No Sponsorship Model</b>	Under FATCA, an entity is permitted to sponsor multiple entities in the group, allowing a single entity to undertake and submit reports on behalf of the sponsored entities.	CRS does not have a sponsorship model.
<b>Reporting</b>	Primarily to U.S. (some U.S. reporting obligations to non-U.S.). Account balances from 2014, with income and sales phased in.	Many-to-many, via local authority. Account balances, income and sale proceeds from day one. Must include countries of residence.

Figure 3

## Reusing FATCA for CRS

Issue	Gap to Model 1 IGA
<b>Preexisting Individual Identification</b>	Additional indicia checks required but only for high value accounts, or accounts where no current residence address is held. Accounts which are sub-\$50k or otherwise FATCA exempt must also be considered.
<b>New Individual Identification</b>	<ol style="list-style-type: none"> <li>1. Current self-certification must be amended to cover all countries, rather than a "U.S. or not U.S." declaration.</li> <li>2. No de minimis.</li> <li>3. Systems need to allow for multiple statuses per customer.</li> </ol>
<b>Preexisting Entity Identification</b>	Minor changes to entity types - documentation standards and workflow largely preserved.
<b>New Entity Identification</b>	A number of changes needed, including a self-certification on residency for all new entity accounts.
<b>Reporting</b>	<p>Possible multiple statuses per customer.</p> <p>Additional customer details reportable.</p>
<b>Withholding</b>	Only applicable to non-IGA countries for FATCA. Is not applicable for CRS.
<b>Compliance</b>	As with Model 1 FATCA, compliance is under local law.

Legend	
Process change and new information requirements	Minor or no redesign effort

Figure 4

### Impact of CRS

CRS covers different kinds of financial institutions, including custodial institutions, depository institutions, investment entities and specified insurance companies, with some institutions eligible for exclusion as they pose a low risk of being used for tax evasion.

CRS is tougher on exemptions as compared with the FATCA regulations or IGAs. Some financial institutions that were exempted under FATCA have been brought under the ambit of CRS. These include certain retirement funds, sponsored investment vehicles, financial institutions with a local client base, local banks, some investment advisors and investment managers, certain investment trusts and financial institutions with only low-value accounts.

CRS will have the most impact on the following areas:

- **Data:** Various aspects of data must be managed to comply with CRS. These include aggregating data from disparate sources of information to determine customer classification, and creating a data repository to track customers' CRS status for reporting. Another challenge is normalizing of data from various

source systems to allow centralized storage of data to drive the reporting for CRS.

- **Systems:** FIs will be revisiting their existing AML/KYC systems to make sure that all CRS requirements are met. They will be required to classify client information across lines of business, types of accounts and countries. Reporting systems also need to be enhanced in order to send automated reports as well as generate ad-hoc reports for both internal and external reporting.
- **Operations:**
  - **KYC and due diligence:** The due diligence procedures mandated by CRS in most cases need to be considered in conjunction with local regulations. For example, the draft regulations published by HMRC enable financial institutions to apply the due diligence procedures required under the DAC for reporting for non-EU jurisdictions as well.
  - **Client documentation:** The responsibility of stakeholder management pertaining to various activities would lie with the FATCA/CRS operations team. Existing KYC/AML procedures need to be reviewed to identify gaps and new client onboarding/account-opening procedures will need to

be developed. The operations team needs to ensure that relevant CRS indicia data elements are captured for new accounts. It also needs to identify existing accounts and conduct a review of all such accounts to classify. Relationship managers and/or the CRM team must enhance their client communication strategy to obtain CRS-related information from clients.

➤ **Reporting:** Tax authorities are working on a single report model, based on FATCA, covering multiple reports required under different regulations. This will involve changes to the existing reporting processes.

## Impact of CRS

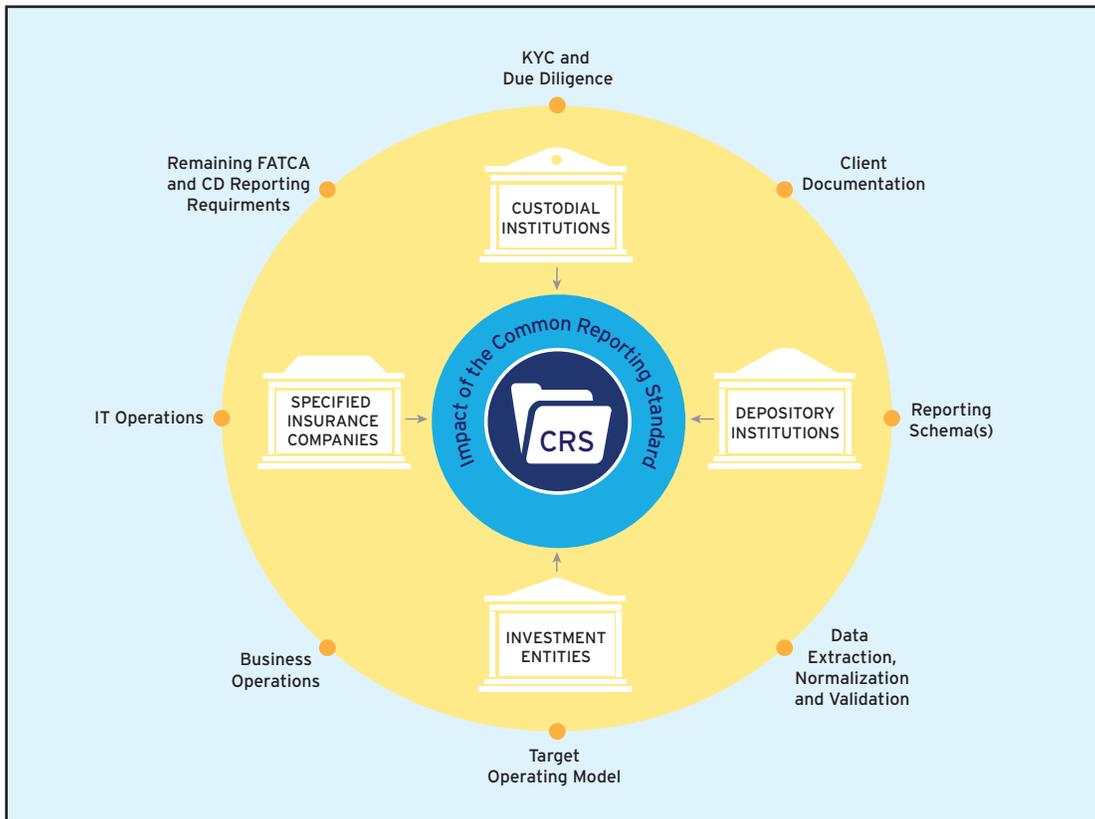


Figure 5

## Looking Forward: Challenges and Opportunities

### Differing Interpretations Across Different Jurisdictions

A CAA can be bilateral, multilateral or nonreciprocal in nature. This implies that each jurisdiction would require reporting of a different set of accounts. There may be differences in CAA between different jurisdictions as well as differences in local implementation. Also, CRS relies heavily on local AML and KYC requirements. As

these requirements vary across jurisdictions, international financial institutions may face difficulties standardizing their approach. The laws regarding tax residency are also complicated, and differ by country. The self-certification validation procedures may therefore not be straightforward. Definitions of financial institutions and exemptions to CRS may vary across jurisdictions. However, the due diligence procedures and broad-based customer classifications are expected to be the same across jurisdictions.

### **Data Privacy Laws**

Local law and data privacy considerations will require closer analysis at the country level.

### **Accommodating Other Regulations**

Areas impacted by CRS are impacted by other regulations as well. Difficulties in standardizing an approach to customer classification will arise out of differences between CRS, FATCA, the European Savings Directive (EUSD) and the Directive on Administrative Cooperation (DAC). With FATCA, agreeing upon and implementing IGAs is a time-consuming process. This suggests it may be unlikely that all jurisdictions intending to participate will be able to enter into and implement agreements in the same timeframe.

### **Larger Scale of Business Operations and Solution Delivery**

FATCA primarily dealt with accounts tied to U.S. citizens. The minimum threshold on CRS is also lower than FATCA for both new and preexist-

ing accounts. There is more information to be collected from account holders with multiple tax residencies, more information to be checked and more information to be reported. For example, when there are conflicting indicia and self-certification is not provided, the account has to be flagged for multiple tax residencies and the account info has to be reported to all concerned jurisdictions. There is a need to create scalable agnostic processes and systems that can meet the current and tentative future requirements.

### **Changes to Existing Systems and Processes**

Clean and consistent data from upstream systems will require changes to those systems and associated business processes (i.e., onboarding and due diligence). The aggregation of customer accounts across various business lines and systems will introduce additional complexity.

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