The Common Reporting Standard: Are you ready?

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Contents

Staying on track with Common Reporting Standard compliance

A survey by KPMG of executives at UK-based financial institutions in the second half of 2015 found 65% anticipated that CRS would affect more accounts than the FATCA regime, with a similar number thinking that their CRS compliance project would require more resources than their FATCA project did. We suspect this result reflects the fact that compliance work on CRS was only just beginning; 40% had not yet started their CRS programmes when the survey was carried out.

The Common Reporting Standard (CRS) is now live in the UK and approximately 60 other jurisdictions. From 1 January 2016, all financial institutions which are headquartered or have operations in these countries will need to have processes and procedures in place to meet their CRS obligations for new accounts; and they should be starting work on collecting the information they need to collect on their existing accounts.

The basic requirements behind CRS are similar to Foreign Account Compliance Act (FATCA) and UK Crown Dependencies & Overseas Territories (CDOT) – but the scale is much greater. CRS is truly global, extending to any customer who is a tax resident in a "reportable jurisdiction". Around 60 early adopter jurisdictions have signed up to start reporting in 2017 with another wave of 40 due to follow from 2018. CRS also covers many more entities, more customers and more accounts than either FATCA or CDOT.

Key CRS deadlines are fast approaching. Financial institutions need to get up to speed on making sure they are on track to be ready for the first reporting in 2017. In this report we set out the main areas that we believe financial institutions should be focusing on in the year ahead to get their CRS compliance into good shape, with our insight into bringing efficiencies into the process.

60 Approximate number of implementing jurisdictions starting in 2016

40 Additional number expected to join within next two years

Building on FATCA

The increased volumes of data to be collected and reported under CRS results in a vast logistical challenge in how to go about gathering, storing and retrieving the information required. But while the size and scope of CRS can be daunting, the fundamental approach is, in the UK at least, similar to that used in FATCA and CDOT. This is why financial institutions (FIs) should build on their experience to help develop their more complex and far-reaching CRS processes and procedures, including the training needed for relationship managers and for the back-office team responsible for the data management.

We have noticed a fair amount of "FATCA fatigue" and a definite trend by financial institutions to stand their FATCA teams down once reporting started. However we believe these teams – or at least their key members – can bring vital experience to bear in making the CRS compliance process as efficient and effective as possible. They are in the best position to combine the technical and management skills required with practical insight from recent similar projects and an understanding of how to minimise the impact on the business.

Entity classification

Financial institutions can follow a similar approach to the classification of entities in their groups for CRS as they did for FATCA. However, there are some marked differences:

- Many entities that only engage in investment management were exempt from FATCA reporting under the certified deemed-compliant status. There is no such exempt classification under CRS.
- Asset managers in non-participating CRS jurisdictions will be classified as passive non-financial entities (PNFEs). These entities will need to identify their controlling persons to see whether they are reportable.

Sponsoring is not available under CRS, so every fund and sub-fund will need to file reports on their own reportable customers, or outsource to a third party service provider, who could also be the FATCA sponsor.

Account classification

There are substantial differences between FATCA and CRS financial account definitions:

- There are no individual de minimis thresholds under CRS, meaning all financial accounts of individuals resident in every reportable jurisdiction will need to be reported.
- The threshold for not reviewing or reporting pre-existing entity accounts is the same at commencement, the difference is when the account needs to reviewed, as the value increases after the commencement date. For CRS purposes as soon as the US$250,000 threshold at a year end is exceeded, due diligence on the Account Holder is required.
- FATCA generally excluded listed shares or listed interests in certain investment vehicles, such as interests in Exchange Traded Funds (ETFs) and shares in Investment Trust Companies (ITCs). These mass-market products are however reportable under CRS.
- FATCA allowed most UK insurance companies to ignore their back books for all accounts held by individuals, while under CDOT only those above a US$250,000 currency equivalent threshold had to be considered. Under CRS, across the EU at least, all existing policies held by individuals come into scope.
- There is no de minimis threshold for the cash value of insurance policies under CRS: this was US$50,000 currency equivalent under FATCA and consequently this brings more products (and policies) into scope.

Onboarding processes

Financial institutions operating in early adopter countries should by now have processes and procedures in place for new account onboarding and should have changed account application forms to gather information on the tax residency of all new account holders.

A new account can only be opened once the customer has provided a valid self certification. This involves the financial institution obtaining the relevant data and carrying out a reasonableness check against other documents provided if data is already held for the customer: data sources include know-your-customer and anti-money laundering information, and the account application form. The self certification should be obtained before the account is opened, however validation may take place afterwards within 90 days in certain circumstances. The UK, under exceptional circumstances, will allow the self certification to be collected within 90 days after account opening.

FATCA experience suggests the main challenge for many has been the follow-up process: filling in the gaps on required customer information. We recommend setting targets for reducing the number and proportion of gaps in the required data fields. Any delay in following up with the customer in a timely and ordered manner will result in a snowballing backlog in undocumented accounts which could quickly draw unwelcome attention from HMRC.

HM Treasury has confirmed that UK financial institutions can adopt the wider approach – asking all their customers (not only those who they think might be resident in a reportable jurisdiction) where they are tax resident and for their tax identification number. While this means much more work and a greater IT investment for financial institutions now it will save having to go back and ask all customers for additional information as more jurisdictions become reportable.

Asset managers often rely on third-party administrators or other service providers to do the new client onboarding. There has to be complete clarity over who is responsible for which procedures and controls of CRS requirements.

The ultimate responsibility always lies with the FI and never with the third party. So whilst there could be a Service Level Agreement stipulating performance criteria – the legal responsibility never moves. If this is outsourced to third parties then the financial institutions must consider how best to ensure and evidence their compliance.

Most of the onboarding work to date has been on current products. But future new products will need to be checked for CRS compliance too. This is particularly relevant to asset managers, some of which launch new funds frequently, as well as insurance companies as they launch innovative insurance products on the market. Procedures therefore need to be future-proofed to include an update of CRS regulations and an automatic trigger to review all new scheme documents and public prospectuses to ensure they reflect the latest CRS position.

Typical CRS due diligence deadlines in early adopter countries

By 31 December 2016:	Pre-existing individual accounts over US$1m currency equivalent
By 31 December 2017:	Pre-existing individual accounts less than US$1m currency equivalent Pre-existing entity accounts over US$250,000 currency equivalent

Financial institutions in early adopter jurisdictions have to determine which of their account holders/ investors/ clients at 31 December 2015 were reportable for CRS purposes. Due diligence will need to be carried out on all individual accounts either this year or next (unlike FATCA and CDOT, there are no thresholds for individuals for which no due diligence is needed).

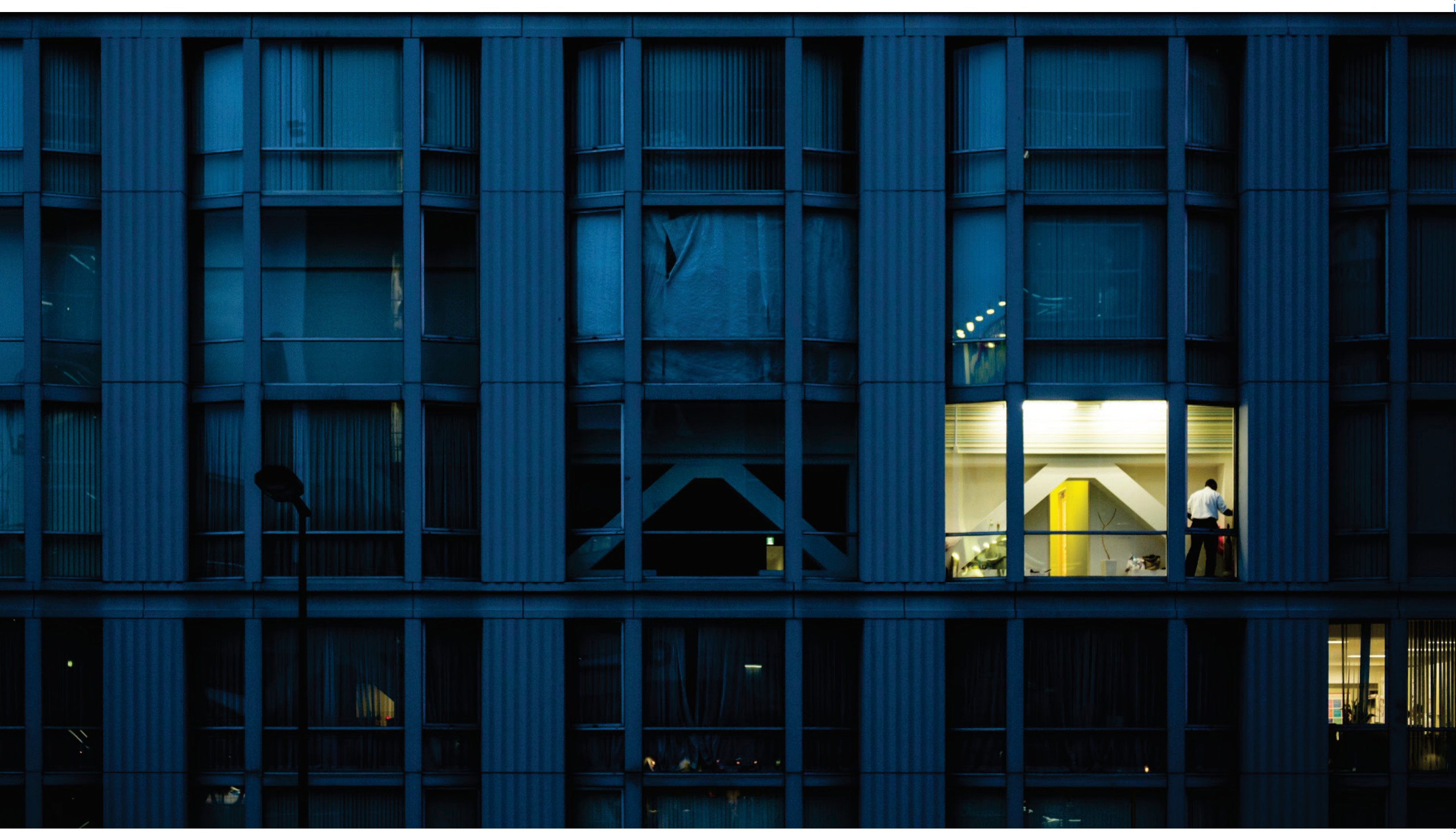
Where jurisdictions allow it, there is a threshold that can be applied for entity accounts, which is US$250,000 currency equivalent. Some financial institutions are finding it operationally easier to ignore this threshold and review all account holders, while other financial institutions are moving from ignoring the threshold to applying it due to low customer response rates.

But regardless of whether the entity threshold is ignored, financial institutions need to devote a huge amount of effort and resources for the due diligence required. This is against a background of constant regulatory change in which they have already had to go to their customers to ask for similar information. The question is how to tread the fine line between getting new information from customers in the least painful and most efficient way while making sure all the data needed is collected.

Financial institutions in early adopter countries should consider whether they can align their FATCA/ CDOT due diligence (which needs to be completed by 30 June 2016) with their CRS requirements as far as possible. This is a challenge for larger financial institutions with millions of small customers. However, smaller financial institutions or those with entity accounts only could potentially contact customers with all FATCA, CDOT and CRS questions by 30 June 2016. Not only does this minimise resources needed by not having to duplicate the process 6 or 18 months down the line – it puts less strain on the customer relationship by reducing repeat information requests.

HMRC reporting deadlines

31 May 2016:	CDOT 1st reporting deadline FATCA 2nd reporting deadline
31 May 2017:	CRS 1st reporting Ongoing reporting for FATCA and CDOT
31 May 2018:	CRS and FATCA ongoing reporting (incorporates CDOT)



UK based financial institutions will have to file CRS reports on financial account balances and payments (such as interest, dividends, distributions from funds as well as proceeds from the sale of investments) for residents of reportable jurisdictions to HMRC by an annual deadline. The first deadline will be 31 May 2017, which is also when financial institutions will need to fulfil their ongoing FATCA and CDOT reporting obligations. HMRC's reporting mechanism means all accounts can be reported in one submission. HMRC are unusual in that respect at the moment as it seems many countries will have to do a separate FATCA and a CRS return.

At the start of 2016, there is still some ambiguity over which jurisdictions are reportable for CRS. There is a long list of implementing jurisdictions – countries which have indicated that they want to participate in CRS – but no clear guidance as to which of these have made the transition to being reportable. This is particularly worrying for large multinational financial institutions who are looking now to automate reporting across the jurisdictions in which they operate, but are faced with several different reporting models and incomplete and changing information regarding which jurisdictions' persons are reportable by which entities.

As the first queries relating to FATCA filings start to trickle in, financial institutions should build on their experience of answering these questions to determine how best to respond to the flow that will follow CRS reports. Reviewing remediation processes and procedures might seem a waste of strained resources at this stage. But we think this is essential, bearing in mind that the volume of queries will rise substantially once CRS information exchange starts, as more jurisdictions become reportable – and as more tax authorities gain experience in analyzing the data that is coming their way.

Compliance and governance

Having the right processes and procedures in place is not the only challenge: there must be good controls to ensure the financial institution is doing what it should to meet its CRS obligations. Financial institutions can again make the most of their recent experience, adapting the governance and compliance framework they introduced for FATCA to arrive at a solution that works best for them for CRS.

Risk and compliance have not been as integrated as we think they should be in the FATCA, CDOT and now CRS processes at financial institutions. We believe risk management needs to be a primary part of the CRS project, linking with different areas of the business (such as tax, operations, reporting, IT and legal) to paint a comprehensive picture of the risks involved, the controls needed to mitigate these, the tests required, and any escalation process in case issues are identified.

Financial institutions need to keep track of how they can incorporate their ongoing CRS processes into their everyday business so that it becomes standard procedure.

Points to consider in making the transition from initial project to business-as-usual include:
— Establish who is responsible for post-CRS-implementation compliance.
— Keep track of developments to the CRS project and new reportable jurisdictions.
— Review and update internal processes and procedures, including staff communication, to reflect changes and review flags.
— Review reporting requirements well in advance of key deadlines to ensure systems and flags are up-to-date.
— Run regular exception reports, follow-up gaps in the information requested promptly, and chase the follow-ups.
— Review processes over data maintenance and data storage.
— Maintain an audit trail of information requests, data gathered and data validation.
— Perform internal audits and health checks of the processes; consider commissioning external independent checks as well.
— Establish a remediation process to deal with client queries once reports have been made to HMRC.
— Provide annual refresher training to client-facing and back-office staff.

CRS checklist

Forming a thorough and complete approach to CRS is a major undertaking and not something to be underestimated. However it's not impossible. With proper planning and a commitment to dedicating the resources required it can be done efficiently and effectively.

Our experience suggests the following areas are the most important in getting CRS compliance up to speed – and to stay that way.

Have you got them covered?
— Establish the reporting classification for each of your organisation's entities.
— Ensure new client onboarding procedures are working properly; assess feedback and adapt the processes as required.
— Plan the due diligence approach well in advance, especially when volumes are high. Consider whether any CRS due diligence can be combined with that for FATCA/ CDOT.
— As each important timeline comes up, review what has been done and set out deadlines for the coming six to nine months.
— Undertake programme reviews at each deadline to ensure all necessary steps have been taken, complete any still outstanding, assess experience and incorporate changes needed into the next step of the compliance process.
— Communicate with existing customers about the reasons for the data collection in the due diligence.
— Establish a strong and flexible system to request, collate and update customer data.
— Stress-test systems regularly to ensure they can cope with changing requirements and volumes.
— Update or change FATCA and CDOT reporting solutions to take account of the more extensive CRS requirements.
— Put internal audit processes in place to ensure operating procedures are being followed and that there is a good audit trail.

How can KPMG help?

KPMG have significant experience in providing a broad set of AEOI services to clients, these include:

- Entity classification.
- Health checks, operational reviews and gap analysis.
- Helpdesk support and ad-hoc technical advice.
- Supporting the interaction with other regimes such as the US Qualified Intermediary regime.
- A full suite of technology tools to support the end to end requirements of the AEOI regimes.
- Live workshops and web based or in-person training.

Meeting the challenges of reporting

Financial institutions face increasingly complex and changing reporting requirements. They need solutions for CRS reporting which take into account factors such as differing size, internal project and technology capabilities, and geographical impact. With these different parameters in mind we have developed an integrated global reporting tool which can be tailored to financial institutions' specific individual requirements.

KPMG AEOI Reporting is a technology-led solution which enables financial institutions to meet their FATCA, CDOT and CRS reporting obligations as simply as possible. This solution converts systems data into the relevant correct reporting schema smoothly and efficiently, interfacing with other systems, and can be interfaced to convert data to the required format.

This can be provided to clients via a licence or KPMG can offer a managed service where we securely take your data and manage the entire filing process for you.

This solution brings together the appropriate KPMG teams so that skill-sets including tax, risk management, technology, and management consulting are properly deployed. It is both scalable and flexible, so can be adapted for changes in financial institutions' operations as well as additions to participating jurisdictions and changes to the CRS regime.

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