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Worth

Why the U.S. May Become the Trust Jurisdiction of Choice for Non-Residents

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Changes to the international tax and estate planning community are coming—here's what you need to know.

Two recent international developments have raised concerns among professionals in the international tax and estate planning communities about the continued viability of utilizing the traditional off-shore so-called "tax havens" or structured product jurisdictions such as the British Virgin Islands, the Cayman Islands, Ireland, the Isle of Man, Jersey, Liechtenstein, Luxembourg, the Netherlands and Panama for trusts and family or private interest foundations. These concerns have caused international practitioners and their clients to consider moving trust assets to the United States and using trusts formed in the United States and governed by protective state laws (like those of Nevada and Delaware) with U.S. resident trustees. The recent Panama Papers disclosures have created great concern in the ultra-wealthy foreign community that its long-treasured confidentiality will be compromised. Furthermore, many countries, including all of the tax havens listed above, have adopted or are on the verge of adopting an international system that will provide for the automatic sharing of the identity and residence of the financial account holders, account details, reporting entity, account balance/value and income, sale and redemption proceeds between participating countries.

The exchange of information will begin for many jurisdictions by September 30, 2017, but the information required is from 2016. That means the countries in the earliest implementation phase should already have started to gather the required information. This global cooperation and sharing of information system is known as the Common Reporting Standard, or CRS, and it creates an information standard for the automatic information exchange between countries that are participating members in the program. The CRS significantly improves transparency in multinational business and investment reporting among the participating jurisdictions' respective tax authorities. The legal basis for exchange of data derives from the Multilateral Competent Authority Agreement on Automatic Exchange of Financial Account Information, the Convention on Mutual Administrative Assistance in Tax Matters and the participating jurisdictions' enabling legislations. The concept emulates the United States' Foreign Account Tax Compliance Act (known as FATCA). FATCA and CRS both require that financial institutions that are resident in a participating country implement due diligence procedures, document and identify reportable accounts and establish a very extensive reporting process.

Under FATCA and the CRS, the burden of reporting is placed on financial institutions, which include depository institutions, custodial institutions and investment entities. Custodial institutions include most corporate trustees that act as paid professional fiduciaries over assets held in trust for others. In addition, the trusts themselves could be reporting financial institutions depending on the circumstances. More than 100 countries have committed to implementing the CRS. Starting in 2017, 55 countries will begin reporting; these countries are known as the Early Adopter Group. Then in 2018, 46 additional countries will start reporting. In April, shortly after the release of the Panama Papers, Panama also agreed to become a cooperating member and will undertake its first exchange by 2018. For example, starting in 2018 if a Colombian resident is a beneficiary of a New Zealand trust or Panamanian foundation, the trustee or foundation council will be required to provide information required by the CRS of the trust or foundation to the New Zealand Department of Inland Revenue which in turn will exchange it with the Colombian taxing authority known as the National Taxes and Customs Direction.

Each participating jurisdiction will be required to enact domestic legislation or rules to provide for the implementation of the CRS. The U.S. has, so far, not joined the CRS initiative because of, among other reasons, the extensive network of intergovernmental agreements it has already implemented under FATCA. Any attempt to better align FATCA with CRS would require Congressional approval and our elected officials are in no hurry to enact changes because of the strength of the U.S. banking lobbying and the desire to give U.S. financial institutions a public relations advantage over their foreign counterparts. Furthermore, Treasury and the IRS believe they do not have the regulatory authority to require U.S. financial institutions to collect all the information required under both FATCA and the CRS in the absence of Congressional approval. One of the big differences in the two disclosure regimes is that under FATCA, if a financial institution fails to comply, the U.S. imposes a punitive withholding tax against the institution. Although domestic laws of other countries may someday impose penalties for non-compliance, CRS does not impose a withholding tax regime for non-compliance. The point is that the U.S. can demand financial information from foreign financial institutions about its citizens, but the countries participating in the CRS cannot impose reciprocal treatment on U.S. financial institutions with respect to their residents.

Because the U.S. has thus far refused to participate in the CRS, trustees of trusts that have direct or indirect beneficiaries who are residents of CRS participating jurisdictions should consider moving their trusts and their trusts' assets to the U.S. if they wish to avoid disclosure of the identity of the beneficiaries and the trusts' business and investment activities in the countries where the beneficiaries are resident.

NewstarWealth is actively assisting its global clients with trust formation in the United States. Please contact us for additional information on our FATA Trust™ structure which is designed specifically for foreign (non-US) clients interested in forming a U.S. protected trust. NewstarWealth is a leader in Generational Wealth Planning and focuses on providing custom-tailored financial planning advice to global individuals and their family corporations.

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