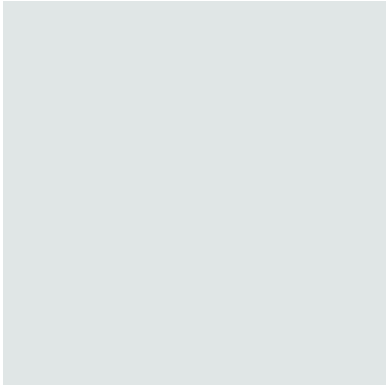


BENEFICIAL OWNERSHIP

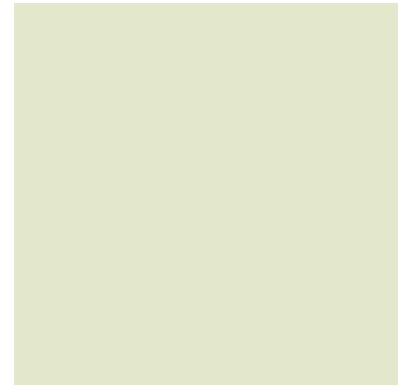
Trusts, Treaties & FATCA

Michael J. Legamaro





What is a Beneficial Owner?



Depends Upon Who You Ask

- Black's Law Dictionary
 - “One recognized in equity as the owner of something because use and title belong to that person, even though legal title may belong to someone else”
- Wolfsberg Group (AML)
 - Term “understood as equating to ultimate control over funds in an account”

What is an “Owner”?

- Black’s Law Dictionary
 - One who has the right to possess, use and convey”
 - A collection of rights allowing to use and enjoy property including the right to convey it.
 - Implies “right to possess” a thing regardless of “actual or constructive control”

“Beneficial” as Adjective

- When added to word “owner”, used to distinguish “a right or power one possesses for his own use and enjoyment from one possessed for use and enjoyment of another”
- For example, trustee holds legal title to property, but holds for it for beneficiary who has “beneficial interest” in or “beneficial enjoyment” of property

Derivative of English “Equity”

- Common law principle that ownership was indivisible
- Equity acknowledges principle that it is possible to have legal title with one person and “beneficial ownership” with another
- Ownership as “legal right” and “equity” as to enjoyment



Context Leads to Varying Conclusions



Financial Action Task Force

- Beneficial owner refers to natural person(s) who “ultimately” “owns” or “controls” a customer and/or the person on whose behalf a transaction is conducted
- Includes persons who exercise “effective control” over a legal person or arrangement

Context Leads to Definition

- Natural person
 - person “entitled” benefit who has “control”
- Company
 - operating businesses generally viewed as beneficial owner itself
 - Investment company look-through to underlying beneficial owners

Context (cont'd)

- Trusts
 - Beneficial interest – entitlement (equity)
 - Control may or may not matter (ownership)
 - US Tax purposes – trust assets held in “grantor trust” for benefit of persons other than the grantor
 - Entitlement to beneficiaries
 - “Ownership” to trust contributor lacking “control”
- Option-holders – enjoy, ability to own, but no current ownership

Owners of Trusts for AML

- Any individual entitled to “specified interest” (i.e., vested) in at least 25% of capital of trust property *or*
- Class of persons in “whose main interest the trust is set up or operates” *or*
- Any individual who has “control” over the trust

UK Registry of Beneficial Ownership

- Trustee(s) or “any individuals who control the activities of the trust”
 - Could be settlor, beneficiary, or protector
- Nowhere is “entitlement” to use or enjoy required

US Supreme Court View

- A right to enjoy property where “legal title is in one person and the right to such beneficial use or interest is in another” *and*
- Such right is recognized by law and can be enforced by the courts.

Catholic Missions v. Missoula County, 200 U.S. 118 (1905)

As Applied To Trusts

- Dual requirements for Beneficial Ownership
 - Right recognized by Law and
 - Enforceable by Courts
- Standard not met for discretionary trust beneficiaries
 - Nonvested, contingent, subject to discretion
- Only class of “beneficiaries” as whole enjoy or own within this definition

Context: As Applied to Tax

- Who is taxable as “owner”?
 - The trust or trustee?
 - Recognized “legal owner”
 - The beneficiaries?
 - Conduit owner
 - Settlor?
 - Deemed owner

US Tax Focus Thus Varies

- In US, a non-grantor trust is recognized as a separate taxpayer – a “beneficial owner” of income earned and not distributed
- Discretionary trust beneficiaries become “owners” of income only as and when distributed

Varied Tax Focus (cont'd)

- Deemed ownership arises in select cases, referred to as “grantor trust”
 - Settlor with retained control over beneficial enjoyment
 - Imputed retained control to settlor via use of a “related or subordinate party”
 - Beneficiary with unrestricted right to withdraw assets or income

Canadian View

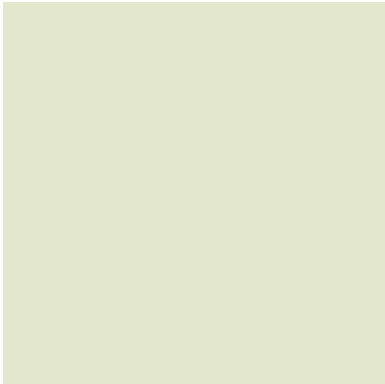
- Someone who receives income for his own use/enjoyment and who assumes risk and control of income =
 - Taxable owner of that income

Treaty Application

- Usually referred to in dividend, interest and sometimes royalties articles
- Reduced level of withholding tax on relevant category of income if “beneficial owner” thereof is resident of state party to treaty
- Designed to reduce treaty-shopping



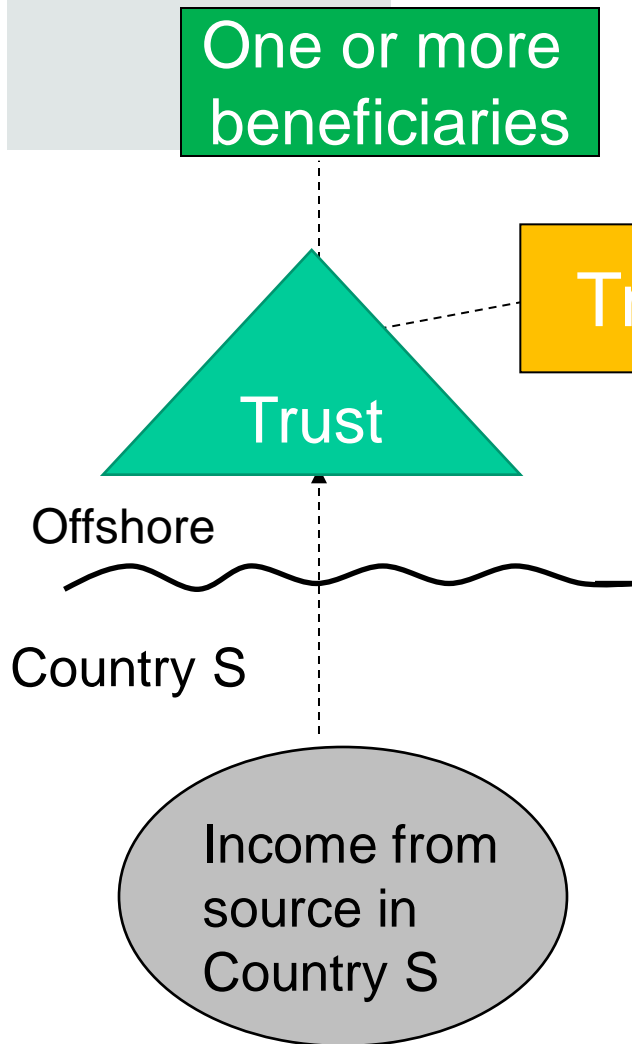
Counterbalance

- Definition of “person” includes a trust
 - Treaty benefits extended to “resident” persons
- 

OECD View

- Trustee of discretionary trust who does not distribute dividends earned could constitute beneficial owner for purposes of Dividend Article notwithstanding that relevant trust law may distinguish between legal and beneficial ownership

Trusts



- Variables :
 - Fixed trust vs. discretionary trust
 - Trustee and all beneficiaries resident in same country vs. multiple countries
 - Residence country tax treatment of trust income: taxation of trustee vs. beneficiaries

Differing Outcomes

- Residence of all in treaty jurisdiction generally results in treaty benefit
- Discretionary Trust “holding” dividends for future distribution becomes “owner” entitled to benefit
- Derivative clauses of treaties may permit “look-through” to beneficiaries for distributed income

Tax, Trusts & Treaties

- Searching for a reasoned approach
- Beneficial entitlement generally translates to treaty privileges
- Limitations on benefits clauses often better suited to anti-abuse than notion of “beneficial ownership” for trusts/partnerships and other conduits



FATCA

Information Sharing for Tax Purposes



FATCA

- Designed to share information regarding ownership of accounts across borders for tax purposes, permitting “home country” to evaluate income and thus tax liability
- Currently US and UK international reporting regimes – “US Reportable Accounts” around globe & “CD/OS Reportable Accounts”

FATCA Applied

- Enacting legislation in US and UK with regulatory guidance, but . . .
- Each jurisdiction signing IGA is permitted to apply its own laws (provided not inconsistent with basic IGA) in determination of which accounts meet which definition

FFI Trusts and FATCA (US/UK)

- A non-domestic trust (or more specifically, a “foreign” trust) may be either
 - a “foreign financial entity” (“FFI”) or
 - an non-financial foreign entity (“NFFE”)
- Accounts held by FFIs trusts are non-reportable
- Accounts held by NFFE trusts are reportable where Controlling Person is “specified”

Trusts as FFIs/NFFEs

- Trusts are “foreign financial entities” (“FFIs”) when
 - Managed by professional trust company and
 - Hold predominantly financial assets
- Trusts are non-financial foreign entities when not FFIs
- Most professionally managed trusts = FFIs

FATCA Reporting for US

- Does any specified US person have an “equity interest” in the trust?
 - FFI Trusts – If any such person holds more than 0% of the “beneficial interests”, then yes
 - NFFE Trusts – Only if specified US persons hold at least 10% of beneficial interests

Equity Interest = Beneficial Interest

- US regulatory Approach to Trusts
 - Grantors of Grantor Trusts
 - Beneficiaries entitled mandatory distributions
 - Discretionary beneficiaries when distributed
- Non-grantor Trust requires current “beneficial entitlement” or “ownership”

“Interest Held By”

- Connotes concept of “interest” or “ownership”, beneficial entitlement
- Ownership “held by” : A Specified U.S. Person =
 - being a beneficiary of a foreign trust if such Person has the right to receive directly or indirectly a mandatory distribution or may receive, directly or indirectly, a *discretionary distribution* from the trust

Discretionary Beneficial Interest or Ownership

- Reportable *only if* beneficiary receives distributions from trust and distributions exceed 10% of total distributions or trust assets
- Thus actual distribution required
- Vested beneficiaries without distributions are not reported
- Contingent, remainder ignored

Sensible Approach for Trusts with US Connections

- Reporting and transparency are about information for “tax purposes”
- Taxability requires distribution to beneficiary in case of non-grantor trust
- Grantors of grantor trusts are taxable currently as trust assets are deemed owned directly by grantor

Equity Interest = Beneficial Interest = Expansion

- Model 1 IGA tracks concept of “ownership” but adds “control”
 - In the case of a trust that is a Financial Institution, an Equity Interest “means ***an interest held by***” a person treated as
 - settlor
 - beneficiary
 - **or any other natural person exercising ultimate effective control over the trust.**

“Interest Held by” Controlling Person

- Natural person exercising “ultimate effective control” - undefined
 - Controlling Person for NFFE Defined
 - Natural persons who exercise control
 - “Means” settlor, trustees, protector, beneficiaries or class of beneficiaries, and any other natural person exercising ultimate effective control
 - Expansive Interpretations

Actual IGAs Expand Further

- In the case of an FFI trust, equity interest “***is considered held***” by
 - settlor
 - beneficiary of all or a portion of the trust, or
 - any other natural person exercising ultimate effective control over the trust.
- No longer focus on whether “interest” is held – in fact – but upon “deemed” holding

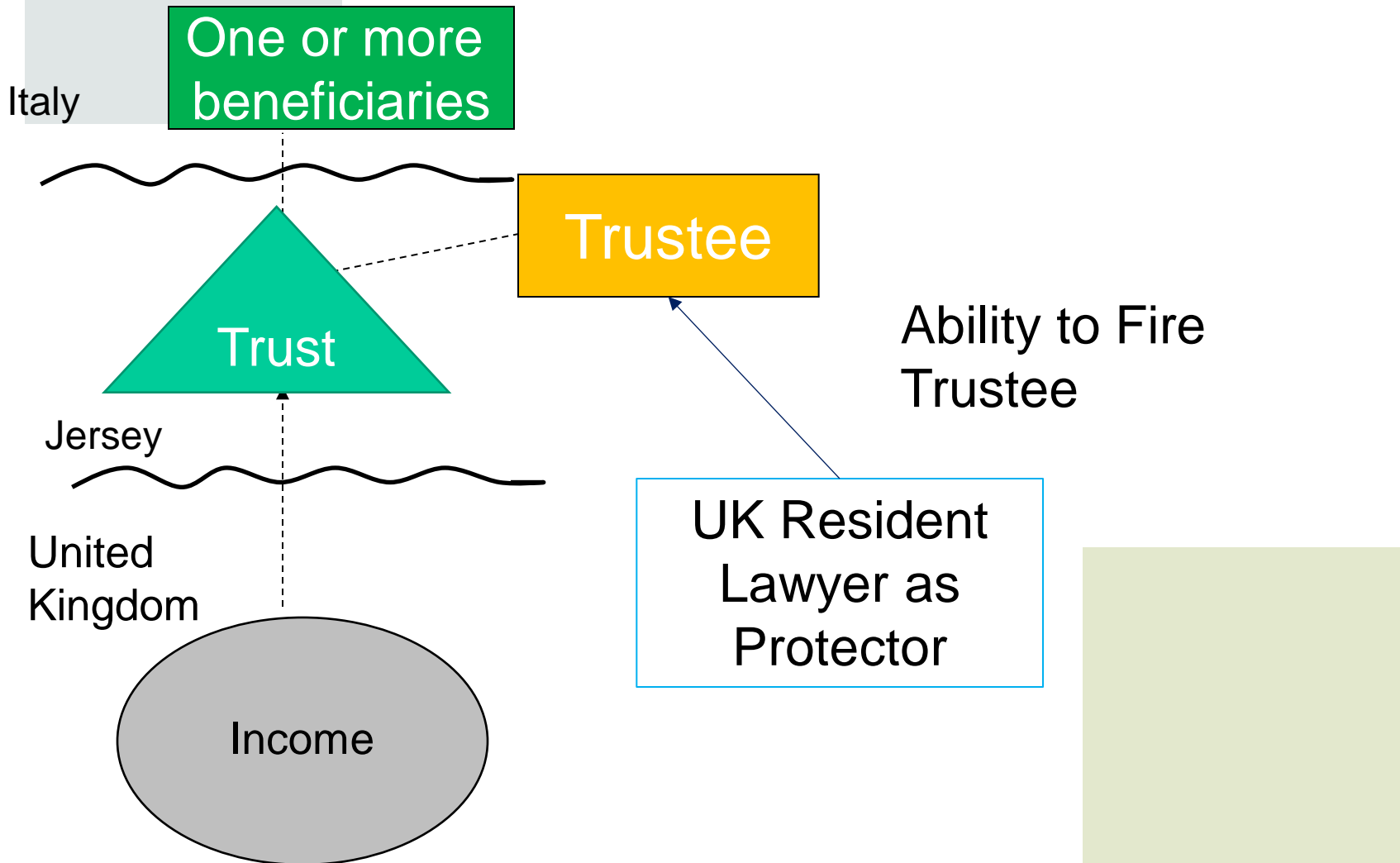
Compare US

- Settlers – No
- Beneficiaries – Only if entitled to distribution in fact
- Control irrelevant
- Settlers not taxed unless “grantor trust”
- Information reported where corresponding tax liability

UK-OS/CD Expansion

- Under “UK FATCA” (with Overseas Territories & Crown Dependencies), “ultimate effective control” subject to interpretation
- Jersey generally concludes that Protector is in “ultimate effective control”
- Consistent with OECD common reporting standard

Jersey Reportable Account



Control v. Ownership

- Ability to remove trustee may be “control”, but still lacks “interest” or “entitlement”
- Taxability lost in focus when seeking information, income irrelevant
- Neither Trust nor Beneficiaries Subject to tax in the UK
- While Accounts of Trust non-reportable, “interest” held by Protector is reportable

Trusts & FATCA

- US Approach -- information reporting to seek income from conduits and thus tax liability
- Other jurisdictions – results less sensible
 - Reporting not necessarily about “entitlement” or “beneficial ownership” but includes “control” w/o rights



Thank you!

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