Tax information exchange

HMRC data powers

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A common reporting standard across the world and crypto-asset reporting framework

International tax reporting comes of age

In conjunction with the G20, the OECD developed the Common Reporting Standard (CRS) as a global standard for the automatic exchange of information.[1]

In August 2022 the OECD introduced the Crypto-Asset Reporting Framework (CARF) and also made updates to CRS to include certain electronic money products and Central Bank Digital Currencies with the new rules expected to come into force from 2026. In addition, indirect investments in crypto-assets are now also covered by CRS.

How CRS works

Each participating jurisdiction has passed domestic legislation requiring 'Financial Institutions' (FIs) in the jurisdiction to provide their local taxation authorities with financial data on relevant persons (broadly asset owners) who are resident in other participating countries. This means that FIs have to make reports on their clients who are resident in other countries: this includes the beneficial owners of bank accounts and those with an interest in trusts and other entities.

As with reporting required under FATCA (the USA's Foreign Account Tax Compliance Act), the FIs that must provide data include banks, trusts, TCSPs, collective investment vehicles, funds of all types, private equity groups, 'carry' vehicles, brokers other depository and custodial institutions, investment entities, some insurance companies and even charities. The reporting institutions will be widened to include e-money and certain crypto businesses following the implementation of the CRS updates (along with CARF). However, unlike FATCA, there are fewer exempt institutions.

The reported data will be passed on automatically to the relevant countries (within nine months of the end of the relevant calendar year) in a standard format that can easily be imported into the taxpayer databases of each country. The data will be analysed to identify those who may have evaded or avoided tax in their country of residence as well as those who may simply have made an error in their tax returns.

A core feature of the CRS rules is that local reporting FIs must do due diligence on account holders. The level of diligence required includes obtaining a self-certification by the client of where the client is tax resident and their tax and personal details plus a review of data for evidence of where each of their customers is resident (including PO boxes, 'care-of' addresses, 'hold mail' instructions and standing instructions to send funds to resident based accounts) and an 'actual knowledge' test for client relationship managers.

Whose data is being exchanged

FIs must report on financial accounts, which includes bank accounts, custodial accounts, debt and equity investments as well as interest in trusts and partnerships. Passive entities will be 'looked through' with reporting taking place in respect of the persons controlling those entities. Note that the US$50,000 de minimis threshold, that applies to individuals under the FATCA, is not replicated in the CRS, so many more account holders need to be identified and reported on.

Reportable information - CRS

How CARF works

About the owner/s	About the asset	Income/gains/ movements
Full name	Name of the financial institution and its identifying number	Gross interest received
Address	Type of asset (financial accounts/products as well as interests in trusts/holding entities)	Dividends received
Date of birth	Local account number/identifier	Gross capital sale proceeds received into account
Place of birth	End of the year balance for cash deposits	Any other income derived from financial assets
Tax identification number	Cash value for other assets	Amounts credited to the beneficial owners

In a similar way to the CRS, the CARF requires Crypto-Asset Service Providers to identify and obtain tax information on their individual and entity clients and report details of relevant transactions in crypto-assets. At November 2023, 48 members of the OECD agreed to implement the CARF by 2027[2] ,with the first reporting for the 2026 calendar year being in May 2027.

1 Source: https://www.oecd.org/tax/automatic-exchange/international-framework-for-the-crs/
2 Sources: https://www.oecd.org/tax/exchange-of-tax-information/crypto-asset-reporting-framework-and-amendments-to-the-common-reporting-standard.htm; https://www.bdo.co.uk/en-gb/insights/tax/tax-dispute-resolution/new-tax-transparency-framework-for-crypto-assets

Are your Crypto-Assets Reportable?

Crypto-assets are defined as any digital representation of value that relies on a cryptographically secured distributed ledger, or a similar technology, to validate and secure transactions. This includes commonly used cryptocurrencies such as Bitcoin and Ethereum, as wells as stablecoins, crypto-asset derivatives and certain non-fungible tokens (NFTs). Where a crypto-asset isn't a digital representation of value but rather just an audit trail or record of a transaction then they may be excluded from the reporting requirements. BDO's crypto-asset team can help analyse whether all or some of your assets meet the requirements to report.

Reportable information - CARF

About the owner/s	About the asset and income/gains/ movements
Full name	Name and address of crypto-asset service provider and its identifying number
Address	Full name of the type of crypto-asset
Date of birth	Gross amounts paid, units and number of transactions in respect of acquisitions using Fiat currency
Place of birth	Gross amounts received, units and number of transactions in respect of disposals into Fiat currency
Tax identification number	Aggregate fair market value, units and number of transactions in relation to retail payment transactions (over $50,000) using crypto-assets as consideration
	Aggregate fair market value, units and number of transactions in relation to acquisitions and disposals involving other crypto-assets (ie exchange of crypto)
	Aggregate fair market value, units and number of transactions in relation to transfers to other third-party wallet addresses

Implications for financial institutions and their clients

CRS places significant responsibilities on FIs

With so many countries involved, such a wide range of assets covered and a very broad spectrum of owners and asset controllers to report on, even those already reporting under FATCA saw a step change in their compliance tasks when CRS began.

Many entities around the world are unexpectedly classified as FIs under the CRS, and so urgently need to consider the implications as a result.

FIs should be aware that HMRC and other tax authorities are being pro-active and requesting evidence of FIs' CRS and FATCA due diligence processes.

Clearly, communicating effectively with clients is key to managing these reporting responsibilities: all customers (including controllers of certain entities resident overseas) must be informed about the reporting requirements for participating countries, and must provide identifying information when opening accounts.

Where are your clients tax resident?

In many cases, clients of FIs should be able to self-certify the country in which their clients are tax resident. However, in certain cases the situation may be complex creating an area of concern for FIs. FIs and their clients need to ensure that the information held by the FI accurately reflects the true tax position.

Although it is often a difficult message to give to new and existing clients, it is vital that they are warned of potential tax consequences of reporting under the CRS. If the relevant income or gains that must be reported have not previously been reported in their country of residence (even for legitimate reasons) they are likely to be investigated by the local tax authorities and could face a large tax bill or worse. No matter which country they live in, putting any tax irregularities right or simply explaining their overseas assets to the tax authorities before the first report for the client is always likely to be the best option.

Reporting avoidance arrangements

The OECD has considered ways to address arrangements that seek to circumvent reporting under the CRS and the use of non-transparent structures. This resulted in the publication of Model Mandatory Disclosure Rules for CRS Avoidance Arrangements and Opaque Offshore Structures (MDR). Jurisdictions can choose whether to implement these rules, however chapter IX of the CRS, to which over 100 jurisdictions have committed, requires these jurisdictions to have rules in place to prevent CRS avoidance arrangements and clearly the MDR can play an important role here.

The OECD has published an information exchange framework to support the MDR and a multilateral competent authority agreement that countries will sign to implement the framework.

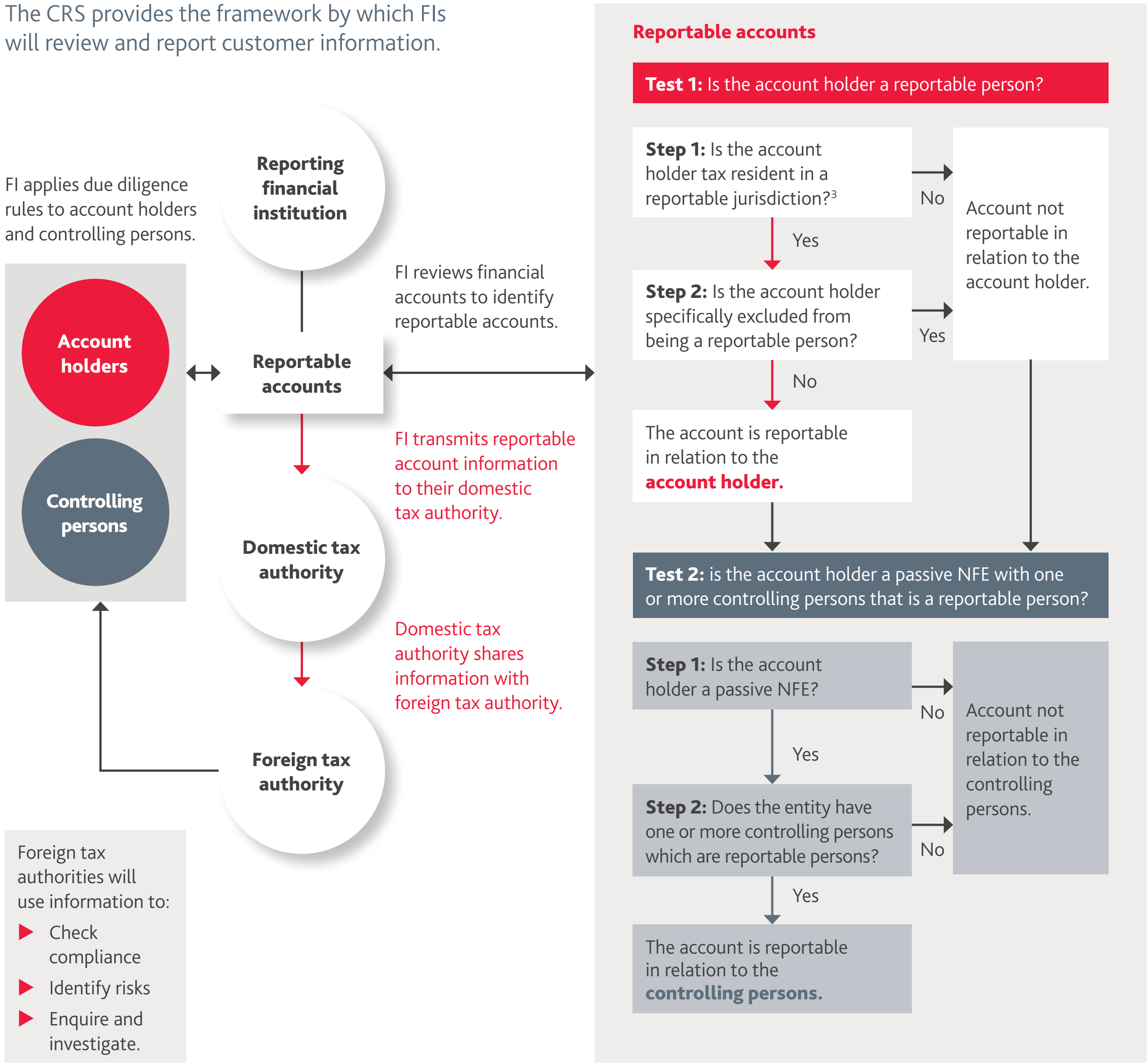
The aim is for jurisdictions to be able to pass on details of financial arrangements that fall within the rules to the jurisdictions in which the users of the arrangements are tax resident. It will then be possible for the jurisdiction to take action to adjust their local tax laws to make the arrangements ineffective or take enforcement action where the arrangements already breach local tax law.

In addition, an EU directive known as DAC 6 (it is the sixth update of the Directive on Administrative Cooperation) also imposes disclosure requirements on cross-border tax arrangements. This incorporates the MDR but also applies to a wider set of arrangements. EU member states must implement DAC 6 for relevant arrangements. For the UK, the application of DAC6 was narrowed post Brexit and the MDR, noted above, has effectively replaced it.

Exchange of information framework

Please note, the same framework should apply to CARF, albeit with different terms (e.g. Reporting Crypto Asset Service Provider and Reportable User).

The CRS provides the framework by which FIs will review and report customer information.



3 In general, a jurisdiction will be a Reportable Jurisdiction if it has an agreement is in place for the exchange of information under the CRS. Each jurisdiction must publish a list of Reportable Jurisdictions.

UK approach to tax transparency

The UK has been at the forefront of global initiatives to increase international tax transparency and HMRC's 'No Safe Havens policy' is designed to increase offshore tax compliance and clamp down on tax avoidance.

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UK asset ownership

Companies

UK companies' annual confirmation statements to Companies House must contain details of its beneficial owners. The details must also be provided when companies are incorporated, and both limited liability partnerships and Societas Europaea must report on the people who own or control their businesses: companies whose shares are listed on a regulated stock market are exempt from these rules. Anyone is able to request to see the information in a company's register unless the company refuses and informs the court of its refusal.

Companies must identify and report substantial information (name, address, nationality etc.) of 'persons with significant control' over the company, ie anyone who:

a. Directly or indirectly owns more than 25% of the shares
b. Directly or indirectly holds more than 25% of the voting rights
c. Directly or indirectly holds the right to appoint or remove the majority of directors
d. Otherwise has the right to exercise, or actually exercises, significant influence or control
e. Holds the right to exercise, or actually exercises, significant influence or control over the activities of a trust or firm which is not a legal entity, but would itself satisfy any of the first four conditions if it were an individual.

Trusts

Any trust liable to UK tax must be registered with the UK's national trust register, this includes trusts where:

1. All individual trustees are UK tax resident or a corporate trustee is incorporated in the UK
2. The settlor was UK resident or UK domiciled at the time it was created
3. It is offshore but has UK assets or income from a UK source.

The trustees must provide basic details of the trust itself (including its tax residence status and the assets it holds), its beneficial owners and any potential beneficiaries.

Land and property beneficial owner register

The identity of offshore beneficial owners of UK property and those who control them, for example non-UK resident companies and their shareholders, is required to be recorded on the register of overseas entities (ROE) with Companies House.

Registration is enforced through the land registration process for transfers of UK property. The ROE came into force in the UK through the Economic Crime (Transparency and Enforcement) Act 2022.

Unexplained Wealth Orders

HMRC can ask the UK High Court to issue an 'Unexplained Wealth Order' where there are reasonable grounds for suspecting that the person's known lawfully obtained income was insufficient to enable them to obtain the property and that fraud or criminal behaviour has occurred. The order allows HMRC to demand information from the asset owner on how it was acquired.

HMRC use of data

Exchanged data

As well as information on individuals, businesses and other entities obtained passively via the CRS, country-by-country reports and the EU directive on mandatory automatic exchange of information, HMRC can also request access to a wide variety of offshore data on UK taxpayers. Where there is a suspicion of omitted income or gains from UK tax returns, HMRC can make specific requests for data on specific taxpayers from other tax jurisdictions with which it has a Tax Information Exchange Agreement.

The Government issued it's policy paper "tackling offshore non-compliance" on 30 October 2024, which demonstrates that HMRC is determined to address offshore tax non-compliance as part of the Government's efforts to close the tax gap. HMRC is taking additional steps to increase the offshore data available, ensuring that tax is paid on AEOI income and providing HMRC with additional resources "to tackle more complex offshore cases".

HMRC's Risk and Intelligence service

HMRC's has a dedicated central department that uses data gathered from a wide array of sources to identify UK residents who may not be declaring all their income and gains. For example, where CRS data on offshore accounts is not reflected in an individual's UK tax return HMRC will investigate further – it may cross-check with information from UK sources such as Companies House and the Land Registry and even review the social media posts of the individual to assess whether their lifestyle is consistent with their income.

This may sound like a daunting task but HMRC has a purpose built analysis tool – CONNECT – which can process very high levels of data to compile financial profiles of individuals and businesses. This helps to automate HMRC's processes: for example, if CRS data about an offshore bank deposit has not been reported on the individual's tax return, an automated 'nudge letter' may be sent to the individual to prompt them to correct their tax position as needed and pay any additional tax due.

Individuals who do not respond to these 'nudge letters' are likely to face a thorough tax enquiry. These can range from a standard self-assessment enquiry to a serious civil investigation or a criminal investigation. HMRC will open these checks, rather than sending 'nudge letters', in some cases. Where HMRC finds more tax is due it may assess up to 20 years' tax depending on why the failure or error occurred.

Of course, there will be many circumstances where an apparent discrepancy is entirely innocent. It is important that such circumstances are explained clearly to HMRC to resolve the position quickly.

Simplification of taxation of offshore income

As announced in the Autumn Budget 2024, HMRC is committed to the simplification of taxation of offshore income. This includes reducing the compliance challenges arising from the mismatch of information on offshore interest being provided via the CRS and similar cross border reporting regimes on a calendar year basis rather than a UK tax year basis and is consulting on this matter.

Putting things right

Voluntary Disclosures

Where it is clear that a person's UK tax returns contain inaccuracies, it is always better to put things right before HMRC discovers them through its risk assessments. Making a voluntary disclosure and paying all tax due, will help to resolve the issue quickly and reduce the tax penalties that may arise. In addition, the taxpayer is likely to escape being named on HMRC's website and the risk of a criminal prosecution is removed.

Help From BDO's Expert Team

Our success in resolving all kinds of investigations, ranging from simple tax enquiries to complex investigations and voluntary disclosures, enables us to minimise the stress and anxiety associated with reaching a resolution with HMRC.

With extensive experience of disclosure and investigation practices, tactics and strategies, we guide our clients smoothly through the process and are fully equipped to protect our clients' interests. We strive to achieve the best possible result for our clients.

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