Latest FATCA/CRS Guidance: What Canadian financial institutions need to know

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What you need to know

- Canadian financial institutions (FIs), as they are broadly defined for purposes of Part XVIII (the *Foreign Account Tax Compliance Act* (FATCA) provisions) and Part XIX (the *Common Reporting Standard* (CRS) provisions) of the *Income Tax Act* (Canada) (the ITA), are subject to due diligence and reporting obligations.
- To assist FIs with these due diligence and reporting obligations, the Canada Revenue Agency (CRA) issues guidance in respect of both Part XVIII (the FATCA Guidance) and Part XIX (the CRS Guidance).
- On March 10, 2022, the CRA released an update to the FATCA Guidance and CRS Guidance (collectively referred to herein as the Latest Guidance).
- The Latest Guidance replaces the CRA's previous FATCA Guidance and CRS Guidance released on July 10, 2020 (collectively referred to herein as the Prior Guidance).
- This article provides an overview of some of the latest amendments relevant to FIs.

The Latest Guidance also includes amendments to the CRA's administrative position on arrangements where multiple FIs maintain the same financial account that are not discussed herein. These changes are discussed separately in *Latest FATCA/CRS Guidance: changes relevant to the asset management industry*.

Overview of amendments

FATCA and CRS: Death of an account holder

The Latest Guidance has clarified the treatment for an account held by a person who has died.

When an account holder dies and the FI has not received a formal notification of death, the FI must treat the account as being held by the individual. The account will have the same status that it had prior to the account holder's death (e.g., if the account was

reportable while the individual was alive, it must continue to be treated as reportable after the account holder's death and until such time that the FI is notified of the death).

Once the FI receives notification of the account holder's death, the deceased's account is deemed to be closed (even if it is not actually closed). If the account is reportable, the account closure must be reflected in the information return.

FATCA and CRS: Accounts held by estates

The Latest Guidance has clarified the FATCA and CRS treatment for an account held by an estate.

If the account is used by the estate solely to distribute assets and manage the affairs of the deceased person, it is *not* considered a financial account. Accordingly, there will be no due diligence or reporting obligations in respect of the account.

On the other hand, if the account is not being used solely for asset distribution or estate administration, it will be considered a financial account. There will be due diligence and reporting obligations in respect of the account.

FATCA and CRS: Penalties for missing self-certifications

FIs are required to obtain a self-certification from the account holder within 90 days of (i) account opening or (ii) the occurrence of a "change in circumstances"[1]. Failure to obtain a self-certification may subject the FI to a $2,500 penalty under *each* of FATCA and CRS (for a maximum cumulative penalty of $5,000 for each undocumented account).

In the New Guidance, the CRA has stated that it will not assess the penalty on FIs that take "effective measures" to obtain a self-certification from the account holder. The CRA states that an "effective measure" may include closing or freezing accounts with missing self-certifications.

FATCA and CRS: New account openings for holders of existing accounts

An individual or entity that already has an existing account (the Existing Account) with the same FI or a related FI in Canada may want to open a new account (the New Account). If certain conditions are met, the FI is relieved from collecting a self-certification for the New Account (the New Account Relief), because it can rely on the self-certification obtained for the Existing Account.

The following conditions must be satisfied in order for the FI to take advantage of the New Account Relief:

- The account holder already holds the Existing Account with the (i) FI or (ii) a related entity of the FI in Canada;
- The opening of the New Account does not require the provision of any new, additional or amended "customer information" by the account holder (other than for CRS purposes);

- If the New Account is subject to Anti-Money Laundering or Know Your Client procedures, the FI is permitted to satisfy those procedures by relying on the procedures performed in connection with the Existing Account; and
- The FI and its related entities in Canada must treat the New Account and Existing Account as a single account. This requires the FI to have internal processes allowing it to:
    - know that the statuses for both accounts are inaccurate if the FI has reason to believe that the status for either of the accounts is inaccurate, and
    - treat both accounts as a single account when applying any account thresholds.

In the Latest Guidance, the CRA has further elaborated on the second condition discussed above. In particular, the CRA has defined "customer information" as information about the identity of the account holder" that does not include "the nature or characteristics of the account or investment such as altering the mix of investments within an account". Furthermore, the CRA expressed its view that the following scenarios likely involve new or amended customer information such that the New Account Relief does not apply:

- The Existing Account is a depository account and the New Account is a custodial account (as the account holder will likely be required to provide information on his or her risk profile for the New Account); or
- The conclusion of a new insurance contract.

FATCA and CRS: Verbal self certifications for telephone account openings

Some FIs open accounts by telephone and capture a verbal self-certification for those purposes (*e.g.,* the FI obtains a voice recording or digital footprint to confirm that a self-certification was completed).

Pursuant to the Prior Guidance, the FI must retain any verbal self-certification for the required retention period unless one of the following exceptions applies:

- The FI secures and appropriately retains a self-certification in an alternative format from the account holder; or
- The FI informs the account holder in writing of how it has recorded the account holder's status, and instructs the account holder to notify it if its record is incorrect.

The Latest Guidance removes the second exception.

FATCA and CRS: Online self-certifications and electronic signatures

FIs may collect the self-certification electronically. An electronic self-certification must still include the account holder's signature.

The Latest Guidance has clarified the rules pertaining to "electronic signatures". An electronic signature is anything unique to the account holder for which a record can be

kept. It may be numeric, character-based or biometric. For example, a client's personal identification number is an electronic signature.

The Latest Guidance also clarifies that FIs should only accept electronic signatures in the following scenarios:

- The account holder sends the electronic signature using the email address most recently provided by the account holder to the FI;
- The account holder provides the electronic signature in the FI's presence (*e.g.,* the account holder signs on a tablet using his or her finger); or
- The account holder provides the electronic signature through an access controlled, secured electronic location (*e.g.,* the FI provides the account holder with access to a secure website that is accessible only by the account holder).

FATCA and CRS: Providing a Canadian TIN on a self-certification

The Latest Guidance has clarified that a self-certification requires the account holder's Canadian TIN only in situations where the account holder is a reportable person.

As a result of this change, account holders are not required to provide a Canadian TIN if Canada is their only jurisdiction of tax residence.

FATCA and CRS: Controlling persons and discretionary beneficiaries

When the account holder is a trust, its controlling persons include the beneficiaries. In the case of discretionary beneficiaries, they are considered controlling persons only for the calendar years in which they receive a distribution. Because of this, the CRA requires FIs to have internal procedures allowing it to be notified when a distribution is made to a discretionary beneficiary in a given year.

The Latest Guidance clarifies the type of internal procedures that the CRA expects from FIs to satisfy their due diligence obligations in this context by providing the following two examples:

- The FI seeks annual refreshment of the self-certification so that the trust or trustee re-certifies whether any discretionary beneficiaries are controlling persons; or
- The FI requires the trust or trustee to provide a new self-certification whenever the trust has made or will make a distribution to a discretionary beneficiary, and this requirement is made a condition of holding the account.

FATCA and CRS: FIs that become reporting FIs

FIs may cease to be a non-reporting FI and become a reporting FI. In these scenarios, the Latest Guidance clarifies that the relevant cut-off date for reviewing accounts is the beginning of the following reportable period.

For example, if the reportable period begins on January 1 of each year and the FI becomes a reporting FI at some point in 2021:

- The FI applies the new account due diligence procedures for financial accounts opened on or after Jan. 1, 2022 (*i.e.,* the beginning of the following reporting period);
- The FI applies the pre-existing account due diligence procedures for any financial account it maintained on Dec. 31, 2021; and
- The FI's first reporting period is Jan. 1, 2022 to Dec. 31, 2022.

FATCA: Completing returns for accounts with missing U.S. TINs

Previously, FIs were advised to enter "000000000" or "AAAAAAAAA" in the U.S. TIN field of the information return if the reportable account had a missing U.S. TIN.

The Latest FATCA Guidance outlines six new codes that were developed by the Internal Revenue Service for accounts that lack a valid U.S. TIN. To review the full list of the new codes and the circumstances in which they are used, please refer to paragraph 12.62 of the Latest FATCA Guidance.

The Latest FATCA Guidance confirms that the use of the new codes is optional, and using them does not necessarily mean that the FI will not be considered to be significantly non-compliant with their obligations under Part XVIII of the ITA.

CRS: Residence and citizenship by investment schemes

The Organization for Economic Co-operation and Development has identified jurisdictions offering residence and citizenship by investment (CBI/RBI) schemes. CBI/RBI schemes allow individuals to obtain citizenship or residence by making local investments or paying a flat fee.

FIs were previously required to make further inquiries to confirm the reasonableness of a self-certification where the account holder listed a CBI/RBI jurisdiction as its jurisdiction of tax residence. This appeared to be the case even if the CBI/RBI jurisdiction was not the only jurisdiction of tax residence identified by the account holder on the self-certification.

The CRA has clarified in the Latest CRS Guidance that these further inquires are only required when the account holder claims to solely reside in a jurisdiction offering a CBI/RBI scheme.

FATCA and CRS: Anti-avoidance

There are anti-avoidance provisions in sections 268 and 280 of the ITA for purposes of FATCA and CRS compliance, respectively. In general, the anti-avoidance rule applies when a person enters into an arrangement or engages in a practice, the primary purpose of which can reasonably be considered to be an avoidance of a FATCA or CRS obligation. Where the anti-avoidance rule applies, the person is nonetheless subject to the FATCA or CRS obligation despite the particular avoidance arrangement or practice.

The Latest Guidance provides two specific examples of how the anti-avoidance rule applies to FIs:

- In the absence of any commercial reason, the FI does not create any electronic records for lower value accounts so that an electronic record search would not yield any results; or
- In the absence of any commercial reason, the FI maintains computerised systems artificially dissociated to avoid application of the entity account aggregation rules.

The Latest Guidance also provides one example of how account holders may be caught by the anti-avoidance rule. This example involves an entity account holder transferring amounts (i) out of a pre-existing account *before* the end of the calendar year and (ii) into the pre-existing account *after* the end of the calendar year. If it is reasonable to conclude that the account holder initiated the transfers to manipulate the year-end account balance to be less than the reporting threshold for pre-existing accounts, the anti-avoidance rule applies.

As pandemic restrictions ease, we expect the CRA to begin commencing on-site audits of FIs for FATCA and CRS compliance. In order to avoid any non-compliance penalties, it is imperative for FIs to ensure that their internal policies and procedures are consistent with the Latest Guidance.

Please contact the authors if you have questions on how your FI's internal policies and procedures should be amended to reflect the Latest Guidance.

[1] A change in circumstances occurs when the FI obtains any information that causes it to know or have reason to know that the original self-certification is incorrect or unreliable.

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