

CHAPTER 11

DUE DILIGENCE: PRE-EXISTING ENTITY ACCOUNTS

Pre-existing accounts are those in existence as at 31 December 2016. An entity for the purposes of AEOI regime is a legal person or legal arrangement. It covers accounts held by any person other than in the capacity of an individual. Thus it covers accounts held by any entity that falls within the definition of company under the Companies Ordinance (Cap. 622) along with legal arrangements including partnerships and trusts.

2. For reporting purposes an entity will either be a financial institution or an NFE.

Threshold exemption

3. Unless election is made by a reporting financial institution, a pre-existing entity account with an aggregate account balance or value that does not exceed \$1.95 million as at 31 December of each year or the last day of other appropriate reporting period is not required to be reviewed, identified, or reported as a reportable account until the aggregate balance or value exceeds \$1.95 million as at the last day of any subsequent calendar year or reporting period.

Reportable accounts

4. A pre-existing entity account is a reportable account where the review procedures identify the account as held by one or more entities that are reportable persons or which are passive NFEs with one or more controlling persons that are reportable persons.

5. For example, the XYZ Partnership is a passive NFE resident in Hong Kong. It has three individuals who are identified as controlling persons of the partnership. Two of these are Hong Kong tax residents but the third is tax resident in France which is a reportable jurisdiction. As a result any accounts held by the partnership with a reporting financial institution will be reportable accounts by virtue of the entity having a controlling person that is a reportable person.

Available information

6. Where the reporting financial institution has carried out the review of

regulatory and customer relationship information and has indications that the account holder is resident in a reportable jurisdiction it may take into account information in its possession, or which is publicly available, which reasonably determines that the account holder is not a reportable person with respect to such reportable jurisdiction.

7. Such information will include the following:
 - (a) information published by an authorised government body of a jurisdiction. For example, the list of Foreign Financial Institutions published by the US tax administration;
 - (b) information in a publicly accessible register maintained or authorised by an authorised government body of a jurisdiction;
 - (c) information disclosed on an established securities market; and
 - (d) information previously recorded in the files of the financial institution;
8. Where the reporting financial institution relies on such information it must retain a notation of the type of information reviewed and the date the review was carried out.

Account holder

9. Reporting financial institutions are required to determine whether a pre-existing account is held by one or more entities that are reportable persons. If any of the entities is a reportable person then the account will be a reportable account.
10. The reporting financial institution must review information maintained for regulatory or customer relationship purposes (including information collected as part of any AML/KYC procedure) to determine where the entity is resident. The entity will be reportable if the information indicates that the entity is resident in a reportable jurisdiction. Such information will include, but is not limited to:
 - (a) a place of incorporation or organisation in a reportable jurisdiction;
 - (b) an address in a reportable jurisdiction; or

- (c) where the entity is a trust, an address of one or more of the trustees in a reportable jurisdiction.

11. As the definition of entity goes beyond corporate structures to include fiscally transparent vehicles such as trusts and partnerships, the address of the entity should be interpreted widely so will include the registered office, principal office and/or the place of effective management.

12. The existence of a permanent establishment (including a branch) in a reportable jurisdiction is not, in isolation, an indication of residence for this purpose.

13. Although there is no exemption from a paper record search for pre-existing entity accounts, such a search is not required in areas where all the information is electronically searchable (for example, information held for AML/KYC purposes).

14. If the information indicates that the account holder is resident in a reportable jurisdiction then the account is a reportable account unless the reporting financial institution obtains a self-certification from the account holder, or determines, based on information in its possession or which is publicly available, that the account holder is not a reportable person.

Self-certification

15. Where the reporting financial institution has carried out the review of regulatory and customer relationship information and has indications that the account holder is resident in a reportable jurisdiction it may obtain a self-certification from the account holder which reasonably determines that the account holder is not a reportable person with respect to such reportable jurisdiction.

16. A self-certification for an entity must be signed (or otherwise positively affirmed) by the person with authority to sign on behalf of the entity. This will include:

- (a) an officer or director of a corporate entity;
- (b) a partner of a partnership;
- (c) a trustee of a trust;
- (d) any person holding an equivalent title to any of the above; and

- (e) any other person with written authorisation from the entity to sign documentation on behalf of the entity.

17. The self-certification must also be dated at the latest at the date of receipt by the reporting financial institution and must contain the following information in respect of the entity:

- (a) the name;
- (b) the address;
- (c) the jurisdiction(s) of residence for tax purposes; and
- (d) the TIN with respect to each jurisdiction.

18. The reporting financial institution may also request the account holder entity to include its status in the self-certification as either a financial institution or an NFE. When requesting this information from an account holder the reporting financial institution is expected to provide the account holder with sufficient information to enable it to determine its status. Reporting financial institutions may produce their own guidance for this purpose or they may make reference to the IRD's Guidance for Financial Institutions or the OECD Standard for Automatic Exchange of Financial Account Information in Tax Matters.

19. The requirements for the validity of such a self-certification are the same as for those for self-certification of new individual accounts.

Financial institution

20. The reporting financial institution may request the account holder entity to include its status in the self-certification as either a financial institution or an NFE. When requesting this information from an account holder the reporting financial institution is expected to provide the account holder with sufficient information to enable it to determine its status.

21. If the account holder entity falls within the definition of a financial institution no further review, identification or reporting will normally be required. The exception to this is where the financial institution is an investment entity as described in paragraph (e) of the definition of investment entity (a managed investment entity) resident in a jurisdiction that is not a participating jurisdiction. In that case the entity is deemed to be a passive NFE for reporting purposes.

22. When seeking a self-certification from an entity the categories that may be recorded for a financial institution are:

- (a) managed investment entity; and
- (b) financial institution other than (a) above.

NFE

23. The reporting financial institution may request the account holder entity to include its status in the self-certification as either a financial institution or an NFE. When requesting this information from an account holder the reporting financial institution is expected to provide the account holder with sufficient information to enable it to determine its status.

24. If the account holder entity falls within the definition of an NFE then the information to be reported will depend on whether the entity is an active NFE or a passive NFE.

Controlling persons

25. When a reporting financial institution has determined that an account holder is an NFE it must carry out review procedures to determine:

- (a) whether the account holder is a passive NFE;
- (b) if so, the controlling persons of that passive NFE; and
- (c) whether any of the controlling persons is a reportable person.

Is the account holder a passive NFE?

26. The reporting financial institution must obtain a self-certification from the account holder unless it has information in its possession, or that is publicly available, based on which it can reasonably determine the status of the account holder as an active NFE or a financial institution (other than a managed investment entity resident in a non-participating jurisdiction). If the reporting financial institution cannot determine the status of the account holder as an active NFE or a financial institution then the reporting FI must presume the account holder to be a passive NFE.

Controlling persons

27. A controlling person is any natural person who has control over an entity, or who is able to use their influence and authority to make decisions on behalf of an entity.

Identifying controlling persons

28. To identify the controlling persons, the reporting financial institution may use information collected and maintained pursuant to AML/KYC procedures.

Are any of the controlling persons a reportable person?

29. If the account balance or value does not exceed an amount equivalent to \$7.8 million, the reporting financial institution may rely on information collected and maintained pursuant to AML/KYC procedures to determine whether the controlling person is a reportable person or it may choose to obtain a self-certification from the account holder or the controlling person.

30. If the account balance exceeds an amount equivalent to \$7.8 million the reporting financial institution must obtain a self-certification from either the account holder or the controlling person. The self-certification requirements are the same as for new individual accounts.

31. If a self-certification is required but is not obtained the reporting financial institution must rely on the electronic record search and paper record search (if applicable) for pre-existing individual accounts to determine if there are indicia present that can be used to determine the reportable status of the controlling person. If none is present in its records, the reporting financial institution need take no further action unless and until there is a change of circumstance that results in one or more indicia with respect to the controlling person being associated with the account. It is acknowledged that there is difference between the wording of the CRS and its Commentary and Annex 5 (i.e. wider approach to CRS), on which section 9(2) of Division 3 of Part 5 in Schedule 17D is based. The OECD has expressed the view that the wider approach section is only an example of how this approach could be operated, whereas the CRS text is the binding minimum set of rules (i.e. electronic and paper record search) for translating the CRS.

Change in circumstances

32. If there is a change in circumstances that casues the reporting financial institution to know or have reason to know that the self-certification or other

documentation associated with the account is incorrect or unreliable, the reporting financial institution must re-determine the status of the account in accordance with the procedures described under Division 3 of Part 5 in Schedule 17D (i.e. to determine whether the entity is a reportable person; and to determine whether the entity is a passive NFE with one or more controlling persons that are reportable persons). In this case, the reporting financial institution must apply the following procedures by the later of the last day of the relevant calendar year or other appropriate reporting period, or 90 days following the notice or discovery of the change in circumstances:

- (a) with respect to the determination whether the account holder is a reportable person: a reporting financial institution must obtain either (i) a self-certification, or (ii) a reasonable explanation and documentation (as appropriate) supporting the reasonableness of the original self-certification or documentation (and retain a copy or a notation of such explanation and documentation). If the reporting financial institution fails to either obtain a self-certification or confirm the reasonableness of the original self-certification or documentation, it must treat the account holder as a reportable person with respect to both jurisdictions.
- (b) with respect to the determination whether the account holder is a financial institution, active NFE or passive NFE: a reporting financial institution must obtain additional documentation or a self-certification (as appropriate) to establish the status of the account holder as an active NFE or financial institution. If the reporting financial institution fails to do so, it must treat the account holder as a passive NFE.
- (c) with respect to the determination whether the controlling person of a passive NFE is a reportable person: a reporting financial institution must obtain either (i) a self-certification, or (ii) a reasonable explanation and documentation (as appropriate) supporting the reasonableness of a previously collected self-certification or documentation (and retain a copy or a notation of such explanation and documentation). If the reporting financial institution fails to either obtain a self-certification or confirm the reasonableness of the previously collected self-certification or documentation, it must rely on the indicia described under section 3(3) of Part 3 in Schedule 17D it has in its records for such controlling person to determine whether it is a reportable person.