



Considine Education Seminar

Foreign Information Reporting Requirements

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Overview

- “Good Old Days” and Financial Statements “Available on Demand”
- Tougher Stance as of January 1, 2009 – Automatic Penalty Notices for 5471s
 - UBS Scandal and Hearings – US Taxpayers Hiding Billions Offshore
 - See, <http://www.irs.gov/businesses/corporations/article/0,,id=188039,00.html>
- 2009 and 2011 Offshore Voluntary Disclosure Programs



Overview

- How Will They Know?
 - President's 2011 Budget – 800 New International Enforcement Personnel
 - Treaty-Based Information Exchanges
 - Civil Summons Process for Foreign Institutions Operating in the U.S.
 - Indictments of Foreign Financial Institutions
 - Information from Whistleblowers and Informants
 - Data-Mining Submissions Received from Participants in Disclosure Programs
 - Cooperation from Taxpayers, Advisors, Foreign Institutions and Bankers Who Have Been Criminally Prosecuted
 - Disclosures Under the Foreign Account Tax Compliance Act (FATCA)

They Will Find Out!!



Overview

- HIRE Act on March 18, 2010
 - FATCA and Disclosure of US Account Holders
 - New Section 6038D for Foreign Financial Assets
 - New Section 1298(f) and Annual Filing for PFIC Shareholders
 - Revision to Section 6501(c)(8) – Entire Tax Return is Open Unless Reasonable Cause
 - New Section 6662(j) and 40% Penalty for Undisclosed Foreign Asset

Increasing Information Reporting Requirements



Current Landscape

- Extreme Pressure for Timely International Reporting Compliance
- Must Have Understanding of Complex Code Provisions



Form TD F 90-22.1 “FBAR” (33 USC 5314 – Bank Secrecy Act)

- Originated in 1970 as part of Bank Secrecy Act to Detect and Combat Money Laundering
- Historically Tax Enforcement
- Patriot Act of 2001 and Report to Congress
 - 2001 – 177,000 Filings
 - 2007 – 322,000 Filings (of 1,000,000 estimated)
 - “Ripe” Area for Enforcement
- Inclusion of Schedule B Question
- Enforcement Transferred from FINCEN to IRS in 2003



Form TD F 90-22.1 “FBAR” (31 USC 5314 – Bank Secrecy Act)

- “US Person”
- “Financial Interest” in, or “Signature or Other Authority Over”
- One or More Bank, Securities or “Financial Accounts”
- Located in a “Foreign Country”
- Aggregate Value of Which > US\$10,000 During Year



Form TD F 90-22.1 “FBAR” (31 USC 5314 – Bank Secrecy Act)

- “U.S. Persons”
 - Previously Required to be Filed by Persons “Subject to Jurisdiction of U.S.”
 - 2010 Proposed Regulations Used § 7701 Definition of “U.S. Person” – Align Title 31 Definition with Title 26 Definition
 - 2011 Final Regulations Adopted “U.S. Person” Definition, with Modifications
 - Foreign Corporations and § 897(i) Election – Still Foreign
 - Trusts Based on Jurisdiction, not Court/Control Test
 - Resident of U.S. under Substantial Presence Test or Green Card
 - No Treaty Override from Treaty Nonresident Position
 - Single Member LLC – Not Disregarded for FBAR Purposes



Form TD F 90-22.1 “FBAR” (31 USC 5314 – Bank Secrecy Act)

- “Other Financial Interest”
 - Ownership through Agent or Nominee
 - >50% Interest in Entity Account Holder (Indirect Ownership)
 - Attribution and Constructive Ownership Rules Do Not Apply
 - Grantor Trusts
 - E.g., U.S. Person Creates Foreign Trust with U.S. Beneficiaries
 - Nongrantor Trusts and Present Beneficial Interest in >50% of Assets or Receives >50% of Income
 - Not Remainder or Discretionary Beneficiary
 - Discretionary (Accumulation) Trusts
 - Should File if Actual Distribution of >50% Income or Assets
 - Anti-Abuse Rule



Form TD F 90-22.1 “FBAR” (31 USC 5314 – Bank Secrecy Act)

- “Financial Account”
 - Broadly Defined and Includes Mutual Funds, Savings, Demands, Checking, Deposit or Any Other Account (including Debit Card and Prepaid Credit Card) Maintained with a Financial Institution
 - Account with Broker/Dealer for Futures or Options Transactions in any Commodity
 - Gold or Precious Metals in Safety Deposit Box
 - Final Regulations – Life Insurance or Annuity with Redemption Feature or Cash Surrender Value



Form TD F 90-22.1 “FBAR” (31 USC 5314 – Bank Secrecy Act)

- “Signature or Other Authority”
 - Authority of an Individual (alone or in conjunction with others) to Control the Disposition of Account Assets by Direct Communication or Otherwise
 - Directors and Officers of Foreign Entities with Power Under Local Law (E.g., Mexican S.R.L.)



Form TD F 90-22.1 “FBAR” (31 USC 5314 – Bank Secrecy Act)

- 6-Year Statute of Limitations from Due Date
- Due June 30 (Must be Received) – No Extension
- Penalties
 - \$10,000 Civil Penalty for Non-Willful for Each Account
 - Reasonable Cause
 - Greater of \$100,000 or 50% of Account for Willful
 - Criminal Penalties (5 Year, \$250,000)
- Marking “No” to Schedule B Question – Willful?



Form TD F 90-22.1 “FBAR” (31 USC 5314 – Bank Secrecy Act)

- Assessment and Collection
 - Not Title 26 Assessment
 - Assessment During Exam or by Notice
 - 30 Days to File Protest to Argue in Appeals
 - IRS Cannot Utilize Title 26 Enforced Collection Methods (Levy, Lien)
 - IRS Must File Action in District Court for Judgment
 - Taxpayer May Contest Validity of Penalty in Court
 - See I.R.M. 4.26.17 for IRS Enforcement Procedure



Form TD F 90-22.1 “FBAR” (31 USC 5314 – Bank Secrecy Act)

- Record Keeping
 - Must Maintain Records (Statements) for Five Years from Date FBAR Due
 - \$10,000 Penalty



Form 5471 for Foreign Corporations (Sections 6038 and 6046)

- Primary Purposes of Form:
 - Disclosure of Foreign Assets
 - § 482 and Transfer Pricing for Related Party Transactions
 - CFC Determination and Inclusion of Subpart F Income (Deemed Dividend from CFC)



Form 5471 for Foreign Corporations (Sections 6038 and 6046)

- Filing Required by:
 - US Officers/Directors Where US Person Acquires $\geq 10\%$ (vote/value) of Stock in One or More Transactions (creeping acquisitions), or an Additional 10% or More of Stock
 - Category 2
 - US Person Who: (i) Acquires $\geq 10\%$; (ii) Disposes of Stock Dropping Interest Below 10%; or (iii) Becomes US Person While Owning $\geq 10\%$ (substantial presence; green card)
 - Category 3
 - US Person in Control ($>50\%$ vote/value) of Foreign Corporation
 - Category 4
 - “US Shareholder” (Owns $\geq 10\%$) of a CFC
 - Category 5

=>Treaty Nonresident Position Does Not Excuse Filing – Still US Person



Form 5471 for Foreign Corporations (Sections 6038 and 6046)

- Complex Ownership Attribution Rules (§§ 267, 318)
- Category of Filer Determines Information That Must Be Reported (schedules)
- Multiple Filer Exception: One Person may file Form 5471 (and applicable schedules) for Other Persons Having Same Filing Requirements and Must Identify Such Other Persons; Identified Persons Must Attach a Statement to Their Income Tax Return



Form 5471 for Foreign Corporations (Sections 6038 and 6046)

- 5471 Must Be Attached to Filer's Timely Filed Tax Return
- Over-Reporting, Under-Reporting and "Substantially Incomplete" Form – CCA 200429007
- Penalties
 - \$10,000 Penalty for Each Foreign Corporation Not Reported; Reasonable Cause
 - FTC Calculation: Foreign Taxes Deemed Paid Reduced by 10%
 - Potential Criminal Penalties



Form 5472 for Domestic Reporting Corporation (Sections 6038A and 6038C)

- Primary Purpose of Form
 - Report Related Party Transactions
 - §482 and Transfer Pricing



Form 5472 for Domestic Reporting Corporation (Sections 6038A and 6038C)

- Reporting Corporation
 - 25% Foreign-Owned U.S. Corporation (direct/indirect/constructive)
 - Foreign Corporation Engaged in a U.S. Trade or Business (net election?)
- Must Report Related Party Transactions
 - Includes Accrued Amounts, e.g., Interest
 - Reasonable Estimates – At Least 75% and Not More Than 125%



Form 5472 for Domestic Reporting Corporation (Sections 6038A and 6038C)

- 5472 Must Be Attached to Filer's Timely Filed Tax Return
- Over-Reporting and "Substantially Incomplete" Form – CCA 200429007
- Penalties
 - \$10,000 Penalty for Failure to File
 - \$10,000 Penalty for Failure to Maintain Records
 - Potential Criminal Penalties



Form 926 Transfers to Foreign Corporations (Sections 6038B and 367)

- Primary Purpose of Form
 - Disclosure of Foreign Assets
 - § 367(a) Outbound Property Transfers
 - §367(d) Outbound Intangible Transfers



Form 926 Transfers to Foreign Corporations (Sections 6038B and 367)

- Transfers of Tangible and Intangible Property
 - Cash Transfers
 - Directly or Indirectly Holds $\geq 10\%$ Vote/Value After the Transfer
 - \$100,000 Transferred in Previous 12 Months
 - Tangible and Intangible Property Transfers



Form 926 Transfers to Foreign Corporations (Sections 6038B and 367)

- Form 926 Must Be Attached to Filer's Timely Filed Tax Return for Year of Transfer
- Penalties
 - 10% of FMV of Property at Time of Transfer
 - Limit of \$100,000 Unless Failure Due to Intentional Disregard



Form 8865 for Foreign Partnerships (Sections 6038, 6038B and 6046A)

- Primary Purpose of Form
 - Disclosure of Foreign Assets
 - Proper Inclusion of Distributive Share



Form 8865 for Foreign Partnerships (Sections 6038, 6038B and 6046A)

- Filing Required by:
 - US Person Who “Controls” Foreign Partnership (>50% Interest in Capital, Profits, or Deductions/Losses)
 - US Person Who Owned $\geq 10\%$ Interest While Partnership “Controlled” by US Persons Owning $\geq 10\%$ Interest
 - US Person Who Contributes Property to Partnership and: (i) Owns $\geq 10\%$ Interest After the Transfer; or (ii) Contribution of > \$100,000 in 12 Months
 - US Person with “Reportable Event”
 - US Person: (i) Acquired Direct $\geq 10\%$ Interest (creeping); or (ii) Interest Increased by 10% (additional acquisition; redemption of another)
 - US Person Disposition: (i) Interest Decreased Below 10%; or (ii) Interest Decreased by $\geq 10\%$

=>Treaty Nonresident Position Does Not Excuse Filing – Still US Person



Form 8865 for Foreign Partnerships (Sections 6038, 6038B and 6046A)

- Complex Ownership Attribution Rules
- Category of Filer Determines Information That Must Be Reported (schedules); If Partnership Files Form 1065, Filer May Attach Form 1065 In Lieu of Schedules
- Multiple Filer Exceptions, With Statements for Non-Filers
- Form 8865 Must Be Attached to Filer's Timely Filed Tax Return



Form 8865 for Foreign Partnerships (Sections 6038, 6038B and 6046A)

- Over-Reporting and “Substantially Incomplete” Form – CCA 200429007
- Penalties
 - \$10,000 Penalty for Failure to File for Each Partnership
 - 10% of FMV of Contributed Property
 - FTC Calculation: Foreign Taxes Deemed Paid Reduced by 10%
 - Potential Criminal Penalties



Form 8858 for Foreign Disregarded Entities (Sections 6011, 6012, 6031 and 6038)

- Primary Purpose of Form
 - Disclosure of Foreign Assets
 - Related Party Transactions and §482



Form 8858 for Foreign Disregarded Entities (Sections 6011, 6012, 6031 and 6038)

- U.S. Persons That Are “Tax Owners” of Foreign Disregarded Entities (“FDEs”) or That Own Interests in Foreign Tax Owners of FDEs Must File
 - U.S. Persons That Are Tax Owners of FDEs at Any Time During Year
 - U.S. Persons Required to File 5471 (Categories 4 and 5) for CFC That is Tax Owner of FDE
 - U.S. Persons Required to File 8865 (Categories 1 and 2) for Controlled Foreign Partnership That is Tax Owner of FDE



Form 8858 for Foreign Disregarded Entities (Sections 6011, 6012, 6031 and 6038)

- Separate 8858 (and all applicable schedules) Required For Each FDE
- Multiple Filer Exceptions, With Statements for Non-Filers
- 8858 Must Be Attached to Filer's Timely Filed Tax Return
- Penalties
 - \$10,000 Penalty for Failure to File
 - FTC Calculation: Foreign Taxes Deemed Paid Reduced by 10%
 - Potential Criminal Penalties



Form 3520 for Foreign Trusts (Section 6048)

- Filing Required by:
 - Responsible Party for Reporting a “Reportable Event”
 - Creation of Foreign Trust by US Person
 - Transfer of Money or Property to Foreign Trust by US Person
 - Death of US Person if: (i) Decedent Treated as Owner of Foreign Grantor Trust; or (ii) Portion of Foreign Trust Included in Estate
 - Receipt of Foreign Gift
 - US Person Treated as Owner of Foreign Grantor Trust
 - US Person Received Distribution from Foreign Trust (including uncompensated use of trust property – HIRE Act)
 - US Person Who Received Either: (i) Gift of >\$100,000 from Nonresident Alien or Foreign Estate (including related persons); or (ii) Gift of >\$14,165 from Foreign Corporations or Foreign Partnerships (including related persons)



Form 3520 for Foreign Trusts (Section 6048)

- Two US Transferors or Grantors of Foreign Trust, or Two US Beneficiaries of Foreign Trust, May Jointly File Form 3520 if They File Joint Income Tax Return
- Schedule B Question
- Form 3520 Filed in Ogden by Due Date of Filer's Income Tax Return



Form 3520 for Foreign Trusts (Section 6048)

- Penalties for Non-Filing or Incomplete Filing Equal to Greater of:
 - Creation or Transfers to Foreign Trust: Greater of \$10,000, or 35% of Gross Value of Property Transferred to Foreign Trust
 - Distributions: Greater of \$10,000, or 35% of Gross Value of Distribution
 - Grantor/Owner: Greater of \$10,000, or 5% of Gross Value of Trust Assets Treated as Owned by US Person
 - Gifts: Greater of \$10,000, or 5% of Amount of Gift for Each Month Failure Continues, not to Exceed 25%



Form 3520-A for Foreign Trusts (Section 6048(b))

- Filed by Foreign Trust with US Owner
 - Technically Obligation of Trustee
 - Foreign Trustees Do Not Comply; Issue for US Grantor/Owner
 - Procedure for U.S. Grantor for File 3520-A



Form 3520-A for Foreign Trusts (Section 6048(b))

- 3520-A Filed in Ogden by 15th Day of Third Month After Trust's Tax Year End (March 15)
 - Foreign Grantor Trust Owner Statement Provided to US Grantor/Owner (to be filed with Form 3520)
 - Foreign Grantor Trust Beneficiary Statement Provided to US Beneficiary (to be filed with Form 3520)
- Penalties for Non-Filing or Incomplete Filing Equal to Greater of:
 - \$10,000, or
 - 5% of Gross Value of Trust Assets Treated as Owned by US Person



Form 8938 for Foreign Financial Assets (New Section 6038D)

- Filed by US Individual Holding Interest in Specified Foreign Financial Assets With Aggregate Value > \$50,000
- Accounts, Stock/Security, Other Instruments/Contracts, Entity Interests
- Draft Instructions Released September 28, 2011
- Notice 2011-55 – Deferred Reporting Requirement
 - Likely 2012 Filing, and Must Include 2011 Information
- 8938 Must Be Attached to Filer's Timely Filed Tax Return
- Penalty of \$10,000



Addressing Noncompliance

- Reasonable Cause Defense – Advisor Generally Must Fall on Sword
- 5471 and Newly Formed Foreign Corporations Unqualified Right to Receive Stock? Property Transferred?
- Form 3520 and Agency Position Mexican Fideicomiso Residential Real Estate Trust
- “Quiet” Disclosures – Pros/Cons

