

Offshore Tax Enforcement 2013

International Tax Compliance and Reporting Issues



Scott D. Michel
Caplin & Drysdale
Washington, DC

INSIDE: TOP THEME PARKS | ARTY LONDON | ASIAN HOTELS TAKE ON EUROPE

SILVERKRIS

THE TRAVEL MAGAZINE OF SINGAPORE AIRLINES

Introduction

March 2010

Singapore Air – New Non-
Stops T/F Zurich

Coincidence?

13 experiences
in new zurich

SINGAPORE AIRLINES
LAUNCHES A380 FLIGHTS TO
THE HEART OF SWITZERLAND

tamil nadu's
chic and sexy side

MAR 10

A STAR ALLIANCE MEMBER

Who Has Money Abroad?

- Historical reasons
- War and persecution
- Families with international presence
- Americans living overseas for a time
- American business interests
- Inheritance, gifts
- Diversification
- Tax Cheats...

Reporting Requirements

- 1040
 - Investment Income
 - Schedule B – check the box, list the country, 2011 new FBAR question
 - Form 8938 – beginning in 2011; SFFAs
- 1041 – Fiduciary income tax return – similar requirements
- Information Returns – 3520/3520A, 5471, 926, etc.
- Estate and gift tax returns
- States
- And the FBAR....

FBAR: What Is It?

- A Treasury Department form implemented pursuant to the Bank Secrecy Act
- Not a tax form, but administered by the IRS
- Data is collected for the Financial Criminal Enforcement Network – “FINCEN”
- Largely used against terrorism, narcotics, money laundering

FBAR: Who Must File?

- Form TD F 90-22.1
 - U.S. individuals and entities must report “financial interest” in offshore “financial accounts” with value of \$10,000 or greater
 - Direct and indirect ownership
 - Must also report signature or other authority over offshore accounts
 - Filed on or before June 30 of the following year; no extensions

2011 FBAR Rule Revisions

- U.S. Resident = Definition for Tax Purposes
 - Includes companies, pass throughs, trusts, etc.
- Signature Authority Filers
 - Moratorium lifted
 - Applies to corporate employees
 - No exemption for:
 - Custodians of employee benefit plans
 - Employees of U.S. subsidiaries of foreign parents
 - Employees of foreign subs of U.S. parents
 - Employees of U.S. parents who sign on foreign sub accounts
 - Some abbreviated filing procedures
- Cash value annuities and insurance (reportable)

2011 FBAR Rule Revisions

- Trusts
 - Grantor Trusts
 - Beneficiary has greater than 50% interest in income or assets
 - Non-grantor trust beneficiary can rely on FBAR filed by Trustee
 - Does not include purely discretionary beneficiaries
 - Broad anti-abuse provision also included in the regs

Sanctions – Criminal Penalties

- Tax evasion
- Filing false returns
- Conspiracy
- Failure to file FBAR
- Proof of intent, willfulness
- Felonies, usually leading to incarceration
- Generally six year statute of limitations



Sanctions – Civil Penalties -- FBAR

- FBAR -- penalties up to *50% of account balances per year* for willful failure to file
 - Six year SOL
 - Non-willful penalties
 - Need to reduce to judgment
 - Mitigation guidelines for smaller accounts
- Definition of Willfulness
 - *Williams/McBride cases* broaden the test
 - What did the return preparer know?
 - Was the box checked “no”?
 - Badges of fraud – concealment, tax loss, etc.

Sanctions – Civil Penalties – Tax Returns

- Accuracy – 20% of the tax + interest
- Fraud – 75% of the tax + interest
- Failure to File/Failure to Pay
- Understatement due to omission of income from foreign sources – 40% (effective 2011)
- Form 8938 (effective 2011)
 - \$10,000, doubled after notice up to \$50,000/return.

Sanctions – Civil Penalties – Information Returns

- 3520 – 35% of trust transfers, 5% - 25% of gifts
- 3520A – 5 % of the trust value
- 8865 -- \$10,000, doubled after notice, and 10% of property transferred to partnership up to \$100,000
- 926 -- 10% of property transferred to foreign corporation up to 100K, unlimited if intentional
- 5271 -- \$10,000 per CFC, could be doubled upon notice and demand
- Others....

War on Foreign Accounts – 2007-2012

- Whistleblowers -- LGT, Birkenfeld (\$104MM US), others
- Criminal Investigations
 - Banks – UBS, Wegelin, Israel, Bank Frey, ZKB, CS...
 - Account holders – UBS, HSBC, CS, Bank Frei, others
 - Enablers – bankers, financial advisors, trustees, fiduciaries, lawyers, return preparers
- Continuing Investigations
 - Switzerland – global settlement or not?
 - Liechtenstein, Israel
 - Asia – new CID presence, Korean SCIP

War on Foreign Accounts – 2007-2012

- Civil Proceedings
 - John Doe Summons – UBS, HSBC (India), First Data
 - US presence necessary
 - IRS forbearance?
 - 2013 – correspondent accounts
 - Audits – UBS 4450, others
 - Global High Net Worth Initiative
 - Forfeiture Actions – US correspondent accounts
- Congressional Actions
 - Hearings, HSBC Report -- 2012

War on Foreign Accounts – 2007-2012

- Information Exchange
 - Switzerland – expanded to “tax evasion,” allowance of “group requests,” conformity to OECD standard
 - Liechtenstein – 2009 TIEA, 2012 one year broadening
 - Reach to banks w/no US presence
- Mining of OVDI Data
 - Intake information
 - Follow up interviews
 - Use of information in Credit Suisse, LLB requests
 - More to come

Foreign Account Tax Compliance Act (“FATCA”)

- Many components:
 - Increased disclosure of beneficial owners
 - Form 8938, extended statute of limitations, provisions related to foreign trusts, etc
- Core Aspect – a new automatic information exchange mechanisms for US account holders at foreign financial institutions worldwide
 - Covers foreign non-financial institutions in some instances as well

Disclose or 30% Withholding

- Basic operation of FATCA
 - Foreign Financial Institutions (“FFI”) or its local government must enter into a FATCA disclosure agreement with the IRS
- OR
- IRS will withhold 30% of ALL U.S. source income and gross proceeds going to the FFI

Reporting and Withholding Provisions

- The FATCA agreement will provide that to avoid the 30% withholding, the FFI must:
 - Obtain “necessary” info from an account holder to determine which accounts are U.S. accounts
 - Comply with to be specified verification and due diligence procedures for identifying U.S. accounts
 - *Comply with IRS requests “for additional information” regarding any U.S. account at the FFI*
 - Obtain waivers from account holders of any rights under domestic bank secrecy laws
 - Or else, to close the account

Reporting and Withholding Provisions

- For any U.S. account at the FFI, the agreement requires reporting of:
 - Name, address, and TIN of each U.S. account holder
 - For accounts held by a U.S.-owned foreign entity, the name address, and TIN of each “substantial U.S. owner of such entity”
 - The account number
 - The account balance or value, and
 - The gross receipts and gross withdrawals or payments from the account
- Like an IRS Form 1099

Implementation

- Effective 2014 for 2013 information (more or less)
- Multiple rounds of technical guidance
 - Significant compliance burden
 - Final regulations (Jan. 2013): 500+ pages
 - Build on IGAs that foster international cooperation;
 - Phase in the timelines for due diligence, reporting and withholding and align them with IGAs;
 - Expand and clarify the scope of payments not subject to withholding;
 - Refine and clarify the treatment of investment entities; and
 - Clarify the compliance and verification obligations of FFIs.

Implementation

- Intergovernmental Agreement (IGA)
 - Model I (A, B): Government-to-government approach.
 - U.K., Denmark, Mexico, and Ireland have signed Model 1A.
 - Model II: Business-to-government approach.
 - Switzerland (and Japan expected)
- Use of data?
 - Matching with 8938s
 - Soft inquiries re prior years
 - Basis for treaty requests
- IRS created new branch 8

Singapore

- Perception in US law enforcement of significant flow of funds from Switzerland
- Endorsed the OECD's standard for EOI for tax purposes
- White listed since 2009
- FATCA and Asset Management Companies
 - Singapore has initiated discussion with the U.S.
- Active in Treaty Negotiations.....US?

Hong Kong

- Use of Hong Kong entities, bank branches of interest to US
 - Chon case – use of HK company and accounts
 - Other Swiss cases w/HK connection
- Has adopted global standard on Exchange of Information
 - Only allows EOI clause as part of a DTA
 - TIEA vs. DTA...leverage to get DTAs, or concern that it remains perceived as a “haven”
 - No known activities on FATCA IGA.

Voluntary Disclosure Program

- Per longstanding IRS policy:
 - Legal source income
 - Timely – disclosure before IRS has info regarding taxpayer
 - Truthful and complete
 - Full cooperation
 - Good faith arrangements to pay

Voluntary Disclosure Program

- 1040s, FBARs
- Also applies to estate tax returns
 - Eliminates criminal exposure for fiduciaries or beneficiaries
- Other forms as well – 3520s, 5471s, etc.
- Generally six year look back driven by criminal SOL
 - There are exceptions...

2012 Offshore Voluntary Disclosure Initiative (“OVDI”) Round Three

- Prior Programs – 2009, 2011
 - Changes in process, increases in penalties
- Eight Years of filings
- CID Preclearance
 - Leumi “revocations”
- Intake Process –letter, detailed attachment
- Eligibility issues
 - 18 USC 3506
 - Possible announced cut offs for specific banks, etc.
- No deadline – could change anytime

2012 OVDI: Financial Aspects

- Tax on Investment Income
 - PFIC Mark to Market Regime in place
- 20% Accuracy Related Penalty
- Interest
- 27.5% of Highest Value of Offshore Assets
 - Financial Assets
 - *Non-financial Assets connected to non-compliance*
- 12.5% penalty -- < 75K USD
- 5% penalty – inherited/gifted, unused, no evidence of concealment, certain longtime non-residents

Longtime Non-Residents

- OVDI 5% Safe Harbor
 - Minimal tax, compliance in home country
 - Special 5% OVDI safe harbor
 - Reside outside US, less than 10K in US source income
 - Compliance in Home Country, including reporting of foreign account income
- OVDI – Retirement Plans, RRSPs (Canada)
- Non-OVDI – new program effective 9/1/12
 - Low compliance risks -- \$1500/year tax presumption
 - 3 years of 1040s, 6 years of FBARs
 - Reasonable cause statement

OVDI: Issues

- “It’s not my money” (or only some of it is)
- Domestic Disclosures w/offshore issues
- Opt Outs – one size does not fit all....
 - Anecdotal experience
 - Initial submissions, Committee
 - Audit? FBAR Penalty Collection Suit?
- Role of Non-Program (“Quiet”) Disclosures
 - Not everyone needs criminal protection
- Follow up interviews
- Relationship to Enforcement – “iron fist/velvet glove”

Another Option?

- Retrospective Cleanup v. Prospective Compliance
 - No obligation to go back
 - BUT...must advise to comply going forward
 - Another vehicle for IRS to learn that account was held in prior years
 - Will a first time FBAR ping the system?
 - \$ Threshold?
 - Trusts, CFCs...

Aggressive Enforcement Will Continue

- Whistleblowers and informants
- Criminal Investigation of banks and bankers
 - Follow Up Activity from OVDI
- Audits and Civil summons process
- Treaty based information exchange
- Administrative (FBAR)
- Legislative (FATCA)

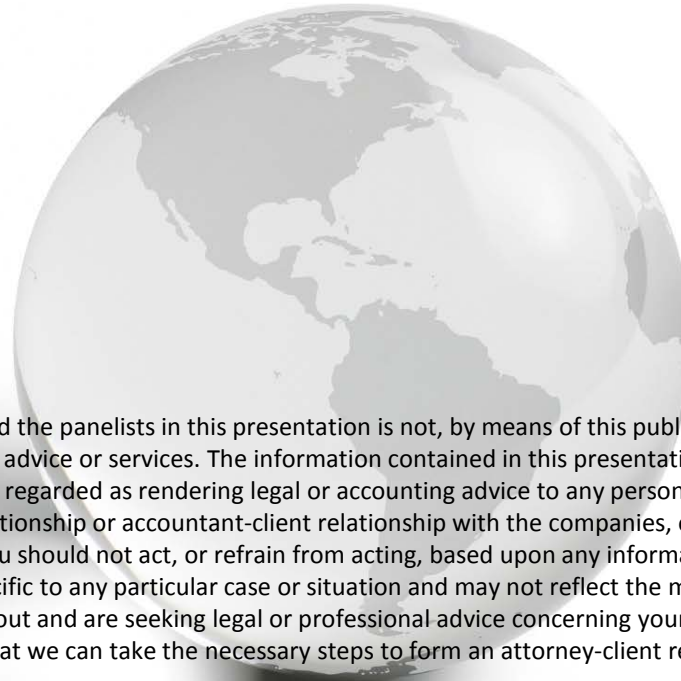
The Future

- Automatic Information Exchange -- beginning in 2014
- Continued Enforcement Activity Worldwide
 - Criminal
 - Civil
- Continued Erosion of Bank Secrecy – Bilateral Agreements
- A “New World Order” of Transparency?
 - Fiscal protection is enough of a reason

Thank You

Scott D. Michel
Caplin & Drysdale
One Thomas Circle NW
Suite 1100
Washington, DC 20005

+ 1 202-862-5030
smichel@capdale.com



This publication contains general information only and the panelists in this presentation is not, by means of this publication, rendering accounting, business, financial, investment, legal, tax, or other professional advice or services. The information contained in this presentation provides background information about certain legal and accounting issues and should not be regarded as rendering legal or accounting advice to any person or entity. As such, the information is not privileged and does not create an attorney-client relationship or accountant-client relationship with the companies, or any of its employees. This presentation does not constitute an offer to represent you, and you should not act, or refrain from acting, based upon any information so provided. In addition, the information contained in this presentation is not specific to any particular case or situation and may not reflect the most current legal developments, verdicts, or settlements. In the event that you have questions about and are seeking legal or professional advice concerning your particular situation in light of the matters discussed in the presentation, please contact us so that we can take the necessary steps to form an attorney-client relationship or professional-client relationship if that is warranted.