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2009 – A year of Increased Focus on International Tax Reporting

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CHAPTER 3 2009—A Year of Increased Focus on International Tax Reporting

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§ 3.01 INTRODUCTION

The Internal Revenue Service ("IRS") and the Treasury Department require the reporting of detailed information concerning a broad array of foreign transactions. These reports and forms enable the IRS to obtain information that is useful for tax, regulatory and investigative purposes. The year 2009 saw increased attention to these forms from the IRS, the judiciary, the legislature, President Obama and the press. This article discusses these developments and considers what may happen in this evolving area in the future.

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68-3 New York University Annual Institute on Federal Taxation § 3.02

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§ 3.02 IRS

[1] Form TD F 90.22-1, Report of Foreign Bank and Financial Account (FBAR)

During the last two years, the FBAR has received a great deal of publicity as the result of the investigation of UBS, UBS bankers and United States persons who own or control undeclared foreign accounts at UBS and other foreign banks. The statutory framework governing FBARs is not contained in Title 26 (Internal Revenue Code), but rather in Title 31 (Money and Finance) of the United States Code,[1] Under regulations promulgated under *31 U.S.C. § 5314*, 31 C.F.R. § 103.24, a "United States person" must file an FBAR if she had a financial interest in or signature authority, or other authority over any financial account in a foreign country, if the aggregate value of these accounts exceeds $10,000 at any time during the calendar year.[2] The FBAR is not filed with individual or corporate income tax returns. It is filed separately and must be filed no later than June 30 of the year following the year for which the report is made.[3]

In October 2008 the FBAR and its instructions were substantially revised by the IRS.[4] For FBAR purposes the term "United States person" is defined as a U.S. citizen or resident, a person in and doing business in the United States (including those filing Form 1040NR), a domestic corporation, domestic partnership, domestic estate or domestic trust.[5] The FBAR instructions also define the terms "financial account," "financial interest," and "signature or other authority" over an account.

There was an outcry from tax practitioners and various taxpayers and taxpayer representative groups regarding the revised form and its many undefined and newly defined terms. During 2009 the IRS extended the date for filing FBAR's for the year 2008 with respect to certain categories of persons.[6] Then because of uncertainty regarding the obligation to file an FBAR with respect to persons who have no financial interest in but have signature authority over a foreign financial account in which the assets are invested in commingled funds (*e.g.*, certain foreign hedge funds), the IRS announced that the filing date for the year 2008 for these entities would be extended to June 30, 2010.[7] The IRS has not yet announced the anticipated guidance for this question.

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[1] Unless otherwise stated, all references to "Section" § or "IRC" are to the Internal Revenue Code of 1986 ("the Code"), and all references to "Treas. Reg. §" are to the Treasury Regulations promulgated thereunder ("the Regulations").

[2] 31 C.F.R. §§ 103.11 to 103.30 (2010).

[3] TD F. 90-22.1, General Instructions, "Who Must File this Report." The FBAR should not be filed with the account-holder's federal income tax return, but should be mailed to the Department of the Treasury, P.O. Box 32621, Detroit MI 44832-0621. *Id.*, Filing Information, "When and Where to File." "The FBAR is considered filed when it is received in Detroit, not when it is postmarked." IRM 4.26.16.3.7 (7/1/08).

[4] For a detailed discussion of these changes see Fletcher and Krebs, *By the Numbers—Coping with International Tax Reporting for International Matters*, 67-15 New York University Institute on Federal Taxation (Matthew Bender 2009).

[5] Announcement 2009-51, I.R.B. 2009-25.

[6] Notice 2009-62, 2009-35, I.R.B. 260.

[7] Id.

The willful failure to file an FBAR or to retain records of a foreign financial account is punishable by a term of imprisonment of up to five years, a criminal fine of up to $250,000 or both.[8] The criminal penalties are enhanced if the violation occurs while violating another law of the United States or if the violation was part of a pattern of any illegal activity involving more than $100,000 in a 12-month period. The enhanced criminal penalties are a term of imprisonment of up to 10 years, a maximum criminal fine of $500,000, or both.[9] A person who willfully submits a false FBAR can be charged under the false statement statute, *18 USC § 1001*, which carries a maximum term of imprisonment of five years, a maximum fine of $250,000 ($500,000 for a corporation), or both.

The applicable civil penalties for FBAR violations are substantial and complex. The civil penalty for a violation of the FBAR statute was increased in 2004.[10] There are civil penalties for negligence, pattern of negligence, non-willful and willful violations. The statutory change with respect to willful violations dramatically increased the potential liability. The statute permits a maximum civil penalty for a willful failure to file an FBAR equal to $100,000 or 50% of the balance in the account at the time of the violation, whichever is greater. Thus, if that maximum civil penalty were applied for two or more years, the total amount of the penalty assessed could equal or exceed the value of the account.[11]

[2] IRS Voluntary Disclosure Program

The IRS has had a long standing practice regarding the voluntary disclosure of unreported income, which is set forth in the Internal Revenue Manual ("IRM").[12] In general, it is the IRS' practice to favorably consider a voluntary disclosure in determining whether to recommend criminal prosecution.[13] The IRM states that a voluntary disclosure will not automatically grant immunity from prosecution, but it may result in prosecution not being recommended.[14] A voluntary disclosure may not be made if the unreported income has an illegal source.[15] A qualified voluntary disclosure is one that is truthful, timely and complete.[16] It also requires full cooperation with the IRS in providing information and arranging for the payment of additional tax, interest and penalties.

On March 23, 2009, the IRS disclosed a memorandum setting forth a settlement initiative for a six month period with respect to taxpayers who wished to make a voluntary disclosure involving an offshore account.[17] Under the settlement initiative the taxpayer was required to pay any additional income tax for the previous six years, interest and a 20% accuracy penalty. In addition, the taxpayer, in lieu of all other civil penalties, including the FBAR penalty, was required to pay a penalty equal to 20% of the highest aggregate value of the account during the previous six years. While this was not an insubstantial penalty to pay, it was far less that the potential penalties that could have been imposed by the IRS.[18] The

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[8] 31 U.S.C. § 5322(a).

[9] 31 U.S.C. § 5322(b).

[10] 31 U.S.C. § 5321(a)(5).

[11] *See* Lawrence S. Feld, Esq, Undeclared Foreign Accounts, Tax Fraud and The UBS Prosecutions: Is a Voluntary Disclosure to the IRS the Right Approach, 50 *Tax Management Memorandum* 227, for a definitive article discussing the FBAR and related issues.

[12] Internal Revenue Manual, Sec. 9.5.11.9 Tax Crimes—General.

[13] Id. at Part (1).

[14] Id. at Part (2).

[15] Id.

[16] Id. at Part (3).

[17] *See* Memorandum from Linda E. Stiff, Deputy Commissioner for Services and Enforcement Division, Department of Treasury to Commissioner, Large and Mid-Size Business Division from, (Mar. 23, 2009).

[18] For a list of the various penalties that could be imposed by the IRS in connection with failing to file these forms, see IRS Voluntary Disclosure, Questions and Answers, Q&A 15, posted at http://www.irs.gov/newsroom/article/0,,id=210027,00.html (initially posted by the IRS on May 9, 2009, as modified by the IRS on June 24, 2009, July 31, 2009, August 25, 2009, September 21, 2009, and January 8, 2010).

deadline for the settlement initiative, which was scheduled to end on September 23, 2009, was extended by the IRS to October 15, 2009.[19] According to the IRS, 14,700 taxpayers came forward under the Voluntary Disclosure Program.[20] These cases are now in various stages of review.

While a voluntary disclosure involving an offshore account may still be made after October 15, 2009, the terms of the pre-October 16, 2009 settlement initiative will not apply.[21] Whether the IRS will issue a similar settlement initiative or guidance for post-October 15, 2009 voluntary disclosures remains to be seen.

[3] Form 926, Return by a U.S. Transferor of Property to a Foreign Corporation

A United States person is required to file Form 926 with its income tax returns to report certain transfers of property to foreign corporations.[22] On February 14, 2009, the IRS redesigned the Form 926, "Return by a U.S. Transferor of Property to a Foreign Corporation".[23] The revised Form 926 includes a new section, Part III, which requires the completion of a schedule detailing the type of property transferred, date of transfer, the fair market value, cost or other basis and any gain recognized.[24] Additionally, Form 926 includes Part IV, "Additional Information Regarding the Transfer of Property".[25] This part has been expanded to include several questions to provide additional information the IRS such as; (1) the U.S. transferor's ownership of the foreign transferee before and after the transaction; (2) gain recognition under select sections of the Code; and (3) recapture amounts under Section 1503(d), and 4) exchange gain.[26] The penalty for failure to file Form 926 is equal to 10 percent of the fair market value of the property at the time of the exchange to a maximum of $100,000.[27]

[4] Form 5471, Information Return of U.S. Persons With Respect To Certain Foreign Corporations

A United States Person[28] is required to file a Form 5471, Information Return of U.S. Persons With Respect To Certain Foreign Corporations, under Section 6038(a) for every foreign corporation that it controls.[29] This reporting requirement is also required for a United States person who acquires at least 10 percent of 1) the total voting power of all the stock of a foreign corporation or 2) total value of the stock of a foreign corporation. Furthermore, a United States citizen or resident who is an officer or director of a foreign corporation and acquires a 10 percent shareholder interest, in vote or value, will also be required to file a Form 5471.[30]

On October 22, 2008, the IRS announced on its website that it began issuing letters informing taxpayers of a procedural change relating to automatic assessments of penalties.[31] The penalties would apply to taxpayers who fail to timely file

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[19] *Infra* note 8.

[20] IR-2006-116, Prepared Remarks of Commissioner Douglas Shulman before the 22nd Annual George Washington University International Tax Conference (Dec. 10, 2009) http://www.irs.gov/newsroom/article/0,,id=216981,00.html.

[21] Jeremiah Coder, *IRS Expanding Examination of International Banking Centers, Official Says*, ***2009 TNT 231-4***.

[22] I.R.C. § 6038B (2009).

[23] *See* Form 926.

[24] *See* Form 926 (rev. Dec. 2008), Part III.

[25] *See* From 926 (rev. Dec. 2008), Part IV.

[26] Id.

[27] I.R.C. § 6038B(c)(1) (2009).

[28] *See* I.R.C. § 7701(a)(30) (2009).

[29] I.R.C. §§ 6038(e)(2) and (3) (2009).

[30] I.R.C. § 6046(a)(1)-(2) (2009).

[31] "Forms 5471—Automatic Assessment of Penalties under IRC Section 6038(b)(1)," http://www.irs.gov/businesses/corporations/article/0,,id=188039,00.html.

required information returns regarding their interests in foreign corporations starting January 1, 2009.[32] The automatic penalties apply to a failure to file a Form 5471, "Information Return of U.S. Persons with Respect to Certain Foreign Corporations".[33]

The penalty for failure to file is $10,000 for each Form 5471 that is filed after the due date of the income tax return (including extensions) or does not include the complete and accurate information described in Section 6038(a).[34] The penalty can increase if the failure continues after notification.[35] If the failure continues in excess of 90 days after notification, an additional $10,000 will be assessed for each 30-day period after the initial 90 days has expired.[36] The maximum increased penalty is $50,000.[37] Another consequence of a failure to file could be the reduction of the foreign tax credit under Sections 901, 902 and 960.[38]

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[32] Id.

[33] *See* Form 5471.

[34] I.R.C. § 6038(b)(1) (2009).

[35] I.R.C. § 6038(b)(2) (2009).

[36] Id.

[37] Id.

[38] I.R.C. § 6038(c) (2009).

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§ 3.03 THE COURTS

[1] U.S. Courts

On February 18, 2009 the Department of Justice entered into a deferred prosecution agreement ("DPA") with UBS, AG (the "Bank"), the largest Swiss bank, based on a charge of conspiracy to defraud the IRS. As part of the DPA, the Bank admitted that it had assisted U.S. taxpayers in establishing accounts in a manner designed to conceal the taxpayers' ownership or beneficial interest in these accounts. According to the DPA, the Bank, through its employees, created accounts that allowed U.S. taxpayers to evade the reporting requirements of the U.S. through the use of offshore entities that traded in securities and conducted other financial transactions.[39] Under the DPA, the Bank agreed to provide the government with records relating to accounts that were held directly or through beneficial arrangements by U.S. persons.[40] In addition to requiring the Bank to pay $780 million in fines and penalties, the DPA obligated the Bank to terminate its U.S. cross-border business and to close the accounts of U.S. customers.

Prior to the DPA, the U.S. government had filed a motion in the U.S. District Court for the Southern District of Florida to enforce a "John Doe" summons previously issued to and served upon the Bank requesting the Bank to provide the IRS with the identities of U.S. persons having accounts at the Bank. The DPA expressly permitted that litigation to go forward. On August 19, 2009 the Department of Justice, the IRS and the Bank announced that they had entered into a settlement agreement resolving the John Doe summons enforcement action. As a result of the agreement, the IRS said that it would receive information concerning substantially all of the accounts at the Bank in which it was interested when it initiated the John Doe summons against the Bank. The Bank agreed to turn over to the IRS details of 4,450 accounts that were believed to hold undeclared assets of American account-holders. The agreement required the IRS to submit a request for administrative assistance, pursuant to the existing United States-Switzerland Double Taxation Treaty, to the Swiss Federal Tax Administration (SFTA). The SFTA, upon receiving the treaty request, would direct the Bank to notify the designated account-holders that their information is included in the IRS treaty request. The Bank was required to send notices to the affected United States account-holders encouraging them to take advantage of the IRS Voluntary Disclosure Program and to instruct the Bank to send their account information and documentation to the IRS. Receipt of the notice would not, by itself, preclude the account-holder from coming into the IRS under the Voluntary Disclosure Program.

[2] Swiss Courts

As stated above, in August 2009, the Swiss and US government reached an agreement to received information from the Swiss on accounts.[41] Under the agreement, the IRS submitted a treaty request to the Swiss government who would direct

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[39] Id.

[40] Id.

[41] Kristen A. Parillo, *Swiss Court Says Government Cannot Disclose UBS Data on U.S. Client*, 2010 TNT 15-1.

UBS to turn over the requested information on the accounts.[42] On January 21, 2010, the Federal Administrative Court in Switzerland "granted a U.S. UBS client's appeal to prevent the Swiss government from disclosing her account information to U.S. authorities under the August 2009 agreement reached by the Swiss and U.S. governments."[43] The Court held that according to the U.S.-Switzerland income tax treaty, information would be exchanged if the information relates to "tax fraud and the like."[44] The Court stated that, "provided the taxpayer did nothing more than not declare income, an account or return the Form W-9, consequently committing tax evasion under Swiss law, he hasn't acted fraudulently."[45] Additionally, the Court stated the mere failure to file a tax form does not constitute tax even if large sums of money are involved. But the Court stated that if the undeclared account was held in the name of a corporation or other entity to conceal the identity of the owner such evidence could be tax fraud.[46]

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[42] *IRS to Receive Unprecedented Amount of Information in UBS Agreement,* Aug. 19, 2009, http://www.irs.gov/newsroom/article/0,,id=212124,00.html.

[43] Parillo, *Swiss Court*.

[44] Id.

[45] Id.

[46] Id.

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§ 3.04 THE PRESS

It is unusual for the press (particularly the popular press) to cover tax matters, let alone international tax matters. But 2009 seemed to change those rules. In 2009 international tax forms became interesting enough to be covered by both the financial press and to a lesser extent the popular press.[47] Moreover, law firm and accounting firm websites were flooded with client alerts and articles trying to keep up with the developments coming out of the Internal Revenue Service, Congress and the courts on almost a daily basis.[48]

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[47] *See*, for example, *I.R.S. to Ease Penalties for Some Offshore Tax Evaders*, N.Y. TIMES, Mar. 26, 2009; *UBS Client Enters Guilty Plea in Tax Case*, N.Y. TIMES, Sept. 25, 2009; *Will Offshore-Account Holders Surrender?*, WALL STREET JOURNAL, April 8, 2009; *IRS Gets Tougher on Offshore Tax Evaders*, WALL STREET JOURNAL, July 20, 2009; *UBS to Give 4,450 Names to U.S.*, WALL STREET JOURNAL, Aug. 20, 2009; *IRS Touts Its Amnesty, Trains Sights on Evaders*, WALL STREET JOURNAL, Oct. 15, 2009; *Bill Targeting Offshore Tax Evasion is Introduced in Congress*, WALL STREET JOURNAL, Oct. 29, 2009; *IRS Deadline Raises Ante to report foreign accounts*, PALM BEACH DAILY NEWS, Sept. 5, 2009; *IRS amnesty for unreported foreign bank accounts—extended!*, JACKSONVILLE DAILY RECORD, Sept. 28, 2009; *7,500 tax dodgers apply for IRS amnesty program*, BOSTON GLOBE, Oct. 14, 2009; CONGRESS TIGHTENING SCREWS ON TAX CHEATS, FORBES, Oct. 27, 2009.

[48] *See*, for example, *Criteria for Disclosure if Swiss Accounts Announced. Now That Offshore IRS Voluntary Disclosure Program has Ended, What's a Taxpayer to Do?* (Nov. 24, 2009), http://www.duanemorris.com/alerts/IRS_Voluntary_Disclosure_3487.html; *IRS Voluntary Disclosure Update—U.S. Accounts to Be Disclosed Under U.S.-Swiss Settlement Agreement: "Amnesty" for Undisclosed Offshore Accounts Expires September 23, 2009* (Aug. 28, 2009), http://www.duanemorris.com/alerts/irs_voluntary_disclosure.html; *President Obama Calls for Crackdown on International Tax Transactions* (May 7, 2009), http://www.bryancave.com/files/Publication/af661e4c-c7f8-40e8-8b22-2debb2733507/Presentation/PublicationAttachment/6a4ac62e-9025-4e20-849b-b21f96b7a9e8/TaxAlert5-07-09.pdf; *Global Leaders Meet and Draft Tools to Combat International Tax Evasion* (April 17, 2009), http://www.bryancave.com/files/Publication/3eeb90ed-a704-4b76-bce4-812de869cb79/Presentation/PublicationAttachment/9774b66b-d90f-494a-9084-1c72c7d7c9a5/Tax%20Alert4-17-09.pdf; *IRS Announces Voluntary Disclosure Program Affecting U.S. Persons with Offshore Accounts* (Mar. 27, 2009) http://www.duanemorris.com/alerts/alert3195.html; *IRS Announces New Penalty Framework for Qualifying Voluntary Disclosures of Offshore Financial Accounts and Entities* (Mar. 27, 2009), http://www.bryancave.com/files/Publication/50a81cb5-0216-4cc8-a66b-dd8e70bc8312/Presentation/PublicationAttachment/edfd74c2-7956-4e46-b0c9-e34d743f06fc/TaxBulletin3-27-09.pdf; *U.S. Authorities Step Up Efforts to Curb Offshore Tax Evasion; UBS AG Enters Into Deferred Prosecution Agreement Requiring the Release of Client Identities* (Feb. 20, 2009), http://www.bryancave.com/files/Publication/6fabbb60-525f-458a-a9ee-13bdbba561ee/Presentation/PublicationAttachment/64842f82-a049-4b8b-a7d6-15e0f2f979f6/WhiteCollar-TaxBulletin2-20-09.pdf.

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§ 3.05 THE ADMINISTRATION

On May 4, 2009 President Obama made a speech on international tax policy reform.[49] During the speech, President Obama stated that the code allowed for "a small number of individuals and companies to abuse overseas tax havens to avoid paying any taxes at all".[50] The President spoke about the use of money offshore and transfers to tax havens.[51] He encouraged Congress to pass measures requiring overseas banks to disclose information on U.S. clients.[52] He suggested that if the banks do not cooperate, to assume that the bank is sheltering money and act accordingly.[53] In order to ensure that the IRS is able to enforce the laws of the U.S., he asked that the IRS "hire nearly 800 more [ ] agents to detect and pursue American tax evaders abroad."[54]

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[49] Grand Foyer, Remarks by the President on International Tax Policy Reform (May 4, 2009), http://www.whitehouse.gov/the_press_office/Remarks-By-The-President-On-International-Tax-Policy-Reform (last visited Jan. 31, 2010).

[50] Id.

[51] Id.

[52] Id.

[53] Id.

[54] Id.

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§ 3.06 LEGISLATIVE ATTENTION

In response to both the UBS case and President Obama's tax reform speech, Congress has proposed an act that creates a system of reporting information on U.S. persons to the United States. On October 27, 2009, the Foreign Account Tax Compliance Act of 2009 ("FATCA") was introduced in both the House and the Senate.[55] FATCA has the support of the President and it is also included in the President's budget proposals for 2011 ("2011 Greenbook").[56] The President's budget proposal states:

> For too long, some Americans have evaded their taxpaying responsibilities by hiding unreported income in a foreign bank account, trust, or corporation. To reduce such evasion, the Administration is proposing a series of measures to strengthen the information reporting and withholding systems that support U.S. taxation of income earned or held through offshore accounts or entities.

According to the proponents of these changes, strengthening the withholding and reporting rules under which Foreign Financial Institutions ("FFI") operate with respect to U.S. persons will help to ensure that U.S. persons are properly paying tax on income earned through foreign accounts and that proper withholding tax applies with respect to foreign persons. The 2011 Greenbook and FATCA contain several key provisions relating to information reporting requirements with respect to international matters.

[1] Require Increased Information Reporting on Certain Foreign Accounts[57]

Under the 2011 Greenbook and FATCA a withholding agent would withhold tax at a rate of 30 percent on payments to a FFI (including certain entities engaged primarily in the business of investing, reinvesting, or trading in securities, partnership interests, commodities, or any interests in the foregoing) of U.S.-source FDAP income and gross proceeds from the sale of any property of a type which can produce U.S.-source interest or dividends, unless the FFI has entered into an agreement with the IRS. The agreement would require the FFI to identify accounts (including debt and equity securities issued by the FFI that are not regularly traded on an established securities market) held at such FFI or at an FFI in the same expanded affiliated group by specified U.S. persons or by foreign entities in which a specified United States person owns, directly or indirectly, an interest of more than 10 percent (a United States owned foreign entity). The FFI would be required to report the name, address, and taxpayer identification number (TIN) of the U.S. account holder (or each substantial U.S. owner of the United States owned foreign entity account holder), the account balance or value, and the gross receipts and gross withdrawals or payments from the account. Instead of reporting the account balance and the gross receipts and gross withdrawals or payments from the account, a FFI may elect to report such information as such FFI would be required to report under *IRC § 6041*, *§ 6042*, *§ 6045*, and *§ 6049* if such FFI were a United States person and each holder of such accounts that is a specified United States person or a United States owned foreign entity were a natural person and citizen of the United States.

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[55] Foreign Account Tax Compliance Act of 2009, H.R. 3933 111th Cong. (2009) and S. 1934 111th Cong. (2009).

[56] *See* Department of the Treasury, General Explanations of the Administration's Fiscal Year 2011 Revenue Proposals, February 2010.

[57] H.R. 3933 § 101; 2011 Greenbook at 51–53.

This proposal would not apply to a payment if the beneficial owner is a foreign government, an international organization, a foreign central bank, or any other class of persons that the Treasury Department concludes presents a low risk of tax evasion. The Treasury Department would be authorized to issue regulations to implement the purposes of this proposal. The rules would be designed so as not to disrupt ordinary and customary market transactions. Foreign beneficial owners of payments (other than FFIs that do not qualify for the benefits of an income tax treaty with the United States) that are subject to withholding tax in excess of their income tax liability as a result of this proposal would be permitted to apply for a refund of any excess tax withheld.

The proposal would be effective beginning after December 31, 2012.

[2] Require Increased Reporting with Respect to Certain Recipients of FDAP Income or Gross Proceeds[58]

Any withholding agent making a payment of U.S.-source FDAP income and gross proceeds from the sale of any property of a type which can produce U.S.-source interest or dividends to a foreign entity (other than a foreign financial institution) would be required to withhold a tax of 30 percent, unless the foreign entity certifies that no U.S. person owns, directly or indirectly, an interest of more than 10 percent or the foreign entity provides the name, address, and TIN of each such substantial U.S. owner, and the withholding agent does not know or have reason to know that any information provided is incorrect. Exceptions would be provided for payments to publicly traded companies and their subsidiaries, foreign governments, international organizations, foreign central banks, any entity that is organized under the laws of a possession of the United States and that is wholly owned by one or more bona fide residents of such possession, and other classes of person identified by the Secretary, or any class of payment identified by the Secretary, as posing a low risk of tax evasion. The proposal would be effective for payments made after December 31, 2012.

[3] Require Disclosure of Foreign Financial Assets to be Filed with Tax Return[59]

Any U.S. individual who holds an interest in a foreign financial account, an interest in a foreign entity or any financial instrument or contract held for investment and issued by a foreign person would be required to file an information return if the aggregate value of all such assets exceeds $50,000. The information return would set forth the name and address of the financial institution that maintains such account or the issuer of the instrument and the maximum value of the asset during the year. The disclosure would be included as part of the tax return for the taxpayer. Penalties for failing to report the foreign financial asset would be consistent with current penalties under current law for failing to disclose an interest in a foreign entity, such that a failure to report the required information would result in a penalty of $10,000, unless the failure is shown to be due to reasonable cause and not willful neglect. The Secretary would be given regulatory authority to apply the proposal to certain domestic entities formed or availed of for purposes of holding foreign financial assets, and to coordinate the proposal with other information returns required under the Code.

A rebuttable evidentiary presumption would be applicable in a civil administrative or judicial proceeding providing that, if it is established that the individual had an interest in an undisclosed foreign financial asset, then the aggregate value of all foreign financial assets in which a U.S. individual has an interest will be presumed to exceed $50,000. The rebuttable evidentiary presumption would not apply in criminal proceedings.

The tax return disclosure would not replace or mitigate the individual's obligation to separately file an FBAR with the Treasury Department as required under Title 31. The penalties imposed under Title 31 for failing to file an FBAR would continue to apply to a failure to file an FBAR as required under Title 31. Failure to disclose the foreign accounts with the income tax return would not be subject to the Title 31 penalties, although it could give rise to penalties and other consequences imposed under the Code, including extension of the statute of limitations. The proposal would be effective for taxable years beginning after the date of enactment.

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[58] H.R. 3933 § 101; 2011 Greenbook at 54–55.

[59] H.R. 3933 § 201; 2011 Greenbook at 58–59.

[4] Impose Penalties for Underpayments Attributable to Undisclosed Foreign Financial Assets[60]

The 20-percent accuracy-related penalty would apply to any understatement attributable to undisclosed foreign financial assets. In addition, the proposal would double the 20-percent accuracy-related penalty to 40 percent in the case of such foreign financial asset understatements. Undisclosed foreign financial assets would be foreign financial assets that the taxpayer failed to disclose properly under *IRC § 6038*, *§ 6038B*, *§ 6046A*, *§ 6048*, or the proposed requirement that taxpayers disclose foreign financial assets. The penalty would not be imposed when the understatement is due to reasonable cause. The proposal would be effective for taxable years beginning after the date of enactment.

[5] Require Reporting of Certain Transfers of Assets to or from Foreign Financial Accounts[61]

A U.S. individual would be required to report, on the individual's income tax return, any transfer of money or property made to, or receipt of money or property from, any foreign bank, brokerage, or other financial account by the individual. Additionally, any entity of which a U.S. individual owns, directly or indirectly, more than 25 percent of the ownership interest would be required to report any transfer of money or property made to, or receipt of money or property from, any foreign bank, brokerage, or other financial account by the entity. Such an entity would also be required to report the name, address, and taxpayer identification number of any U.S. individual who owns more than 25 percent of the ownership interest in the entity. This reporting requirement would not apply if the cumulative amount or value of transfers, and the cumulative amount or value of receipts that would otherwise be reportable for a given year were each less than $50,000. The Treasury Department would receive regulatory authority to require the reporting of additional information, including classifying transfers and receipts as for investment or for arm's-length payments in the ordinary course of business for services or tangible property, or such other categories as the Secretary may prescribe. Failure to report a covered transfer would result in the imposition of a penalty equal to the lesser of $10,000 per reportable transfer or 10 percent of the cumulative amount or value of the unreported covered transfers. No penalty would be imposed for a failure to report due to reasonable cause. The Treasury Department would receive regulatory authority to issue rules to prevent abuse of the reporting exemptions and to provide exceptions to the reporting requirement. The proposal would be effective for transfers made after December 31, 2012.

[6] Require Third-party Information Reporting Regarding the Transfer of Assets to or from Foreign Financial Accounts and the Establishment of Foreign Financial Accounts[62]

Any U.S. financial institution that during the year transfers to, or receives from, a foreign bank, brokerage, or other financial account money or property with an aggregate value of more than $50,000 on behalf of a U.S. individual, or on behalf of any entity of which a U.S. individual owns, directly or indirectly, more than 25 percent of the ownership interest, would be required to file an information return regarding such transfer or receipt (including, in the case of a transfer by an entity, the name, address, and taxpayer identification number (TIN) of any U.S. individual who owns more than 25 percent of the ownership interest in such entity). Any U.S. financial institution that opens a foreign bank, brokerage, or other financial account on behalf of a U.S. individual, or on behalf of any entity of which a U.S. individual owns, directly or indirectly, more than 25 percent of the ownership interest, would be required to file an information return with the IRS regarding such account, including reporting any amounts of money or property transferred by the financial institution to, or received by it from, such account.

In addition to filing an information return with the Internal Revenue Service, the U.S. financial institution would be required to send a copy of such return to the U.S. individual, or entity, as to which the return is made.

Reporting would not be required where the U.S. financial institution determined the entity making or receiving the transfer was: a publicly traded corporation, or a subsidiary thereof; an organization exempt from tax under section 501; an

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[60] H.R. 3933 § 202; 2011 Greenbook at 60.

[61] H.R. 3933 § 203; 2011 Greenbook at 62.

[62] 2011 Greenbook at 63–64.

individual retirement plan; the United States or any wholly owned agency or instrumentality thereof; any State, the District of Columbia, any possession of the United States, any political subdivision of any of the foregoing, or any wholly owned agency or instrumentality of any one or more of the foregoing; any bank (as defined in section 581); any real estate investment trust (as defined in section 856); any regulated investment company (as defined in section 851); any common trust fund (as defined in section 584(a)); any trust which is exempt from tax under section 664(c) or is described in section 4947(a)(1); or an entity engaged in an active trade or business (other than the business of investing or similar activities).

Failure to file a required information return or to provide a copy of such return to the U.S. individual would result in the imposition of a penalty of $50 with respect to each such failure. In the case of a failure to file due to intentional disregard, the penalty would be the greater of $100 or 5 percent of the amount of the items required to be reported. No penalty would be imposed for a failure to report due to reasonable cause.

The Treasury Department would receive regulatory authority to provide additional exceptions (including where the Secretary determines that the reporting would be duplicative of other reporting requirements), to limit the types of transfers subject to the reporting requirement, to require that certain additional information be reported, and to permit U.S. financial institutions to report additional transfers of money or property to, or from, a foreign bank, brokerage, or other financial account on behalf of a U.S. individual (or on behalf of an entity of which the U.S. individual owns, actually or constructively, more than 25 percent of the ownership interest). The proposal would be effective for amounts transferred and accounts opened beginning after December 31, 2012.

[7] Improve Foreign Trust Reporting Penalty[63]

The penalty provision would be amended to impose an initial penalty of the greater of $10,000 or 35 percent of the gross reportable amount (if the gross reportable amount is known). The additional $10,000 penalty for continued failure to report would remain unchanged. Thus, even if the gross reportable amount is not known, the IRS may impose a $10,000 penalty on a person who fails to report timely or correctly as required, and may impose a $10,000 penalty for each 30-day period (or fraction thereof) that the failure to report continues. If the person subsequently provides enough information for the IRS to determine the gross reportable amount, the total penalties would be capped at that amount and any excess penalty already paid would be refunded. Accordingly, a person can stop the compounding of penalties by cooperating with the IRS so that it can determine the gross reportable amount.

The proposal would be effective for information reports required to be filed after December 31 of the year of enactment.

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[63] H.R. 3933 § 405; 2011 Greenbook at 68.

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§ 3.07 WHAT LIES AHEAD?

Unfortunately neither of the authors has access to a working crystal ball, but if we were betting people (which we are not), we would expect 2010 and beyond to continue to be years of focus on international tax reporting. With the extensive press coverage of the U.S. international tax form requirements in 2009, it will be difficult for U.S. taxpayers and their tax return preparers to continue to plead ignorance in future years with respect to the U.S. tax filing requirements with respect to international accounts, investments and operations. The IRS will begin to process anecdotal information it collects from taxpayers in the Voluntary Disclosure Program and use that information to audit and assert penalties against other taxpayers. By June 30, 2010, the IRS should issue long-awaited FBAR guidance regarding interests in offshore hedge funds. With the hiring and training of 800 new international examiners, taxpayers can expect that international issues will become a much more robust component of an IRS audit. Further cooperation among nations to exchange information on each other's residents will expand and may extend to those nations with which the United States does not even have a formal exchange of information agreement. The UBS case will need to resolve itself, with the likely result that Switzerland will find a way to legally provide the 4,500 promised names to the IRS, notwithstanding the January 2010 Swiss court decision prohibiting same. Legislation will continue to focus on how to raise revenue from taxpayers with offshore operations and investments.

What can we expect in 2010 and beyond in the international tax reporting area? Stay tuned. As the late great Bette Davis once said, "Fasten your seat belts. It's going to be a bumpy night!"[64]

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[64] As Margo Channing in *All About Eve* (1950).