



NEW FOREIGN REPORTING RULES

To pay for the hiring incentives in the recently enacted Hiring Incentives to Restore Employment (HIRE) Act (the “Act”), Congress passed several offsetting revenue raisers, including a comprehensive set of measures to increase offshore reporting compliance by giving the IRS new administrative tools to detect, deter and discourage offshore tax abuses.

A brief overview of the new offshore anti-abuse provisions follows – unless otherwise noted the provisions of the Act take effect on March 18, 2010:

Increased disclosure of beneficial owners

Reporting on certain foreign bank accounts. The Act imposes a 30% withholding tax on income from U.S. financial assets held by a foreign financial institution unless such institution agrees to disclose the identity of any U.S. individuals with accounts at the institution (or the institution's affiliates) and to annually report on the account balance, gross receipts and gross withdrawals/payments from each such account. Foreign financial institutions must also agree to disclose and report on foreign entities that have substantial U.S. owners. Congress expects that foreign financial institutions will comply with these disclosure and reporting requirements in order to avoid paying the 30% withholding tax. ***These provisions are effective generally for payments made after 2012.***

Reporting on owners of foreign corporations, foreign partnerships and foreign trusts. The Act requires foreign entities to provide withholding agents with the name, address and tax identification number of any U.S. individual that is a substantial owner of the foreign entity. Withholding agents will report this information to the Treasury Department. The Act exempts publicly-held and certain other foreign corporations from these reporting requirements and provides the Treasury Department with the regulatory authority to exclude other recipients that pose a low risk of tax evasion. Any withholding agent making a withholdable payment to a foreign entity that does not comply with these disclosure and reporting requirements is required to withhold tax at a rate of 30%. ***These provisions also are effective generally for payments made after 2012.***

Foreign financial asset reporting

Disclosure of information with respect to specified foreign financial assets. The new law requires

individuals, and subject to regulation, certain domestic entities, to report offshore accounts and other foreign financial assets with values of \$50,000 or more on their tax returns. This is in addition to the requirement to file Form TD F 90-22.1 (the FBAR). The financial assets covered are (1) depository or custodial accounts at foreign financial institutions, and (2) to the extent not held in such an account (i) stocks or securities issued by foreign persons, (ii) other financial instruments or contracts held for investment issued by or with a counterparty that is a foreign person, and (iii) any interest in a foreign entity. Individuals who fail to make the required disclosures are subject to a penalty of \$10,000 for the tax year, with an additional penalty if the failure to disclose continues after Treasury notifies an individual by mail of the failure to disclose.

Penalties for underpayments attributable to undisclosed foreign financial assets. Currently the IRS may impose a 20% accuracy related penalty on certain understatements. The Act increases and expands the penalty to 40% of the amount of any understatement that is attributable to an undisclosed foreign financial asset (i.e., any foreign financial asset that a taxpayer is required to disclose and fails to disclose on an information return).

New 6-year limitations period/ suspension of limitation period. For returns filed after March 18, 2010 as well as for any other return for which the assessment period has not yet expired, the Act imposes a new six-year limitations period for omissions of items from a tax return that are attributable to one or more reportable foreign assets and that exceed \$5,000. The Act also clarifies that the statute of limitations does not begin to run until the taxpayer files the information return disclosing the taxpayer's reportable foreign assets or

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interests in passive foreign investment companies (PFICs). The Act extends this new limitation period to the new reporting rules for holders of PFIC interests (see below).

Other disclosure provisions

New reporting rule for PFICs. Activities with respect to PFICs are subject to a new reporting rule. Unless otherwise provided by the IRS, each U.S. person who is a shareholder of a PFIC must file an annual information return containing such information as the IRS may require. A person that meets this new reporting requirement could, however, also have to meet the new reporting rule requiring disclosure of information with respect to foreign financial assets (see above). It is anticipated that the IRS will exercise its regulatory authority to avoid duplicative reporting.

Provisions related to foreign trusts

Presumption with respect to transfers to foreign trusts. The Act provides that if a U.S. person directly or indirectly transfers property to a foreign trust (other than a trust established for deferred compensation or a charitable trust), the IRS will treat the trust as having a U.S. beneficiary unless such person submits information as required by the IRS and demonstrates to the satisfaction of IRS that under the terms of the trust, (1) no part of the trust may be paid or accumulated during the year for the benefit of a U.S. person, and (2) if the trust were terminated during the year, no part of the trust could be paid to a U.S. person.

Minimum penalty with respect to failure to report on certain foreign trusts. Under pre-Act law, a taxpayer that fails to file an information return with respect to certain transactions involving foreign trusts (e.g., the creation of a foreign trust, the transfer of money or property to a foreign trust, or the death of a U.S. owner of a foreign trust) is subject to a penalty of 35% of the amount required to be disclosed on such return. If the IRS uncovers

the existence of an undisclosed foreign trust but is unable to determine the amount required to be disclosed on such return, currently it is unable to impose the penalty. The Act strengthens this penalty by imposing a minimum penalty of \$10,000 on any such failure to file. This provision applies to notices and returns required to be filed after Dec. 31, 2009. Notwithstanding this minimum penalty, in no event may the penalties imposed on taxpayers for failing to file an information return with respect to a foreign trust exceed the amount required to be disclosed on the return.

Dividend equivalent payments

Dividend equivalents treated as dividends. The Act contains a new provision treating a dividend equivalent as a dividend from U.S. sources for certain purposes, including the U.S. withholding tax rules applicable to foreign persons. A dividend equivalent is any substitute dividend made pursuant to a securities lending or a sale-repurchase transaction that (directly or indirectly) is contingent upon, or determined by reference to, the payment of a dividend from sources within the U.S. or any payment made under a specified notional principal contract that directly or indirectly is contingent upon, or determined by reference to, the payment of a dividend from sources within the U.S. A dividend equivalent also includes any other payment that the IRS determines is substantially similar to a payment described in the preceding sentence. Under this rule, for example, the IRS may conclude that payments under certain forward contracts or other financial contracts that reference stock of U.S. corporations are dividend equivalents.

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