SELECTED U.S. TAX COMPLIANCE ISSUES FOR FOREIGN INVESTORS AND BUSINESSES

ESTATE PLANNING COUNCIL OF GREATER MIAMI WORKSHOP
MARCH 16, 2017

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CURRENT COMMON U.S. TAX COMPLIANCE ISSUES

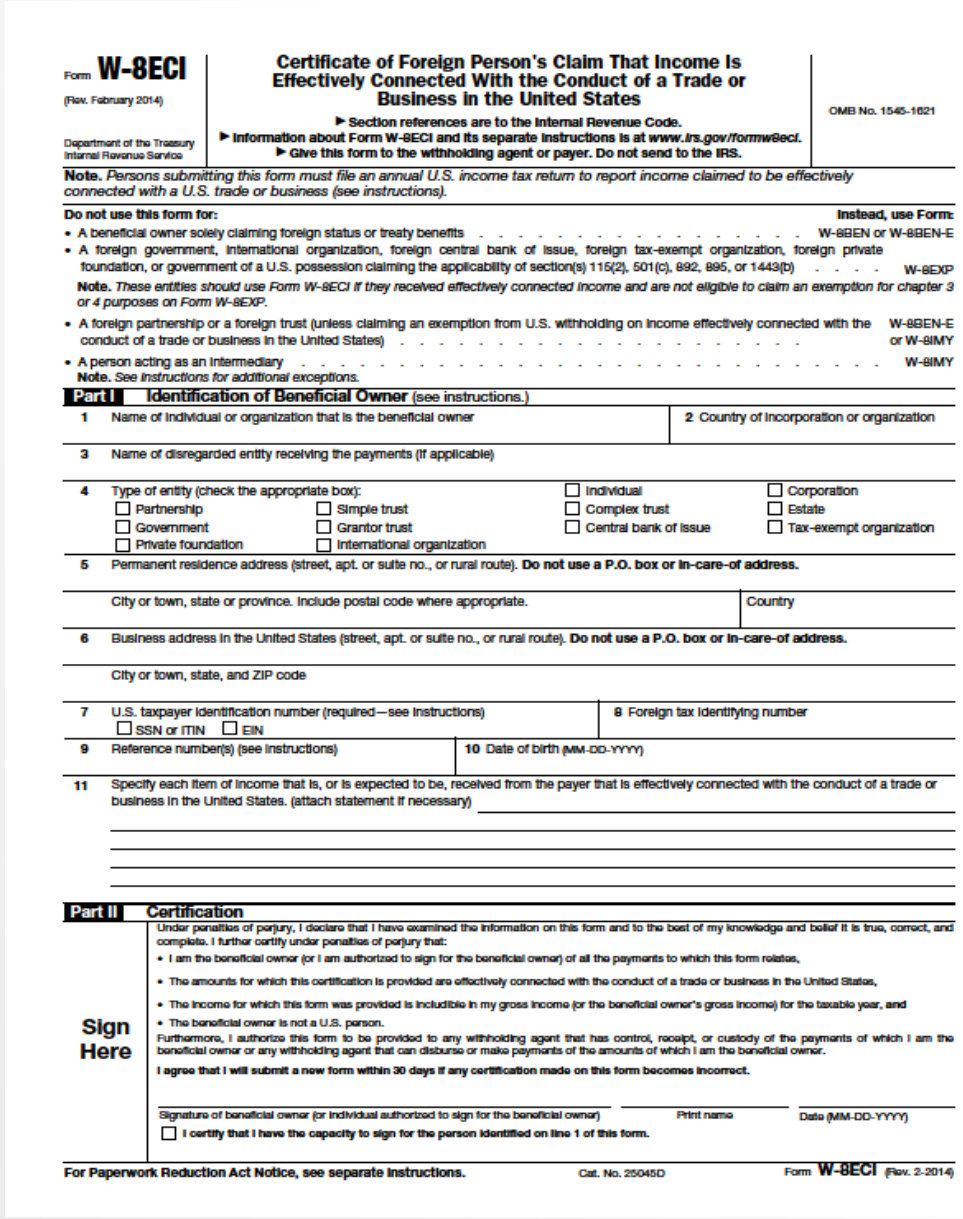
- Rent-free personal use of a U.S. house or condominium unit by foreign members of the UBO's family
- "Borderline" U.S. resident/domiciled individuals, including persons from countries with which the U.S. has an income tax treaty
- Possible U.S. trade or business activities, either through employees or certain agents, without any related filing
- Inbound use of tax treaties to avoid USTB/ECI
- Real estate rental income paid to a foreign lessor
- Partnership business income paid to a foreign partner
- Unreported distributions/loans from foreign trusts
- Unreported or improperly reported/made gifts from foreign persons

RENTING U.S. REAL ESTATE ISN'T NECESSARILY A U.S. BUSINESS ACTIVITY

- In general, if a foreign lessor rents a U.S. house or condominium unit, the rent is subject to a gross 30% "FDAPI" withholding tax, which is due from the "withholding agent"
- The "withholding agent" is the tenant or the broker handling the lease—usually the person who pays the proceeds to the lessor
- If the withholding agent fails to collect the tax and pay it to the IRS, **he/she is liable for the tax and potential related interest and penalties**—see IRC § 1461—an especially big problem for brokers or agents handling multiple properties
- If you represent the withholding agent—your advice should be, "**when in doubt, WITHHOLD**."

RENTING U.S. REAL ESTATE ISN'T NECESSARILY A U.S. BUSINESS ACTIVITY (CONTINUED)

- If the foreign lessor later files Form 1040NR or 1120F and pays the 30% tax (as required), the withholding agent is off the hook, but this doesn't happen very often in practice
- Until the first taxable year that U.S. real estate with a foreign owner produces income (or is sold), related expenses can neither be deducted nor capitalized
- However, once the property produces income, the 30% gross tax on rent can be avoided and expenses claimed through making the "net basis election" under IRC §§ 871(d)/882(d), which can be made in all years thereafter regardless of whether there is additional income
- The lessor must provide the withholding agent with Form W-8 ECI



Form **W-8ECI**

(Rev. February 2014)

Department of the Treasury
Internal Revenue Service

Certificate of Foreign Person's Claim That Income Is Effectively Connected With the Conduct of a Trade or Business in the United States

▶ Section references are to the Internal Revenue Code.
▶ Information about Form W-8ECI and its separate instructions is at www.irs.gov/formw8eci.
▶ Give this form to the withholding agent or payer. Do not send to the IRS.

OMB No. 1545-1621

Note. *Persons submitting this form must file an annual U.S. income tax return to report income claimed to be effectively connected with a U.S. trade or business (see instructions).*

Do not use this form for:	**Instead, use Form:**
• A beneficial owner solely claiming foreign status or treaty benefits	W-8BEN or W-8BEN-E
• A foreign government, international organization, foreign central bank of issue, foreign tax-exempt organization, foreign private foundation, or government of a U.S. possession claiming the applicability of section(s) 115(2), 501(c), 892, 895, or 1443(b)	W-8EXP
Note. *These entities should use Form W-8ECI if they received effectively connected income and are not eligible to claim an exemption for chapter 3 or 4 purposes on Form W-8EXP.*	
• A foreign partnership or a foreign trust (unless claiming an exemption from U.S. withholding on income effectively connected with the conduct of a trade or business in the United States)	W-8BEN-E or W-8IMY
• A person acting as an intermediary	W-8IMY
Note. *See instructions for additional exceptions.*	

Part I Identification of Beneficial Owner (see instructions.)

1 Name of individual or organization that is the beneficial owner

2 Country of incorporation or organization

3 Name of disregarded entity receiving the payments (if applicable)

4 Type of entity (check the appropriate box):
☐ Individual ☐ Corporation
☐ Partnership ☐ Simple trust ☐ Complex trust ☐ Estate
☐ Government ☐ Grantor trust ☐ Central bank of issue ☐ Tax-exempt organization
☐ Private foundation ☐ International organization

5 Permanent residence address (street, apt. or suite no., or rural route). **Do not use a P.O. box or in-care-of address.**

City or town, state or province. Include postal code where appropriate. Country

6 Business address in the United States (street, apt. or suite no., or rural route). **Do not use a P.O. box or in-care-of address.**

City or town, state, and ZIP code

7 U.S. taxpayer identification number (required—see instructions)
☐ SSN or ITIN ☐ EIN

8 Foreign tax identifying number

9 Reference number(s) (see instructions)

10 Date of birth (MM-DD-YYYY)

11 Specify each item of income that is, or is expected to be, received from the payer that is effectively connected with the conduct of a trade or business in the United States. (attach statement if necessary)

Part II Certification

Sign Here

Under penalties of perjury, I declare that I have examined the information on this form and to the best of my knowledge and belief it is true, correct, and complete. I further certify under penalties of perjury that:

- I am the beneficial owner (or I am authorized to sign for the beneficial owner) of all the payments to which this form relates,
- The amounts for which this certification is provided are effectively connected with the conduct of a trade or business in the United States,
- The income for which this form was provided is includible in my gross income (or the beneficial owner's gross income) for the taxable year, and
- The beneficial owner is not a U.S. person.

Furthermore, I authorize this form to be provided to any withholding agent that has control, receipt, or custody of the payments of which I am the beneficial owner or any withholding agent that can disburse or make payments of the amounts of which I am the beneficial owner.

I agree that I will submit a new form within 30 days if any certification made on this form becomes incorrect.

Signature of beneficial owner (or individual authorized to sign for the beneficial owner) Print name Date (MM-DD-YYYY)

☐ **I certify that I have the capacity to sign for the person identified on line 1 of this form.**

For Paperwork Reduction Act Notice, see separate instructions. Cat. No. 25045D Form **W-8ECI** (Rev. 2-2014)

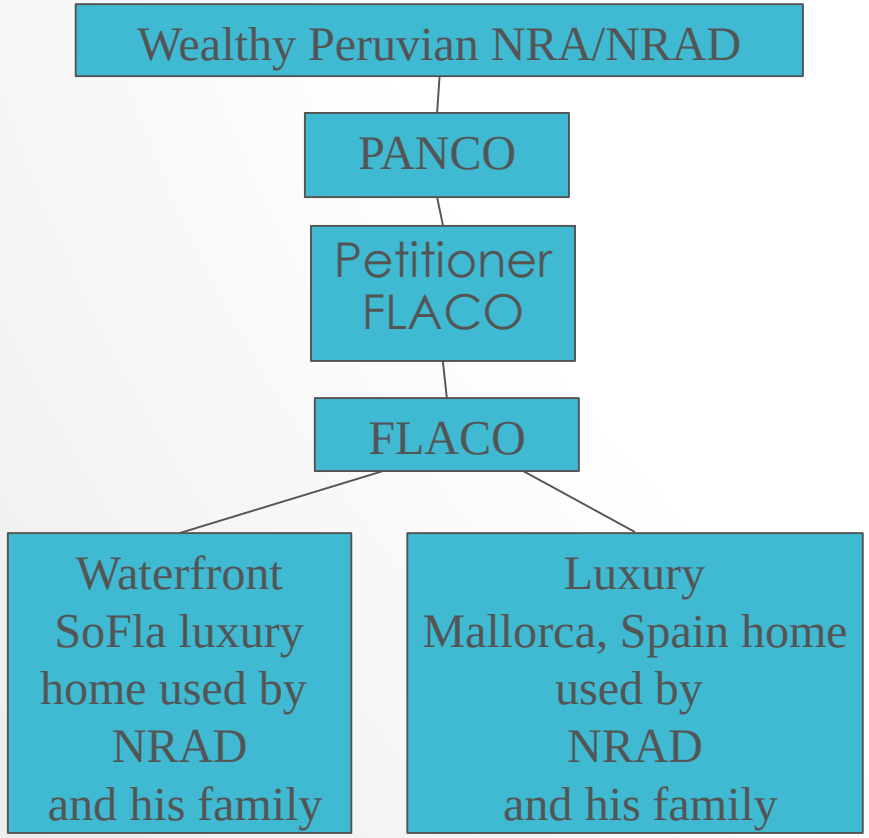
PERSONAL USE OF FOREIGN OWNED U.S. REAL ESTATE

- Tax practitioners have debated for many years whether family members using U.S. residential real estate should pay rent of be allowed to use the property rent-free
- Note that the property will require funding for related expenses—HOA fees, property taxes, landscaping, utilities, etc.—why not provide this with rent?
- Other practitioners and clients for various reasons don't want to file U.S. tax returns under any circumstances until mandated for the taxable year of the property's sale or other disposition
- Bottom-line—very few clients actually had a written lease and paid rent until the G.D. Parker 2012 U.S. Tax Court decision—the rules have now been set

G.D. PARKER INC. V. COMMISSIONER (T.C. 2012)

- A client's common planning question—do I have to pay rent for the use of a residential property owned by my offshore/U.S. holding structure—and if so, how much?
- M. Vanini Investments, Inc. (Vanini), a Florida corporation, owned waterfront luxury homes in both Key Biscayne, Florida and Mallorca, Spain—arguably a strange holding structure
- Vanini's stock was owned by G.D. Parker, Inc. a Florida corporation in turn owned by Vilanova, S.A. (Vilanova), a Panama corporation
- Vilanova was owned by Parker, a Peruvian citizen and resident and an NRA for all relevant U.S. tax purposes
- Parker and his family used both properties rent-free and almost exclusively for their personal use
- Petitioner's return was likely examined because an aggressive CPA suggested sheltering a $7 million capital gain using a technique that was later foreclosed under U.S. Tax law (contributing a built-in loss asset)

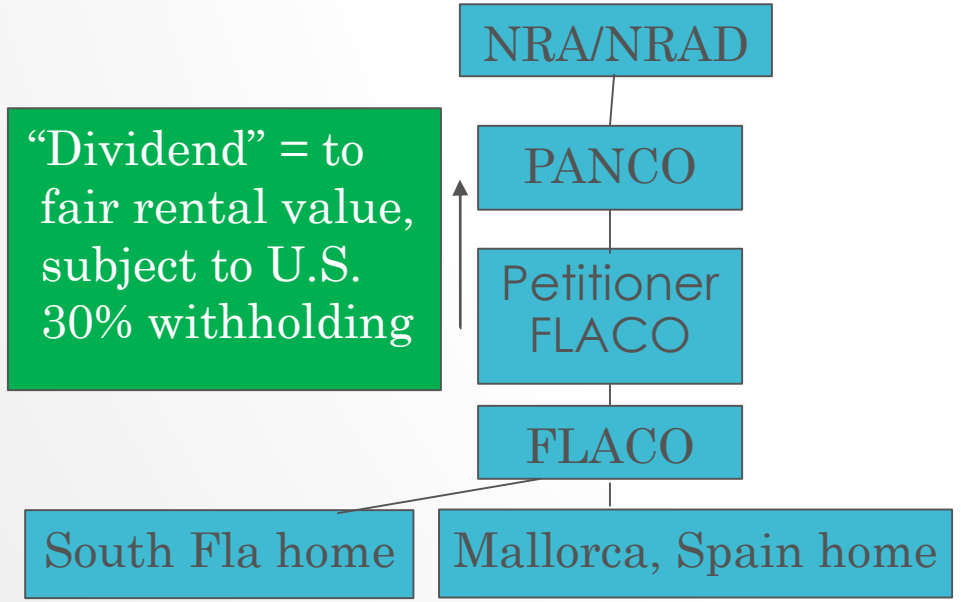
G.D. PARKER INC. V. COMMISSIONER (T.C. 2012)



G.D. PARKER INC. V. COMMISSIONER (T.C. 2012)

- The taxpayer's Federal income tax returns reported "rental income" from the Key Biscayne and Mallorca homes through the "reduction of a loan" from the beneficial owner to the taxpayer, but there was no written evidence of the alleged loan
- The Tax Court held that as the "withholding agent," G.D. Parker, Inc. was liable for the 30% U.S. withholding tax for the rental value of the U.S. and Mallorca properties based upon the "constructive dividends" paid from Vanini "up the corporate chain" to the foreign shareholder
- The court noted that any such "rent" should have been paid to Vanini, the actual owner of the homes, not petitioner—in other words, follow corporate formalities when making payments of income or expenses
- "On the evidence in the record, we do not believe Mr. Parker ever intended to pay rent for his use of the two homes. Rental income was included in petitioner's Federal income tax returns only at the behest of Mr. Parker's accountants. We find that Mr. Parker's rent-free use of the home was a distribution from Vanini to petitioner, followed by a distribution from petitioner to Vilanova, and so on up the chain of corporations to Mr. Parker. "

G.D. PARKER INC. V. COMMISSIONER (T.C. 2012)



Note— the rental value/dividend amount was determined based upon the testimony of the IRS' expert (a licensed appraiser) and not the taxpayer's expert (a real estate broker/sales associate)—use a qualified expert in a tax matter!

THRESHOLD QUESTIONS FOR FOREIGN INVESTORS AND BUSINESSES

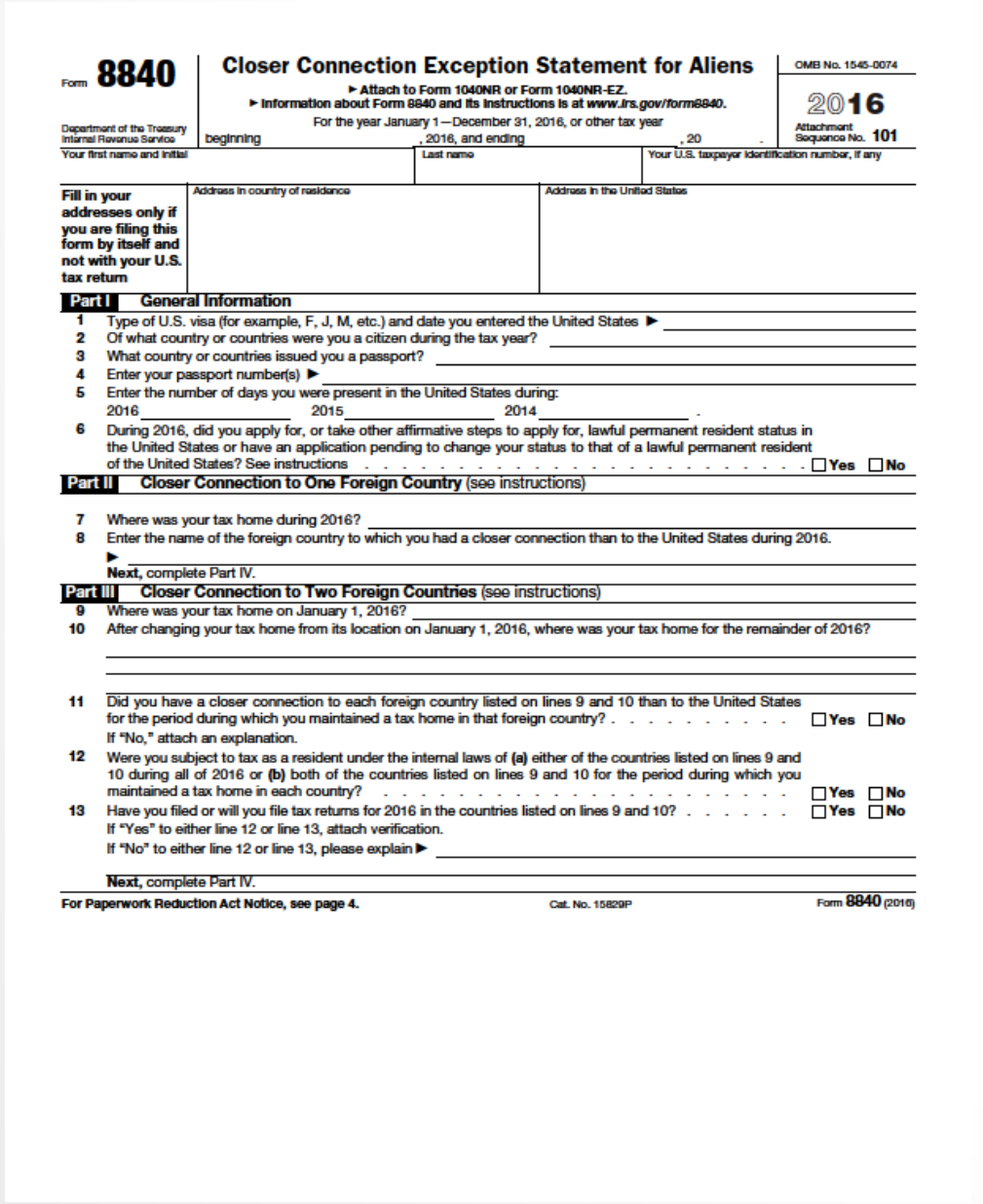
- Are they non-US or US persons? Does U.S. tax apply to worldwide income, estate and gift tax or only on U.S. source/situs items?
- If they're "foreign" now, will they be "U.S. shortly?
- Engaged in a U.S. trade or business that generates "effectively-connected income?" If so, does the U.S. branch profits tax apply?
- Does a potentially beneficial bilateral U.S. income tax treaty apply to the income, gift or estate in question?
- Is the foreign investor concerned about disclose of U.S. activities to the home country tax authorities?
- Should you be personally concerned about assisting a foreign investor who wants "privacy?"

FOREIGN PERSONS WHO ARE OR WHO MAY BECOME U.S. PERSONS

- This has become our most common everyday international tax practice issue—individuals who have moved here or are considering moving here, along with "accidental" U.S. citizens
- Primary difference—taxed on worldwide income, gifts and estate, rather than only U.S. source income, income that effectively-connected with the conduct of a USTB, and gratuitous transfers of U.S. situs assets
- Advance planning techniques may differ depending upon the country of origin and how long they plan to stay in the U.S., although it isn't always easy to be certain
- Will it just be "mom and the kids" or the whole family?
- It's NEVER too late to do U.S. tax and estate planning.

HOW DO FOREIGN INDIVIDUALS BECOME U.S. PERSONS?

- For income tax purposes—becoming a U.S. citizen, obtaining a U.S. green card, or meeting the "Substantial Presence Test"—183 days in a particular calendar year or based upon a three-year test (# days in current year + 1/3 days in prior year + 1/6 days in second prior year)
- "Days" don't count for certain teachers, students, or diplomats or medical conditions first arising in the United States—see Form 8843
- "Closer connection"/"Tax home" test can override three-year Substantial Presence Test—see Form 8840 (unless the person applied for a U.S. green card
- Treaty residence "tiebreaker" provisions can also override U.S. green cards and the Substantial Presence Test—see Form 8833



Form **8840**

Department of the Treasury
Internal Revenue Service

Closer Connection Exception Statement for Aliens

► Attach to Form 1040NR or Form 1040NR-EZ.
► Information about Form 8840 and its instructions is at *www.irs.gov/form8840*.

For the year January 1—December 31, 2016, or other tax year
beginning , 2016, and ending , 20

OMB No. 1545-0074

2016

Attachment Sequence No. **101**

Your first name and initial	Last name	Your U.S. taxpayer identification number, if any

Fill in your addresses only if you are filing this form by itself and not with your U.S. tax return	Address in country of residence	Address in the United States

Part I General Information

1 Type of U.S. visa (for example, F, J, M, etc.) and date you entered the United States ►
2 Of what country or countries were you a citizen during the tax year?
3 What country or countries issued you a passport?
4 Enter your passport number(s) ►
5 Enter the number of days you were present in the United States during:
2016 2015 2014
6 During 2016, did you apply for, or take other affirmative steps to apply for, lawful permanent resident status in the United States or have an application pending to change your status to that of a lawful permanent resident of the United States? See instructions . . . ☐ Yes ☐ No

Part II Closer Connection to One Foreign Country (see instructions)

7 Where was your tax home during 2016?
8 Enter the name of the foreign country to which you had a closer connection than to the United States during 2016.
►
Next, complete Part IV.

Part III Closer Connection to Two Foreign Countries (see instructions)

9 Where was your tax home on January 1, 2016?
10 After changing your tax home from its location on January 1, 2016, where was your tax home for the remainder of 2016?
11 Did you have a closer connection to each foreign country listed on lines 9 and 10 than to the United States for the period during which you maintained a tax home in that foreign country? . . . ☐ Yes ☐ No
If "No," attach an explanation.
12 Were you subject to tax as a resident under the internal laws of **(a)** either of the countries listed on lines 9 and 10 during all of 2016 or **(b)** both of the countries listed on lines 9 and 10 for the period during which you maintained a tax home in each country? . . . ☐ Yes ☐ No
13 Have you filed or will you file tax returns for 2016 in the countries listed on lines 9 and 10? . . . ☐ Yes ☐ No
If "Yes" to either line 12 or line 13, attach verification.
If "No" to either line 12 or line 13, please explain ►
Next, complete Part IV.

For Paperwork Reduction Act Notice, see page 4. Cat. No. 15829P Form **8840** (2016)

Form **8843**

Department of the Treasury
Internal Revenue Service

Statement for Exempt Individuals and Individuals With a Medical Condition

For use by alien individuals only.

► **Information about Form 8843 and its instructions is at *www.irs.gov/form8843*.**

OMB No. 1545-0074

2016

Attachment Sequence No. **102**

For the year January 1—December 31, 2016, or other tax year beginning _____, 2016, and ending _____, 20 _____.

Your first name and initial	Last name	Your U.S. taxpayer identification number, if any

Fill in your addresses only if you are filing this form by itself and not with your tax return	Address in country of residence	Address in the United States

Part I General Information

1a Type of U.S. visa (for example, F, J, M, Q, etc.) and date you entered the United States ► _____

b Current nonimmigrant status and date of change (see instructions) ► _____

2 Of what country were you a citizen during the tax year? _____

3a What country issued you a passport? _____

b Enter your passport number ► _____

4a Enter the actual number of days you were present in the United States during:
2016 _____ 2015 _____ 2014 _____

b Enter the number of days in 2016 you claim you can exclude for purposes of the substantial presence test ► _____

Part II Teachers and Trainees

5 For teachers, enter the name, address, and telephone number of the academic institution where you taught in 2016 ► _____

6 For trainees, enter the name, address, and telephone number of the director of the academic or other specialized program you participated in during 2016 ► _____

7 Enter the type of U.S. visa (J or Q) you held during: ► 2010 _____ 2011 _____ 2012 _____ 2013 _____ 2014 _____ 2015 _____. If the type of visa you held during any of these years changed, attach a statement showing the new visa type and the date it was acquired.

8 Were you present in the United States as a teacher, trainee, or student for any part of 2 of the 6 prior calendar years (2010 through 2015)? . . . . . ☐ Yes ☐ No
If you checked the "Yes" box on line 8, you cannot exclude days of presence as a teacher or trainee unless you meet the *Exception* explained in the instructions.

Part III Students

9 Enter the name, address, and telephone number of the academic institution you attended during 2016 ► _____

10 Enter the name, address, and telephone number of the director of the academic or other specialized program you participated in during 2016 ► _____

11 Enter the type of U.S. visa (F, J, M, or Q) you held during: ► 2010 _____ 2011 _____ 2012 _____ 2013 _____ 2014 _____ 2015 _____. If the type of visa you held during any of these years changed, attach a statement showing the new visa type and the date it was acquired.

12 Were you present in the United States as a teacher, trainee, or student for any part of more than 5 calendar years? . . . . . ☐ Yes ☐ No
If you checked the "Yes" box on line 12, you must provide sufficient facts on an attached statement to establish that you do not intend to reside permanently in the United States.

13 During 2016, did you apply for, or take other affirmative steps to apply for, lawful permanent resident status in the United States or have an application pending to change your status to that of a lawful permanent resident of the United States? . . . . . ☐ Yes ☐ No

14 If you checked the "Yes" box on line 13, explain ► _____

Form **8833**
(Rev. December 2013)
Department of the Treasury
Internal Revenue Service

Treaty-Based Return Position Disclosure Under Section 6114 or 7701(b)

► Attach to your tax return.
► Information about Form 8833 and its instructions is at *www.irs.gov/form8833*.

OMB No. 1545-1354

Attach a separate Form 8833 for each treaty-based return position taken. Failure to disclose a treaty-based return position may result in a penalty of $1,000 ($10,000 in the case of a C corporation) (see section 6712).

Name	U.S. taxpayer identifying number	Reference ID number, if any (see instructions)

Address in country of residence	Address in the United States

Check one or both of the following boxes as applicable:

- The taxpayer is disclosing a treaty-based return position as required by section 6114 . . . . . ► ☐
- The taxpayer is a dual-resident taxpayer and is disclosing a treaty-based return position as required by Regulations section 301.7701(b)-7 . . . . . ► ☐

Note. If the taxpayer is a dual-resident taxpayer and a long-term resident, by electing to be treated as a resident of a foreign country for purposes of claiming benefits under an applicable income tax treaty, the taxpayer will be deemed to have expatriated pursuant to section 877A. For more information, see the instructions.

Check this box if the taxpayer is a U.S. citizen or resident or is incorporated in the United States . . . . . ► ☐

1 Enter the specific treaty position relied on:
- **a** Treaty country _____
- **b** Article(s)

2 List the Internal Revenue Code provision(s) overruled or modified by the treaty-based return position

3 Name, identifying number (if available to the taxpayer), and address in the United States of the payor of the income (if fixed or determinable annual or periodical). See instructions.

4 List the provision(s) of the limitation on benefits article (if any) in the treaty that the taxpayer relies on to prevent application of that article ►

5 Is the taxpayer disclosing a treaty-based return position for which reporting is specifically required pursuant to Regulations section 301.6114-1(b)? . . . . . ☐ Yes ☐ No

If "Yes," enter the specific subsection(s) of Regulations section 301.6114-1(b) requiring reporting . . . . ► _____

Also include the information requested in line 6.

6 Explain the treaty-based return position taken. Include a brief summary of the facts on which it is based. Also, list the nature and amount (or a reasonable estimate) of gross receipts, each separate gross payment, each separate gross income item, or other item (as applicable) for which the treaty benefit is claimed _____

For Paperwork Reduction Act Notice, see the instructions. Cat. No. 14895L Form **8833** (Rev. 12-2013)

HOW DO FOREIGN INDIVIDUALS BECOME U.S. PERSONS? (CONTINUED)

- For estate and gift tax purposes—a U.S. citizen, or U.S. domicile may be obtained through either becoming or the individual's intent, as shown by the related facts and circumstances, is to make the U.S. his or her permanent home
- This determination is often a classic "scales of justice" analysis
- Obtaining a U.S. green card or meeting the "Substantial Presence Test" are important facts for this purpose—but aren't controlling, unlike for income tax purposes—see Estate of Barkat A. Khan, 75 TCM 1597 (1998) where the IRS argued that possession of a U.S. green card did not automatically make the decedent a U.S. domiciliary
- If your client's U.S.–situs assets exceed US$60,000, but his/her total assets are less than the lifetime/death applicable exclusion amount (US$5,490,000 in 2017), you may **WANT** to claim U.S. domicile in borderline cases
- Treaty residence "tiebreaker" provisions can also override general U.S. domicile law, and other treaty provisions may proved significant benefits (see, e.g., Canada, France, Germany and the U.K.)—see Form 8833

HOW DO FOREIGN INDIVIDUALS AND ENTITIES BECOME U.S. TAXPAYERS?

- "FDAPI" gross 30% U.S. withholding tax on passive U.S. source income—interest (with exceptions), dividends, royalties, rents, etc.
- Most common USTB issues—sale of U.S. real property interest, U.S. sales of tangible personal property, performance of services in the United States
- In general, the seller's residence is the source of income from the sale of personal property—§ 865(a)
- Major exception—title passage test applies to sales of inventory property —§ 865(b)
- Sales of certain inventory and other tangible property by foreign persons which are attributable to a U.S. office/fixed place of business are U.S. source income, unless sold for foreign use, consumption or disposition, with the material participation of the seller's foreign office—§865(e)

HOW DO FOREIGN INDIVIDUALS AND ENTITIES BECOME U.S. TAXPAYERS? (CONTINUED)

- **This is the most common inbound U.S. business tax planning issue at PNR**
- **Typical situation—large non-U.S. company wants to set up a U.S. "representative office" to sell goods or services to foreign (or new U.S.) customers to allow family member to run it from South Florida**
- Even if no actual U.S. office or employees, an NRA or FC still may be deemed to have a USTB through the U.S. office of a "dependent" or exclusive U.S. agent, but not through an "independent agent"

HOW DO FOREIGN INDIVIDUALS AND ENTITIES BECOME U.S. TAXPAYERS? (CONTINUED)

- InverWorld, Inc. U.S. Tax Court case is a great "how not to" primer on this issue, botched planning at it most expensive with huge penalties
- Somewhat different "permanent establishment" rule applies under U.S. tax treaties
- Be careful of this rule for "offshore" sales or services businesses
- File a “protective return” to preserve the right to claim deductions—otherwise, tax of USTB income will generally be on a gross basis

A USTB "SURPRISE" FOR FOREIGN LENDERS WITH U.S. AGENTS

- Memorandum AM 2009-010 dated September 22, 2009 from the Associate Chief Counsel (International) to LMSB/Financial Services concludes that a foreign lender received taxable effectively connected U.S. source interest income on loans generated in the U.S. by an independent contractor that did not have power to bind the nonresident lender, simply by virtue of the domestic activities being regular and continuous and carried out on behalf of the nonresident lender, without evidence of either: (a) control of the agent by the lender, or (b) the agent having power to bind the lender

A USTB "SURPRISE" FOR FOREIGN LENDERS WITH U.S. AGENTS (CONTINUED)

- For purposes of this rule, an agent shall be considered regularly to exercise authority to negotiate and conclude contracts or regularly to fill orders on behalf of his foreign principal only if the authority is exercised, or the orders are filled, with some frequency over a continuous period of time, based upon the facts and circumstances in each case, taking into account the nature of the business of the principal
- This Memorandum evidences the aggressive approach that the IRS often takes when attempting to treat a foreign person or company as being engaged in a USTB generating ECI

POTENTIAL CONSEQUENCES FOR A FOREIGN CORPORATION ENGAGED IN A U.S. TRADE OR BUSINESS

- Watch out for using an FC to engage in a U.S. trade or business, especially if owned by a U.S. Person.
  - Potential for **three levels** of U.S. income tax!
  - Federal and Florida Corporate tax.
  - Branch Profits Tax.
  - Tax on Dividend to U.S. Person shareholders (possibly at capital gains rates if a Qualified Foreign Corporation).

BRANCH PROFITS TAX—IRC §884

- **A 30%** annual tax imposed upon the "dividend equivalent amount" of an foreign corporation **in addition to** U.S. income tax—§884(a)
- "DEA" = the FC's effectively-connected earnings and profits for the taxable year, adjusted by increases and decreases in U.S. net equity—§884(b)
- "ECEP" = (in general) earnings and profits which are ECI/USTB or treated as ECI/USTB—§884(d)
- "U.S. Net Equity" = "U.S. Assets" less "U.S. Liabilities"—§884(c)

CONTINUING EXPANSION OF NONRESIDENT ALIEN DEPOSIT INTEREST REPORTING

- The countries with which the IRS will automatically exchange information are presently: Australia, Azerbaijan, Brazil, Canada, Czech Republic, Denmark Estonia, Finland, France, Germany, Gibraltar, Guernsey, Hungary, Iceland, India, Ireland, Isle of Man, Italy, Jamaica, Jersey, Latvia, Liechtenstein, Lithuania, Luxembourg, Malta, Mauritius, Mexico, Netherlands, New Zealand, Norway, Poland, Slovak Republic, Slovenia, South Africa, Spain, Sweden, and the United Kingdom
- Fla. Bankers Ass'n v. Dep't of Treasury, a SCOTUS petition for certiorari was denied on June 6, 2016, finally ending the court battle to avoid the application of these reporting rules

REPORTING FOREIGN GIFTS AND FOREIGN TRUST DISTRIBUTIONS

- Gifts from foreign donors in excess of $100,000 in a particular calendar year must be reported on Form 3520
- Cash gifts from foreign personal accounts should be tax-free—but it's not as certain where the gift is made from a foreign individual's U.S. bank account
- Distributions from a foreign trust are separately reported on Form 3520—U.S. beneficiaries will need access to information as to whether they are tax-free (e.g., from a grantor trust or from trust principal) or taxable (and if so, as trust DNI or UNI—if the latter, note the related complex throwback/interest charge rules of §§665-668)
- **Beware of**:

(1) "Purported gifts" from foreign corporations and partnerships—the IRS treats them as **potentially taxable distributions, NOT** as "gifts" —§ 672(f)(4)

(2) Loans from foreign trusts that are not "qualified obligations"—§ 643(i)

(3) Uncompensated use of trust property by a U.S. beneficiary—§ 679(c)(6)

PENALTIES FOR FAILURE TO FILE FORM 3520

- A penalty of 5% of the amount of the unreported gift applies for each month for which the failure to report exists (not to exceed 25%).
- If a U.S. person beneficiary fails to make the return or reports inadequate information, the U.S. person beneficiary would be subject to a civil penalty equivalent to thirty-five percent (35%) of the amount of the distribution, and if such failure continues for more than 90 days after the day on which the Service mails notice of such failure, such U.S. person would be subject to an additional penalty of $10,000 for each 30-day period (or fraction thereof) thereafter.

REDSTONE V. COMMISSIONER, T.C. MEMO 2015-237, 12/9/15—HOW FAR BACK CAN THE IRS GO TO TAX AN UNREPORTED TAXABLE GIFT?

- Many NRA taxable gifts of U.S.-situs tangible personal property and USRPIs go unreported—how long afterward can they be discovered and potentially cause an IRS exam?
- Example—NRA parent transfers a Miami condo unit to her children as joint tenants with right of survivorship, and then one of the children dies, or the unit will be sold
- If fraud or no reporting—potential exposure FOREVER
- The IRS likely became aware of the gifts as a result of family litigation that commenced in 2006
- The IRS successfully argued that **1972** transfers of stock to trusts for the benefit of the taxpayer's children were taxable gifts, but penalties were abated due to the taxpayer's reliance upon tax counsel in deciding not to file
- Because no U.S. gift tax return was filed to report the gifts, the statute of limitations remained open for the IRS to assess the gift tax deficiency in **2013—more than 40 years** after the transfer

NEW REPORTING REQUIREMENTS FOR DOMESTIC SINGLE-MEMBER LLCS—FORM 5472

- New Reg. §§1.6038A-1 and -2, issued December 13, 2016, following earlier Proposed Regulations
- Treat a domestic single-member LLC/disregarded entity ("SMLLCs")that is wholly owned by one foreign person as a domestic corporation separate from its owner for the limited purposes of the reporting and record maintenance requirements under § 6038A (Form 5472)
- Consequently, most likely beginning in 2018 (for the 2017 tax year), these SMLLCs will be required to:

(1) obtain EINs from the IRS which will require identification of a natural person related to the LLC;

(2) annually file Form 5472, Information Return of a 25% Foreign-Owned U.S. Corporation or a Foreign Corporation Engaged in a U.S. Trade or Business;

(3) identify a more expanded version of "reportable transactions" between the LLC and any related parties, including the LLC's foreign owner; and

(4) maintain supporting books and records.

FATCA ENFORCEMENT HAS BEGUN

- On May 9, 2016, the Justice Department announced that Gregg R. Mulholland, a dual U.S. and Canadian citizen and owner of an offshore broker-dealer and investment management company based in Panama and Belize, pleaded guilty to money laundering conspiracy for fraudulently manipulating the stocks of more than 40 U.S. publicly-traded companies and then laundering more than $250 million in profits through at least five offshore law firms.
- Law enforcement authorities employed undercover agents and wiretaps to record numerous conversations involving the defendants.

FATCA ENFORCEMENT HAS BEGUN

- In one recorded meeting, two of the defendants bragged that their strategy enabled clients to evade FATCA's requirements through the use of offshore nominee companies.
- This prosecution represents the first time the Justice Department has brought criminal charges against individuals for conspiring to violate FATCA's reporting requirements.
- With FATCA's provisions only becoming effective on July 1, 2014, and with the Justice Department's offshore crackdown showing no signs of slowing down, we expect to see more criminal prosecutions in the future alleging violations of FATCA's provisions.

IRC §1446 PARTNERSHIP WITHHOLDING RULES

- Often overlooked tax rule that can affect general partners or LLC managers who fail to withhold (and are thus liable for the tax under §1461)—once you make distributions are made, good luck on getting them back!
- Withholding applies to a foreign partner's share of partnership effectively-connected taxable income
- Foreign partners **must** obtain a TIN or ITIN

IRC §1446 PARTNERSHIP WITHHOLDING RULES (CONTINUED)

- "ECTI" is partnership taxable income which is effectively connected (or treated as effectively connected) with a USTB, with certain adjustments
- Use Forms 8804, 8805, and 8813
- Partner status is determined through W-8 or W-9 forms received by the partnership
- Highest §1 and §11 rates apply for withholding requirement

IRC §1446 PARTNERSHIP WITHHOLDING RULES
(CONTINUED)

- Highest §1 and §11 rates apply
- §1446 withholding tax is treated as a credit against the foreign partner's tax liability in the tax year in which the partnership's tax year ends
- To claim a credit for the Code §1446 tax, the foreign partner must attach proof of payment to its U.S. tax return for the taxable year in which it claims the credit—use a copy of Form 8805 as proof of payment

IRC §1446 PARTNERSHIP WITHHOLDING RULES
(CONTINUED)

- The amount of tax that a partnership must withhold and pay over relates to the ECTI allocable to the foreign partners for the taxable year
- Based upon a foreign partner's distributive share of effectively connected gross income of the partnership reduced by the foreign partner's distributive share of deductions for the year that are connected with such income and are properly allocable to the partner under §704

IRC §1446 PARTNERSHIP WITHHOLDING RULES
(CONTINUED)

- Rev. Proc. 92-66, 1992-2 C.B. 428, exempts from §1445(e)(1) FIRPTA withholding any domestic partnership that is subject to the withholding requirements of §1446 and compliance with the §1446 withholding requirements satisfies the §1445(e) withholding requirements
- Special rules for tiered partnership structures

WHERE DO WE GO FROM HERE?

Check Twitter daily!