Tax Advice & Controversy Client Service Group

To: Our Clients and Friends

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New Law Expands US Tax Reporting and Anti-Abuse Provisions Designed to Discourage U.S. Persons from Hiding Income and Assets in Foreign Countries

On March 18, 2010 President Obama signed into law the Hiring Incentive To Restore Employment Act (the "Hire Act"). The Hire Act contains provisions which impose a withholding tax on payments to "non-compliant foreign financial institutions" and additional reporting requirements for U.S. Taxpayers and Foreign Financial Institutions.

Withholding Tax on Payments to Foreign Financial Institutions and Other Foreign Entities

- Every "foreign financial institution" (regardless of whether it has "Qualified Intermediary" status) must certify to the US Treasury that the institution has implemented specified procedures designed to identify "United States accounts" and provide to the Treasury annually detailed information about US taxpayers who are either "account holders" or "substantial United States owners" of an entity that is an account holder.

- A 30% withholding tax is imposed on the gross amount of US source income, including the proceeds of certain asset sales, ("withholdable payments") made to foreign financial institutions that do not comply with the above requirements.

- A similar withholding regime requiring certification to withholding agents (rather than the Treasury) is imposed on any payment to a "non-financial foreign entity" payee. This applies, for example, to a US custodian making payments directly to a foreign entity such as a foreign private corporation.

- Withholding tax on withholdable payments becomes effective for payments made on and after January 1, 2013.

- In addition to the withholding tax on withholdable payments, the Hire Act subjects dividend equivalent payments included in notional principal contracts and paid to overseas corporations to the same 30 percent withholding tax levied on dividends paid to foreign investors. NOTE: that this new withholding tax is effective for payments made on or after 180 days after March 18, 2010.

Information Reporting

- A new annual information reporting regime takes effect as of January 1, 2011. "Any individual" who "holds any interest in a specified foreign financial asset" must file a report for each year during which the aggregate value of all such assets at any time exceeds $50,000. The definition of "specified foreign financial assets" includes stock, securities or other contractual obligations issued by anyone other than a US person. It also includes "any interest in a foreign entity". This regime is similar to the current "Foreign Bank Account Report" (FBAR) regime imposed by US banking laws, but the FBAR regime is not eliminated.

- Direct and indirect shareholders in a foreign corporation classified as a passive foreign investment company (PFIC) (i.e. any person who would be subject to tax under the PFIC regime if an "excess distribution" were received by the direct owner of a PFIC) are required to file an annual PFIC information return containing information that the IRS may require in regulations to be promulgated. This provisions is effective March 18, 2010.

- Finally, there are a number of their changes relating to increased penalties and the extension of certain statutes of limitations thereby extending the time the IRS has to audit tax returns and assess additional taxes. .

Expanded Taxation of Foreign Trust Income and Gains

- Tax is imposed on the value of a US beneficiary's use of property owned by a foreign trust if the US beneficiary does not pay fair market value for that use within "a reasonable period of time". The tax will take effect with respect to any use occurring on or after March 18, 2010.

- The rules that cause a US settlor to be taxed on the income and gains of a foreign trust (i.e. as a grantor trust) under Internal Revenue Code section 679 are expanded.

- A new requirement that a US settlor must "demonstrate to the satisfaction of the Secretary" that a foreign trust does not have a United States beneficiary is imposed as a condition of avoiding taxation under the grantor trust rule of section 679.

To discuss this issue further, please speak to your Bryan Cave contact, or to:

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