

## **FATCA #1: HIRE Foreign Account Tax Compliance Summary** **(The Act)**

On March 18, 2010, President Obama signed the Hiring Incentives to Restore Employment (“HIRE”) Act (P.L. 111-147) (The “Act”) which included the Foreign Account Tax Compliance Act containing new foreign account tax compliance rules.

Under the Act, new reporting and disclosure requirements for foreign assets will be phased in between 2010 – 2013:

- 1. Foreign Institutional Reporting:** Foreign Institutions have new reporting and withholding obligations for accounts held by U.S. Persons (generally effective after 12/31/12, commencing 1/1/13).
- 2. Foreign Financial Assets (\$50,000):** Individuals with an interest in a “Foreign Financial Asset” have new disclosure requirements. If foreign financial assets are valued in excess of \$50,000, the U.S. Taxpayer must attach certain information to their income tax returns for tax years beginning after March 18, 2010. (U.S. Taxpayers are not required to disclose interests that are held in a custodial account with a U.S. financial institution).

The penalty is substantial (\$10,000, plus additional amounts for continued failures, up to a maximum of \$50,000 for each applicable tax period). The penalty may be waived if the individual can establish that the failure was due to reasonable cause and not willful neglect.

- 3. 40% Penalty:** A 40% accuracy-related penalty is imposed for underpayment of tax that is attributable to an undisclosed foreign financial asset understatement. Applicable assets are those subject to mandatory information reporting when the disclosure requirements were not met. The penalties are effective for tax years beginning after March 18, 2010.
- 4. 6 Year Statute of Limitations:** Statute of limitations re: omission of income in connection with foreign assets: The statute of limitations for assessments of tax is extended to six (6) years if there is an omission of gross income in excess of \$5,000 attributable to the foreign financial asset. The six year statute of limitations is effective for tax returns filed after March 18, 2010, as well as for any other tax return for which the assessment period has not yet expired as of March 18, 2010.

5. **Passive Foreign Investment Companies:** The Act imposes an information disclosure requirement on U.S. Persons who are PFIC shareholders.

A PFIC is any foreign corporation if:

- a. 75% or more of the gross income of the corporation for the taxable year is passive income; or
- b. The average percentage of assets held by such corporation during a taxable year which produce passive income or which are held for the production of passive income are at least 50%.

6. **Foreign Trusts with U.S. Beneficiaries:** The Act clarifies if a foreign trust is treated as having a U.S. Beneficiary, an amount accumulated is treated as accumulated for the U.S. Person's benefit even if that Person's trust interest is contingent. The Act clarifies that the discretion to identify beneficiaries may cause the trust to be treated as having a U.S. Beneficiary. This provision is effective after March 18, 2010.

7. **Rebuttable Presumption/Foreign Trust – U.S. Beneficiary:** The Act creates a rebuttable presumption that a foreign trust has a U.S. Beneficiary if a U.S. Person directly or indirectly transfers property to a foreign trust (unless the transferor provides satisfactory information to the contrary to the IRS). This provision is effective for property transfers after March 18, 2010.

8. **Uncompensated Use of the Foreign Trust Property:** The Act provides that the uncompensated use of the foreign trust property by a U.S. Grantor, a U.S. Beneficiary (or a U.S. Person, related to either of them), is treated as a distribution by the trust.

The use of the trust property is treated as a distribution to the extent of the fair market value of the property's use to the U.S. Grantor/U.S. Beneficiary, unless the fair market value of that use is paid to the trust.

The loan of cash or marketable securities by a foreign trust, or the use of any other property of the trust, to or by any U.S. Person is also treated as paid or accumulated for the benefit of the U.S. Person. This provision applies to loans made and uses of property after March 18, 2010.

9. **Reporting Requirements, U.S. Owners of Foreign Trusts:** This provision requires any U.S. Person treated as the owner of any portion of a foreign trust to submit IRS-required information and insure that the trust files a return on its activities and provides such information to its owners and distributees.

This new requirement imposed on U.S. Persons treated as owners is in addition to the current requirement that such U.S. Persons are responsible for insuring that the foreign trust complies with its own reporting obligations. This provision is effective for taxable years beginning after March 18, 2010.

**10. Minimum Penalty re: Failure to Report Certain Foreign Trusts:**

This provision increases the minimum penalty for failure to provide timely and complete disclosure on foreign trusts to the greater of \$10,000 or 35% of the amount that should have been reported.

In the case of failure to properly disclose by the U.S. Owner of a foreign trust of the year-end value, the minimum penalty would be the greater of \$10,000 or 5% of the amount that should have been reported.

This provision is effective for notices and returns required to be filed after December 31, 2009.

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