

From FBAR to Twice Cooked Pork (回鍋肉):

How one small US tax form is changing what
Chinese people eat

People's Republic of China,
June 2014



德恒律師事務所
DeHeng Law Offices



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Chinese connections to the U.S.A.



Chinese commercial real estate purchases in the U.S.A. totaled over \$3 billion: Tishman, China Vanke to Build 655-Unit San Francisco Condo Tower

Chinese Investment in U.S. reaches \$14 Billion in 2013: Shuanghui's \$7.1 billion takeover of pork processor Smithfield.

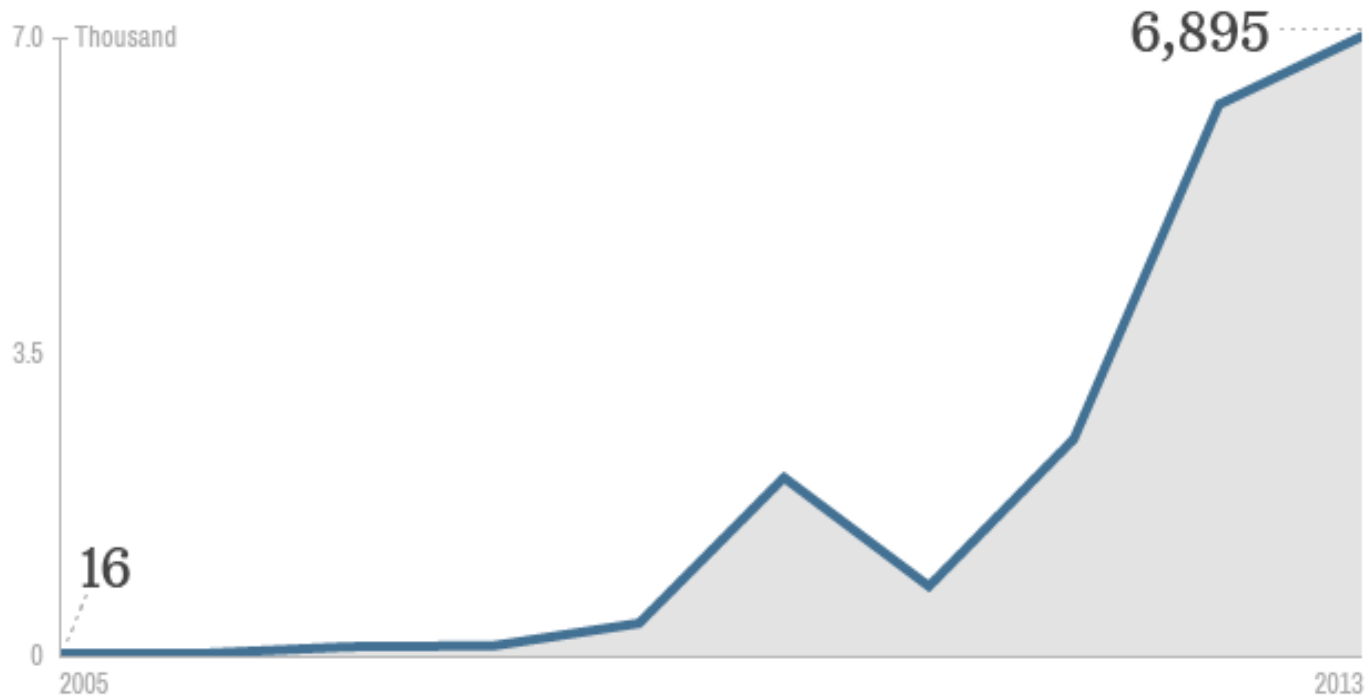
May 17, 2014: Baidu \$300 million R&D center in Silicon Valley with 200 employees.

6,895 EB5 visas in 2013: 64% of Chinese millionaires plan to leave China and 1/3 of the super rich (those with more than \$16,000,000) have already emigrated.

Over 3,000,000 Chinese in the USA.

Growth of EB5 applications

EB-5 U.S visas issued to the Chinese



NOTE: FIGURES DO NOT INCLUDE VISAS ISSUED TO RESIDENTS OF HONG KONG OR TAIWAN; SOURCE: U.S. STATE DEPARTMENT





Department of the Treasury
Internal Revenue Service



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U.S. TAX BACKGROUND - REPORTING

- U.S. tax payers (Citizens, Green Card Holders, certain Visa Holders) are required to report worldwide income regardless where they live.
- In addition, U.S. taxpayers are required to file information returns such as:
 - FBAR
 - Form 8938 : Foreign Assets
 - Form 5471: Foreign Corporation
 - Form 3520: Foreign Trust and Gifts



FBAR - Background

- FinCen 114: Report of Foreign Bank and Financial Accounts a/k/a the Foreign Bank Account Report or “FBAR” (Treasury Form, not IRS Form).
- In 1970, U.S. Congress enacted the Bank Secrecy Act, which is codified in Title 31 (Money and Finance) of the U.S. Tax Code. The purpose of the Bank Secrecy Act was to require the filing of reports and the retention of records where doing so would be helpful to the U.S. government in carrying out criminal, tax and regulatory investigations.



FBAR - Enforcement

- The U.S. Treasury Department delegated full investigatory and enforcement authority to the IRS.
- Increased enforcement after the 9/11 terrorist attacks in the United States under the Patriot Act (*Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism (USA PATRIOT ACT) Act of 2001*).
- IRS has in its arsenal several formidable weapons, including the power to take “any action reasonably necessary” to enforce FBAR compliance.
- From Fox America's Newsroom June 13, 2013: Rep. Jeff Duncan (R-SC) has raised some eyebrows on Capitol Hill this morning, claiming that he saw IRS agents training with AR-15 assault rifles. According to Fox, no IRS enforcement agent has ever been killed in the line of duty, but they have had used their weapons **8** times, and accidentally fired a weapon on **11** occasions.



FBAR - Who Must File an FBAR

United States persons are required to file an FBAR if:

- The United States person had a financial interest in or signature authority over at least one financial account located outside of the United States;

and

- The aggregate value of all foreign financial accounts exceeded \$10,000 at any time during the calendar year to be reported, e.g., \$2,000+\$3,000+\$6,000.



FBAR - Reporting and Filing Information

A person who holds a foreign financial account may have a reporting obligation even though the account produces no taxable income.

The reporting obligation is met by answering questions on a tax return about foreign accounts (for example, the questions about foreign accounts on Form 1040 Schedule B or on the New York State income tax return) and by filing an FBAR.

The FBAR is a calendar year report, which must be filed electronically with the Department of Treasury on or before June 30 of the year following the calendar year reported. Extensions of time to file an FBAR are not granted.

The FBAR is not filed with a federal tax return. Any filing extensions of time granted by the IRS to file a tax return does not extend the time to file an FBAR.

FBAR - United States Person

The United States person had a financial interest in or signature authority over at least one financial account located outside of the United States:

United States person means:

U.S. citizens;

U.S. residents;

Entities, including but not limited to, corporations, partnerships, or limited liability companies, created or organized in the United States or under the laws of the United States; and

Trusts or estates formed under the laws of the United States.

FBAR – Financial Interest

The United States person had a financial interest in or signature authority over at least one financial account located outside of the United States:

A United States person has a financial interest in a foreign financial account for which:

- (1) The United States person is the owner of record or holder of title, regardless of whether the account is maintained for the benefit of the United States person or for the benefit of another person;
- (2) The owner of record or holder of legal title is one of the following:
 - (a) An agent, nominee, attorney, or a person acting in some capacity on behalf of the United States person with respect to the account;
 - (b) A corporation in which the United States person owns directly or indirectly: (i) more than 50 percent of the total value of shares of stock or (ii) more than 50 percent of the voting power of all shares of stock;
 - (c) A partnership in which the United States person owns directly or indirectly: (i) an interest in more than 50 percent of the partnership's profits (e.g., distributive share of partnership income taking into account any special allocation agreement) or (ii) an interest in more than 50 percent of the partnership capital;
 - (d) A trust of which the United States person: (i) is the trust grantor and (ii) has an ownership interest in the trust for United States federal tax purposes
 - (e) A trust in which the United States person has a greater than 50 percent present beneficial interest in the assets or income of trust for the calendar year; or
 - (f) Any other entity in which the United States person owns directly or indirectly more than 50 percent of the voting power, equity interest or assets, or interest in profits.

FBAR – Signature Authority

The United States person had a financial interest in or signature authority over at least one financial account located outside of the United States:

- Signature authority is the authority of an individual (alone or in conjunction with another individual) to control the disposition of assets held in a foreign financial account by direct communication (whether in writing or otherwise) to the bank or other financial institution that maintains the financial account:
 - US attorneys with foreign escrow accounts
 - CFOs

FBAR – Financial Account

The United States person had a financial interest in or signature authority over at least one financial account located outside of the United States:

A financial account includes, but is not limited to, a securities, brokerage, savings, demand, checking, deposit, time deposit or other account maintained with a financial institution (or other person performing the services of a financial institution) whether the account holds cash or non-monetary assets.

A financial account also includes a commodity futures or options account, an insurance policy with a cash value (such as a whole life insurance policy), an annuity policy with a cash value, and shares in a mutual fund or similar pooled fund.

Individual bonds, notes, or stock certificates held by the filer are not a financial account.

United States v. Hom: gambling accounts at FirePay.com; PokerStars.com; and Partypoker.com



FBAR Penalties

Failure to properly report the foreign account on Schedule B of Form 1040 and to file an FBAR may warrant civil and criminal sanctions. The two primary civil FBAR penalties are referred to as “non-willful” and “willful.”

The non-willful penalty is up to \$10,000 for each negligent violation of the FBAR filing or record-keeping requirements, and it may be waived if the violation was “due to reasonable cause” and the amount of the transaction or the balance in the account at the time of the transaction was properly reported.

Willfully failing to file an FBAR can warrant both criminal sanctions and civil penalties equivalent to the greater of \$100,000 or 50 percent of the high balance in an unreported foreign account per year — for each year (maximum 6) for which an FBAR was not filled.

Willfulness is generally determined by “a voluntary, intentional violation of a known legal duty.” The IRS' Internal Revenue Manual provides that willfulness is demonstrated by the person’s knowledge of the FBAR requirements or conscious choice to ignore coupled with his conscious choice not to comply with them.

UBS Settlement 19/08/2009

- The landmark settlement was expected to provide a road map for the IRS as it tried to clamp down on tax evasion by Americans who use offshore accounts.
- UBS handed over 4450 names of U.S. clients to the IRS.
- UBS paid fine of \$780,000,000

New York Times 19/08/2009:

- ❖ “Whether the deal will change the Swiss banking industry’s culture of secrecy remains to be seen. Smaller Swiss banks say they are confident that they can blunt its effects and continue to profit by finding new, more elaborate ways to protect the privacy of clients. But American authorities have made clear that their pursuit of tax evaders will not stop at UBS.”
- ❖ “Some smaller, centuries-old private Swiss banks, however, are stepping up their efforts to attract American money, given the importance of foreign clients to the nation’s financial institutions. Executives at smaller Swiss banks and trade groups say they are increasingly working with Swiss financial and legal companies to set up offshore entities as a way to shield assets from prying regulatory eyes. They have also been reassuring clients that their accounts will remain confidential.”
- ❖ Sebastian Dovey, a managing partner at Scorpio Partnership, a wealth consulting firm in London, said that “we have not seen huge amounts of movement” of American money out of Swiss banks.

UBS Settlement 19/08/2009

- ❖ Other countries have also pressured Switzerland for names of suspected tax cheats, including Germany and Italy. The attention has left Swiss bankers upset about demands that they ensure that their clients pay their taxes.
- ❖ “The American authorities are trying to use the banks as guardians of the clients’ conscience, which is not really what we’re here for,” said Michel Y. Dérobert, secretary general of the Swiss Private Bankers Association in Geneva, a trade group of traditional private banks. “Priests are better for that.”

Wegelin & Co - 04/01/2013

Reuters 04/01/2013:

- ❖ Wegelin & Co, the oldest Swiss private bank closed the doors permanently after more than 2 1/2 centuries, following its guilty plea to charges of helping wealthy Americans evade taxes through secret accounts. The plea, in U.S. District Court in Manhattan, marks the death knell for one of Switzerland's most storied banks, whose original European clients pre-date the American Revolution.
- ❖ Wegelin admitted to charges of conspiracy in helping Americans evade taxes on at least \$1.2 billion for nearly a decade. Wegelin agreed to pay \$57.8 million to the United States in restitution and fines.
- ❖ In addition, three Wegelin bankers were indicted in January 2012.
- ❖ In 2012, the U.S. government separately seized more than \$16 million of Wegelin funds in a UBS AG account in Stamford, Connecticut, via a civil forfeiture complaint. Since Wegelin has no branches outside Switzerland, it used UBS for correspondent banking services, a standard industry practice, to handle money for U.S.-based clients. In court papers, Wegelin's president Bruder said that Wegelin "believed it would not be prosecuted in the United States for this conduct because it had no branches or offices in the United States and because of its understanding that it acted in accordance with, and not in violation of, Swiss law and that such conduct was common in the Swiss banking industry."

IRS Voluntary Disclosure Alternatives

- 2012 Offshore Voluntary Disclosure Initiative
- FS-2011-13, December 2011
- 2012 Streamlined Filing Compliance Procedures for Non-Resident, Non-Filing U.S. Taxpayers
- 2014 OVDP and New Streamlined Procedures for Non-Resident and Resident US Taxpayers



Voluntary Disclosure

Under the terms of the 2014 Offshore Voluntary Disclosure Initiative, taxpayers must:

- File amended or original returns for the last 8 years of non compliance (2006-2013);
- File amended or original FBARs for same period;
- Pay 20% accuracy-related penalties on the full amount of underpayments of tax for all years;
- Pay an FBAR penalty of 27.5% or 50% of the highest balance in the undeclared bank accounts or value of foreign assets which had a tax liability during the period covered by the voluntary disclosure;
- Cooperate in the voluntary disclosure process, including providing information on offshore financial accounts, institutions and facilitators.



OVDI – CIVIL PENALTIES AVOIDED

Depending on a taxpayer's particular facts and circumstances, the following civil penalties could apply:

- A penalty for failing to file the **FBAR** form. Generally, the civil penalty for willfully failing to file an FBAR can be as high as the greater of \$100,000 or 50% of the total balance of the foreign account per violation. Ty Warner penalty was \$55,552,248 i.e., 50% of the highest balance.

Non-willful violations that the IRS determines were not due to reasonable cause are subject to a maximum \$10,000 penalty per violation.

- A penalty for failing to file **Form 3520**, Annual Return to Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts. The penalty for failing to file this information return, or for filing an incomplete return, is 35% of the gross reportable amount, except for returns reporting gifts, where the penalty is 5% of the gift per month, up to a maximum penalty of 25% of the gift.

- A penalty for failing to file **Form 3520-A**, Information Return of Foreign Trust With a U.S. Owner. Taxpayers must also report ownership interests in foreign trusts, by United States persons with various interests in and powers over those trusts. The penalty for failing to file this information return or for filing an incomplete return, is 5% of the gross value of trust assets determined to be owned by the United States person.

CIVIL PENALTIES AVOIDED

- A penalty for failing to file **Form 5471**, Information Return of U.S. Persons with Respect to Certain Foreign Corporations. The penalty for failing to file this information return is \$10,000, with an additional \$10,000 added for each month the failure continues beginning 90 days after the taxpayer is notified of the delinquency, up to a maximum of \$50,000 per return.
- A penalty for failing to 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. The penalty for failing to file this information return, or to keep certain records regarding reportable transactions, is \$10,000, with an additional \$10,000 added for each month the failure continues beginning 90 days after the taxpayer is notified of the delinquency.
- A penalty for failing to file **Form 926**, Return by a U.S. Transferor of Property to a Foreign Corporation. The penalty for failing to file is 10% of the value of the property transferred, up to a maximum of \$100,000 per return, with no limit if the failure to report the transfer was intentional.
- A penalty for failing to file **Form 8865**, Return of U.S. Persons With Respect to Certain Foreign Partnerships. Penalties include \$10,000 for failure to file the return, with an additional \$10,000 added for each month the failure continues beginning 90 days after the taxpayer is notified of the delinquency, up to a maximum of \$50,000 per return, and 10% of the value of any transferred property that is not reported, subject to a \$100,000 limit.

CIVIL PENALTIES AVOIDED

- Fraud penalties imposed under IRC § 6651(f) or 6663. Where an **underpayment of tax**, or a failure to file a tax return, is due to fraud, the taxpayer is liable for penalties that amount to 75% of the unpaid tax.
- Forfeiture** of all the funds under IRC § 981(a)(1)(A) (in addition to FBAR penalty) (US versus \$12,234,647.79)
- A penalty for failing to file a tax return imposed under IRC § 6651(a)(1). Generally, taxpayers are required to **file income tax returns**. If a taxpayer fails to do so, a penalty of 5% of the balance due, plus an additional 5% for each month or fraction thereof during which the failure continues may be imposed. The penalty shall not exceed 25%.
- A penalty for failing to pay the amount of tax shown on the return under IRC § 6651(a)(2). If a taxpayer **fails to pay the amount of tax** shown on the return, he or she may be liable for a penalty of 0.5% of the amount of tax shown on the return, plus an additional 0.5% for each additional month or fraction thereof that the amount remains unpaid, not exceeding 25%.
- An accuracy-related penalty on underpayments imposed under IRC § 6662. Depending upon which component of the accuracy-related penalty is applicable, a taxpayer may be liable for a 20% or 40% penalty.

OVDI – CRIMINAL PENALTIES AVOIDED

- Possible criminal charges related to tax returns include:
 - **Tax evasion** (26 U.S.C. § 7201). A person convicted of tax evasion is subject to a prison term of up to five years and a fine of up to \$250,000
 - **Filing a false return** (26 U.S.C. § 7206(1)). Filing a false return subjects a person to a prison term of up to three years and a fine of up to \$250,000.
 - **Failure to file** an income tax return (26 U.S.C. § 7203). A person who fails to file a tax return is subject to a prison term of up to one year and a fine of up to \$100,000.
 - **Willfully failing to file an FBAR and willfully filing a false FBAR** are both violations that are subject to criminal penalties under 31 U.S.C. § 5322. Willfully failing to file an FBAR subjects a person to a prison term of up to ten years and criminal penalties of up to \$500,000.

Green Card consequences of non compliance

- Under the EB-5 process an applicant is granted “conditional permanent residence” for a two year period. At the end of the two year period assuming that the conditions of the visa have been met, the applicant can become a permanent resident. For EB-5 visa holders, the failure to file FBAR’s could be asserted as a failure to comply with U.S. law and be a reason for denial of the Application to remove the two year condition to become a permanent resident
- Lawful permanent residents who have pled guilty to charges related to the filing of false tax returns that resulted in a loss to the government of more than \$10,000 have committed aggravated felonies involving fraud or deceit and are subject to deportation (Kawashima v. Holder)



Voluntary Disclosure – Why:

- Avoid severe civil and criminal penalties
- The ability of a U.S. taxpayer to maintain a “secret” foreign financial account is fast becoming nonexistent.
- Foreign account information is flowing into the IRS through :
 - The worldwide deployment of civil and criminal tax enforcement resources;
 - The development of relationships with corresponding taxing agencies in other countries;
 - Treaty-based information exchanges;
 - The use of the civil summons process to seek the identification of account holders in foreign institutions operating within the jurisdiction of the United States;
 - Indictments and investigations of foreign institutions and their bankers such as UBS (\$780 Million fine) and Credit Suisse in Switzerland (\$2.6 Billion fine), HSBC in India and Singapore and branches of foreign banks in Switzerland;
 - The receipt of information from whistleblowers and informants;
 - Cooperation from taxpayers, advisers, foreign banks, and bankers who have been criminally prosecuted;
 - Cooperation from taxpayers from OVDP participants who identified their banks, bankers, advisers, and others; and
 - FATCA regulations



Voluntary Disclosure – other jurisdictions

Germany:



Bayern Munich president Uli Hoeness was sentenced to three and a half years of prison after hiding around €3.2 million in a Swiss bank account.

Austria, Italy, Israel, the Netherlands, United Kingdom

Criminal prosecution of Swiss bankers

March 2014 – Andreas Bachmann, Credit Suisse banker pled guilty

Nov. 18, 2011 — Renzo Gadola, a citizen and resident of Switzerland, was sentenced to five years probation. Gadola pleaded guilty in December 2010 to assisting an American client in concealing an offshore bank account from the United States government. From 1995 through August 2008, he was employed as a private banker by UBS AG.

Aug. 4, 2011 — Gian Gisler, a former UBS AG banker, was charged with conspiring to hide more than \$215 million offshore at various Swiss banks. Gisler had more than 38 U.S. taxpayer clients and allegedly opened and/or managed more than 60 hidden accounts on their behalf.

Aug. 2, 2011 — Martin Lack, a former UBS AG banker was charged with conspiracy to defraud the United States. Lack assisted U.S. customers to open and maintain secret bank accounts at a Swiss cantonal bank headquartered in Basel, Switzerland.

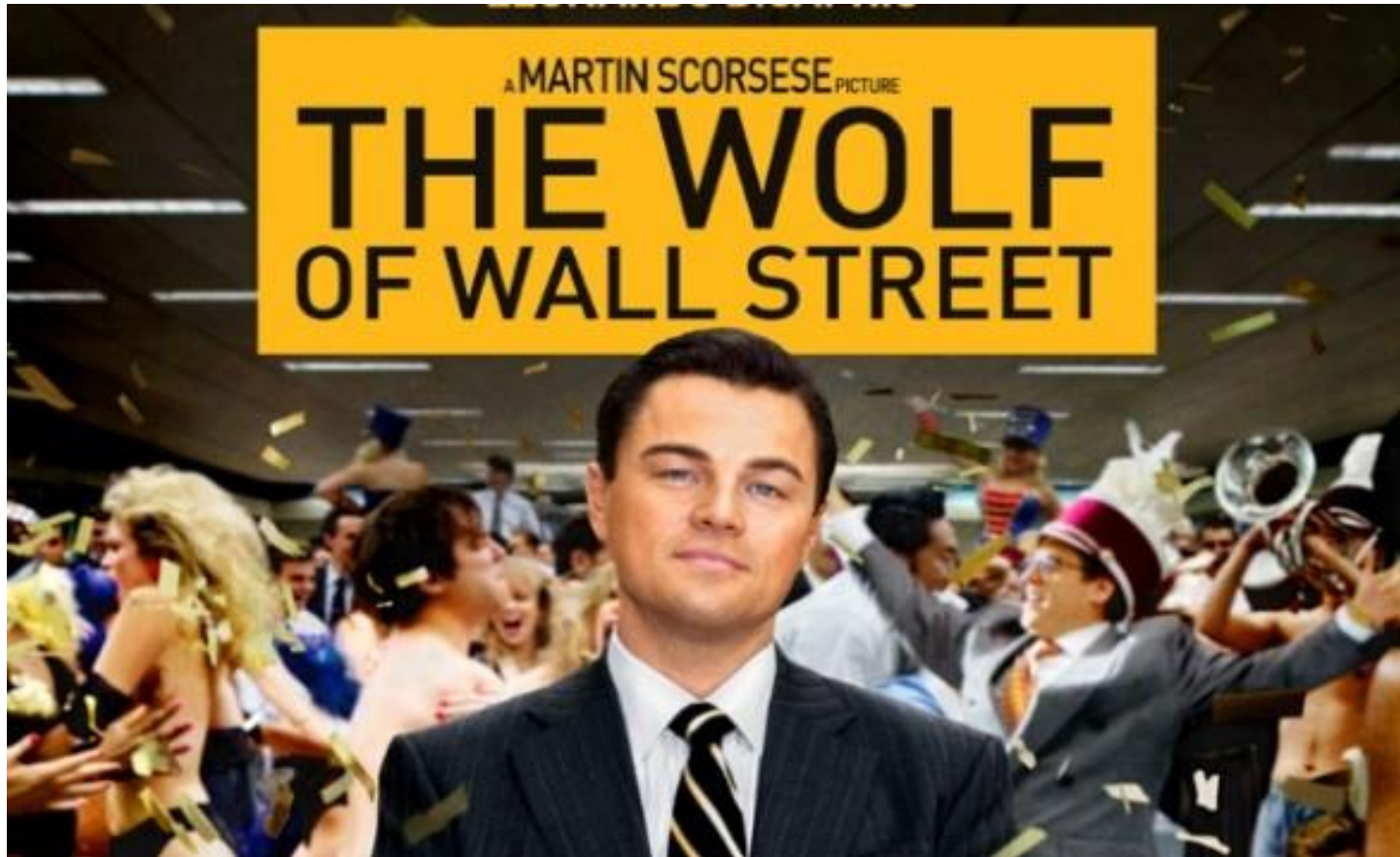
July 21, 2011 — Beda Singenberger, a Swiss financial advisor, was indicted for conspiring with U.S. taxpayers and others to hide more than \$184 million in offshore Swiss bank accounts.

Aug. 20, 2009 — Hansruedi Schumacher and Matthias Rickenbach were indicted for conspiring to assist wealthy American clients conceal their assets by establishing sham offshore entities. Schumacher was an executive manager at Neue Zuercher Bank (NZB), a private Swiss bank. Rickenbach was a Swiss attorney who advised U.S. clients.

Nov. 12, 2008 — Raoul Weil, a senior executive of a large Swiss bank, was charged with conspiring with other executives, managers, private bankers and clients of the banking firm to defraud the United States. On October 19, 2013, Weil was arrested in Bologna, Italy while on vacation and extradited to the USA.

May 13, 2008 — Banker Mario Staggl was indicted for conspiring with banker Bradley Birkenfeld to assist an American billionaire real estate developer evade paying \$7.2 million in taxes by assisting in concealing \$200 million of assets in Switzerland and Liechtenstein.

Criminal prosecution of Swiss bankers



Jean-Jacques Handali (a/k/a/ Jean Jacques Saurel in The Wolf of Wall Street) of UBP Geneva

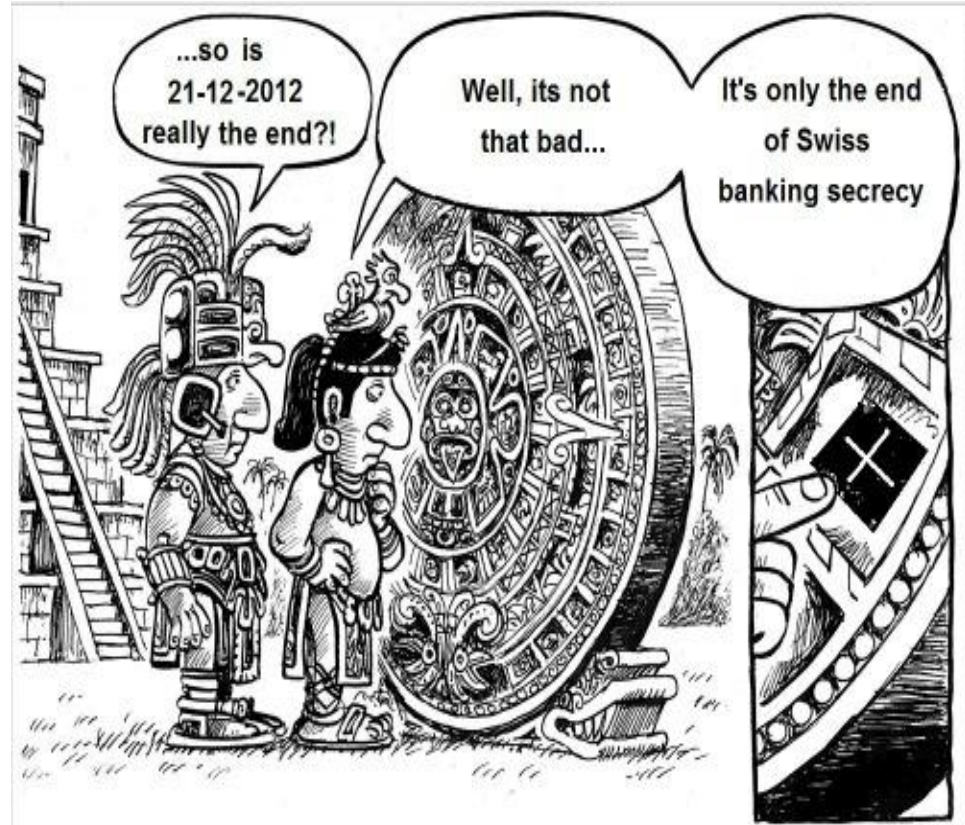
Criminal prosecution of banks

August 2013: Liechtensteinische Landesbank AG will pay \$23.8 million to U.S. authorities in order to avoid prosecution for its role in helping American clients violate federal tax law. The bank was found guilty of helping account holders maintain secret accounts between 2001 and 2011. However, the company was largely able to make a deal with U.S. authorities after it began cooperating in 2008 by handing over information on clients and helping change Liechtenstein secrecy laws, according to Forbes.

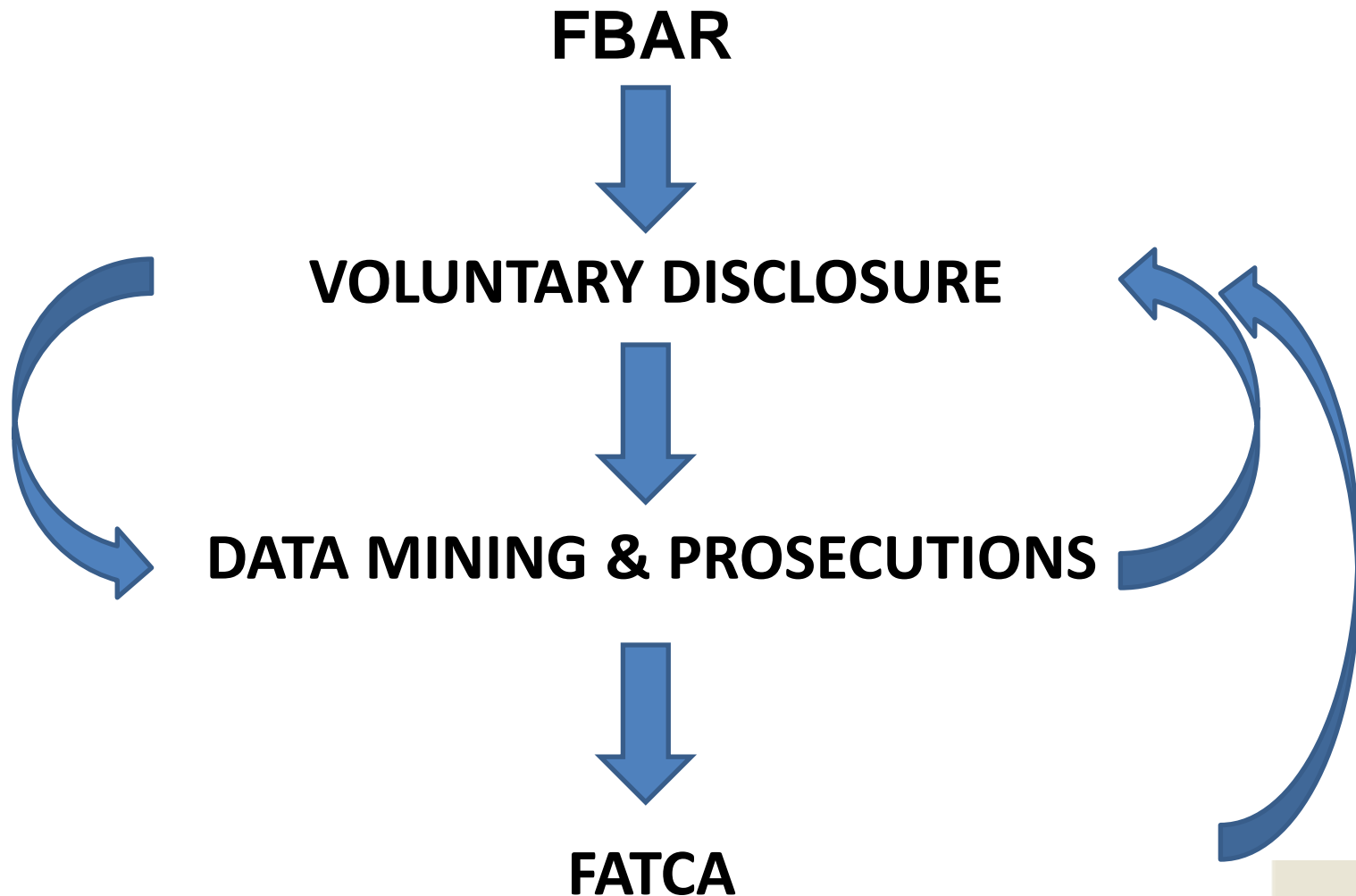
September 2013: Rahn & Bodmer Co., the Swiss private bank established by silk traders in 1750, said it's cooperating with a U.S. Department of Justice probe into cross-border accounts of American clients. The bank was probably named by its own clients participating in a U.S. initiative for the voluntary disclosure of offshore assets, according to Christian Rahn, a partner.

Rahn & Bodmer is part of a group of Swiss financial firms under investigation by the Department Of Justice or allegedly helping U.S. clients hide money from the Internal Revenue Service. The group of 14 includes Credit Suisse Group AG, the nation's second-biggest bank, wealth manager Julius Baer Group Ltd. and the Swiss unit of HSBC Holdings Plc., Bank Frey, the Swiss branches of banks and certain Kantonal banks such as the Basler Kantonalbank and Zürcher Kantonalbank.

Criminal prosecution of banks



Voluntary Disclosure – WHY:



FATCA

The Foreign Account Tax Compliance Act or FATCA, as it is colloquially known, was enacted by the Hiring Incentives to Restore Employment Act on March 18, 2010.

FATCA for individuals:

U.S. persons owning foreign accounts or other specified financial assets must report them on a new Form 8938 which is filed with the person's U.S. tax returns if they are generally worth more than US\$50,000; a higher reporting threshold applies to overseas residents.

It also requires taxpayers to report financial assets that are not held in a custodial account, e.g., income deriving real estate, physical stock or bond certificates.



FATCA

FATCA for corporations:

FATCA requires non-US financial institutions ("FFIs") and non-US non-financial entities ("NFFEs") to identify and disclose their US account holders or become subject to a new 30% US withholding tax with respect to payments of US source income such as interest, dividends, rents, salaries ("FDAP Income") and gross proceeds from the sale or disposition of US stocks and securities.

Banks

Hedge Funds / Investment Companies

Pension Funds

Insurance Companies

In addition to complying with the reporting and diligence procedures, a participating FFI is required to withhold 30% of any "passthru" payments that it makes to "recalcitrant" account holders or nonparticipating FFIs.



FATCA

FATCA for corporations:

Full implementation in 2018, including:

- ✓ Registration with the IRS for Global Intermediary Identification Number
- ✓ Identification of accounts for existing customers
- ✓ Revised account opening procedures to identify new US accounts
- ✓ Withholding on non participating banks and institutions
- ✓ Reporting of compliant and non compliant accounts

FATCA

For participating FFIs, investments will be needed in four key areas:

Documentation: capturing process changes and analyzing the customer base.

Withholding: building systems for withholding on recalcitrant account holders.

Reporting: building and sustaining an annual reporting model for all US individuals to cover account balances and gross payments.

Legal: review all documentation like operating and lending agreements

The United States Congress Joint Committee on Taxation estimated that the FATCA bill would raise \$792 million of additional taxes a year in the next ten years.

Estimate of the costs to the private sector alone has been roughly estimated at US\$8 billion a year, approximately ten times the amount of estimated revenue raised. The UK government has estimated that the cost to British businesses alone will be £1 billion - £2 billion for the first five years.

FATCA – Foreign Financial Institutions

A Foreign Financial Institution is defined as any foreign entity that:

- Accept deposits in the ordinary course of a banking or similar business;
- Hold financial assets for the account of others as a substantial portion of their business;
- Are foreign investment entities, including entities that conduct certain investment and asset management activities for customers, entities that are managed by other FFIs and the gross income of which is primarily attributable to investing, reinvesting, or trading in financial assets, and certain collective investment vehicles with investment strategies of investing, reinvesting, or trading in financial assets³;
- Are insurance companies that issue investment-like contracts or annuity contracts; or
- Are certain holding companies or treasury centers that are members of corporate groups that include FFIs or that are formed by certain investment vehicles.

The definition of an FFI is broad and includes entities that would not typically be considered to be financial institutions such as trust companies, investment funds, hedge funds, certain family investment vehicles, foreign feeder funds and insurance companies.



FATCA – Foreign Non Financial Institutions

A Non Foreign Financial Institution NFFE is any foreign entity that is not a financial institution.

A foreign entity is an entity that is not a “U.S. person”.

An NFFE generally will not be required to comply with the diligence and reporting requirements applicable to FFIs. However, in certain circumstances, an NFFE may be required to identify and make a certification to a withholding agent regarding US persons that own accounts or substantial interests in the NFFE.



FATCA - Financial Account

- Any deposit account maintained by a financial institution
- Any custodial account maintained by a financial institution
- Any cash value insurance contract and any annuity contract issued or maintained by a financial institution
- Some exceptions to the notion of financial account, e.g. (i) certain savings account, (ii) term life insurance contracts, (iii) account held by exempt beneficial owner.



FATCA - Withholding

New Account Opening Procedures. Withholding agents under FATCA generally will be required to implement the new FATCA account opening procedures by July 1, 2014.

Due Diligence on Pre-Existing Obligations. FATCA establishes that a "preexisting obligation" is an obligation that is outstanding on June 30, 2014.

First FATCA Information Report. The first deadline for FFIs to file FATCA information reports with the IRS is March 31, 2015 and will cover tax year 2014.

FATCA - Withholding

Payments of FDAP income will be subject to FATCA withholding from July 1, 2014.

Gross proceeds from the disposition of property that can produce US-source interest and dividends will only be subject to FATCA withholding for dispositions occurring after December 31, 2016.

FATCA will not apply, however, with respect to FDAP income derived from, and gross proceeds from a disposition of, any "**grandfathered obligations**"

FATCA - Reporting

FATCA requires a FFI to track and identify all U.S. money on behalf of the IRS. This includes ascertaining and disclosing to the IRS the:

- Name, Address and Tax Identification Number (TIN) of each account holder that is a U.S. person;
- Name, Address and TIN of each substantial U.S. owner of any account held by a U.S. owned foreign entity;
- Account number;
- Account balance or value; and
- Gross receipts and withdrawals/payments from the account.

Substantial U.S. owners of foreign entities include any U.S. person who owns directly or indirectly more than 10% beneficial interest in a company, partnership or trust.

FATCA - PASSTHRU PAYMENTS

A portion of any payment made by a FFI will be treated as a passthru payment, and therefore subject to 30% withholding, in proportion to the ratio of the FFI's U.S. assets to its total assets (the passthru percentage).

As the International Swaps and Derivatives Association (ISDA) notes:

“the passthru payment rules could potentially impose US withholding tax on an interest payment made by a British Bank's London office to a German Bank's Frankfurt office if the German Bank is a nonparticipating FFI and the British Bank is a participating FFI, provided the British Bank holds any US assets in any of its global offices. The FATCA withholding rate in such case is 30% times the passthru payment percentage of the British Bank. The passthru payment percentage is expected to be calculated at least annually by dividing an FFI's Total US Assets by the FFI's Total Assets (in each case determined on a global basis).”

FATCA - CONTROVERSY



**STOP
FATCA**
Protect our borders from USA laws



FATCA - CONTROVERSY

❑ Cost

❑ **Capital flight.** Strong incentive for foreign financial institutions to not invest in US assets to avoid 30% withholding

❑ **Foreign relations.** Forcing foreign financial institutions and foreign governments to collect data on US citizens at their own expense and transmit it to the IRS is controversial. *There are also reports of many foreign banks refusing to open accounts for Americans, making it harder for Americans to live and work abroad.*

❑ **Citizenship renunciations.** 1001 in first quarter of 2014, jump of 50% (Tina Turner). 2,999 in 2013 and over 4,000 expected in 2014

❑ **Workability:** Complexity and postponing of the implementation

FATCA - CONTROVERSY

Russia's VTB to ditch Russia-based U.S. taxpayer clients

June 5, 2014

Reuters: Russia's second-largest bank, VTB, said it is phasing out business with around 2,000 Russia-based individual and corporate clients that are U.S. taxpayers ahead of a new law to fight tax dodging by Americans.

State-controlled VTB said it registered with the IRS in order to maintain compliance with FATCA and would voluntarily abide by the legislation.

"However, as part of its prudent approach to managing risk, VTB's senior management has instructed the group's entities to gradually phase out business with clients, both individuals and legal entities, that are US taxpayers," VTB said.

VTB said it would phase out business with Russia-based U.S. taxpayer clients only; those based in the United States are not affected.

Even at this late stage, Russian law and FATCA are incompatible — Russian banks will be able to comply with U.S. law or Russian law, but not both, the head of the Association of Russian Banks said.

FATCA - CONTROVERSY

❑ Technology:

International Data Exchange System (IDES):

FATCA data to flow on time but what about:

- Encryption protocols?
- Transmission securely?
- Confidentiality?
- Use limited to tax issues?

FATCA - IGAs

The United States Department of Treasury has published model Intergovernmental Agreements (IGAs) which follow two approaches:

Under Model 1, financial institutions in the partner country report information about U.S. accounts to the tax authority of the partner country. That tax authority then provides the information to the United States.

Model 1 comes in a reciprocal version (Model 1A), under which the United States will also share information about the partner country's taxpayers with the partner country, and a nonreciprocal version (Model 1B).

Under Model 2, partner country financial institutions report directly the U.S. Internal Revenue Service, and the partner country agrees to lower any legal barriers to that reporting.



FATCA - IGAs

Jurisdictions that have signed agreements:

Model 1 IGA

Australia, Belgium, Canada, Cayman Islands, Costa Rica, Denmark, Estonia, Finland, France, Germany, Gibraltar, Guernsey, Hungary, Honduras, Isle of Man, Italy, Jamaica, Jersey, Luxembourg, Malta, Mauritius, Mexico, Netherlands, Norway, Spain, United Kingdom

Model 2 IGA

Austria, Bermuda, Chile, Japan, Switzerland

Jurisdictions that have reached agreements in substance:

Model 1 IGA

Azerbaijan, Bahamas, Brazil, British Virgin Islands, Bulgaria, Colombia, Croatia, Curaçao, Czech Republic, Cyprus, India, Indonesia, Israel, Kosovo, Kuwait, Latvia, Liechtenstein, Lithuania, New Zealand, Panama, Peru, Poland, Portugal, Qatar, Romania, Singapore, Slovak Republic, Slovenia, South Africa, South Korea, Sweden, Turks and Caicos Islands

Model 2 IGA

Armenia and Hong Kong

FATCA EFFECT



FATCA Effect

U.K. Banks refuse to do business with Americans

The Netherlands: Private wealth management firms ask American account holders to leave

Switzerland: Major banks close U.S. departments.

Other countries:

- ✓ U.S. persons preferred not to be directors in foreign companies.
- ✓ accounts frozen or closed
- ✓ sale of securities portfolio
- ✓ no release of money even after signing of W-9 statement and FATCA statement

FATCA Effect

United Kingdom:

Son-of-FATCA for British offshore financial centers

Financial details for 2014 and 2015 will have to be reported to the HMRC by September 30, 2016.

Crown dependencies and British overseas territories will have to tell the HMRC:

- Names and addresses and dates of birth of client holders
- Account numbers
- Balances and details of payments made into those accounts

The financial centers covered include the Isle of Man, Guernsey, Jersey, Anguilla, Bermuda, the British Virgin Islands, the Cayman Islands, Gibraltar, Montserrat and the Turks and Caicos Islands.

FATCA Effect - China

South China Morning Post 南華早報

Monday, 12 May, 2014: Fatca dealt with, but clones of tax evasion law may emerge

Since many Hong Kong-based financial firms and private banks are targeting wealthy mainlanders as clients, they could be severely affected if China introduces its own version of Fatca.

The implications for their reporting and compliance efforts would be even broader than in the case of Fatca, because of the numbers involved.

In March, China's deputy tax commissioner, Zhang Zhiyong, said the mainland needed to step up its international tax collection efforts and to take part in the international exchange of information to curb cross-border tax evasion.

The Hong Kong government may now need to turn its lobbying efforts, successful in the case of the US, towards Beijing for exemptions from a Chinese Fatca.



FATCA Effect - China

Order of the PRC State Council No. 642 outlining the "Decision of the State Council on Amending the Measures for Reporting of Statistics on International Receipts and Payments".

Reporting requirements under Circular 642 are imposed on PRC Residents, as well as non-PRC residents carrying out economic activities within the PRC.

WHO ARE PRC RESIDENTS:

- Individuals residing in the PRC for one year or more
- PRC nationals staying abroad for a period of less than one year;
- PRC incorporated enterprises (including foreign-invested enterprises and foreign-invested financial institutions);
- Representative offices and branches of foreign legal persons (excluding the offices of international organizations, Embassies and Consulates); and
- PRC state authorities (including PRC Embassies and Consulates abroad), PRC organizations

WHAT:

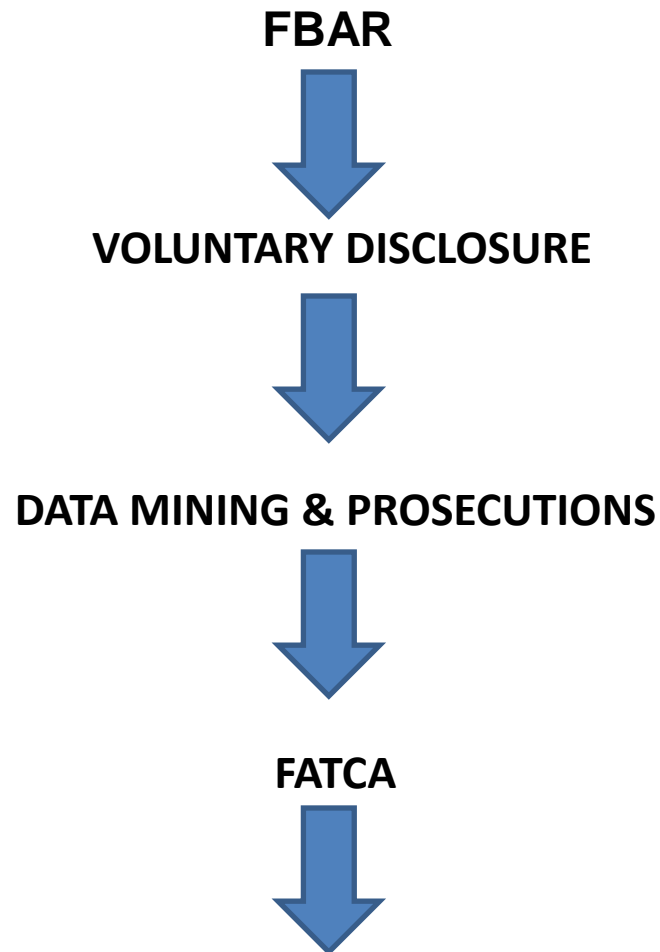
- Economic transactions between PRC residents and non-PRC residents
- The status of foreign financial assets and liabilities of the PRC

FATCA Effect - China - Circular 642

Non-PRC residents carrying out economic activities within the PRC:

- Foreigners buying real estate in China?
- Foreigners investing in China?
- Foreigners providing consulting services in China?

FATCA Effect: From FBAR to the OECD



TAX INFORMATION EXCHANGE AGREEMENTS

Tax Information Exchange

Bilateral:

Double Taxation Agreements (DTA):

- Clause in agreement to prevent double taxation
- OECD Model Convention
- UN Committee of Tax Experts Model Convention
- Nordic Countries : Denmark, Faroe Islands, Finland, Iceland, Norway and Sweden. Automatic exchange on income and ownership of real estate
- Mexico and U.S.A. : Non-US resident interest income
- Switzerland and U.K.: Swiss authorities are set to implement an agreement for a monthly exchange of information to the UK tax authorities. The agreement signed in April 2012 calls on the Swiss authorities to provide information on income and gains derived from investments held by UK taxpayers in Swiss banks.
- Tax authorities of the U.S.A., the United Kingdom and Australia have announced a plan to share tax information involving companies and trusts holding offshore assets of taxpayers under their respective jurisdictions.

OECD MODEL TAX CONVENTION ON INCOME AND CAPITAL

Article 26 EXCHANGE OF INFORMATION

1. The competent authorities of the Contracting States shall exchange such information as is foreseeable relevant for carrying out the provisions of this Convention or to the administration or enforcement of the domestic laws concerning taxes of every kind and description imposed on behalf of the Contracting States, or of their political subdivisions or local authorities, insofar as the taxation there under is not contrary to the Convention. The exchange of information is not restricted by Articles 1 and 2.

2. Any information received under paragraph 1 by a Contracting State shall be treated as secret in the same manner as information obtained under the domestic laws of that State and shall be disclosed only to persons or authorities (including courts and administrative bodies) concerned with the assessment or collection of, the enforcement or prosecution in respect of, the determination of appeals in relation to the taxes referred to in paragraph 1, or the oversight of the above. Such persons or authorities shall use the information only for such purposes. They may disclose the information in public court proceedings or in judicial decisions.

3. In no case shall the provisions of paragraphs 1 and 2 be construed so as to impose on a Contracting State the obligation:

- a) to carry out administrative measures at variance with the laws and administrative practice of that or of the other Contracting State;
- b) to supply information which is not obtainable under the laws or in the normal course of the administration of that or of the other Contracting State;
- c) to supply information which would disclose any trade, business, industrial, commercial or professional secret or trade process, or information the disclosure of which would be contrary to public policy (ordre public).

4. If information is requested by a Contracting State in accordance with this Article, the other Contracting State shall use its information gathering measures to obtain the requested information, even though that other State may not need such information for its own tax purposes. The obligation contained in the preceding sentence is subject to the limitations of paragraph 3 but in no case shall such limitations be construed to permit a Contracting State to decline to supply information solely because it has no domestic interest in such information.

5. In no case shall the provisions of paragraph 3 be construed to permit a Contracting State **to decline to supply information solely because the information is held by a bank**, other financial institution, nominee or person acting in an agency or a fiduciary capacity or because it relates to ownership interests in a person.

Tax Information Exchange

Bilateral:

- Tax Information Exchange Agreement (TIEA)
 - Complement DTAs
 - For use with countries for which there is no DTA because for example they have no or low taxes on income
 - Usually narrower in scope than DTAs but more detailed on the exchange of information
 - The more the better, less regarded as tax haven: UK Crown dependencies (Isle of Man, Jersey and Guernsey) with Danish Crown Dependencies: Greenland and Faroe Islands
- Mutual Legal Assistance in Criminal Matters
 - some exclude tax matters
- U.S. Qualified Intermediary (QI)
 - Foreign QI needs to report to the USA about U.S. persons investing in the U.S.A. through that QI

Tax Information Exchange

Multilateral:

- European Union's Savings Directive
 - Limitations: only interest
 - Automatic exchange
 - Opt out of information exchange and withholding tax for some jurisdictions such as Austria, Belgium, and Luxembourg.

- The Convention on Mutual Administrative Assistance in Tax Matters
 - Counsel of Europe and OECD
 - More than 50 countries have signed

- European Union finance ministers meeting of September 13 and 14
 - European Union finance ministers met to discuss a system for an EU-wide automatic exchange of bank account information, among other issues.

Tax Information Exchange

- G-20 meeting of September 5 and 6, 2013
 - Endorsement of OECD proposal for global model for automatic information exchange for tax purposes.
 - Automatic sharing of tax information by the end of 2015
 - China was last one to sign

- OECD's Common Reporting Standard
 - 44 countries
 - Declaration on Automatic Exchange of Information in Tax Matters
 - Committed to the new single global standard for the automatic exchange of information between tax authorities as established in G-20 meeting September 2013
 - The information on new accounts and pre-existing individual high-value accounts will be exchanged by the end of September 2017
 - All other account information will be exchanged by the end of September 2018

Automatic Exchange of Information

Shift to an international standard on automatic exchange of tax information has been accelerated by FATCA

Automatic exchange of information involves the systematic and periodic transmission of “bulk” taxpayer information by the source country to the residence country concerning various categories of income (e.g. dividends, interest, royalties, salaries, pensions, etc).

It can provide timely information on non-compliance where tax has been evaded either on an investment return or the underlying capital sum even where tax administrations have had no previous indications of non-compliance.

Automatic Exchange of Information

The information which is exchanged automatically is normally collected in the source country on a routine basis, generally through reporting of the payments by the payer (financial institution, employer, etc).

Automatic exchange can also be used to transmit other types of useful information such as changes of residence, the purchase or disposition of immovable property, value added tax refunds, etc.

Information may be transmitted electronically or by CD ROMs. If the CD ROMs are sent by mail, it must be done via an international registration system where a mail tracking function is in place.

Automatic Exchange of Information

1. Payer or paying agent collects information from the taxpayer and/or generates information itself .
2. Payer or paying agent reports information to the tax authorities.
3. Tax authorities consolidate information by country of residence.
4. Information is encrypted and bundles are sent to residence country tax authorities.
5. Information is received and decrypted.
6. Residence country feeds relevant information into an automatic or manual matching process.
7. Residence country analyses the results and takes compliance action as appropriate.

Butterfly Effect



Butterfly Effect

FBAR



VOLUNTARY DISCLOSURE



DATA MINING & PROSECUTIONS



FATCA



TAX INFORMATION EXCHANGE AGREEMENTS

Butterfly Effect – FATCA as a new Global Standard

How one small tax form is changing the world of International Taxation, Finance and Banking

- 100 Swiss banks sign agreement to hand over information to a third country
- Americans are persona non grata in the world of banking and company management
- Criminal prosecution in several countries because of data sharing
- FATCA has global effect from fund managers in Kuwait until banks in Greenland
- Tax havens no longer tax havens
- New industry providing FATCA services such as consultants, lawyers, accountants and software companies

From FBAR to Twice Cooked Pork (回鍋肉):

FBAR



FATCA



Investments in the U.S.A.



Shuanghui's \$7.1 billion takeover of pork processor Smithfield



回鍋肉



回鍋肉 a/k/a FATCA consequences for China

Corporations:

➤ U.S. investments in China

- Signatory authority for a U.S. tax payer?
- U.S. director?
- Registration and Reporting to the IRS
- Reporting to Chinese Authorities

➤ Chinese investments in the U.S.A.

- Fatca withholding taxes
- Reporting by the IRS to China about US accounts/investments?
- Compliance costs

➤ Joint Venture with US corporation in third country

- Fatca withholding taxes
- Reporting to the IRS and subsequently to China about the investments
- Risk that one non-participating FFI in a series of transactions could cause other FFIs to incur 30% withholding tax.

回鍋肉 a/k/a FATCA consequences for China

Individuals:

- EB5 immigration: pre immigration tax planning, wealth management, estate tax, PFICs, FBARs.
- Green card holders/citizens in the USA or China: comply with FBAR and FATCA
- Reporting by the IRS to China about US accounts/investments

回鍋肉

Worldwide automatic exchange of information:

Hong Kong

Singapore

Switzerland

U.S.A.

European Union

FATCA – FOR LAWYERS

- ✓ Escrow accounts for American clients
- ✓ Escrow account for non American clients if Trustee is American
- ✓ Company bank accounts
- ✓ Signatory authority for U.S. employees?
- ✓ Due Diligence on ultimate beneficiary?
- ✓ Clients to apply for FATCA GIIN numbers or avoid doing business with the U.S.A.?
- ✓ Avoid assisting tax evasion, e.g. buying real estate with clients' undeclared funds
- ✓ More paperwork in different jurisdictions
- ✓ Have you assisted U.S. clients opening bank accounts outside the U.S.A .e.g., Hong Kong, Singapore, Switzerland, Luxembourg, Liechtenstein

FATCA – FOR COMPLIANCE OFFICERS

FATCA RESPONSIBLE OFFICER (FRO):

- ✓ Learning curve of complex intricacies of FATCA
- ✓ Coordination between legal, operations, tax, accounting and technology departments; Coordination between CEO, COO, CFO, CLO etc.
- ✓ Review legal documents such as operating agreements;
- ✓ Personal liability: Model 1, possibly. Model 2: yes
 - ❖ US\$250,000 and 3 years in jail
 - ❖ Indemnification by FFI
- ✓ Outsource/outside counsel?
- ✓ FRO ≠ US person: Form 5471 → disclosure of FFI's ownership

Butterfly Effect

Baidu \$300 million R&D center in Silicon Valley with 200 employees:

- ✓ Chinese employees relocated to California are subject to US federal and state worldwide taxation
- ✓ Chinese employees relocated to California are subject to FBAR reporting for their own and corporate accounts and other financial assets such as income deriving real estate, companies etc.
- ✓ Payments from the USA to PRC subject to FATCA regulations and possible withholding tax if applicable

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