

Treasury Announces Regulations to Address Use of U.S. LLCs to Disguise Beneficial Ownership

April 5, 2016

In a statement issued on March 30th, the U.S. Treasury Department announced that it will soon be issuing proposed regulations that will require foreign-owned, single-member LLCs to disclose to the IRS their beneficial owners. *Penalties could be significant for continued non-compliance, and information regarding foreign beneficial ownership will likely be shared with foreign tax authorities.*

The regulations are likely in response to the growing view of the United States as a tax haven for foreigners seeking to evade their foreign tax obligations or otherwise conceal their holdings. In particular, laws in states such as Delaware that permit LLCs to register without disclosing their beneficial ownership have been subject to international criticism. The United States has also been criticized for pressuring other countries to implement the Foreign Account Tax Compliance Act (“FATCA”), which requires foreign financial institutions to report to the IRS regarding accounts with direct or indirect U.S. beneficial ownership, while failing to enact legislation that would require American banks to collect and disclose reciprocal information to foreign countries and refusing to sign on to the more wide-reaching Common Standard on Reporting and Due Diligence for Financial Account Information proposed in 2014 by the OECD. In its March 30th statement, the Treasury Department noted that one purpose of the new regulations will be to assist foreign countries in obtaining information regarding their own taxpayers under the United States’ tax treaties and tax information exchange agreements.

The new regulations will be issued under section 6038A of the Internal Revenue Code, which requires certain foreign-owned U.S. corporations to file a Form 5472 disclosing the identity of their foreign owners and reporting certain related-party transactions. The filing requirement generally applies where more than 25% of the voting power or value of all classes of stock are owned by a single foreign owner. The announcement indicates that this filing requirement will be extended to foreign-owned, single-member LLCs, by treating LLCs as corporations solely for the purposes of section 6038A. This will require such LLCs to obtain U.S. taxpayer identification numbers and report the identity of their foreign owners to the IRS, even if they own no U.S. assets and generate no U.S.-source income. Failing to file the Form 5472 can result in a \$10,000 penalty, with additional incremental penalties of \$10,000 if the failure continues for more than 90 days after the taxpayer is notified by the IRS. There is no cap on the total penalty, so a persistent refusal to comply with the filing requirement could result in significant penalties.

The new regulations are part of a trend in the U.S. toward expanding scrutiny and increasing transparency as to foreign investors who may be using more relaxed federal or state law to conceal beneficial ownership. For example, the U.S. Financial Crimes Enforcement Network (“FinCEN”) recently adopted new rules requiring enhanced scrutiny of all cash purchases of high-end real estate in New York and Miami, requiring the identification of beneficial owners. Wealth advisors and private client professionals around the world should be mindful of these

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U.S. efforts and of the now clear intention of the U.S. to collect and share information about foreign investors with other tax authorities. Moreover, advisors and practitioners here should be increasingly diligent about foreign clients transferring assets into the U.S., as the Justice Department has longstanding power to charge Americans with criminal fraud or even money laundering if they knowingly facilitate in the evasion of foreign tax.

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