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PRACTICING EXCLUSIVELY IN:

ESTATE & GIFT TAX PLANNING

ASSET PRESERVATION PLANNING

WILLS & TRUSTS

BUSINESS STRUCTURING &
SUCCESSION PLANNING

DOMESTIC & INTERNATIONAL TAX PLANNING

PROBATE & TRUST ADMINISTRATION

SPECIAL NEEDS PLANNING

2010 TAX COMPLIANCE MEMORANDUM

The purpose of this memorandum is to outline the tax compliance matters you will need to attend to regarding the estate planning or corporate work we have structured for you. Upon the creation of a foreign trust or other type of entity (including but not limited to a foreign corporation), or a domestic trust which contains provisions to become a foreign trust, and at other intervals during the existence of those trusts, there are various informational and tax return filing requirements imposed by the Internal Revenue Service (“IRS”) on the parties connected to the trust or other entity. This memorandum briefly explains the various potential filing requirements for a foreign trust, foreign corporation, or other type of foreign business entity, as well as for a settled trust that may in the future become a foreign trust. This memorandum is not intended to take the place of competent advice from an accountant, tax return preparer, or other tax professional experienced in the filing of tax and informational returns relating to international transactions, but only to put you on notice of filings that may be required. Failure to comply with these reporting requirements may subject the fiduciary, grantor, settlor, and/or the beneficiary(ies) to possible civil penalties, and in some cases, if the failure to file is intentional, criminal penalties. It is highly recommended that professional advice be sought and adhered to in complying with the IRS requirements regarding your activities.

INITIAL FILING REQUIREMENTS

<u>Form</u>	<u>Description</u>
56	<u>Notice of Fiduciary Relationship.</u> To be filed by the fiduciary (i.e., Trustee, Executor, Personal Representative, or other fiduciary) to advise and inform the IRS of the creation or termination of a fiduciary relationship. The settling of a trust creates a fiduciary relationship. Consult your tax professional for applicability of this form to you.
8832	<u>Entity Classification Election.</u> Form 8832 Entity Classification Election generally need not be filed by foreign trusts. However, because they are associated with other foreign business entities, such as a foreign corporation or limited liability company, you should review this form carefully. It is very important to note that for foreign entities the default rules are often exactly the opposite of domestic default rules. Under the foreign regime, a limited liability company will be treated as a corporation unless the owner elects to have it treated as a disregarded entity. This rule operates similarly for multiple member limited liability companies. They will be treated as corporations unless an election is made for them to be treated as a partnership. Generally Form 8832 must be filed within 75 days of

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the entity's creation. The IRS has established late election relief provided the election is made, in general, before the due day of the entity's tax return. A copy should also be attached to the owner's income tax return for the year the election is made. Consult your tax professional for applicability of this form to you.

W-8 Certificate of Foreign Status. If the trust is a "foreign trust" for U.S. tax purposes or a business entity is considered "foreign" for U.S. tax purposes, the trust or business entity should file form W-8 with the payors of certain U.S. source income. Consult your tax professional for applicability of this form to you.

W-8BEN Certificate of Foreign Status of Beneficial Owner for United States Tax Withholding. In certain circumstances, the beneficial owner of a foreign trust or other non-U.S. person must disclose to payors the basis claimed for the non-application of federal income tax withholding, if applicable. In the event this form is not provided, or if there is no exception from tax withholding, payors will be required to withhold, generally at the rate of thirty (30) percent. Consult your tax professional for applicability of this form to you.

W-8ECI Certificate of Foreign Person's Claim for Exemption From Withholding on Income Effectively Connected with the Conduct of a Trade or Business in the United States. Foreign persons with income which is effectively connected with the conduct of a trade or business in the United States may claim certain benefits so as to not have the U.S. tax withholding apply. Consult your tax professional for applicability of this form to you.

W-8EXP Certificate of Foreign Government or Other Foreign Organization for United States Tax Withholding. Certain international organizations, foreign central banks of issue, foreign governments, and foreign tax-exempt organizations may claim certain benefits so as to not have the U.S. tax withholding rules apply. Consult your tax professional for applicability to you.

W-9 Request for Taxpayer Identification Number and Certification. If the trust is considered to be either a "grantor" trust or a U.S. trust for U.S. tax purposes, form W-9 should be used instead of form W-8. Consult your tax professional for applicability of this form to you.

ANNUAL FILING REQUIREMENTS

709 U.S. Gift Tax Return. Form 709 is required to be filed for transfers of assets to a foreign trust. Treas. Reg. § 25.2511-2(b) and (j) requires the grantor of a trust to file a Form 709 even where transfers are not completed gifts. Also, if you make a transfer to a person (in or outside of the U.S.) that is not for their medical or educational expenses or payments to political organizations, or gifts to nonresident alien spouses in excess of \$103,000 per year, the gifts must be reported on Form 709. Consult your tax professional for applicability of this form to you.

3520 Annual Return to Report Transactions with Foreign Trusts and Receipt of Certain Foreign Gifts. Form 3520 must be filed by US persons who either own, directly or indirectly, an interest in a foreign trust or who transferred money to such a trust. Must be filed on an annual basis. It is due when the income tax return of the responsible party is due, including extensions. Consult your tax professional for applicability of this form to you.

3520-A Annual Information Return of Foreign Trust with a U.S. Owner. Form 3520-A must be filed by each trust that has a U.S. owner. Please note that the trust, and not the grantor or

any beneficiary, must be the filer of the return. Must also be filed together with the Grantor's (or Transferor's) annual federal income tax return, or sooner if the trust's tax year ends on December 31st, in which case the 3520-A return is due no later than March 15th. Extensions to file income tax returns extend the time to file these forms except that with the 3520-A Form, the Form 2758 must be filed in order to obtain an extension to file Form 3520-A. The extension date is September 15 of the following tax year. The determination of whether or not a trust is considered "foreign" for U.S. tax purposes should be discussed with a tax professional. This form must be filed for each foreign trust. This form requires disclosure of the name, addresses, and taxpayer identification numbers and data of the fiduciary (trustee), the U.S. Limited Agent, and the grantor(s) and beneficiaries of the trust. It also requests information relating to the percentage interests of the beneficiaries, amount of cash and value of other property transferred to and from the foreign trust, and the location of the foreign trust's books and records. This form is filed both with the IRS Service Center in Philadelphia, Pennsylvania, and the district IRS office where the grantor(s) files his or her income tax return. The failure to file form 3520-A carries a civil penalty equal to 5% of the value of the trust. Further, there are criminal penalties imposed upon the US person for the failure to file form 3520-A. Consult your tax professional for applicability of this form to you.

TDF 90-22.1 Report of Foreign Banks and Financial Accounts. U.S. citizens and residents (including individuals, corporations, partnerships, trusts and estates) who have a financial interest in or signature or other authority over any "financial accounts" in a foreign country are required to make a separate filing if the aggregate value of these accounts exceeded \$10,000. To be filed by June 30th of each calendar year. Filing requirements also apply to those with direct or indirect control over a foreign or domestic entity with foreign financial accounts, even if the taxpayer does not have foreign financial accounts of its own. Financial interest includes interests in foreign accounts titled in the names of trusts or foreign entities, if the beneficial interest in the trust or foreign entity exceeds 50% (in corpus or income with regard to trusts). Signature authority includes control of the disposition of the foreign account by oral or written instructions to the signatory or title holder of the foreign account. There is a 6 year statute of limitations with regard to this filing. Consult your tax professional for applicability of this form to you.

1040NR Non-Resident Alien Income Tax Return. A foreign trust that receives US income that is effectively connected with a trade or business must file Form 1040NR to report the income and pay the tax. The trust files 1040NR because the IRS has not developed the equivalent of a Form 1041 for a foreign trust. The IRS has recently approved a joint project with the AICPA Foreign Trust Task Force to develop a new Form 1041NR. Should be filed by the fiduciary of the trust, due by the 15th day of the fourth month following the close of the tax year of the trust, provided that the trust has an office in the U.S. Otherwise, this income tax return is due by the 15th day of the sixth month following the close of the tax year. This form is filed with the IRS Service Center in Philadelphia, Pennsylvania. If the transferor(s) to the foreign trust is/are taxable as the owner(s) of the trust under the grantor trust rules with respect to all of the holdings of the trust, this filing requirement would be informational in nature but nonetheless required as the transferor(s) would be reporting the transaction(s) on her/their individual returns. Consult your tax professional for applicability of this form to you.

5471 Information Return of U.S. Persons With Respect to Certain Foreign Corporations. A U.S. person who controls a foreign corporation for an uninterrupted period of 30 days or

more must file an information return on Form 5471. Failure to file the return can lead to a \$10,000 penalty and reductions in the taxpayer's allowable foreign tax credit. If the failure to file is not corrected within 90 days after the return is due, there is an additional \$10,000 penalty for each 30-day period for which the failure to file is not corrected, up to a maximum of \$50,000. Officers, directors and 10% shareholders in foreign personal holding companies must file a Form 5471. U.S. persons who acquire 10% of the shares of a foreign corporation and U.S. citizens who are officers and directors of foreign corporations in which a U.S. person is a 10% shareholder must also file. Form 5471 must be filed on or before the due date of the person's income tax return. No statute of limitations on obligation to file. Consult your tax professional for applicability of this form to you.

8858 Information Return of U.S. Persons with Respect to Foreign Disregarded Entities. Any U.S. person that is treated as the owner of the assets or liabilities of a foreign disregarded entity at any time during the U.S. person's taxable year is required to file a Form 8858 with its timely filed income tax return, including extensions. Penalties for failing to file a Form 8858 include (1) a fixed \$10,000 penalty, (2) 10% foreign tax reduction, and (3) additional penalties for failure to respond to an IRS notice of violation. Consult your tax professional for applicability of this form to you.

8865 Return of U.S. Persons with Respect to Certain Foreign Partnerships. A partnership formed in a foreign country that is controlled by U.S. partners is required to file tax Form 8865. Control means that five or fewer U.S. persons who each own a 10% or greater interest in the partnership also own (in the aggregate) more than 50% of the partnership interests. A US person who is a partner in a foreign partnership (or an entity electing to be taxed as a partnership) is required to file Form 8865 to report the income and financial position of the partnership and to report certain transactions between the partner and the partnership. The form is required to be filed with the partner's tax return. A controlled foreign corporation (with multiple owners) that elects to be taxed as a disregarded entity should file Form 8865 and should file a Form K-1 for each U.S. partner. Consult your tax professional for applicability of this form to you.

1040 U.S. Income Tax Return. Income from the trust must be reported on the U.S. income tax return of the trust's beneficiaries, unless the trust is classified as a "grantor" trust. In addition, a notation must be made indicating that the Settlor has transferred assets to a foreign trust. Schedule B, Part III requests information regarding the creation of or the transfer of property to a foreign trust which must be reported on this schedule of the grantor (or transferor's) individual income tax return for the year the creation or transfer occurs. This schedule also requests information relating to financial accounts in foreign countries in which the taxpayer has signatory authority or other interest.

1120F Foreign Corporation U.S. Income Tax Return. U.S. income tax return for the foreign corporation if there is any U.S. source income. This form is to be used by a foreign corporation that has income that is "effectively connected" with a U.S. trade or business. Generally, that means any foreign corporation that has an employee, office, warehouse or production facility in the U.S. Consult your tax professional for applicability of this form to you.

8621 Return by a Shareholder of a Passive Foreign Investment Company or Qualified Electing Fund. It is not mandatory to file this form unless there is a distribution of income from a passive foreign investment company (PFICs) in which a U.S. person is a shareholder or a

disposition of the shares of a PFIC by gift, death and most types of otherwise tax free exchanges or redemptions. A PFIC is a corporation and in most cases, a trust or partnership would not be a PFIC. Having to file this form to pay tax on the current income of a PFIC can be avoided when the sole U.S. owner of a foreign corporation has elected to have the foreign corporation taxed as a disregarded entity and where the foreign corporation has not invested in a PFIC. This form should not be filed by beneficiaries of a foreign trust unless the foreign trust has invested in a PFIC. Consult your tax professional for applicability of this form to you.

State Tax Returns State income and/or intangible tax returns may be required under some circumstances. Consult your tax professional for the applicability of state filing requirements to you.

926 Return by a Transferor of Property to a Foreign Corporation, Foreign Estate, Foreign Trust, or Foreign Partnership. To be filed by the transferor on the transfer of property to a foreign corporation, estate, trust, or partnership on the day of the transfer. In addition, Form 926 should be made as an attachment to the transferor's income tax return. Failure to file can lead to a penalty of 10% of the fair market value of the property transferred, up to a maximum of \$100,000. Consult your tax professional for applicability of this form to you.

8288-A Statement of Withholding on Dispositions by Foreign Persons of U.S. Real Property Interests. To be filed when a foreign person, foreign trust, or foreign corporation conveys or otherwise transfers interests in U.S. real property. If the foreign trust is a grantor trust then the grantor will be treated as holding the U.S. real property and the withholding of tax and the filing of this form may not be required. Consult your tax professional for applicability of this form to you.

720 Quarterly Federal Excise Tax Return. This form is used to report an assortment of excise taxes and is filed quarterly. It should be used to accompany any payment of the 1% federal excise tax on premium payments to foreign insurance companies, unless such payments are exempted by a treaty. If the payment is exempt from the 1% excise tax because of a treaty, a disclosure is required on Form 8833 - which is filed with the taxpayer's income tax return. Consult your tax professional for applicability of this form to you.

- U.S. source income is generally defined as income produced from within the U.S.