



## **Foreign Bank Account Report (FBAR) Due by June 30, 2010**

Any U.S. person who has a financial interest in, or signatory authority over, any foreign financial account and the aggregate value of the foreign financial account exceeds \$10,000 at any time during 2009 is required to file the Form TD F 90-22.1 with the Treasury Department by June 30, 2010. There is certain information required to be disclosed on the form, including actual maximum balance for any foreign financial account during 2009 and actual name and address of the foreign bank or other foreign financial institution. U.S. persons include a citizen or resident of the U.S., a U.S. corporation, partnership, trust or estate. A financial account includes any bank, securities, derivatives, foreign mutual fund, or other financial instruments account including any savings, demand, checking, deposit, annuities, life insurance contract, or other account maintained with a foreign financial institution. For any U.S. person who is required to file this form and fails to do so, the Treasury Department will impose a \$10,000 penalty per form, even if the non-filing is unintentional. In addition, if it is determined that the non-compliance is a willful violation, the penalty can be as high as the greater of \$100,000 or 50% of the maximum value of the foreign account.

As a revenue raiser, there are several offshore anti-abuse provisions included in the 2010 Hiring Incentives to Restore Employment (HIRE) Act. Here is a brief overview of the new offshore anti-abuse provisions.

### **Increased disclosure of beneficial owners**

The Act imposes a 30% withholding tax on certain income from U.S. financial assets held by a foreign institution, unless the foreign financial institution agrees to disclose the identity of any U.S. individual who has an account at the institution (or the institution's affiliates). In addition, the foreign institution has to annually report the account balance, gross receipts, and gross withdrawals/payments from such account. Foreign financial institutions also have to agree to disclose and report on foreign entities that have account at the institute (or the institution's affiliates) and have substantial U.S. owners. Congress expects that foreign financial institutions will comply with these disclosure and reporting requirements in order to avoid paying this withholding tax. These provisions are effective generally for payments made after 2012.

*Reporting on owners of foreign corporations, foreign partnerships and foreign trusts.* The Act also requires foreign entities to provide withholding agents with the name, address, and tax identification number of any U.S. individual that is a substantial owner of the foreign entity. Withholding agents are required to report this information to the U.S. Treasury Department. The Act exempts publicly held and certain other foreign corporations from these

reporting requirements. Any withholding agent making a payment to a foreign entity that does not comply with these disclosure and reporting requirements is required to withhold tax at a rate of 30%. These provisions are effective generally for payments made after 2012.

### **Foreign financial asset reporting**

*Disclosure of information with respect to foreign financial assets.* The new law requires individuals to report offshore accounts and other foreign financial assets with values of \$50,000 or more on their tax returns. Individuals who fail to make the required disclosures are subject to a penalty of \$10,000 for the tax year. An additional penalty can apply if Treasury notifies an individual by mail of the failure to disclose and the failure to disclose continues. These provisions apply to tax years beginning after March 19, 2010.

*Penalties for underpayments attributable to undisclosed foreign financial assets.* For tax years beginning after March 19, 2010, the Act imposes a penalty equal to 40% of the amount of any understatement that is attributable to an undisclosed foreign financial asset (i.e., any foreign financial asset that a taxpayer is required to disclose and fails to disclose on an information return).

*New six-year limitations period.* For returns filed after March 19, 2010, as well as for any other return for which the assessment period has not yet expired as of March 19, 2010, the Act imposes a new six-year limitations period for omissions of items from a tax return that exceed \$5,000 and are attributable to one or more reportable foreign assets. The Act also clarifies that the statute of limitations does not begin to run until the taxpayer files the information return disclosing the taxpayer's reportable foreign assets.

## **Franchise Tax Board (FTB) Now Accepting Applications for Homebuyer Credits - Act Quickly Before the Credits Run Out**

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The FTB began accepting applications for the New Home and First-Time Buyer Credits on May 1, 2010. They will continue accepting applications until each credit reaches its \$100 million limit. Assembly Bill 183 provides a modified version of the 2009 New Home Credit, which allows credits for first-time homebuyers and taxpayers buying homes that have never been occupied. Taxpayers who purchase a "qualified principal residence" on or after May 1, 2010 and before January 1, 2011 will be allowed a credit equal to the lesser of 5% of the purchase price or \$10,000, until the \$100 million cap for each credit is reached. The New Home Credit is also extended to taxpayers who enter into an enforceable contract on or after May 1, 2010 and before January 1, 2011, so long as the sale is complete before August 1, 2011. However, the taxpayer must request allocation of the credit before the credit is used up. The FTB will keep a running total of the credit allocation for each credit.

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To apply for the credit, the completed application must be faxed to the FTB within 14 days after the close of escrow. To complete the application:

- the buyer and seller must complete Form FTB 3549-A, Application for New Home / First-Time Buyer Credit; and
- fax the completed Form FTB 3549-A and the final settlement statement (generally the buyer's HUD-1 statement) to the FTB at (916) 855-5577.

The FTB has indicated that, due to the high volume of faxes they are receiving, there might be some delays or difficulties connecting to their fax number during normal business hours. It can take several minutes or possibly up to an hour to connect and transmit the fax. If a busy signal is received, try again later. Also, the applicant should check the fax confirmation to make sure all pages were transmitted successfully and keep a copy of the fax confirmation. The fax line is open 24 hours a day, so it may be better to fax the applications during non-business hours when the line is not so busy. In addition, the applicant should make sure that the 2010 Form FTB 3549-A is used. The FTB will deny the application if the 2009 form is used.

To find out more as well as the most current information on the credits, go to:

[www.ftb.ca.gov/individuals/New\\_Home\\_Credit.shtml](http://www.ftb.ca.gov/individuals/New_Home_Credit.shtml)

For frequently asked questions on the California homebuyer credit, go to:

[http://www.ftb.ca.gov/individuals/New\\_Home\\_Credit\\_FAQs.shtml](http://www.ftb.ca.gov/individuals/New_Home_Credit_FAQs.shtml)

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## California Governor's Revised Budget Proposal

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The Governor released his revision to the state's proposed 2010-11 budget on May 14, 2010. The only two tax-related increases that seem to appear in the budget are a cost recovery fee for the Board of Equalization (BOE), similar to the fees charged by the FTB, and a 4.8% charge on all property insurance to fund emergency response services.

The proposed budget does not include:

- extension of the net operating loss (NOL) suspensions;
- delaying NOL carrybacks;
- extension of decreased dependent exemption credits;
- delaying credit sharing among unitary taxpayers; or
- delaying the single sales factor allocation method for apportioning multistate taxpayers.

However, based on the past experiences, the final budget seldom bears much similarity to the Governor's proposals.

In addition, three-day-a-month state worker furloughs would end on June 30 under the Governor's proposal. All state employees instead would be subject to a once-a-month unpaid personal day. However, it appears that the Governor may exclude tax collectors from this furlough. The Governor also wants to reduce state employee's salaries by 5%.

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## 2010 May Be the Year to Make Large Charitable Contributions

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For the past 20 years, high-income taxpayers have faced higher marginal tax rates resulting not just from higher income, but also due to a phase out of certain itemized deductions and exemptions that are allowed to other taxpayers. For 2010, these phase-outs are removed which creates an opportunity for high-income taxpayers to maximize their itemized deductions.

In 1990, Congress passed the Omnibus Budget Reconciliation Act of 1990 (OBRA) which had two provisions with significant implications for high-income taxpayers. The first is known as the "Pease provision," which phases out the benefits of itemized deductions for high-income taxpayers, including the deductions for mortgage interest, state and local taxes paid, and charitable contributions. Under this provision, taxpayers with an adjusted gross income (AGI) exceeding a statutory threshold and claiming certain itemized deductions would have to reduce their total itemized deductions by 3% of their AGI above the threshold, up to 80% of the taxpayer's total itemized deductions. In 2009, the threshold amount adjusted for inflation was \$166,800 for married-joint filers and \$83,400 for other filers.

The second provision in the OBRA that affects high-income taxpayers is the personal exemption phase-out (PEP). Similar to the Pease provision, PEP reduced the amount of the personal exemption amount that can be claimed by taxpayers with an AGI over a statutory threshold. Both these provisions can push up the marginal tax rate substantially for those taxpayers affected.

In 2001, in an attempt to reduce the complexity of tax reporting, Congress enacted the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA), in which it established a gradual phase-out of the effects of both Pease and PEP. This phase-out began in 2006, reducing the itemized deduction phase-out to 2% for tax years 2006 and 2007 and then to 1% for tax years 2008 and 2009. In 2010, the effects of Pease and PEP have been completely repealed, which gives high-income taxpayers the full benefit of their charitable contributions and other itemized deductions, as well as the full amount of exemptions.

This hiatus of the deduction and exemption phase-outs is only temporary and is scheduled to revert back to the old rule in 2011. Under President Obama's policies, the threshold for Pease would increase to \$254,550 for married filing jointly and \$203,650 for all other filers. If you plan to increase your charitable giving, buy a house with a larger mortgage, or are looking for a way to offset the income that you have to recognize in 2010, this is a great opportunity to get the full benefit of your total itemized deductions.

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# Wealth Transfer Strategies Going Extinct?

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Congress has not yet resolved the estate tax issues that may affect many taxpayers, and there is no indication on when or if these issues will be addressed before the end of this year. However, members of Congress understand the importance of bringing these issues to the forefront.

As the law currently stands, the estate tax is temporarily repealed and is substituted with a carryover-basis regime for all deaths that occur in 2010, only to be reinstated after December 31, 2010 with a \$1M exemption. This reversion to the \$1M estate tax exemption is substantially reduced from the \$3.5M exemption that was available to the taxpayers last year. Although this could have far-reaching implications to many of us, there are opportunities to minimize the estate tax exposure through the use of estate-freeze strategies, which may not be around much longer.

One such strategy is to implement a grantor retained annuity trust (GRAT). This is a very effective tax-reduction method for transferring wealth to future generations without paying gift tax. A key element to a successful GRAT is for the grantor to survive the life of such a trust. Often times, GRATs are set up with a term of less than 10 years to increase the probability of the grantor outliving the GRAT. Congress is currently considering a law that would mandate GRATs to have a minimum life of 10 years, which could effectively eliminate the benefits from the use of GRATs.

Congress is also debating on taking away the ability to transfer a personal residence to a qualified personal residence trust (QPRT). In the past, taxpayers would transfer their homes to QPRTs to escape paying estate taxes on the future appreciation of the home, without disrupting the enjoyments of living in the home. However, the window of opportunity to use this strategy is diminishing as Congress considers abolishing the use of QPRTs.

There are also some discussions about disallowing valuation discounts for minority partnership or limited liability company interests holding passive assets (e.g., marketable securities and real estate). This is another strategy that has been prevalent over the past decade in transferring substantial amounts of wealth estate tax free. Although this has been a highly litigated strategy over the years, taxpayers with strong business purposes for setting up such a structure have been successful in defending the valuation discounts. Current debates in Congress could put an end to this very soon.

In light of what may or may not happen to the estate tax and various wealth transfer strategies, now is a critical time to review your estate plan and be proactive through these uncertain times considering the potential extinction of some tried-and-true wealth preservation tools that exist today.

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