



Duke Law Firm, P.C.—in the News

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Conferences

J. Richard Duke will be speaking at the *Legalease Conferences*:

Practical Issues in Trust Administration, 19 September 2005, Westin Casuarina Hotel, Grand Cayman; and Practical Issues in Company Administration, 20 September 2005, Westin Casuarina Hotel, Grand Cayman. Practical Issues in Company Administration, 22 September 2005, British Colonial Hilton, Nassau, Bahamas; and Practical Issues in Trust Administration, 23 September 2005, British Colonial Hilton, Nassau, Bahamas: <http://www.Legalease.co.uk>

Report of Foreign Bank and Financial Accounts (FBAR)—TD F 90-22.1—Due June 30

A U.S. person who has a financial interest in, signature authority, or other authority over one or more financial accounts in foreign countries, including bank, securities, or other types of financial accounts in a foreign country, of which the value of the account or the aggregate value of more than one account exceeds \$10,000 at any time during the calendar year, is required to file TD F 90-22.1 with the Department of the Treasury, on or before June 30 of the succeeding year.

The penalties are severe for the failure to file this report. The American Jobs Creation Act of 2004, effective October 22, 2004, sets forth a penalty for willful failure to file the report as the greater of \$100,000 or 50% of the amount of the transaction or account. Also,

it provides a maximum \$10,000 penalty if the failure is non-willful. If the government pursues criminal action against the U.S. person for failure to file this report, the result may be a fine not to exceed \$250,000 or five years of imprisonment, or both. And, if the failure to file can be shown as being part of an ongoing illegal activity, the fine may be as high as \$500,000 or up to ten years imprisonment, or both.

One Clarification Made to Filing Requirements With Respect to the FBAR

On June 9, 2005, the IRS clarified an exception for when officers or employees of domestic subsidiaries of certain domestic corporations are not required to report signature authority over the subsidiary's foreign financial accounts.

The specifics of this Official Announcement from the IRS states as follows:

An officer or employee of a domestic subsidiary of a domestic corporation which has securities listed on national securities exchanges or which has assets exceeding \$10 million and 500 or more shareholders of record need not report that he has a signature authority over a foreign financial account of the subsidiary if he has no personal financial interest in the account and has been advised in writing by the chief financial officer of the parent corporation that the subsidiary corporation has filed a current report which includes that account. *Published by Tax Analysts™, 2005 TNT 114-18.*

Controversial Report from the UK Regarding International Financial Centers

The Society of Trust and Estate Practitioners (STEP) Journal May/June 05, Volume 13, Issue 3 reports on an article in the UK's Observer newspaper that published details of controversial research that claims the world's richest individuals have placed some \$11.5 trillion of assets, ten times Britain's GDP in international financial centers. This figure was originally published in a study by the Tax Justice Network (TJN), a group of left-leaning accountants and economists who oppose international tax planning and tax competition.

Quoting, David Woodward, Director of the Global Economy Programme at the New Economics Foundation, "If we are serious about reducing poverty, one of the first things we need to tackle is an international financial system run by the rich, for the rich, at the expense of the poor. It is time to rethink what the system is for—and dealing with tax havens and tax competition could be an important first step."

However, Veronique DeRugy research fellow at the American Enterprise Institute stated: "The Tax Justice Network assumes that low-tax nations have an obligation to enforce bad tax laws of high-tax nations. This assault on sovereignty is disturbing, particularly since it is an effort to promote the interests of relatively wealthy white nations like France and Germany at the expense of low-tax jurisdictions, many of which are deve-

loping nations governed by people of colour. Why do the organizations participating in the briefing believe that developing nations should be forced to act as fiscal colonies?"

STEP is the professional body for the trust and estate profession worldwide. Its home office is in London, England, with branches around the world, including in New York and Miami.

<http://www.step.org/>

Treasury, IRS Officials Deny Tougher Stance on International Audits

Published by Tax AnalystsTM

Three tax officials on June 2 denied that IRS audit teams were purposefully promoting stricter examinations of international issues. David Marion, chief of international technical specialists in the IRS's Large and Midsize Business Division (LMSB), joined Frederick W. Heggi, LMSB international manager, and Christopher J. Bello, an attorney-adviser in Treasury's Office of Associate Chief Counsel (International), in discussing the nuances of international audits at a meeting of the District of Columbia Bar Association. The three officials acknowledged that U.S. international tax rules are often complex, but dismissed the notion of any covert agenda requiring tougher international audits.

To the extent practitioners perceive increased IRS scrutiny of international issues, the likely culprit is the complexity of the applicable law combined with the presence of large dollar amounts at issue. Former Treasury official Phil West, now of Steptoe & Johnson LLP, identified transfer pricing, permanent establishment, and foreign tax credits as significant practice areas viewed as "ripe for audits."

West added that IRS audit teams appear to have become more aggressive across the board in seeking taxpayer documentation.

"It's no secret that the IRS is focusing on the value of paper in building their case," he said. Increasingly, the agency is seeking written information previously regarded as confidential or otherwise protected under taxpayer privacy rules, such as taxpayer accrual workpapers.

Document: (Doc 2005-12145)
Electronic Citation: See 2005 TNT 106-5.

Under Pressure, French Law Firm Embraces U.S. Market

The National Law Journal

Amid mounting competition, France's largest independent law firm is broaching North America's financial markets. Gide Loyrette Nouel has hired its first two American lawyers to staff its New York office, and hopes to add as many as 15 more in the next year. The expansion may seem conservative compared to that of hulking U.S. firms, whose one-stop-shopping mantra has spawned rapid proliferation in European and Asian markets. But the move indicates globalization may be inevitable for firms to stay viable.

Tax Protest Leader Sentenced to 10 Years in Jail.

Published by Tax AnalystsTM

A prominent tax protester was sentenced on June 6 to more than 10 years in federal prison for failing to pay income taxes and conspiring to defraud the IRS, according to the Justice Department.

Lynne Meredith, 55, published best-selling books and toured the country between 1991 and 2002 promoting strategies purported to provide legal ways to avoid paying income taxes. During that period, authorities said her organization, We the People, peddled phony "pure trusts" designed to shield income and assets from tax liability. Meredith gained media notoriety as an icon of the tax

protest movement following her indictment in 2002.

Authorities also charged her with failing to pay income taxes on nearly \$9 million in income. Meredith, who was convicted of the charges last year, was also ordered to pay \$2 million in restitution to the IRS.

Four of Meredith's associates at We the People received lesser sentences, the longest of which was five years in federal prison. Document: (Doc 2005-12462)
Electronic Citation: See 2005 TNT 109-7

Tax Advisers Who Promote "Abusive" Avoidance Schemes Face Big Penalties

By Vanessa Houlder

Published: June 10 2005

Tax advisers who help clients avoid tax could face heavy penalties under rules being considered by senior officials of HM Revenue & Customs.

Officials are monitoring the penalty regimes used in the US and elsewhere, where advisers involved in flagrant tax abuses can be hit with huge penalties.

Other options described as "very interesting" by HMRC officials include increased penalties for errant taxpayers and more prosecutions of taxpayers suspected of dishonesty.

The discussions in HMRC come against the backdrop of a wider crackdown on tax avoidance initiated by Gordon Brown.

The chancellor's search for additional weapons in his battle against abusive tax planning reflects the challenge he faces in closing the tax "gap" - between theoretical expectations of tax revenues and those actually received - which the Treasury estimates at £20bn-£30bn.

The Treasury has benefited from tax disclosure rules introduced last autumn. These force advisers to give officials early warning of new tax schemes and have yielded more information than expected, enabling HMRC to close loopholes.

The interest shown by HMRC in penalties for tax advisers reflects frustration that some tax professionals, particularly in smaller firms, have continued to promote what it considers to be abusive plans.

Several countries, including the US, Canada and New Zealand, have decided to tackle advisers on the grounds that they may be misleading taxpayers. The penalties are not intended to apply to honest mistakes or differences of interpretation where there are genuine grounds for uncertainty.

New penalties would require legislation and be likely to meet resistance from tax professionals. There have already been calls to rein in some of HMRC's powers, which are the subject of a consultation following April's merger between the Inland Revenue and HM Customs and Excise.

But some HMRC officials would like to see stiff penalties. "A question that needs to be asked is whether tax avoidance is a risk-free game in the UK," said an official.

The UK only charges tax and interest when a scheme is deemed unacceptable, and could learn from countries that impose substantial underpayment penalties, he said.

Tougher sanctions against cases involving deceit are also being discussed. "We are beginning to ask whether these very artificial schemes slip across the border between avoidance and evasion," the official said. "We are doing work with lawyers in relation to the more

aggressive schemes of avoidance."

There is some evidence that the biggest accountancy firms have cut back their tax avoidance activities in response to the government's crackdown. There are also signs that large companies are increasingly reluctant to take risks in their tax planning.

The Federal Reserve System banned a church elder, Carl V. Thomas, from South Florida who sought to form a "Christian" bank in Broward County, Florida, to help process checks for a nationwide Ponzi scheme.

Mr. Thomas, an elder of the Greater Ministries International of Tampa, was enlisted by followers to gain control of the former First Western Bank in Cooper City, according to the Federal Reserve. The Federal Reserve also issued cease-and-desist orders against Thomas and seventeen followers and family members for their alleged roles in a scheme ultimately costing 18,000 investor-followers between \$50 million and \$60 million.

The Federal Reserve states that First Western was seen by leaders at the Great Ministries as a conduit for cashing illicitly collected checks, even as national banks refused to do so because of pressure from federal regulators and law enforcement authorities. According to the order of the Federal Reserve, Greater Ministries persuaded followers, including white supremacists and Pennsylvania Mennonites to leverage their homes, credit cards and retirement funds to invest with the fund managers of the church. The Federal Reserve order further stated that followers were reminded of Luke 6:38 that states: "Give and it shall be given unto you."

Mr. Thomas responds that the Federal Reserve is trying to blackmail him. Reported by Law.com:

<http://www.law.com/jsp/article.jsp?id=1118739912789>

San Francisco Accounting Firm Challenges the Internal Revenue Service

The NEW YORK TIMES, In a June 11, 2005 article titled "Court Case Gives Rare Look at Tax Shelter Clients," states that Presidio, a San Francisco accounting firm that sold tax shelters to allow investors to shield billions of dollars in income, has gone to the court to defend those shelters. Presidio, which worked with the accounting firm KPMG, maintains that the particular tax shelter in question is legal and is seeking to force the IRS to disclose the internal deliberations and legal reason behind its decision to ban the tax shelter.

The report states that the judge denied Presidio's motion to depose IRS officials, stating that the request was not properly written, but further stated that the firm may refile its request to do so. The IRS and Justice Department deposed Presidio's efforts, fearing that disclosure may provide ammunition to tax shelter promoters, as well as jeopardize major criminal investigations into the promoters, including KPMG.

This case will be watched closely by tax professionals.

Targeted Estate and Gift Tax Planning Techniques

The June/July 2005 issue of Worth magazine includes an article titled "Taxes—Mind the Gaps." According to the author of the article, estate and gift tax shelters will likely be curtailed, or eliminated outright, in the battle to reduce government tax gaps (failure to receive tax revenue). It appears that some common and basic planning techniques are now being referred to as "tax shelters" by the government.

The Joint Committee on Taxation has targeted several estate and gift tax planning techniques as non-compliance threats, tax shel-

ters and loopholes. Spearheaded by Senator Charles Grassley, the Joint Committee on Taxation argues that these "dodgy strategies" account for a significant portion of the current revenue gap. Two of the proposals addressing these loopholes have a reasonable chance of passing; two do not.

The first proposal prohibits the sale by an heir of an inherited item from claiming a higher valuation for the item than was used on the estate's final tax return. Apparently, this problem primarily arises with respect to tangible assets, such as artwork and collectibles. When an heir sells an item, he will pay capital gains tax (lesser rate than estate taxes) on the difference between the sale price and the higher option house valuation, rather than the lower estate appraiser's estate valuation. This proposal is likely to pass.

The second proposal involves limiting the availability of minority and marketability discounts for federal transfer tax purposes. This is most commonly used among tax practitioners with respect to transferring interests in family limited partnerships or limited liability companies. The position of the Joint Committee on Taxation is that the discount, which reflects the illiquid nature of the interests, is used to suppress the market value of securities and bonds for tax purposes. Based on the article, this may apply only to limited partnerships and limited liability companies that own securities and bonds, not property that cannot be sold readily on the market, such as real estate. Because of the recent history of the IRS aggressively pursuing discounting by individuals for U.S. estate and gift tax transfer purposes, it appears that Congress may well enact this proposal.

The third and fourth proposals are to obliterate both dynasty and Crummey trusts. The dynasty trust is one in which assets will pass from generation to generation free

of federal estate taxation and generation-skipping transfer taxation. A Crummey trust is one in which assets are transferred by a settlor to the trustee of an irrevocable trust and beneficiaries have the right to withdraw gifts to the trust, for some period of time such as thirty days. This right to withdraw makes the gift qualify for the \$11,000 annual exclusion for avoiding gift taxes. The Joint Committee on Taxation is concerned that practitioners are including many persons as Crummey withdrawal beneficiaries so they can multiply that number of beneficiaries by \$11,000 to avoid making an adjusted taxable gift.

The Rule Against Perpetuities permits trusts only to last for a specified period of time. Several states in the U.S. have repealed the Rule Against Perpetuities, allowing trusts to continue until the end of the age, if desired. Other states have extended the period of time for which trusts can continue.

According to this article, the proposals to obliterate the use of dynasty and Crummey trusts may not pass in Congress.

<http://www.worth.com>

KPMG Faces Being Indicted On Tax Shelters

The Wall Street Journal, on June 16, 2005, reported that federal prosecutors have built a criminal case against KPMG LLP for obstruction of justice and the sale of abusive tax shelters, igniting a debate among top Justice Department officials over whether to indict the company. The concern is that the indictment will destroy the company. Federal prosecutors are engaged in negotiations that will decide the fate of the company. An alternative to indictment is to issue a large deferred prosecution penalty, which will give KPMG a period of time, such as a year, to show that it has met required conditions, such as changing its procedures, in order to avoid indictment.

U.S. House of Representatives Votes to Limit Patriot Act

By a 238-187 vote, the U.S. House of Representatives amended the Justice Department's budget to bar the use of its post-Sept. 11 powers to gain access to such items as library patron lists and bookstore sales records without a traditional search warrant.

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