



# ***Duke Law Firm, P.C.-in the News***

1572 Montgomery Highway, Suite 205  
Birmingham, Alabama 35216 USA

Volume 5, Issue 3, October 2008

The following is a publication of Duke Law Firm, P.C. All Rights Reserved © 2008

## **OFFSHORE DIVERSIFICATION TELECONFERENCE**

Increased Business/Wealth Protection—Diversification into Offshore Asset Management

**Date:** Thursday, October 30, 2008

Individuals and businesses are watching the value of their U.S. dollar-backed investments fall. Some currencies are faring better than the U.S. dollar. Clients may wish to diversify their portfolios by placing some of their assets with banks or solid asset managers located primarily in Switzerland, Abu Dhabi/Dubai, Denmark and other countries.

This area of law is highly specialized and beyond the focus of most firms. Duke Law Firm has twenty years of experience in establishing accounts with such banks and asset managers in Switzerland, Abu Dhabi/Dubai UAE and Denmark.

Join our free\* teleconference with Q/A session to learn how our firm can provide the needed expertise to enable your firm retain and create business that your clients may be taking elsewhere, or to reduce your tax exposure by keeping your offshore investments IRS-compliant.

Key Topics to be covered:

- Why currency management is key to riding out this credit crisis
- The structures most efficient and effective for offshore investing
- Why working with Duke Law Firm simplifies your business or lessens your tax exposure

**Time (CDT):**

**Investors:** 10:00 A.M.

**CPAs:** 1:00 P.M.

**Attorneys:** 3:00 P.M.

**Sign up on line to reserve your space:**

[www.AssetLaw.com/conference.html](http://www.AssetLaw.com/conference.html)

\* Long distance charges may apply to telephone calls made from some countries.



The Alabama Bar Rules of Professional Conduct, Rule 1.1, Competence, state: "A lawyer shall provide competent representation to a client."

The Florida Bar Rules of Professional Conduct, Rule 4-1.1, Competence, state: "A lawyer shall provide competent representation to a client. Competent representation requires the legal knowledge, skill, thoroughness, and preparation reasonably necessary for the representation."

## **Now May Be the Time to Make Gifts to Your Heirs**

On October 18, 2008, the Wall Street Journal included the article titled "Why Now Is the Time to Help Your Heirs." The article points out that because interest rates are low and property values have fallen, now is the time to make gifts to lower generation beneficiaries in order to reduce the estates owned by the donors.

An individual can make gifts of \$12,000 per person under the annual exclusion and transfer those assets out of his estate without gift tax consequences. Family loans can be made with repayments at low federal rates ranging from 2.5% to 4.5%, depending on the loan's maturity. The primary advantage of inter-family loans is that the donee may be able to invest the loan proceeds wisely and earn income in excess of the amount of the interest paid to the donor.

Another important planning device that the article discusses is the intentionally defective grantor trust where the grantor/settlor (person creating a trust) sets up a trust in such a manner that the income of the trust is taxable to the grantor under the Internal Revenue Code. The purpose of this trust is to allow sales of assets on a tax-free basis by the seller (no capital gains and no taxation of the interest received by the seller) and shift the future potential appreciation of the assets held in trust to the beneficiaries of the trust, generally children.

Another popular planning vehicle discussed is the grantor retained annuity trust where the grantor sells assets to a trust and retains an annuity amount. This annuity amount is based on the percentage of the initial value of the assets that are transferred to the trust. After the specified period of time ends as stated in the trust with respect to the annuity payments back to the settlor, the assets pass to the children as gifts. However, the gift is made and valued on the date of the transfer to the trust and the value of the income stream from the annuity payments reduces the amount of the gift for gift tax reporting purposes. If the assets in the trust appreciate, the appreciation will not cause the annuity payments to increase (because they are based on the initial value of the property transferred) and the appreciation is shifted to the children's estate and out of the donor's estate.

*Why Now Is the Time to Help Your Heirs*  
*The Wall Street Journal*  
*October 18, 2008*  
*By Anne Tergesen*

## **Interest-Based Lending vs. Risk-Sharing Lending**

by John M. Walker, Esq.

In the U.S., as well as Western countries and those that follow English Common Law or French Civil Law, banks and financial institutions charge interest on monies lent to the borrower. The interest is the cost of borrowing money. Historically, the interest rate reflected the riskiness of the loan; although in years leading up to our current credit crisis, the interest rates were simply kept low by the Federal Reserve. As the risk of default or non-payment increases, so will the interest rate charged. Risk is affected by several factors, including the credit worthiness of the borrower, the collateral offered by the borrower to secure the loan, the cash flow of the borrower and various influential interest rates, such as the Federal Discount Rate and the London Interbank Offered Rate (LIBOR). Banks and financial institutions' analysis of risk tend to be credit based.

The principles of Islamic banking include:

- Prohibits interest (pre-determined loan repayment)
- The central focus of the Islamic financial system is risk sharing (profits and losses)
- Financial transactions must be asset-backed (making money out of money is unacceptable)
- Speculative behavior is prohibited
- Only Shari'a-approved contracts are acceptable
- The sanctity of contracts is strongly recognized

Basic principles of Islamic banking follow the law of Shari'a known as fiqh al-muamalat (Islamic rules on transaction). The term "Islamic banking" is synonymous with "full-reserve banking." Interest-free (riba) banking is based on the concepts of shirkah (partnership) and mudaraba (profit sharing). The Islamic bank acts as a financial intermediary receiving savings from the public on a profit-sharing basis and advancing capital to entrepreneurs on the same basis. Investments must carry a pro-rated profit, not a fixed rate of return.

The bank can invest in any type of activities, including the duration, location of projects or enterprise and monitor the investments, except the funds cannot be used for activities forbidden by Islam. The bank may aggregate and pool the profit from different investments and, after deducting administrative costs, capital depreciation and Islamic tax, the net profit is shared according to a specified formula with depositors. If losses are incurred, depositors lose a proportionate share or the entire amount of their funds. Any return to the bank is based solely on the share of profits.

The bank provides funds to entrepreneurs and may monitor the investments, but the bank is restricted from harming the performance of the entrepreneur and the bank cannot interfere with the management of the investment. Generally, loan covenants and other such constraints used in conventional commercial bank lending are allowed. The bank cannot require any guarantee in the form of security or other collateral from the entrepreneur.

The bank's liability is limited to the capital provided, whereas the entrepreneur's liability is restricted to labor and effort employed. However, if it is proven that the entrepreneur is engaged in negligence or mismanagement, the entrepreneur may be liable for the financial loss and required to remunerate the bank accordingly.

Savings accounts also operate under the al-wadiah principle, which means that the depositors are guaranteed repayment of their funds. Savings accounts differ from current deposits in that they earn depositors income: depending upon financial results, the Islamic bank may decide to pay a premium, hiba, at its discretion, to the holders of savings accounts. Current accounts are also based on the principle of al-wadiah and, upon deposit, the depositor receives no remuneration for because the guaranteed funds are not used for profit-sharing ventures but used to accumulate within these accounts to balance liquidity needs of the bank and for short-term transactions with respect to the bank's responsibilities.

A Shari'a Supervisory Board, consisting of Shari'a scholars of Muslim jurisprudence who act as advisors to the banks, is required in order to ensure that the practices and activities of Islamic banks do not contradict Islamic ethical standards. These Shari'a scholars become increasingly important when Shari'a-compliant banks begin to offer services to Western banks, businesses and individuals. Also, these Shari'a-compliant banks are not allowed to be involved with businesses that make products or offer services that are contrary to Islamic tenets.

#### **IRS Engaged in Coordinated Effort to Halt Offshore Tax Evasion, Fraud, Officials Say.**

SAN FRANCISCO--The government now is engaged in a coordinated effort to stop offshore tax abuses, and that approach will continue, senior officials said Sept. 13 [2008] at the fall meeting of the American Bar Association Section of Taxation.

IRS's new, stringent focus on reporting foreign bank accounts was a major topic of discussion at the session on offshore enforcement sponsored by the Civil and Criminal Tax Penalties Committee.

Over the past few months, IRS has made a concerted effort to get taxpayers to file their Report of Foreign Bank and Financial Accounts (FBAR), required to be filed by U.S. persons with foreign accounts.

Civil penalties for a willful violation can range up to the greater of \$100,000 or 50 percent of the amount in the account at the time of the violation, IRS noted. Criminal penalties for violating the FBAR requirements while also violating certain other laws can range up to a \$500,000 fine or 10 years' imprisonment or both. Civil and criminal penalties may be imposed together, the news release said.

... [T]he government has recently appointed two senior prosecutors, one for FBAR and offshore banking issues, and one a national security tax coordinator. He also pointed out that FBARs are not tax forms, and IRS can freely share them with all other federal law enforcement agencies.

... [The] IRS has trained 800 law enforcement officers around the world in financial and banking investigative issues, and "we're going to increase our footprint in this area so we can get those investigators working with us."

Astengo said his district "has never been a stranger" to a broad range of tools to get information, including informants, treaty exchanges, and penalties, among others.

He said IRS is undergoing a major effort to educate and teach agents throughout the country about both civil and criminal penalties. For international enforcement, he said, IRS seeks agents with "the right skill sets," such as those who have worked on exchange of information agreements, those with knowledge of controlled foreign corporations, and those with trial experience, among others.

"We are focused on getting the right agents with the right attributes to do these jobs," Astengo said.

Senior criminal enforcement officials at both the Internal Revenue Service and the Department of Justice Sept. 13 gave strong indications they are looking for offshore tax fraud and tax evasion by banks other than the much-publicized investigations involving UBS in Switzerland and LGT in Liechtenstein.

As part of a discussion in which private-sector panelists raised the UBS and LGT investigations, IRS Deputy Chief of Criminal Investigation Victor Song said IRS is casting a wider net, although neither he nor any other government speakers specifically named those two banks or any other banks.

"I can say that just because you see a couple of banks that are making the press doesn't mean, with the agents that we have and the things we're doing around the world, that it's limited to two banks," Song said at the fall meeting of the American Bar Association Section of Taxation.

[Mark] Matthews [former IRS Deputy Commissioner for Services and Enforcement], now with Morgan Lewis, Washington, D.C., said, "we now have a belief that there are widespread investigations at IRS and the Department of Justice, other subpoenas that have been issued."

He noted that DOJ "has never been bound by a green light from IRS," and has at its disposal the Report of Foreign Bank and Financial Accounts (FBAR). This form, required to be filed by U.S. persons with foreign accounts, is not under the jurisdiction of IRS and is freely available to DOJ (see related report in this section).

Matthews said he believes that, as IRS cracks down on FBAR nonfilers and urges audits in this area, the documents also may be used to assist in bank investigations.

Another tool in the government's arsenal is the whistleblower program, Brown said. She noted amendments to the whistleblower rules have caused that program to be much more effective in encouraging informants to come forward. "I rarely go a week where I don't get a call from a whistleblower and a lawyer for a whistleblower," Brown said.

Alison Bennett, *IRS Engaged in Coordinated Effort to Halt Offshore Tax Evasion, Fraud, Officials Say*, FEDERAL TAX & ACCOUNTING, TAX ENFORCEMENT, Bureau of National Affairs (Sept. 16, 2008).

**CIRCULAR 230 NOTICE--NOT A RELIANCE OPINION; NOT A MARKETED OPINION. THIS NEWSLETTER AND ITS CONTENTS WERE NOT INTENDED OR WRITTEN BY DUKE LAW FIRM, P.C. TO BE USED, AND CANNOT BE USED, BY ANYONE FOR THE PURPOSE OF (i) AVOIDING U.S. TAX PENALTIES, OR (ii) PROMOTING, MARKETING OR RECOMMENDING TO ANOTHER PARTY ANY TRANSACTION OR MATTER ADDRESSED OR STATED HEREIN. THIS NEWSLETTER AND ITS CONTENTS AND ANY ATTACHMENTS ARE NOT TREATED AS A MARKETED OPINION BECAUSE "(A) THE ADVICE WAS NOT INTENDED OR WRITTEN BY DUKE LAW FIRM, P.C. TO BE USED, AND IT CANNOT BE USED BY ANY TAXPAYER, FOR THE PURPOSE OF AVOIDING PENALTIES THAT MAY BE IMPOSED ON THE TAXPAYER; (B) THE ADVICE WAS WRITTEN TO SUPPORT THE PROMOTION OR MARKETING OF THE TRANSACTION(S) OR MATTER(S) ADDRESSED BY ANY WRITTEN ADVICE; AND (C) THE TAXPAYER SHOULD SEEK ADVICE BASED ON THE TAXPAYER'S PARTICULAR CIRCUMSTANCES FROM AN INDEPENDENT TAX ADVISOR." 31 C.F.R. SECTIONS 10.35(b)(4)(ii); 10.35(b)(5)(i); and (b)(5)(ii)(A), (B) AND (C).**

This newsletter is purely a public resource of general information that is intended, but not promised or guaranteed, to be correct, complete and up-to-date. This newsletter is not a source of advertising, solicitation or legal advice, and thus the material provided in this newsletter is not intended to create, and the receipt of it does not constitute, an attorney-client relationship. Do not rely on information provided herein, and always seek the advice of competent counsel in the reader's state or country outside the United States. The publisher of this newsletter is a law firm that includes attorneys licensed in the States of Alabama and Florida, and Duke Law Firm and its attorneys do not desire to represent anyone who views this newsletter in a state or country outside the United States where this newsletter fails to comply with all laws and ethical rules of that state or foreign country. Please speak with one of our lawyers before sending information to the publisher of this newsletter, Duke Law Firm, or anyone listed herein.

No comparison is made for the services of Duke Law Firm and its lawyers, and the services of other law firms and their lawyers. Alabama State Bar Rules of Professional Conduct, Rule 7.1(c) and The Florida Bar Rules of Professional Conduct, Rule 4-7.2(b)(1)(D).

**Duke Law Firm, P.C.**  
**(205) 823-3900**  
**Facsimile: (205) 823-2630**  
**1572 Montgomery Highway, Suite 205**  
**Hoover, AL 35216 USA**  
<http://www.assetlaw.com>