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IRS Compels Disclosure of Offshore Asset Protection Trusts

November 13, 2011

As we approach the 2012 income tax filing season planning should already begin for tax preparers and taxpayers to deal with offshore trust disclosure. Form 8938 is still draft form, but the disclosure requirements of IRC§ 6048 should receive careful care and attention.

For tax years beginning after March 18, 2010 (the effective date of the HIRE Act), a U.S. taxpayer who is treated as the owner of a foreign trust must provide such information as IRS may require. An owner of a foreign trust is a U.S. person who directly or indirectly transfer property to a foreign trust. What this means is that for 2011 tax returns a Form 8938 must be completed and attached to Form 1040 if an individual taxpayer has at the end of the year 2011 more than \$50,000 in specified foreign financial assets (\$100,000 for married taxpayers). Specified foreign financial assets include the assets transferred and held by an offshore trust. Specified foreign financial assets, include bank accounts, brokerage accounts and other financial instruments as well as interests in private companies foundation and partnerships. The important part about the disclosure requirements is that it applies to the transferor without limit as to how long ago the transfer was made. So for existing as well as newly established offshore trusts even if the taxpayer who made the transfer is not a trustee or beneficiary of the trust, or even a trust protector. There are penalties for not making the required disclosure including the possibility of prosecution for income tax evasion based upon falsely signing a tax return under penalty of perjury without the disclosure.

There is no doubt that the focus of income tax enforcement, according to the Commissioner of Internal Revenue is offshore tax evasion. With foreign financial institutions now taking a serious look at who their account holder really are for purposes of future disclosure to the RS under the Foreign Account Tax Compliance Act, FATCA, U.S. taxpayers who set up foreign trusts, often known as foreign asset protection trusts, need to start planning their disclosures now.

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