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MAY 2017 NEWSLETTER

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Firm News

MMPPH congratulates Judy Bae on recently being named by her peers in the San Diego Business Journal as "Best of the Bar" for Probate Litigation. Judy is very active in the local bar community, including serving as the current President of the Pan Asian Lawyers of San Diego (PALSD), and as Chair of the Estate Planning, Trust and Probate Section of the San Diego County Bar Association (SDCBA). She will also be joining the Executive Board of The Honorable William B. Enright American Inn of Court later this summer for a three year term. Click here for more information about the "Best of the Bar."

IN THIS ISSUE

FAILURE TO REPORT FOREIGN ACCOUNTS CAN BE COSTLY

by DeEtte L. Loeffler, *J.D., LL.M., Taxation*

Under the Federal Bank Secrecy Act[1], taxpayers who have signature authority over, or a financial interest in, a foreign financial (i.e., bank or investment) account have a duty to report that fact to the IRS if the value of the account exceeds $10,000 at any time during the year. Taxpayers are required to file a Financial Crimes Enforcement Network (FinCEN) form 114, "Report of Foreign Bank and Financial Accounts" (FBAR) online. As of 2015, the due date for submitting this report is April 15th (it was due by June 30th prior to 2015).

A person holding a financial power of attorney for someone else may be treated as having "signature authority" over a foreign account - even if the agent is not aware of the existence of the account. We now recommend that financial agents ask the maker of the financial power of attorney (the "principal") if he or she has any such foreign accounts. We also include a provision in many of our financial powers of attorney denying the agent any powers over foreign accounts as long as the principal remains competent. The goal of this provision is to protect the agent from having to complete an FBAR.

The penalties for willfully failing to file an FBAR are significant - the greater of $100,000 or fifty percent (50%) of the value of the account. In a recent case, the federal district court for central California ruled that the term "willful" includes reckless behavior. In *US v. Bohanec*, No. 2: 15-CV-4347 DDP (FFMx) (C.D. Cal. Dec. 20, 2016), the taxpayers were foreign born US

[1] 31 U.S.C. § 5314.

residents who owned an interest in several foreign accounts. US persons are taxable on their worldwide income. The taxpayers failed to report both their foreign source income which was deposited into these accounts, and the existence of the accounts. In 2011, they asked to participate in the IRS Voluntary Disclosure Program to report the existence of the accounts after transferring over $500,000 from a Swiss UBS account (via an Austrian account) to their bank in Pasadena, California.

The *Bohanec* court first noted that the Federal Bank Secrecy Act does not define the term "willful", so this term has been defined by the courts. The US Supreme Court in *Safeco Ins. Co. of America v. Burrhas* explained that the meaning of "willful" depends on the context in which it appears.[2] The taxpayers argued that the term only encompassed intentional violations of known legal duties, but the court rejected that position, relying on the *Safeco* decision to find that where willfulness is an element of civil liability, the term includes "not only knowing violations of a standard, but reckless ones as well."[3] The *Safeco* court defined "recklessness" as conduct which entails an unjustifiably high risk of harm that is either known or so obvious that it should be known.[4]

The court in *Bohanec* found that the taxpayers were sufficiently reckless to justify imposition of the penalty for several reasons. They were sophisticated people, taking advantage of the law in connection with their business to obtain patents and avoid a competitor's exclusive product distribution rights. In addition, they did not report most of their foreign source income, diverting it to the UBS account, failed to report US source income from internet sales, failed to report all of their foreign accounts in the Voluntary Program, and lied on tax returns they did file in connection with the Voluntary Program that all funds in the UBS account were deposited after payment of US taxes.

While an agent under a power of attorney who fails to report a principal's foreign accounts is unlikely to face the level of IRS scrutiny faced by the taxpayers on *Bohanec*, it is possible the agent's failure to inquire if the principal owns foreign financial accounts might constitute reckless behavior. If you have been named as an agent under a financial power of attorney, we strongly recommend you inquire annually about such accounts, or ask the principal to provide you with a new financial power which restricts your power over foreign financial accounts until such time as the principal is incapacitated.

If you have questions about financial powers of attorney, or other estate planning documents, we would be happy to discuss them with you.

FEDERAL TAX UPDATE

by DeEtte L. Loeffler, *J.D., LL.M., Taxation*

Trump Tax Reform Proposed. On April 26th, the White House released a one-page outline of the President's goals for tax reform. The release did not include details or analysis of how these changes could impact the economy. The outline included many items from Candidate Trump's tax plan in 2016. The plan proposes:

* Repeal the death tax (i.e., the federal estate tax);
* Repeal the Alternative Minimum Tax;
* Repeal the 3.8% Obamacare tax (the Net Investment Income Tax);
* Reduce the federal income tax brackets from seven (ranging from 10% - 39.6%) to three (10%, 25% and 35%). (No income levels for these brackets were proposed);
* Double the standard income tax deduction (currently $6,350 [single] and $12,700 [married]);
* Protect the home ownership and charitable gift tax deduction (which presumably means eliminating all others);
* Reduce the "business" tax rate to 15% (presumably for not only corporations but also for pass-through entities including S corporations and LLCs);

[2] 551 U.S. 47, 57 (2007)
[3] Id.
[4] Id. at 68.

* Adopt a territorial tax system (i.e., not tax US companies for overseas sales);
* One-time tax on trillions of dollars held overseas (i.e., a forced repatriation tax).

The proposal does not include the border adjustment tax proposed by Republican leadership. It also does not discuss the gift and generation skipping taxes. Also missing is the proposed capital gains tax for estates over $10 million which was in the prior plan. Most troubling is the lack of information about how these tax cuts would be funded. Under current law, no tax cut can be made to exceed 10 years unless it is offset by spending cuts or other taxes. In March, the Tax Foundation has estimated similar cuts could reduce revenue by $5.9 trillion over a decade (or 14% of total revenue). The White House estimates these cuts will stimulate the economy to increase by at least 3.0% and should offset the lost revenue. Other experts say that the stimulus would need to be twice as great to offset the losses.

STATE TAX NEWS

by DeEtte L. Loeffler, *J.D., LL.M., Taxation*

Loss of Federal Deductions Would Hurt Californians. President Trump's new tax plan appears to eliminate federal income tax deductions except the mortgage interest and charitable deductions. This change would harm seniors, the disabled and those with a catastrophic illness who rely on the medical deduction to offset these expenses. In home care costs can run as high as $20,000 per month, so the deduction represents a significant benefit. In addition, since California is a very high tax state, the loss of the income and sales tax deductions, and the real estate taxes deduction, would greatly impact those who itemize. Taxpayers in California and six other states could expect to pay significantly higher taxes if the state income tax deduction is taken away.

Controversy Over New Transportation Tax. There is new controversy over the transportation funding bill, SB 1, which Governor Brown signed into law on April 28th. The new law, which was promoted as a way to fix California's crumbling transportation infrastructure, will increase the tax on a gallon of diesel by 0.20 cents and gasoline by 0.12 cents in November (raising it to the second highest in the nation at 73.2 cents per gallon), and beginning in 2018 will increase vehicle registration fees by $25-$175 per year and add a $100 per year fee on low emission vehicles. The controversy relates to the lack of restrictions on use of the funds (estimated at $52.4 billion over 10 years), and last minute side deals which benefit four legislators whose votes allowed the measure to pass. It appears only 20% of the funds will go to the transportation fund - the rest will go into the General Fund and can be used however the legislature decides. In addition, SB 496 and SB 132 benefit these four legislators and/or their districts. SB 496 shields engineers from government lawsuits (one senator is an engineer), and SB 132 diverts transportation funds to Merced and Riverside Counties (where the other legislators reside).

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