January 17, 2013

Going Global – Preparing to do Business in Another Country

Going Global - Agenda

1. Welcome/Introduction – CPAmerica/Horwath …… Mike Gillis

2. DMJ Tax – FBAR and FACTA …….. Milton Howell

3. Advanced International and Planning Strategies …… Sean King

4. International Financial Reporting and Assurance Standards …… Art Winstead

5. Questions and Closing …… Mike Gillis

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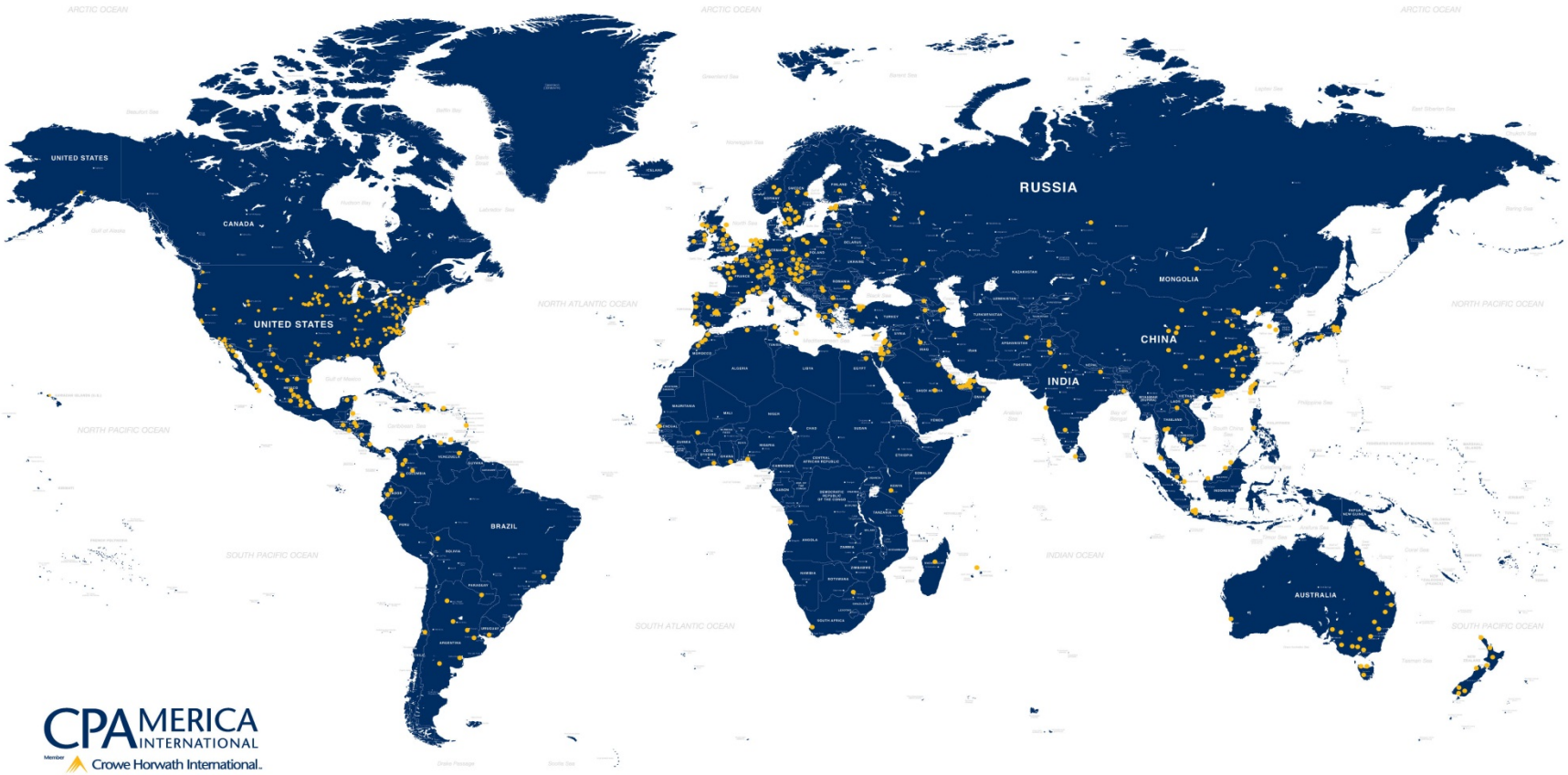
CPAmerica International

Connecting Global Resources



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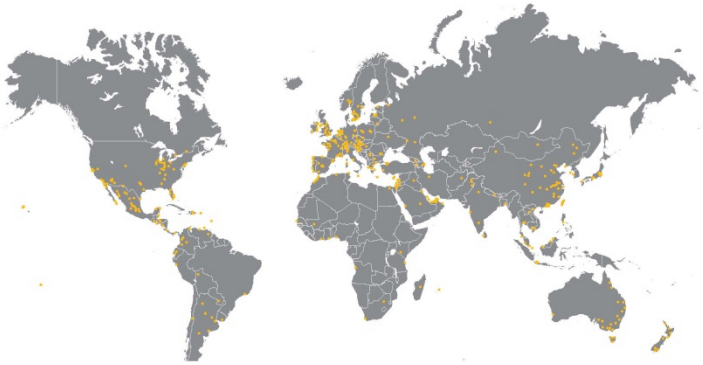
Accounting Organizations World Rankings

CPAmerica International/Crowe Horwath International

Worldwide Ranking

RANK	FIRM	REVENUE	PARTNERS	EMPLOYEES	OFFICES
1	PricewaterhouseCoopers	$29.22 billion	8,697	168,710	771
2	Deloitte	$28.80 billion	9,673	181,566	---
3	Ernst & Young	$22.88 billion	8,671	151,841	718
4	KPMG	$22.71 billion	8,150	144,677	700
5	BDO	$5.67 billion	4,723	48,767	1,118
6	RSM International	$3.90 billion	3,132	32,674	698
7	Grant Thornton International	$3.79 billion	2,619	31,581	527
8	Baker Tilly International	$3.22 billion	2,577	24,481	642
9	CPAmerica International/Crowe Horwath Intl.	$2.89 billion	3,283	27,294	650
10	PKF International	$2.62 billion	2,234	21,432	440



Based on 2011 figures from *International Accounting Bulletin*.

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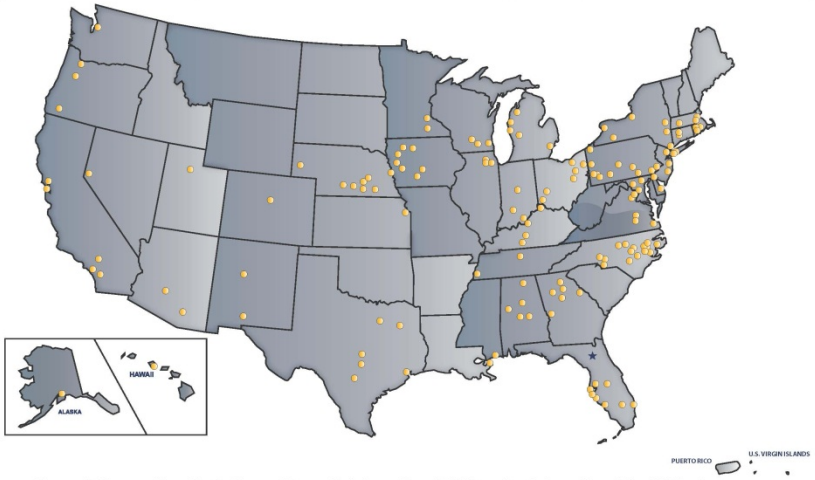
On The Map

CPAmerica International



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Cambodia
Canada
Channel Islands
Chile
China
Colombia
Costa Rica
Croatia
Cyprus
Czech Republic
Denmark
Dominican Republic
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DMJ Tax –
FBAR and FACTA

R. Milton Howell, III, CPA, CSEP, CGMA

Two Different Foreign Asset Disclosures

- Form 90-22.1 – Foreign Bank Account Report "FBAR"
  - Submitted to the US Treasury annually on June 30 for the prior calendar year – unrelated to your tax return.
- Form 8938 – Statement of Specified Foreign Financial Assets "FACTA"
  - Included with your form 1040 tax return – currently only a requirement for individual taxpayers but that may change in the future.
- These requirements are unrelated and you well may be subject to both!

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Foreign Bank Account Report

- Who must file – US persons (citizens, resident aliens, trusts, estates, corporations, and partnerships),
- Who have an interest or signatory authority in a foreign financial account that meets the threshold.
- If you have a joint interest in the account, each joint owner must report the entire balance.
- Threshold is an aggregate value of $10,000 or more at any time during the calendar year.

Foreign Bank Account Report

- A foreign financial account is –
  - Checking, savings, brokerage, securities, deposit, futures, commodities, or other similar financial institution account.
  - Includes an insurance policy with a cash value, an annuity with a cash value, or shares in a mutual or other pooled fund.
- It does not matter whether it is a US or a foreign financial institution. For example – A US account with UBS is not subject, but an account with a Chinese branch of Bank of America is subject.

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Foreign Bank Account Report

- A US person has a financial interest in a foreign account where any of these are true –
  - The US person is the owner of record with the institution, regardless of whether the US person owns the assets in the account.
  - The owner of record is –
    - An agent, nominee, attorney or other person acting on behalf of a US person,
    - A corporation in which a US person owns 50% or more, directly or indirectly,
    - A partnership in which a US person owns 50% or more in profits or capital,
    - A trust in which a US person is the grantor and retains an ownership interest,
    - A trust in which a US person has a greater than 50% interest in assets or income,
    - Any other entity in which a US person owns 50% of the voting power, value of equity or assets, or interest in profits

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Specified Foreign Financial Asset Report

- Who must file – US citizens, resident aliens (including nonresidents elect to be taxed as resident aliens), bona fide residents of American Samoa or Puerto Rico,
- Who have an interest in certain financial assets over the reporting threshold and who file a form 1040 series tax return.
- Threshold is an aggregate value of –
  - Unmarried taxpayers – $50,000 on the last day of the year or $75,000 at any time during the year
  - Married taxpayers filing jointly – $100,000 on the last day of the year or $150,000 at any time during the year
  - Married taxpayers filing separately – ½ the joint amounts
  - For taxpayers living abroad who meet the presence abroad test – the above thresholds are quadrupled

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Specified Foreign Financial Asset Report

- Presence abroad test – satisfy one of these tests –
  - Bona fide resident test – A US citizen who has been a bona fide resident of a foreign country for an uninterrupted period that includes the entire tax year.
  - Physical presence test – A US citizen or resident who is present in a foreign country at least 330 days in any 12 consecutive months that end in the tax year.

Specified Foreign Financial Asset Report

- A specified foreign financial account is –
  - Any account subject to the FBAR requirement.
  - Interest in foreign pensions and foreign deferred compensation plans.
  - Foreign-issued life insurance or annuities with a cash surrender value.
  - Loans by a US person to a foreign person.
  - Certain other foreign financial assets held for investment but not in a financial institution account such as –
    - Stocks, bonds, or similar securities issued by a non-US entity.
    - Any interest in a foreign partnership.
    - Known interests in trusts or estates.
    - Any financial instrument or contract where the issuer or counterparty is not a US person.

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Specified Foreign Financial Asset Report

- A specified foreign financial account is NOT –
  - A financial account of a domestic branch of a foreign financial institution.
  - An interest in a foreign government social security, social insurance, or similar program.
  - Directly-owned foreign currency.
  - Directly-owned precious metals.
  - Directly-owned personal property.
  - Directly-owned personal or business real estate.

Penalties

- Penalty for failure to file FBAR report –
  - Can be as high as the greater of 50% of the value of the account, or $100,000 annually.
- Penalty for failure to file FACTA report –
  - Up to $10,000 for failure to file or fully disclose, and an additional $10,000 for each 30 days of non-filing after IRS notice of failure to disclose, for up to $60,000 annually. Additional criminal penalties may apply.

Preparing to do Business in Another Country

Sean M. King

Agenda

- Operational / non-tax considerations
- Taxation of US corporations doing business outside of the US
- Cross-border planning opportunities

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Operational / non-tax Considerations

Initial Considerations

- What is the opportunity?
  - Export/Distribution?
  - Manufacturing
    - Is “foreign” manufacturing permitted?
  - Contract manufacturing?
    - Can I protect my IP?
  - Procurement?
    - Can I avoid FCPA risk?
  - Local sales?
    - Employees or ind. contractors?

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Initial Considerations con'd

- Do I know the counter-party?
  - The importance of due diligence
- What is the angle?
  - Profit-generation as a goal?
  - Or, mere relationship facilitation?
- Am I allowed to do it?
  - Regulatory restrictions?
    - OFAC, for instance

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Major Structuring Considerations

- What entity form to use?
- How to finance the entity?
- How do we access our profits?
- How do we get out?

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Taxation of US corporations doing business outside of the US

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The Challenge

- US persons are taxed on their worldwide income.
- Conversely, the majority of jurisdictions tax their corporations based upon the effective place of management and control, not merely on place of incorporation.
- The result: double or triple taxation.

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Exposure to Foreign Income Tax

- US firms generally face exposure to foreign income taxes when their activities in the foreign jurisdiction rise to the level of a “trade or business” within that jurisdiction.
- This concept is similar to “nexus” in a multi-state context.
- When income tax treaties exist, the generic “trade or business” concept is replaced with the more formal definition of a permanent establishment.

Permanent Establishment

- The Permanent Establishment (PE) tax treaty concept is similar to “trade or business” but allows more activities without giving rise to an income tax exposure in the jurisdiction.
- A PE generally is created by a fixed place of business.
- Fixed place of business includes:
    - place of management
    - branch
    - office
    - factory
    - workshop

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Permanent Establishment con'd

- Permanent Establishment <u>excludes</u>:
  - Facility for maintenance of goods solely for storage, display or delivery.
  - Maintenance of a fixed place of business solely for carrying on activities that are preparatory or auxiliary in nature.
  - Engagement of broker or agent of independent status.
  - Subsidiary of parent unless parent carries on business itself.

Anti-deferral regimes

- Controlled Foreign Corporations
  - Subpart F Income
  - Investment in U.S. Property (Sec. 956)
- Passive Foreign Investment Companies (PFIC)
- Foreign Personal Holding Company (FPHC)

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Why FTC Does Not Eliminate Double Taxation?

- Some foreign tax payments are not creditable
- Not all U.S. taxes can be reduced by the credit
- FTC limitation restricts creditability
- Differences in source of income rules

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Creation of Foreign Entities & Outbound Transfer of US Assets

- Creation of foreign entities and outbound transfer of US assets may have tax consequences under § 367
  - Otherwise tax deferred transactions (e.g., § 351 or § 368 reorganization) may be currently taxed (the "toll charge")
- Certain cross-border and foreign-to foreign reorganizations may trigger current taxation
- Always consider potential § 367 implications when expanding overseas or reorganizing foreign group

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“Check the Box” Rules for Entity Classification

- Use of check-the-box entities is a valuable planning tool in cross-border operations
- Post “Check the Box” rules:
  - Meet regulations criteria and elect
    - Reg. § 301.7701-1 through 3
    - Can’t check the box on *per se* entities

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Cross-border planning opportunities

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Tax positions
From the shareholder perspective

Best Case	Next Best Case – Closely Held
US Shareholder of Haven Corp Haven Corp principle to all operating entities Cost-plus to affiliates Reinvest earnings in Haven Capital gains tax on shareholder disposal Net effective rate = 20-30%	US shareholder of LLC All affiliates are Check the Box All income and tax flows to shareholders Less cash to reinvest if pay s/h tax Net effective rate = 40%
Next Best Case - Public	**Worst Case**
US Shareholder of US Corp Operating entities in hi-lo jurisdiction Deferral and Territorial Repatriation Capital gains on disposal Net effective rate = 30-60% - depending on non–US revenue mix	US shareholder of US Corp Operating entities in high tax jurisdiction Exposure to double taxation Distributed earnings Net effective rate = 65+%

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Treasury Management

- Repatriation planning:
  - Applicability of treaty network
    - LOB provisions
    - Treaty shopping
  - Need for substance

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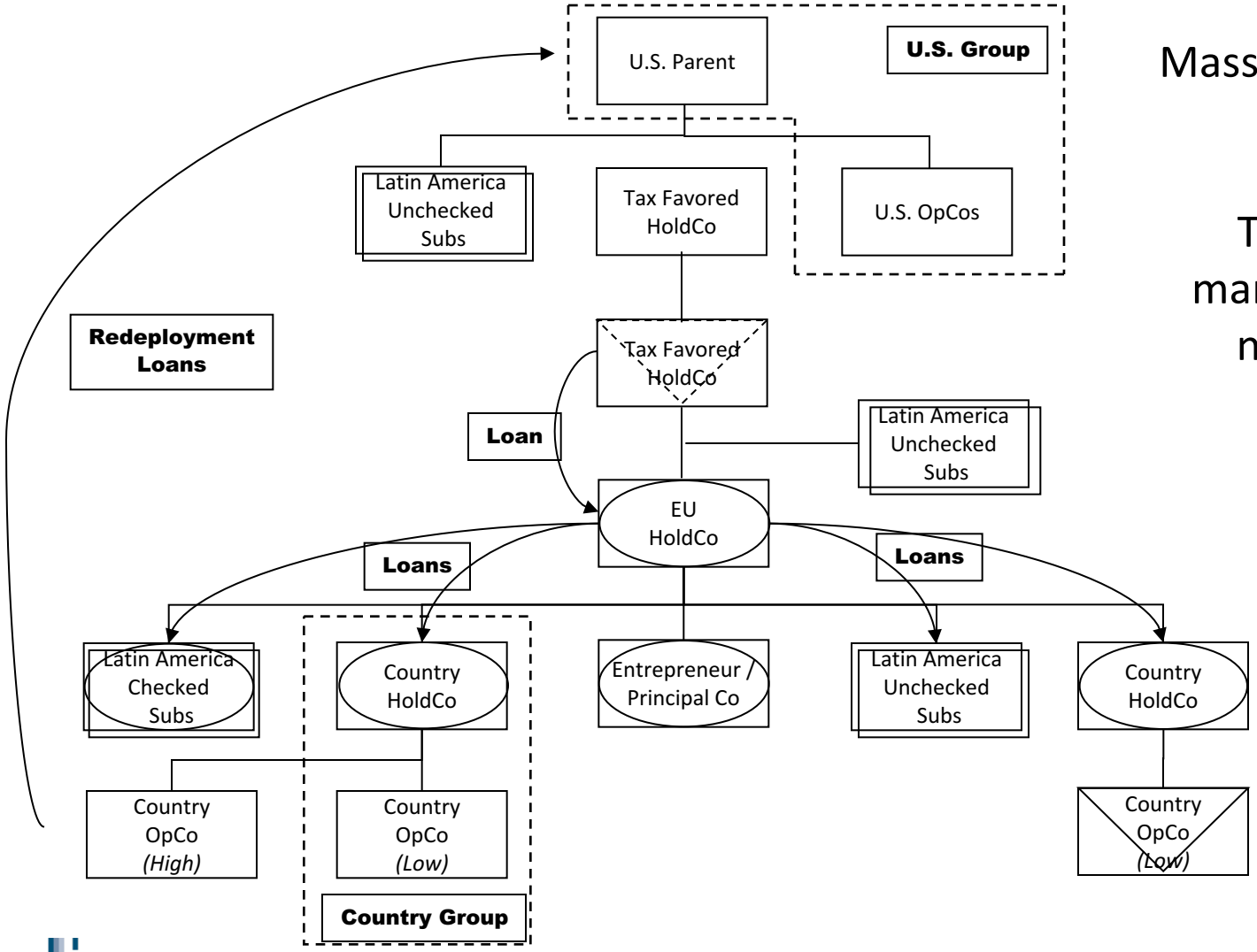
Effective Holding Company Structuring:



Mass confusion?

Or

Treasury management nirvana?

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Effective Holding Company Structuring

- Daily Benefits:
  - "Cleaner" cash repatriation and redeployment
  - Availability of broader treaty network
    - » Mitigation of LOB restrictions
  - Management of anti-deferral regime – "Subpart F"
    - » Avoids current income inclusion without corresponding cash repatriation

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Effective Holding Company Structuring

- Long-term Benefits:
  - Global effective tax rate management (cash & financial statement)
  - Reduction of worldwide effective tax rate
  - Increased global control on group liquidity
  - Reduced operating costs by eliminating day-to-day operations
  - Improved overall attractiveness of structure as a potential acquisition “target”

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International Financial Reporting and Assurance Standards - IFRS, IAASB ISAs, and IAASB Review and Compilation Standards

International Standards

Takeaway- This is the easy part!

Do not let IFRS and its differences with the FASB codification bother you!

International Standards

- Are there differences in the U.S. Standards and the International Standards?

YES!

- Are these differences significant?

YES!

- Should these differences prevent you from conducting international business?

NO!

International Standards – A Short History

- IFAC- International Federation of Accountants
  - Somewhat similar to the oversight provided by the AICPA in establishing the Boards (ASB and ARSC) and the FAF provides for the FASB.
  - IFAC appoints the Boards responsible for both the international financial reporting (IASB - accounting) and the international assurance (IAASB – audit, review, and compilation) standards.

International History (cont'd)

- In 2002 the AICPA initiated a process through which audit, review, and compilation standards would be clarified and converged. Audit standards are complete. Review and compilation standards are still in process.
- Today the AICPA assurance standards are known as "international plus/+."
- If an assurance engagement is performed in accordance with the AICPA standards, the engagement is performed in excess of the international assurance standards.

International History (cont'd)

- In 2006, the FASB and the IASB entered into an agreement to converge financial reporting standards. Progress has been made, but differences still exist today.
- Frustration has developed within the IASB/IFAC, the FASB, the SEC, international business market participants and market makers in the lack of convergence being achieved.
- In recent some individuals within the groups listed above have expressed "convergence in financial reporting standards may never be achieved".

International History (cont'd)

- Several years ago, the AICPA and the SEC (non-U.S. companies) permitted the use of IFRS as an acceptable financial reporting framework; i.e., there is no longer a qualification to an assurance report regarding the use of IFRS by a reporting entity.
- So, today assurance standards = converged in form for and substance for audits and substance for other assurance engagements.

International Financial Reporting Standards - Where Are We Today?

- FASB = condorsement concept with IFRS
- SEC = discussing the condorsement concept
- What does condorsement equal? It depends on whom you ask. The FASB codification would continue to exist. The current MOU would be completed. The FASB would not begin work on any MAJOR projects. Rather, the FASB would initiate a new project with the priority being convergence with IFRS only for IFRS standards not currently on the IASB agenda.
- Yes, not much changes for the foreseeable future.

The Differences – There Is No Intent To Discuss Them All……

- Editorial comment- regardless if convergence is never achieved, IFRS will continue to greatly influence the development of the FASB Codification.

Differences (cont'd) – Financial Periods Presented

- While most differences are somewhat "similar" and easy to understand, the presentation of required financial periods is somewhat difficult to understand. IFRS requires the presentation of the previous period while FASB does not.

Differences (cont'd) – Revenue Recognition

- FASB – two broad categories:
  1. **Realized or realizable**
  2. **Earned**
- IFRS – four broad categories:
  1. **Sale of goods**
  2. **Rendering of services**
  3. **Others using the entities assets**
  4. **Construction contracts**

IFRS revenue recognition principles are by type and principles based. FASB revenue recognition principles are extensive.

Differences – Revenue Recognition (cont'd)

- IFRS does use the principle of "milestones" for revenue recognition. FASB uses a more rules laden basis for revenue recognition. However, more often than not, most revenue recognized in most exchange transactions is very easy to apply to both – differences exist for transactions of production, construction, and service or warranties.
- FASB allows vendor-specific objective evidence (VSOE) while IFRS does not. This results in more elements meeting the separation requirement under IFRS.

Differences – Revenue Recognition (cont'd)

- IFRS places more emphasis on fair value in an exchange transaction that FASB does not require.
- FASB requires the satisfaction of ALL contingencies before recognizing revenue. IFRS uses a concept of "more likely than not" in regard to the contingency, thereby, possibly recognizing revenue earlier than under FASB.

Differences (cont'd) - Consolidations

- IFRS may have this one right - IFRS prefers a control principle while FASB uses a rewards (beneficiary) and risk principle.

Differences (cont'd) – Statement of Income

- IFRS may have this one correct. IFRS <u>does not</u> segregate extraordinary items. FASB <u>does</u> segregate extraordinary items.

Differences (cont'd) – Inventory

- FASB permits the use of LIFO.
- IFRS does not permit the use of LIFO.

U.S. IRS "conformity" requirement may be the biggest hurdle here.

Differences (cont'd) – Earnings Per Share

- IFRS may have this one wrong. IFRS does not average the interim period changes. FASB does compute the averages based on the individual interim period incremental or changes to shares outstanding.

Differences (cont'd) – Development Costs

- Under certain circumstances, these costs are capitalized while under FASB, these costs are always expensed in the period the costs are incurred. Not sure who has that one correct.

Differences (cont'd) – Deferred Taxes

- FASB = current and non-current classification.
- IFRS = non-current only.

Differences (cont'd) – Income Statement Classification of Expenses

- FASB = disclosed by function.
- IFRS = function or nature.

Differences (cont'd) - Restatements

- IFRS requires the disclosure of the balance sheet at the beginning of the earliest comparative period restated. FASB does not require that disclosure. IFRS requirement would require three balance sheets due to the restatement - 1) current period, 2) prior period and 3) beginning of the prior period as restated.

Differences (cont'd) – Extraordinary Items

- FASB = recognized based on both unusual and infrequent.
- IFRS = prohibited.

Differences (cont'd) - Valuation

- Perhaps the greatest difference that exists in the standards is in regard to "value."
- There are differences regarding value for different types of assets and liabilities between the FASB and IASB.
- For the most part, there is consistency for financial assets and liabilities; but there are significant differences for non-financial assets and liabilities.
- A small difference, still needing to be agreed to, is the definition of financial and non-financial assets and liabilities.

Differences (cont'd) - Leases

- The FASB and IASB have reached a significant agreement in accounting for leases.
- This agreement will significantly affect accounting for leases in accordance with the FASB.
- The FASB is scheduled to re-expose the Lease ASU in the 2nd quarter of this year. The biggest delay in the release is the proposed effective date.

Differences (cont'd) – Perhaps Insignificant Accounting

- Other differences seeming to be easy to reconcile:
  - Segment reporting
  - Subsequent events
  - Related parties – a somewhat interesting discussion due to some related parties being families owning most of the significant business entities in some countries - OIL!

Questions and Closing

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