US imposes reporting rules on Delaware Companies

Revamped rules for Delaware Companies create new obligations for owners and eliminate any vestiges of confidentiality that once made these offshore structures attractive for some property buyers. Effective since the beginning of 2017, Delaware Limited Liability Companies (LLCs) that are wholly owned by a non-resident now become subject to specific US reporting requirements. The changes are intended to provide the Internal Revenue Service with improved access to information that it needs to satisfy its obligations under tax treaties, information exchange agreements as well as to strengthen the enforcement of US fiscal laws.

> ***"Under these rules, a Delaware Company engaging in holiday lets or long-term rentals with their Portuguese property now has reporting obligations both in the US and in Portugal."***

New and existing LLCs need to obtain an "EIN" (US Tax Identification Number) and, in the process, designate a *Responsible Person* (beneficial owner). The LLC is seen as foreign-owned *Disregarded Entity*. This is a fiscally transparent company, meaning the US tax authority will "look thru" the company structure and assess the *responsible person* (beneficial owner) directly for any tax due on *Reportable Transactions* (chargeable events).

The LLC needs to maintain books and records of transactions to track any payments or transfers of money, property or other *reportable transactions* between the *disregarded entity* and its member, whether such operations are direct or indirect. These records must be available for inspection by the US Internal Revenue Service (IRS) on demand.

Some important definitions

In order to understand these changes, semantics become crucial, particularly when contrasting British and American usage of technical and judicial jargon. Beyond the brief synonyms given in the text (above in brackets), the following definitions translate US tax-speak used by the Internal Revenue Service into plain English.

- "A *foreign person* includes a non-resident alien individual, foreign corporation, foreign partnership, foreign trust, a foreign estate, and any other person that is not a US person".
- A Delaware LLC that has elected not to be treated as a normal US taxable corporation is automatically treated as a *disregarded entity*. A *Disregarded Entity* is a company that exists for legal purposes but not for income tax purposes. It is seen to be transparent. An LLC is considered to be a sole proprietorship when owned by an individual or a branch when owned by a corporation, trust or other entity.
- The *Responsible Person* (beneficial owner) is "the individual who has a level of control over, or entitlement to, the funds or assets in the Company". Any change in the *Responsible Person* must be reported to the Internal Revenue Service.
- *Reportable Transactions* are "any exchange of money or property between the LLC and its foreign member, such as sale, assignment, lease, license, loan, advance, contribution, or other transfer of any interest in or a right to use any property or money." For example, under these rules, a Delaware Company engaging in holiday lets or long-term rentals with their Portuguese property now has reporting obligations both in the US and in Portugal.

Reporting Transactions

Reportable Transactions must be declared on form 5472. Failure to file this form on a timely basis incurs a fine of $10,000. If the form is submitted on time but is incomplete or inaccurate, it is considered to be late and is still subject to the $10,000 penalty.

After an LLC is dissolved, cancelled or liquidated, it must file a final Form 5472, including any distribution of assets to its member. If the LLC changes status by electing to be treated as a taxable company, or adds members, becoming a partnership, it still must complete a final Form 5472.

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Conclusion

Coupled with "look-thru" changes in Portuguese law in the 2018 Budget governing the taxation of foreign companies holding Portuguese properties, these additional US regulations make life more complicated – and expensive – for Delaware Company owners.

While the US may still not be a co-signatory to the Common Reporting Standard (the international tax information sharing agreement between 105 countries worldwide), Uncle Sam has his own ways of tightening the screws when it is in the United States interest to do so.

Redomiciliation to Portugal continues to be the best long-term alternative to this increasing complex conundrum in Delaware. While the walls continue to close in on Offshore Companies in general and Delaware LLCs in particular, Portuguese Nominee Companies continue to be a rock of stability in an ever changing world.

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