Spring / Summer 2012

Legal Alert

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Foreign Accounts and the 2012 Offshore Voluntary Disclosure Initiative

By Caron N. Ikeda

One set of IRS rules that is receiving a great deal of attention recently is that related to reporting interests in foreign bank accounts. These reporting requirements have caught many taxpayers by surprise. Under these rules, any U.S. citizen or resident, domestic partnership, corporation, estate or trust with a financial interest in or signature or other authority over any financial account in a foreign country must report such interest if the aggregate value of the accounts exceeds $10,000 at any time during the calendar year. Besides owners or direct signatories, any person authorized to exercise a power in a manner comparable to signature authority, for example, a person who is authorized to act using a power of attorney, may also be subject to this reporting requirement. To comply, a person must annually complete and submit a Department of the Treasury Form TD F 90-22.1, Report of Foreign Bank and Financial Accounts ("FBAR"). The deadline to file the FBAR is June 30 of the year following the year the $10,000 test is met. The penalties for failing to do so can be severe. Failure to file FBARs can result in civil penalties of up to $10,000 per violation, with additional civil and criminal penalties to be applied for willful failures to report the foreign accounts.

Thanks to the reinstated Offshore Voluntary Disclosure Initiative Program ("OVDI"), there may be some relief out there for those who did not report taxable foreign account income in the past and did not file FBARs to disclose the associated accounts. Similar programs in 2009 and 2011 have been successful for the IRS, resulting in the collection of $4.4 billion from delinquent taxpayers. Under the 2012 OVDI program, taxpayers must (1) provide copies of previously filed original and amended income tax returns, (2) file original and amended offshore-related information returns and FBARs, (3) cooperate in the voluntary disclosure process, and (4) pay all tax, interest and penalties. Taxpayers can only participate in the program if they are not currently being examined by the IRS. Even under this amnesty program, the penalty is punitive. The penalty is 27.5% of the highest account value during the eight full tax years prior to the disclosure.

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This may result in significantly lower penalties, however, than those imposed if the taxpayer is not under this program. The penalty for willful failure to file FBARs can be the greater of $100,000 or 50% of the balance of each foreign account for each of the eight full tax years prior to disclosure. There are several lower levels of penalty, but these infrequently apply. There is a lower 5% penalty that applies in limited circumstances such as if taxpayer did not open, have frequent contact with or make withdrawals of more than $1,000 per year from the foreign account, or if the taxpayer is a foreign resident who is a U.S. citizen and is not aware that he or she is a U.S. citizen. A second lower 12.5% penalty applies if the aggregate value of all foreign accounts is less than $75,000. Another bonus of the program is that it allows taxpayers to avoid criminal penalties. The IRS may impose an accuracy-related or failure to file or failure to pay penalty whether or not taxpayer participates in the program. Unlike earlier programs, the 2012 OVDI program does not have an expiration date, but the IRS can terminate the program at any time.

Taxpayers should also be aware of the recently enacted Foreign Account Tax Compliance Act ("FATCA") which imposes certain income tax return reporting requirements on U.S. citizens and residents with foreign financial assets with an aggregate value exceeding $50,000 (or $100,000 for married taxpayers) on the last day of the tax year, or more than $75,000 (or $150,000 for married taxpayers) at any time during the tax year. Different thresholds apply to U.S. citizens and residents living abroad. Beginning with tax year 2011, those required to report must include IRS Form 8938 with their income tax return. Failure to file Form 8938 can result in a maximum civil penalty of $60,000. Additionally, underpayments of tax attributable to the non-disclosed foreign asset may be subject to a substantial understatement penalty of 40% and criminal penalties also may apply. The goal behind FATCA reporting is to cause taxpayers to report their income from these foreign accounts on their individual income tax returns.

Starting next year, it will become even more difficult for taxpayers to evade payment of tax on offshore accounts. Under the FATCA provisions, foreign financial institutions will be required to report to the IRS information about financial accounts held by U.S. taxpayers or by foreign entities in which U.S. taxpayers hold a substantial interest. Foreign financial institutions will also be required to withhold 30% on certain types of payments including U.S. source interest and dividends, gross proceeds from the disposition of U.S. securities, and pass through payments, unless an institution enters into an agreement with the IRS. The terms of the agreement with the IRS would require the foreign financial institution to (1) identify its U.S. accounts, (2) report certain information to the IRS regarding these accounts including the name, address and taxpayer identifying number of each account holder and the account number and balance in the account, and (3) withhold 30% on certain payments to non-participating foreign financial institutions and account holders who are unwilling to provide the required information.

The important thing for U.S. taxpayers to remember is that any foreign account holdings will require some additional reporting. Overlooking this requirement may lead to significant penalties and perhaps unwanted extra visits with lawyers and accountants.

For more information on this article, please call Caron at 531-8031 ext 609, email her at cni@hawaiilawyer.com, or scan the code with your smartphone.

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ADA and Service Animals

Under the Americans with Disabilities Act ("ADA"), State and local governments, businesses, and nonprofit organizations that serve the general public must allow service animals to accompany people with disabilities in all places where the public is normally allowed to go. For example, a restaurant must allow service animals in public areas even if health codes would prohibit animals on the premises; a hotel must allow service animals into all areas where customers are generally allowed, even if the hotel has a no-animals policy.

Last year, amendments to certain provisions of the ADA went into effect. One major change included revision of the definition of a "service animal". Under the amended definition, a service animal is "any dog [and in certain circumstances, miniature horses] that is individually trained to do work or perform tasks for the benefit of an individual with a disability, including a physical, sensory, psychiatric, intellectual, or other mental disability." The new regulations make clear that dogs, and in certain circumstances miniature horses, are the only species acceptable as service animals; other species which may have been acceptable under the old regulations no longer qualify.

The amended ADA regulations also make clear that the work or tasks performed by the service animal must be directly related to the handler's disability. Examples of acceptable work or tasks include, but are not limited to, assisting blind individuals with navigation and alerting deaf individuals to the presence of sounds. However, the provision of emotional support, well-being, comfort, or companionship does not constitute a qualifying work or task under the revised regulations.

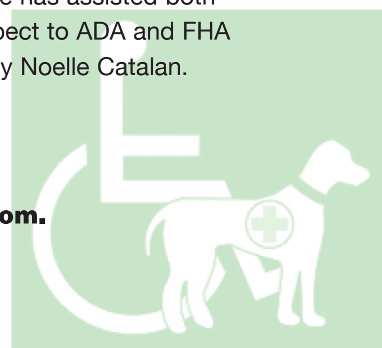
While these changes in the ADA regulations significantly affect businesses, they present much less impact for residential developments, such as condominiums. However, such residential developments are still subject to the Fair Housing Act ("FHA"), which requires landlords, condominium associations, and other housing providers to offer "reasonable accommodation" to residents with disabilities. In certain circumstances, "reasonable accommodation" may include allowing a resident to keep a service animal in his or her residence. Unlike the ADA, the FHA does not provide a per se definition of a service animal and does not make any distinctions between qualifying species, certified and non-certified animals, and animals that provide purely psychological support.

In order to be protected under the FHA with regard to service animals:

1. The individual must have a disability (under the FHA, a person with a disability is an individual who has a physical or mental impairment that substantially limits one or more major life activities, or has a record of an impairment, or is regarded as having an impairment. It is not necessary that the disability be obvious);
2. The animal must serve a function directly related to the individual's disability; and
3. The individual's request for the service animal must be reasonable.

An example of "reasonable accommodation" under the FHA is modification of a condominium's no-pet policy to accommodate the right of a person with a disability to have a service animal, provided that the animal serves a function directly related to the individual's disability. Refusal to permit such an exception may constitute a discriminatory practice, as it may deprive a disabled individual of the use and enjoyment of his or her dwelling.

While ADA and FHA regulations may be confusing and sometimes tricky, businesses, housing providers, and individuals must be aware of their rights and responsibilities regarding service animals. Our office has assisted both businesses and individuals with respect to ADA and FHA compliance issues. Article written by Noelle Catalan.



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Did Anna Nicole Smith (or her heirs) get The Money?

By Michael A. Yoshida

You probably know the name Anna Nicole Smith: celebrity, model, and actress. Famous for who-knows-what. But did you know that a case about her ended up in the Supreme Court, and is a landmark in bankruptcy law?

Before I get to Anna Nicole's case, here's some background. In 1982, the Supreme Court held that under the Constitution, federal bankruptcy courts, unlike other federal courts, may hear only a limited range of issues. In response, Congress created a system which allows bankruptcy courts to consider "core proceedings," which include matters involving the administration of a bankruptcy case, and the allowance or disallowances of claims and counterclaims asserted by a bankruptcy estate. Technical issues, to be sure. Here's where the Anna Nicole case comes in. Last June, the Supreme Court placed further limits on the jurisdiction of bankruptcy courts in these "core proceedings."

In 1991, Texas magnate J. Howard Marshall II met Anna Nicole, then named Vickie Lynn Smith. Three years later, the 89 year-old Marshall and the 26 year-old married. The marriage lasted 14 months until Marshall's death. Earlier, starting in 1982, Marshall transferred most of his property to a trust which named Marshall and his son Pierce as co-trustees. Marshall also had personal property and income outside of the trust. When his first wife died in 1991, Pierce became the trust's primary beneficiary, and continued as its trustee.

After Marshall and Anna Nicole married, he gave her gifts of cash and property, including $6 million in cash, jewelry, title to a Texas ranch, and a Mercedes Benz. However, she was never identified as a legatee, devisee or beneficiary of the trust, and was not permitted to participate in any capacity with respect to Marshall's business interests. In 1992, Marshall created a will, which required the distribution of his probate estate to the trust.

Shortly before Marshall's death, Anna Nicole filed suit in Texas against Pierce, asserting that Marshall intended to provide for her after his death and Pierce had interfered and breached his fiduciary duty as trustee under the trust. She also challenged the validity of the trust on the basis of undue influence and the lack of mental capacity of Marshall (although she did not challenge Marshall's mental capacity to make the gifts to her previously mentioned). She asked the court to name her the owner of the property in the trust. Three days after Marshall died, she filed another action in a Texas probate court seeking to establish that Marshall died intestate (without a valid will). If she was right, then under Texas' intestate succession laws, Anna Nicole would inherit a large portion of Marshall's estate.

In 1996, Anna Nicole filed a Chapter 11 bankruptcy petition in the federal bankruptcy court in California. Pierce filed a claim, and an adversary complaint alleging defamation. In response, Anna Nicole filed a counterclaim asserting claims similar to those she made in the earlier Texas lawsuits, and requested damages totaling several hundred million dollars as well as punitive damages. After a five month trial, a jury in the Texas probate action returned a unanimous verdict in favor of Pierce; Anna Nicole was not entitled to any distribution from Marshall's estate. The following year, a California U.S. District Court, after reviewing the Bankruptcy Court's proposed findings and conclusions suggesting a total award of $474,754,134.00, awarded judgment in favor of Anna Nicole in the amount of $88,585,534.66 in compensatory and punitive damages.

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The Ninth Circuit reversed the judgment, concluding that Anna Nicole's counterclaim was not a "core proceeding." This meant that the bankruptcy court lacked jurisdiction, and Anna Nicole's award was void. As a result, the Texas probate court's judgment was the final judgment resolving the parties' dispute.

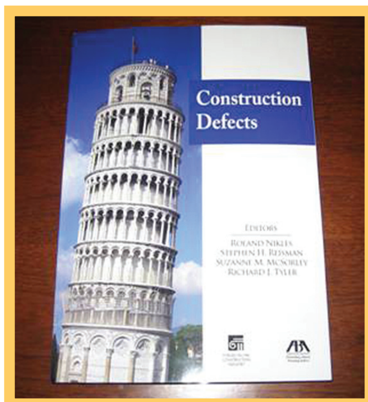
In a 5-4 decision, the U.S. Supreme Court held that although Anna Nicole's counterclaim may have been a "core proceeding," the bankruptcy court lacked the constitutional authority to issue a final ruling on state law counterclaims. Under Article III of the U.S. Constitution, except for very few limited exceptions not applicable in the case, such power is limited to Article III judges whose independence is guaranteed by lifetime tenure. Bankruptcy judges serve for limited terms, and, as a result, are not "Article III" judges. Accordingly, the Supreme Court affirmed the Ninth Circuit's decision and held that the District Court should not have given any weight to the bankruptcy court's findings and conclusions and should have afforded preclusive effect to the Texas state probate court judgment. By this time, however, both Anna Nicole and Pierce had died, so their estates were left to carry on.

Apart from being a very public and notorious celebrity case, why does the result matter? Commentators have opined that the Supreme Court's rationale calls into question the ability of bankruptcy courts to consider and resolve a wide range of what were considered "core matters." In addition, bankruptcy court jurisdiction over state law matters or claims based on non-bankruptcy federal law against creditors is in doubt. Others have suggested that the case should be narrowly construed and limited to state law counterclaims that are not fully resolved in the claims resolution process.

To answer the question posed by the title – no, Anna Nicole or her heirs did not get the money.

For more information on this article, please call Mike at 526-3626, email him at may@hawaiilawyer.com, or scan the code with your smartphone.

Did You Know



Anna Oshiro co-authored a chapter in a book entitled Construction Defects that was just published by the American Bar Association and sponsored by the Forum on the Construction Industry. Construction Defects delves into various legal aspects related to issues that commonly arise on construction projects.

To order, scan the code with your smartphone or go to: http://delivr.com/1h23w

USCIS Announces New I-9 Form

By David P. McCauley

U.S. Citizenship and Immigration Services (USCIS) announced it has re-designed its I-9 Employment Eligibility Verification Form. US employers should be familiar with I-9 forms, as they have been required since 1987 under the 1986 Immigration Reform & Control Act (IRCA). IRCA made it illegal to knowingly "hire, recruit or refer for a fee" anyone not authorized to work in the US. Employers must verify employment authorization with Form I-9. It was always a one-page form, but that's about to change. **It has not changed yet, so for now keep using the current form.**

The new two-page form and its instructions can be found at http://www.regulations.gov/#!documentDetail;D=USCIS-2006-0068-0013, or go to the "News" tab at www.uscis.gov and click on the March 27, 2012 story, "USCIS Seeks Public Comment on Revisions to Employment Eligibility Verification Form I-9."

Failure to complete the I-9 form, or to complete it correctly, can be a serious, costly mistake. Recently, Department of Homeland Security and US Immigration and Customs Enforcement have moved from workplace raids targeting workers to focusing on employers through I-9 audits and administrative fines. In testimony before the House Judiciary Committee, DHS Secretary Napolitano said that since FY-2009 ICE conducted more than 6,000 audits, double the number during the Bush administration, assessing more than $76 million in fines. The new I-9 may help employers avoid these costly mistakes.

So what's different in the new I-9? It's two pages long, so there's more room. (Well, maybe not the address block: Kalanianaole Highway will be a tight fit.) Employee and employer sections are on separate pages, making it clear who is responsible for what. This and the fact that Section headings (e.g., "Employee Information and Attestation" and "Employer Review and Verification") are now shaded, should make the most common mistakes, such as failing to complete and/or sign and date their respective sections of the form, less likely. And there won't be questions about where to sign: instead of signature lines ("Do I sign above or below?"), the new form has boxes. The new I-9 asks the employee's "first day of work for pay." The current form asks when the employee "began employment," often confused with the date of hire.

In addition to required information, the new I-9 has optional blocks for employees' email addresses and phone numbers. The instructions explain this "may assist DHS in contacting you regarding verification of your employment authorization." Employees may think twice about this...

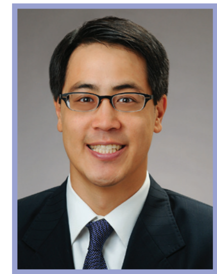
One source of confusion on the new form pertains to "aliens authorized to work," a box which must be checked, if applicable. If checked, the form asks for the person's Alien Registration Number or Form I-94 number. Form I-94 is the arrival/departure card issued when someone enters the US with a nonimmigrant visa. Employers may not know what these numbers are, and employees may not have them handy. For persons issued I-94 forms, the new I-9 asks for the passport number and country of issuance. Asking to see the employee's passport could violate US anti-discrimination laws.

As of this writing, the new form is not yet in use. Before it is, changes will likely be made. Expect changes in the informative USCIS Handbook for Employers, too. Readily available at USCIS.gov, it and Form I-9 are USCIS' most downloaded files.

For more information on this article, please call David at 531-8031 ext 618, email him at dpm@hawaiilawyer.com or scan the code with your smartphone.

Recent Developments Concerning Hawaii Vacation Rentals

By Gregory W. Kugle



By Christopher Pan

Damon Key represents a number of clients who are involved in Hawaii's short term vacation rental industry. We believe along with these clients that vacation rentals are an important part of diversifying Hawaii's tourism and economy.

During the 2012 spring legislative session, the Hawaii State Legislature considered a number of bills addressing vacation rentals. Senate Bill 2089 was first introduced in January 2012. The proposed bill would have required non-resident vacation rental owners to hire a local property manager. A subsequent amendment to the bill changed the requirement from employing a local property manager to employing a local real estate agent. The bill was supported by property management companies and realtors.

The bill was targeted at those property owners that lived outside of the state of Hawaii or on a different island from where their vacation property was located. The stated rationale was that the bill would collect millions of dollars of uncollected tax revenue from vacation rentals, although the assumption that non-resident owners were avoiding their tax obligations was not supported by evidence and fiercely contested by non-resident owners.

Following the mobilization and testimony of numerous property owners both in Hawaii and from out of state, the initial bill H.B. 2089 was deferred on March 12, 2012. This effectively killed the bill, and was a victory for its opponents. Opponents from as far away as Canada, Alaska, Washington, Oregon and California submitted testimony in opposition.

However, in a startling illustration of how the legislature operates, the Hawaii Senate resurrected the bill 10 days later and inserted the language from the deferred bill wholesale into another bill, House Bill 2078. The bill retained the requirement for non-resident vacation rental owners to employ a real estate agent, along with requiring the prominent posting of information about the non-resident owner and his or her local contact.

On behalf of our clients, we continued to express our concerns to the Legislature about the constitutionality of the proposed bill. We believed that the bill was patently unconstitutional discrimination against non-resident property owners by the State of Hawai'i, in violation of the United States Constitution. The United States Constitution prohibits discrimination against non-residents through the Equal Protection, Privileges and Immunities and Commerce Clauses. It is well-settled law that the right to own and dispose of privately-held property is a "fundamental right" for purposes of the Constitution. Under the Equal Protection and Privileges and Immunities Clauses, discrimination on the basis of residency is reviewed under strict scrutiny. The proposed bill would be unconstitutional if it was not necessary to further a compelling state interest. Likewise, under the Commerce Clause, the inquiry is whether the law regulates evenhandedly with only incidental effects on interstate commerce, or whether it discriminates against interstate commerce, which means different treatment of in-state and out-of-state economic interests. The courts have held that if a restriction on commerce is discriminatory, it is virtually per se invalid.

While the bill proceeded through the legislative process, it was repeatedly amended, with various onerous and potentially unconstitutional requirements removed at each stage. The requirement to employ a real estate agent was replaced with the requirement to employ a local contact, and later, the requirement that the local contact be employed for pay was also removed. Finally, the distinction between non-resident owners and resident owners was removed entirely, so that the bill now requires all vacation rental owners to designate a local contact of their own choosing.

As of the writing of this article, the bill has been passed by the Legislature and is awaiting the Governor's signature. While the problematic provisions discriminating against non-resident owners were removed from the bill, other onerous and legally problematic requirements remain. These include the requirement that vacation rental owners post certain information in their advertisements that other owners are not required to disclose, information that raises concerns regarding privacy, fraud and identity theft. We, along with our clients, will continue to monitor the progress of HB 2078, along with other legislation that impacts vacation rental owners.

For more information on this article, please call Greg at 526-3603, email him at gwk@hawaiilawyer.com or call Christopher Pan at 526-3614, email him at cp@hawaiilawyer.com, or scan the code with your smartphone.

Greg

Chris

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ADVERTISING MATERIAL

Legal Alert is published periodically by Damon Key Leong Kupchak Hastert to inform clients of legal matters of general interest. It is not intended to provide legal advice or opinion.

Attorneys in the News

Tred R. Eyerly was a panel member on June 13, 2012 on a webinar put on by Strafford Publications. The title of his presentation is “Triggers in First Party Property Claims.”

Rebecca A. Copeland was selected as a Fellow for the 2012 Hawaii State Bar Association Leadership Institute.

Courtney S. Kajikawa and **Caron N. Ikeda** spoke at an estate planning seminar hosted by Palolo Chinese Home at Waialae Country Club on April 26, 2012.

Christine A. Kubota served as Facilitator at the Hawaii Justice to Access Conference on June 12, 2012 - JUSTICE IN JEOPARDY: Expanding Access to Justice in Challenging Economic Times, leading the conversation on Overcoming Linguistic and Cultural Barriers. As Chair of the Honolulu Japanese Chamber of Commerce, Chris will celebrate the Chamber’s 30th sister-chamber relationship with executives from the Hiroshima Chamber of Commerce and Mayor of Hiroshima. They will participate in the Pan-Pacific Festival Parade on June 10th. Chris is being installed as the United Japanese Society President on June 23, 2012. Her year as Chair of the Japanese Chamber ends on June 30, 2012.

Gregory W. Kugle has been appointed to the Board of Directors for Meritas, a global alliance of independent full service business law firms located in more than 75 countries. Greg was elected to the position during the alliance’s recent annual meeting. Damon Key Leong Kupchak Hastert is the only representative in Hawaii.

Mark Murakami was the Planning Chair of the “Hawaii Eminent Domain and Land Use Conference” in Honolulu on May 9, 2012. Robert Thomas, Anna Oshiro, and Greg Kugle were also on the faculty. The Conference focused on legal issues surrounding the Honolulu rail project, including condemnation, construction bid protests, rail financing, and burial and environmental issues.

Christopher Pan was selected as a Fellow for the 2012 Hawaii State Bar Association Leadership Institute.

Robert Thomas, **Anna Oshiro**, and **Mark Murakami** are the attorneys representing the plaintiffs in a federal lawsuit seeking to invalidate the 2012 Hawaii legislative reapportionment plan. The firm represents eight plaintiffs – active duty military, spouses, prior service military, and Oahu residents – in a challenge under the Equal Protection Clause of the U.S. Constitution. The 2012 Reapportionment Plan is unconstitutional because it did not include 108,000 military, military families, and university students who do not qualify to pay resident tuition, in Hawaii’s apportionment and districting process. They are included in the U.S. Census as Hawaii residents and in Hawaii’s Congressional districting, but expressly excluded in the state legislative plan. In April, the Honolulu Star-Advertiser’s lead editorial supported the lawsuit, writing “Census should guide election boundaries.”