

# gyb

Growing your business™

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**pwc**



## ***GYB***

is published by PwC's Private Company Services (PCS) practice. Here we discuss the challenges privately owned businesses face and where the opportunities lie, suggesting how you can effectively make the most of both.

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**Rich Stovsky**  
US Leader  
Private Company Services

Private companies are feeling optimistic again. After a wary few years, confidence in the US economy has returned to pre-recession levels, where it's been holding steady since late 2010. Looking ahead, many privately held businesses expect positive revenue growth over the next year and plan to increase their operational spending. Projected major capital investments are up as well.<sup>1</sup>

One place that private companies' renewed confidence is evident is in the US IPO market, where fourth-quarter 2010 activity reached levels unmatched since 2007. A strong first-quarter IPO performance suggests that equity-market activity in 2011 will prove even more impressive than in 2010. That's good news for companies contemplating an initial public offering. Important as market timing is, however, companies should wait to take the plunge until after they have thoroughly assessed whether they are indeed ready for public life and the many responsibilities it brings.

In some cases, an IPO is a way to raise capital for business expansion. Increasingly we're seeing such expansion take place abroad, particularly in emerging and fast-growing markets (EFGMs). China ranks as the top EFGM destination — 69% of private companies surveyed for PwC by the Economist Intelligence Unit say they are either already investing in China or planning to do so soon.<sup>2</sup>

As China's economic clout grows, the way Western companies do business in that country is beginning to change: Foreign businesses are increasingly finding that they need to take the interests of Chinese stakeholders into greater account. This calls for adaptability and a willingness to seek common ground. Private companies, which are often more nimble than their public counterparts, may therefore find they have an advantage when it comes to achieving Chinese stakeholder alignment.

In looking for growth opportunities in China and elsewhere around the globe, private companies inevitably confront a variety of risks, chief among them corruption — cited as the top risk of doing business in EFGMs among surveyed private companies. Such risk includes the possibility that a company could unwittingly engage in corrupt practices itself.

One way companies can mitigate corruption risk is by complying with the Foreign Corrupt Practices Act (FCPA). While violations are more frequent than management may suspect and can come at considerable cost — particularly now that the US Department of Justice has stepped up its FCPA enforcement — they are also avoidable if a company has adequate understanding of the act's provisions.

This also holds true of reporting requirements for individuals investing abroad — an understanding of what needs to be reported and when will help taxpayers avoid sanction by the IRS. New rules introduced under the Foreign Account Tax Compliance Act of 2010 add a layer of complexity to an already complicated reporting scheme and should be carefully reviewed by individuals with global holdings.

I hope you find this issue of *GYB* helpful as you and your business chart the course ahead. My Private Company Services colleagues welcome your thoughts about the topics discussed in these pages, as well as other issues facing your business. Please feel free to contact me, any of the authors, or your local team to start the discussion.

Sincerely,

A handwritten signature in dark ink, appearing to read "Rich". The signature is fluid and cursive, written in a professional style.

<sup>1</sup> PwC's quarterly *Trendsetter Barometer Business Outlook Survey*

<sup>2</sup> *Building a Presence in Today's Growth Markets: The Experience of Privately Held Companies*, PwC, 2011



**04**

**IPOs are back:  
What potential players need to know**

While one of the most rewarding transactions a company may undertake, an IPO can also be among the most daunting. Ample preparation will improve the odds of making a successful entrance in a newly robust IPO market.

**Volume 63**  
**Growing your business  
in today's economy  
and beyond**

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**Foreign Corrupt Practices Act:  
What you don't know could cost you**

Companies may be violating anti-corruption laws without realizing it, potentially leading to criminal charges and forfeited business opportunities. With adequate awareness, businesses can avoid such pitfalls.

A man in a dark suit and blue shirt is looking intently at a large display of business cards. The display is a wall of cards, some of which are held by a hand in the foreground. The background is a trade show booth with blue and red lighting. The man is wearing a name tag that says "EST@CBS".

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### China strategy: Refining yours could open new doors

Private companies' entrepreneurial agility may give them a key advantage in today's China, where business success increasingly depends on flexibility and finding common ground.

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### Personal investments abroad: The IRS is taking a closer look

For all that the intricacy of new global-reporting requirements may confuse taxpayers, the IRS won't accept that as an excuse for noncompliance. Individuals should familiarize themselves with the new rules now to avoid costly oversights.

# *IPOs are back: What potential players need to know*

While one of the most rewarding transactions a company may undertake, an IPO can also be among the most daunting. Ample preparation will improve the odds of making a successful entrance in a newly robust IPO market.

## ***IPO volume and proceeds***

### **IPO volume (completed IPOs)**



### **IPO proceeds (in billion \$)**



Source: 2010 US IPO Watch: Analysis and Trends, PwC, March 2011

After a lackluster couple of years, the US IPO market made a strong comeback in 2010, with a 143% increase in volume over the prior year and a 55% leap in deal value. Fourth-quarter IPO activity proved especially vigorous, reaching levels the market hadn't seen since 2007.<sup>3</sup>

Continuing the momentum of 2010, IPO proceeds in the first quarter of 2011 reached \$12.4 billion, the highest first-quarter value since 2008 and a 194% increase in offering proceeds over first-quarter 2010. The strong first-quarter performance puts the US IPO market on pace to eclipse the proceeds for all of 2010, which totaled \$39 billion. The first quarter of 2011 also saw 52 new companies enter the IPO pipeline, signaling growing confidence in the US equity markets.<sup>4</sup>

Certainly this is welcome news to companies that have been contemplating an initial public offering. A positive market environment, however, is just one — albeit critical — factor in successfully executing an IPO. If a company isn't sufficiently prepared for public life and the many responsibilities it brings, the best market timing in the world will be of only so much help to that business.

Preparing to be a public company is more than just a one-day event. The process requires intense, long-term planning and execution to avoid the many potential pitfalls that come with transitioning to life as a public entity. The markets are still in recovery mode and short-term volatility will continue to challenge prospective issuers if they're not thoroughly prepared to move when the moment is right.

“In short, an IPO is not something to enter into lightly,” says Henri Leveque, a partner in PwC's Transaction Services group. “That said, with the right preparation and approach, going public can be an effective way to tap the capital market and a key component of an organization's growth strategy.”

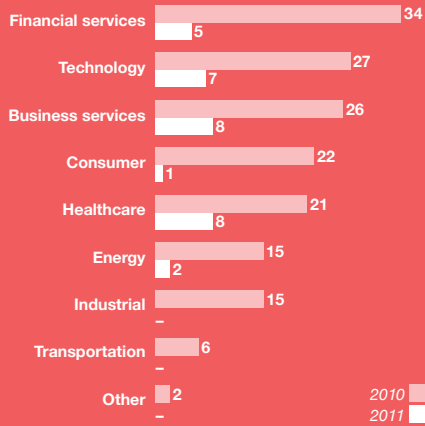
<sup>3</sup> 2010 US IPO Watch: Analysis and Trends, PwC, March 2011

<sup>4</sup> US IPO Watch Q1 2011, PwC, March 2011



### Market snapshot

Where the deals are happening:  
Completed IPOs in 2010 and 2011



### Who's behind them

#### The main players

*Financial sponsors:* In 2010, 128 IPOs were backed by financial sponsors, amounting to 76% of total IPO volume and 45% of total proceeds. With financial sponsors contributing 75% of the IPO volume in the first quarter of 2011, private equity looks to be a major player this year, too.

*Non-US issuers:* Issuers from outside the United States contributed 58 IPOs in 2010. Among the 13 countries represented, China was most active, with 42 IPOs. In the first quarter of 2011, foreign issuers accounted for 11 IPOs, six of them from China.

Source: 2010 US IPO Watch: Analysis and Trends, PwC, and US IPO Watch Q1 2011, PwC, March 2011

**Many tightly held private companies keep their cards close to their chest. Once a company goes public, it will have to show those cards.**

### **Sizing things up**

In considering an IPO, private companies should carefully assess their organizational and market readiness for going public. Most importantly, they should determine whether leaving the private sphere is indeed the right move for them.

### **Why go public?**

There are various reasons for going public. Common goals include

- Raising capital for expansion
- Raising capital for future acquisitions
- Attracting and retaining top talent
- Diversifying and reducing investor holdings

A company's owners may also have reasons other than these, including personal ones. Those objectives should be clearly communicated to the company's key stakeholders, with everyone agreeing on what the business hopes to achieve by going public.

There should also be consensus on whether going public is in fact the best way to achieve the agreed-upon objectives. Companies seeking capital, for instance, may find that accessing funds via other avenues (e.g., debt, private equity sources, or mezzanine funds) is a better or more-efficient option than an IPO.<sup>5</sup> A business should explore all reasonable alternatives before making a decision.

Then, too, there's the matter of knowing what exactly an IPO entails—both the preparation for the transaction itself (no small undertaking), as well as the ongoing demands and responsibilities of being a public company. Companies that venture down the IPO path with a well-studied roadmap in hand should be well equipped to face the challenges ahead.

### **A public-company mindset: Does your business have one?**

While IPO preparedness involves many logistical considerations (accounting, regulatory, legal, tax), there's also the matter of whether a company is mentally prepared for the public arena. Before proceeding with an IPO, a company should gauge whether it is both culturally and psychologically ready for the changes that public status will bring.

### **Withstanding public scrutiny**

"Many tightly held private companies keep their cards close to their chest," notes Dan Frey, a partner in PwC's Private Company Services practice. "Once a company goes public, it will have to show those cards." This forfeiture of privacy starts with the initial registration statement that's filed with the Securities and Exchange Commission (SEC) and continues with the various ongoing financial-statement disclosures that a public company must make about numerous aspects of its business, operations, finances, and executive compensation.

"Because private companies often keep these details to themselves, suddenly having this information come under the scrutiny of regulators, analysts, shareholders, and the financial press can be quite jarring," says Frey. "Companies that prepare themselves for this new reality should have an easier time adapting to it."

### **Meeting performance expectations**

A company must be ready to meet shareholder and market expectations from Day One. For their part, shareholders will expect the company to meet short-term performance goals and want to see steady growth in areas such as sales, profits, market share, and product innovation. Analysts' short-term earnings expectations must be met as well. A company's failure to hit these marks can dramatically hurt the long-term valuation of its business. Chief among a newly public company's challenges, then, is learning how to balance short-term growth objectives with the long-term health of its business.

<sup>5</sup> For more on the range of capital sources available to private companies, please see *Growing Your Business*, Issue 62, "Financing the Future: Strategies for Accessing Capital," PwC, 2011.

## Spotlight on compensation

### The Dodd-Frank Act

Companies contemplating an IPO will want to be alert to the executive-compensation provisions in the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010. The provisions apply to all public companies. Here's a glance at some of them:

*Expanded compensation disclosures:* Companies will now need to disclose (1) the relationship between executive compensation and the company's financial performance, including stock performance and dividend policy; (2) the median compensation of all employees (excluding the CEO), the CEO's total compensation, and the ratio of the two; and (3) the company's policy regarding whether employees or directors are allowed to hedge the risk in equity securities that are received as part of their compensation.

*Say on pay:* These are nonbinding, advisory shareholder votes regarding executive compensation. Boards may be under pressure to react to say-on-pay voting results. If they ignore the results, board members could become the target of a withhold-vote campaign in subsequent board elections.

*Clawback provisions:* These are more stringent than the clawback provisions under Sarbanes-Oxley. A company will now have to claw back all excess financial compensation that was paid based on erroneous financial statements (even if the reporting errors were unintentional). Clawbacks will reach back three years before the year of the financial restatement and extend to the compensation of all executive officers (not just the CEO and CFO), including those who have left the company.

*Compensation committee independence:* The Act introduces independence requirements similar to those required of audit committees, primarily by mandating that the SEC direct national securities exchanges to prohibit listing any company lacking an independent compensation committee.

## Spotlight on sustainability

Public companies have a fiduciary responsibility to provide investors with transparent information about the risks and opportunities that can influence stock prices. Such risks and opportunities include those pertaining to sustainability and climate change.

Regulators — including the SEC and EPA — expect corporations to adequately disclose and appropriately manage the potential impact of climate change. Consumers, prospective investors, and other stakeholders have expectations as well.

Take shareholders, for instance. In the 2010 proxy season, they filed a record 100-plus climate change resolutions — an almost 50% increase over the previous year.\* The targets of those resolutions were not limited to companies in the energy sector. They also included big-box retailers, financial institutions, and construction companies.

Board members and management at IPO-bound companies should therefore develop a plan for addressing public expectations and concerns about sustainability. The time to initiate this effort is in the IPO-planning stage. Doing so will help the business respond appropriately to due diligence inquiries from prospective investors, underwriters, and credit rating agencies.

During this process, the company should assess the financial and reputational risks that sustainability and climate change pose to the business, as well as see how competitors are positioning themselves in the marketplace vis-à-vis these concerns.

\* Investor Network on Climate Risk, a project of Ceres



## ***The market moment***

### **Determining whether yours has arrived**

The demand for and timeliness of an initial public offering can vary dramatically, depending on a number of market forces. Financial-reporting considerations may influence an IPO's timing, too. Staying alert to these factors is critical, since missing an IPO window by as little as a few weeks can result in a postponed or withdrawn IPO or a lower market valuation.

A good way to gauge whether now is the right time to make your public debut is to look at your business through the eyes of the market. Determine, for instance, whether your company has a sufficiently appealing track record. Generally, a company that outpaces the industry average in growth will have a better chance of attracting prospective investors.

Also determine how well your business can demonstrate, through historical sales data and accurate forecasting, that it has a reasonably good prospect of maintaining strong sales and earnings growth. Prospective investors will want to see such indications. In the case of early-stage companies, they may need to rely on emphasizing the uniqueness of their products or services in lieu of presenting an established track record.

### Relinquishing control

Once a company issues publicly traded shares, the company's owners must forfeit a portion of the returns associated with the business's growth. They'll also have less ability to control the company's ownership.

These and other considerations (including IPO expenses—legal, accounting, actuarial) should be taken into account when a company weighs the pros and cons of going public.

### **The evolution of your company**

There are three general phases of an IPO:

- IPO readiness
- The IPO process
- Life after the IPO

While each phase has its own set of activities and concerns, the second and third phases overlap a good deal. That's because the completion of an IPO isn't so much the end of a process as it is the beginning of the company's new life.

Indeed, life at the company changes as soon as the decision to go public is made. The required preparation in the months leading up to an IPO is considerable and often distracting to the business, which will need to devote significant time, effort, and money to the undertaking. It is important, therefore, that a company be sure it has adequate in-house resources before venturing down the IPO path, or else enlists outside expertise. A business must be ready to meet shareholder, regulatory, and market expectations at the outset.

"Not only that," says Fentress Seagroves, a principal in PwC's Transaction Services group. "A company needs to realize that the hard work isn't over once the initial public offering is completed. The business must match the effort it put into going public with the effort of actually being public." This includes meeting a range of ongoing obligations to regulators, shareholders, and other market participants.

### **IPO readiness: Learning to think and act like a public company**

While the planning process for an IPO can start as little as three months before a public offering, PwC recommends that a well-considered plan be executed over a period of one to two years: "This window gives a private business the chance to properly assess the challenges of being public," says Leveque, "as well as time to practice thinking and acting like a public company." During this period, a company should take the following steps:

#### *Build an effective management team:*

The investment community wants to be sure a company isn't being run single-handedly. The management team needs to be cohesive and share a long-term vision for the company, to obtain maximum financial return and valuation.

#### *Appoint independent members to the board of directors and create an audit committee:*

All of the major stock exchanges and markets require that a registered company have a majority of independent directors on its board. "Taking the time to build out the board of directors well before an IPO event is critical to the overall success of going public," says Frey. A public company's board must also have an audit committee, which plays a key role in ensuring the integrity and transparency of a company's financial reporting. Investors now expect such reporting to undergo objective, board-level review.

#### *Evaluate corporate governance principles and practices:*

Both the NYSE and NASDAQ require that corporate governance standards be met. NYSE companies must, in addition, have an internal audit function. Institutional and other investors will also be looking to see whether sound corporate governance is in place.

#### *Take stock of processes and infrastructure:*

Any weakness in systems or failure to comply with regulatory requirements could bring the company public embarrassment, reputational damage, and fines.

*Check whether your financial reporting and internal controls are up to speed:*

Life as a public company means getting comfortable with the rhythm of quarterly and annual reporting and ensuring that there are sufficient internal controls for that reporting.

— *Assess readiness to meet stringent compliance demands:* A public company's finance department must have sufficient accounting and reporting expertise to file quarterly and annual financial statements with the SEC. The company's CEO and CFO will also have to personally evaluate and explicitly report to the public the effectiveness of the company's internal controls for financial reporting (per the Sarbanes-Oxley Act of 2002). The company's external auditor, too, will need to annually attest to the effectiveness of those internal controls.

— *Have your financial statements audited and resolve potential issues:* Part of this entails being able to describe, in both the initial registration statement and all future financial statements, the effect that underlying factors have had on the company's performance. Failure to do this will shake investor confidence and might even result in delisting.

— *Lax reporting isn't an option:* Without adequate financial reporting, a company not only makes itself vulnerable to enforcement action by the SEC, but also impairs its ability to (1) accurately forecast results and (2) analyze current-period results for purposes of budgeting and subsequent financial reporting—a vicious cycle any company would wish to avoid.

“However, financial reporting, done well, is more than just a compliance exercise,” points out Frey. “It's also an effective way to communicate to investors. Presenting an accurate and transparent narrative in its financial statements is critical to a company's ongoing success in the marketplace.”

*Have a tax checkup:*

This exercise helps a company understand the tax advantages and tax costs of going public. There are often significant tax-saving opportunities that can reduce the taxes of the company or individual owners if properly planned before the IPO.

— *Assess tax-allocation consequences:*

Most companies are generally in the form of a C corporation. Therefore, either prior to going public or as a result of an IPO transaction, an S corporation will generally terminate its S corporation status and become a C corporation. The next day, the company will begin a new tax year as a C corporation and have to decide how to allocate its taxable income, deductions, and credits between the two tax years (the S corporation tax year and the C corporation tax year). This allocation choice will have significant tax consequences that should be planned for well in advance of the IPO.

*The IPO process / Life after the IPO*

Preparing for life as a public company should happen in parallel with the IPO process. Although there are activities that occur only in the run-up to an IPO, such as choosing a stock market and an underwriter, many of the IPO-preparation activities will carry over into the company's post-IPO life.

Perhaps the biggest difference between these two phases is that during the IPO process, the unavoidable flurry of preparatory activity poses a considerable distraction to the business. During that time, much attention is given to the initial filing of documents, due diligence, and marketing effort, which compete with the day-to-day business for management's attention. Once the transaction is completed, however, certain other IPO activities will simply become par for the course in the company's new life as a public entity:

*Develop budgets, forecasts, and performance measures:*

Proper budgeting, forecasting, and performance measurement, along with a public company's ability to meet its (and analysts') earnings estimates, can significantly impact the company's stock performance. The market allows very little margin for error in this area.

*Maintain investor enthusiasm:*

Public perception of a company has a direct effect on the value of its stock. "If investor enthusiasm wanes, so will trading," cautions Seagroves. "If a company's shares trade thinly, there's a good chance the intended benefits of the IPO won't be achieved." It's important, therefore, that a public company have a solid investor-relations team that communicates regularly with investors, analysts, and the media to maintain a positive image and to ensure that the company's story is being told accurately.

*Comply with Sarbanes-Oxley requirements:*

Upon filing its financial statements with the SEC, a company must comply with certain provisions of the Sarbanes-Oxley Act. The most significant of these provisions is the requirement that an independent auditor report on the effectiveness of a company's internal controls. "That requirement generally kicks in with the company's second annual report after the IPO, depending on the company's overall market capitalization," says Frey. "Compliance can be both time-consuming and resource-intensive, so companies should make sure they schedule accordingly and line up sufficient expertise."

**Conclusion**

Thinking through these realities well before deciding to go public is as important as market timing, if an IPO is to achieve the desired benefits. In some cases, those benefits can materialize as early as the first year after going public. In other cases, it might not be until several years after an IPO that a company knows for sure whether the benefits outweigh the costs. By planning early and striking the right balance of resources, a company can give itself the best possible chance for success when its IPO window opens.

**More information**

Want to learn more about IPOs? Please contact someone on the PwC team, including:

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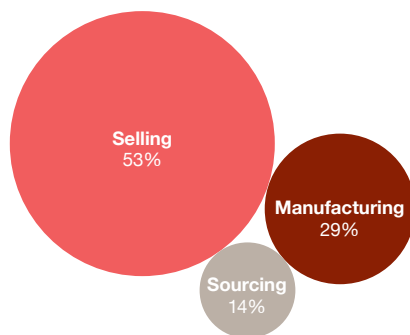
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# China strategy: Refining yours could open new doors

Private companies' entrepreneurial agility may give them a key advantage in today's China, where business success increasingly depends on flexibility and finding common ground.

## Best business opportunities in China, as cited by private companies

Source: *Building a Presence in Today's Growth Markets: The Experience of Privately Held Companies*, PwC, 2011



Looking to regain growth momentum lost during the recession, many private companies are setting their sights on China.<sup>6</sup> And for good reason: China is the world's fastest-growing major economy, providing ample business opportunities for companies headquartered in slower-growing Western markets.<sup>7</sup> But what Western businesses want from China—and the best way to go about it—is changing in many cases. What China wants in return is changing as well.

For their part, Western private companies are less interested in making goods in China these days than they are in selling them there. This reflects how rising wages are not only turning Chinese workers into consumers, but also making those individuals more expensive to employ. So while low-cost manufacturing continues to draw private companies to China, for many of them it's no longer the primary lure. Nor is China, for its part, relying wholly on exports to drive its growth, as it once did.

Rather, China's 12th Five-Year Plan (unveiled in March 2011) is focused on boosting domestic consumption, as well as shifting growth and investment inland. That shift may open up new opportunities for businesses that are willing to venture away from China's coastal cities, where competitors are saturating the market and skilled workers are at a premium. At the same time, higher wages and better employee benefits (additional goals of China's Five-Year Plan) should encourage more household spending across the country, leading to potential windfalls for appropriately positioned foreign businesses—while also presenting challenges for companies relying on China as a manufacturing hub.

Challenges are by no means restricted to manufacturing companies. Western businesses in general—whether they be big or small, public or private, manufacturers or sellers—are grappling with China's highly localized, relationship-driven culture, lack of protection for intellectual property rights, perceived growing protectionism, and struggles with an evolving regulatory environment, among other conditions.

<sup>6</sup> *Building a Presence in Today's Growth Markets: The Experience of Privately Held Companies*, PwC, 2011: A whitepaper based on a survey of 158 private-company executives primarily headquartered in North America and Western Europe.

<sup>7</sup> In a 2010 survey by the American Chamber of Commerce in Shanghai, 87% of respondents reported revenue growth; 79% reported being either very profitable or profitable; 61% reported gaining market share for their China products/services; and 71% expect a revenue increase in China of more than 10% in 2011. All indicators were up significantly from the corresponding figures in the 2008 and 2009 surveys.



**69%** of Western private companies say they are either doing or planning to do business in China.

Source: *Building a Presence in Today's Growth Markets: The Experience of Privately Held Companies*, PwC, 2011

“One way that some Western companies are dealing with these challenges is by paying closer attention to the interests of Chinese stakeholders and seeing where alignment can be achieved,” says Martin Foley, a PwC partner who’s worked with a variety of US private companies operating in China. “Those businesses have begun to seek common ground and mutually beneficial value propositions with China’s stakeholders—including the government, customers, suppliers, employees, and even competitors—making this a key part of their China strategy.”

Some would say this approach accords with the direction of US-China relations overall: As Eswar Prasad, a senior fellow at the Washington-based Brookings Institution, recently noted, “The two countries are becoming increasingly evenly matched in terms of economic clout.... The *quid pro quo* approach may be the only productive avenue.”<sup>8</sup>

### **The traditional strategy**

Whether a *quid pro quo* approach and stakeholder alignment become standard practice for Western companies operating in China remains to be seen. To date, such companies have tended to rely on a handful of well-rehearsed methods for market entry and expansion in China: set up a sales representative office, enter a joint venture with a Chinese partner (often required for investment in certain industries), or establish a wholly foreign-owned enterprise (WFOE)—with Hong Kong and China’s seaboard being the favored locations. Foreign businesses with deep pockets have also made outright acquisitions of Chinese companies.

Common to all of these methods—acquisitions, WFOEs, majority-ownership joint ventures, and sales-rep office setups—has been the foreign company’s ability to maintain control (over operations and quality) and efficiently export profits.

Often such approaches have been a logical extension of a company’s larger global strategy, with a team of experienced expatriate executives brought in to adapt the company’s global business practices to local operations. Chinese staff have been expected to adapt as well—to the business culture of their Western employer. Many are English-speaking graduates from China’s top universities, which tends to hasten the assimilation process, as do employee-development programs that some companies offer.

That many foreign investors—large multinational corporations (MNCs) and small businesses alike—continue to apply this overall strategy for doing business in China speaks to its ability to achieve positive results.

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8 US-China Strategic and Economic Dialogue; two-day high-level policy talks held in Washington, D.C. on May 9 and 10, 2011

9 *ibid*

10 [http://www.uschina.org/statistics/fdi\\_cumulative.htm](http://www.uschina.org/statistics/fdi_cumulative.htm)

11 National Bureau of Statistics of China

12 Jeffrey Immelt speech to AmCham Shanghai at the 2010 Shanghai World Expo, June 2, 2010  
<http://www.amcham-shanghai.org/AmChamPortal/Event/EventDetail.aspx?EventId=4486>

13 *Financial Times*, “Foreign Groups Told to Make Chinese Cars,” March 20, 2011

### ***New considerations***

As China continues to evolve, and at an accelerated pace, some Western companies have begun to consider refining their business strategy in that country. They see a China that, strengthened by its economic success over the past 30 years—as well as emboldened by its quick recovery from the global economic crisis—is changing the way it views both itself and its trading partners, with implications for how foreign businesses will operate in China going forward.

Some of those implications appear favorable to Western businesses, such as those likely to result from China's continued effort to align its policies and business practices with mature markets—e.g., via participation in the World Trade Organization and the country's recent commitment to delink its government procurement policies from its indigenous innovation policies.

Nevertheless, many Western businesses are skeptical. Not all of them are convinced that China's government will heed Treasury Secretary Timothy Geithner's call for the two countries to “share in the fortunes and bear the hardships together.”<sup>9</sup> Rather, they see a China that's seeking its own path of development, one that won't necessarily converge with the intended path of Western MNCs.

Why, such skeptics might ask, would China want to change policies and institutions that ushered in \$641 billion in foreign direct investment from 2000 to 2009,<sup>10</sup> produced 9.91% average GDP growth from 1979 to 2010,<sup>11</sup> helped to create globally competitive Chinese companies such as technology giant Lenovo and home-appliance producer Haier, and allowed China's economy to emerge from the global recession relatively unscathed?

Their skepticism notwithstanding, MNCs are unlikely to drop China from their business strategy. What they may do instead is seek a clearer understanding of where the ground is shifting—the better to position themselves for success in China's evolving business landscape.

### ***Where the ground is shifting: Challenges and opportunities***

There is no crystal ball that can show US companies precisely where and how China's business landscape will change over the next several years. But there is a blueprint: China's latest Five-Year Plan, which presents the central government's agenda for China's economic growth through 2015.

“What I love about China is that it's transparent,” remarked GE Chairman and CEO Jeffrey Immelt in a speech last year. “You don't have to guess. You just say, ‘What's the next Five-Year Plan?’ Okay, here's our company strategy...here's where we're going.”<sup>12</sup> Admittedly, the average private company might not find it so easy as all that. Still, an understanding of China's Five-Year Plan, and its socioeconomic backdrop, provides an indispensable compass for any Western business attempting to navigate the Chinese market. Here are some chief considerations for private companies to keep in mind as they chart their course forward:

#### ***China's desire to move up the value chain***

As China focuses less on low-cost manufacturing and more on moving up the value chain, various sectors have begun to question whether continued cooperation with foreign companies is the best way to achieve that goal. Some Chinese stakeholders argue that decades of foreign investment and growth have resulted mostly in massive profit exportation while doing little to build Chinese brands and develop local intellectual property.

“During 10 years of trying, China has become a big factory for foreign companies, and their Chinese partners didn't get advanced technology,” says Lang Xuehong, automotive analyst with Sinotrust. “Through [its new industrial policy, the central government] would like Chinese carmakers to get IP in order to own this market.”<sup>13</sup>



特价  
promotion

欧尚产品  
product

特价

特价  
promotion

The industrial policy Lang references has led to a number of significant changes in China's regulatory environment vis-à-vis foreign companies. Gone, for instance, are the nationwide tax incentives for foreign-invested enterprises, which had once helped to defray initial investment costs.<sup>14</sup> Instead the government is now targeting specific industries (e.g., the high-tech sector) and regions (Western/inland provinces) for development incentives, with the aim of bringing in intellectual property (IP) while downplaying low-cost, export-oriented industries.

These actions have inevitably heightened Western concern about Chinese protectionism, regulatory discrimination, and continued infringement of IP rights. In 2010, surveys by both the American Chamber of Commerce (AmCham) in Shanghai and the US-China Business Council (USCBC) pointed to perceived protectionism, lack of protection for IP rights, and struggles with the evolving regulatory environment.

But not all Western companies are equally worried. With respect to IP protection, CEO Bill Kozyra says that after 25 years of operating in China, his Detroit-headquartered company TI Automotive—a privately held global supplier of automotive fluid systems—is comfortable that the company is not at risk when it puts its most valuable technology in China.<sup>15</sup>

Indeed, the more experienced a private company is in emerging and fast-growth markets generally, the less risky China appears—this according to a recent joint study by the Economist Intelligence Unit and PwC. The study found that 75% of private companies investing in just one or two emerging and fast-growing markets consider China “high risk,” compared with just 41% of companies investing in five or more such markets. It also found that 93% of private companies investing (or planning to invest) in China characterize return on that investment as either high (55% of participants) or medium (38%).<sup>16</sup>

For companies such as these—which see as much (or more) promise in China's evolving business landscape as they do difficulty—a willingness to explore new types of cooperation with Chinese partners could help gradually ease the latter's mistrust, leading to mutually beneficial opportunities as China makes its way up the value chain. Private companies, which tend to have greater flexibility and swiftness than their larger public counterparts when it comes to adopting and executing new strategies, may be particularly well positioned to enter such relationships.

#### Focus on economic development inland

Another chief objective of China's 12th Five-Year Plan is greater economic development in its inland regions. This supports the central government's larger goal of reducing wealth disparity between the country's interior and the coastal cities.

Western companies willing to venture into China's interior may be able to take advantage of new tax incentives and other preferential policies. These are being rolled out by China's inland provinces to encourage foreign investment in certain industries (e.g., high tech and new energy). They include exemptions from or reductions in corporate income tax, value-added taxes, import taxes, and urban land taxes.

The provincial governments in China's interior are offering other, nontax incentives as well, such as subsidies, guarantees, and cost reductions for land, rentals, utilities, and the like. “Some of the incentives are quite substantial,” says Wendy Guo, a PwC tax partner in Beijing. “And they are available to companies in general, not just those in encouraged industries.”

Guo adds, however, that “foreign private companies are often unaware of these incentives. Consequently, many of them don't shop around to see what's available through the various local governments before deciding where to set up operations.”

***Western companies willing to venture into China's interior may be able to take advantage of new tax incentives and other preferential policies.***

<sup>14</sup> The favored tax treatment once given to foreign-invested enterprises was phased out with the 2008 implementation of the Enterprise Income Tax Law.

<sup>15</sup> *Building a Presence in Today's Growth Markets: The Experience of Privately Held Companies*, PwC, 2011

<sup>16</sup> *ibid*

Despite government incentives, an inland strategy in China could be a hard sell for many private companies just now and might not be appropriate in all instances. A key obstacle is that the business and physical infrastructure in China's western provinces currently lags behind that in coastal regions, often requiring foreign companies to establish their own.

For companies that aren't in a position to implement such solutions, a move inland may have to wait—although perhaps not for long: Roughly a dozen “supercities” are being rapidly developed throughout inland China and are scheduled to be linked by high-speed rail come 2015. With the interconnection of these once relatively isolated areas, large new markets should open up to Western businesses that look beyond China's seaboard.

#### **Tighter Chinese labor market in saturated coastal cities**

Much as Western companies may prefer to operate in China's coastal cities, those markets are becoming saturated with competition from MNCs and domestic businesses (both state-owned and private). The competition for talent, in particular, has intensified. Chinese companies can offer attractive pay these days and are—for the first time—actually becoming employers of choice.<sup>17</sup> Indications suggest that they're also providing work for a broader group (e.g., non-English-speaking Chinese employees), offering better opportunities for advancement, and enabling greater work/life balance.

Foreign companies in China are feeling the effect of these shifting expectations among Chinese workers. The AmCham and USCBC surveys both show that finding and retaining qualified staff in China is the number one issue for their survey respondents—a problem that has in turn contributed to increased wage costs (another key concern among the USCBC respondents) and higher turnover. Western companies may therefore want to consider exploring indigenous talent development and other creative HR solutions as they refine their China strategy (see sidebar on leveraging China's local talent).

#### **Greater bargaining power among Chinese competitors**

A tighter labor market is just one challenge posed by increasingly formidable Chinese competitors. Well financed and commanding high valuations, Chinese companies are also becoming more difficult for foreign MNCs to acquire. And they're growing less receptive to arrangements involving foreign majority ownership and control, choosing instead to set new conditions for joint business relationships, such as the contribution of intellectual property, technical know-how, and access to foreign markets. Western businesses that are open to these more-equitable arrangements may find new business opportunities available to them in China.

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<sup>17</sup> [http://www.chinadaily.com.cn/business/2010-08/23/content\\_11188800.htm](http://www.chinadaily.com.cn/business/2010-08/23/content_11188800.htm)

## Where policymaking = growth opportunity

Understanding Chinese government policies and then aligning a company's business strategy with them can be a winning approach, if done right. Take Caterpillar, for example:

When the Chinese government announced its \$586 billion stimulus package in 2008, Caterpillar identified opportunities in infrastructure spending and was ready to capitalize on them. Caterpillar's group president, Rich Lavin, who's responsible for the company's China operations, credits the company's strong growth to effective cooperation with the Chinese government on its stimulus package.

"With increasing domestic demand, the requirement for infrastructure will simply increase," says Lavin.\* The company continues to ramp up capacity in China, where this year it expects to produce 60% more excavators than in 2010.\*\*

\* [http://news.xinhuanet.com/english/2009-11/11/content\\_12428998.htm](http://news.xinhuanet.com/english/2009-11/11/content_12428998.htm)

\*\* <http://www.ft.com/cms/s/0/3d32d17c-2a18-11e0-997c-00144feab49a.html>

## Leveraging China's local talent

As it continues to modernize, China wishes to transition from being a labor-rich country to one that's talent-intensive. To this end, the government aims to increase China's pool of highly skilled workers from 114 million to 180 million by 2020\* — primarily through greater investment in higher education and human resources.

In the meantime, a number of Western companies have already been using local talent, placing them in management-level positions traditionally filled by expatriates. Not only does this help companies address the talent-shortage challenges they're starting to face in China, but it also helps them lower their costs and leverage the cultural intelligence of local workers. Such intelligence is particularly useful in an environment where complex social dynamics underlie all business interactions.

Indeed, for some private businesses, relying on local talent is nothing new. Take the privately held business TI Automotive, which has been operating in China for 25 years: The company employs only local staff. "Our president [of operations in China] is a Chinese national," says the company's CEO Bill Kozyra. "His whole management team is Chinese nationals. We don't have any Westerners running our business for us."\*\*

Local Chinese hires tend to be assimilated to Western business practices and possess leadership skills. Some foreign companies, however, have also begun hiring Chinese workers who don't fit the traditional mold. That's because while traditional hires generally make a good match for MNCs operating in coastal cities, they may be less well suited to a company looking to access markets outside China's top-tier cities. There, local culture and institutions can be markedly different from what many Western businesses are accustomed to in China, creating barriers to market penetration if the right local talent isn't on hand to help negotiate the cultural differences.

Negotiating cultural differences invariably helps foreign businesses better align themselves with Chinese stakeholders, such as customers, suppliers, and local officials. Admittedly, indigenous talent development might not suit every Western company, but for those willing to explore that avenue, it may present a distinct opportunity to build a sustainable competitive advantage over other foreign companies in China.

\* [http://news.xinhuanet.com/english2010/culture/2010-06/07/c\\_13336664.htm](http://news.xinhuanet.com/english2010/culture/2010-06/07/c_13336664.htm)

\*\* *Building a Presence in Today's Growth Markets: The Experience of Privately Held Companies*, PwC, 2011

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## ***Tax considerations***

Chinese tax law has become more detailed in recent years. Here are a few issues that China-bound US businesses may want to keep in mind:

### ***Interpretation / implementation***

While Chinese tax policy is clearer since enactment of sweeping changes in 2008, the interpretation, implementation, and enforcement of the tax code remain uneven across China. A business may find, for instance, that it can deduct certain expenses in one city but not in another. Likewise, the central government may indicate that particular entities qualify for certain tax incentives, whereas the local government may interpret the tax code as suggesting something else.

“To limit uncertainty about how to apply Chinese tax laws, it’s important for a company to know the priorities of the local government,” says Eugenia Rao, a partner in PwC’s Private Company Services practice, with a special focus on tax. “Enlisting advisors with knowledge of local tax-policy implementation can help you in negotiations with the local tax authority, as well as reduce the need for such negotiations.”

### ***Transfer pricing / management fees***

Companies operating in China should exercise caution when it comes to transfer pricing. “This is an area of focus for the Chinese tax authority,” says Rao. “It is conducting audits and taking a close look at mandatory transfer-pricing documentation. Businesses should therefore make sure their methodology is correct and robust.”

The allocation of management fees in particular may draw the Chinese tax authority’s attention. “Chinese law does not allow such fees to be charged at the Chinese-company level,” explains Rao. “If such charges are attempted, the tax bureau won’t issue a tax-clearance certificate, and so remittance on such charges will be impossible.”

If there is a US parent company, allocated management fees can be charged through to it, but the parent must be ready to withstand a high degree of scrutiny and supply adequate substantiation. The Chinese tax authority will require detailed information, such as the kind of management services the US company provided and hourly rates paid to the individuals providing those services.

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The Chinese tax authority is looking at service fees generally, not just management fees. “It’s important that the service fee of a US partner or parent be structured properly,” emphasizes PwC tax partner Wendy Guo, “so that it’s comparable to the benefits the Chinese company receives. Recognizing that some foreign companies may use service fees to export money out of China, Chinese tax authorities are increasingly viewing inter-company service payments closely—not only with regard to tax deductions for the Chinese payees but also with respect to levying Chinese business tax and potential corporate income tax for the foreign recipients.”

Smaller and midsize companies that haven’t built up political goodwill in China or have limited international tax expertise may be particularly vulnerable to the Chinese tax authority’s scrutiny. Pursuing more-collaborative approaches to doing business in China, whereby a fair amount of the profit is used to grow the business rather than being expatriated to the United States, could help alleviate the tax authority’s concern.

#### ***VAT/accounting discrepancies***

China’s value-added tax (VAT) is imposed on the transfer of tangible property. Generally, a business in China prefers to issue a VAT invoice and pay the tax after the goods have been physically received and paid for. That way, the recipient of the VAT cannot take a tax deduction until rendering payment, and the issuer of the VAT avoids being out of pocket for potential non-payment, as well as avoids the process of obtaining a VAT refund from the government.

Under these circumstances, a Chinese accountant usually will not record a sale until payment is received. In the case of a joint venture or other partnership between a US business and Chinese company, the US partner’s accountant would most likely follow accrual-basis accounting. Therefore, a variety of adjustments would have to be made to reconcile the US and Chinese approaches to accounting for the sale of tangible property.

To avoid the need for reconciliation (which can be onerous), management should devise a set of assimilated procedures and train their accountants in them. (For larger private companies, using a shared-services center is another option.) As both the United States and China continue to converge their accounting systems with International Financial Reporting Standards (IFRS), accounting discrepancies should become less frequent.

***Private companies' entrepreneurial agility may actually put them in a better position than their public counterparts when it comes to taking advantage of collaborative opportunities with Chinese partners.***

***Reimagining collaboration:  
Seeking greater common ground***

So what do these new business opportunities and arrangements look like? Currently, a number of deals in the pipeline involve Western MNCs taking a minority ownership stake in joint ventures with Chinese companies — a departure from the traditional approach. We've also begun to see MNCs explore creative minority cross-ownership structures, such as those in which the Chinese party has a majority ownership interest and management control in the Chinese joint venture while holding a minority interest in the MNC. In many of these instances, Western MNCs are offering technology, expertise, and global distribution support for Chinese products and services in exchange for distribution support for the MNCs in China and capital from the Chinese party.

While such arrangements might not be a natural fit for some US private companies — or, for that matter, Chinese businesses (which tend to be run by tightly knit management teams, with much of the decision-making often residing with the business owner) — these more equitable relationships are not the exclusive domain of public MNCs. Indeed, private companies' entrepreneurial agility — their ability to swiftly decide on a strategy, obtain the necessary approvals, commit capital, and then execute — may actually put them in a better position than their public counterparts when it comes to taking advantage of collaborative opportunities with Chinese partners.

Take, for instance, Thayer Lodging Group, a privately held real estate investment company that's based in Maryland. Last year it entered into a joint venture with Shanghai's Jin Jiang International Hotels to purchase Interstate Hotels & Resorts, a large independent hotel management company. Whereas in the past a US joint venture partner might have been the one supplying most of the capital in exchange for access to China's market, we've begun to see interests on both sides of the table converge, with the Chinese partner contributing substantial capital and proving equally intent on widening its market access. In the case of the Interstate deal, says Jin Jiang Group chairman Yu Minliang, "This acquisition significantly accelerates our ability to expand internationally, giving us immediate access to a worldwide platform."<sup>18</sup>

Approaches like these may require a psychological shift by companies that are accustomed to following a more traditional business model in China. Yet while larger MNCs tend to lead the way in embracing new market-entry and expansion strategies, smaller private companies have the advantage of generally being more nimble, with fewer corporate silos and more-centralized decision-making. Because these attributes are shared by many private-sector Chinese businesses as well, that common ground may make it easier for Western private companies to understand and appreciate the perspective of their Chinese counterparts — a distinct benefit in China's business culture, where relationships are critical.

Of course, before entering into a relationship with a Chinese company, a business will want to adequately assess the needs, interests, and capabilities of potential partners to determine whether there is indeed enough common surface. Proper due diligence is therefore essential. Once an appropriate partner has been vetted and taken on, a robust integration strategy should be put in place to ensure a smooth bridging of people and processes.

<sup>18</sup> <http://www.hospitalityworldnetwork.com/trends/developing-story-thayer-jin-jiang-hotels-purchase-interstate>

## **Conclusion**

While the traditional model of doing business in China will remain preferable and best suited to many private companies, it may be worth refining if China is a key component of their growth strategy. “Even if you choose not to explore more-innovative approaches to operating in China, it is important that you take the interests of Chinese stakeholders into consideration when reviewing your China agenda, seeking ways to align and reconcile those interests when they diverge, and doing so in ways that are mutually beneficial,” emphasizes Alan Chu, PwC partner and leader of US-China Business Services. “This allows you to essentially co-opt China’s long-term goal of economic stability and prosperity, making it integral to your China strategy—an approach that should benefit stakeholders on all sides.”

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## **More information**

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# ***Foreign Corrupt Practices Act: What you don't know could cost you***

Companies may be violating anti-corruption laws without realizing it, potentially leading to criminal charges and forfeited business opportunities. With adequate awareness, businesses can avoid such pitfalls.

As private companies continue to pursue growth abroad, they need to be mindful of the Foreign Corrupt Practices Act (FCPA), particularly now that the US Department of Justice (DOJ) has stepped up its enforcement of the act's provisions. Violations can come at considerable cost — not just in dollars and reputation, but also in lost business opportunities.

Many of today's business opportunities are in emerging and fast-growing markets (EFGMs), where private companies are increasingly venturing. Among recently surveyed private-company leaders, 76% cited corruption as a key risk in those markets.<sup>19</sup> There is also the risk of a company *unwittingly* engaging in what the FCPA deems corrupt practices — via routine procedures employees thought were permissible or through indirect violations.

“At times, it's more a function of what you don't know,” says Mark Reffner, a partner in PwC's Private Company Services practice, “and less a matter of your employees actively engaging in corrupt practices. A company may be proceeding in a way that it thinks is entirely above board, only to later find out it has unintentionally violated the act.”

Small and midsize businesses that do not retain in-house general counsel or a compliance officer could be at higher risk for violating the act than some of their larger multinational peers that routinely train international employees in FCPA awareness and have a compliance officer overseeing those efforts.<sup>20</sup>

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<sup>19</sup> *Building a Presence in Today's Growth Markets: The Experience of Privately Held Companies*, PwC, 2011

<sup>20</sup> Of the companies that participated in PwC's *Global Economic Crime Survey* (2009), over half with 1,001 to 5,000 employees reported encountering fraud.



“Such companies entering foreign markets for the first time are often unfamiliar with the nuances of the FCPA,” notes Sulaksh Shah, a director in PwC’s Forensic Services group. “Company leadership should definitely give the finer points of the act careful consideration, making sure their employees and business associates are aware of these, especially since the CEO, CFO, and other executive officers may be on the hook for corrupt actions taken by third parties on the company’s behalf.”

While all of this may sound like work and worry for companies, there’s good news as well: Other countries are following the United States’ lead by implementing anti-corruption measures of their own. Over time, these should help mitigate the corruption risk in EFGMs, making internationally active private companies less hesitant to pursue growth opportunities in those fast-evolving markets.

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## Brass tacks

### **Why the FCPA was enacted**

The FCPA was enacted in 1977 to

- Criminalize bribery of foreign officials by US companies
- Promote fair business practices, integrity, and accountability among US companies and individuals doing business in foreign markets

### **Who’s affected**

Any company that has significant operations in the United States falls under the FCPA, regardless of whether a corrupt act takes place in or outside the United States.

### **Who enforces it**

The DOJ enforces the FCPA for private and public companies (for the latter, certain FCPA provisions come under SEC enforcement).

### **Main provisions**

The FCPA has two main sets of provisions:

*Anti-bribery provisions:* These prohibit the promise, payment, or giving of money or anything of value to any foreign official for the purpose of obtaining or retaining business or gaining an improper advantage.

*Accounting and internal-control requirements:* These apply to SEC registrants only but are worth noting by private companies that may be contemplating an IPO or an exit strategy via a public-company buyer. Under the FCPA, public companies must

- Devise and maintain a system of internal accounting controls sufficient to provide reasonable assurance that transactions are recorded appropriately and in accordance with rules and regulations
- Make and keep books, records, and accounts that, in reasonable detail, accurately reflect the issuer’s transactions and dispositions of assets

### **Exception to the rule**

Facilitation payments are explicitly excluded from the FCPA’s bribery prohibition. These are small payments made for routine, nondiscretionary governmental actions (e.g., payments made to a local branch of a government-run bank to process a company’s paperwork to open a bank account).

### **Why companies need to pay attention**

Although the FCPA was enacted over three decades ago, the number of regulatory enforcement actions has soared in recent years due to stepped-up enforcement by the DOJ. In 2010 there were forty-eight DOJ actions, compared with just two in 2004.<sup>21</sup>

The DOJ's more aggressive enforcement has included focusing on individuals, not just companies. Indeed, US Attorney General Eric Holder has said that "prosecuting individuals is a cornerstone of [the DOJ's] enforcement strategy."<sup>22</sup> This statement, made in spring 2010, came shortly after a person was sentenced to over seven years in prison upon pleading guilty to, among other things, conspiring to violate the FCPA.

With the DOJ's focus on individual accountability, corporate executives are now at risk for business procedures that, until recently, they might have considered routine rubber-stamping, such as securing government permits, processing customs papers, and procuring sales licenses.

"The same holds true of various routine interactions with business associates," says Shah. "Take, for instance, a US medical-device company's sales manager who sponsors the attendance of an industry conference by a healthcare provider in China. If the healthcare provider is employed by a state-owned hospital, he or she could be considered a government official, consequently increasing the potential risk of FCPA violation."

The heat is only apt to intensify if the Overseas Contractor Reform Act is passed by the Senate (the act was passed by the House of Representatives in September 2010, without opposition). The bill proposes that any US company in violation of the FCPA's anti-bribery provisions be disqualified from obtaining federal government contracts. If the DOJ's recent FCPA enforcement activity is any indication, whatever contractor-reform legislation Congress may ultimately pass is likely to have teeth where the FCPA-related provisions are concerned.

### **Greater global scrutiny**

The United States is not alone in its efforts. Around the globe, various governments are collaborating on international initiatives to combat corruption. Participants include once-reluctant EFGM governments, which are recognizing the risk that corruption poses to foreign direct investment in their countries — and hence the risk to their economic growth.

Consequently, various global anti-corruption standards are gaining traction, including the United Nations Convention against Corruption (UNCAC) and the OECD's Anti-Bribery Convention; although, to date, results are mixed.<sup>23</sup> Meanwhile, the World Economic Forum is waging an anti-corruption campaign that focuses on private companies in particular. Called Partnering Against Corruption Initiative (PACI), the campaign was instituted in 2004 and now has nearly 160 signatory companies.

***The DOJ's more aggressive enforcement has included focusing on individuals, not just companies.***

<sup>21</sup> 2010 Year-End FCPA Alert, Gibson Dunn

<sup>22</sup> <http://business-ethics.com/2010/06/01/0653>

<sup>23</sup> Progress Report 2010: Enforcement of the OECD Anti-Bribery Convention, Transparency International

***The price that the company ultimately pays may be much higher than the bribe itself or even any eventual penalties brought by the DOJ—with the biggest bite coming out of the company’s bottom line.***

### ***How companies benefit from greater enforcement***

Greater enforcement of the FCPA should lead to improved corporate awareness about corruption risk generally. That awareness, in turn, is likely to sharpen companies’ focus on protecting their reputation and brand in foreign markets, as well as preserving their license to operate there. In the long run, as companies and governments alike make anti-corruption strides, the number of markets regarded as too risky by US private companies may start to dwindle, paving the way to new growth opportunities.

### ***Protection of reputation and license to operate***

Although tone at the top is critical if a company is to combat corruption risk internally, the employees who are actually confronting that risk firsthand may be thousands of miles from company headquarters, disconnected from the tone at the top. The on-the-ground perspective of those employees may be that, to operate effectively in their place of business, it is necessary to pay small bribes and engage in other minor forms of corruption as a matter of course. But the price that the company ultimately pays may be much higher than the bribe itself or even any eventual penalties brought by the DOJ—with the biggest bite coming out of the company’s bottom line. A US toymaker manufacturing abroad but selling primarily at home, for instance, might very well see its sales dip if US customers were to learn of corrupt practices at the company.

This is hardly a revelation to executives. More than half of those interviewed for PwC’s survey on confronting corruption said that if corruption were exposed at their company, the severest impact would be on their reputation.<sup>24</sup> Most of the survey respondents also said that an anti-corruption program is either very or somewhat valuable to a company’s brand if the public knows the program is in place. The trick is to make that program truly effective—which companies may be more apt to put effort into now that the DOJ is aggressively pursuing FCPA investigations and prosecuting wrongdoers.

“If you have a robust FCPA compliance program in place before a violation comes up, the government is likely to take that into consideration, giving you credit where due,” says Karl Sening, a partner in PwC’s Retail and Consumer Products group, with a focus on clients operating abroad. “In our experience, however, private companies generally haven’t made as large an investment in FCPA compliance programs as their public counterparts. Nor do the majority of them have an audit committee or compliance office, which might be tasked with overseeing such a program. That said, private companies can develop a number of best practices and defenses that will help their employees avoid committing FCPA violations.”

In addition to customers’ perception of a company, there’s the perception of the business in the foreign country where it’s operating. Corrupt practices that may benefit certain individuals in a foreign market (say, a local bureaucrat) may be at the expense of the larger community, potentially causing a company to forfeit its social license to practice there. With stakes as high as that, corruption simply doesn’t pay. “An investment in FCPA awareness, on the other hand,” says Shah, “should deliver long-term dividends.”

24 *Confronting Corruption: The Business Case for an Effective Anti-Corruption Programme*, PwC, 2008

### Fewer markets considered off-limits / too risky

In PwC's *Confronting Corruption* survey, 44% of global executives said they avoided certain markets or chose not to pursue significant opportunities because of corruption risks; almost 40% said they had lost bids because of corrupt officials.<sup>25</sup> Yet as governments abroad step up enforcement of their anti-corruption statutes or institute them for the first time, US private companies may start to find that traditionally risky (but lucrative) markets are becoming places worth seriously considering. Improvements are already evident in many of those markets: Since 2002, the overall risk of operating in emerging and fast-growing markets has fallen—in some cases, dramatically.<sup>26</sup>

Take Indonesia (mentioned in the sidebar on working with foreign representatives), as just one example: That country's ranking on Transparency International's Corruption Index improved by 32 points during the period spanning 2007 to 2010. Such progress bodes well for the increasing number of US private companies seeking growth opportunities abroad in the face of sluggish economic recovery at home.

## Working with foreign representatives

### Best practices for avoiding FCPA violations

“As private companies look to expand into markets abroad, they often enlist a local representative to evaluate new opportunities for them,” says PwC's Mark Reffner. “But this can pose a reputational risk for the company—for instance, if the representative isn't properly vetted or if the contract between the company and that individual doesn't adequately reflect FCPA considerations.”

This is especially true now that the DOJ is turning a deaf ear to the “hear no evil, see no evil” plea that some executives make when confronted with FCPA violations. As a consequence, business leaders should make sure that, as a matter of corporate policy, company personnel conduct thorough reputational due diligence regarding local representatives who are used in foreign locations, obtain referrals for them, and draw up contracts that set the tone for how the company expects the representative to do business on its behalf.

Another best practice is to limit the duration of the contract, so that ties with the representative can be severed if the company isn't happy with the person's conduct. Indeed, the unsatisfactory conduct needn't be on the company's behalf for it to damage the company's reputation.

Says Reffner: “Consider, for instance, a company that hired a representative in Indonesia to help it evaluate business opportunities there, only to end up reading a newspaper account of the representative's alleged involvement in a bribery scandal. Fortunately, the representative hadn't done anything illegal on the company's behalf, nor did the business suffer any collateral damage as a result of the media coverage. All the same, it was a wakeup call for the company.”

The company is now enlisting outside experts to help it establish best practices for evaluating local representatives, conduct FCPA training for its employees and high-risk third-party intermediaries, and review the internal controls and accounting for potential weak spots that could make the company vulnerable to fraud and other corrupt practices in its foreign operations.

<sup>25</sup> Ibid

<sup>26</sup> This according to the Economist Intelligence Unit's risk ratings. For a more-detailed look at the changing risk landscape in emerging and fast-growing markets, please see *Building a Presence in Today's Growth Markets: The Experience of Privately Held Companies*, PwC, 2011.



### **What companies can do**

More than half of the executives interviewed for PwC's *Confronting Corruption* survey said that a better understanding of corruption risks would help them compete more effectively, foster better decision-making, and facilitate entry into new markets. Obtaining that understanding entails increased collaboration across a company's risk, compliance, finance, operations, and corporate-development functions.

It also entails knowing the breadth of international anti-corruption frameworks, monitoring the extent to which emerging policies are being implemented and enforced around the world, and assessing their potential impact on business strategy.

To mitigate the risk of FCPA violations in particular, companies should consider taking the following measures:

- Establish and enforce a clearly articulated anti-corruption policy that reflects the provisions of the FCPA and other anti-corruption laws around the globe—to be followed by all employees and business partners (including agents, consultants, representatives, and joint venture partners)
- Institute FCPA and anti-corruption training for employees engaged in international aspects of the business, with periodic certification required
- Appoint compliance officers (regionally and locally)
- Establish a system for reporting FCPA violations (including a hotline)
- Perform extensive due diligence on business partners (including suppliers), representatives, personnel, transactions, and contracts, particularly when venturing into new markets abroad

***More than half of the executives interviewed for PwC's Confronting Corruption survey said that a better understanding of corruption risks would help them compete more effectively, foster better decision-making, and facilitate entry into new markets.***

- Include in all agreements and contracts with partners, representatives, and other business associates clear language about compliance with the FCPA and other foreign anti-corruption laws/regulations, as well as the stipulation that the arrangement be terminated if any of those laws/regulations are breached
- Streamline and integrate payment systems to easily show where, why, and how much money is being spent
- Routinely test payment systems and controls to ensure that all expenditures are accounted for at all times
- Perform regular field tests and compliance audits to determine whether employees understand the company's anti-corruption policy and are putting it into practice
- Establish and implement appropriate disciplinary procedures

Considering that bribery and corruption have consistently been among the top three types of fraud cited by executives,<sup>27</sup> taking the measures noted here makes good sense in general, irrespective of more aggressive DOJ enforcement.

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<sup>27</sup> *Global Economic Crime Survey* (US supplement), PwC, 2009

## ***M&A due diligence—New focus on FCPA***

In just a few short years, the FCPA has gone from almost an afterthought in M&A risk considerations to a major factor, becoming a focal point of due diligence efforts. A business needs to understand that upon acquiring the stock of a company that has a history of corrupt practices, it may be assuming all of that company's potential successor FCPA liability.

### ***Here's what acquisitive companies should keep in mind:***

***Mitigating successor liability:*** If Company X fails to conduct FCPA due diligence before acquiring Company Y, and the latter is subject to the FCPA's provisions, Company X will essentially be regarded as having inherited Company Y's liability for both past and current violations.\* If, however, Company Y wasn't subject to the FCPA before the acquisition, Company X will have acquired only the liabilities for Company Y's ongoing violations.

Note that the structure of a deal is not relevant for purposes of avoiding successor liability (whereas it would be relevant in the case of financial or tax due diligence). The only way for an acquirer to mitigate the risk of successor liability is to perform adequate FCPA due diligence.

***Avoiding future purchase-price adjustments:*** Performing rigorous pre-acquisition FCPA due diligence on a potential target helps to prevent the purchase of a revenue stream that's tainted by FCPA violations (such violations could, in turn, necessitate a divestiture down the road or cause a line of business to be discontinued).

Sometimes the due diligence process uncovers circumstances that require still stronger medicine. For instance, a company may find that the target's local government contracts are being obtained with the assistance of an elected official whose spouse receives consulting payments from the target. In a risk-fraught situation like this, precautions should be incorporated directly into the purchase agreement.\*\*

Such precautions may include

- Certain representations, including compliance with the FCPA and local anti-corruption statutes
- The stipulation that the seller be liable for the prorated cost of any potential investigation and remediation—along with any fines, penalties, and disgorgement of profits imposed by regulators (in the US or abroad)—stemming from undisclosed continuing business practices that result in violations of the FCPA or other anti-corruption statutes around the globe

***Long story short:*** Given that the number of active investigations continues to soar—along with the number and size of related penalties—buyers should fold FCPA due diligence into their pre-acquisition practices, thereby setting the tone and building the foundation for a strong compliance culture in the company going forward.

\* This would be subject to the statute of limitations.

\*\* This would be done in addition to performing a detailed analysis of the relationship and the value it provides.

## **Conclusion**

While growing globally brings many new opportunities to companies, it also carries a host of risks, some of them harder to manage than others. Corruption risk is among the more manageable ones (when compared with macroeconomic, political, and regulatory risks, for instance) if companies exercise vigilance. What that means for companies wanting to do business abroad—while also protecting their reputation, brand, and bottom line—is that familiarity with the FCPA isn't just a best practice, it's an imperative.

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## **More information**

Want to learn more about FCPA compliance? Please contact someone on the PwC team, including:

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# Personal investments abroad: The IRS is taking a closer look

For all that the complexity of new global-reporting requirements may confuse taxpayers, the IRS won't accept that as an excuse for noncompliance. Individuals should familiarize themselves with the new rules now to avoid costly oversights.

*Although all US taxpayers are required to report their worldwide income on their US tax returns, many people fail to report income from their foreign investments. This has prompted the IRS to take a closer look at certain taxpayers.*

As the US government continues to push for greater transparency and more-rigorous disclosure of offshore activities, it is stepping up reporting requirements for individuals who invest abroad. Not only are the reporting requirements increasing, but they're also becoming more complex and stringent, as well as broader in scope.

US taxpayers—including business owners and members of flow-through entities—should keep abreast of these changes to ensure that their global financial transactions stay in compliance, particularly as oversights can be expensive. The cost? Potentially \$250,000 for each violation and five years in prison.

#### **Intensified scrutiny across the board**


Although all US taxpayers are required to report their worldwide income on their US tax returns, many people fail to report income from their foreign investments. This has prompted the IRS to take a closer look at certain taxpayers.

One result has been the IRS's creation of the Global High Wealth Industry Group in late 2009. This special group within the IRS scrutinizes taxpayers who are engaged in complex financial arrangements, such as the international sourcing of income or the use of offshore structures and bank accounts.

The IRS has also made the filing requirements for the Report of Foreign Bank and Financial Accounts (FBAR) more complicated and the penalties that individuals must pay for noncompliance more severe.

Congress has taken action as well, introducing new reporting requirements and penalties under the Foreign Account Tax Compliance Act (FATCA). This was passed as part of the Hiring Incentives to Restore Employment Act (HIRE) in 2010. The FATCA provisions apply to a much broader range of assets than do the FBAR requirements.

Meanwhile, in tandem with US efforts, the European Union Commission and various EU member states have also undertaken a number of initiatives designed to curb tax evasion, with a focus on eliminating bank secrecy. As a consequence, there's been an increasing exchange of tax information among countries in recent years, along with an effort to accelerate tax receipts and motivate delinquent taxpayers via tax amnesties and/or voluntary disclosure programs.

A photograph of three business professionals in a meeting. Two men and one woman are seated around a glass table. The woman in the center is looking at a laptop screen. The man on the left is looking at her, and the man on the right is looking at the laptop. They are all dressed in business attire. The background is a wall with large, light-colored square panels.

Given the increased scrutiny, individuals should make sure they're familiar with the intricacies of the latest reporting requirements.

***US persons are not exempt from filing an FBAR on the grounds that they live outside the United States or have foreign accounts that are regulated by another agency or country.***

“Given the increased scrutiny, individuals should make sure they’re familiar with the intricacies of the latest reporting requirements,” says Roxanne Laine, a managing director in PwC’s Personal Financial Services group. “Some of the new requirements overlap with those already in place, while others do not. It’s important that taxpayers not assume where the overlap occurs, since a wrong guess could lead to costly mistakes.”

***FBAR reporting obligations***

The Report of Foreign Bank and Financial Accounts (FBAR) stems from the Bank Secrecy Act (BSA) of 1970. The BSA gave the Department of Treasury authority to establish recordkeeping and filing requirements for US persons<sup>28</sup> with financial interests in — or signature authority (or other authority) over — financial accounts maintained with financial institutions in foreign countries.

The US Treasury uses the FBAR to obtain information that might be used to investigate and resolve criminal, tax, and other regulatory matters. Such information has helped investigators track illicit funds and unreported income, as well as provided prosecutorial tools for combating money laundering and other crimes.

Although the requirement to file an FBAR is not new, the process became much more complicated after the IRS took over FBAR administration and enforcement from the US Treasury in 2003, with filers having to furnish more details than were previously required.

***Who needs to file an FBAR?***

All US persons who have a financial interest in, or signature authority over, foreign financial accounts with aggregate balances greater than \$10,000 at any time during the calendar year must file an FBAR.

The US Treasury Department’s Financial Crimes Enforcement Network (FinCEN) recently clarified what it means by signature authority vis-à-vis FBAR, stating that “signature authority” or “other authority” denotes authority to control the disposition of assets in a financial account by “direct communication” to the person with whom the account is maintained.

FinCEN has also narrowed its definition of “foreign account” to exclude foreign holdings maintained at a bank in the United States and any offshore assets held in an omnibus account by a US bank that acts as a “global custodian.” Customers with such accounts do not have to disclose them in an FBAR.

The maximum balance for each foreign account must be reported annually. Note that US persons are not exempt from filing an FBAR on the grounds that they live outside the United States or have foreign accounts that are regulated by another agency or country.

Foreign accounts that must be disclosed in an FBAR include those containing the following assets, among other holdings:

- Private investments in a foreign country
- Any funds coming from a foreign country
- Inheritances from family members abroad
- Beneficial interests in foreign trusts
- Certain foreign life insurance policies

Despite the recent narrowing of the definition for “foreign account,” the range of accounts that qualify as such is still quite broad. Consequently, many investments that a taxpayer might think needn’t be disclosed in an FBAR do in fact have to be reported.

<sup>28</sup> Regulatory guidance issued on February 23, 2011 clarified the definition of “US person” as a resident and/or citizen of the United States (or someone who wishes to be treated as a US resident for tax purposes).

### Inadvertent FBAR violations

The US Treasury requires information on worldwide income regardless of whether the funds have ever been on US soil. “This can take well-intentioned people by surprise,” says Alfred Peguero, a partner in PwC’s Personal Financial Services group. “For example, a couple who’ve lived in Europe for much of their married life might assume that although the wife is a US citizen, she doesn’t have to file an FBAR, because she has lived outside the United States for so long. However, because the US spouse’s name is on the couple’s joint financial accounts, the FBAR requirements do in fact apply to her.”

In other cases, the FBAR filing requirement could be overlooked by a person who invests in a US corporation that has a foreign subsidiary. Consider, for instance, a US person who owns 75% of a Florida corporation, which in turn owns 100% of a foreign company that has foreign financial accounts. First of all, the Florida corporation would have to file an FBAR, because it is considered a “US person” and is the owner of record of (or holder of legal title in) a corporation that directly owns more than 50% of the total value of the foreign company’s stock. And then the investor with the stake in the Florida corporation would have to file as well, because he owns 75% of that corporation and indirectly owns more than 50% of the foreign corporation’s total share value.

Taxpayers also need to be alert to potential filing requirements when power of attorney is involved. “Suppose that a US citizen who resides in Mexico decides to give his sister in the United States power of attorney over his Mexican bank accounts,” says Laine. “Although the sister is merely acting on her brother’s behalf, the US Treasury regards her as having a financial interest in the accounts, since power of attorney makes her the owner of record. Therefore, both siblings must file an FBAR.”<sup>29</sup>

Other people who may unwittingly fail to file an FBAR include those who are told by a promoter of tax-shelter arrangements that they do not need to complete FBARs. Individuals who enter tax-motivated transactions of this kind and don’t file an FBAR may face steeper penalties than other inadvertent non-filers.

Individuals who become aware of a potential reporting oversight should review the FBAR requirements carefully and determine whether they do indeed need to file. Because the rules are very complex, taxpayers are encouraged to seek competent advisors regarding their filing responsibilities.

***The US Treasury requires information on worldwide income regardless of whether the funds have ever been on US soil.***

## ***When to file an FBAR***

Form TD F 90-22.1 (FBAR) is not submitted as part of an individual’s tax return. The IRS must receive an individual’s FBAR by June 30 (date of receipt, not postmark date) in the year following the calendar year that the aggregate value of the individual’s foreign accounts exceeded \$10,000 on any given day.

To be sure to meet the deadline, filers should factor in the time needed to accurately complete and submit the required forms. Filers should also hold on to their FBAR records for a minimum of six years from the date of filing.

*Extension for small subset of individuals:* Certain individuals with only signature authority (no financial interest) who are required to file an FBAR will receive an extension beyond the filing date of June 30, 2011.\*

\* <http://www.irs.gov/pub/irs-drop/n-11-54.pdf>

29 If the brother were a Mexican citizen, he would not have to file an FBAR.

### **The consequences of not filing an FBAR**

Although individuals are not required to pay any tax when they file an FBAR (the income amounts are included in their individual income tax return), the penalties for failing to file are steep. These can include both civil and/or criminal penalties, with fines as high as \$500,000 and a potential prison term of up to 10 years. The severity of the penalty hinges on whether the failure is considered to be negligent or willful, and whether there's a pattern of such activity.

The IRS has said it will waive penalties for unfiled reports over the past six years if it determines that the late filings were due to reasonable cause *and* the taxpayer has no unreported income. Accountholders who have reported all their income but failed to file FBARs for earlier years should file their delinquent FBAR reports now, with a statement explaining their lateness. To avoid inadvertently subjecting themselves to penalties in the future, accountholders should consult a tax advisor before making further foreign-investment decisions.

As for individuals who intentionally refrain from filing an FBAR, the chance that they will evade detection is slim. Most foreign holdings of US citizens will ultimately become known by the US Treasury. To this end, the IRS has persuaded a number of countries to share information as it more aggressively investigates tax shelters outside the United States.

### **FATCA reporting obligations**

The Foreign Account Tax Compliance Act (FATCA) was passed as part of the Hiring Incentives to Restore Employment (HIRE) Act in 2010, with an eye toward strengthening information-reporting and tax-withholding compliance by US persons. The FATCA provisions affect many, if not most, taxpayers holding more than an aggregate of \$50,000 in "specified foreign financial assets." Such assets include

- A depository, custodial, or other financial account maintained at a foreign financial institution
- Any foreign-issued stock or security
- Any interest in a foreign investment fund or derivative with a foreign counterparty
- Interest in a foreign entity

## ***Giving violators a break, sort of*** **2011 Offshore Voluntary Disclosure Initiative**

In its continued effort to bring offshore money back to the United States, the IRS launched a second round of its Offshore Voluntary Disclosure Initiative (OVDI) early this year.

Under this program, the IRS is looking back eight years (to 2003) for any back taxes and penalties. Failure to disclose foreign assets by the deadline of August 31, 2011 will result in a taxpayer's case being sent to the IRS's Criminal Investigations Unit.

The IRS will also impose a penalty equal to 25% of the highest aggregate balance that the individual had in foreign bank accounts during the unreported period. For accounts of \$75,000 or less, or for individuals who inherited an account but had minimal exposure to it, a reduced penalty may apply.

While many holders of foreign accounts are likely to take advantage of the OVDI program, some taxpayers are concerned about the expense and effort involved in complying with the foreign-account reporting rules. Such expense and effort are important for individuals to keep in mind when contemplating whether global investing is indeed the right strategy for meeting their particular wealth management goals.

Among the taxpayers affected by the new rules are US beneficiaries of foreign estates and trusts. FATCA stipulates that, for any person who directly or indirectly transfers property to a foreign trust, the IRS may treat the trust as having a US beneficiary. Also affected are fiduciaries of foreign trusts and estates that have US beneficiaries, as well as US persons who directly or indirectly own stock in a passive foreign investment company (PFIC).<sup>30</sup>

The US government aims to detect non-compliance with FATCA by obtaining US accountholder information from foreign financial institutions and other entities. That said, the United States doesn't have legal jurisdiction to demand such information. The US government therefore plans to apply pressure on foreign financial institutions by imposing a 30% withholding tax on any US-source payments that those institutions accept, including indirect payments from foreign companies with "substantial" US ownership. Foreign institutions/entities that agree to provide the IRS with information about their US accountholders will avoid this tax.<sup>31</sup> Individuals and/or their advisers should bear in mind the possibility that some foreign banks and investment funds could decide to close out their existing US accounts and cease opening new accounts for US investors, as a result of enhanced US scrutiny.

#### How do individuals comply with FATCA?

US investors who are already required to report their holdings in PFICs are also subject to the new annual reporting requirements under FATCA. This is the case even if a person's holdings haven't changed since FATCA was enacted (March 2010). Hence US investors in PFICs must now file a report each year, whereas previously they had to report annually only if they received a distribution from, or disposed of their interest in, a PFIC, or, if they made certain elections with respect to a PFIC.

Under FATCA, individuals holding more than an aggregate of \$50,000 in foreign reportable assets during a tax year must report the following information about those assets on their tax returns (in addition to any other foreign reporting they are already required to do — PFIC/FBAR, 3520s, 5471s, etc.):<sup>32</sup>

- Name and address of the foreign financial institution in which an account is maintained, as well as the filer's account number
- Name and address of the issuer of a foreign security, along with the information necessary to identify the class or issue of the security
- In the case of any other reportable instrument, contract, or interest, any information that's necessary to identify the item, along with the names and addresses of all issuers and counterparties
- Maximum value of the asset during the taxable year

Since the provisions of FATCA do not affect FBAR filing requirements, investors who have made FBAR filings in the past should continue to do so.

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30 PFICs include foreign-based mutual funds, partnerships, and other pooled investment vehicles that have at least one US shareholder. Most investors in PFICs must pay income tax on all distributions and appreciated share value, regardless of whether capital-gains tax rates would normally apply.

31 This goes into effect for payments made after December 31, 2012. FATCA had initially been introduced as a separate bill in 2009 but was ultimately included in the HIRE Act in the hope that the anticipated IRS collections from foreign institutions would help to fund the projected costs of the jobs portion of the HIRE Act.

32 As of this writing, the IRS hasn't yet released the forms for the additional reporting required under FATCA.



**High stakes: The price of noncompliance**

Failure to comply with FBAR and FATCA requirements can lead to a range of punitive consequences, some tougher than others:

**FBAR civil & criminal penalties\***

Civil penalties up to \$10,000 for each *negligent* (non-willful) violation

Civil penalties up to the greater of \$100,000 for each *willful* violation or 50% of what the account balance was when the violation took place

For each *willful* violation, criminal penalties up to \$250,000 or five years' imprisonment, or both\*\*

**FATCA civil penalties**

A penalty of \$10,000 for the tax year (up to \$50,000 if the necessary disclosures aren't made within 90 days after IRS notification)

A 40% accuracy-related penalty for any understatement of tax attributable to a transaction involving an undisclosed foreign financial asset

A penalty of the greater of \$10,000 or 35% of the gross reportable amount that wasn't reported

\* Civil and criminal penalties may be imposed together.

\*\* Willful violation of FBAR requirements, combined with violation of certain other laws, may result in criminal penalties up to \$500,000, 10 years imprisonment, or both.

**Reporting the use of foreign-trust property**  
FATCA stipulates that individuals who use assets that are held in a foreign trust must now determine and report the fair market value of that use *and be taxed on it* as though it were a deemed distribution (if the trust is generating income).

Distribution includes uncompensated use of trust property by US persons, as well as the lending of cash or marketable securities, or the use of other foreign-trust property.

Laine elaborates: “Say, for example, that you’re the beneficiary of a trust, and one of the trust’s assets is a summer home in France. In the past, you could use that home without worrying about recognizing income. Not anymore. Now you will have to determine the fair market value of that trust property for the time that you used it. If the trust is generating income—which it probably is, since the home has to be maintained—that income can be taxable as a deemed distribution. This is taking a lot of people by surprise.”

The new FATCA requirements add an extra layer of complexity and potential confusion to an already complicated reporting regimen, particularly as the sands are likely to keep shifting. The sooner taxpayers familiarize themselves with the new requirements, the better.

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## ***Individuals who use assets that are held in a foreign trust must now determine and report the fair market value of that use and be taxed on it.***

### **Conclusion**

Reporting global investments is not a process to put off, given the repercussions of not reporting or of doing so inadequately. As for US taxpayers who have, for one reason or another, overlooked their reporting obligations, setting things right sooner rather than later is decidedly the best course of action. This approach, coupled with vigilant attention to changes in the reporting guidance, should help to ensure that your foreign financial affairs stand up to inspection.

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1 2010 Forbes America's Largest Private Companies List