

FOREIGN INVESTMENT IN THE UNITED STATES—REPORTING REQUIREMENTS

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The United States has for years served as an attractive investment location for foreign investors looking for political stability and reasonable economic reward. The opportunity to make the investment in a foreign country with minimum public disclosure of the identity and country of origin of the investor has added to the attractiveness of such investment for many foreign investors.

Three recently adopted federal statutes, the International Investment Survey Act of 1976,¹ the Agricultural Foreign Investment Disclosure Act of 1978,² and the Foreign Investment in Real Property Tax Act of 1980,³ have substantially changed the ability of the foreign investor to remain anonymous and have imposed significant regulatory rules and regulations on such investors in excess of the reporting rules applicable to U.S. investors holding identical property in the United States. The scope of the coverage of the laws is comprehensive with applicability to all types of investments regardless of whether the businesses or investments involved are industries vital to the national security. The reporting forms required under these statutes are in many cases complex and require preparation and disclosure of detailed financial information.

In addition to the legal, accounting and administrative expense of complying with these statutes and the regulations promulgated thereunder, many foreign investors would have a number of reasons to be concerned about the resulting loss of investment confidentiality. Although home country exchange control or tax evasion violations may be a concern in some cases and the legitimate foreign investor may have genuine fears of political reprisals, the potential for future ex-

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1. International Investment Survey Act of 1976, Pub. L. No. 94-472, 90 Stat. 2059 (codified at 22 U.S.C. §§ 3101-3108 (Supp. III 1979)) [hereinafter cited as the Survey Act].

2. Agricultural Foreign Investment Disclosure Act of 1978, Pub. L. No. 95-460, 92 Stat. 1263 (codified at 7 U.S.C. §§ 3501-3508 (Supp. IV 1980)).

3. Omnibus Reconciliation Act of 1980, Pub. L. No. 96-499, Title XI, Subtitle C, §§ 1121-1125, 94 Stat. 2682, (codified in scattered sections of I.R.C.) [hereinafter cited as the Act].

change-related controls that might lead to compelled repatriation of assets to the home country or other internal problems within their countries is one from which U.S. investors are, luckily, immune.

Consequently, foreign investors, in analyzing the necessary compliance with the United States investment disclosure statutes and regulations, will be interested in the exemptions and structuring techniques which may be available to minimize the reporting expense and the termination of investment confidentiality, while providing the United States government with the disclosures required by law. Each of the three investment disclosure laws has a different legislative purpose and scope, and each foreign investor will most likely be required to comply with one and, in some cases, all three.

I. INTERNATIONAL INVESTMENT SURVEY ACT OF 1976

The International Investment Survey Act of 1976 (the Survey Act) and the regulations⁴ promulgated thereunder, require reporting to the Department of Commerce, Bureau of Economic Analysis (BEA), information related to investment by foreign persons in U.S. assets, businesses and enterprises (including real estate). The Survey Act, which does not prohibit any type of foreign investment, was enacted for the purpose of allowing for the collection of statistical and analytical data concerning foreign investments for policy formulation and analysis purposes.⁵ The Survey Act and regulations require filing with the BEA when a foreign individual, trust, partnership, corporation or other organization (foreign person), directly or indirectly, through a U.S. business enterprise in which it already owns 10% or more voting interest (U.S. affiliate): (1) establishes or acquires a 10% or more voting interest in a U.S. business enterprise which thus becomes a U.S. affiliate, or (2) acquires a business segment or operating unit of an existing U.S. business enterprise and either organizes it as a separate legal entity or merges it into its own operations or the operations of its existing U.S. affiliate.⁶

Definitions. As is the case with many federal statutes, the scope of definitions must be closely reviewed. The definition of *U.S. business enterprise* includes any ownership of real estate including undeveloped land.⁷ The term *person* includes any associated group which would in-

4. 15 C.F.R. § 806 (1980), as amended in 46 Fed. Reg. 23,225, 30,336 (1981).

5. 22 U.S.C. § 3101 (Supp. III 1979). There are federal statutes restricting foreign investment in certain industries such as communications, transportation, fishing, financial institutions and insurance, the discussion of which is beyond the scope of this Article.

6. 15 C.F.R. § 806.15 (1980), as amended in 46 Fed. Reg. 23,226 (1981).

7. *Id.* § 806.7(f).

clude “[t]wo or more persons who, by the appearance of their actions, by agreement, or by an understanding, exercise their voting privileges in a concerted manner to influence the management of a business enterprise.”⁸ Members of the same family, a business entity and one or more of its officers and directors, members of a syndicate or joint venture or a corporation and its subsidiaries are all considered to be an associated group.

Foreign direct investment in the United States is defined as “the ownership or control, directly or indirectly, by one foreign person of 10% or more of the voting securities of an incorporated U.S. business enterprise or an equivalent interest in an unincorporated U.S. business enterprise, including a branch.”⁹ *Ultimate beneficial owner* is, “[t]hat person, proceeding up the ownership chain beginning with and including the foreign parent, that is not more than 50% owned or controlled by another person.”¹⁰

Confidentiality. The Survey Act provides specific restrictions concerning use and access to the information reported by foreign investors.¹¹ Access to the information is required to be made available only to officials and employees of agencies designated by the President to perform functions under the Survey Act. The information is required to be used solely for analytical or statistical purposes. The Survey Act further provides that no person can compel the disclosure of any Survey Act report without the prior written permission of the person filing the report. This confidentiality requirement, even if complied with, is not total. Persons filing reports under the Survey Act do take the risk that in the event the reports are deemed to be inadequate and the Government pursues civil, injunctive or criminal penalties pursuant to the Survey Act, the information submitted under the Survey Act could be utilized in such enforcement proceedings, which would then place such information on the public record.¹² Thus, a party desiring confidentiality will be at a disadvantage in the event of dispute with the BEA concerning full compliance, since litigation with the BEA would result in loss of confidentiality.

Reporting Requirements. U.S. business enterprises are required to report when a foreign person establishes or acquires, directly or indirectly, through a U.S. affiliate, a 10% or more voting interest in that

8. *Id.* § 806.7(1).

9. *Id.* § 806.15(a)(1).

10. 46 Fed. Reg. 23,226 (1981) (to be codified in 15 C.F.R. § 806.15(a)(6)).

11. 22 U.S.C. § 3104(c) (1976).

12. *Id.*

enterprise. This would include the acquisition of real estate which by definition is a U.S. business enterprise. Also, an existing U.S. affiliate of a foreign person would have to report when that affiliate acquires and merges the affiliate with a U.S. business enterprise. Both of these reports require utilization of form BE-13A.¹³ The foreign person or its existing U.S. affiliate that establishes or acquires a 10% voting interest in a U.S. business enterprise or acquires a U.S. business enterprise that merges into the affiliate's operation is required to report on form BE-13B.¹⁴ Forms BE-13A and B are due within forty-five days after the investment transaction occurs.

In addition, quarterly reports utilizing form BE-605 are required for each U.S. affiliate.¹⁵ Such forms must be filed within thirty days after the close of each calendar or fiscal quarter, except for the final quarter, where forty-five days is allowed. The financial data required by such reports are extensive. Benchmark surveys of foreign direct investments in the United States are also required utilizing form BE-12.¹⁶ Form BE-12 for the 1980 Survey was to be filed no later than August 15, 1981; however, the BEA has informally indicated that it will continue to accept voluntary compliance, without penalty, for a reasonable period of time. Any party required to file any of the other BEA Survey Act forms is also required to file the Industry Classification Questionnaire on form BE-607.¹⁷

Intermediary Reporting Requirements. An intermediary, who is defined as "[a]n agent, nominee, manager, custodian, trust or any person acting in a similar capacity,"¹⁸ is required to file the applicable reports, if the intermediary holds, exercises, administers or manages the U.S. business enterprise for the foreign beneficial owner.¹⁹ This requirement includes nominees holding real estate interests. The intermediary may file on behalf of the U.S. business enterprise or instruct the enter-

13. 46 Fed. Reg. 23,226 (1981) (to be codified in 15 C.F.R. § 806.15(j)(3)(i)).

14. *Id.* § 806.15(j)(3)(ii). The BEA has proposed amending the regulations to eliminate the reporting of a portion of the data presently required in Forms BEA-13A and B and to combine such forms into one report. *See* 47 Fed. Reg. 4,530 (1982).

15. 46 Fed. Reg. 23,226 (1981) (to be codified in 15 C.F.R. *Id.* § 806.15(h)(1)). A U.S. banking branch or agency with a foreign parent must utilize quarterly report form BE-606B rather than BE-605.

16. 46 Fed. Reg. 30,336 (1981) (to be codified 15 C.F.R. § 806.17). The BEA in the past has also conducted interim annual surveys utilizing form BE-15, with the last such interim survey having been conducted in 1979. The BEA has not as of yet announced an interim survey for 1981. The BEA has initiated under the Survey Act a survey of foreign owned U.S. businesses engaged in the processing, packaging or wholesale distribution of fish or seafood. *See* 46 Fed. Reg. 34,812, 60,191 (1981).

17. 46 Fed. Reg. 23,226 (1981) (to be codified in 15 C.F.R. § 806.15(j)(1)).

18. 15 C.F.R. *Id.* § 806.7(n) (1980).

19. *Id.* § 806.11(c)(3).

prise to submit the report. In the latter case, the intermediary shall be released from further liability to report as long as the intermediary informs the BEA of the date such instructions were given and the name and address of the U.S. affiliate and supplies the U.S. affiliate with any information available to the intermediary that is required for the report.

In addition, form BE-14 must be filed by certain U.S. intermediaries participating in an acquisition by a foreign person or a U.S. affiliate of a U.S. business enterprise in the event the U.S. business enterprise acquired has total assets of \$1,000,000 or in the event more than 200 acres is involved in the acquisition, regardless of the asset value.²⁰ This requirement does not apply to the acquisition of residential real estate for personal use. The U.S. intermediary shall be required to file a report only when such a foreign involvement is known and it is not incumbent upon the U.S. intermediary to ascertain the foreign status of a person involved in an acquisition unless the intermediary has reason to believe the acquiring party may be a foreign person. In the event the principal files form BE-13A, the intermediary does not have to file form BE-14. In regard to a transaction where the nationality status of participants is unclear, intermediaries may desire to insert representations in the appropriate documents since the "reason to believe" standard is extremely vague.

The question exists as to whether a lawyer representing a foreign person in a U.S. acquisition transaction is required under any circumstances to file form BE-14. The BEA has advised one law firm that rendering tax and other preacquisition advice does not result in the law firm becoming an intermediary. However, it is not clear whether a law firm becomes an intermediary by the preparation of articles of incorporation, deeds and other acquisition documents for execution and filing.

Many of the customary participants in the acquisition of a direct investment in a U.S. business enterprise may be included within the intermediary definition, including the brokers for the purchaser and the seller, the lenders to the purchaser, civil engineers or economic consultants to the purchaser, title insurance companies and escrow agents. Since there is no specific reference to legal counsel in the definition of an intermediary and because of the strong policies related to attorney/client privilege, performance of actual legal services should not be sufficient to make the attorney an intermediary. However, in the event the attorney utilizes a power of attorney for the foreign person or otherwise

20. 46 Fed. Reg. 23,226 (1981) (to be codified in 15 C.F.R. § 806.15(j)(4)). Note that the exemption level is based on asset value rather than the amount of cash investment or net worth.

serves as an agent of the purchaser (possibly including serving as the incorporator of a new corporation owned by the foreign person) such functions are beyond that of furnishing legal services and may require intermediary compliance.

Exemptions. Portfolio investments, including interests constituting less than 10% voting interest and nonvoting interest, such as limited partnership interests, do not have to be reported to the BEA.²¹ In addition, residential real estate held exclusively for personal use and not for profit-making purposes is not subject to reporting requirements.²² A residence which was an owner's primary residence that is leased by the owner while outside his country of usual residence, but which the owner intends to reoccupy, is considered real estate held for personal use. Ownership of residential real estate by a corporation whose sole purpose is to hold the real estate, and the real estate is for the personal use of the individual owners of the corporation, is considered real estate held for personal use.

In addition, there are specific exemption levels related to specific transactions and use of each of the specific reporting forms. Exemption levels for individual report forms are stated in terms of total assets, sales or gross operating revenues and net income after taxes. If any one of the three items exceeds the exemption level then the report must be filed. The party claiming exemption from filing a given report form must furnish a certification as to the level of the items on which the exemption is based or must certify that the data requests are not applicable.²³

The quarterly report form BE-605 regarding transactions of U.S. affiliates with their foreign owners is required for each U.S. affiliate exceeding an exemption level of \$5,000,000.²⁴ For the 1980 Benchmark Survey form BE-12, the \$1,000,000 and less than 200 acre exemptions are applicable.²⁵ If a U.S. affiliate is not required to file form BE-12 because it falls below the exemption level then it must complete and file a "Claim For Not Filing A BE-12" which is attached to the BE-12

21. 22 U.S.C. § 3102(11) (1976) and 15 C.F.R. § 806.15(a)(1). However, under the Survey Act and Exec. Order No. 11,961, Fed. Reg. 4,321 (1977), certain larger issuers of securities are required to disclose foreign ownership of such securities to the U.S. Department of the Treasury pursuant to regulations set forth in 31 C.F.R. § 129 (1980). Such Treasury Department regulations do not require the extensive detail of disclosure required by the BEA regulations.

22. 46 Fed. Reg. 23,225 (1981) (to be codified in 15 C.F.R. § 806.8).

23. *Id.* § 806.15(g).

24. *Id.* § 806.15(h)(1).

25. 46 Fed. Reg. 30,336 (1981) (to be codified in 15 C.F.R. *Id.* § 806.17(b)).

form. The deadline for claiming such exemption has passed; however, the BEA apparently will continue to accept the exemption claim forms.

In regard to form BE-13, an existing U.S. affiliate is exempt from reporting the acquisition of either a U.S. business enterprise or a business segment or operating unit of a U.S. business enterprise that it then merges into its own operations, if the total cost of the acquisition was \$1,000,000 or less and the acquisition involves less than 200 acres. An established or acquired U.S. business enterprise is exempt if its total assets at the time of acquisition or immediately after being established were \$1,000,000 and it does not own 200 acres or more. In the event form BE-13A is not required to be filed, the foreign person or U.S. affiliate is not required to file form BE-13B. In order to claim an exemption under form BE-13A, the exemption form which is attached to form BE-13A must be filed within forty-five days after the occurrence of the applicable transaction.²⁶

It should be emphasized that even though an initial transaction may be exempt from the form BE-13 filing requirement, a U.S. affiliate, through internal growth, acquisitions, new infusions of capital, the purchase of land, etc., may eventually exceed the exemption criteria of the quarterly and annual surveys; and it is the affiliate's legal responsibility to secure and file the appropriate forms when such exemption is no longer available. The use of separate U.S. affiliates for various separate U.S. investments may help to reduce reporting requirements since disclosure exemptions are based on the size of the U.S. affiliates or acquisitions. This approach will not be helpful in regard to real estate investments because a foreign person holding real estate investments that are foreign direct investments in the United States must aggregate all such holdings for the purpose of applying the exemption level tests. If the aggregate of such holdings exceeds one or more of the exemption levels, then the holdings must be reported even if individually they would be exempt.²⁷ If this provision is interpreted to include real estate holdings held by partially owned affiliates, this requirement would appear to create a hardship on any other part owners of such affiliates (where the ownership interests in each affiliate are not identical) who would thus be subject to reporting requirements solely because of one of their partner's separate real estate investments. It is also not clear who would be required to file the reports, since the separate U.S. affiliates would not have sufficient information concerning the other invest-

26. 46 Fed. Reg. 23,225 (1981) (to be codified in 15 C.F.R. § 806.15(j)(3)(i)) and instructions to BEA form BE-13A.

27. 46 Fed. Reg. 23,225 (1981) (to be codified in 15 C.F.R. § 806.15(d)).

ments. For this reason, the aggregation requirement should only be interpreted to apply to wholly owned real estate investments.

Structuring Transactions to Preserve Confidentiality. Prior to 1981, form BE-13 required disclosure of the identity of persons who were the ultimate beneficial owners (UBO) of the U.S. investment. The BEA no longer requires the names of individuals where a foreign entity constitutes the first foreign parent in a multiple tier foreign ownership chain.²⁸ Instead, only the country of location of the UBO is required by the regulations. The other necessary forms only require disclosure of the first foreign parent. Thus, the ownership of the U.S. investment by a foreign corporation or other entity which, in turn, is owned by foreign individuals would result in the disclosure under the Survey Act of the name and address of the foreign entity but only the Country of residence of the owners of the foreign entity.

The revised BEA regulations and forms are intended to prevent the utilization of several previously applied methods of avoiding disclosure. These include bearer shares, offshore trusts and related party ownership structures. In the case of related party ownership structures, a substantial number of individuals or entities would be owners of the property with each holding less than a 10% ownership and with the ownership being brought back under the control of the prime investor or investors at the next tier of ownership. However, the broadened definition of person to include associated group appears to have negated planning possibilities of this type.²⁹

Bearer shares of corporations such as Netherlands Antilles N.V. corporations have also been utilized to preserve confidentiality. Such shares could in turn be held by a bank in Switzerland or a trust company in the Cayman Islands. Such depositories under the laws of their respective jurisdictions are precluded from disclosing identity of the beneficial interest holders. This approach also fails to comply with the new Survey Act regulations. Although it is questionable whether the United States can extend its jurisdiction to override the jurisdiction of a foreign country which has laws respecting the preservation of confidential ownership relationships, the BEA has clearly indicated that this objection is unacceptable as far as compliance with the regulations is concerned. As stated in the amended regulations effective April 24, 1981, "[f]or closely held companies with non-publicly traded bearers shares, identifying the foreign parent or the UBO as 'bearer shares' is not an acceptable response. The U.S. affiliate must pursue the identifi-

28. *Id.* § 806.15(b).

29. See text accompanying note 8, *supra*.

cation of the UBO through managing directors or any other official or intermediary."³⁰ Presumably, failure of the U.S. affiliate to pursue this identification will cause violations of the Survey Act by the affiliate and perhaps its officers and directors, followed by the enforcement of the applicable penalties. Companies with publicly traded bearer shares are the only exception to this provision.

A third method previously utilized for confidentiality involved ownership by a trust. This approach is also rendered ineffective by the new regulations which state that, "[a]n owner who creates a trust, proxy, power of attorney, arrangement or device with the purpose or effect of divesting such owner of the ownership of an equity interest as part of a plan or scheme to avoid reporting, is deemed to be the owner of the equity interest."³¹ The new regulations clearly attack investment structures previously relied on by foreign investors to preserve investor anonymity. The amendment favorable to investor privacy, which requires only the individual UBO's country of residence and not his name, remains only a partial offsetting factor since a multiple tier ownership structure will be required for parties desiring anonymity and this may be expensive and/or impossible due to tax or economic reasons.

Penalties. Failure to furnish required information may result in a civil penalty not to exceed \$10,000. Willful failure to comply with the requirements is a criminal offense which may result in a fine of up to \$10,000 and imprisonment for not more than one year. Any officer, director, employee or agent of any corporation who knowingly participates in such violation upon conviction may be punished by a like fine, imprisonment or both.³²

Summary. Foreign investors desiring anonymity under the Survey Act will be required to institute at least a two tier foreign ownership structure with a foreign parent entity owned by them. The utilization of separate U.S. affiliates to acquire separate investments may, under certain circumstances, reduce reporting requirements because of the method of calculating exemptions; however, this approach in regard to real estate holdings is restricted by an ambiguous amalgamation rule. Former planning approaches utilizing bearer certificates, multiple ownerships and trust ownership to avoid reporting will no longer satisfy the

30. 46 Fed. Reg. 23,225 (1981) (to be codified in 15 C.F.R. § 806.15(c)).

31. *Id.* § 806.15(a)(6).

32. 22 U.S.C. § 3105 (1976).

revised regulations; however, the interference of the reporting requirements of the United States under the Survey Act with the legal ownership privacy laws of other countries has not been reconciled.

II. AGRICULTURAL FOREIGN INVESTMENT DISCLOSURE ACT OF 1978

Additional and overlapping reporting requirements concerning foreign ownership of agricultural land must be complied with under the Agricultural Foreign Investment Disclosure Act of 1978³³ (AFIDA) and the regulations promulgated thereunder.³⁴ AFIDA was enacted in response to the objections voiced by rural constituencies that foreign investment was causing a speculative escalation of the sales price and market value of U.S. agricultural land.³⁵

AFIDA and the regulations promulgated thereunder constitute a disclosure of ownership rather than a prohibition on the investment. AFIDA provides that any foreign person who acquires or transfers any interest, other than a security interest, in agricultural land shall submit a report to the Secretary of Agriculture not later than ninety days after the date of such acquisition or transfer.³⁶

In addition, any foreign person who held any interest, other than a security interest, in agricultural land on the day before the effective day of AFIDA (October 14, 1978) is required to submit a report to the Secretary not later than 180 days after the effective date.³⁷ Additional requirements require similar disclosure in the event a person who owns agricultural land becomes a foreign person³⁸ or in regard to land owned by a foreign person which is converted to agricultural use.³⁹ The Secretary of Agriculture is also empowered to obtain information concerning name, address and citizenship of persons holding an interest in a foreign person.⁴⁰

Definitions. The regulations define agricultural land as "[l]and in the United States which is currently used for, or if idle and its last use within the past five years was for agricultural, forestry, or timber production, except land not exceeding one acre in the aggregate from

33. 7 U.S.C. §§ 3501-3508 (Supp. IV 1980).

34. 7 C.F.R. § 781 (1980).

35. See 124 CONG. REC. H10,757-766 (daily ed. Sept. 26, 1978).

36. 7 U.S.C. § 3501(a) (Supp. IV 1980). Federal law does impose restrictions on some types of foreign ownership of real property, e.g., 30 U.S.C. § 181 (Supp. III 1979) (imposing reciprocity requirement for foreign citizens to lease U.S. mineral lands) and 48 U.S.C. §§ 1501-1507 (1976) (limiting foreign ownership of certain land in U.S. territories).

37. 7 U.S.C. § 3501(b) (Supp. IV 1980).

38. *Id.* § 3501(c).

39. *Id.* § 3501(d).

40. *Id.* §§ 3501(e)-(f).

which the agricultural, forestry or timber products are less than \$1,000 in annual gross sales and such products are produced for the personal or household use of the person or persons holding an interest in such land."⁴¹ Thus, a foreign person who acquires idle land with the intention to develop the land for nonagricultural purposes would still be required to report the acquisition if the land had recently been used for agricultural purposes.

The definition of an interest in agricultural land, in addition to the statutory exclusion of mortgages and other security interests, also excludes leaseholds of less than ten years, contingent future interests, and surface and subsurface easements and rights-of-way used for a purpose not related to agricultural production. In addition, an interest in mineral rights is not considered an interest in agricultural land.⁴² The regulations do not specify whether purchase contracts (including contracts for deed) or options are reportable interests; however, the report form ASCS-153 (the Report Form) includes both options and purchase contracts as reportable interests.

Foreign person is defined to include foreign governments, corporations and other entities which are created or organized under the laws of a foreign government, and any individual who is not a United States citizen or lawfully admitted to the United States for permanent residence. *Foreign person* also includes any domestic corporation or other business entity, such as a partnership, which is created or organized under the laws of any State and in which a significant interest or substantial control is directly or indirectly held by any foreign person.⁴³

Where one or more legal entities exist in the ownership chain between the foreign person who controls the investment and the legal entity which is the holder of record title to the U.S. agricultural land, the regulations have been interpreted to provide that such foreign person will be said to indirectly hold significant interest or substantial control in the entity holding record title only if each of the legal entities existing in the ownership chain, which is at least 5% owned by foreign persons, itself (or combined with the holdings of all other foreign persons) holds 5% or more interest in each succeeding intervening legal entity.⁴⁴ The aggregating of unrelated foreign interests under the 5% test would appear to cause severe reporting calculation problems. The regulations specifically provide that no common objective is necessary among the foreign persons as a condition to aggregating their interest

41. 7 C.F.R. § 781.2(b) (1980).

42. *Id.* § 781.2(c)(4), Interpretation.

43. *Id.* § 781.2(g).

44. *Id.* § 781.2(g)(4)(ii), Interpretation.

to determine if the 5% test is satisfied.⁴⁵ Thus, if the aggregate of equity interests of foreign persons in a U.S. entity, including a publicly traded U.S. corporation, equals 5%, that entity becomes a foreign person under the regulations and is liable to report its interest in any U.S. agricultural land. A proposed amendment to the AFIDA regulations would modify the definitions to provide that the combination of individuals must be "acting in concert" before they are counted together for purposes of the 5% test; however, such amendment proposed an aggregate 20% test for all foreign persons regardless of any "acting in concert."⁴⁶ As discussed in this article, such an amendment to the Regulations has been withdrawn for further review.⁴⁷

Legal entities with diverse ownership which own agricultural land will have particular problems in determining whether they are foreign persons required to comply with AFIDA. An entity with fewer than 100,000 shares shall be considered to have satisfactorily determined whether it has an obligation to file a report under the AFIDA regulations if information within its knowledge and quarterly examination of its business records fails to reveal entities with foreign mailing addresses which hold in the aggregate 5% or more of the ownership interest. Entities with more than 100,000 shares outstanding which have institutional investors and foreign address shareholders aggregating in excess of 5% of the ownership interest, must send questionnaires to each investment institution holding an interest in it, inquiring as to whether the entities for which they are investing are foreign persons. Such entities are then required to determine from their shareholder records and the responses from institutional investors whether the 5% test has been met. The regulations do not discuss what problems with compliance will result from failure of such institutions to respond to the inquiry.⁴⁸

Reporting Requirements. The report forms must be filed with the Agricultural Stabilization and Conservation Service county office in the county where the land is located or where the administrative ASCS office is located which administers programs carried out on such land.⁴⁹ The report form requires disclosure of the name of the foreign person who is the owner of the tract, the type of legal entity, if other than an individual, the type of interest held, how the tract was acquired, the purchase price of the land, how much of the purchase price remains to

45. *Id.*

46. 45 Fed. Reg. 6,115 (1980).

47. See text accompanying note 59, *infra*.

48. 7 C.F.R. § 781.3 (1980), Interpretation.

49. *Id.* § 781.3(a).

be paid and the estimated current value of the land. In addition, the type of relationship between the owner and any producer such as a tenant or sharecropper must be disclosed. Several of these questions on the report form, including the request for the "estimated current value," appear to be beyond the scope of the promulgated AFIDA regulations.

Specific rules as to the disclosure of the actual entities or individuals controlling the investment apply where the legal owner of the land is other than an individual. The Secretary of Agriculture has implemented his discretionary authority concerning disclosure of multiple tier legal ownership. The foreign person record title owner filing the report form must disclose the legal name, address, and citizenship of each foreign individual or entity holding 5% or more interest in such foreign person.⁵⁰ Any foreign person, other than an individual, who is disclosed on the report form as an owner of record title must also disclose its owners and their addresses.⁵¹ The Secretary has interpreted the applicable provisions of AFIDA⁵² to limit his inquiries to the third tier interest holder and has further concluded that the "tracing to the third tier is more than adequate" in uncovering ownership of U.S. agricultural land.⁵³

Penalties. Violations of AFIDA include failure to submit any report required or knowingly filing a report which does not contain all the information required or contains misleading or false information.⁵⁴ Amendments to the regulations effective February 5, 1980,⁵⁵ revised the procedures in the case of incomplete returns to provide for a thirty-day grace period after the report is returned by the Agriculture Department to the reporter requesting the complete information before the penalty provisions can apply.⁵⁶ This grace period applies only to incomplete information and not misleading or false information. For late reports, the prescribed penalty is one-tenth of one percent of the fair market value of the land for each week or portion thereof that such violation continues (subject to a maximum penalty of 25%). The full

50. *Id.* § 781.3(f)(1).

51. *Id.* § 781.3(g)(1)(i).

52. 7 U.S.C. § 3501(f) (Supp. IV 1980) states concerning the report form filed by the first tier owner disclosing the name of the second tier owner that, "[w]ith respect to any person, other than an individual or a government, whose legal name is contained in any report submitted under subsection (e) of this section, the Secretary may require such person to submit to the Secretary a report containing— (A) the legal name and the address of any person who holds any interest in the person submitting the report. . . ."

53. 44 Fed. Reg. 29,030 (1979).

54. 7 C.F.R. § 781.4(a) (1980).

55. 45 Fed. Reg. 7,775 (1980).

56. 7 C.F.R. § 781.4(a)(2)(i) (1980).

25% of the fair market value penalty applies in the case of incomplete reports and misleading and false reports or failure to submit a report. The penalties prescribed are subject to downward adjustment based on factors including the total time a violation existed, the method of discovery of the violation, extenuating circumstances, and the nature of the information misstated or not reported.⁵⁷

Whenever it appears that a foreign person has violated the reporting obligation, a written notice of apparent liability will be sent to such person at the last known address. This notice will set forth the facts which will indicate apparent liability, identify the type of violation, state the amount of penalty to be imposed, include a statement of fair market value and summarize the course of action available to the foreign person. The foreign person involved shall be required to respond to the notice within sixty days. Failure to respond would make the penalty final. Any of the following actions by the foreign person shall constitute a response negating, at least temporarily, a final penalty: (1) payment of the proposed penalty and filing of a report; (2) submission of a written statement denying liability supported by detailed factual data; or (3) submission of a written request for a hearing in Washington, D.C., with the Administrator of the ASCS or with the Administrator's designee. After the submission of a written statement and/or after the hearing, the Administrator will make a final determination. In the event a foreign person contests the initial notice of penalty, the foreign person has the option of payment of the whole fine subject to refund in the event of a favorable determination which will terminate additional fines, or withhold payment, which in the event of an adverse determination would result in additional fines for the additional period. If the fines are not paid after a final determination, the matter would be referred to the Department of Justice for prosecution and recovery of the penalty.⁵⁸

Proposed Amendments. On January 25, 1980, the Department of Agriculture proposed amendments to its regulations to revise the definition of "significant interest or substantial control" as described above.⁵⁹ In addition, a proposed amendment to the regulations would require the disclosure of the unpaid portion of the purchase price and value of the land which is presently being requested by the report form but not authorized by regulations. The proposed amendments would amend the definition of agricultural land to exclude tracts of less than

57. *Id.* § 781.4(b).

58. *Id.* § 781.5(g).

59. *See* text accompanying note 46, *supra*.

ten acres rather than tracts of one acre unless more than \$1,000 in gross sales receipts are received. The amendment would further define the perimeters of agricultural, forestry or timber products by the parenthetical reference to certain activities set forth in the Standard Industrial Classification Manual. Such proposed amendments, which on the whole would appear to provide several beneficial clarifications (especially for corporations with diverse shareholders ownership), have been withdrawn for further study and revision.

Summary. AFIDA specifically provides that all information and the reports actually filed by the reporting entities and individuals are available for public inspection.⁶⁰ Consequently, any foreign person required to comply with AFIDA who desires confidentiality of ownership would be required to implement a four tier ownership structure with intervening entities to preserve personal anonymity. AFIDA is a trap for the unwary since it applies to idle land previously utilized for agricultural or timber production at anytime during the prior five years and is applicable to domestic corporations including publicly held corporations which own agricultural land and which have more than 5% foreign ownership even if the foreign ownership represents numerous portfolio investments by noncontrol persons.

III. FOREIGN INVESTMENT IN REAL PROPERTY TAX ACT OF 1980

The Foreign Investment in Real Property Act of 1980⁶¹ (the Act) imposed several reporting requirements in order to identify foreign owners of U.S. real property interests who would not otherwise be required to file U.S. tax returns. First, a foreign person who directly holds U.S. real property interests exceeding \$50,000 in value and who does not engage in a trade or business in the United States for a given calendar year, will be required to file a return setting forth (i) his name and address, (ii) a description of all United States real property interests held by him at any time during the calendar year, and (iii) such other information as the Internal Revenue Service (the Service) may by regulation prescribe.⁶²

Second, in regard to a foreign person who is a shareholder of the United States corporation that is a U.S. real property holding corporation during a given calendar year, the reporting requirements of the Act will identify the foreign person by requiring such U.S. corporation (unless its shares are traded in an established securities market) to file re-

60. 7 U.S.C. § 3506 (Supp. IV 1980).

61. See note 3, *supra*.

62. I.R.C. § 6039C(c).

turns setting forth (i) the name and address of each person who was a shareholder and is known by the corporation to be a foreign person, (ii) information with respect to transfers of stock in the U.S. corporation to or from foreign persons during the calendar year, and (iii) such other information as may be prescribed by the Service in regulations.⁶³

Third, in the event the U.S. real property interest (either U.S. real property or stock in a U.S. real property holding corporation) is held by a foreign corporation or a domestic or foreign partnership, trust or estate, the Act requires that if such entity has at any time during the given calendar year a substantial investor in the United States real property, the entity will be required to file a return for the calendar year setting forth (i) the name and address of each substantial investor, (ii) such information with respect to the assets of the entity during the calendar year as the Service may prescribe by regulations, and (iii) such other information as the Service may by regulations prescribe.⁶⁴

Definitions. An interest in real property is defined to include any fee ownership, co-ownership and leasehold of land or improvements, mineral interests or options to acquire any of those interests; however, it is not clear whether a contract to purchase real property (including a contract for deed) is an interest in real property.⁶⁵

A United States real property interest (USRPI) is defined as an interest in real property located in the United States and any interest in any domestic corporation that is a U.S. real property holding corporation at any time during the holding period unless the interest in the corporation is a security interest or the applicable stock is regularly traded on an established securities market and the shareholder owns less than five (5%) percent of the stock outstanding.⁶⁶

A U.S. real property holding corporation (RPHC) is any corporation, domestic or foreign, if the fair market value of its USRPI is equal to or greater than 50% of the sum of its fair market value of its USRPI, its interest in real property outside of the United States and other assets used in or held for use in a trade or business.⁶⁷ In making the 50% computation, a flow-through concept is employed with respect to controlled corporations, and the parent company is treated as if it owned its pro rata share of each asset of any subsidiary. The flow-through rules are applied to each succeeding level of ownership.⁶⁸

63. *Id.* § 6039C(a)(1).

64. *Id.* §§ 6039C(b)(1).

65. *Id.* §§ 897(c)(6)(A).

66. *Id.* §§ 897(c)(1).

67. *Id.* §§ 897(c)(2).

68. *Id.* § 897(c)(5).

The Act defines a substantial investor in United States real property to mean any foreign person who at any time during the calendar year held an interest in a foreign corporation or a domestic or foreign partnership, trust or estate which owned an USRPI, but only if the fair market value of such person's pro rata share of the USRPI held by such holding entity exceeded \$50,000.⁶⁹

A foreign person who is a partner in a partnership or a beneficiary of a trust or estate is considered to own directly its proportionate share of the USRPI owned by the partnership, trust or estate. A foreign person also is considered to own the USRPI held by the person's spouse or minor children.⁷⁰

Exceptions. One exception to the reporting requirements of the Act provides that no reporting will be required for an entity for a calendar year if such entity furnishes to the Service such security as the Service determines to be necessary to ensure that any tax imposed with respect to the USRPI held by such entity will be paid.⁷¹ The conference report for the Act discusses the type of security at some length.⁷² The security interest could include a recorded security interest in a tract of U.S. land held by the foreign entity or a personal guaranty from an individual or corporation with substantial business assets in the United States. This exception is applicable to security from foreign corporations and domestic and foreign trusts, estates and partnerships which have substantial investors and does not appear to apply to USRPI held by domestic corporations or individual foreign investors. The Act does not specify the amount of security. Once the security is posted the real estate will no longer be considered an USRPI.⁷³

Penalties. The penalty for failure to file returns required under the Act by U.S. corporations will be \$25 per return per day. The maximum penalty for any single year for failure to file returns required under the Act is \$25,000 for U.S. corporations, foreign corporations, and domestic and foreign trusts, partnerships and estates with substantial investors.⁷⁴ The maximum penalty for any single year for failure to file returns required by foreign individuals with direct investments in an USRPI is the lesser of \$25,000 or 5% of the aggregate value of the

69. *Id.* § 6039C(b)(4)(B)(i).

70. *Id.* § 6039C(e)(1).

71. *Id.* § 6039C(b)(2).

72. H.R. REP. No. 96-1479, 96th Cong., 2d Sess. 191 (1980).

73. *Id.* at 192.

74. I.R.C. § 6652(g)(3)(A).

USRPI held during the calendar year.⁷⁵ Failure to file returns could also result in the imposition of criminal penalties.⁷⁶

Filing Procedures. The reporting requirements are effective for 1980 and subsequent calendar years beginning June 19, 1980.⁷⁷ Nominees who hold shares of a RPHC on behalf of foreign persons, including holders of bearer shares, either are required to provide the corporation with the information necessary for the corporation to file the return or, failing to do so, are required to file the return themselves with respect to such stock.⁷⁸

Protection of confidentiality will be more difficult under the Act than under either the Survey Act or AFIDA. Direct individual ownership appears to provide the least protection of confidentiality since the individual would be required to file a return disclosing his name and address. Domestic corporations having foreign shareholders are to furnish information that is known to the corporation (presumably the officers of the corporation). Consequently, such corporation would only be required to disclose such shareholder addresses as it had on file; however, the foreign shareholder as the holder of an USRPI (the corporate stock) would also be required to file. Many multiple tiered ownership structures would also appear to be ineffective. For example, if a German resident establishes a German corporation which in turn establishes a wholly owned U.S. subsidiary which acquires an USRPI with a fair market value in excess of \$50,000, the West German corporation would be deemed to hold an USRPI (i.e., stock in the U.S. real property holding corporation) with a fair market value in excess of \$50,000 which would make the German resident a substantial investor in U.S. real property. Thus, the name and address of the German resident would have to be disclosed to the Service on a return. Further, it would appear useless to set up a chain of corporations because the Act contains an attribution rule which would contribute the underlying USRPI to each corporation in the chain;⁷⁹ however, the scope of reporting of indirect investments will have to be determined by the regulations which have not yet been issued under the Act.

Temporary regulations have been drafted by the Service and are likely to be published shortly.⁸⁰ Tax forms for reporting under the Act

75. *Id.* § 6652(g)(3)(B).

76. *Id.* § 7203.

77. The Act, *supra* note 3 § 1125(b).

78. I.R.C. § 6039C(a)(3).

79. *Id.* § 6039C(b)(4)(C).

80. A final draft of temporary regulations dealing with the information reporting requirements under the Act prepared by the Legislative and Regulations Division of the Na-

will not be finalized until after the first regulations are issued. The Service indicates that tax forms should be available approximately one month after the first temporary regulations are issued and that a reasonable period of time will be given after the issuance of the first regulations before filing of the information returns for calendar year 1980 is required. Accordingly, it is expected that the due date for the return for calendar year 1980 will be approximately three months after the issuance of the regulations.

Summary. Until the regulations under the Act are published, the scope of the full disclosure requirements will not be known. One method of avoiding RPHC status would be to maintain foreign real property and/or trade or business property, other than realty, in a U.S. corporation that is worth substantially more than the USRPI held by the corporation. In such case, the domestic corporation would not be a RPHC and its stock would not constitute an USRPI.⁸¹ This result could also allow for possible tax free liquidation of the investment, the discussion of which is beyond the scope of this article.

IV. CONCLUSIONS AND RECOMMENDATIONS

At a time of national review of administrative policies related to the possible reduction of government regulation compliance, the U.S. government should also review foreign disclosure requirements presently in effect under the above described statutes. The foreign investors who are willing to invest capital in the United States and create or preserve additional employment are faced with an intricate maze of compliance requirements which, in some cases, conflict with the internal laws of other countries. The scope of the Survey Act should be limited only to those industries and resources deemed by Congress to be vital to the national security. The agricultural disclosures should be eliminated, unless this is deemed to be a vital national security area. In the event the agricultural acquisition information on larger tracts shall be deemed vital, it should be obtained on a confidential basis under the Survey Act, with the elimination of AFIDA. Disclosure of foreign investment owners under the Act should be limited to the first level of foreign ownership which should be sufficient for tax collection purposes. The provisions for providing security in the alternative to disclosure under the Act should be broadened to include all types of

tional Office of the Service, were sent on November 2, 1981, to the Commissioner of the Service for approval.

81. I.R.C. § 897(c)(2).

investment ownership structures, and the regulation promulgated should be extremely clear and broad as to the type of security available.

U.S. persons involved with foreign investment transactions should be aware that the disclosure requirements may, in some cases, be applicable to them. The regulations under all the reporting statutes should be modified to specifically define the scope of intermediary activity, which should include protection of the attorney-client privilege. Due to the intermediary reporting requirements, attorneys will need to re-evaluate their role in foreign transactions in regard to performing non-legal functions.

Foreign investors concerned about confidentiality will want to review the possibility of multiple tiered ownership structures to preserve their personal anonymity as long as such structuring does not create adverse tax or economic consequences. Foreign investors, on the other hand, must recognize the legitimate interest of the United States government in collection of taxes, which U.S. citizens are also required to pay, and in the collection of foreign investment ownership information, at least as it relates to vital industries.