

*Excerpt from eBook*

# The IRS and Offshore Tax Evasion - U.S. Foreign Grantor Trusts

Penalty Regime for Foreign Bank Account Filing

Tax Practitioners and Professional Responsibility

FBAR Annual Filing Requirements and Reasonable Cause Exception

FBAR Civil and Criminal Penalties

Criminal Penalties: Willful Failure to File (Defenses)

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September 2016

Excerpt from eBook - The IRS and Offshore Tax Evasion - U.S. Foreign Grantor Trusts, Penalty Regime for Foreign Bank Account Filing, Tax Practitioners and Professional Responsibility, FBAR Annual Filing Requirements and Reasonable Cause Exception, FBAR Civil and Criminal Penalties, Criminal Penalties: Willful Failure to File (Defenses), ©2016 Lorman Education Services. All Rights Reserved.

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# THE WOLFE LAW GROUP

Gary S. Wolfe has over 34 years of experience, specializing in IRS Tax Audits and International Tax Matters including: International Tax Planning/Tax Compliance, and International Asset Protection.

As of July 2016, Gary Wolfe has internationally published 15 books and 28 articles. Gary has received 14 international tax awards from five different Global expert societies in LONDON/UK including being voted one of the 100 leading world's law firms with votes from over 150,000 voters in over 160 countries with the following award: Global 100 (2016) (KMH Media Group) - CA/US International Tax Planning Law Firm of the Year.

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## **Chapter 14 - Penalty Regime for Foreign Bank Account Filing**

By Gary S. Wolfe, Published in The California Tax Lawyer (Summer 2009 Edition)

### **Penalty Regime for Foreign Bank Account Filing (FBAR)**

Each U.S. person who has a financial interest in, or signature or other authority over, one or more foreign financial accounts (valued over \$10,000, at any time during a calendar year) is required to report the account on Schedule B/Form 1040, and TD F 90-22.1 (Report of Foreign Bank and Financial Accounts (FBAR)), due by June 30 of the succeeding year (I.R.M. 5.21.6.1. (2/17/09)). The IRS has six years to assess a civil penalty against a taxpayer who violates the FBAR reporting rules.

Failure to file the required report or maintain adequate records (for 5 years) is a violation of Title 31, with civil and criminal penalties (or both). For each violation a separate penalty may be asserted.

(I) Non Willful Violation: Civil Penalty – Up to \$10,000 for each violation.

(II) Negligent Violation: Civil Penalty – Up to the greater of \$100,000, or 35 percent of the greatest amount in the account.

(III) Intentional Violations -

(1) Willful Failure to File FBAR or retain records of account: (a) Civil Penalty – Up to the greater of \$100,000, or 50 percent of the greatest amount in the account; (b) Criminal Penalty – Up to \$250,000 or 5 years or both.

(2) Knowingly and Willfully Filing False FBAR: (a) Civil Penalty – Up to the greater of \$100,000, or 50 percent of the greatest amount in the account; (b) Criminal Penalty – \$10,000 or 5 years or both.

(3) Willful Failure to File FBAR or retain records of account while violating certain other laws: (a) Civil Penalty – Up to the greater of \$100,000, or 50 percent of the greatest amount in the account; (b) Criminal Penalty – Up to \$500,000 or 10 years or both.

### **Failure to File Penalties**

A willful violation of the Form TD F 90.22-1 requirements (i.e., failure to file Form TD F 90.22-1, failure to supply information on the report, or filing a false or fraudulent report) could result in the imposition of civil and/or criminal penalties. (The instructions for Form TD F 90.22-1 specifically provide that criminal penalties for failing to comply with FBAR are provided in 31 U.S.C. § 5322(a) and (b), and 18 U.S.C. § 1001. In addition, civil penalties for failure to comply are generally provided in 31 U.S.C. § 5321.)

### **Civil Penalties**

If any U.S. person willfully violates the Form TD F 90.22-1 filing requirement, such person may be liable to the U.S. government for a civil penalty of not more than \$25,000 (31 U.S.C. § 5321. Section 5321 generally provides that if a U.S. person willfully violates a regulation, such person may be liable for a civil penalty of not more than the greater of the amount (not to exceed \$ 100,000) involved in the transaction (if any) or \$25,000.

With respect to reporting on Form TD F 90.22-1, a U.S. person is not reporting a transaction but, rather, reporting his interest or signature authority over a foreign financial account. Thus, the maximum amount of potential civil penalty is \$25,000.):

### **Criminal Penalties**

If a U.S. person willfully violates the reporting requirement, such person may be subject to a fine of not more than \$250,000, or imprisoned for not more than 5 years, or both (31 U.S.C. § 5322(a)); and

If a U.S. person willfully violates the reporting requirement while violating another law of the United States, or as part of a pattern of any illegal activity involving more than \$100,000 in a 12-month period, such U.S. person may be subject to a monetary fine of not more than \$500,000, or imprisoned for not more than 10 years, or both (31 U.S.C. § 5322(b)).

If a U.S. person, with respect to Form TD F 90.22-1, (1) falsifies, conceals, or covers up by any trick, scheme, or device a material fact, (2) makes any materially false, fictitious, or fraudulent statement or representation, or (3) makes or uses any false writing or document knowing the same to contain any materially false, fictitious, or fraudulent statement or entry, such person may be fined, or imprisoned for not more than 5 years, or both (18 U.S.C. § 1001).

## **Chapter 15 - Tax Practitioners and Professional Responsibility**

U.S. Taxpayers, who fail to file FBAR's to disclose foreign bank accounts, may seek a reasonable cause exception based on their "tax preparer's" failure to file the FBAR.

Tax Practitioners (Attorneys, CPA's) must comply with the FBAR rules as part of their due diligence (as to accuracy) obligation under IRS Circular 230 (Section 10.22).

The FBAR (TD F 90-22.1) is not a tax return. The FBAR is an information report required under the Bank Secrecy Act (BSA) 31 USC 5314 (and related regulations CFR 103.24, 103.27). Related records are required under 31 CFR 103.24 and 103.32.

The Practitioners' professional responsibility does not require that the Practitioner "audit" their client.

The Practitioner must:

1. Make reasonable inquiries in response to Taxpayer's information of overseas accounts/transactions.
2. A Practitioner may rely on information provided by a client in good faith.
3. The Practitioner must make reasonable inquiries if information appears incorrect, inconsistent or incomplete.

## **Chapter 16 - FBAR Annual Filing Requirements and Reasonable Cause Exception**

In April 2003, the Financial Crimes Enforcement Network delegated authority of the TD F 90-22.1 form (i.e., FBAR form) to the Internal Revenue Service (see IR 2003-48 (4/10/03); 31 CFR §103.5(6)(b)(8)). The IRS enforces all penalties associated with the FBAR with the same power it enforces tax reporting and payment compliance.

The IRS has been given the authority to enforce the filing rules and audit the reports as appropriate.

The FBAR filing is due by June 30th of the year following the year of the report with no provisions for extensions. The due date means the date it must be received by the US Treasury. Mailing it on the date it is due will result in a late filing. The FBAR form, filed separately from the income tax, must be mailed to US Department of Treasury, PO Box 32621, Detroit, Michigan 48232-0621.

If there is an emergency, the form can be hand-delivered to a local IRS office for forwarding to the Treasury Department in Detroit.

An amended FBAR may be filed by completing a revised FBAR with the correct information writing the words "Amended" at the top of the revised FBAR and stapling it to a copy of the original FBAR. For Taxpayers amending a late-filed FBAR, they should include a statement explaining their reasons for a late filing (i.e., request a reasonable cause exception from penalty).

A failure to file a FBAR has civil and criminal penalties (which are in addition to any income tax penalties if the income is not reported). The IRS must assess the civil penalties within 6 years of the FBAR violation (31 USC 5321(b)(1)).

For a willful failure to file, the civil penalty increases from \$10,000 (non-willful failure to file) to the greater of \$100,000 or 50% of the account balance in the foreign account for the tax year.

The civil penalties for non-willful failure to file may be waived by the IRS if the Taxpayer can show reasonable cause. If the Taxpayer has a reasonable cause exception, the FBAR should be filed with an explanation (i.e., the reasonable cause, with an express request for waiver of penalties).

The waiver of civil penalties for a reasonable cause exception may include among other factors:

1. All the income from the foreign account was included on the US Taxpayer's return.

2. The Taxpayer was unaware of the requirement to file (for example, lack of understanding of what constitutes a financial interest).

3. Once the Taxpayer became aware of the filing requirements, he filed all delinquent reports (up to 6 years).



## **Chapter 17 – FBAR Civil and Criminal Penalties**

Each U.S. Person who has a financial interest in, or signature or other authority over, one or more foreign financial accounts (value over \$10,000, at any time during a calendar year) is required to report the account on Schedule B/Form 1040, and TD F 90-22.1 (Report of Foreign Bank and Financial Accounts (FBAR)), due by June 30 of the succeeding year (I.R.M. 5.21.6.1. (2/17/09).

Failure to file the required report or maintain adequate records (for 5 years) is a violation of Title 31 with civil and criminal penalties (or both). For each violation a separate penalty may be asserted.

### **(I) Non-Willful Violation**

Civil Penalty – Up to \$10,000 for each violation. 31 U.S.C. § 5321(a)(5)(A)

### **(II) Negligent Violation**

Civil Penalty – Up to the greater of \$100,000, or 35 percent of the greatest amount in the account. 31 U.S.C.

### **(III) Intentional Violations**

#### **1) Willful – Failure to File FBAR or retain records of account**

Civil Penalty -Up to the greater of \$100,000, or 50 percent of the greatest amount in the account. Criminal Penalty -Up to \$250,000 or 5 years or both. 31 U.S.C. §5321(a)(5)(C), 31 U.S.C. § 5322(a) and 31 C.F.R. §103.59(b) for criminal

#### **(2) Knowingly and Willfully Filing False FBAR**

Civil Penalty – Up to the greater of \$100,000, or 50 percent of the greatest amount in the account. Criminal Penalty – \$10,000 or 5 years or both. 18 U.S.C. § 1001, 31 C.F.R. § 103.59(d) for criminal

#### **(3) Willful – Failure to File FBAR or retain records of account while violating certain other laws**

Civil Penalty – Up to the greater of \$100,000, or 50 percent of the greatest amount in the account. Criminal Penalty – Up to \$500,000 or 10 years or both. 31 U.S.C. § 5322(b) and 31 C.F.R. §103.59(c) for criminal

## **Chapter 18 - Criminal Penalties: Willful Failure to File (Defenses)**

Under IRS Form 1040, at the bottom of Schedule B, Part III, on Page 2, Question 7(a) states: “at any time during the previous year, did you have any interest in or signatory or other authority over a financial account in a foreign country, such as a bank account, a security account, or other financial account? The answer is either yes or no. If yes, Question 7(b) requires the name of the foreign country (with the account). Question 8 requires confirmation of receipt of distribution from the account, or if the Taxpayer was a grantor of, or transferor to a foreign trust (which requires filing Form 3520).

A willful failure to file a FBAR can lead to a felony of up to 10 years in jail and a \$500,000 fine. The IRS must prove willfulness in order to assert the \$500,000 monetary penalty and the imprisonment for up to 10 years (see 31 USC 5321(a)(5)(B); CCA 200603026; Eisenstein, 731 F.2d 1540 (CA – 11, 1984)).

Willfulness must be proven by the IRS under the standard of clear and convincing evidence. If the Taxpayer knew about the requirement to file, it would affect his defense. If the Taxpayer failed to report the foreign account interest or other income on his income tax return, it would affect his defense.

If a failure to file is deemed to be part of a criminal activity involving more than \$100,000 in a 12-month period, the penalty limit increases to \$500,000 with up to 10 years in jail. The issue of whether a failure to file is willful or non-willful is based on the facts of each case. Willfulness has been defined as the voluntary, intentional violation of a known legal duty, see Cheek 498 US 192, 67 AFTR 2d 91-344 (Supreme Court 1991).

A Taxpayer’s good faith belief that he does not have to file (or even his negligent failure to file) can be a defense to the charge of willful failure to file (i.e., a defense to criminal charges).

A defense may include that the Taxpayer was advised by his advisor that no FBAR was required.

Failure to maintain adequate records of the foreign account for the years the FBAR filing is due may result in additional civil and criminal penalties.

