

**FOREIGN REPORTING COMPLIANCE:
FBAR, FORM 8938, AND FORM 3520**

FBAR

A Report of Foreign Bank and Financial Accounts, commonly referred to as an FBAR, is a report that is filed electronically with the Financial Crimes Enforcement Network (FinCEN). Any U.S. person with a financial interest in or signature authority over one or more foreign financial accounts with an aggregate value of greater than \$10,000 at any time during the prior calendar year is required to file an FBAR. Accounts subject to FBAR reporting requirements include bank accounts, brokerage accounts, direct ownership of foreign mutual funds, and foreign-issued cash-value life insurance. A U.S. Person includes (A) a citizen of the United States, (B) a resident of the United States, or (C) an entity formed under the laws of the United States, any state, the District of Columbia, any territory or possession of the United States, or an Indian tribe. 31 CFR 1010.350(b).

PENALTIES FOR FAILURE TO FILE FBAR

Failure to timely file an FBAR can result in both civil and criminal penalties. There are four civil penalties for FBAR violations: (A) negligence, (B) pattern of negligent activity, (C) penalty for non-willful violation, and (D) penalty for willful violation. 31 USC 5321(a)(5)-(6).

The due date for filing is June 30th of the year following the calendar year to be reported. Failure to file an FBAR by the due date will result in a recordkeeping violation. The penalty for non-willful FBAR violations may be imposed on any person who violates or causes any violation of the FBAR filing and recordkeeping requirements. The amount of the penalty shall not exceed \$10,000. 31 USC 5321(a)(5)(B)(i). However, there is a reasonable cause exception to non-willful FBAR violations, which provides that no penalty shall be imposed if such violation was due to reasonable cause *and* the amount of the transaction or the balance in the account at the time of the transaction was properly reported. 31 USC 5321(a)(5)(B)(ii). Examiners will generally recommend one penalty per open year, which is limited to \$10,000 per year.

A willful violation increases the maximum penalty to the greater of \$100,000 or 50-percent of the amount involved in the transaction or unidentified account. 31 USC 5321(a)(5)(C). A willful violation is defined as the voluntary, intentional violation of a known legal duty, based on conduct meant to conceal sources of income or other financial information.

A civil fine and a criminal penalty may be imposed for the same violation. 31 USC 5321(d). Criminal penalties for willful violation include up \$250,000 in penalties, imprisonment for up to 5 years, or both. 31 USC 5322(a).

TIME LIMITATIONS FOR PENALTIES

A civil penalty for FBAR violations may be assessed within six years of the date of the transaction. 31 USC 5321(b)(1). A civil action to recover a civil penalty may be commenced at any time before the end of the two year period beginning on the later of the date the penalty was assessed or the judgment in any criminal action related to the same transaction for which the civil penalty is assessed. 31 USC 5321(b)(2).

MITIGATION OF PENALTIES

The Act provides a ceiling for penalties for FBAR violations, which are imposed at the discretion of the IRS. In order for the IRS to administer a penalty of less than the maximum amount, the following four conditions must be met: (1) no history of criminal tax or Banking Secrecy Act (BSA) convictions for the preceding 10 years, as well as no past FBAR penalty assessments, (2) no money passing through the foreign accounts at issue is from an illegal source or used to further a criminal purpose, (3) cooperation during the examination, and (4) no civil fraud penalty for underpayment of tax during the year in question due to failure to report income related to amount in the foreign account.

HOW TO FILE AND COMPLY WITH FBAR REQUIREMENTS

All FBARs must be filed electronically with FinCEN through the BSA E-Filing System. An individual owner of a reportable foreign financial account that requires an FBAR filing does not need to register to become a BSA E-Filer. An attorney, CPA, or enrolled agent representative must register as a BSA E-Filer in order to file an FBAR on behalf of a client.

DELINQUENT FBAR SUBMISSION PROCEDURES

Filers who are not required to use either the OVDP or the Streamlined Filing Compliance Procedures (as described below) should file delinquent FBARs through the normal filing procedures. These procedures are available to filers who (1) have not filed a required FBAR, (2) are not under civil examination or a criminal investigation by the IRS, and (3) have not already been contacted by the IRS about delinquent FBARs. The filer is required to include a statement explaining why he or she is filing the FBAR late. Additionally, the cover page requires the filer to select a reason for filing late. No penalties will be imposed for failure to file FBARs as long as the filer properly reported all foreign accounts on tax returns, properly paid all taxes related to income on foreign accounts, and has not been contacted by the IRS regarding delinquent FBARs.

STREAMLINED FILING COMPLIANCE PROCEDURES

Streamlined filing compliance procedures are available to taxpayers whose failure to comply with FBAR reporting requirements and pay all taxes due with respect to foreign financial assets did not result from willful conduct. The streamlined procedures are designed to help taxpayers with filing amended or delinquent returns, resolving tax and penalty procedures for filing amended or delinquent returns, and resolving tax and penalty obligations. The taxpayer

must certify that the failure to comply with FBAR reporting requirements, pay all taxes, and submit all required information was due to non-willful conduct.

Streamlined filing compliance procedures require the taxpayer to file tax returns or amended returns (if a return was filed previously) for the most recent 3 years with required information returns (e.g. Form 8938). Additionally, the taxpayer must complete and sign a Form 14654 – Certification by U.S. Person Residing in the United States for Streamlined Domestic Offshore Procedures or a Form 14653 – Certification by U.S. Person Residing Outside of the United States for Streamlined Foreign Offshore Procedures, whichever is appropriate. The taxpayer must file delinquent FBARs for the most recent 6 years. Additionally, the taxpayer must pay a 5% miscellaneous offshore penalty on the highest aggregate balance/value of the taxpayer's foreign financial assets for the 6-year covered FBAR period and all tax due on the tax returns plus interest for each late payment amount during each year for the 3-year covered tax return period.

Returns submitted under the Streamlined Offshore Procedures will be processed like any other return submitted to the IRS and, therefore, may be subject to IRS examination and additional penalties

A taxpayer who uses the Streamlined Offshore Procedures is not eligible to participate in the Offshore Voluntary Disclosure Program (OVDP). However, a taxpayer eligible for treatment under streamlined procedures who submits, or has submitted, a voluntary disclosure letter under the OVDP prior to July 1, 2014, but who does yet have a fully executed OVDP closing agreement, may request treatment under the applicable penalty terms available under the streamlined procedures.

OFFSHORE VOLUNTARY DISCLOSURE PROGRAM (OVDP)

The Offshore Voluntary Disclosure Program (OVDP) is a program in which taxpayers may voluntarily disclose previously undisclosed foreign accounts and assets in exchange for reduced penalties and a promise that the IRS will not recommend criminal prosecution for any issue relating to tax noncompliance or failure to file FBARs. The OVDP program is aimed at taxpayers whose conduct may reflect non-willful compliance and wish to avoid criminal prosecution.

The OVDP program requires taxpayers to:

1. Provide all documents required by FAQ 25
2. Cooperate in the voluntary disclosure process
3. Pay a 20% accuracy related penalty under IRC § 6662(a) of the full amount of the underpayments of tax related to foreign accounts and assets for all tax years
4. Pay any related failure-to-file and failure-to-pay penalties
5. Pay any compliance related penalties for years prior to the OVDP
6. Submit full payment for any tax liabilities for years included in the offshore disclosure period

7. Execute a Closing Agreement on Final Determination Covering Specific Matters (Form 906)
8. Agree to cooperate with IRS and Department of Justice offshore enforcement efforts.

The taxpayer will be subject to a 50% penalty if before the taxpayer submits a OVDP pre-clearance request, it becomes public that the financial institution where the taxpayer holds an account or another party facilitating the taxpayer's offshore arrangement is under investigation by the IRS or Department of Justice.

DELINQUENT INTERNATIONAL INFORMATION RETURN SUBMISSION PROCEDURES

The Delinquent International Information Return Submission Procedures are available to taxpayers who need to file delinquent or amended tax returns to report and pay additional tax and do not need to use the OVDP or the Streamline Filing Compliance Procedures. Taxpayers must: (1) have reasonable cause for not timely filing, (2) not be under examination or a criminal investigation by the IRS, and (3) have not been contacted by the IRS about delinquent information returns.

The return must include a reasonable cause statement and the taxpayer must certify that the entity for which the information returns are being filed was not engaged in tax evasion. Penalties may be imposed if the IRS does not accept the taxpayer's explanation of reasonable cause.

FORM 8938
STATEMENT OF SPECIFIED FOREIGN
FINANCIAL ASSETS

In addition to filing an FBAR, taxpayers with significant foreign assets may be required to file a Form 8938. There are separate reporting thresholds for taxpayers living in the US and taxpayers living outside the US. For taxpayers living in the US who are unmarried or married filing separate returns, the reporting threshold is total value of foreign financial assets of more than \$50,000 on the last day of the tax year or more than \$75,000 at any time during the tax year. For taxpayers living in the US who are married and filing a joint return, the reporting threshold is total value of foreign financial assets is more than \$100,000 on the last day of the tax year or more than \$150,000 at any time during the year for married taxpayers filing a joint income tax return. For taxpayers living outside the US who are unmarried or married filing separate returns, the reporting threshold is total value of foreign financial assets of more than \$200,000 on the last day of the tax year or more than \$300,000 at any time during the tax year. For taxpayers living outside the US who are married and filing a joint return, the reporting threshold is total value of foreign financial assets is more than \$400,000 on the last day of the tax year or more than \$600,000 at any time during the year for married taxpayers filing a joint income tax return.

The value of foreign assets is the fair market value. The currency exchange rate for purposes of the Form 8938 is the exchange rate on the last day of the tax year.

Specified foreign financial assets that are required to be reported include financial accounts maintained by a foreign financial institution and certain foreign financial assets not held in an account maintained by a financial institution, including stock or securities issued by someone that is not a U.S. person, any interest in a foreign entity, and any financial instrument or contract that has an issuer or counterparty that is not a US person. However, a taxpayer is not required to report financial accounts maintained by a US payer, such as a domestic financial institution.

If you are considered an owner of a foreign grantor trust, you are not required to report any foreign financial assets held by the trust as long as you timely file a Form 3520 (discussed below) and the trust timely files a Form 3520-A.

FORM 3520
REPORTING TRANSACTIONS WITH FOREIGN TRUSTS AND
RECEIPT OF CERTAIN FOREIGN GIFTS

You may be required to file a Form 3520 if you held a loan from a related foreign trust, you were treated as the owner of any assets of a foreign trust, received a distribution from a foreign trust, or received a gift of more than \$10,000 from a nonresident alien individual or a foreign estate or more than \$15,601 from a foreign corporation or partnership.

The Form 3520 is due on the date that your income tax return is due, including extensions.

In general, the penalty for failure to timely file a Form 3520 is equal to the greater of \$10,000 or 35-percent of the gross reportable amount. I.R.C. § 6677(a). Penalties will not be imposed if the taxpayer can show the failure to file was due to reasonable cause and not willful neglect. I.R.C. § 6677(d). The penalty for failure report a reportable foreign gift is equal to 5-percent of the amount of the gift for each month, not to exceed 25-percent of such amount. I.R.C. § 6039F. Section 6039F also contains a reasonable cause exception.

The reporting of transactions or gifts required to be reported on a Form 3520 are not affected by the tax consequences of the transaction or gift. Therefore, a U.S. citizen who receives a bequest from a foreign estate that is not subject to tax, must report the bequest if it, in combination with other gifts, exceeds \$10,000 in value.