

FBAR UPDATE: WHAT YOU NEED TO KNOW

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Background

- Origin: the Bank Secrecy Act of 1970
- Not a tax law: filing requirement codified under Title 31 of the U.S.C.
 - Used for anti-money laundering purposes
- In 2003: FinCEN delegated its enforcement authority of the reporting rules to the I.R.S. (IR-2003-48)
- Final Regulations issued in 2011 by FinCEN and applicable as of the June 30, 2011 filings.

FBAR Reporting – General Requirement (31 C.F.R. 1010.350(a))

“Each **United States person** having a **financial interest** in, or **signature or other authority** over, **a bank, securities, or other financial account** in a **foreign country** shall report such relationship to the Commissioner of Internal Revenue for each year in which such relationship exists and shall provide such information as shall be specified in **a reporting form prescribed under 31 U.S.C. 5314** to be filed by such persons.”
(emphasis added)

U.S. Persons Subject to Reporting (31 C.F.R. 1010.350(b))

- U.S. citizens (including minors)
- U.S. residents (as defined under §7701(b) of the I.R.C. but using the definition of “United States” as provided in 31 C.F.R. 1010.100(hhh)) including green card holders claiming nonresident status under Treaty tiebreaker rules
- No special provision for minors

U.S. Persons Subject to Reporting (C'd) (31 C.F.R. 1010.350(b))

- Entities including, but not limited, to the following:
 - Corporations (federal tax treatment irrelevant);
 - Partnerships (federal tax treatment irrelevant)
 - Trusts (the definition of §7701(a)(30) does not apply); includes grantor trusts
 - Limited liability companies (federal tax treatment irrelevant);

That are created, *organized or formed under the laws of the U.S.*, a U.S. State, the District of Columbia, the Territories and Insular Possessions of the U.S., or the Indian Tribes.

Accounts Subject to Reporting (31 C.F.R. 1010.350(c))

- **Bank Accounts:**
 - Savings deposits;
 - Demand deposit;
 - Checking account; or
 - Any other account maintained with a person engaged in the banking business.
- **Securities Accounts:**
 - Accounts opened with a person engaged in the business of buying, selling, holding or trading stock or other securities.

Accounts Subject to Reporting (C'd)

(31 C.F.R. 1010.350(c))

- “Other Financial Accounts”:
 - An account with a person that is in the business of accepting deposits as a financial agency;
 - An account that is an insurance or annuity policy with a cash value;
 - An account with a person that acts as a broker or dealer for futures or options transactions in any commodity on or subject to the rules of a commodity exchange or association; or
 - An account with a mutual fund or similar pooled fund which issues shares available to the general public that have a regular net asset value determination and regular redemptions.

Accounts Subject to Reporting (C'd)

(31 C.F.R. 1010.350(c))

- Exceptions:
 - Certain accounts held by the department or agency of the U.S., an Indian Tribe, or any State or political subdivision thereof, or a wholly-owned entity, agency or instrumentality of any of the foregoing.
 - An account of an international financial institution of which the U.S. government is a member;
 - An account in an institution known as a U.S. military banking facility.
 - Correspondent or nostro accounts (which are maintained by banks and used solely for bank-to-bank settlements).

Foreign Country (31 C.F.R. 1010.350(d))

- A foreign financial account is a financial account located outside of the United States.
 - An account maintained with a branch of a United States bank that is physically located outside of the United States is a foreign financial account.
 - An account maintained with a branch of a foreign bank that is physically located in the United States is not a foreign financial account.

Financial Interest

(31 C.F.R. 1010.350(e))

- **Direct:** owner of record or holder of legal title (whether maintained for person's own benefit or for the benefit of others)
- **Indirect:** the following U.S. person if the owner of record or holder of legal title is:
 - Another person acting as an agent, nominee, attorney or in some other capacity on behalf of that U.S. person with respect to a foreign account;
 - A corporation in which that person owns directly or indirectly more than 50% of the voting power or the total value of the shares;
 - A partnership in which the United States person owns directly or indirectly more than 50% of the interest in profits or capital;
 - Any other entity (other than trusts described below) in which the United States person owns directly or indirectly more than 50% of the voting power, total value of the equity interest or assets, or interest in profits.

Financial Interest (C'd)

(31 C.F.R. 1010.350(e))

- **Indirect (C'd):**

- A trust, if the United States person is the trust **grantor** and has an ownership interest in the trust for United States Federal tax purposes (as defined by §§671-679 I.R.C.);
- A trust in which the United States person either has a present **beneficial interest** in more than 50% of the assets or from which such person receives more than 50% of the current income (emphasis added) (unless trust, trustee or agent of trust is U.S. person filing FBAR for trust); or

- **Anti-Avoidance Rule:**

- A United States person that creates an entity for FBAR reporting avoidance purposes shall have a financial interest in any bank, securities, or other financial account in a foreign country for which the entity is the owner of record or holder of legal title

Signature or Other Authority (31 C.F.R. 1010.350(f))

- **In general:**

- When a U.S. person (alone or in conjunction with another person) has the authority to **control** the disposition of money, funds or other assets held in a financial account by direct communication (whether in writing or otherwise) to the person with whom the financial account is maintained.

Signature or Other Authority(C'd)

(31 C.F.R. 1010.350(f))

- Exceptions - Individuals who have signature authority over, but no financial interest in, a foreign financial account are not required to report the account in the following situations:
 - An officer or employee of a bank that is examined by the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the Office of Thrift Supervision, or the National Credit Union Administration is not required to report signature authority over a foreign financial account owned or maintained by the bank.
 - An officer or employee of a financial institution that is registered with and examined by the Securities and Exchange Commission or Commodity Futures Trading Commission is not required to report signature authority over a foreign financial account owned or maintained by the financial institution.

Signature or Other Authority(C'd)

(31 C.F.R. 1010.350(f))

- Exceptions - Individuals who have signature authority over, but no financial interest in, a foreign financial account are not required to report the account in the following situations (C'd):
 - An officer or employee of an Authorized Service Provider is not required to report signature authority over a foreign financial account that is owned or maintained by an investment company that is registered with the Securities and Exchange Commission. Authorized Service Provider means an entity that is registered with and examined by the Securities and Exchange Commission and provides services to an investment company registered under the Investment Company Act of 1940.
 - An officer or employee of an entity that has a class of equity securities listed (or American depository receipts listed) on any United States national securities exchange is not required to report signature authority over a foreign financial account of such entity.

Signature or Other Authority(C'd)

(31 C.F.R. 1010.350(f))

- Exceptions - Individuals who have signature authority over, but no financial interest in, a foreign financial account are not required to report the account in the following situations (C'd):
 - An officer or employee of a United States subsidiary is not required to report signature authority over a foreign financial account of the subsidiary if its United States parent has a class of equity securities listed on any United States national securities exchange and the subsidiary is included in a consolidated FBAR report of the United States parent.
 - An officer or employee of an entity that has a class of equity securities registered (or American depository receipts in respect of equity securities registered) under section 12(g) of the Securities Exchange Act is not required to report signature authority over a foreign financial account of such entity.

Special Rules (31 C.F.R. 1010.350(g))

- Special Rules
 - When over 25 or more foreign financial accounts:
 - Report only the number of accounts and certain other basic information
 - Will be required to provide information upon request.
 - Consolidated Reports:
 - An entity that is a U.S. person and which owns directly or indirectly more than a 50% interest in one or more entities required to report will be permitted to file a consolidated report on behalf of itself and such other entities.
 - Participants and Beneficiaries in Certain Retirement Plans:
 - Participants and beneficiaries in retirement plans under sections 401(a), 403(a) or 403(b) of the Internal Revenue Code as well as owners and beneficiaries of individual retirement accounts under section 408 of the Internal Revenue Code or Roth IRAs under section 408A of the Internal Revenue Code are not required to file an FBAR with respect to a foreign financial account held by or on behalf of the retirement plan or IRA.

Special Rules (31 C.F.R. 1010.350(g))

- Special Rules:
 - Trust Beneficiaries:
 - A trust beneficiary with a financial interest is not required to report the trust's foreign financial accounts on an FBAR if the trust, trustee of the trust, or agent of the trust: (1) is a United States person and (2) files an FBAR disclosing the trust's foreign financial accounts.

Special Rules (Instructions)

- Spousal Reporting:
 - The spouse of an individual who files an FBAR is not required to file a separate FBAR if the following conditions are met:
 - All the financial accounts that the non-filing spouse is required to report are jointly owned with the filing spouse;
 - The filing spouse reports the jointly owned accounts on a *timely* filed FBAR electronically signed; and
 - The filers have completed and signed Form 114a, “Record of Authorization to Electronically File FBAR’s” (maintained with the filers’ records).
 - Otherwise, both spouses are required to file separate FBARs, and each spouse must report the entire value of the jointly owned accounts.

Filing and Record Retention Requirements

- Filing Requirements

- An FBAR must be filed if the aggregate value of the above-mentioned foreign financial accounts held by a U.S. person exceeds \$10,000 at any time during the calendar year.
- The FBAR must be filed electronically on FinCEN Form 114 on or before June 30 of the year following the calendar year for which reporting is required.
- There is no extension of time to file.
- There is no mail-box rule.

Filing and Record Retention Requirements

- Record Retention:

- Persons required to file an FBAR must retain records that contain the name in which each account is maintained, the number or other designation of the account, the name and address of the foreign financial institution that maintains the account, the type of account, and the maximum account value of each account during the reporting period.
- The records must be retained for a period of 5 years from June 30th of the year following the calendar year reported and must be available for inspection as provided by law. Retaining a copy of the filed FBAR can help to satisfy the record keeping requirements. An officer or employee who files an FBAR to report signature authority over an employer's foreign financial account is not required to personally retain records regarding these accounts.

Filing and Record Retention Requirements (C'd)

- Note:
 - Part III of Schedule B to Form 1040 (U.S. income return) must be filled out accordingly (existence of foreign account, requirement to file F.B.A.R., foreign country where account is located)

Penalties for Non-Filing

Civil Penalties

- Non-Willful:
 - Maximum penalty of \$10,000.
 - Showing of reasonable cause can waive penalty.
- Willful:
 - The maximum penalty is the greater of \$100,000 or 50% of the balance in the account in the year of the violation.

Criminal Penalties

- Highest exposure:
 - A fine of \$500,000; and
 - Imprisonment for up to ten years.

Statute of Limitations / Collections

- Civil Penalty – Statute of Limitation (“S.O.L.”):
 - Time to Assess: six years from the date of the relevant F.B.A.R. violation.
 - Collection Phase (after assessment):
 - Two years to file a suit for the collection of an assessed civil penalty from the date of assessment, or the date any judgment becomes final in any criminal action with respect to which the penalty is assessed.
 - There is no S.O.L. with respect to the collection of debt under 31 U.S.C. 3716 (e)(1). *But* in I.R.M. 8.11.6.3 (11-01-2011) the I.R.S indicates a limit of 10 years to collect the F.B.A.R. penalty from the date of assessment, or the date any judgment becomes final in any criminal action with respect to which the penalty is assessed.
 - Note: tax court lacks jurisdiction and debt cannot be discharged in bankruptcy.
- Criminal
 - 5-years from filing date.

Updates

- Child Filings Requirements
- Bitcoin
- Recent Cases

Updates (C'd)

- Child Filing Requirements
 - Updated 6/11/2014 (Form 114 instructions)
 - Responsibility for Child's FBAR
 - Generally, a child is responsible for filing his or her own FBAR report. If a child cannot file his or her own FBAR for any reason, such as age, the child's parent, guardian, or other legally responsible person must file it for the child.
 - Signing the child's FBAR.
 - If the child cannot sign his or her FBAR, a parent or guardian must electronically sign the child's FBAR. In item 45 Filer Title enter "Parent/Guardian filing for child."

Updates (C'd)

- Bitcoin
 - On a recent panel, I.R.S. official stated that Bitcoins are not reportable on F.B.A.R., at least this year, with a caveat that the view may change.
 - However, tax practitioners have stated that, without official guidance, taxpayers should file protective disclosures if and to the extent the Bitcoin is held through exchange accounts.
 - The risk is the company performing the services will be treated as a bank or similar financial institution.
- Whether it is FBAR reportable will depend on how it is held.
 - If direct, cf. real property.
 - If indirect and held through a custodial account or similar account, likely FBAR reportable.
 - If indirect and held through an entity (e.g., (non-grantor) trust), beneficiary must have control of the trust using a greater than 50% test in order to look through the entity.

United States v. Zwerner

- *United States v. Zwerner*, S.D. Fla., No. 1:13-cv-22082, 5/28/14.
 - Taxpayer has undisclosed accounts offshore held through entities.
 - Taxpayer mistakenly believes he entered into voluntary disclosure based on reliance on counsel.
 - Taxpayer amends returns and is audited.
 - I.R.S. assesses willful F.B.A.R. penalty for the period 2004-2007:
 - 2004 - \$723,762, assessed on June 21, 2011;
 - 2005 - \$745,209, assessed on August 10, 2011;
 - 2006 - \$772,838, assessed on August 10, 2011;
 - 2007 - \$845,527, assessed on August 10, 2011.

United States v. Zwerner (C'd)

- *United States v. Zwerner*, S.D. Fla., No. 1:13-cv-22082, 5/28/14.
 - Taxpayer refuses to pay.
 - U.S. files a complaint to collect 10 days before S.O.L. expires on first assessment.
 - Taxpayer makes several affirmative defenses, including, *e.g.*, based on equity, reliance on counsel, and lastly on the Eighth Amendment's prohibition against excessive fines.
 - After a jury trial, the jury finds 3 willful violations (2004-2006).
 - Taxpayer ultimately settles for 2 violations, plus interest and penalties.
 - T.B.D.: whether the fines violate the Eighth Amendment.

U.S. v. Hom

- U.S. v. HOM, 113 AFTR 2d 2014-XXXX, (DC CA), 06/04/2014
 - Facts
 - During 2006, pro se defendant John Hom (“D”) gambled online through internet accounts with PokerStars.com and PartyPoker.com. In 2007, D continued to gamble online through his PokerStars account. Both poker websites allowed D to deposit money or make withdrawals.
 - D used his account at FirePay.com, an online financial organization that receives, holds, and pays funds on behalf of its customers, to fund his online PokerStars and PartyPoker accounts. He deposited money into his FirePay account via his domestic Wells Fargo bank account or other online financial institutions, such as Western Union.

U.S. v. Hom

- U.S. v. HOM, 113 AFTR 2d 2014-XXXX, (DC CA), 06/04/2014
 - Facts (C'd)
 - In 2006, FirePay ceased allowing United States customers to transfer funds from their FirePay accounts to offshore internet gambling sites, so D used Western Union and other online financial institutions to transfer money from his Wells Fargo bank account to his online poker accounts.
 - D admitted that at some points in both 2006 and 2007, the aggregate amount of funds in his FirePay, PokerStars, and PartyPoker accounts exceeded \$10,000 in U.S. currency.

U.S. v. Hom (C'd)

- U.S. v. HOM, 113 AFTR 2d 2014-XXXX, (DC CA), 06/04/2014
 - Facts (C'd)
 - After the I.R.S. detected discrepancies in defendant's federal income tax returns for 2006 and 2007, it opened an FBAR examination.
 - D did not file his 2006 or 2007 FBARs until June 26, 2010. Moreover, his submitted an FBAR for 2006 did not include his FirePay account.
 - On September 20, 2011, the I.R.S. assessed defendant with civil penalties for his non-willful failure to submit F.B.A.R.'s regarding his interest in his FirePay, PokerStars, and PartyPoker accounts.
 - The I.R.S. assessed a \$30,000 penalty for 2006, which included a \$10,000 penalty for each of the three accounts, and a \$10,000 penalty for 2007 based solely on defendant's PokerStars account.

U.S. v. Hom (C'd)

- U.S. v. HOM, 113 AFTR 2d 2014-XXXX, (DC CA), 06/04/2014
 - Held:
 - “While our court of appeals has not yet answered what constitutes ‘other financial account[s]’ ... the Court of Appeals for the Fourth Circuit found that an account with a financial agency is a financial account under Section 5314 ... Under Section 5312(a)(1), a ‘person acting for a person’ as a ‘financial institution’ or a person who is ‘acting in a similar way related to money’ is considered a ‘financial agency.’ Section 5312(a)(2) lists 26 different types of entities that may qualify as a “financial institution.” Based on the breadth of the definition, our court of appeals has held that “the term ‘financial institution’ is to be given a broad definition.’ ... The government claims that FirePay, PokerStars, and PartyPoker are all financial institutions because they function as ‘commercial bank[s].’ ... The Fourth Circuit in Clines found that ‘[b]y holding funds for third parties and disbursing them at their direction, [the organization at issue]functioned as a bank [under Section 5314] ... As FirePay, PokerStars, and PartyPoker functioned as banks, defendant's online accounts with them are reportable.”

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