

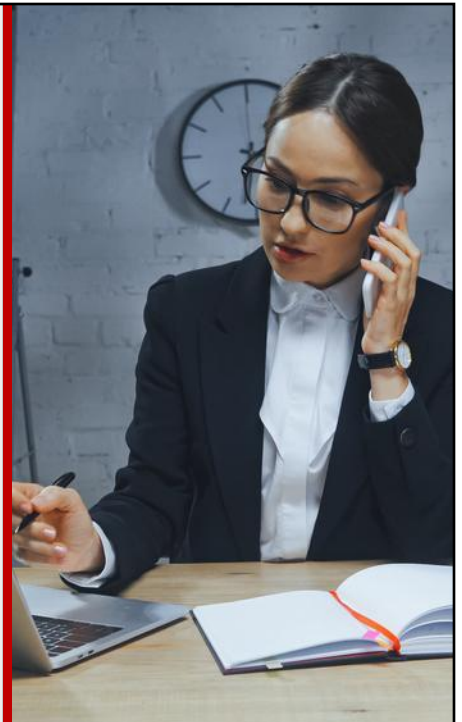


HUGHES NOFF TAX LAW, LLC

Foreign Bank Accounts and Informational Reporting



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MEET THE SPEAKER

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Eli Noff is a partner at Hughes Noff Tax Law, where he utilizes his skills as an attorney and CPA to defend clients before the IRS and state taxing authorities.

He also handles international tax matters, resolving issues involving offshore voluntary disclosures, IRS examination of foreign bank accounts and other complex compliance matters.

He has successfully represented clients across numerous federal and state examinations and appeals, IRS criminal investigations, and other matters before the federal and state tax courts.

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Objectives

- Summarize international informational reporting requirements
- Identify the consequences of failure to file informational reports, such as information reporting penalties and when the statute of limitations comes into play
- Outline compliance programs and procedures, such as voluntary disclosures and streamlined filing compliance procedures
- Determine practical and ethical challenges associated with providing advice in this space

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FBAR Filing Criteria

- An FBAR is required if **all** of the following apply:
 - The filer is a U.S. person
 - The U.S. person has a financial interest in a financial account or signature or other authority over a financial account
 - The financial account is in a foreign country
 - The aggregate amount(s) in the account(s) valued in dollars exceed \$10,000 at any time during the calendar year

FBAR – General

- The new annual due date for filing Reports of Foreign Bank and Financial Accounts (FBAR) for foreign financial accounts is April 15. This date change was mandated by the *Surface Transportation and Veterans Health Care Choice Improvement Act of 2015*.
- The act also mandates a maximum six-month extension of the filing deadline. To implement the statute with minimal burden to the public and FinCEN, FinCEN will grant filers failing to meet the FBAR annual due date of April 15 an **automatic extension** to Oct. 15 each year.
 - Consider possibility of current year compliance even if the client already filed their 1040
- The FBAR statute of limitation for failure to file is six years from the due date of the FBAR report. For calendar years 2015 and prior, due date is 6/30/YYYY. For calendar years 2016 and later, due date is 4/15/YYYY. 31 U.S.C. 5321(b)(1).

FBAR: Financial Account

- Bank account, such as a savings deposit, demand deposit, checking, time deposit (CD), or any other account maintained with a financial institution or other person engaged in the business of banking
- Securities account, securities derivatives account, or other financial instruments account held with a person engaged in the business of buying, selling, holding or trading stock, or other securities
- An account with a person in the business of accepting deposits as a financial agency
- An insurance or annuity policy that has 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
- A mutual fund or similar pooled fund
- More...

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FBAR: Financial Account

- What is not considered a financial account?
 - Stocks, bonds or similar financial instruments held directly by the person
 - Real estate or an account holding solely real estate (e.g., Mexican "fideicomiso")
 - A safety deposit box
 - Exception where the financial institution has access and authority to dispose of the contents of the box
 - See 31 USC 5314 for definition of "foreign financial agency"

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FBAR: Financial Interest (Direct)

- The owner of record or has legal title, whether the account is maintained for their own benefit or for the benefit of others, including non-U.S. persons
- If an account is maintained in the name of two persons jointly, or if several persons each own a partial interest in an account, each of those U.S. persons has a financial interest in that account and, generally, each person must file the FBAR
 - Special rules for spousal filing in IRM 4.26.16.4
- **Note:** Because the FBAR is a report of foreign financial accounts, the entire account value for jointly-owned accounts is reported on each FBAR. Accounts are not prorated for a person's percentage of ownership.

FBAR: Financial Interest (Indirect)

- A U.S. person has an "other financial interest" in each bank, securities, or other financial account in a foreign country for which the owner of record or holder of legal title is:
 - A person acting as an agent, nominee, attorney or in some other capacity on behalf of the U.S. person
 - A corporation, whether foreign or domestic, in which the U.S. person owns directly or indirectly more than 50% of the total value of shares of stock or more than 50% of the voting power for all shares of stock
 - A partnership, whether foreign or domestic, in which the United States person owns an interest in more than 50% of the profits (distributive share of income, taking into account any special allocation agreement) or more than 50% of the capital of the partnership
 - Any other entity in which the U.S. person owns directly or indirectly more than 50% of the voting power, total value of the equity interest or assets, or interest in profits

FBAR: Financial Interest (Indirect)

- A trust, if the U.S. person is the trust grantor and has an ownership interest in the trust for U.S. federal tax purposes under 26 USC 671–679 and the regulations thereunder
- A trust, whether foreign or domestic, in which the U.S. person either has a present beneficial interest, either directly or indirectly, in more than 50% of the assets of the trust or from which such person receives more than 50% of the trust's current income
- Anti-avoidance rule: A U.S. person that causes an entity including, but not limited to, a corporation, partnership or trust, to be created for the purpose of evading the FBAR reporting and/or recordkeeping requirements 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. 31 CFR 1010.350(e)(3)

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FBAR: Financial Interest (Indirect)

Practice tip:

- Look to the control of the account and source of funds, not just legal title
- Taxpayers sometimes title accounts and offshore assets in the names of other parties believing that absolves them of a filing requirement
- Interview client thoroughly to ensure all offshore assets are taken into consideration



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FBAR: Signature Authority

- An individual has signature or other authority over an account if that individual (alone or in conjunction with another) can 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
- Individuals **not** considered as having signature authority:
 - Individuals with only the authority to buy or sell investments within the account, but no authority to disburse assets from the account
 - Individuals with supervisory authority over the individuals who actually communicate with the person with whom the account is maintained
 - Only individuals can have signature authority. Signature authority attributed to entities must be exercised by individuals.

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FBAR: Foreign Country

- Generally, location of an account controls.
 - Accounts of foreign financial institutions located in the U.S. are not considered foreign accounts for FBAR
 - Accounts of U.S. financial institutions located outside the U.S. are considered foreign accounts

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FBAR: Penalties – Non-willful Violations

- Violations occurring prior to Nov. 2, 2015, the civil penalty is not to exceed \$10,000 **per violation**
- Violations occurring after Jan. 25, 2024, the civil penalty is not to exceed \$16,117 **per violation**
- *Bittner v. United States*
- Penalty should not be imposed if:
 - Violation was due to reasonable cause, and
 - Delinquent FBARs accurately filed

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FBAR: Penalties – Willful Violations

- Penalty applies to individuals and businesses
- Violations occurring prior to Nov. 2, 2015, the civil penalty may be the greater of \$100,000 or 50% of the balance in the account at the time of the violation, **for each violation**
- Violations occurring after Jan. 25, 2024, the civil penalty may be the greater of \$161,166 or 50% of the balance in the account at the time of the violation, **for each violation**
- *Violation* definition

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FBAR: Penalties – 4. Willful Violations

- The **IRM** test for willfulness is whether there was a voluntary, intentional violation of a known legal duty.
 - Courts have largely expanded scope of willfulness.
- Burden of establishing willfulness is on the service
- Court cases have been largely unfriendly to taxpayers
- Consider “constructive knowledge” and presence of Schedule B in the return
- Consider “willful blindness” or “reckless” behavior

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FBAR: Mitigation Guidelines

- For most willful FBAR cases, if four threshold conditions met, lower FBAR penalty
 1. The person has no history of criminal tax or BSA convictions for the preceding 10 years, as well as no history of past FBAR penalty assessments
 2. No money passing through any of the foreign accounts associated with the person was from an illegal source or used to further a criminal purpose
 3. The person cooperated during the examination (i.e., IRS did not have to resort to a summons to obtain non-privileged information; the taxpayer responded to reasonable requests for documents, meetings and interviews; and the taxpayer back-filed correct reports)
 4. IRS did not sustain a civil fraud penalty against the person for an underpayment for the year in question due to the failure to report income related to any amount in a foreign account

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FBAR: Mitigation Guidelines (Willful)

Penalties for Willful Violation	
To qualify for Level I-Willful – determine aggregate balance	If the maximum aggregate balance for all accounts to which the violations relate did not exceed \$50,000 during the calendar year, Level I-Willful mitigation applies to all violations
The Level I willful penalty is	The greater of \$1,000 per year or 5% of the maximum aggregate balance of the accounts during the year to which the violations relate
To qualify for Level II-Willful – determine aggregate balance	If the maximum aggregate balance for all accounts to which the violations relate exceeds \$50,000 but does not exceed \$250,000, Level II-Willful mitigation applies to all violations. Level II-Willful penalties are computed on a per account basis.
The Level II-Willful penalty is	For each account for which there was a violation, the greater of \$5,000 or 10% of the maximum account balance during the calendar year at issue
To qualify for Level III-Willful – determine aggregate balance	If the maximum aggregate balance for all accounts to which the violations relate exceeds \$250,000 but does not exceed \$1,000,000, Level III-Willful mitigation applies to all violations. Level III-Willful penalties are computed on a per account basis.
The Level III-Willful penalty is	For each account for which there was a violation, the greater of 10% of the maximum account balance during the calendar year at issue or 50% of the account balance on the day of the violation
To qualify for Level IV-Willful – determine aggregate balance	If the maximum aggregate balance for all accounts to which the violations relate exceeds \$1,000,000, Level IV-Willful mitigation applies to all violations. Level IV-Willful penalties are computed on a per account basis.
The Level IV-Willful penalty is	For each account for which there was a violation, the greater of 50% of the balance in the account at the time of the violation or \$100,000 (i.e., the statutory maximum penalty)

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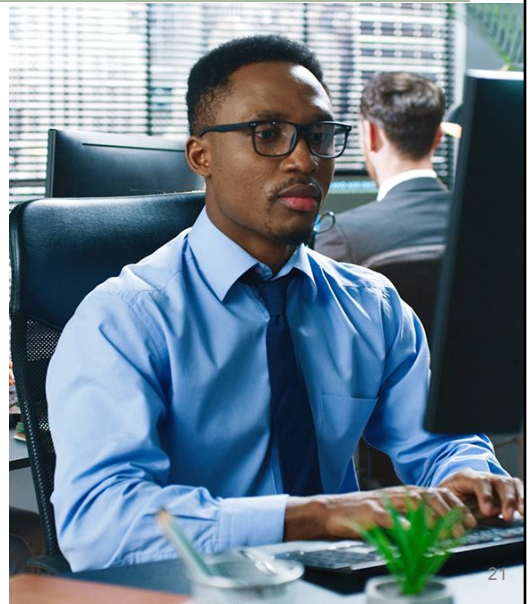
FBAR: Penalties and Appeal

- FBAR penalties can be administratively appealed in one of two ways:
 - Pre-assessment
 - Post-assessment
- If administrative appeal is lost, DOJ may bring suit to collect the FBAR penalty within two years of assessment
 - Penalty can be litigated as part of that legal proceeding
 - Possible settlement discussions

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FBAR: Collection Statute Expiration

- Two-year limitation on FBAR penalty collection suit 31 U.S.C. 5321(b)(2)
- The two-year limitation period for filing an FBAR penalty collection suit cannot be extended
 - However, the government may obtain payment of the FBAR penalty by offsetting payments without a statute of limitation. IRM 8.11.6.4.1.1 (09-27-2018).



Key IRS Outbound International Forms

Form 8938

- In effect for tax years beginning after March 18, 2010 (tax year 2011 forward)
- Required to be filed by **specified individuals** with an interest in a **specified foreign financial asset**
- Specified individuals:
 - U.S. citizen
 - Resident alien
 - Nonresident alien who elects to be treated as a resident alien
 - Resident of certain U.S. possessions
 - **Specified domestic entity** (anti abuse)

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Form 8938 – Specified Foreign Financial Assets

- Specified Foreign Financial Assets:
 - Financial accounts (depository or custodial) maintained by a foreign financial institution
 - The following foreign financial assets if they are held for investment and not held in an account maintained by a financial institution:
 - Stock or securities issued by someone that is not a U.S. person (including stock or securities issued by a person organized under the laws of a U.S. possession),
 - Any interest in a foreign entity, and
 - Foreign partnership interests
 - Foreign mutual funds
 - Foreign accounts and foreign non-account investment assets held by foreign or domestic grantor trust for which you are the grantor
 - Foreign issued life insurance or annuity contract with a cash value
 - A note, bond, debenture or other form of indebtedness issued by a foreign person
 - An interest in a foreign trust or foreign estate
 - More...

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Form 8938 Filing Thresholds

Taxpayers living in the U.S.:

- Unmarried taxpayers – total value of your specified foreign financial assets is more than \$50,000 on the last day of the tax year or more than \$75,000 at any time during the tax year
- Married taxpayers filing a joint return – total value of your specified 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 tax year
- Married taxpayers filing separate – total value of your specified foreign financial assets is more than \$50,000 on the last day of the tax year or more than \$75,000 at any time during the tax year

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Form 8938 Filing Thresholds

Taxpayers living outside the U.S. :

- Unmarried taxpayers – total value of your specified foreign financial assets is more than \$200,000 on the last day of the tax year or more than \$300,000 at any time during the tax year
- Married taxpayers filing a joint return – total value of your specified 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 tax year
- Married taxpayers filing separate – total value of your specified foreign financial assets is more than \$200,000 on the last day of the tax year or more than \$300,000 at any time during the tax year

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Form 8938 – Exceptions

- Certain specified foreign financial assets need not be reported (itemized) on Form 8938 if they are being reported on the following forms:
 - **Form 3520**, *Annual Return to Report Transactions with Foreign Trusts and Receipt of Certain Foreign Gifts*
 - **Form 3520-A**, *Annual Information Return of Foreign Trust with a U.S. Owner*
 - **Form 5471**, *Information Return of U.S. Persons With Respect to Certain Foreign Corporations*
 - **Form 8621**, *Information Return by a Shareholder of a Passive Foreign Investment Company*
 - **Form 8865**, *Return of U.S. Persons With Respect to Certain Foreign Partnerships*

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Form 8938 Penalties

- Failure to file by the due date may result in imposition of \$10,000 penalty
- Once IRS solicits missing report, failure to correct may result in imposition of additional \$10,000 penalty per month (up to \$50,000)
- Reasonable cause exceptions applies – see IRC 6038D(g)
- 40% penalty on balance applies to understatement attributable to an undisclosed foreign financial asset

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Form 3520

- Form 3520, *Annual Return To Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts*
- Required to be filed by:
 1. U.S. person who directly or indirectly transfers property or cash to a foreign trust
 2. U.S. owner of a foreign trust under IRC 671-679
 3. U.S. person receiving distribution, direct or indirect, from a foreign trust
 4. Gifts or inheritances from foreign person or foreign corporation
- Consider possible Form 3520 obligations for foreign pensions and IRS Notice 2020-17 exclusions, and proposed regulations issued May 8, 2024.

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Form 3520

- When to file – in general, a U.S. person's Form 3520 is due on the 15th day of the 4th month following the end of such person's tax year for income tax purposes, which, for individuals, is April 15
- Where to file – sent to IRS Service Center in Ogden, Utah



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Form 3520 – Penalties

- Penalty applies if form is not timely filed or if information incomplete or incorrect
- Penalty is greater of \$10,000 or the following:
 - 35% of the gross value of any property transferred to a foreign trust for failure by a U.S. transferor to report the creation of or transfer to a foreign trust
 - 35% of the gross value of the distributions received from a foreign trust for failure by a U.S. person to report receipt of the distribution
 - 5% of the gross value of the portion of the foreign trust's assets treated as owned by a U.S. person under the grantor trust rules (Sections 671 through 679) for failure by the U.S. person to report the U.S. owner information. Such U.S. person is subject to an additional separate 5% penalty (or \$10,000 if greater), if the foreign trust (a) fails to file a timely Form 3520-A or (b) does not furnish all of the information required by Section 6048(b) or includes incorrect information. See Section 6677(a) through (c) and the Instructions for Form 3520-A.
 - In the case of a failure to report foreign gifts described in Section 6039F, a penalty equal to 5% of the amount of such foreign gifts applies for each month for which the failure to report continues (not to exceed a total of 25%)
- IRS Announcement October 24, 2024.

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Form 3520 – Penalties

- Additional penalties will be imposed if the noncompliance continues for more than 90 days after the IRS mails a notice of failure to comply with the required reporting
 - For more information, see Section 6677 and 6039F
- Reasonable cause – no penalties will be imposed if the taxpayer can demonstrate that the failure to comply was due to reasonable cause and not willful neglect
- Accuracy penalty of 40% under IRC 6662(j)

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Form 3520-A

- Form 3520-A, *Annual Information Return of Foreign Trust With A U.S. Owner*
- Required to be filed by foreign grantor trust with a U.S. owner (IRC 671-679)
- Not required by owners of certain Canadian RRSPs or RRIFs
- Due by 15th day of the 3rd month following foreign trust's tax year end
- Penalties – greater of \$10,000 or 5% of trust's assets considered owned by U.S. person

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Form 5471

- Form 5471, *Information Return of U.S. Persons With Respect to Certain Foreign Corporations*
- Filed by U.S. person to report ownership interest in a foreign corporation
 - Consider constructive ownership rules
- Category 1 filer – Specified Foreign Corporation – 2017 Transition Tax
- Category 2 filer – U.S. citizen or resident who is an officer or director of a foreign corporation in which a U.S. person has acquired 10% of the voting power or value of a foreign corporation's stock
- Category 3 filer – U.S. person who acquired 10% stock ownership in a foreign corporation or who becomes a U.S. person while owning 10% or disposes of stock to reduce ownership to less than the requirement
- Category 4 filer – U.S. person who controls (owns more than 50% of the stock value and voting power) of a foreign corporation during the annual accounting period of the foreign corporation
- Category 5 filer – U.S. person who owns at least 10% of the voting stock of a controlled foreign corporation when more than 50% of the voting power or stock value is owned by U.S. persons

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Form 5471 – Penalties

- A \$10,000 penalty is imposed for each annual accounting period of each foreign corporation for failure to furnish the required information within the time prescribed
- If the information is not filed within 90 days after the IRS has mailed a notice of the failure, an additional \$10,000 penalty (per foreign corporation) is charged for each 30-day period
- The additional penalty is limited to a maximum of \$50,000 for each failure
- IRC 6662(j) penalties may be imposed for understatements attributable to undisclosed foreign financial assets
- Reasonable cause exception
- Litigation Update

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Form 8865 (Including Forms K-2 & K-3)

- Form 8865, *Information Return for U.S. Partners of a Foreign Partnership*
- Category 1 filer – U.S. person who controls (owns more than 50%) of a foreign partnership at any time during the partnership's tax year
- Category 2 filer – U.S. person who at any time during the tax year of the foreign partnership owned a 10% or greater interest in the partnership while the partnership was controlled by U.S. persons each owning at least a 10% interest
- Category 3 filer – U.S. person who contributes property to a foreign partnership and owns (directly or constructively) at least 10% of the foreign partnership after the contribution or the value of the property contributed in the 12 months ending on the date of the transfer exceeds \$100,000 USD
- Category 4 filer – U.S. person who has a reportable event, such as: acquisition resulting in an increase to 10% or by 10% in ownership interest, or a disposition of 10% or that results in a change of 10% of the ownership interest in the foreign partnership
- Form 8865 penalty is \$10,000 USD per foreign partnership per year for failure to file, or inaccurate filing. Penalties vary based on category filer.

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Form 8621

- Form 8621, *Information Return by U.S. Shareholder of PFIC or QEF*
 - Any foreign corporation that meets one of the following conditions:
 - Income test:
 - 75% or more of the corporation's gross income for its taxable year is passive income, or
 - Asset test
 - At least 50% of the average percentage of assets held by the foreign corporation during the taxable year are assets that produce passive income or that are held for the production of passive income
- CFC Overlap Rule (since 1997)
- Once a PFIC always a PFIC, absent elections

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Form 8621

- PFIC examples commonly found in offshore disclosures:
 - Foreign mutual funds
 - Businesses in early stages – limited startup exception
- Attribution and look-through rules
- PFIC exceptions exist
- Reporting thresholds

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Form 8858

- **Information Return of U.S. Persons With Respect to Foreign Disregarded Entities (FDEs) and Foreign Branches (FBs)**
- The U.S. person filing Form 8858 is any U.S. person that:
 - Is the tax owner of an FDE,
 - Owns a specified interest in an FDE indirectly or constructively through a CFC or a CFP (see items 2 and 3 under [Who Must File](#), earlier, for more detailed information), or
 - Operates (directly or indirectly through a tier of FDEs or partnerships) an FB
- Penalties – \$10,000 plus reduction in foreign tax credits

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Informational Report Code Sections

I.R.C. § § 1295(b) and 1298(f)	Form 8621
I.R.C. § 6038	Forms 5471, 8865, 8858
I.R.C. § 6038A	Form 5472
I.R.C. § 6038B	Form 8865
I.R.C. § 6038D	Form 8938
I.R.C. § 6046	Form 5471
I.R.C. § 6046A	Form 8865
I.R.C. § 6039F, 6048	Forms 3520, 3520-A

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Assessment Statute Expiration Date - Considerations

- I.R.C. § 6501(c)(8) provides that the period of limitations on assessment does not expire until three years after the date on which the IRS is furnished the information reports required under I.R.C. § 1298(f), 6038, 6038A, 6038B, 6038D, 6046, 6046A or 6048
- I.R.C. § 6501(c)(8) holds open the statute of limitations **for the entire tax return** if a foreign information return was required to be filed but was not **even if the three-year or the six-year period of limitations on assessment has expired**
- Applies to any income tax return filed after March 18, 2010, and to any return to which the period of limitations on assessment had not yet expired as of that date

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Voluntary Compliance Procedures

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Voluntary Compliance Procedures

- Voluntary Disclosure Practice (post-OVDP)
- Streamlined Filing Compliance Procedures
- Delinquent FBAR Submission Procedures
- Delinquent International Information Return Submission Procedures

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Updated Voluntary Disclosure Practice

(IRS Memorandum – LB&I-09-1118-014)
(Nov. 20, 2018)

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Voluntary Compliance Procedures

- Voluntary Disclosure Practice (post-OVDP)
- Streamlined Filing Compliance Procedures
- Delinquent FBAR Submission Procedures
- Delinquent International Information Return Submission Procedures

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Updated Voluntary Disclosure Practice: Steps

- Criminal Investigation (CI) Pre-clearance (Form 14457)
 - Requires disclosure of taxpayer's name and basic offshore financial and entity information
 - Provides ability to check taxpayer status before proceeding
- After pre-clearance, taxpayer submits more robust application to CI as required on Form 14457
 - Side note: what happens if taxpayer does not clear?
- Revenue agent assignment and examination
- Case closure
- Possible additional step: IRS appeals

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Updated Voluntary Disclosure Practice: Scope

- Six-year disclosure period (most recent six years)
- An examination is performed
- Examiners will propose tax, penalties and interest
- After process is completed, taxpayers and IRS are expected to reach an agreement
- General penalty framework (see next slide)
- IRS expects taxpayer to make arrangements to pay the liability
 - "In general, the Service expects that voluntary disclosures will be resolved by agreement with full payment of all taxes, interest, and penalties for the disclosure period. In the event a taxpayer fails to cooperate with the civil examination, the examiner may request that CI revoke preliminary acceptance. See I.R.M. 9.5.11.9.4 (discussing cooperation)." IRM 4.63.3.26.1(5)(04-27-2021).

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Updated Voluntary Disclosure Practice: Penalties

- Generally, fraud penalty (under either § 6663 or 6651(f)) will be asserted to the one year with highest tax liability
- Taxpayer has ability to argue for accuracy-related penalty instead, **but** "[g]iven the objective of the voluntary disclosure practice, granting requests for the imposition of lesser penalties is expected to be exceptional"
- "In limited circumstances, examiners may apply the civil fraud penalty to more than one year in the six-year scope (up to all six years) based on the facts and circumstances of the case, **for example, if there is no agreement as to the tax liability**"
- "Examiners may apply the civil fraud penalty beyond six years if the taxpayer fails to cooperate and resolve the examination by agreement"
- "Willful FBAR penalties will be asserted in accordance with existing IRS penalty guidelines under IRM 4.26.16 and 4.26.17"

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Updated Voluntary Disclosure Practice: Penalties

- “Penalties for the failure to file information returns will not be automatically imposed”
 - Examiner discretion will consider the application of other penalties (such as civil fraud penalty and willful FBAR penalty) and resolve the examination by agreement
- Taxpayers retain the right to request an appeal with the Office of Appeals
- Note the significant discretion afforded to the IRS in various aspects of the disclosure

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Streamlined Filing Compliance Procedures

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Streamlined Filing Compliance Procedures

- Program does not provide protection from criminal prosecution if the IRS and DOJ determine that the particular circumstances warrant prosecution
 - If that is a concern, consider eligibility for SFCP to begin with
- Once streamlined submission filed, ineligible for voluntary disclosure
- Must have unreported income (from foreign financial assets) to be eligible



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Streamlined Filing Compliance Procedures

- Two different streamlined procedures available:
 1. U.S. taxpayers **residing outside** of the United States (SFOP)
 2. U.S. taxpayers **residing in** the United States (SDOP)

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Streamlined Filing Compliance Procedures

- Taxpayer must certify **under penalties of perjury** that their conduct was non-willful – “conduct that is due to negligence, inadvertence, or mistake, or conduct that is the result of a good faith misunderstanding of the requirements of the law”
- Careful consideration of willfulness required

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SFOP: Non-Resident Defined

- U.S. persons (U.S. citizens or lawful permanent residents, or estates of U.S. citizens or lawful permanent residents) – in any one or more of the most recent three years for which the U.S. tax return due date (or properly applied for extended due date) has passed, the individual did not have a U.S. abode and the individual was physically outside the United States for at least 330 full days
- Non-U.S. persons – in any one or more of the last three years for which the U.S. tax return due date (or properly applied for extended due date) has passed, the individual did not meet the substantial presence test of IRC Section 7701(b)(3)
- For joint returns, both spouses must meet non-residency eligibility to qualify for SFOP

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SFOP: Procedure

- File amended or delinquent tax returns along with required information returns (e.g. Forms 8938, 5471, 3520 and 8621) for most recent three years for which the tax return due date (or properly extended due date) has passed
- Electronically file delinquent FBARs for most recent six years for which the FBAR due date has passed
- Submit payment of tax and interest along with disclosure

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SFOP: Certification

- Must complete and sign *Certification by U.S. Person Residing Outside of the U.S.* (Form 14653), certifying under penalties of perjury:
 - Meet eligibility for SFOP procedures
 - All required FBAR have been filed
 - Statement that failure to report all income, pay tax and submit informational reports was due to non-willful conduct

Certification must include both good and bad facts.

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SFOP: Penalties

- Under SFOP, **no** assessment of:
 - Miscellaneous offshore penalties
 - Failure to file penalties
 - Failure to pay penalties
 - Accuracy-related penalties
 - Informational reporting penalties
- Taxpayer may be examined and penalized if taxpayer found to be willful

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SDOP: Eligibility

- Taxpayers eligible if:
 - Do not meet the non-residency requirement
 - Previously **filed** U.S. return (if required) for most recent three years for which the due date (or properly extended due date) has passed
 - Failed to report gross income from a foreign financial asset and pay tax and failure to file international informational reports
 - Failure to file informational reports and pay tax resulted from non-willful conduct

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SDOP: Procedures

- File amended tax returns, including **all** required information returns, for the most recent three years for which the U.S. tax return due date (or properly extended due date) has passed
- For the most recent six years for which the FBAR due date has passed, e-file the delinquent FBARs (FinCEN 114)
- Pay tax and interest due per amended returns, along with payment of 5% miscellaneous offshore penalty on highest year-end aggregate balance for most recent six years for which FBARs are being filed

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SDOP: Procedures

- 5% penalty includes any offshore assets which were:
 1. Not previously reported on a timely filed FBAR, or
 2. Not previously reported on a timely filed Form 8938, or
 3. The income from that asset was not reported on the original return

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SDOP: Procedures

- Complete and sign, under penalties of perjury, a *Certification by U.S. Person Residing in the U.S.*, (Form 14654) certifying:
 - Eligibility for the SDOP
 - That all required FBARs have now been filed
 - That the failure to report income, pay tax and file the informational reports resulted from non-willful conduct
 - Accuracy of the 5% miscellaneous offshore penalty

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SDOP

- IRS will **not** assert accuracy-related penalties, FBAR penalties or information return penalties for the information on returns submitted, **unless** IRS examines and determines FBAR violation was willful or income tax non-compliance was due to fraud
- IRS may assert penalties on any additional deficiencies it determines through examination

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Delinquent Submission Procedures

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Delinquent Submission Procedures

- Delinquent FBAR submission procedures
- Delinquent International Information return submission procedures

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Delinquent Submission Procedures

Delinquent FBAR Submission Procedures

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Delinquent FBAR Submission Procedures

- For taxpayers who do not need to use VD or Streamlined to file delinquent or amended tax returns to report and pay additional tax, but who:
 - Have not filed a required Report of Foreign Bank and Financial Accounts (FBAR) (FinCEN Form 114),
 - Are not under a civil examination or a criminal investigation by the IRS, and
 - Have not already been contacted by the IRS about the delinquent FBARs
 - Should file the delinquent FBARs according to the FBAR instructions

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Delinquent FBAR Submission Procedures

- Must include reasonable cause statement for late filed FBAR
- The IRS will not impose a penalty for the failure to file the delinquent FBARs if you properly reported on your U.S. tax returns, and paid all tax on, the income from the foreign financial accounts reported on the delinquent FBARs, and you have not previously been contacted regarding an income tax examination or a request for delinquent returns for the years for which the delinquent FBARs are submitted
- FBARs will not be automatically subject to audit but may be selected for audit

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Delinquent Submission Procedures

**Delinquent International Information Return
Submission Procedures**

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Delinquent International Information Return Submission Procedures

- For taxpayers who do not need to use VD or Streamlined to file delinquent or amended tax returns to report and pay additional tax, but who:
 - Have not filed one or more required international information returns,
 - Have reasonable cause for not timely filing the information returns,
 - Are not under a civil examination or a criminal investigation by the IRS, and
 - Have not already been contacted by the IRS about the delinquent information returns
 - Should file the delinquent information returns with a statement of all facts establishing reasonable cause for the failure to file

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Delinquent International Information Return Submission Procedures

- As part of reasonable cause must certify that any entity for which the information returns is being filed was not engaged in tax evasion
- Must attach the reasonable cause statement to **each** delinquent information report being filed
- All delinquent international information returns other than Forms 3520 and 3520-A should be attached to an amended return and filed according to the applicable instructions for the amended return
- All delinquent Forms 3520 and 3520-A should be filed according to the applicable instructions for those forms
- Subject to examination

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Delinquent International Information Return Submission Procedures

- Under **prior** guidance, penalties would **not** automatically be assessed if the taxpayer had reasonable cause
- **Updated** guidance late 2020 – “penalties may be assessed **without considering the attached reasonable cause statement**. It may be necessary for taxpayers to respond to specific correspondence and submit or resubmit reasonable cause information.”

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Delinquent International Information Return Submission Procedures – UPDATE 10/2024

- The IRS has ended its practice of automatically assessing penalties at the time of filing for late-filed Forms 3520, Part IV, which deal with reporting foreign gifts and bequests
- By the end of the year the IRS will begin reviewing any reasonable cause statements taxpayers attach to late-filed Forms 3520 and 3520-A for the trust portion of the form before assessing any Internal Revenue Code (IRC) § 6677 penalty

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Penalty Defense

- Consider substantive and procedural defenses:
 - Form not required to have been filed
 - IRC 6751(b) defense
 - Reasonable cause
 - Reliance on a professional
 - First time penalty abatement (limited circumstances)
 - *Farhy* and other constitutional arguments
- Even if appealed, for many assessable international informational reporting penalties, collection case continues
 - Monitor Collection Due Process (CDP) rights