

# Report of Foreign Bank and Financial Accounts: Significant Revisions and Severe Penalties

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In September 2008, the IRS website posted revisions to the Report of Foreign Bank and Financial Accounts (Form TD F 90-22.1) that surprised many practitioners. This article discusses new traps for the uninitiated created by these revisions and the new reporting requirements for certain taxpayers who previously may not have been required to file this form.

## Background

The Report of Foreign Bank and Financial Accounts (FBAR) originated with the Bank Secrecy Act (BSA) enacted in 1970.<sup>1</sup> The U.S. government was concerned that U.S. persons were using certain foreign banks to hide proceeds from illegal activities, to evade U.S. federal taxes, and for other non-tax evasion purposes. Under the BSA<sup>2</sup> Treasury developed new forms as law enforcement tools to track the movement of cash and to improve enforcement against certain nonfilers. Financial institutions and individuals are required to file these forms, including the FBAR.

The FBAR is a law enforcement tool administered by the IRS. The Financial Crimes Enforcement Network (FinCen) discloses information reported on the FBAR to international, national, and local law enforcement agencies as provided under U.S.C. title 31. The FBAR is not a tax return and is not covered under the confidentiality provisions of title 26. Since 1992, the IRS has been responsible for the investigation of certain aspects of compliance with respect to FBAR reporting.<sup>3</sup> The civil enforcement of FBAR violations was the responsibility of FinCen.<sup>4</sup> FinCen's "mission is to enhance U.S. national security, deter and detect criminal activity, and safeguard financial systems from abuse by promoting transparency in the U.S. and international financial systems."<sup>5</sup> FinCen delegated its authority to the IRS in 2003.<sup>6</sup>

## The Revised FBAR Form

The revised FBAR form increased in scope from two to five reporting sections that may apply to the taxpayer. The form

continues to report the foreign bank and financial account (accounts held outside the United States) information on a calendar-year basis, regardless of the filer's tax year end. The FBAR is not filed with the taxpayer's U.S. federal income tax return and is due on June 30 of the succeeding calendar year. It is filed with the Department of Treasury in Detroit regardless of where the taxpayer files its U.S. federal income tax return. No extension of time to file this form is permitted, even if the taxpayer has an extension to file its U.S. federal income tax return.

As with the previous version of FBAR, Part I includes information about the filer, including the type of entity. Revised Parts II-V separate each type of account. Instead of indicating the account's value as within a range, such as between \$10,000 and \$99,999, the taxpayer should list the maximum account value in U.S. dollars of monetary and nonmonetary assets held during the year. The taxpayer should convert foreign currencies to U.S. dollars by using an official year-end exchange

1 12 U.S.C. Sections 1951-1959 and 31 U.S.C. Sections 5311-5330.

2 BSA §5314.

3 Treasury Directive 15-41 (12/1/92).

4 31 C.F.R. §103.56(b).

5 Financial Crimes Enforcement Network, [www.fincen.gov](http://www.fincen.gov), November 23, 2008.

6 IR-2003-48 (4/10/03).

rate. The FBAR instructions provide guidance for valuations of other assets required to be reported.<sup>7</sup> For example, the value of stock, other securities, or other nonmonetary assets in an account reported on TD F 90-22.1 is the fair market value at the end of the calendar year or, if withdrawn from the account, at the time of the withdrawal.

Part II reports information on financial account(s) owned separately. Part III covers information for financial accounts held in joint ownership. Part IV specifies where the filer has signature or other authority but no financial interest. Finally, Part V reports where the corporate filer is filing a consolidated report, i.e., where the corporation directly or indirectly owns more than a 50% interest in one or more other entities subject to FBAR reporting. In addition, there is now a box to check if the taxpayer is filing an amended FBAR.

## Penalties

On June 17, 2008, the IRS issued a news release to remind taxpayers of the FBAR reporting requirements and to emphasize the severity of the penalties for failure to file the FBAR.<sup>8</sup> The IRS indicated that

[c]ivil penalties for a non-willful violation can range up to \$10,000 per violation. Civil penalties for a willful violation can range up to the greater of \$100,000 or 50 percent of the amount in the account at the time of the violation. Criminal penalties for violating the FBAR requirements while also violating certain other laws can range up to a \$500,000 fine or 10 years imprisonment or both. Civil and criminal penalties may be imposed together.

The revised form provides that “[c]ivil and criminal penalties, including in cer-

tain circumstances a fine of not more than \$500,000 and imprisonment of not more than five years, are provided for failure to file a report, supply information, and for filing a false or fraudulent report.”<sup>9</sup>

## FBAR Filing Requirements

The FBAR filing requirements apply to “[e]ach United States person who has a financial interest in or signature or other authority over any foreign financial accounts, including bank, securities, or other types of financial accounts, in a foreign country, if the aggregate value of these financial accounts exceeds \$10,000 at any time during the calendar year.”<sup>10</sup> The BSA regulations define a person as “an individual, a corporation, a partnership, a trust or estate, a joint stock company, an association, a syndicate, joint venture, or other unincorporated organization or group, an Indian Tribe (as that term is defined in the Indian Gaming Regulatory Act), and all entities cognizable as legal personalities.”<sup>11</sup> The FBAR instructions define a U.S. person as “a citizen or resident of the United States, or a person in and doing business in the United States.”<sup>12</sup> Accordingly, an officer or an employee of a U.S. corporation, subject to certain exceptions, may be subject to a duplicate FBAR filing requirement, discussed in further detail below.

Nonresident aliens are not required to file an FBAR. However, an individual who otherwise meets the definition of a nonresident alien must be careful to avoid being classified as a resident alien under the substantial presence test of Sec. 7701(b)(3) and thus subject to the FBAR filing requirements (and related severe penalties for failure to comply).<sup>13</sup>

The BSA regulations define United States as “the states of the United States, the District of Columbia, the Indian lands

(as that term is defined in the Indian Gaming Regulatory Act), and the Territories and Insular Possessions of the United States.”<sup>14</sup> The revised FBAR instructions specify that a foreign subsidiary of a U.S. person (as defined above) is not subject to the FBAR; however, its U.S. parent corporation may be.<sup>15</sup> An important reporting change now requires a foreign entity that is doing business in the United States to file the FBAR even if it is not incorporated under U.S. law.<sup>16</sup> The foreign entity should report its foreign identification number if it does not have a U.S. identification number.<sup>17</sup>

## Exceptions to Reporting

An officer or employee of a U.S. corporation, if its equity securities are listed on any U.S. national securities exchange, or if the corporation has assets exceeding \$10 million and has 500 or more shareholders of record, is not required to file the FBAR concerning such individual’s signature or other authority over a foreign financial account of such corporation. However, the individual must not have any personal financial interest in such account and must also have been advised in writing by the chief financial officer or similar responsible officer of the corporation that the corporation has filed a current-year report that includes that account. If the corporation does not notify the individual in writing as discussed above, the individual would be subject to FBAR reporting as well.<sup>18</sup>

An officer or employee of a subsidiary of a U.S. corporation should not be considered to have signature or other authority over the foreign financial account if the U.S. parent corporation satisfies all the above requirements. In addition, the individual must not have any personal financial interest in the account and must have

7 Form TD F 90-22.1, instructions (rev. October 2008), part II, item 15, p. 7.

8 IR-2008-79 (6/17/08), describing the penalties that can be imposed under 31 U.S.C. Sections 5321 and 5322.

9 Form TD F 90-22.1 (rev. October 2008).

10 Form TD F 90-22.1, instructions (rev. October 2008), p. 6.

11 31 C.F.R. §103.11(z).

12 Form TD F 90-22.1, instructions (rev. October 2008), p. 6.

13 Sec. 7701(b)(3) provides that an individual meets the substantial presence test for any calendar (current) year if: (1) he or she was physically present in the United States on at least 31 days during the current year and (2) the

sum of the days he or she was physically present in the United States during the current year, plus one-third the number of days he or she was physically present in the United States during the first preceding calendar year, plus one-sixth the number of days he or she was physically present in the United States during the second preceding year equals or exceeds 183 days.

14 31 C.F.R. §103.11(nn).

15 Form TD F 90-22.1, instructions (rev. October 2008), p. 6.

16 Id.

17 Form TD F 90-22.1, question 4.

18 Form TD F 90-22.1, instructions (rev. October 2008), p. 6.

been notified in writing by the responsible officer of the parent corporation that the subsidiary has filed the FBAR for the current year that includes the account. If a subsidiary of a U.S. corporation is identified in a consolidated FBAR (discussed above) of the U.S. parent corporation, the subsidiary will be deemed to have filed the FBAR for purposes of the exception enumerated above. Finally, an officer or employee of a foreign subsidiary company that is more than 50% owned by a U.S. corporation would be subject to the same reporting exceptions as discussed above.

## Financial Interest

The instructions for the new FBAR form provide guidance as to what constitutes a financial interest in an account. “A United States person has a financial interest in each account for which such person is the owner of record or has legal title, whether the account is maintained for his or her own benefit or for the benefit of others including non–United States persons.”<sup>19</sup> A U.S. person may also have to file an FBAR if it has an indirect financial interest in a foreign account through ownership of an entity owning a foreign account. This includes accounts owned by:

- A corporation in which a U.S. person owns, directly or indirectly, more than 50% of the total value of shares of stock;
- A partnership in which the U.S. person owns an interest in more than 50% of the profits; or
- A trust in which the U.S. person has a present beneficial interest in more than 50% of the assets or from which the person receives more than 50% of the current income.<sup>20</sup>

In addition, a U.S. person will now have an interest in a financial account if the trust that owns the interest is a trust protector.<sup>21</sup> “A trust protector is a person who is responsible for monitoring the activities of a trustee, with the authority to influence the decisions of the trustee or to replace, or recommend the replacement of, the trustee.”<sup>22</sup>

## Financial Account

The term “financial account” includes “any bank, securities, securities derivatives or other financial instruments accounts.”<sup>23</sup> This would also include any checking account or deposit account, and the term is now extended to debit card and prepaid credit card accounts “maintained with a financial institution or other person engaged in the business of a financial institution.”<sup>24</sup>

## Summary

To avoid severe penalties for noncompliance, practitioners and taxpayers need to carefully examine these reporting requirements. Local IRS enforcement activity increased under Delegation Order 4-35 issued on March 24, 2008, which delegated certain responsibilities to IRS field offices concerning FBAR compliance.

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## EditorNotes

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<sup>19</sup> Id.

<sup>20</sup> Id.

<sup>21</sup> Id.

<sup>22</sup> Id.

<sup>23</sup> Id.

<sup>24</sup> Id.