



IRS Guidance To Cap Potential FBAR Penalties

On May 13, 2015, the IRS issued guidance which establishes limits to the potential penalties that the IRS will assert for a taxpayer's failure to file Foreign Bank Account Reports (FBARs). The guidance is designed to promote consistency by the IRS in administering its FBAR compliance program. The clarification of the maximum penalty amounts that the IRS expects to assess in normal circumstances should ease taxpayers' concerns about being penalized amounts far greater than the value of their accounts, and will help guide taxpayers and their advisers in weighing the benefits of various IRS programs in order to resolve any delinquent reporting of offshore accounts.

Foreign Bank Account Reporting

A United States person who has a financial interest in or signature authority over foreign financial accounts must file an FBAR if the aggregate value of the foreign financial accounts exceeds \$10,000 at any time during the calendar year. The FBAR is an annual report that must be electronically filed with the Department of Treasury on or before June 30 of the year following the calendar year being reported. There is no extension of time to file an FBAR.

FBAR Penalties

Civil penalties for failing to file an FBAR can be significant. The IRS can impose a \$10,000 penalty for each non-willful violation of the FBAR filing requirement. Where a person willfully fails to file an FBAR, the IRS may impose a penalty equal to the greater of \$100,000 or 50 percent of the account's highest balance. In addition, criminal penalties for a willful failure to file can reach \$250,000, 5 years in prison or both. Civil and criminal FBAR penalties may be imposed together. Generally, as a matter of law, the IRS has six years to assert an FBAR penalty.

Penalty Concerns

In the past, the IRS has not been uniform in applying the FBAR penalty. In some cases, the IRS has aggressively asserted FBAR penalties over multiple years whether the taxpayer was willful or not in failing to file an FBAR. The IRS has even taken the position that the \$10,000 non-willful penalty should apply per account in each year rather than being limited to a one-time \$10,000 penalty per FBAR in each year. The clear concern for taxpayers is that the IRS's aggressive approach could result in the assertion of multiple penalties over several years which could lead to penalty amounts that far exceed the value of the account. This aggressive IRS position can be seen in cases like *U.S. v. Zwerner*, S.D. Fla., No. 1:13-cv-22082, 5/28/14. In *Zwerner*, the taxpayer was found to have willfully failed to file FBARs for three out of the four years asserted by the government and the Court sustained the IRS's position of asserting the maximum 50 percent penalty over several years. The government's victory in *Zwerner* indicated to taxpayers that the IRS will increasingly look to assert multiple 50 percent willful FBAR penalties whenever it could.

New Guidance Procedures

The May 13, 2015, guidance issued by the IRS should ease taxpayers' concerns that the IRS will look to penalize taxpayers far in excess of the value of their unreported accounts. The guidance instructs IRS employees to take into account all available facts and circumstances and to use their best judgment in determining if an FBAR violation occurred, and, if so, the appropriate penalty amount. For any asserted willful FBAR penalty, the IRS agent is obligated to fully develop and adequately document the reason for a willfulness claim. Any case involving an FBAR penalty must be reviewed by an IRS FBAR coordinator. IRS Chief Counsel will now review FBAR penalty recommendations only when the conduct is charged as willful, and will limit its legal advice to whether an FBAR violation occurred, whether the violation was willful, and whether the proposed penalty is within the statutory limitations. The final determination regarding assertion (or not) of an FBAR penalty is made by the group manager.

Generally, a willful penalty will not be higher than 50 percent of the highest aggregate balance of all unreported foreign financial accounts during the years under examination. This means that the penalty will be allocated among multiple years based on account balances. Importantly, although the guidance permits agents to recommend penalty amounts either higher or lower than 50 percent based upon the applicable facts, "in no event will the total penalty amount exceed 100 percent" of the highest aggregate account balances. This clarification removes the possibility of a taxpayer owing more than his/her account was ever worth.

According to the IRS guidance, a non-willful penalty will not be recommended if a taxpayer has reasonable cause for the reporting failure and subsequently filed complete and correct FBARs. A non-willful penalty will only be asserted as one penalty for each year of violation (no matter how many unreported offshore accounts the taxpayer held in a single year). The non-willful penalty is limited to \$10,000, and may be less depending upon the aggregate balance of all the unreported accounts per year. Only in extreme cases will the IRS assert a separate non-willful penalty for each account in a particular year. Regardless, "in no event will the total amount of the penalties for nonwillful violations exceed 50 percent of the highest aggregate balance of all unreported foreign financial accounts for the years under examination."

Unreported foreign accounts with multiple owners require the IRS to make a separate determination regarding any violation with respect to each co-owner. Penalties arising from co-owned accounts will be made based on percentage ownership of the highest balance of the account.

The IRS guidance is effective immediately for all open FBAR examinations. The application of these administrative instructions is best analyzed on a case-by-case basis by a professional tax advisor taking the taxpayer's particular factual situation into account.

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