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DEVELOPMENTS IN OFFSHORE TAX COMPLIANCE: PRACTITIONER VIEW

Andrew H. **Weinstein**
Holland & Knight LLP
Miami, Florida

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I. Voluntary Disclosure
a) Internal Revenue Manual —IRM 9.5.11.9.
b) Department of Justice Manual — DOJ — CTM §4.01 [2]; 6-4.000.
c) IRS Offshore Income Reporting Initiative
i. 57 DTR GG — 1 -(3/26/09 announcement).
ii. IRS SBSE, LMSB Memorandum regarding Development of Offshore Examination Cases, et al. (3/23/09).
iii. IRS SBSE, LMSB Memorandum on Routing of Voluntary Disclosure Cases (3/23/09).
iv. IRS Deputy Commissioner Memorandum on Authorization to Apply Penalty Framework to Voluntary Disclosure Requests Regarding Unreported Offshore Accounts, Entities (3/23/09).
v. IRS Deputy Commissioner Shulman Statement (3/26/09).
vi. 71 DTR G-4 IRS offers guidance on How to Voluntarily Disclose Offshore Assets Under New Program (telephone contacts); IRS website (IRS.gov/compliance/enforcement/article/O, id = 205909.00.html (4/16/09).
vii. Frequently asked questions
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• Practitioner hotline # (215) 516-4777.
(3) Criminal Investigation-Offshore Voluntary Disclosures-Optional Format for Submission to IRS (IRS Website).
viii. Staff Report, Joint Committee on Taxation, Tax Compliance and Enforcement Issues With Respect to Offshore Accounts and Entities. (3/30/09, JCX-23-09).
ix. Criminal Investigation Preliminary Approval Letter
d) Federal Sentencing Guidelines, Departures, Sec 5K2.16, Voluntary Disclosure of Offense (Policy Statement).
e) GAO Report on Penalties and Voluntary Compliance, 127 DTR G-4 (7/7/09).
f) Treasury Report-Update on Reducing the Federal Tax Gap and Improving Voluntary Compliance (BNA DTR, 7/9/09).
g) TEP Meeting Materials, August 13, 2009
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a) TDF 90-22.1 (10/08).
b) CCA 200603026 (willfulness standard).
c) IRM Examining Process.
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ii. 4.26.16 (Reports)
iii. 4.26.17 Reports/Procedures).
d) FBAR — Foreign Bank Account Reporting: Obligations: A Primer for the Practitioner (J. Tax, Jan. 2007).
e) Update on FBAR Developments — New Enforcements Efforts Likely (J. Tax, May 2007).
f) Significant New FBAR Developments from IRS and the Tax Court (J. Tax, Nov. 2008).
g) FBAR Questions SB/SE Counsel Approved 10/22/07 (phone forum).
i. Updates to General Filing Requirements, Definition of Financial Account and of US Person (IRS Website, 7/14/09).
h) FBAR PowerPoint.
i) Comments of Bernard Vischer, Esq. re: Swiss situation as of April, 2009.
j) Comments on Swiss law by Markus Zwicky, Esq. as of April, 2009.
k) Ethical Issues
i. ABA Standards of Tax Practice on Sec. 10.22 of C. 230 (May, 2009).
ii. ABA Standards of Tax Practice on Model Rules of Professional Conduct (May 2009).
l) Privileges, Sec. 7525, Work Product, ABA Survey, J.D. August ABA Standards of Tax Practice (May, 2009).
m) Boulware and Sec. 301, 2009 TNT 94-11 (5/18/09).
n) OPR Statement on Practitioner Responsibilities and FBAR (OPR Website, 6/5/09).
o) Fifth Amendment FBAR. See Michel, Advising a Client With Secret Offshore Accounts-Current Filing and Reporting Problems, J. Tax., Sept. 2009.
p) FBAR Resources (Research Links), Journal of Accountancy (6/25/09).
q) NYSBA Members Seek Guidance on FBAR Filing Requirements (2009 TNT 137-13 (7/21/09).
r) Extended Filing Date re: Signature Authority and re: Foreign Commingled Funds

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a) 18 USC Sec. 981 — Civil forfeiture of funds used in "specified unlawful activities." Civil seizure and forfeiture powers under 18 USC Sec. 981 available to IRS — use of postal service or of electronic fraud means to file a fraudulent return gives rise to mail, wire or bank fraud (specified unlawful activities).
b) 18 USC Sec. 1956 — Specified unlawful activities listed.
c) 18 USC Sec. 1957 — Criminal offenses involving specified unlawful activities.
d) 18 USC Sec. 982 — Criminal forfeiture incident to conviction of offenses in violation of 18 USC Sec. 1956.
e) Senate Bill 386 to apply the International Money Laundering Statute to tax evasion amends 18 USC Sec. 1956 (A)(2) [transportation money laundering] so that any transportation of funds into or out of the U.S. for the purpose of evading U.S. tax is a money laundering offense [a 20 year felony and civil or criminal forfeiture of the entire amount, plus a fine]. Note: taxes are still due, too.
f) BNA 94 DTR G-2 — international tax evasion struck from Senate bill to conform to House version.
g) ABA Tax Section Committee on Civil and Criminal penalties letter dated May, 2009 opposing inclusion of international tax evasion as a money laundering offense. 52 DTR G-7.
i. 26 USC Sec. 7321 - power to seize assets that may be forfeitable pursuant to any provision of the Code.
(1) 26 USC Sec. 7301 — property intended to be sold, removed, concealed or deposited to defraud the U.S. of tax or to avoid payment of tax.
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h) U.S. v. Greenstein, Indictment (BNA 6/8/09) re: wire fraud, money laundering and forfeiture in addition to tax

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evasion indictment.
i) U.S. v. Madoff, Order of Forfeiture, 6/26/09 (BNA DTR 6/30/09).
j) U.S. v. Daugerdas, Superseding Indictment (6/23/09).
k) USAM 6-4.210 (Wire Fraud in Tax-Related Prosecutions)
i. Tax Division Directive No. 128 (10/29/04)
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b) Primer, Steven M. Harris, BNA Doc. 2005-4011, Tax Notes Vol. 106, No. 10 (3/7/05)
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a) Rubinger & Weinstein, Tax Notes (6/6/05).
b) Power Point.
VI. Complex International IDR's
a) IRS Strategic Plan.
b) IRS Form 4564.
c) IRS Interview Questions.
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IRS Voluntary Disclosure Practice, Tax Crimes-General, IRM 9.5.11.9

Related Terms

Topics:
Tax Reporting

IRS Voluntary Disclosure Practice

TAX CRIMES — GENERAL

IRM 9.5.11.9

Voluntary Disclosure Practice

(1) It is currently the practice of the IRS that a voluntary disclosure will be considered along with all other factors in the investigation in determining whether criminal prosecution will be recommended. This voluntary disclosure practice creates no substantive or procedural rights for taxpayers, but rather is a matter of internal IRS practice, provided solely for guidance to IRS personnel. Taxpayers cannot rely on the fact that other similarly situated taxpayers may not have been recommended for criminal prosecution.
(2) A voluntary disclosure will not automatically guarantee immunity from prosecution; however, a voluntary disclosure may result in prosecution not being recommended. This practice does not apply to taxpayers with illegal source income.
(3) A voluntary disclosure occurs when the communication is truthful, timely, complete, and when:
a. the taxpayer shows a willingness to cooperate (and does in fact cooperate) with the IRS in determining his or her

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correct tax liability; and

b. the taxpayer makes good faith arrangements with the IRS to pay in full, the tax, interest, and any penalties determined by the IRS to be applicable.

(4) A disclosure is timely if it is received before:

a. the IRS has initiated a civil examination or criminal investigation of the taxpayer, or has notified the taxpayer that it intends to commence such an examination or investigation;

b. the IRS has received information from a third party (e.g., informant, other governmental agency, or the media) alerting the IRS to the specific taxpayer's noncompliance;

c. the IRS has initiated a civil examination or criminal investigation which is directly related to the specific liability of the taxpayer; or

d. the IRS has acquired information directly related to the specific liability of the taxpayer from a criminal enforcement action (e.g., search warrant, grand jury subpoena).

(5) Any taxpayer who contacts the IRS in person or through a representative regarding voluntary disclosure will be directed to Criminal Investigation for evaluation of the disclosure. Special agents are encouraged to consult Area Counsel, Criminal Tax on voluntary disclosure issues.

(6) Examples of voluntary disclosures include:

a. a letter from an attorney which encloses amended returns from a client which are complete and accurate (reporting legal source income omitted from the original returns), which offers to pay the tax, interest, and any penalties determined by the IRS to be applicable in full and which meets the timeliness standard set forth above. This is a voluntary disclosure because all elements of (3), above are met.

b. a disclosure made by a taxpayer of omitted income facilitated through a barter exchange after the IRS has announced that it has begun a civil compliance project targeting barter exchanges; however the IRS has not yet commenced an examination or investigation of the taxpayer or notified the taxpayer of its intention to do so. In addition, the taxpayer files complete and accurate amended returns and makes arrangements with the IRS to pay in full, the tax, interest, and any penalties determined by the IRS to be applicable. This is a voluntary disclosure because the civil compliance project involving barter exchanges does not yet directly relate to the specific liability of the taxpayer and because all other elements of (3), above are met

c. a disclosure made by a taxpayer of omitted income facilitated through a widely promoted scheme regarding which the IRS has begun a civil compliance project and already obtained information which might lead to an examination of the taxpayer; however, the IRS has not yet commenced an examination or investigation of the taxpayer or notified the taxpayer of its intent to do so. In addition, the taxpayer files complete and accurate returns and makes arrangements with the IRS to pay in full, the tax, interest, and any penalties determined by the IRS to be applicable. This is a voluntary disclosure because the civil compliance project involving the scheme does not yet directly relate to the specific liability of the taxpayer and because all other elements of (3), above are met.

d. A disclosure made by an individual who has not filed tax returns after the individual has received a notice stating that the IRS has no record of receiving a return for a particular year and inquiring into whether the taxpayer filed a return for that year. The individual files complete and accurate returns and makes arrangements with the IRS to pay the tax, interest, and any penalties determined by the IRS to be applicable in full. This is a voluntary disclosure because the IRS has not yet commenced an examination or investigation of the taxpayer or notified the taxpayer of its intent to do so and because all other elements of (3), above, are met.

(7) Examples of what are not voluntary disclosures include:

a. a letter from an attorney stating his or her client, who wishes to remain anonymous, wants to resolve his or her tax liability. This is not a voluntary disclosure until the identity of the taxpayer is disclosed and all other elements of (3) above have been met.

b. a disclosure made by a taxpayer who is under grand jury investigation. This is not a voluntary disclosure because the

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taxpayer is already under criminal investigation. The conclusion would be the same whether or not the taxpayer knew of the grand jury investigation.

c. a disclosure made by a taxpayer, who is not currently under examination or investigation, of omitted gross receipts from a partnership, but whose partner is already under investigation for omitted income skimmed from the partnership. This is not a voluntary disclosure because the IRS has already initiated an investigation which is directly related to the specific liability of this taxpayer. The conclusion would be the same whether or not the taxpayer knew of the ongoing investigation.

d. a disclosure made by a taxpayer, who is not currently under examination or investigation, of omitted constructive dividends received from a corporation which is currently under examination. This is not a voluntary disclosure because the IRS has already initiated an examination which is directly related to the specific liability of this taxpayer. The conclusion would be the same whether or not the taxpayer knew of the ongoing examination.

e. a disclosure made by a taxpayer after an employee has contacted the IRS regarding the taxpayer's double set of books. This is not a voluntary disclosure even if no examination or investigation has yet commenced because the IRS has already been informed by the third party of the specific taxpayer's noncompliance. The conclusion would be the same whether or not the taxpayer knew of the informant's contact with the IRS.

4.01 **VOLUNTARY DISCLOSURE**

4.01[1] **Policy Respecting Voluntary Disclosure**

Prior to 1952, it was the policy of the Treasury Department not to recommend criminal prosecution where a taxpayer voluntarily revealed his commission of a tax crime to an appropriate IRS official before any investigation of his affairs had commenced.

Due to the controversy which ensued in the courts over what constituted a true "voluntary disclosure," and because it was difficult, "and sometimes impossible" to ascertain administratively whether the taxpayer had made a voluntary disclosure or had merely discovered he was under investigation, the Treasury Department abandoned this policy on January 10, 1952. Treasury Department Information Release No. S-2930; 1952 C.C.H., ¶ 6079. *See United States v. Shotwell Manufacturing Co*., 355 U.S. 233, 235 n.2 (1957).

In 1961, the Internal Revenue Service adopted an "informal" policy regarding voluntary disclosure, under which it considered voluntary disclosure, along with other facts and circumstances, on a case-by-case basis in determining whether or not to recommend prosecution. *See* Statement of Commissioner Mortimer M. Caplin, News Release IR-432, Dec. 13, 1961; IRM Part IX, §9781- 342.14 and CCDM Part (31)134.

In December 1992, the IRS clarified, but did not change, its "informal" policy, noting that, in the past, it had not generally recommended prosecution if the taxpayer:

1. Informed the IRS of the failure to file for one or more taxable years;
2. Had only legal source income;
3. Made the disclosure prior to being contacted by the IRS in the form of a telephone call, letter, or personal visit informing the taxpayer that he is under criminal investigation;
4. Filed a true and correct tax return or cooperated with the IRS in ascertaining his correct tax liability; and
5. Made full payment of amounts due, or in those situations where the taxpayer was unable to make full payment, made bona fide arrangements to pay.

"Peterson [IRS Commissioner Shirley D. Peterson] Formalizes Practice of Not Prosecuting Non-Filers Who Come Forward." BNA Daily Tax Report (Dec. 7, 1992). *See United States v. Knottnerus*, 139 F.3d 558, 559-560 (7th Cir. 1998) (holding that prior visit by special agent disqualified defendant from voluntary disclosure program).

However, the 1992 clarification by the Service created confusion as to the application of the voluntary disclosure policy with respect to nonfilers.

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See United States v. Tenzer, 127 F.3d 222, 226-28 (2d Cir. 1997), *vacated in part and remanded on other grounds*, 213 F.3d 34, 40-41 (2d Cir. 2000). Thus, in 1995, the Service reinstated its former voluntary disclosure practice, eliminated the language relative to nonfilers, and modified the triggering event example.

Currently, the Service's voluntary disclosure practice is that a voluntary disclosure will be considered along with all other factors in a case in determining whether criminal prosecution will be recommended. Under the Service's practice, a voluntary disclosure occurs when the communication is: (1)truthful; (2) timely; (3) complete; and (4) the taxpayer shows a willingness to cooperate, and, in fact cooperates, with the Service in determining his or her tax liability. A disclosure is timely if received before: (1) the Service has initiated an inquiry that is likely to lead to the taxpayer and the taxpayer is reasonably thought to be aware of that activity; or (2) some event known by the taxpayer occurred which event is likely to cause an audit into the taxpayer's liabilities. The Service tests voluntariness by the following factors: (1) actual status of the Service's awareness of the taxpayer as to specific tax investigation potential; (2) taxpayer's knowledge or awareness of the Service's interest; and (3) taxpayer's fear of a “trigger” or “potential trigger” to make the Service aware of violations (where the disclosure is ‘triggered’ by an event which would have led the Service to the fraud, the disclosure is not considered to be voluntary). *See* United States v. Knottnerus, 139 F.3d at 559-560; United States v. Tenzer, 127 F.3d at 226-228.

At present, the Department of Justice continues to give consideration to a “voluntary disclosure” on a case-by-case basis in determining whether to prosecute but such disclosure is not conclusive on the issue. *See* United States v. Hebel, 668 F.2d 995 (8th Cir. 1982). Specifically, the Tax Division considers the timeliness of the disclosure and whether the taxpayer fully cooperated with the Government in deciding whether a disclosure was voluntary.

4.01[2] **Timeliness of Disclosure**

There are two elements to a voluntary disclosure: (1) it must be made timely and (2) the taxpayer must thereafter fully cooperate with the government. There has been considerable debate among practitioners as to the meaning of “timely.” Some argue that the test for timeliness should be strictly objective, hat is, a disclosure is timely if the disclosure is made before the taxpayer's return is selected by the Internal Revenue Service for audit regardless of the taxpayer's motivation for making the disclosure. Under this approach, a disclosure would not be timely if the return had been selected for audit, even if the taxpayer did not know that the return had already been selected for audit at the time of the disclosure.

The objective test does have simplicity of application in its favor. On the other hand, if all of the circumstances are considered, then whether or not a return has been selected for audit at the time of disclosure is not necessarily conclusive. For example, if the disclosure followed closely upon an IRS inquiry directed to a third party which reasonably could be anticipated to lead to selection of the taxpayer's return for audit, then the disclosure reasonably could be described as “triggered,” rather than as “voluntary.”

Although not yet subject to audit, the taxpayer was obviously attempting to place himself or herself in the best light possible after concluding that an audit was inevitable.

United States v. McCormick, 67 F.2d 867, 868 (2d Cir. 1933).

Conversely, if the taxpayer was in fact clearly unaware that his or her return had been selected for audit at the time of the disclosure and “triggering” circumstances are absent, then seemingly consideration should be given for having come forward voluntarily. *Cf.* United States v. Levy, 99 F. Supp. 529, 533 (D.Conn. 1951). Similarly, there may be situations where an audit is already in progress, and the taxpayer discloses a transaction that almost certainly would not have been found by the auditing agent. On a strictly objective test, the disclosure of the unknown transaction would not be a “timely disclosure” since the return was under audit.

Because the objective test is essentially arbitrary, the Department has rejected it, and, instead, favors an “all events” test in assessing whether a disclosure was timely. That is, a disclosure is not timely if:

1. The IRS has already initiated an inquiry that is likely to lead to the taxpayer and the taxpayer is reasonably thought

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to be aware of that activity; or

2. Some event occurred before the disclosure which the taxpayer probably knew about and which event is likely to cause an audit into the taxpayer's liabilities, e.g., a newspaper article high-lighting commercial bribery in a particular industry or corruption in a governmental office. *Cf.* *United States v. McCormick*, 67 F.2d 867 (2d Cir. 1933).

4.01[3] **Cooperation of Taxpayer**

If it is concluded that the disclosure was timely, a second point of inquiry is whether the taxpayer has fully cooperated with the IRS in ascertaining and paying the taxes owed. Thus, the Department's position on cooperation is that the taxpayer must make a full disclosure of all facts and cooperate with the Service in determining the proper amount of taxes owed. If the taxes are not paid because of a claim of inability to pay, then full and accurate disclosure must be made by the taxpayer of his financial position.

At bottom, application of the "voluntary disclosure" policy is an exercise of prosecutorial discretion that does not, and legally could not, confer any legal rights on taxpayers. Whether there is or is not a voluntary disclosure is only a factor in evaluating a case, and even if there has been a voluntary disclosure, prosecution and conviction may still result. In short, a voluntary disclosure is not a bar to prosecution, but merely a factor to be considered.

See *United States v. Hebel*, 668 F.2d 995 (8th Cir. 1982).

See February 17, 1993, Tax Division memorandum on *Tax Division Voluntary Disclosure Policy* from Acting Assistant Attorney General James A. Bruton, Tax Division. A copy of this memorandum is contained in Section 3.00 of this *Manual*.

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6-4.010 Federal Criminal Tax Enforcement

The Government helps to preserve the integrity of this Nation's self-assessment tax system through vigorous and uniform criminal enforcement of the internal revenue laws. Criminal prosecutions punish tax law violators and deter other persons who would violate those laws. To achieve maximum deterrence, the Government must pursue broad, balanced, and uniform criminal tax enforcement. Uniformity in tax cases is necessary because tax enforcement potentially affects more individuals than any other area of criminal enforcement. Broad and balanced enforcement is essential to effectively deter persons of varying economic and vocational status, violators in different geographic areas, and different types of tax law violations.

To achieve uniform, broad, and balanced criminal tax enforcement, the Attorney General has authorized the Tax Division to oversee all federal criminal tax enforcement and to authorize or decline investigations and prosecutions in tax matters. *See* USAM 6-4.200. For a map reflecting the geographical assignments of the Tax Division Criminal Enforcement Sections, see Tax Resource Manual 1. For contact information, including mailing addresses and telephone and fax numbers, see Tax Resource Manual 2.

[updated September 2007] [cited in USAM 6-4.211]

6-4.011 Criminal Tax Manual and Other Tax Division Publications

The Tax Division's Criminal Tax Manual (2001) contains comprehensive discussions of statutes, methods of proof, various specialized areas, and policies and procedures pertaining to criminal tax prosecutions. The Manual also contains indictment and information forms and jury instructions. All prosecutors involved in federal criminal tax cases should consult the Manual for guidance on handling criminal tax cases. The Criminal Tax Manual may be accessed in at http://www.usdoj.gov/tax/readingroom/foia/tax.htm. The Tax Division also compiles other resources useful in criminal tax prosecutions. Should those resources conflict with this Title of the USAM, this Title of the USAM controls.

[updated September 2007]

6-4.110 IRS Administrative Investigations

The special agents of IRS Criminal Investigation conduct the administrative investigations into allegations of criminal

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violations arising under the internal revenue laws and related provisions of Title 18, U.S.C. (*e.g.*, 18 U.S.C. §§ 286, 287, 371, 1341). *See* Tax Resource Manual 5 and 6.

After an administrative investigation is completed, the special agent must prepare a special agent's report (SAR), together with exhibits, in order to recommend that the Government prosecute the matter. The SAR contains a detailed account of the investigation and the special agent's recommendations, and is reviewed by both the special agent's supervisors and the Chief Counsel, Criminal Tax Division (CT). CT then prepares a Criminal Enforcement Memorandum (CEM) that discusses the nature of the crime(s) for which the agent recommends prosecution, the evidence relied upon to prove the crime(s), technical or legal issues, anticipated difficulties in prosecution, and the special agent's specific recommendation. Thereafter, if CI concludes that the Government should prosecute the matter, the CI Special Agent-in-Charge (SAC) refers the matter to the Tax Division or, in some cases, the United States Attorney. *See* USAM 6-4.243. When the IRS directly refers a matter to the United States Attorney, it simultaneously forwards a copy of the transmittal letter to the Tax Division.

During an administrative investigation of a criminal tax case, the IRS may refer the case directly and simultaneously to both the United States Attorney and the Tax Division for an expedited guilty plea, if only legal source income is involved (*i.e.*, neither narcotics nor organized crime), and the taxpayer's counsel states that the taxpayer wishes to enter such a guilty plea. The plea must be consistent with the Tax Division's major count policy. *See* Tax Resource Manual 7.

When the IRS refers a criminal matter to the Department of Justice, it may share returns or return information with the Department of Justice (*see* 26 U.S.C. § 6103(h)(2)). Once a criminal referral is made, the IRS, including CI, may not issue or commence an action to enforce an administrative summons with respect to the taxpayer for the same tax and the same taxable period. *See* 26 U.S.C. § 7602(d), Tax Resource Manual 8.

[updated September 2007]

6-4.120 Grand Jury Investigations—Generally

Although a federal grand jury is empowered to investigate both tax and non-tax violations of federal criminal laws, the Tax Division must first approve and authorize the United States Attorney's use of a grand jury to investigate criminal tax violations (*see* 28 C.F.R. § 0.70). The Tax Division has delegated to the United States Attorneys, however, the authority to approve grand jury investigations of certain false and fictitious claims for tax refunds in violation of 18 U.S.C. § 286 and 18 U.S.C. § 287 (other than those investigations involving a professional tax return preparer). *See* Tax Division Directive No. 96 (December 31, 1991), Tax Resource Manual 9.

[updated September 2007] [cited in USAM 6-2.000]

6-4.121 IRS Requests to Authorize Grand Jury Investigations

In addition to using administrative process to secure evidence in an investigation, CI also may request that the Tax Division authorize a grand jury investigation when CI either cannot complete its investigation or otherwise determines that it cannot feasibly gather evidence through the administrative process. The IRS's request to authorize a grand jury investigation constitutes a referral of the matter to the Department of Justice. Once a criminal referral is made, the IRS, including CI, may not issue or commence an action to enforce an administrative summons with respect to the taxpayer for the same tax and the same taxable period. *See* 26 U.S.C. § 7602(d).

[updated September 2007]

6-4.122 United States Attorney's Grand Jury Investigations and Prosecutions

A. Tax Division Referrals for Prosecution. The Tax Division authorizes the United States Attorney to conduct grand jury investigations into matters arising under the internal revenue laws to the extent necessary to perfect those

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tax charges that the Tax Division refers for prosecution.

B. Tax Division Referrals for Grand Jury Investigation. The Tax Division authorizes the United States Attorney to conduct grand jury investigations into matters arising under the internal revenue laws to the extent necessary to 1) perfect the tax charges for which the Tax Division authorizes an investigation or 2) determine whether the Tax Division should authorize prosecution. *See* USAM 6-4.242.

C. Expansion of Non-tax Grand Jury Investigation to Possible Federal Criminal Tax Violations. The Assistant Attorney General, Tax Division, has delegated limited authority to the United States Attorney to expand non-tax investigations in order to inquire into possible federal criminal tax violations, designate targets (subjects), determine the scope of the expanded investigation, and terminate such proceedings. Before a United States Attorney may file an information or seek the return of an indictment on matters arising under the internal revenue laws in an expanded investigation, however, the Tax Division must first authorize the specific tax charges. *See* Tax Division Directive No. 86-59 (October 1, 1986), Tax Resource Manual 10.

D. IRS Direct Referrals for Prosecution. In limited categories of cases, the Tax Division authorizes the IRS to refer certain matters arising under the internal revenue laws directly to the United States Attorney for prosecution. *See* USAM 6-4.243. In turn, the Tax Division authorizes the United States Attorney to conduct grand jury investigations into these matters, to the extent necessary to perfect the charges that the IRS has directly referred.

[updated September 2007] [cited in USAM 6-4.212]

6-4.123 Joint United States Attorney—IRS Request to Expand Tax Grand Jury Investigation

The United States Attorney may not, without Tax Division approval, expand grand jury investigations into matters arising under the internal revenue laws to include targets that the Tax Division did not previously authorize. The United States Attorney, together with the IRS, must submit a written request to obtain Tax Division approval. The request must establish the basis for the Tax Division to authorize expansion of the investigation. *See* USAM 6-4.211(B).

[updated September 2007] [cited in USAM 6-2.000; 6-4.212]

6-4.125 IRS Transmittal of United States Attorney's Recommendation, Special Agent's and Criminal Tax Counsel's Reports, and Exhibits from Grand Jury Investigation

When a grand jury investigation is complete and the United States Attorney concludes that the Government has gathered sufficient evidence to proceed with prosecution, the United States Attorney should request that the special agent assigned to the matter prepare a SAR. After the SAR is completed, the special agent should request that CT Counsel review the SAR and prepare a CEM. Then, the SAC must forward the SAR, with copies of the relevant exhibits, and the CEM to the Tax Division for review and authorization. At the same time, the United States Attorney or the SAC must forward to the Tax Division the United States Attorney's written recommendation regarding prosecution of a target(s) for tax violations. *See* USAM 6-4.200. Whenever possible, the Tax Division will complete its review of the prosecution recommendation within thirty (30) days of receiving the transmittal letter, reports, and exhibits. *See* USAM 6-4.242.

The IRS also must transmit a recommendation against prosecution resulting from a grand jury investigation to the Tax Division for evaluation. Alternatively, the IRS must advise the Tax Division that it has no recommendation. *See* IRM 9.5.14.12.2(3); *see also* USAM 6-4.242. The Tax Division will complete its evaluation of the matter and authorize declination or other actions within thirty (30) days of receiving the recommendation.

[updated September 2007] [cited in USAM 6-4.242]

6-4.126 Restriction on Disclosure of Grand Jury Matters to IRS for Civil Use

Federal Rule of Criminal Procedure 6(e)(3)(C)(i) prohibits the United States Attorney from disclosing "matters occur-

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ring before the grand jury" to the IRS for use in civil tax audit or administrative collection proceedings. *See United States v. Baggot*, 463 U.S. 476 (1983). The court may grant the Government's motion for disclosure of grand jury matters for use in certain civil proceedings, if the United States Attorney satisfies the exception requirements set forth in Rule 6(e)(3)(C)(i)(I), which require the Government to show that it will make the disclosure "preliminarily to or in connection with a judicial proceeding...." and that it has a "particularized need" for the requested materials. *See United States v. John Doe, Inc. I*, 481 U.S. 102, 108 (1987). Information that is not deemed to be "matters occurring before the grand jury" may be disclosed consistent with the requirements of 26 U.S.C. section 6103. *See* Tax Resource Manual 11.

[updated September 2007]

6-4.130 Search Warrants

The Assistant Attorney General, Tax Division, has delegated to the United States Attorney and other specified supervisory officials in United States Attorney's Offices the authority to approve search warrants in many matters arising under the internal revenue laws: a warrant directed at an office, structure, or premises of a target or subject of an investigation; a warrant directed to a provider of electronic communication services or remote computing services and relating to a subject or target of a criminal investigation; and a warrant directed to a disinterested third party owning a storage space business or similar business and relating to a subject or target of a criminal investigation. See Tax Division Directive No. 52 (modified March 17, 2008) and related documents in Tax Resource Manual 12 and 13. The United States Attorney must, however, submit a written request and obtain the approval of the Tax Division for any search warrant where the target or subject is reasonably believed to be

- an accountant
- a lawyer
- a physician
- a public official/political candidate
- a member of the clergy
- a news media representative
- a labor union official or
- an official of an organization exempt from tax under 26 U.S.C. § 501(c)(3)

Except as provided above, the United States Attorney must also submit a written request and obtain the approval of the Tax Division for any search warrant directed at an office, structure, or premises of a third party, i.e., a person who is not a target or subject of the investigation.

[updated April 2008]

6-4.200 Tax Division Jurisdiction and Procedures

The Assistant Attorney General, Tax Division, has responsibility for all criminal proceedings arising under the internal revenue laws, with the exception of proceedings that pertain to: misconduct of IRS personnel; taxes on liquor, narcotics, firearms, coin-operated gambling and amusement machines, and wagering; forcible rescue of seized property (26 U.S.C. § 7212(b)); corrupt or forcible interference with an officer or employee acting under the internal revenue laws (26 U.S.C. § 7212(a) (but not the "omnibus clause")); unauthorized disclosure of information (26 U.S.C. § 7213); and counterfeiting, mutilation, removal, or reuse of stamps (26 U.S.C. § 7208). *See* 28 C.F.R. § 0.70.

[updated September 2007]

[cited in USAM 6-1.110; 6-2.000; 6-4.010; 6-4.125; 6-4.210]

6-4.210 Tax-Related Mail, Wire, or Bank Fraud, RICO, or Money Laundering Charges

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The Tax Division must approve any and all criminal charges that a United States Attorney intends to bring against a defendant in connection with conduct arising under the internal revenue laws, regardless of which criminal statute(s) the United States Attorney proposes to use in charging the defendant. *See* USAM 6-4.200; 28 C.F.R. § 0.70. Thus, a United States Attorney must obtain Tax Division approval *before* bringing mail, wire or bank fraud charges, either alone or as the predicate to RICO or money laundering charges, if the conduct arises under the internal revenue laws. Conduct arising under the internal revenue laws includes a defendant's submission of a document or information to the IRS. A United States Attorney also must obtain Tax Division approval to bring charges based on state tax violations if the case involves parallel federal tax violations. *See* Tax Division Directive No. 128 (October 29, 2004), Tax Resource Manual 14.

A. Mail, Wire or Bank Fraud Charges. The Tax Division may approve mail, wire or bank fraud charges in tax- related cases involving schemes to defraud the Government or other persons if there was a large fraud loss or a substantial pattern of conduct and there is a significant benefit to bringing the charges instead of or in addition to Title 26 violations. *See generally* USAM 9-43.100. Absent unusual circumstances, however, the Tax Division will not approve mail or wire fraud charges if a case involves only one person's tax liability or when all submissions to the IRS were truthful.

Examples of situations where, with Tax Division approval, a United States Attorney may appropriately use mail, wire or bank fraud charges in a tax case include:

1) when a target has filed multiple fraudulent returns seeking tax refunds, using fictitious names, or using the names of real taxpayers without their knowledge, appropriate charges may include mail fraud (18 U.S.C. § 1341) or wire fraud (18 U.S.C. §1343);

2) when a target has promoted a fraudulent tax scheme, appropriate charges may include mail fraud (18 U.S.C. § 1341) or wire fraud (18 U.S.C. §1343);

3) when a target has induced a financial institution to approve refund anticipation loans on the basis of the fraudulent information submitted to the IRS, appropriate charges may include bank fraud charges (18 U.S.C. § 1344).

The Government may derive significant benefits at different stages of the litigation by using mail, wire or bank fraud charges. First, at the charging stage, the charges may support the Government's effort to forfeit the proceeds of the fraud scheme or may enable the Government to describe the entire scheme in the indictment. Second, at trial, the charges may support the Government's presentation of all relevant evidence of the scheme or permit flexibility in the Government's choice of witnesses. And third, at sentencing, the charges may support the Government's efforts to obtain full restitution. *See* USAM 9-27.320(B)(3) ("If the evidence is available, it is proper to consider the tactical advantages of bringing certain charges.").

B. Racketeering and Money Laundering Charges Based on Tax Offenses. The Tax Division will not authorize the use of mail, wire or bank fraud charges to convert routine tax prosecutions into RICO or money laundering cases, but will authorize prosecution of tax-related RICO and money laundering offenses when unusual circumstances warrant such a prosecution. A United States Attorney who wishes to bring a RICO charge (18 U.S.C. § 1962) in any criminal matter arising under the internal revenue laws, must first obtain the authorization of the Tax Division and the Criminal Division's Organized Crime and Racketeering Section. *See* USAM 9-110.101. This requirement also applies to RICO cases where the predicate act is a state tax violation and there is a parallel federal violation. A United States Attorney who wishes to bring a money laundering charge (18 U.S.C. § 1956) based on conduct arising under the internal revenue laws, must first obtain the authorization of the Tax Division and, if necessary, the Criminal Division's Asset Forfeiture and Money Laundering Section. *See* USAM 9-105.300.

[updated September 2007] [cited in USAM 6-2.000]

6-4.211 Standards of Review

A. Prosecution. The Principles of Federal Prosecution set forth the standards that govern the Tax Division's review

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of a criminal tax matter to determine whether to authorize prosecution. Under these principles, before authorizing a prosecution, the Tax Division must conclude that the Government has: 1) sufficient evidence to support a prima facie case; and 2) a reasonable probability of conviction. *See* USAM 9-27.220. The Tax Division also considers factors such as uniformity, balanced and broad enforcement goals, and Department and IRS priorities and policies in criminal enforcement matters. *See generally* USAM 6-4.010.

B. Grand Jury Investigation. When it reviews a criminal tax matter to decide whether it should authorize a grand jury investigation, the Tax Division considers whether articulable facts support a reasonable belief that a target or subject is committing or has committed a tax crime.

[updated September 2007] [cited in USAM 6-2.000; 6-4.123]

6-4.212 Categories of Matters Reviewed

A. IRS Referrals. The Tax Division utilizes a complex/non-complex case designation procedure to expedite the review of administrative criminal tax matters that the IRS has referred while maintaining uniformity of prosecution standards.

1) Complex Matters. The Tax Division designates as “complex” referrals that have the following characteristics: a) the IRS utilized an indirect method of proof in developing the case; b) the facts or legal issues are complicated; or c) the case contains technical and/or sensitive issues or tax or policy issues. A docket attorney from one of the three regional Criminal Enforcement Sections reviews each complex referral and prepares a prosecution memorandum (“pros. memo”) that analyzes the evidence, highlights procedural and/or substantive problems with the case, and makes recommendations for further action. At least one senior Criminal Enforcement Section attorney reviews each pros. memo. The Tax Division then decides to authorize or decline prosecution.

2) Non-complex Matters. Non-complex matters are referrals that are relatively straightforward and uncomplicated and that do not present technical tax or sensitive policy issues. Senior Criminal Enforcement Section attorneys review these referrals to ensure that they do not present issues that require in-depth review. The Tax Division transmits a non-complex matter to the appropriate United States Attorney within two weeks of receiving the referral from the IRS. In turn, the United States Attorney must consider the matter within 90 days. *See* USAM 6-4.244.

B. United States Attorney Requests for Grand Jury Authorization. When a United States Attorney requests that the Tax Division authorize a grand jury investigation into a matter arising under the internal revenue laws, Criminal Enforcement Section personnel review the request and then approve or deny it. *See* USAM 6-4.122 and 6-4.123.

[updated September 2007]

6-4.213 Review of Direct Referrals

The Tax Division monitors all matters that the IRS refers directly to the United States Attorneys. *See* USAM 6-4.243. If the Tax Division determines that the IRS has improperly referred a matter to the United States Attorney, the Tax Division will inform the United States Attorney to forward the matter to the Tax Division for review.

[updated September 2007] [cited in USAM 6-4.213]

6-4.214 Conferences

If time and circumstances permit, the Tax Division generally grants a taxpayer's written request for a conference with the Division in Washington, D.C. If the taxpayer makes the request for a conference after the Tax Division has forwarded the matter to the United States Attorney, the Tax Division will deny the request and suggest that the taxpayer ask the United States Attorney for a conference. The United States Attorney has discretion to grant or deny a taxpayer's request for a conference. On rare occasions, the Tax Division may ask a United States Attorney to hold a conference and submit

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a written recommendation about whether the Division should change its decision regarding prosecution.

During the conference, the Tax Division usually advises conferees of the proposed charges, the method of proof, and the income and tax computations that the IRS recommended. The Division also advises them that these may change. The taxpayer or the taxpayer's representative may present explanations or evidence for the Tax Division to consider in reaching a decision regarding prosecution. The conferees may not use the conference, however, as an opportunity to explore the Government's evidence.

The Government may use any statements made by the taxpayer at the conference not only to evaluate the matter, but also in any court proceeding, whether criminal or civil. *See* Fed. R. Evid. 801(d)(2). The Government does not, however, use in general court proceedings statements made at these conferences by attorneys for the taxpayer, *i.e.*, vicarious admissions,. The Government may also develop investigative leads from any information provided at the conference. The Tax Division permits plea negotiations during conferences in non-grand jury cases. A plea obtained in such a case must be consistent with the Tax Division's major count policy and the policies of the appropriate United States Attorney's Office. *See* Tax Division Directive No. 86-58 (May 14, 1986), Tax Resource Manual 15.

[updated September 2007]

6-4.217 On-Site Review

The United States Attorney may request that the Tax Division perform an on-site review of a matter by personally submitting a written request that outlines the reasons for the review. The Division grants such a request only in exceptional circumstances. Criminal Enforcement Section personnel will perform the approved review.

[updated September 2007]

6-4.218 Tax Division Authorizations and Declinations

The final authority for the prosecution or declination of all criminal matters arising under the internal revenue laws rests with the Assistant Attorney General, Tax Division. 28 C.F.R. § 0.70.

[updated September 2007] [cited in USAM 6-2.000]

6-4.219 Assistance of Criminal Enforcement Section Personnel

The Tax Division will consider the following reasons in support of a United States Attorney's request for litigation assistance:

1) Recusal of the United States Attorney and his/her office; and

2) The United States Attorney's lack of sufficient resources, personnel or expertise.

The Tax Division generally expects the United States Attorney to handle non-complex matters that have been accepted for prosecution. *See* USAM 6-4.244.

[updated September 2007] [cited in USAM 6-4.244]

6-4.240 United States Attorney's Responsibilities

The United States Attorney is normally responsible for the investigation and prosecution of criminal tax matters that the Tax Division has authorized.

[updated September 2007]

6-4.242 Recommendation Following a Grand Jury Investigation

At the conclusion of a tax or joint tax and non-tax grand jury investigation, the United States Attorney should submit

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to the Tax Division a written analysis of the investigation, along with a recommendation regarding whether the Government should bring charges or decline prosecution. If the United States Attorney is recommending that the Government should bring non-tax charges as well, the analysis must explain how the non-tax charges relate to the tax charges. *See* USAM 6-4.125.

The United States Attorney must ensure that the Tax Division receives the material at least 60 days prior to the expiration of the statute of limitations.

[updated September 2007] [cited in USAM 6-2.000; 6-4.122; 6-4.125]

6-4.243 Review of Direct Referral Matters

The Tax Division authorizes the IRS to refer directly to the United States Attorney for prosecution the following categories of matters:

A. Excise taxes. This category includes all 26 U.S.C. and 18 U.S.C. offenses involving taxes imposed under Subtitles C, D, and E of the Internal Revenue Code (26 U.S.C.), except taxes imposed under Chapter 24 (withholding from wages), 32A parts I through III (motor and aviation fuels), and 38D (ozone-depleting chemicals).

B. Multiple filings of false and fictitious returns claiming refunds. This category includes all 18 U.S.C. §§ 286 and 287 charges that arise when a taxpayer files, in a single tax year, two or more returns on which false refunds are claimed. This category does not include, and the IRS may not directly refer to the United States Attorney, cases involving return preparers who falsified returns to claim refunds or cases involving persons who submitted false or fictitious claims for refund to the IRS through the Electronic Filing (ELF) program. (18 U.S.C. §§ 286 and 287).

C. Trust fund matters. This category involves alleged violations of the trust fund laws. (26 U.S.C. §§ 7215 and 7512).

D. "Ten percenter" matters. This category includes wage-related cases in which the holder of a winning bet pays a nominee a percentage of winnings in exchange for the nominee's redemption of the winning bet. The IRS may directly refer such cases to the United States only if they involve an arrest that occurs at the time of the offense. (26 U.S.C. § 7206(2)).

E. IRS Form 8300 Returns. This category involves cases in which a taxpayer who receives cash in a trade or business and is required under 26 U.S.C. § 6050I to file an IRS Form 8300, fails to file or files a false Form 8300. With some exceptions, the Tax Division authorizes direct referrals in such cases to prosecute violations under 26 U.S.C. §§ 7203 and 7206. *See* Tax Division Directive No. 87-61 (February 27, 1987), Tax Resource Manual 16.

The United States Attorney may initiate or decline prosecution of direct referral matters without first obtaining Tax Division approval, but in all other tax matters may initiate proceedings only after the Tax Division authorizes prosecution. Once a prosecution of *any* tax matter, including a direct referral matter, is initiated, however, the United States Attorney may not dismiss the indictment, information, or complaint unless and until the Tax Division authorizes dismissal. *See* USAM 6-4.246.

[updated September 2007] [cited in USAM 6-4.110; 6-4.122]

6-4.244 Review of Non-complex Matters

Within 90 days of receiving a designated non-complex matter, a United States Attorney must either initiate proceedings or request that the Tax Division decline the matter (*see* USAM 6-4.245) or handle it (*see* USAM 6-4.219).

[updated September 2007] [cited in USAM 6-4.212; 6-4.219]

6-4.245 Request to Decline Prosecution

A. Request by United States Attorney. A United States Attorney who concludes that the Government should not

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prosecute a particular tax matter must submit a written recommendation to the Tax Division for consideration. The Assistant Attorney General, Tax Division, will then evaluate the matter and determine whether the matter should be prosecuted or declined. If the Assistant Attorney General determines that the matter should be prosecuted, the United States Attorney will be requested to proceed. If the United States Attorney declines to proceed, Criminal Enforcement Section personnel from the Tax Division will handle the matter. The United States Attorney must send the recommendation to the Chief of the appropriate Criminal Tax Enforcement Section sufficiently in advance of the expiration of the statute of limitations or any other deadlines to give the Assistant Attorney General, Tax Division, sufficient time to consider the recommendation and to give Tax Division personnel sufficient time to prepare for prosecution.

B. Grand Jury No Bill. Once a grand jury returns a no bill or otherwise acts on the merits in declining to return an indictment, the United States Attorney must not present the same matter (*i.e.*, same transaction or event and the same putative defendant) to another grand jury or present it again to the same grand jury without the prior approval of the Assistant Attorney General, Tax Division. Ordinarily, the Assistant Attorney General does not give that approval unless the Government finds additional or newly-discovered evidence or there would be a clear miscarriage of justice if the Government did not make a second attempt to obtain an indictment.

[updated September 2007] [cited in USAM 6-2.000; 6-4.244; 9-27.640]

6-4.246 Request to Dismiss Prosecution

The United States Attorney may not dismiss an indictment, information, or complaint unless and until the Tax Division approves the dismissal. There are two exceptions to this rule: 1) the grand jury returns a superseding indictment; or 2) the defendant has died. In all other cases, an Assistant United States Attorney must submit to the Tax Division a written request for dismissal which outlines the reasons for the request and indicates that the United States Attorney concurs with the request.

[updated September 2007] [cited in USAM 6-2.000; 6-4.243]

6-4.247 United States Attorney's Protest of Declination

If a United States Attorney disagrees with the Tax Division's decision to decline prosecution of a matter arising out of a grand jury investigation, the United States Attorney may submit a written request for reconsideration explaining why prosecution is warranted.

[updated September 2007]

6-4.248 Status Reports

After the Tax Division refers a criminal tax case to the United States Attorney, it is essential that the United States Attorney keep the Division apprised of all developments through periodic case status reports. *See* Tax Resource Manual 17. As the case progresses, the Tax Division requires the following information:

1) A copy of the indictment returned (or no billed), or the information filed that reflects the date of the return (or no bill) or filing;
2) The date of arraignment and kind of plea;
3) The date of trial;
4) The verdict and date verdict returned;
5) The date and terms of sentence;
6) The date of appeal and appellate decision; and
7) copy of any press release.

It is important for the United States Attorney to provide the Tax Division with timely and regular updates regarding de-

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velopments in pending cases. The Tax Division's files must reflect the true case status so that, upon completion of the criminal case, the Division can close the criminal case in a timely manner and return it to the IRS.

[updated September 2007]

6-4.249 Return of Reports and Exhibits

After obtaining both a final judgment from the trial court and a final appellate decision, the United States Attorney should take the following actions:

1) Retain grand jury materials under secure conditions, in accordance with the requirements of Federal Rule of Criminal Procedure 6(e) for maintaining the secrecy of grand jury material;

2) Return all exhibits and other materials that the Government obtained from witnesses; and

3) Return to the SAC, by certified mail, return receipt requested, all non-grand jury reports, exhibits, and other materials that the IRS furnished for use in the investigation or trial.

[updated September 2007]

6-4.270 Criminal Division Responsibility

The Criminal Division of the Department of Justice is responsible for prosecuting persons who have committed the following tax-related offenses:

- liquor tax
- narcotics
- stamp tax
- firearms
- wagering
- coin-operated gambling and amusement machines
- malfeasance offenses that IRS personnel have committed
- forcible rescue of seized property
- corrupt or forcible interference with an officer or employee acting under the internal revenue laws (but not omnibus clause)
- counterfeiting, mutilation, removal, or misuse of stamps

See 28 C.F.R. § 0.70.

[updated September 2007]

6-4.310 Major Count Policy in Plea Agreements

Disposition of tax cases through pleas. The Government disposes of an overwhelming percentage of all criminal tax cases by entry of a plea of guilty. The Tax Division authorizes the United States Attorney to accept a plea of guilty to the major count(s) of the indictment or information, without first obtaining Tax Division approval. The United States Attorney also may seek a plea to more than the major count(s) if he or she thinks the Government should accept such a plea. In most cases, the Tax Division identifies the major count(s) that have been authorized for prosecution in the Tax Division's prosecution memorandum or in its case transmittal letter.

Major Count Designations. When it designates the major count, the Tax Division primarily considers the following:

1) Felony counts have priority over misdemeanor counts.

2) Tax evasion counts (26 U.S.C. § 7201) have priority over all other substantive tax counts.

3) The count charged in the indictment or information that carries the longest prison sentence is the major count.

4) As between counts under the same statute, the count involving the greatest financial detriment to the United States

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(*i.e.*, the greatest additional tax due and owing) is the major count.

5) As between counts, if the financial detriment does not differ significantly, the relative flagrancy of the offense is determinative.

The United States Attorney may request the Tax Division to consider other factors not included above.

Other Factors in Designating Major Count. The Tax Division may need to designate more than a single count as a major count when the computed guideline sentencing range exceeds the maximum sentence that the court can impose under a single count.

If the Government charges both tax and non-tax counts, the Tax Division's selection of which tax count to designate as the major count may not have any effect on the applicable guideline range. This lack of effect occurs when the offense level of the group or groups of non-tax offenses is nine (9) or more levels higher than the offense level of the group containing the tax charges. *See* U.S.S.G. §§ 3D1.2 and 3D1.4. In such a case, if its designation will not affect the applicable guideline range, the Tax Division may designate a less serious tax offense in the group as the major count.

If all of the tax charges are not part of the same course of conduct or common scheme or plan, the Department's plea policy for Sentencing Guidelines cases may require that the Tax Division either designate one count from each group of unrelated counts as major counts or designate one count from one of the groups of unrelated counts as the major count and have the prosecutor obtain a stipulation from the defendant establishing the commission of the offenses in the other group. *See* U.S.S.G. § 1B1.2(c). The Tax Division engages in this process to determine the combined offense level for the case under U.S.S.G. § 3D1.4.

No Reduction From Felony to Misdemeanor. When the major count of a tax indictment charges a felony offense, the United States Attorney may not accept a plea to a lesser-included offense nor substitute a misdemeanor offense for the felony offense charged. Absent unusual circumstances, the Tax Division will not approve the reduction of a charge from a felony to a misdemeanor merely to secure a plea.

Post-Plea Dismissal of Remaining Counts. After the court accepts a defendant's guilty plea to one or more major counts and imposes a sentence, the United States Attorney may move to dismiss the remaining counts of the indictment or information.

Pleas Taken in Advance of Indictment or Information. A defendant who has not yet been charged sometimes indicates an intent to enter a guilty plea to the major count(s). If this occurs, the United States Attorney, when presenting the factual basis for the prosecution, in compliance with Federal Rule of Criminal Procedure 11, must include the full extent of the defendant's tax violations on all of the counts in order to demonstrate the defendant's actual criminal intent. In most cases, all of the tax charges are related. Consequently, even if the defendant pleads to only a single count, the court should take into account the tax loss from all of the years when it determines the tax loss for the offense to which the defendant pleads.

[updated September 2007] [cited in USAM 6-2.000]

6-4.320 Nolo Contendere Pleas

Under Department of Justice policy, all government attorneys must oppose the acceptance of nolo contendere pleas. In cases involving tax charges, the United States Attorney may not consent to a plea of “nolo contendere” except in the most unusual circumstances and only after the Assistant Attorney General, Tax Division, has approved a written request. *See* USAM 9-16.010 and 9-27.500. The United States Attorney also must oppose dismissal of any charges to which the defendant does not plead nolo contendere. *See* USAM 9-27.530.

There are several reasons for the Government's opposition to nolo pleas. When pleading “nolo,” the defendant may create the impression that the Government has only a technically adequate case that the defendant elects not to contest. Further, a standard guilty plea permits the Government to use collateral estoppel in subsequent civil proceedings (*e.g.*, when a defendant contests a civil fraud penalty). When it obtains a “nolo” plea, however, the Government will not be

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able to use collateral estoppel in the civil proceeding.
[updated September 2007] [cited in USAM 6-2.000]

6-4.330 Alford Pleas

In *North Carolina v. Alford*, 400 U.S. 25 (1970), the Supreme Court held that a trial court may accept a defendant's plea of guilty over the defendant's claims of innocence. The United States Attorney should discourage *Alford* pleas by refusing to agree to terminate prosecutions in situations where a defendant proffers a plea to fewer than all of the pending charges. The United States Attorney may not consent to a so-called *Alford* plea except in the most unusual circumstances and only after the Assistant Attorney General, Tax Division, or a higher Departmental official, has approved a written request. *See* USAM 9-16.015 and 9-27.440.

Furthermore, if a defendant tenders an *Alford* plea to fewer than all of the charges and the court accepts it over the Government's objection, the United States Attorney must proceed to trial on all of the remaining counts that are not barred on double jeopardy grounds, unless the Assistant Attorney General, Tax Division, approves dismissal of the remaining charges.
[updated September 2007] [cited in USAM 6-2.000]

6-4.340 Sentencing

Rule 32(i)(4)(A)(iii) of the Federal Rules of Criminal Procedure permits the Government to make a statement to the court at the time of sentencing. The United States Attorney should make a full statement of the facts, including the amount of tax that the defendant evaded for all relevant conduct, including how the defendant perpetrated and concealed the fraud, the defendant's past criminal record, and all other information that the court may consider important in imposing an appropriate sentence.

Because a jail sentence provides the maximum deterrent value, the Tax Division prefers that the United States Attorney's sentencing recommendation request that the court impose a jail sentence in addition to a fine and the costs of prosecution. A court's order of probation and a defendant's payment of any civil tax liability in addition to a fine and costs, do not constitute a satisfactory disposition of a criminal tax case.

Notwithstanding the foregoing, the United States Attorney may agree to a sentence of probation (preferably with alternative conditions of confinement) when: 1) the defendant pleads guilty; 2) the sentencing guidelines range is 0-6 months (and within Criminal History Category I); and 3) the United States Attorney personally signs and approves a written memorandum that identifies those unusual and exceptional circumstances that support the appropriateness of agreeing to probation. Examples of exceptional circumstances include the need to secure cooperation against a more culpable party or a serious, post-indictment degradation in the evidence available for trial (such as the death of a witness or the loss or suppression of evidence). The United States Attorney must keep this memorandum in the case file and must forward a copy to the Tax Division when closing the case.
[updated September 2007]

6-4.350 Costs of Prosecution

Congress has provided that, after a jury or court convicts a defendant of any of the principal substantive criminal tax offenses (*e.g*, 26 U.S.C. §§ 7201, 7203, 7206 (1) and (2)), the court must order the defendant to pay the Government's costs of prosecution. Thus, the United States Attorney should seek recovery of the costs of prosecution in criminal tax cases.
[updated September 2007]

6-4.360 Compromise of Criminal Liability/Civil Settlement

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While statutory authority under 26 U.S.C. Sec. 7122(a) does exist for the Attorney General, after referral of a case to the Department, to enter into agreements to compromise criminal tax cases without prosecution, as a matter of longstanding policy, such authority is very rarely exercised. If it is concluded that there is a reasonable probability of conviction and that prosecution would advance the administration of the internal revenue laws, any decision to forgo prosecution on the ground that the taxpayer is willing to pay a fixed sum to the United States, would be susceptible to the attack that a taxpayer who is able to pay whatever amount of money the government demanded had been given preferential treatment.

Consequently, proposed criminal tax cases are reviewed without any consideration being given to the matter of civil liability or the collection of taxes, penalties, and interest. In short, proposed criminal tax cases are examined with the view to determining whether a violation has occurred, to the exclusion of any consideration of civil liability.

Absent extraordinary circumstances, such as permanent loss of tax revenues unless immediate protective action is taken, settlement of the civil liability is postponed until after sentence has been imposed in the criminal case, except when the court chooses to defer sentencing pending the outcome of such settlement. In this event, the IRS should be notified so that it can begin civil negotiations with the defendant.

However, the Tax Division strongly encourages, but does not require, that a plea agreement include certain civil admissions by the defendant, including: (1) admission of either receipt of enumerated amounts of unreported income or claimed enumerated amounts of illegal deductions or improper credits for years set forth in the plea agreement; (2) a stipulation that defendant is liable for the fraud penalty imposed by the Internal Revenue Code (26 U.S.C. Sec. 6663) on the understatements of liability for the years involved; and (3) an agreement by the defendant to file, prior to sentencing, complete and correct initial or amended personal returns for the years subject to the above admissions and, if requested, to provide the IRS with information regarding the years covered by the returns and to pay, at sentencing, all additional taxes, penalties and interest which are due and owing; and (4) an agreement by the defendant not to file any claims for refund of taxes, penalties, or interest for amounts attributable to the returns filed incident to the plea.

[updated September 2007] [cited in USAM 6-6.200]

6-4.370 Restitution

The Department of Justice authorizes and encourages United States Attorneys to seek restitution in criminal tax cases. In May 2005, the Attorney General issued new Guidelines on Victim and Witness Assistance. Those Guidelines require that prosecutors in all cases “must consider “requesting that the defendant provide full restitution to all victims of all charges contained in the indictment or information, without regard to the counts to which the defendant actually plead[s].” (Pub. L. No. 104-132 § 209; 18 U.S.C. § 3551 note).

A Joint IRS/DOJ Task Force on Restitution developed standard language for the restitution portion of a plea agreement and a proposed restitution order for use by prosecutors in criminal tax cases involving defendants who agree or are ordered to pay restitution. For the Task Force Memorandum, standard restitution plea language, optional restitution plea language, and the recommended form for a restitution, see Tax Resource Manual 18 through 21.

A United States Attorney should direct any questions about restitution in criminal tax cases to the Criminal Appeals and Tax Enforcement Policy Section (CATEPS) of the Tax Division. *See* Tax Resource Manual 2.

[updated September 2007]

6-4.400 Parallel Proceedings

Consistent with the Department's policies for coordinating criminal, civil, and administrative actions, the Tax Division uses all available judicial remedies and procedures to enforce the tax laws. These actions include criminal prosecutions, civil injunction actions, summons enforcement actions, collection actions, and the defense of civil refund suits. The Government may take these actions simultaneously or sequentially. *See* Tax Resource Manual 22.

[updated September 2007]

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57 DTR GG-1

Tax Reporting

New IRS Penalty Structure for Offshore

Accounts Encourages Voluntary Disclosure

The Internal Revenue Service March 26 announced it has put a new penalty structure in place designed to encourage taxpayers with offshore assets to come into its voluntary disclosure program, offering those who comply the chance to avoid criminal prosecution and a battery of additional penalties.

Under the voluntary disclosure guidelines, IRS will look back six years and taxpayers must pay taxes, interest, and an accuracy or delinquency penalty for all years.

The agency unveiled a set of memorandums it sent to the highest officials in the Large and Mid-Size Business Division, the Small Business and Self-Employed Division, and Criminal Investigations, stressing a heightened focus on audits of offshore issues as well as the new structure.

Under the voluntary disclosure guidelines, IRS will look back six years and taxpayers must pay taxes, interest, and an accuracy or delinquency penalty for all years.

Central Feature 20 Percent Penalty

In lieu of all other penalties, taxpayers will be assessed a penalty equal to 20 percent of the amount in foreign bank accounts and entities in the year with the highest aggregate account/asset value.

In a conference call with reporters, Commissioner of Internal Revenue Douglas Shulman stressed this will be available only to those who disclose voluntarily and called the new structure “a firm but fair resolution to these cases.” He cautioned that “this guidance will be for the next six months only. For taxpayers who continue to hide their head in the sand, the situation will only become more dire.”

Both Shulman and two senior IRS officials who spoke to reporters on background stressed that taxpayers who do not disclose continue to face fully developed exams, the possibility of combinations of steep penalties, and potential criminal prosecution.

However, “my goal has always been clear and that is to get taxpayers who are hiding assets offshore back into the system,” Shulman told reporters. With the structure that IRS has developed, “taxpayers will pay back taxes, interest, and a significant penalty, but can avoid criminal prosecution.”

IRS Addresses Issue of Names in Possession

The initiative appears to leave open the voluntary disclosure option for taxpayers whose names are on lists obtained by IRS from outside sources, such as foreign banks, if those taxpayers are not facing criminal charges.

The IRS officials said even if IRS already has taxpayers' names on a list from an outside source, those taxpayers likely still can make a voluntary disclosure as long as IRS has not opened an investigation on that taxpayer.

The agency said in a statement later in the day that “to be clear, it is too late for any taxpayer who is under criminal investigation to make a voluntary disclosure. The IRS cannot discuss specific situations, but the voluntary disclosure process does not apply when the IRS has information related to a specific taxpayer from a criminal enforcement action.”

The agency noted in the statement that “voluntary disclosure depends on the facts and circumstances involved in each

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case. Taxpayers with unreported offshore income should immediately discuss with their tax professional their options to get right with the government, including taking advantage of coming in voluntarily."

"To be clear, it is too late for any taxpayer who is under criminal investigation to make a voluntary disclosure."

IRS

Penalty Framework Outlined

The three memorandums IRS made available March 26, all dated March 23, addressed different facets of the voluntary disclosure issue. The agency also released the section of its Internal Revenue Manual addressing voluntary disclosure.

A key memo, addressed to the commissioners of LMSB and SB/SE, set forth the penalty framework for voluntary disclosure requests containing offshore issues, noting that the framework will be applied to all requests that have been submitted to IRS and are not yet resolved.

The guidance will remain in effect for six months starting March 23, IRS said, stressing that "all voluntary disclosure requests are mandatory work."

The Criminal Investigations unit will make preliminary determinations that taxpayers are eligible to seek voluntary disclosure and forward their requests to the Philadelphia Offshore Identification Unit (POIU) for civil processing, IRS said in the memo.

IRS Provides Details of Process

Agents who specialize in offshore audits will work the cases, and the resulting closing agreements will be reviewed and executed as prescribed by existing delegation orders.

The memo authorized the commissioners to resolve tax liabilities for those requesting voluntary disclosure by taking a three-prong strategy.

First, agents will assess all taxes and interest due going back six years, or the earliest year within that six-year period in which an account was opened or acquired or an entity was formed. They also will require taxpayers to file or amend all returns, including information returns and Form TD F 90-22.1, Report of Foreign Bank and Financial Accounts, commonly known as an FBAR.

Second, agents will assess either a 20 percent accuracy penalty or a 25 percent delinquency penalty on all years, with no reasonable cause exception allowed.

Third, in lieu of all other penalties that may apply, including FBAR and information return penalties, IRS will look at the amounts in the foreign bank accounts or entities in each of the six years and impose a penalty equal to 20 percent of the amount in the accounts or entities in the year with the highest aggregate account/asset value.

Smaller Penalty Available in Some Cases

IRS said it will reduce that latter 20 percent penalty to 5 percent in cases where (1) the taxpayer did not open or cause any accounts to be opened or entities formed, (2) there has been no activity during the period when the account or entity was controlled by the taxpayer, and (3) all U.S. taxes have been paid on the funds in the account or entity.

"The terms outlined herein are only applicable to taxpayers that make voluntary disclosure requests, and who fully cooperate with IRS, both civilly and criminally," the memo said.

In a second memo unveiled by IRS March 26, the agency emphasized to SB/SE examination area directors and SB/SE industry directors that "offshore cases sent to the field are of the highest priority. Examiners should use the full range of information gathering tools in properly developing offshore issues, with special emphasis on detecting unreported income."

IRS said techniques should include interviewing taxpayers, making third-party contacts, and timely issuing summonses

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to taxpayers and third parties.

Increased Stress on Offshore Exams

"In particular, examiners should request foreign-based information through exchange of information under applicable treaties and tax information exchange agreements (TIEAs) in any cases where the taxpayers have accounts or transactions in countries with such agreements,"IRS said.

The memo urged examiners to be "alert to the badges of fraud"and said managers should ensure that income and penalty considerations are sufficiently developed and documented.

In addition, the memo said IRS will no longer allow taxpayers the chance to minimize their exposure to penalties through the terms of the agency's Last Chance Compliance Initiative (LCCI). All notices and letters with respect to the LCCI, as well as relevant sections of the Internal Revenue Manual, are in the process of being obsoleted.

For currently open exams where taxpayers already have been offered terms under LCCI, they will be allowed to resolve their cases using that initiative if they respond to their examiner within 15 days, IRS said.

Practitioners React to Guidelines

The new voluntary disclosure guidelines generally drew praise from practitioners, although some expressed caution about how they would be applied.

"We've been looking for something like this for quite some time,"Mark Matthews, former IRS deputy commissioner and former chief of IRS criminal investigations, now with Morgan, Lewis & Bockius LLP, said. "This brings some clarity to an area that's been very confused."

"We've been looking for something like this for quite some time."

Mark Matthews, Morgan, Lewis & Bockius LLP

He said in his view, the certainty offered in the new guidance is likely to bring more people into the voluntary disclosure program, and "we would encourage clients to take them up on this offer."

Previously, Matthews said, many clients were hesitant because so many different penalties could potentially apply, and IRS has now put together "a more one size fits all approach. I think it's a simple, fairly understandable system," he told BNA.

Response Measured

Charles Rettig, Hochman, Salkin, Rettig, Toscher, & Perez, PC, was more measured, saying, "It is great for the IRS to finally get an initiative together on this issue. Practitioners have been pushing for guidance re offshore voluntary disclosures for quite some time."

However, he stressed, "Hopefully, the penalty administration in this guidance will not be harshly applied for taxpayers who came in early, before the initiative. Fairness in application of this initiative is important for the future of voluntary disclosures over the long term.

"Practitioners and future taxpayers need to know those who come in voluntarily will be treated fairly, and certainly better than others who were discovered before deciding to comply," Rettig said.

While "some guidance is always better than none," Rettig said he remains concerned that some taxpayers will likely be looking at a 20 percent penalty under the initiative when the IRS may otherwise have determined that, based on the actual facts, no penalty is warranted. "The deemed fairness of the overall voluntary disclosure system is significantly more important to all taxpayers than presently imposing harsh penalties on those with offshore accounts," he said.

By Alison Bennett

Texts of the SBSE/LMSB, SBSE/LMSB/CID, and deputy commissioner's memos are in TaxCore, along with IRM

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95.11.9 on IRS voluntary disclosure practice for potential tax crimes, along with Commissioner Shulman's statement.

Daily Tax Report: All Issues > 2009 > March > 03/27/2009 > TaxCore® - IRS Documents > Audit Technique Guidelines > IRS SBSE, LMSB Memorandum Regarding Development of Offshore Examination Cases, Managerial Review, Revocation of Last Chance Compliance Initiative

IRS SBSE, LMSB Memorandum Regarding Development of Offshore Examination Cases, Managerial Review, Revocation of Last Chance Compliance Initiative

Related Terms

Topics:

Tax Reporting

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
Washington, D.C. 20224
Small Business Self-Employed Division
Large and Mid-Size Business Division
March 23, 2009
MEMORANDUM FOR SBSE EXAMINATION AREA DIRECTORS LMSB INDUSTRY DIRECTORS
FROM: Faris R. Fink /s/
Deputy Commissioner, SBSE
Barry B. Shott /s/
Deputy Commissioner, LMSB International
SUBJECT: Emphasis on and Proper Development of Offshore Examination Cases, Managerial Review, and Revocation of Last Chance Compliance Initiative

The purpose of this memorandum is to ensure examinations with offshore transactions and/or entities continue to be emphasized and receive priority treatment daring the examination process. This memorandum also provides for managerial oversight of offshore cases, and revokes the Last Chance Compliance Initiative.

Offshore Case Development

The IRS Strategic Plan for 2009-2013 outlines the Service's commitment to meet the challenges of international tax administration and of allocating compliance resources to target existing and emerging high-risk areas. Similarly, both the SBSE Examination Program Letter and the Servicewide Approach to International Tax Administration documents address our continuing commitment to prioritize and investigate abusive offshore transactions designed to defeat our tax system.

Offshore cases sent to the field are work of the highest priority. Examiners should utilize the full range of information gathering tools in properly developing offshore issues, with special emphasis on detecting unreported income. This includes interviewing taxpayers, making third party contacts, and timely issuing summonses to taxpayers and third parties. In particular, examiners should request foreign-based information through exchange of information under applicable treaties and tax information exchange agreements (TIEAs) in any cases where the taxpayers have accounts or transactions in countries with such agreements. Examiners should be alert the to badges of fraud and consult with Fraud Technical Advisors in developing cases for criminal referrals or the assertion of the civil fraud penalty. Counsel is available to assist SBSE and LMSB personnel as needed. Attachment 1 contains a brief summary of potential foreign information reporting requirements and civil penalties that could apply to a taxpayer depending on his/her particular facts and circum-

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stances.

Managerial Oversight

Managers should ensure that income and penalty considerations are sufficiently developed and documented during both unagreed and Embedded Quality reviews. Cases should be discussed with employees regarding the need for additional income probes, use of indirect methods of proof to reconstruct income, penalty development and/or other considerations as necessary.

Revocation of Last Chance Compliance Initiative

Effective as of the date of this memorandum, the Service will no longer afford taxpayers the opportunity to minimize their exposure to penalties through the terms of the Last Chance Compliance Initiative (LCCI). All notices and letters with respect to the LOCI and relevant portions of IRM sections 4.26.16, 4.26.17 and 25.6.23 are in the process of being obsoleted. On any currently open examinations where the LCCI terms have already been offered, taxpayers will be afforded the opportunity to resolve their cases under LCCI if they respond to the examiner within 15 days of their prior notification.

If you have questions, members of your staff may contact Karen Warfel, SBSE Offshore Program Manager at __, Frank Bucci, SBSE Offshore Technical Advisor __ or Lori Nichols, LMSB Director, International Compliance Strategy and Policy at _

Attachment

Attachment 1

The following summary of potential reporting requirements and civil penalties is not necessarily all encompassing, and it is unlikely that any one taxpayer would be subject to all of the reporting obligations or penal listed below:

(1) Penalties for failure to comply with the Bank Secrecy Act requirement that United States persons report heir financial interest in, or authority over, financial accounts located in a foreign country.

U S citizens, residents, and certain other persons, must annually report their financial interest in, or signature authority (or other authority that is comparable to signature authority) over, a financial account (such as a bank or investment account) that is maintained with a financial institution located in a foreign country if, for any calendar year, the aggregate vale of all foreign accounts exceeded $10,000 at any time during the year. This reporting requirement is met by filing *Form TD F 90-22.1* (Report of Foreign Bank and Financial Accounts, commonly known as an “FBAR”) FBARs are filed with a Department of the Treasury facility located in Detroit and are not to be filed with tax. returns; the filing date for FBARs is June 30th The requirement to file FBARs is in the regulations under 31 U.S.C. §5314 (which is a provision of the Bank Secrecy Act) Generally, the civil penalty for willfully falling to file an FBAR can be as high as the greater of $100,000 or 50 percent of the total balance of the foreign account. Criminal penalties may also apply. Refer to IRM 4.26.16.4 for additional FBAR penalty considerations.

(2) Fraud Penalties (Sections 6651(f) and 6663):

Where an underpayment of tax, or a failure to file a tax return, is due to fraud, the taxpayer liable for-penalties that, although calculated differently, essentially amount to 7 percent of the unpaid tax.

(3) Failure to File Tax Return (Section 6651):

When a taxpayer is required to file a tax return and does not do so on or before the due date of the return Section 6651(a)(1) imposes a penalty of 6 percent of the net tax amount required to be shown on the tax return for each month (or fraction of a month) that the return is late The maximum penalty is 25 percent. This penalty is increased to 15% with a maximum of 75%, if the taxpayer's failure to file is fraudulent

(4) Failure to Pay Tax Penalties (Sections 6651(a)(2) and 6651(a)(3))

When a taxpayer fails to timely pay the amount of tax shown on the return, Sections 6651(a)(2) imposes a late payment

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penalty equal to 5 percent of the late payment for each month (or part of a month) that the payment is late. The maximum penalty is 25 percent.

When a taxpayer fails to pay a tax that is required to be (but was not) shown on a return within 21 days after the date of the Service's notice and demand for that tax, Section 6651(a)(3) imposes a penalty of .5 percent for each month (or part thereof) that the assessment remains unpaid. The maximum penalty is 25 percent.

(5) Accuracy-Related Penalty (Section 6662):

The accuracy-related penalty for underpayments is imposed at the rate of 20 percent on the portion of any underpayment of tax required to be shown on a return attributable to negligence, a substantial understatement of tax, a substantial overstatement of pension liabilities or a substantial estate of gift tax valuation understatement. The accuracy-related penalty with respect to a substantial valuation misstatement can be as high as 40 percent.

(6) Penalties for failure to file certain information returns (Sections 6035, 6038, 6038A, 6038B, 6038C, 6039F, 6046, 6046A, and 6048):

Form 5471. information Return of U.S. Persons With Respect To Certain Foreign Corporations, U.S. persons who are officers, directors, or shareholders in certain foreign corporations (including, for example, an International Business Corporation used in an offshore scheme) report information required by Sections **6035, 6038, and 6046,** and compute income from controlled foreign corporations under Sections 951-964. The penalty for failing to file each one of these information returns is 10,000, with an additional $10,000 added for each month the failure continues beginning 90 days after the taxpayer is notified of the delinquency, up to a maximum of $50,000 per return.

Form 5472. Information Return of a 25% Foreign-Owned U.S. Corporation or a Foreign Corporation Engaged in a U.S. Trade or Business. Reports transactions between a 25% foreign-owned domestic corporation or a foreign corporation engaged in a trade or business in the United States and a related party as required by Sections **6038A and 6038C**. The penalty for failing to file each one of these information returns, or to keep certain records regarding reportable transactions, is $10,000, with an additional $10,000 added for each month the failure continues beginning 90 days after the taxpayer is notified of the delinquency, up to a maximum of $50.000 per return.

Form 926. Return by a U S. Transferor of Property to a Foreign Corporation Reports transfers of property to a foreign corporation and to report information under Section **6038B.** The penalty for failing to file each one of these information returns is ten percent of the value of the property transferred, up to a maximum of $100,000 per return, with no limit if the failure to report the transfer was intentional.

Form 3520. Annual Return to Report Transactions with Foreign Trusts and Receipt of Certain Foreign Gifts. Report various transactions involving foreign trusts, including creation of a foreign trust by a U.S. person, transfers of property from a U.S. person to a foreign trust, and receipt of distributions from foreign trusts under Section **6048**. This return also reports the receipt of gifts from foreign entities under Section **6039F**. The penalty for failing to file each one of these information returns, or for filing an incomplete return, is 35 percent of the gross reportable amount, except for returns reporting gifts, where the penalty is five percent of the gift per month, up to a maximum penalty of 25 percent of the gift.

Form 3520-A. Annual Information Return of Foreign Trust with a U. S. Owner Reports ownership interests in foreign trusts, by U S. persons with various interests in and powers over such trusts under Section **6048(b)**. The penalty for failing to file each one of these information returns, or for filing an incomplete return, is five percent of the gross value of Vest assets determined to be owned by the U.S. person.

Form 8865. Return of U.S. Persons With Respect to Certain Foreign Partnerships, U.S. persons with certain Interests in foreign partnerships use this form to report interests in and transactions of the foreign partnerships, transfers of property to the foreign partnerships, and acquisitions, dispositions, and changes in foreign partnership interests under Sections **6038, 6038B, and 6046A**. Penalties include $10.000 for failure to file each return, with an additional $10,000 added for each month the failure continues beginning 90 days after the taxpayer is notified of the delinquency, up to a maximum $50,000 per return, and ten percent of the value of arty transferred property that is not reported, subject to a $100,000 limit.

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Daily Tax Report: All Issues > 2009 > March > 03/27/2009 > TaxCore® - IRS Documents > Audit Technique Guidelines > IRS SBSE, LMSB, CID Memorandum on Routing of Voluntary Disclosure Cases

IRS SBSE, LMSB, CID Memorandum on Routing of Voluntary Disclosure Cases

Related Terms

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Tax Reporting

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
Washington, D.C. 20224
March 23, 2009
MEMORANDUM FOR SBSE EXAMINATION AREA DIRECTORS
LMSB INDUSTRY DIRECTORS
CI DIRECTORS OF FIELD OPERATIONS
FROM: Fairs R. Fink /s/
Deputy Commissioner, SBSE
Barry B. Shott /s/
Deputy Commissioner, LMSB International
Victor Song /s/
Deputy Chief, Criminal Investigation
SUBJECT: Routing of Voluntary Disclosure Cases

The purpose of the memorandum is to alert you to a change in the processing of voluntary disclosure requests containing offshore issues. All voluntary disclosure requests are mandatory work.

All incoming voluntary disclosure requests will continue to initially be screened by Criminal Investigation (CI) to determine if the taxpayer is eligible to make a voluntary disclosure. Refer to IRM 9.5.11.9 for questions pertaining to taxpayer eligibility. For voluntary disclosure requests containing only domestic issues, where CI has preliminarily determined taxpayer eligibility. CI will continue to forward those requests to the appropriate Area/Industry PSP for civil processing.

Effective as of the date of this memorandum, voluntary disclosure requests containing offshore issues, where CI has preliminarily determined taxpayer eligibility will now be forwarded by CI to the Philadelphia Offshore Identification Unit (POIU) for civil processing. Additionally, any voluntary disclosures with offshore issues that are currently in Area/ Industry case inventories (whether or not there has been prior taxpayer contact by SB SE or LMSB) should also be forwarded to the POIU.

The address for the POIU follows:
Internal Revenue Service
11501 Roosevelt Blvd.
South Bldg., Room 2002
Philadelphia, PA 19154
Attn: Charlie Judge, Offshore Unit, DP S-611

If you have questions, members of your staff may contact Karen Warfel, SBSE Offshore Program Manager __ Frank Bucci, SBSE Offshore Technical Advisor __ or Lori Nichols, LMSB Director, International Compliance Strategy and Policy.

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Daily Tax Report: All Issues > 2009 > March > 03/27/2009 > TaxCore® - IRS Documents > Audit Technique Guidelines > IRS Deputy Commissioner Stiff Memorandum on Authorization to Apply Penalty Framework to Voluntary Disclosure Requests Regarding Unreported Offshore Accounts, Entities

IRS Deputy Commissioner Stiff Memorandum on Authorization to Apply Penalty Framework to Voluntary Disclosure Requests Regarding Unreported Offshore Accounts, Entities

Related Terms

Topics:

Tax Reporting

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224
March 23, 2009
MEMORANDUM FOR COMMISSIONER, LARGE AND MID-SIZE BUSINESS DIVISION COMMISSIONER, SMALL BUSINESS/SELF-EMPLOYED DIVISION
FROM: Linda E. Stiff /s/
Deputy Commissioner for Services and Enforcement
SUBJECT: Authorization to Apply Penalty Framework to Voluntary Disclosure Requests Regarding Unreported Offshore Accounts and Entities

The purpose of this memorandum is to set forth a penalty framework to be applied to voluntary disclosure requests containing offshore issues. The outlined framework will be applied to all such requests that have been submitted to the IRS and are not yet resolved, and will remain in effect for six months from the date of this memorandum. All voluntary disclosure requests are mandatory work.

As criminal investigation (CI) makes preliminary determinations that taxpayers are eligible to make voluntary disclosures, it will forward voluntary disclosure requests with offshore implications to the Philadelphia Offshore Identification Unit (POIU) FOR CIVIL processing. Those requests will be distributed to and worked by examiners who specialize in offshore examinations. All resulting closing agreements will be reviewed and executed as prescribed by existing delegation orders.

Effective as of the date of this memorandum, you are authorized to execute agreements to resolve the tax liabilities related to offshore issues of taxpayers who make voluntary disclosure requests in the following manner:

(1) Access all taxes and interest due going back six years (exception: where an account/entity was formed or acquired within the six year look back period, taxes and interest will be assessed starting with the earliest year in which an account was opened/acquired or entity formed). Require the taxpayer to file or amend all returns, including information returns and Form TD F 90-22.1, Report of Foreign Bank and Financial Accounts, commonly known as an “FBAR”.

2. Access either an accuracy or delinquency penalty on all years (no reasonable cause exception may be applied), and

(3) In lieu of all other penalties that may apply, including FBAR and information return penalties, assess a penalty equal to 20% of the amount in foreign bank accounts/entities in the year with the highest aggregate account/asset value.

If, (a) the taxpayer did not open or cause any accounts to be opened or entities formed (b) there has been no activity in any account or entity (no deposits, withdrawals, etc.) during the period the account/entity was controlled by the taxpayer, and (c) all applicable U.S. taxes have been paid on the funds in the accounts/entities (where only account/entity earnings have escaped U.S. taxation), then the penalty in (3) is reduced to 5%.

The terms outlined herein are only applicable to taxpayers that make voluntary disclosure requests, and who fully co-

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operate with the IRS, both civilly and criminally.

cc: Acting Chief Counsel

Senior Advisor to the Commissioner

Commissioner, Tax Exempt and Government Entities

Chief, Criminal Investigation

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IRS Commissioner Shulman Statement on IRS Offshore Income Reporting Initiative

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Statement from IRS Commissioner Doug Shulman

On Offshore Income

March 26, 2009

My goal has always been clear — to get those taxpayers hiding assets offshore back into the system. We recently provided guidance to our examination personnel who are addressing voluntary disclosure requests involving unreported offshore income. We believe the guidance represents a firm but fair resolution of these cases and will provide consistent treatment for taxpayers. The goal is to have a predictable set of outcomes to encourage people to come forward and take advantage of our voluntary disclosure practice while they still can.

In the guidance to our people, we draw a clear line between those individual taxpayers with offshore accounts who voluntarily come forward to get right with the government and those who continue to fail to meet their tax obligations. People who come in voluntarily will get a fair settlement. We set up a penalty framework that makes sense for them — they need to pay back-taxes and interest for six years, and pay either an accuracy or delinquency penalty on all six years. They will also pay a penalty of 20% of the amount in the foreign bank accounts in the year with the highest aggregate account or asset value. Just to be clear, this is 20% of the highest asset value of an account anytime in the past six years. This gives taxpayers — and tax practitioners — certainty and consistency in how their case will be handled.

We have instructed our agents to resolve these taxpayers' cases in a uniform, consistent manner. Those who truly come in voluntarily will pay back taxes, interest and a significant penalty, but can avoid criminal prosecution.

At the same time, we have also provided guidance to our agents who have cases of unreported offshore income when the taxpayer did not come in through our voluntary disclosure practice. In these cases, we are instructing our agents to fully develop these cases, pursuing both civil and criminal avenues, and consider all available penalties including the maximum penalty for the willful failure to file the FBAR report and the fraud penalty.

We believe this is a firm, but fair resolution of these cases. It will make sure that those who hid money offshore pay a significant price, but also allow them to avoid criminal prosecution if they come in voluntarily. As we continue to step up our international enforcement efforts, this is a chance for people to come clean on their own. Our guidance to the field is for the next six months only, after which we will re-evaluate our options.

For taxpayers who continue to hide their head in the sand, the situation will only become more dire. They should come forward now under our voluntary disclosure practice and get right with the government.

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Daily Tax Report: All Issues > 2009 > April > 04/16/2009 > Federal Tax & Accounting > Tax Reporting: IRS Offers Guidance on How to Voluntarily Disclose Offshore Assets Under New Program

71 DTR G-4

Tax Reporting

IRS Offers Guidance on How to Voluntarily

Disclose Offshore Assets Under New Program

Related Terms

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International Taxes
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The Internal Revenue Service is offering more guidance to taxpayers on how to voluntarily disclose their offshore assets, as it works to encourage more taxpayers to come into compliance under its new penalty structure.

In new information posted on its Web site, IRS stressed that acceptance into a voluntary disclosure arrangement depends on the individual facts and circumstances involved in each case, noting that "taxpayers with unreported income should immediately discuss with their tax professional their options to get right with the government, including taking advantage of coming in voluntarily."

The agency said a voluntary disclosure occurs when the communication is truthful, timely, and complete, and when a taxpayer shows a willingness to cooperate (and does in fact cooperate) with IRS in determining correct tax liability.

"Taxpayers cannot rely on the fact that other similarly situated taxpayers may not have been recommended for criminal prosecution," IRS said.

While a voluntary disclosure will not automatically guarantee immunity from prosecution, such a disclosure may result in prosecution not being recommended, the agency said. It stressed, however, that this practice does not apply to taxpayers with illegal source income.

IRS provided a list of telephone numbers for voluntary disclosures and said tax professionals or individuals who want to disclose should call the number associated with the state or country in which the taxpayer resides.

List of Telephone Numbers Provided

There is a separate telephone number for each U.S. state, and separate numbers for the following countries and regions:

- Puerto Rico;
- South America;
- the Caribbean;
- Mexico and Central America;
- Canada;
- Germany, Switzerland, Italy, the Russian Federation, Eurasia, Eastern Europe, and Southern Europe;

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- the United Kingdom, France, Western Europe, Africa, and the Middle East;
- the Far East, Australia, the South Pacific Islands, and
- Iraq.

The Information follows IRS's March 26 announcement of a new penalty structure designed to encourage voluntary disclosures, offering those who comply the chance to avoid criminal prosecution and a battery of additional penalties (57 DTR GG-1, 3/27/09).

The agency unveiled a set of memoranda it sent to the highest officials in the Large and Mid-Size Business Division, the Small Business and Self-Employed Division, and Criminal Investigations, stressing a heightened focus on audits of offshore issues as well as the new structure.

Under the voluntary disclosure guidelines, IRS will look back six years and taxpayers must pay taxes, interest, and an accuracy or delinquency penalty for all years.

In lieu of all other penalties, taxpayers will be assessed a penalty equal to 20 percent of the amount in foreign bank accounts and entities in the year with the highest aggregate account/asset value.

By Alison Bennett

Text of the list of telephone numbers and other information on voluntary disclosure can be found on the IRS Web site at http:// www.irs.gov/compliance/enforcement/article/0,,Id=205909,00.html.

Contact IRS About Voluntary Disclosure

The IRS stresses that acceptance into a voluntary disclosure arrangement depends on the individual facts and circumstances involved in each case. Taxpayers with unreported income should immediately discuss with their tax professional their options to get right with the government, including taking advantage of coming in voluntarily.

A voluntary disclosure occurs when the communication is truthful, timely, complete, and when: A taxpayer shows a willingness to cooperate (and does in fact cooperate) with the IRS in determining his/her correct tax liability.

For a complete understanding of the voluntary disclosure procedures, see Internal Revenue Manual (IRM) 9.5.11.9

Taxpayers cannot rely on the fact that other similarly situated taxpayers may not have been recommended for criminal prosecution. Also, a voluntary disclosure will not automatically guarantee immunity from prosecution; however, a voluntary disclosure may result in prosecution not being recommended. This practice does not apply to taxpayers with illegal source income.

Tax professionals or individuals who want to make a voluntary disclosure, should call the contact phone number below associated with the State in which the taxpayer resides.

These phone numbers are for the purpose of making voluntary disclosures ***ONLY***.

Alabama	404-338-7540
Alaska	907-271-6911
Arizona	602-207-8964
Arkansas	615-250-5005
California — Northern	510-637-1031
California — Southern	714-347-9226
Colorado	303-603-4936
Connecticut	617-316-2073
Delaware	215-861-1392
District of Columbia	202-874-0155

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Florida - Northern	727-568-2561
Florida — Southern	954-725-1956
Georgla	404-338-7540
Hawaii	808-539-2843
Idaho	720-956-4341
Illinois	312-566-4503
Indiana	312-566-4503
Iowa	402-233-7452
Kansas	402-233-7452
Kentucky	615-250-5005
Louisiana	504-558-1535
Maine	617-316-2073
Maryland	202-927-9351
Massachusetts	617-316-2073
Michigan	313-234-2410
Minnesota	651-767-3254
Mississippi	504-558-1535
Missouri	402-233-7452
Montana	720-956-4341
Nebraska	402-233-7452
Nevada	801-799-6763
New Hampshire	617-316-2073
New Jersey	732-761-3381
New Mexico	505-837-9033
New York	212-436-1588
North Carolina	919-856-4283 ext 408
North Dakota	701-239-5143 ext 292
Ohio	614-744-3130
Oklahoma	214-413-5979
Oregon	503-326-3207
Pennsylvania - Eastem	215-861-1392
Pennsylvania - Western	412-395-6771
Rhode Island	617-316-2073
South Carolina	919-856-4283 ext 408
South Dakota	605-330-4449 ext 266
Tennessee	615-250-5005

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Texas - Dallas	214-413-5979
Texas - Houston	281-721-6341
Texas - San Antonio	512-499-5261
Utah	801-799-6763
Vermont	617-316-2073
Virginia	703-647-5502
Washington	206-464-4916
West Virginia	412-395-6771
Wisconsin	414-231-2448
Wyoming	720-956-4341
INTERNATIONAL	
Puerto Rico	954-423-7872
South America	011-571-383-2769
Caribbean	246-227-4143
Mexico & Central America	011-52-55-50-80-29-01
Canada	613-688-5292
Germany, Switzerland, Italy, Russian Federation, Eurasia, Eastern Europe, and Southern Europe	011-49-69-7535-3647 or 3638
United Kingdom, France, Western Europe, Africa, and Middle East	011-4420-7894-0036 or 0037
Far East, Australia, & South Pacific Islands	011-852-2841-2361
Iraq	011-964-770-443-0356

1. What prompted you to want to participate in Voluntary Disclosure?
2. Where are the funds held regarding the disclosure?
3. Do you have any records? If not, whom are you working with at the bank? (Note: If the taxpayer is a UBS client and if they don't have the records IRS will attempt to assist them in record retrieval).
4. When was the account opened?
5. How was the account opened?
6. Who assisted you with the account opening?
7. Who told you about the bank and how to initiate opening an account?
8. Do you have a trust set up relating to the account or the funds?
9. How did you deposit money into the account?
10. How did you withdraw money from the account?
11. Did you have any credit or debit cards associated with the account?
12. How did you correspond with the bank? Do you have records relating to the correspondence?
13. Who is your current point of contact at the bank?
14. Did you ever meet face to face with anyone from the bank? If so where? When?
15. Did you travel outside of the United States to conduct business relating to your account and or tax activities?
16. Where was your bank statements sent?
17. Who has access to the account? Is it a joint account?

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18. What is the source of the funds?
19. Do you have tax returns?
20. Have you prepared amended tax returns? If so, have you submitted them to the IRS?
21. Who prepared your tax returns?
22. When were your returns prepared?
23. Did they know about the issues discussed today?
24. Did you file FBARs? If not, why not?
25. When did you take control of this account? And, all the related questions a “yes” answer makes us ask.
26. Did you trade US and/or foreign securities with this account? If yes, describe the mechanism for doing that (buy/sell orders, etc.).
27. Did you file returns?
28. Do you or have you directly or indirectly controlled any foreign entities? Did you file the required returns for them?
29. Have you been notified that the US requested information relating to your account(s)?
30. What countries do you have accounts in?

Original Frequently Asked Questions — Posted May 6, 2009

1. Why did the IRS issue internal guidance regarding offshore activities now?

The IRS has had a voluntary disclosure practice in its Criminal Manual for many years. Once IRS Criminal Investigation has determined preliminary acceptance into the voluntary disclosure program, the case is referred to the civil side of IRS for examination and resolution of taxes and penalties. Recent IRS enforcement efforts in the offshore area have led to an increased number of voluntary disclosures. Additional taxpayers are considering making voluntary disclosures but are reportedly reluctant to come forward because of uncertainty about the amount of their liability for potentially onerous civil penalties. In order to resolve these cases in an organized, coordinated manner and to make exposure to civil penalties more predictable, the IRS has decided to centralize the civil processing of offshore voluntary disclosures and to offer a uniform penalty structure for taxpayers who voluntarily come forward. These steps were taken to ensure that taxpayers are treated consistently and predictably.

2. What is the objective of these steps?

The objective is to bring taxpayers that have used undisclosed foreign accounts and undisclosed foreign entities to avoid or evade tax into compliance with United States tax laws. Additionally, the information gathered from taxpayers making voluntary disclosures under this practice will be used to further the IRS's understanding of how foreign accounts and foreign entities are promoted to United States taxpayers as ways to avoid or evade tax. Data gathered will be used in developing additional strategies to inhibit promoters and facilitators from soliciting new clients.

3. Why should I make a voluntary disclosure?

Taxpayers with undisclosed foreign accounts or entities should make a voluntary disclosure because it enables them to become compliant, avoid substantial civil penalties and generally eliminate the risk of criminal prosecution. Making a voluntary disclosure also provides the opportunity to calculate, with a reasonable degree of certainty, the total cost of resolving all offshore tax issues. Taxpayers who do not submit a voluntary disclosure run the risk of detection by the IRS and the imposition of substantial penalties, including the fraud penalty and foreign information return penalties, and an increased risk of criminal prosecution.

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4. What is the IRS's Voluntary Disclosure Practice?

The Voluntary Disclosure Practice is a longstanding practice of IRS Criminal Investigation of taking timely, accurate, and complete voluntary disclosures into account in deciding whether to recommend to the Department of Justice that a taxpayer be criminally prosecuted. It enables noncompliant taxpayers to resolve their tax liabilities and minimize their chances of criminal prosecution. When a taxpayer truthfully, timely, and completely complies with all provisions of the voluntary disclosure practice, the IRS will not recommend criminal prosecution to the Department of Justice.

5. How do I make a voluntary disclosure and where should I submit my voluntary disclosure?

A voluntary disclosure is made by following the procedures described in I.R.M. 9.5.11.9. Tax professionals or individuals who want to initiate a voluntary disclosure, should call their local CI office. For a list of CI offices, visit: http://www.irs.gov/compliance/enforcement/article/0,, id=205909,00.html

Taxpayers with questions may call the IRS Voluntary Disclosure Hotline at (215)516-4777, visit www.irs.gov, or contact their nearest CI office.

6. What form should my voluntary disclosure take?

You should send a letter to the nearest Special Agent in Charge, IRS Criminal Investigation, stating that you wish to make a voluntary disclosure. Ideally, the letter should contain all your identifying information, including name, address, Social Security Number or other Taxpayer Identification Number, passport number and date of birth, and should also include an explanation of any previously unreported or underreported income or incorrectly claimed deductions or credits related to undisclosed foreign accounts or undisclosed foreign entities, including the reason(s) for the error or omission. It should also include a power of attorney (Form 2648), if you are represented, and daytime contact information for you or your representative. If you have already completed the amended or delinquent returns, those should be submitted with the letter; but it is not necessary to include them with the initial submission if you are unable to do so. At a minimum, however, the initial submission must include the taxpayer's name and identifying information described above. IRS Criminal Investigation will follow up on the facts and circumstances to assess the timeliness, completeness, and truthfulness of the voluntary disclosure.

7. I'm currently under examination. Can I come in under voluntary disclosure?

No. If the IRS has initiated a civil examination, regardless of whether it relates to undisclosed foreign accounts or undisclosed foreign entities, the taxpayer will not be eligible to come in under the IRS's Voluntary Disclosure Practice.

8. I have an offshore merchant account upon which I have not reported all of the income. Can I come in under the IRS's voluntary disclosure practice?

Yes. Taxpayers with unreported income from an offshore merchant account can make a voluntary disclosure.

9. I have properly reported all my taxable income but I only recently learned that I should have been filing FBARs in prior years to report my personal foreign bank account or to report the fact that I have signature authority over bank accounts owned by my employer. May I come forward under the voluntary disclosure practice to correct this?

The purpose for the voluntary disclosure practice is to provide a way for taxpayers who did not report taxable income in the past to voluntarily come forward and resolve their tax matters. Thus, If you reported and paid tax on all taxable income but did not file FBARs, do not use the voluntary disclosure process.

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For taxpayers who reported and paid tax on all their taxable income for prior years but did not file FBARs, you should file the delinquent FBAR reports according to the instructions and attach a statement explaining why the reports are filed late. Send copies of the delinquent FBARs, together with copies of tax returns for all relevant years, by September 23, 2009, to the Philadelphia Offshore Identification Unit at:

Internal Revenue Service 11501 Roosevelt Blvd. South Bldg., Room 2002 Philadelphia, PA 19154 Attn: Charlie Judge, Offshore Unit, DP S-611

The IRS will not impose a penalty for the failure to file the FBARs.

10. What if the taxpayer has already filed amended returns reporting the additional unreported income, without making a voluntary disclosure (i.e., quiet disclosure)?

The IRS is aware that some taxpayers have attempted so-called “quiet” disclosures by filing amended returns and paying any related tax and interest for previously unreported offshore income without otherwise notifying the IRS. Taxpayers who have already made “quiet” disclosures may take advantage of the penalty framework applicable to voluntary disclosure requests regarding unreported offshore accounts and entities. Those taxpayers must send previously submitted documents, including copies of amended returns, to their local CI office by September 23, 2009. See FAQ 5.

Taxpayers are strongly encouraged to come forward under the Voluntary Disclosure Practice to make timely, accurate, and complete disclosures. Those taxpayers making “quiet” disclosures should be aware of the risk of being examined and potentially criminally prosecuted for all applicable years.

The IRS has identified, and will continue to identify, amended tax returns reporting increases in income. The IRS will be closely reviewing these returns to determine whether enforcement action is appropriate.

11. Is a taxpayer who sought relief under the IRS's Voluntary Disclosure Practice before this internal guidance was issued, eligible for the terms described in this internal guidance?

Yes. If a taxpayer sought relief under the IRS's Voluntary Disclosure Practice before this internal guidance was issued he or she may be eligible, as long as the voluntary disclosure has not yet resulted in an assessment.

12. How does the penalty framework work? Can you give us an example?

Assume the taxpayer has the following amounts in a foreign account over a period of six years. Although the amount on deposit may have been in the account for many years, it is assumed for purposes of the example that it is not unreported income in 2003.

Year	Amount on Deposit	Interest Income	Account Balance
2003	$ 1,000,000	$ 50,000	$ 1,050,000
2004		$ 50,000	$ 1,100,000
2005		$ 50,000	$ 1,150,000
2006		$ 50,000	$ 1,200,000
2007		$ 50,000	$ 1,250,000
2008		$ 50,000	$ 1,300,000

(NOTE: This example does not provide for compounded interest, and assumes the taxpayer is in the 35-percent tax bracket, files a return but does not include the foreign account or the interest income on the return, and the maximum applicable penalties are imposed.)

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If the taxpayer comes forward and has their voluntary disclosure accepted by the IRS, they face this potential scenario:

They would pay $386,000 plus interest. This includes:

- Tax of $105,000 (six years at $17,500) plus interest,
- An accuracy-related penalty of $21,000 (i.e., $105,000 × 20%), and
- An additional penalty, in lieu of the FBAR and other potential penalties that may apply, of $260,000 (i.e., $1,300,000 × 20%).

If the taxpayer didn't come forward and the IRS discovered their offshore activities, they face up to $2,306,000 in tax, accuracy-related penalty, and FBAR penalty. The taxpayer would also be liable for interest and possibly additional penalties, and an examination could lead to criminal prosecution.

The civil liabilities potentially include:

- The tax and accuracy-related penalty, plus interest, as described above,
- FBAR penalties totaling up to $2,175,000 for willful failures to file complete and correct FBARs (2003- $100,000, 2004 - $100,000, 2005 - $100,000, 2006 - $600,000, 2007 - $625,000 and 2008 - $650,000),
- The potential of having the fraud penalty (75 percent) apply, and
- The potential of substantial additional information return penalties if the foreign account or assets is held through a foreign entity such as a trust or corporation and required information returns were not filed.

Note that if the foreign activity started more than six years ago, the Service may also have the right to examine additional years.

13. What years are included in the 6-year period?

A taxpayer is expected to file correct delinquent or amended tax returns for tax year 2008 back to 2003.

14. What are some of the criminal charges I might face if I don't come in under voluntary disclosure and the IRS finds me?

Possible criminal charges related to tax returns include tax evasion (26 U.S.C. § 7201), filing a false return (26 U.S.C. § 7206(1)) and failure to file an income tax return (26 U.S.C. § 7203). The failure to file an FBAR and the filing of a false FBAR are both violations that are subject to criminal penalties under 31 U.S.C. § 5322.

A person convicted of tax evasion is subject to a prison term of up to five years and a fine of up to $250,000. Filing a false return subjects a person to a prison term of up to three years and a fine of up to $250,000. A person who fails to file a tax return is subject to a prison term of up to one year and a fine of up to $100,000. Failing to file an FBAR subjects a person to a prison term of up to ten years and criminal penalties of up to $500,000.

15. What are some of the civil penalties that might apply if I don't come in under voluntary disclosure and the IRS finds me? How do they work?

The following is a summary of potential reporting requirements and civil penalties that could apply to a taxpayer, depending on his or her particular facts and circumstances.

- A penalty for failing to file the Form TD F 90-22.1 (Report of Foreign Bank and Financial Accounts, commonly known as an "FBAR"). United States citizens, residents and certain other persons must annually report their direct or indirect financial interest in, or signature authority (or other authority that is comparable to signature authority) over, a financial account that is maintained with a financial institution located in a foreign country if, for any calendar year, the aggregate value of all foreign accounts exceeded $10,000 at any time during the year. Generally, the civil penalty for willfully failing to file an FBAR can be as high as the greater of $100,000 or 50 percent of the total balance of the

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foreign account. See 31 U.S.C. § 5321(a)(5). Nonwillful violations are subject to a civil penalty of not more than $10,000.

- A penalty for failing to file Form 3520, Annual Return to Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts. Taxpayers must also report various transactions involving foreign trusts, including creation of a foreign trust by a United States person, transfers of property from a United States person to a foreign trust and receipt of distributions from foreign trusts under section 6048. This return also reports the receipt of gifts from foreign entities under section 6039F. The penalty for failing to file each one of these information returns, or for filing an incomplete return, is 35 percent of the gross reportable amount, except for returns reporting gifts, where the penalty is five percent of the gift per month, up to a maximum penalty of 25 percent of the gift.

- A penalty for failing to file Form 3520-A, Information Return of Foreign Trust With a U.S. Owner. Taxpayers must also report ownership interests in foreign trusts, by United States persons with various interests in and powers over those trusts under section 6048(b). The penalty for failing to file each one of these information returns or for filing an incomplete return, is five percent of the gross value of trust assets determined to be owned by the United States person.

- A penalty for failing to file Form 5471, Information Return of U.S. Person with Respect to Certain Foreign Corporations. Certain United States persons who are officers, directors or shareholders in certain foreign corporations (including International Business Corporations) are required to report information under sections 6035, 6038 and 6046. The penalty for failing to file each one of these information returns is $10,000, with an additional $10,000 added for each month the failure continues beginning 90 days after the taxpayer is notified of the delinquency, up to a maximum of $50,000 per return.

- A penalty for failing to file Form 5472, Information Return of a 25% Foreign-Owned U.S. Corporation or a Foreign Corporation Engaged in a U.S. Trade or Business. Taxpayers may be required to report transactions between a 25 percent foreign-owned domestic corporation or a foreign corporation engaged in a trade or business in the United States and a related party as required by sections 6038A and 6038C. The penalty for failing to file each one of these information returns, or to keep certain records regarding reportable transactions, is $10,000, with an additional $10,000 added for each month the failure continues beginning 90 days after the taxpayer is notified of the delinquency, up to a maximum of $50,000 per return.

- A penalty for failing to file Form 926, Return by a U.S. Transferor of Property to a Foreign Corporation. Taxpayers are required to report transfers of property to foreign corporations and other information under section 6038B. The penalty for failing to file each one of these information returns is ten percent of the value of the property transferred, up to a maximum of $100,000 per return, with no limit if the failure to report the transfer was intentional.

- A penalty for failing to file Form 8865, Return of U.S. Persons With Respect to Certain Foreign Partnerships. United States persons with certain interests in foreign partnerships use this form to report interests in and transactions of the foreign partnerships, transfers of property to the foreign partnerships, and acquisitions, dispositions and changes in foreign partnership interests under sections 6038, 6038B, and 6046A. Penalties include $10,000 for failure to file each return, with an additional $10,000 added for each month the failure continues beginning 90 days after the taxpayer is notified of the delinquency, up to a maximum of $50,000 per return, and ten percent of the value of any transferred property that is not reported, subject to a $100,000 limit.

- Fraud penalties imposed under sections 6651(f) or 6663. Where an underpayment of tax, or a failure to file a tax return, is due to fraud, the taxpayer is liable for penalties that, although calculated differently, essentially amount to 75 percent of the unpaid tax.

- A penalty for failing to file a tax return imposed under section 6651(a)(1). Generally, taxpayers are required to file income tax returns. If a taxpayer fails to do so, a penalty of 5 percent of the balance due, plus an additional 5 percent for each month or fraction thereof during which the failure continues may be imposed. The penalty shall not exceed 25 percent.

- A penalty for failing to pay the amount of tax shown on the return under section 6651(a)(2). If a taxpayer fails to

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pay the amount of tax shown on the return, he or she may be liable for a penalty of .5 percent of the amount of tax shown on the return, plus an additional .5 percent for each additional month or fraction thereof that the amount remains unpaid, not exceeding 25 percent.

- An accuracy-related penalty on underpayments imposed under section 6662. Depending upon which component of the accuracy-related penalty is applicable, a taxpayer may be liable for a 20 percent or 40 percent penalty.

16. Why did the IRS pick 6 months?

The March 23, 2009 memorandum communicating the approved penalty framework for resolving the civil side of offshore voluntary disclosures is effective for 6 months because the Service intends to re-evaluate the framework at that time. Six months is a reasonable time to close out a number of voluntary disclosures, evaluate our experience and the feedback from the practitioner community, and decide whether or how to continue the practice going forward.

17. What happens at the end of 6 months? Will I get a better deal if I wait to see what the IRS does at the end of 6 months?

Taxpayers should not wait until the end of the 6-month period to make their voluntary disclosures as there is no guarantee that the taxpayer will still be eligible or that the current penalty terms will be available after 6 months.

Taxpayers who wait until the end of the 6-month period run the risk that they will be disqualified from the Voluntary Disclosure Practice. The IRS has stepped up its enforcement efforts, including the use of John Doe summonses, to identify taxpayers using offshore accounts and entities to avoid tax. In addition, the IRS continues to receive information from whistleblowers and other taxpayers making voluntary disclosures. If the IRS receives specific information about a taxpayer's noncompliance before the taxpayer attempts to make a voluntary disclosure, the disclosure will not be timely and the taxpayer will not be eligible for the criminal and civil penalty relief available under the voluntary disclosure practice. Finally, taxpayers run a substantial risk that the uniform penalty structure described in the internal guidance will not be available past the 6-month deadline or that the terms will be less beneficial to taxpayers.

18. What should I do if I am having difficulty obtaining my records from overseas?

Our experience with offshore cases in recent years is that taxpayers are successful in retrieving copies of statements and other records from foreign banks when they genuinely attempt to do so. If assistance is needed, the agent assigned to a case will work with the taxpayer in preparing a request that should be acceptable to the foreign bank. The penalty framework described in the March 23 memorandum will apply to all voluntary disclosures in process within the 6-month timeframe, so difficulty in completing a voluntary disclosure started during that period will not disqualify a cooperative taxpayer from the penalty relief. The key is to notify the Service of your intent to make a voluntary disclosure as soon as possible, and in any event, by September 23, 2009.

19. Are entities, such as corporations, partnerships and trusts eligible to make voluntary disclosures?

Yes, entities are eligible to participate in the IRS's Voluntary Disclosure Practice.

20. Does the twenty percent penalty apply to entitles? Does the twenty percent penalty apply only to cash and securities held in foreign accounts or entities or to tangible and Intangible assets as well?

The twenty percent penalty applies to entities. The twenty percent penalty applies to all assets (or at least the taxpayer's share) held by foreign entities (e.g., trusts and corporations) for which the taxpayer was required to file information returns, as well as all foreign assets (e.g., financial accounts, tangible assets such as real estate or art, and intangible assets

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such as patents or stock or other interests in a U.S. business) held or controlled by the taxpayer.

21. Are taxpayers required to complete a questionnaire as part of the voluntary disclosure practice?

There is no specific questionnaire for taxpayers to complete.

22. Is there a list of questions taxpayers are expected to answer as part of the voluntary disclosure process?

There is no standard list of questions for these cases. The Service may require an interview with the taxpayer making a voluntary disclosure, depending on the facts of each case.

23. When determining the highest amount in each undisclosed foreign account for each year or the highest asset balance of all undisclosed foreign entities for each year, what exchange rate should be used?

Convert foreign currency by using the foreign currency exchange rate at the end of the year. In valuing currency of a country that uses multiple exchange rates, use the rate that would apply if the currency in the account were converted into United States dollars at the close of the calendar year. Each account is to be valued separately.

24. Will I have to file or amend my old tax returns?

Yes. Any tax return not filed during the previous 6-year period that was otherwise required to be filed by law, must be filed by the taxpayer. In addition, any inaccurate returns for any of the 6 years must be amended by the taxpayer.

25. Besides federal income tax returns, what forms or other returns must be filed?

- Copies of original and amended federal income tax returns for tax periods covered by the voluntary disclosure;
- Complete and accurate amended federal income tax returns (or original returns, if not previously filed) of the taxpayer for all tax years covered by the voluntary disclosure;
- An explanation of previously unreported or underreported income or incorrectly claimed deductions or credits related to undisclosed foreign accounts or undisclosed foreign entities, including the reason(s) for the error or omission;
- If the taxpayer is a decedent's estate, or is an individual who participated in the failure to report the foreign account or foreign entity in a required gift or estate tax return, either as executor or advisor, complete and accurate amended estate or gift tax returns (original returns, if not previously filed) necessary to correct the underreporting of assets held in or transferred through undisclosed foreign accounts or foreign entities;
- Complete and accurate amended information returns required to be filed by the taxpayer, including, but not limited to, Forms 3520, 3520-A, 5471, 5472, 926 and 8865 (or originals, if not previously filed) for all tax years covered by the voluntary disclosure, for which the taxpayer requests relief; and
- Complete and accurate Form TD F 90.22-1, *Report of Foreign Bank and Financial Accounts*, for foreign accounts maintained during calendar years covered by the voluntary disclosure.

26. If I had an FBAR reporting obligation for years covered by the voluntary disclosure, what version of the Form TD F 90-22.1 should I use to report my interests in foreign accounts?

[Revised June 24, 2009] Taxpayers should use the current version of Form TD F 90-22.1, (revised in October 2008), to file delinquent FBARs to report foreign accounts maintained in prior years. The taxpayer may, however, rely on the instructions for the prior version of the form (revised in July 2000) for purposes of determining who must file to report foreign accounts maintained in 2008 and prior calendar years.

Although the FBAR was revised in October 2008, IRS News Release IR-2009-58 (June 5, 2009) and IRS Announce-

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ment 2009-51, both available at http:// www.irs.gov/newsroom/article/0,,id=209418,00.html, permit the use of the definition of “United States person” in the prior version of the FBAR in determining who must file FBARs that are due on June 30, 2009. Accordingly, for all FBARs that are due in the current and prior years, the term “United States person” means (1) a citizen or resident of the United States; (2) a domestic partnership; (3) a domestic corporation; or (4) a domestic estate or trust.

27. If I don't have the ability to full pay can I still participate in the IRS's Voluntary Disclosure Practice?

Yes. The March 23, 2009 guidance requires the taxpayer to fully pay all taxes and interest for all years covered, and the Voluntary Disclosure penalty, as well as all other unpaid, previously assessed liabilities, when the signed closing agreement is returned to the Service. However, it is possible for a taxpayer who is unable to make full payment at that time to submit a request that includes other payment arrangements acceptable to the IRS.

The burden will be on the taxpayer to establish inability to pay, to the satisfaction of the IRS, based on full disclosure of all assets and income sources, domestic and offshore, under the taxpayer's control. Assuming that the IRS determines that the inability to fully pay is genuine, the taxpayer must work out other financial arrangements, acceptable to the IRS, to resolve all outstanding liabilities, in order to be entitled to the penalty relief set forth in the March 23, 2009 guidance.

28. If the taxpayer and the IRS cannot agree to the terms of the closing agreement, will mediation with Appeals be an option with respect to the terms of the closing agreement?

No. The penalty framework and the agreement to limit tax exposure to the most recent 6 years are package terms. If any part of the penalty framework is unacceptable to the taxpayer, the case will be examined and all applicable penalties may be imposed. Any tax and penalties imposed by the Service on examination may be appealed, but not the Service's decision on the terms of the closing agreement applying the penalty framework.

29. I have a client who may be eligible to make a voluntary disclosure. What are my responsibilities to my client under Circular 230?

The IRS expects taxpayers to seek qualified legal advice and representation in connection with considering and making a voluntary disclosure. If a taxpayer seeks the advice of a tax practitioner but nonetheless decides not to make a voluntary disclosure despite the taxpayer's noncompliance with Untied States tax laws, Circular 230, section 10.21, requires the practitioner to advise the client of the fact of the client's noncompliance and the consequences of the client's noncompliance as provided under the Code and regulations.

30. Can I talk to the IRS without revealing my client's identity?

Hypothetical situations present a potential for misunderstanding that exists when there is no assurance that the hypothetical contains all relevant facts. In addition, tax practitioners should be aware that posing a situation as a hypothetical does not satisfy the requirements of making a voluntary disclosure. If the IRS receives information relating specifically to the taxpayer's undisclosed foreign accounts or undisclosed foreign entities while the hypothetical question is pending, the taxpayer may become ineligible to make a voluntary disclosure.

If practitioners have questions about the terms of the voluntary disclosure program, they should contact the IRS Voluntary Disclosure Hotline at (215) 516-4777, visit www.irs.gov, or contact their nearest CI office with questions. For a list of CI offices, visit: http:// www.irs.gov/compliance/enforcement/article/0,,id=205909,00.html

Additional Frequently Asked Questions — Posted June 24, 2009

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31. How can the IRS propose adjustments to tax for a six-year period without either an agreement from the taxpayer or a statutory exception to the normal three-year statute of limitations for making those adjustments?

Going back six years is part of the resolution offered by the IRS for resolving offshore voluntary disclosures. The taxpayer must agree to assessment of the liabilities for those years in order to get the benefit of the reduced penalty framework. If the taxpayer does not agree to the tax, interest and penalty proposed by the voluntary disclosure examiner, the case will be referred to the field for a complete examination. In that examination, normal statute of limitations rules will apply. If no exception to the normal three-year statute applies, the IRS will only be able to assess tax, penalty and interest for three years. However, if the period of limitations was open because, for example, the IRS can prove a substantial omission of gross income, six years of liability may be assessed. Similarly, if there was a failure to file certain information returns, such as Form 3520 or Form 5471, the statute of limitations will not have begun to run. If the IRS can prove fraud, there is no statute of limitations for assessing tax.

32. If a taxpayer's violation includes unreported individual foreign accounts and business accounts (for an active business), does the 20 percent offshore penalty include the business accounts?

Yes. Assuming that there is unreported income with respect to all the accounts, they all will be included in the penalty base. No distinction is to be drawn based on whether the account is a business account or a savings or investment account.

33. If the lookback period is 2003-2008, what does the taxpayer do if the taxpayer held foreign real estate, sold it in 2002, and did not report the gain on his 2002 return? Does the taxpayer compute the 20 percent on the highest aggregate balance in 2003-2008? What, if anything, does IRS expect the taxpayer to do with respect to 2002?

Gain realized on a foreign transaction occurring before 2003 does not need to be included as part of the voluntary disclosure. If the proceeds of the transaction were repatriated and were not offshore after January 1, 2003, they will not be included in the base for the 20 percent offshore penalty. On the other hand, if the proceeds remained offshore after January 1, 2003, and the income in the account was not reported, they will be included in the base for the penalty.

34. If, after making a voluntary disclosure, a taxpayer disagrees with the 20 percent offshore penalty, what can the taxpayer do?

If any part of the penalty structure is unacceptable to a taxpayer, that case will follow the standard audit process. All relevant years and issues will be subject to a complete examination. At the conclusion of the examination, all applicable penalties (including information return and FBAR penalties) will be imposed. Those penalties could be substantially greater than the 20 percent penalty. If the case is unagreed, the taxpayer will have recourse to Appeals.

35. Will examiners have any discretion to settle cases? For example, if a penalty for failing to file a Form 5471 for 6 years is $10,000 per year, will that be compared to 20 percent of the corporation's asset value? Would the lesser amount apply?

Voluntary disclosure examiners do not have discretion to settle cases for amounts less than what is properly due and owing. These examiners will compare the 20 percent offshore penalty to the total penalties that would otherwise apply to a particular taxpayer. Under no circumstances will a taxpayer be required to pay a penalty greater than what he would otherwise be liable for under existing statutes. If the taxpayer disagrees with the IRS's determination, as set forth in the closing agreement, the taxpayer may request that the case be referred for a standard examination of all relevant years and issues. At the conclusion of this examination, all applicable penalties, including information return penalties and FBAR

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penalties, will be imposed. If, after the standard examination is concluded the case is closed unagreed, the taxpayer will have recourse to Appeals. See FAQ 34.

36. Re: FAQ 12 Does interest run on any of the penalties? If so, which ones and from what date does interest accrue?

With regard to the accuracy-related and delinquency penalties, interest runs from the due date of the return in question. With regard to all other penalties, interest runs from the date of assessment of the penalty.

37. Re: FAQ 20 A taxpayer owns valuable land and artwork located in a foreign jurisdiction. This property produces no income and there were no reporting requirements regarding this property. Must the taxpayer report the land and artwork and pay a 20 percent penalty?

FAQ 20 relates to income producing property for which no income was reported. Under those circumstances, no distinction is made between assets held directly and assets held through an entity in computing the 20 percent offshore penalty. However, if the taxpayer owns nonincome producing property in the taxpayer's own name, there has been no U.S. taxable event and no reporting obligation to disclose. The taxpayer will be required to report any current income from the property or gain from its sale or other disposition at such time in the future as the income is realized. Because there has as yet been no tax noncompliance, the 20 percent offshore penalty would not apply to those assets. If the foreign assets were held in the name of an entity such as a trust or corporation, there would have been an information return filing obligation that may need to be disclosed. See FAQ 42.

38. If a taxpayer transferred funds from one unreported foreign account to another between 2003 and 2008, will he have to pay a 20 percent offshore penalty on both accounts?

No. If the taxpayer can establish that funds were transferred from one account to another, any duplication will be removed before calculating the 20 percent penalty. However, the burden will be on the taxpayer to establish the extent of the duplication.

39. How is the 20 percent offshore penalty computed if the taxpayer has multiple accounts or entities where the highest value of some accounts is not in the same year? Are separate penalties determined at the rate of 20 percent for each account or entity value?

The values of accounts and other assets are aggregated for each year and the penalty is calculated at 20 percent of the highest year's aggregate value.

40. A taxpayer has two offshore accounts. No FBARs were filed. The taxpayer reported all income from one account but not the other. Mechanically, how does the taxpayer report this? Does the taxpayer report both accounts as a voluntary disclosure or bifurcate it into a delinquent FBAR filing for the reported account and a voluntary disclosure for the unreported account?

Because the annual FBAR requirement is to file a single report reporting all foreign accounts meeting the reporting requirement, it is not possible to bifurcate the corrected filing. The taxpayer should make a voluntary disclosure for the omitted income and include the delinquent FBARs with respect to both accounts. The account with no income tax issue is unrelated to the taxpayer's tax noncompliance, so no penalty will be imposed with respect to that account. See FAQ 9.

41. If, in addition to other noncompliance, a taxpayer has failed to file an FBAR to report an account over which the taxpayer has signature authority but no beneficial interest (e.g., an account owned by his employer), will that

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foreign account be included in the base for calculating the taxpayer's 20 percent offshore penalty?

No. The account on which the taxpayer has mere signature authority will be treated as unrelated to the tax noncompliance the taxpayer is voluntarily disclosing. The taxpayer may cure the FBAR delinquency for the account the taxpayer does not own by filing the FBAR with an explanatory statement by September 23, 2009. See FAQ 9. The answer might be different (1) if the account over which the taxpayer has signature authority is held in the name of a related person, such as a family member or a corporation controlled by the taxpayer; (2) if the account is held in the name of a foreign corporation or trust for which the taxpayer had a Title 26 reporting obligation; or (3) if the account was related in some other way to the taxpayer's tax noncompliance. In these cases, the taxpayer will be liable for the 20 percent offshore penalty if there is unreported income on the account. On the other hand, if there is no unreported income with respect to the account, no penalty will be imposed under the rationale of FAQ 40.

42. FAQ 9 states that a taxpayer who only failed to file an FBAR should not use this process. What about a taxpayer who only has delinquent Form 5471s or Form 3520s but no tax due? Does that taxpayer fall outside this voluntary disclosure process?

A taxpayer who has failed to file tax information returns, such as Form 5471 for controlled foreign corporations (CFCs) or Form 3520 for foreign trusts but who has reported and paid tax on all their taxable income with respect to all transactions related to the CFCs or foreign trusts, should file delinquent information returns with the appropriate service center according to the instructions for the form and attach a statement explaining why the information returns are filed late. (The Form 5471 should be submitted with an amended return showing no change to income or tax liability.) Send copies of the delinquent information returns, together with copies of tax returns for all relevant years, by September 23, 2009, to the Philadelphia Offshore Identification Unit at:

Internal Revenue Service 11501 Roosevelt Blvd. South Bldg., Room 2002 Philadelphia, PA 19154 Attn: Charlie Judge, Offshore Unit, DP S-611

The IRS will not impose a penalty for the failure to file the information returns.

43. Re: FAQ 9 A taxpayer recently learned that they have an FBAR filing obligation but they do not have sufficient time to gather the information necessary to properly file the FBAR by the June 30, 2009 due date. How should the taxpayer proceed?

Taxpayers who reported and paid tax on all their 2008 taxable income but only recently learned of their FBAR filing obligation and have insufficient time to gather the necessary information to complete the FBAR, should file the delinquent FBAR report according to the instructions and attach a statement explaining why the report is filed late. Send a copy of the delinquent FBAR, together with a copy of the 2008 tax return, by September 23, 2009, to the Philadelphia Offshore Identification Unit at the address in FAQ 9.

In this situation, the IRS will not impose a penalty for the failure to file the FBAR.

Additionally, if all 2008 taxable income with respect to a foreign financial account is timely reported and a United States person only recently learned they have a 2008 FBAR obligation and there is insufficient time to gather the necessary information to complete the FBAR, the United States person may follow the procedures set forth above and no penalty will be imposed.

For 2008 tax returns due after September 23, 2009, the tax return does not need to accompany the 2008 FBAR.

44. Re: FAQ 12 The due date for the 2008 FBAR is June 30, 2009. Should a taxpayer file a 2008 FBAR in the normal manner or should a taxpayer submit it with the voluntary disclosure request?

Except as described in FAQ 43, the taxpayer should timely file the 2008 FBAR in the normal manner by the June 30,

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2009 deadline and submit an additional copy with the taxpayer's voluntary disclosure.

45. If a taxpayer is uncertain about whether he is required to file an FBAR with respect to a particular foreign account, how can the taxpayer get help with this question?

Help with questions about FBAR filing requirements is available on the FBAR Hotline at 1-800-800-2877. When the call is answered, select option 2. You can also submit written questions about the FBAR rules by e-mail addressed to FBARQuestions@irs.gov. The instructions to the FBAR form are available at www.irs.gov. Do not call the Voluntary Disclosure Hotline with questions about whether you have an FBAR filing requirement. The purpose of the Voluntary Disclosure Hotline is to answer questions about how to make voluntary disclosures and what penalties apply, assuming a taxpayer was required to file.

46. A taxpayer moved to the U.S. in 2007 and is now a permanent resident of the U.S. The taxpayer had a requirement to file an FBAR for one year but failed to do so. Is the taxpayer subject to a penalty equal to 20 percent of the account?

First, the taxpayer should confirm that the taxpayer had an FBAR filing requirement. Assuming that the taxpayer was required to report the interest earned on the account during the year the taxpayer was in the U.S. and failed to do so, the taxpayer is subject to a penalty based on the high account balance during the year. The penalty may be limited to five percent if the taxpayer did not avoid U.S. tax with respect to the deposits and if the account was passively held during the year the taxpayer was in the U.S. If there was no unreported taxable income related to the unreported foreign accounts that would have been reported on the FBAR, the taxpayer will not be subject to the 20 percent offshore penalty. In that case, the taxpayer should file delinquent FBARs attaching a statement explaining why the FBAR was not timely filed. For more information, see FAQ 9.

47. If parents have a jointly owned foreign account on which they have made their children signatories, the children have an FBAR filing requirement but no income. Should the children just file delinquent FBARs as described by FAQ 9 and have the parents submit a voluntary disclosure? Will both parents be penalized 20 percent each? Will each have a 20 percent penalty on 50 percent of the balance?

Only one 20 percent offshore penalty will be applied with respect to voluntary disclosures relating to the same account. In the example, the parents will be jointly required to pay a single 20 percent penalty on the account. This can be through one parent paying the total penalty or through each paying a portion, at the taxpayers option. For those signatories with no ownership interest in the account, such as the children in these facts, they may file delinquent FBARs with no penalty as described in FAQs 9 and 41. However, any joint account owner who does not make a voluntary disclosure may be examined and subject to all appropriate penalties.

48. If there are multiple individuals with signature authority over a trust account, does everyone involved need to file delinquent FBARs? If so, could everyone be subject to a 20 percent offshore penalty?

Only one 20 percent offshore penalty will be applied with respect to voluntary disclosures relating to the same account. The penalty may be allocated among the taxpayers making the disclosures in any way they choose. The reporting requirements for filing an FBAR, however, do not change. Therefore, every individual who is required to file an FBAR must file one.

49. Re: FAQ 10 Some taxpayers have made quiet disclosures by filing amended returns. Will the IRS audit these taxpayers? If so, will they be eligible for the 20 percent offshore penalty? Is the IRS really going to prosecute

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someone who filed an amended return and correctly reported all their income?

The IRS is reviewing amended returns and could select any amended return for examination. If a return is selected for examination, the 20 percent offshore penalty would not be available. When criminal behavior is evident and the disclosure does not meet the requirements of a voluntary disclosure under IRM 9.5.11.9, the IRS may recommend criminal prosecution to the Department of Justice. Taxpayers who have already made quiet disclosures but have not yet been selected for examination may take advantage of the penalty framework applicable to voluntary disclosure requests regarding unreported offshore accounts and entities, provided they otherwise meet the criteria for voluntary disclosure set forth in IRM 9.5.11.9. Those taxpayers must send previously submitted documents, including copies of amended returns, to their local CI office by September 23, 2009. See FAQs 4 and 10 for more information.

50. What is the distinction between filing amended returns to correct errors and filing a voluntary disclosure?

An amended return is the proper vehicle to correct an error on a filed return, whether a taxpayer receives a refund or owes additional tax. A voluntary disclosure is a truthful, timely and complete communication to the IRS in which a taxpayer shows a willingness to cooperate (and does in fact cooperate) with the IRS in determining the taxpayer's correct tax liability and makes arrangements in good faith to fully pay that liability. Filing correct amended returns is normally a part of the process of making a voluntary disclosure under IRM 9.5.11.9.

Taxpayers and practitioners trying to decide whether to simply file an amended return with a Service Center or to make a formal voluntary disclosure under the process described in IRM 9.5.11.9 and the March 23, 2009 memoranda should consider the nature of the error they are trying to correct. Taxpayers with undisclosed foreign accounts or entities should consider making a voluntary disclosure because it enables them to become compliant, avoid substantial civil penalties and generally eliminate the risk of criminal prosecution. Making a voluntary disclosure also provides the opportunity to calculate, with a reasonable degree of certainty, the total cost of resolving all offshore tax issues. It is anticipated that the voluntary disclosure process is appropriate for most taxpayers who have underreported their income with respect to offshore accounts and assets. However, there will be some cases, such as where a taxpayer has reported all income but failed to file the FBAR (FAQ 9), or only failed to file information returns (FAQ 42), where it remains appropriate for the taxpayer to simply file amended returns with the applicable Service Center (with copies to the Philadelphia office listed in FAQ 9).

51. If the Service has served a John Doe summons seeking information that may identify a taxpayer as holding an undisclosed foreign account or undisclosed foreign entity, does that make the taxpayer ineligible to make a voluntary disclosure in accordance with the March 23, 2009 guidance?

No. The mere fact that the Service served a John Doe summons does not make every member of the John Doe class ineligible to participate. However, once the Service obtains information under a John Doe summons that provides evidence of a specific taxpayer's noncompliance with the tax laws, that particular taxpayer may become ineligible. For this reason, a taxpayer concerned that a party served with a John Doe summons will provide information about them to the Service should apply to make a voluntary disclosure as soon as possible.

Offshore Voluntary Disclosures — Optional Format

If taxpayer has domestic issues only, please have them contact their local Criminal Investigation office for a traditional voluntary disclosure.

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<DATE>

Internal Revenue Service
Criminal Investigation
ATTN: Voluntary Disclosure Coordinator
<CITY Field Office>
<Address>
<CITY, ST ZIP CODE>
Re: Taxpayer Name
Tax Identification Number
Taxpayer Date of Birth
Taxpayer Address

Dear Voluntary Disclosure Coordinator:

To assist in a timely determination of my acceptance into the Voluntary Disclosure Program, (*for Voluntary Disclosures involving offshore accounts or assets)*. I have addressed *all* of the following items:

- Please include your:
  - Complete name:
  - Social Security Number:
  - DOB:
  - Address:
  - Passport Number (and Country):
  - Current Occupation
- Taxpayer Representative and his/her contact information.
- Explain the source of the funds.
- Disclose if you or any related entities are currently under audit or criminal investigation by the Internal Revenue Service or any other law enforcement authority.
  - Has the IRS notified you that it intends to commence an examination or investigation? **Yes No**
  - Are you under criminal investigation by any law enforcement authority? **Yes No**
  - If yes, please explain.
- Do you believe that the IRS has obtained information concerning your tax liability? **Yes No**
  - If yes, please specify.
- Please check the box to estimate the annual range of the highest aggregate *value* of your offshore accounts/assets.

Highest Aggregate Account/Asset Value	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**
$0 to $100,000						
$100,000 to $1,000,000						
$1,000,000 to $2,500,000						
$2,500,000 to						

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$10,000,000						
Greater than $10,000,000						
Greater than $100,000,000						

• Please check the box to estimate the potential total unreported *income* from the offshore account(s) during each disclosure period. If known, please enter exact amounts/assets.

Estimated Total Unreported Income	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**
$0 to $100,000						
$100,000 to $1,000,000						
$1,000,000 to $2,500,000						
$2,500,000 to $10,000,000						
Greater than $10,000,000						

• For accounts or assets where you have control or are a beneficial owner of the account or asset, list any and all financial institutions and the country where the institution is located. For accounts, please also list the dates the accounts were opened and/or closed. Provide your point of contact at each financial institution.

• Explain the purpose for establishing the offshore account or assets. For example: Holocaust Compensation or Restitution; inherited account; account established prior to World War II, etc.; if tax non-compliance — please explain.

• List each person or entity affiliated with the account, their formal structure (i.e., if a corporation, foundation, or trust), and the nature of their relationship to the account (i.e. owner, power of attorney, parent entity of corporate account holder, etc.).

• Explain all face to face meetings, and any other communications you had regarding the accounts or assets with the financial institution(s). Also include face to face meetings or communications regarding the accounts or assets with independent advisors/investment managers not from the financial institution(s) where the funds are held. Provide the names, locations and dates of these meetings and/or communications.

To be included with all letters:

By signing this document, I certify that I am willing to continue to cooperate with the Internal Revenue Service, including in assessing my income tax liabilities and making good faith arrangements to pay all taxes, interest, and penalties associated with this voluntary disclosure.

Under penalties of perjury, I declare that I have examined this document and accompanying statements, and to the best of my knowledge and belief, they are true, correct, and complete.

——————————   ——————————   ——————————

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Signature of Taxpayer	Print Name	Date

IRS reserves the right to make further contacts with the taxpayer to clarify his/her submission.

Contact IRS About Voluntary Disclosure

The IRS stresses that acceptance into a voluntary disclosure arrangement depends on the individual facts and circumstances involved in each case. Taxpayers with unreported income should immediately discuss with their tax professional their options to get right with the government, including taking advantage of coming in voluntarily.

A voluntary disclosure occurs when the communication is truthful, timely, complete, and when: A taxpayer shows a willingness to cooperate (and does in fact cooperate) with the IRS in determining his/her correct tax liability.

For a complete understanding of the voluntary disclosure procedures, see Internal Revenue Manual (IRM) 9.5.11.9

Taxpayers cannot rely on the fact that other similarly situated taxpayers may not have been recommended for criminal prosecution. Also, a voluntary disclosure will not automatically guarantee immunity from prosecution; however, a voluntary disclosure may result in prosecution not being recommended. This practice does not apply to taxpayers with illegal source income.

Tax professionals or individuals who want to make a voluntary disclosure, may call the phone number below associated with the State in which the taxpayer resides. Or taxpayers may send a letter to the IRS providing all of the requested information and mailing the signed letter to the appropriate address listed below.

These phone numbers are for the purpose of making voluntary disclosures ONLY.

Alabama	404-338-7540	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Atlanta Field Office 401 W. Peachtree Street, N.W. Suite 600, STOP 400-D Atlanta, GA 30308
Alaska	907-271-6911	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Seattle Field Office 800 Fifth Avenue, Suite 3950 Seattle, WA 98104
Arizona	602-207-8964	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Phoenix Field Office 4041 N. Central Avenue Suite 112, MS 9000 Phoenix, AZ 85012-5000
Arkansas	615-250-5005	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Nashville Field Office 801 Broadway, Suite 400 Nashville, TN 37203
California - Northern	510-637-1031	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Oakland Field Office 1301 Clay Street, Suite 1780S Oakland, CA 94612
California - Southern	714-347-9226	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Los Angeles

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		Field Office 801 Civic Center Drive West Room 218, MS 8000 Santa Ana, CA 92701
Colorado	303-603-4936	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Denver Field Office PO Box 1767 Denver, CO 80201
Connecticut	617-316-2073	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Boston Field Office 1 Montvale Avenue, Room 205 Stoneham, MA 02180
Delaware	215-861-1392	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Philadelphia Field Office 600 Arch Street, Room 6224 Philadelphia, PA 19106
District of Columbia	202-874-0155	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Washington DC Field Office P.O. Box 1038 Baileys Crossroads, VA 22041
Florida - Northern	727-568-2561	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Tampa Field Office 9450 Koger Blvd, Suite 101 St. Petersburg, FL 33702
Florida - Southern	954-423-7245	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Miami Field Office 7850 SW 6th Court Plantation, FL 33324
Georgia	404-338-7540	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Atlanta Field Office 401 W. Peachtree Street, N.W. Suite 600, STOP 400-D Atlanta, GA 30308
Hawaii	808-539-2843	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Seattle Field Office 800 Fifth Avenue, Suite 3950 Seattle, WA 98104
Idaho	303-603-4936	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Denver Field Office PO Box 1767 Denver, CO 80201
Illinois	312-566-4503	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Chicago Field Office 230 South Dearborn, Room 1400 Chicago, IL 60604

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Indiana	312-566-4503	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Chicago Field Office 230 South Dearborn, Room 1400 Chicago, IL 60604
Iowa	402-233-7452	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator St. Louis Field Office 1616 Capitol Avenue, Suite 460 MS 9000 Omaha, NE 68102
Kansas	402-233-7452	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator St. Louis Field Office 1616 Capitol Avenue, Suite 460 MS 9000 Omaha, NE 68102
Kentucky	615-250-5005	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Nashville Field Office 801 Broadway, Suite 400 Nashville, TN 37203
Louisiana	504-558-1535	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator New Orleans Field Office P.O. Box 2230 New Orleans, LA 70176-2230
Maine	617-316-2073	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Boston Field Office 1 Montvale Avenue, Room 205 Stoneham, MA 02180
Maryland	202-927-9351	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Washington DC Field Office P.O. Box 1038 Baileys Crossroads, VA 22041
Massachusetts	617-316-2073	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Boston Field Office 1 Montvale Avenue, Room 205 Stoneham, MA 02180
Michigan	313-234-2410	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Detroit Field Office 985 Michigan Ave, Room 251 Detroit, Michigan 48226
Minnesota	651-767-3254	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator St. Paul Field Office 30 East 7th Street, Stop 9000 St. Paul, MN 55101
Mississippi	504-558-1535	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator New Orleans

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		Field Office P.O. Box 2230 New Orleans, LA 70176-2230
Missouri	402-233-7452	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator St. Louis Field Office 1616 Capitol Avenue, Suite 460 MS 9000 Omaha, NE 68102
Montana	303-603-4936	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Denver Field Office PO Box 1767 Denver, CO 80201
Nebraska	402-233-7452	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator St. Louis Field Office 1616 Capitol Avenue, Suite 460 MS 9000 Omaha, NE 68102
Nevada	801-799-6763	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Las Vegas Field Office 50 S. 200 E. PO Box 1466 Salt Lake City, UT 84111
New Hampshire	617-316-2073	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Boston Field Office 1 Montvale Avenue, Room 205 Stoneham, MA 02180
New Jersey	732-761-3381	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Newark Field Office P.O. Box 741 Springfield, NJ 07081
New Mexico	505-837-9033	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Phoenix Field Office 4041 N. Central Avenue Suite 112, MS 9000 Phoenix, AZ 85012-5000
New York	212-436-1588	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator New York Field Office 290 Broadway, 4th Floor New York, NY 10007
North Carolina	919-856-4283 ext 408	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Charlotte Field Office 310 New Bern Ave, Suite 210 Raleigh, NC 27601
North Dakota	701-239-5143 ext 292	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator St. Paul Field Office 30 East 7th Street, Stop 9000 St. Paul, MN 55101
Ohio	614-744-3130	IRS Criminal Investigation Attn: Volun-

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		tary Disclosure Coordinator Cincinnati Field Office P.O. Box 973 Cincinnati, OH 45201
Oklahoma	214-413-5979	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Dallas Field Office 1100 Commerce Street, Room 1222 Dallas, TX 75242
Oregon	503-326-3207	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Seattle Field Office 800 Fifth Avenue, Suite 3950 Seattle, WA 98104
Pennsylvania - Eastern	215-861-1392	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Philadelphia Field Office 600 Arch Street, Room 6224 Philadelphia, PA 19106
Pennsylvania - Western	412-395-6771	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Pittsburgh Field Office P.O. Box 534 Pittsburgh, PA 15230
Rhode Island	617-316-2073	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Boston Field Office 1 Montvale Avenue, Room 205 Stoneham, MA 02180
South Carolina	919-856-4283 ext 408	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Charlotte Field Office 310 New Bern Ave, Suite 210 Raleigh, NC 27601
South Dakota	605-330-4449 ext 266	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator St. Paul Field Office 30 East 7th Street, Stop 9000 St. Paul, MN 55101
Tennessee	615-250-5005	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Nashville Field Office 801 Broadway, Suite 400 Nashville, TN 37203
Texas - Dallas	214-413-5979	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Dallas Field Office 1100 Commerce Street, Room 1222 Dallas, TX 75242
Texas - Houston	281-721-8341	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Houston Field Office 8701 S. Gessner, Stop 9000 HAL

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		Houston, TX 77074
Texas - San Antonio	512-499-5261	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator San Antonio Field Office One International Centre 100 NE Loop 410, Suite 400 San Antonio, TX 78216
Utah	801-799-6763	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Las Vegas Field Office 50 S. 200 E. PO Box 1466 Salt Lake City, UT 84111
Vermont	617-316-2073	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Boston Field Office 1 Montvale Avenue, Room 205 Stoneham, MA 02180
Virginia	703-647-5502	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Washington DC Field Office P.O. Box 1038 Baileys Crossroads, VA 22041
Washington	206-464-4916	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Seattle Field Office 800 Fifth Avenue, Suite 3950 Seattle, WA 98104
West Virginia	412-395-6771	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Pittsburgh Field Office P.O. Box 534 Pittsburgh, PA 15230
Wisconsin	414-231-2448	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator St. Paul Field Office 30 East 7th Street, Stop 9000 St. Paul, MN 55101
Wyoming	303-603-4936	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Denver Field Office PO Box 1767 Denver, CO 80201
INTERNATIONAL		
Puerto Rico	954-423-7872	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Miami Field Office 7850 SW 6th Court Plantation, FL 33324
South America	011-571-383-2769	IRS Criminal Investigation International Section, SE:CI:OPS:I 1111 Constitution Avenue, NW Room 2547 Washington, DC 20224 Attn: International Voluntary Dis-

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		closure Coordinator
Canbbean	246-227-4143	IRS Criminal Investigation International Section, SE:CI:OPS:I 1111 Constitution Avenue, NW Room 2547 Washington, DC 20224 Attn: International Voluntary Disclosure Coordinator
Mexico & Central America	011-52-55-50-80-29-01	IRS Criminal Investigation International Section, SE:CI:OPS:I 1111 Constitution Avenue, NW Room 2547 Washington, DC 20224 Attn: International Voluntary Disclosure Coordinator
Canada	613-688-5292	IRS Criminal Investigation International Section, SE:CI:OPS:I 1111 Constitution Avenue, NW Room 2547 Washington, DC 20224 Attn: International Voluntary Disclosure Coordinator
Germany, Switzerland, Italy, Russian Federation, Eurasia, Eastern Europe, and Southern Europe	011-49-69-7535-3647 or 3638	IRS Criminal Investigation International Section, SE:CI:OPS:I 1111 Constitution Avenue, NW Room 2547 Washington, DC 20224 Attn: International Voluntary Disclosure Coordinator
United Kingdom, France, Western Europe, Africa, and Middle East	011-4420-7894-0036 or 0037	IRS Criminal Investigation International Section, SE:CI:OPS:I 1111 Constitution Avenue, NW Room 2547 Washington, DC 20224 Attn: International Voluntary Disclosure Coordinator
Far East, Australia, & South Pacific Islands	011-852-2841-2361	IRS Criminal Investigation International Section, SE:CI:OPS:I 1111 Constitution Avenue, NW Room 2547 Washington, DC 20224 Attn: International Voluntary Disclosure Coordinator
Iraq	011-964-770-443-0356	IRS Criminal Investigation International Section, SE:CI:OPS:I 1111 Constitution Avenue, NW Room 2547 Washington, DC 20224 Attn: International Voluntary Disclosure Coordinator

TAX COMPLIANCE AND ENFORCEMENT ISSUES WITH RESPECT TO OFFSHORE ACCOUNTS AND ENTITIES

Scheduled for a Public Hearing Before the SUBCOMMITTEE ON SELECT REVENUE MEASURES of the HOUSE COMMITTEE ON WAYS AND MEANS on March 31, 2009

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Prepared by the Staff of the JOINT COMMITTEE ON TAXATION

March 30, 2009

JCX-23-09

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1. European Union Savings Directive
APPENDIX

INTRODUCTION

The Subcommittee on Select Revenue Measures of the House Committee on Ways and Means has scheduled a public hearing for March 31, 2009 on issues relating to banking secrecy practices and wealthy American taxpayers. This document, [FN1] prepared by the staff of the Joint Committee on Taxation, provides background on withholding and information reporting requirements applicable to payments of U.S.-source portfolio investment income to nonresidents, the Internal Revenue Service ("IRS") Qualified Intermediary program, the effect of bank secrecy laws and practices on U.S tax compliance and enforcement efforts involving offshore accounts, and information exchange procedures under U.S. income tax treaties and tax information exchange agreements.

I. NONRESIDENT WITHHOLDING

Introduction

Under present law, nonresidents who receive payments of U.S.-source investment income are generally subject to U.S. withholding tax imposed at a 30 percent rate. This withholding tax serves as the only mechanism for collection of tax in the case of payments made to foreign persons who are not otherwise required to file a U.S. income tax return. There are, however, a number of significant statutory exemptions from the 30-percent withholding tax (including for interest paid on bank deposits, portfolio interest and most capital gains), and income tax treaties typically provide additional withholding tax relief.

Distinguishing U.S. from foreign persons is therefore important in this context. The IRS has a variety of enforcement tools (including information reporting and backup withholding) [FN2] to enforce compliance by U.S. taxpayers. The IRS faces significant enforcement challenges, however, in confirming the status of an offshore payee as a bona fide non-U.S. investor. These challenges include resource constraints (and the resulting need to rely on compliance by both U.S. and foreign intermediaries), the difficulties inherent in determining beneficial ownership of income earned through intermediate vehicles (for example, trusts or partnerships), which typically are organized under foreign law and often do not have close analogies in U.S. trust or company law practice, and disclosure limitations imposed by foreign law.

If a U.S. person can arrange to receive investment income through means that permit the U.S. person to appear to be a foreign person, the U.S. investor may be able to evade U.S. income tax entirely. This problem lies at the heart of the ongoing investigation into the role played by UBS AG ("UBS"), based in Switzerland and one of the world's largest financial institutions, in facilitating tax evasion by U.S. clients and avoidance of U.S. reporting requirements.

This section provides an overview of the nonresident withholding tax rules, particularly as those rules apply to payments of portfolio investment income by financial institutions to U.S. and nonresident customers. It then discusses briefly the enforcement challenges arising under those rules, both as a result of their substantive effect and as a matter of administration.

A. U.S. Tax Treatment of Payments to Nonresident Investors

Payments of U.S.-source "fixed and determinable annual or periodic" income, including interest, dividends, and similar types of investment income, that are made to foreign persons are subject to U.S. withholding tax at a 30 percent rate, unless the withholding agent can establish that the beneficial owner of the amount is eligible for an exemption from withholding or a reduced rate of withholding under an income tax treaty. [FN3]

The principal statutory exemptions from the 30-percent nonresident withholding tax apply to interest on bank deposits, portfolio interest and capital gains. Since 1984 the United States has imposed no tax on "portfolio interest" received by a

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nonresident individual or foreign corporation from sources within the United States. [FN4] Portfolio interest includes generally any interest (including original issue discount) other than interest received by a 10-percent shareholder, [FN5] certain contingent interest, [FN6] interest received by a controlled foreign corporation from a related person, [FN7] and interest received by a bank on an extension of credit made pursuant to a loan agreement entered into in the ordinary course of its trade or business. [FN8]

In the case of interest paid on a debt obligation that is in registered form, [FN9] the portfolio interest exemption is available only to the extent that the U.S. person otherwise required to withhold tax (the "withholding agent") has received a statement made by the beneficial owner of the obligation (or a securities clearing organization, bank or other financial institution that holds customers' securities in the ordinary course of its trade or business) that the beneficial owner is not a United States person. [FN10] This certification of non-U.S. ownership most commonly is made on an IRS Form W-8.

U.S. tax law also contemplates that U.S. issuers (other than the United States itself) may issue debt obligations in bearer form. Historically, in such cases, a holder would present a physical interest coupon for payment free of U.S. withholding tax, without that holder being required to provide any certification of non-U.S. ownership. Now, however, so-called "bearer bonds" are typically held in "dematerialized" (or electronic) form, much like debt obligations that are issued in registered form; their "bearer" status arises solely from the fact that a holder may request a physical certificate with interest coupons from the issuer. As a practical matter, such requests for physical certificates are extremely rare. Nonetheless, the principal U.S. tax enforcement focus for "bearer bonds" rests on the historical premise that these bonds are actually held in physical form and relates to their mode of original distribution. More particularly, (i) the obligation must be offered and sold pursuant to arrangements that are reasonably designed to ensure that the obligation will be sold in connection with its original issuance only to a non-United States person, (ii) interest on the obligation must be payable only outside the United States, and (iii) the obligation must bear a legend to the effect that any United States person who holds the obligation will be subject to limitations under the U.S. income tax laws. [FN11]

Interest on deposits with foreign branches of domestic banks and domestic savings and loan associations is not treated as U.S.-source income and is thus exempt from U.S. withholding tax (regardless of whether the recipient is a U.S. or foreign person). [FN12] In addition, interest on bank deposits, deposits with domestic savings and loan associations, and certain amounts held by insurance companies are not subject to the U.S. withholding tax when paid to a foreign person, unless the interest is effectively connected with a U.S. trade or business of the recipient. [FN13] Similarly, interest and OID on certain short-term obligations is also exempt from the U.S. withholding tax when paid to a foreign person. [FN14] Consequently, there is no information reporting on Form 1042-S with respect to payments of such amounts. [FN15]

Gains derived from the sale of property by a nonresident individual or foreign corporation similarly are exempt from U.S. tax, unless they are effectively connected with the conduct of a U.S. trade or business. Gains derived by a nonresident alien individual are subject to U.S. taxation only if the individual is present in the United States for 183 days or more during the taxable year. [FN16] Foreign corporations are subject to tax only with respect to certain gains on disposal of timber, coal, or domestic iron ore and certain gains from contingent payments made in connection with sales or exchanges of patents, copyrights, goodwill, trademarks and similar intangible property. [FN17] Most capital gains realized by foreign investors on the sale of portfolio investment securities thus are exempt from U.S. taxation.

Treasury regulations provide additional rules governing the treatment of notional principal contract payments and substitute dividend or interest payments made to nonresidents. Payments made pursuant to a notional principal contract (i.e., a derivative) are sourced in accordance with the residence of the recipient. [FN18] Accordingly, when such payments are made by a U.S. party to a nonresident counterparty, the payment is treated as foreign source and, as such, is generally not subject to U.S. taxation. This rule applies even the payment is calculated in whole or part by reference, for example, to U.S.-source dividends paid on an underlying reference security. However, if the nonresident counterparty is engaged in a U.S. trade or business to which the payment is effectively connected, the payment is subject to regular U.S. net income

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taxation (and not withholding tax) in the same manner as if paid to a U.S. resident. [FN19]

On the other hand, substitute payments made in lieu of interest or dividend payments pursuant to a securities lending arrangement or similar transaction are treated by regulation as having the same source and character as the payments for which they substitute (a so-called "look-through" approach). As a result, substitute interest payments made to a nonresident with respect to interest paid on a debt obligation of a U.S. obligor may qualify for the portfolio interest exemption, to the extent that they meet the conditions otherwise applicable to actual interest payments on the obligation. Substitute dividends paid to a nonresident with respect to stock of a U.S. corporation are similarly treated as U.S.-source dividends and are subject to 30-percent nonresident withholding tax. [FN20] Substitute payments are also eligible for treaty benefits (described below) to the same extent and subject to the same conditions as the actual payments for which they substitute.

As the above summary suggests, many forms of income or gain from U.S. investments are simply not subject to U.S. withholding tax when earned by a non-U.S. investor. On the other hand, the Code does impose withholding tax on some important classes of U.S.-source income earned by non-U.S. investors. In particular, dividends paid by U.S. corporations (but, as described above, not dividend-equivalent payments made in respect of equity derivative contracts) to foreign investors are subject to U.S. withholding tax. So, too, are nonportfolio interest payments (e.g., interest paid by a U.S. subsidiary to a foreign parent company), and certain rent and royalty payments made in respect of property used in the United States (if not incurred in connection with the conduct of a trade or business in the United States).

Even in those cases where the Code imposes the general 30-percent withholding tax on the income or gain of a foreign investor, that tentative tax liability may be reduced or eliminated by a tax treaty between the United States and the country in which the investor is domiciled. Thus, most U.S. income tax treaties provide for a zero rate of withholding tax on interest payments (other than contingent interest of the type described in section 871(h)(4)), with the result that virtually all U.S.-source interest paid to residents of a treaty country is typically exempt from U.S. withholding tax. Most U.S. income tax treaties also reduce the rate of withholding on dividends to 15 percent (in the case of portfolio dividends) and to five percent (in the case of "direct investment" dividends paid to a 10 percent-or-greater shareholder). For royalties, the U.S. withholding rate is typically reduced to five percent or to zero in certain cases. In each case, the reduced withholding rate is available only to a beneficial owner who qualifies as a resident of the treaty country within the meaning of the treaty and otherwise satisfies any applicable limitation on benefits provisions of the treaty.

B. Why Impose Withholding Taxes?

As a practical matter, withholding taxes are the only viable collection mechanism for taxing foreign investors with respect to U.S.-source portfolio income. This observation begs the question, however, of why the United States should seek to tax this income in the first place. Some commentators have described a longstanding global consensus in the allocation of rights to tax cross-border income. Under this norm, business income is taxed by the country in which it is derived (the source country) and passive or portfolio income is taxed by the country in which the recipient of the income resides (the residence country). [FN21] Unlike, for example, a corporation operating a business in a source country, a portfolio investor may have no ties to the source country other than the investor's passive holding of the investment. The source country therefore may have no clear economic claim to the income.

In this allocation of taxing rights, source-based withholding tax arguably is an anomaly. The current practice of the United States not to tax U.S.-source portfolio interest income (even where the interest expense reduces the U.S. tax base) or capital gains derived by nonresidents can be said to be consistent with this norm.

U.S. tax policy with respect to U.S.-source income earned by non-U.S. portfolio investors also may be influenced by larger macroeconomic trends. This observation is particularly relevant to the exception for interest paid on bank deposits and the portfolio interest exception.

First, the financial markets are largely global; investment choices are not generally constrained by currency exchange

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controls, and information about global investment opportunities is relatively easy to obtain. As a result, non-U.S. investors have available to them a wide range of investment opportunities, many of which can be said to be close substitutes for one another. Thus, for example, a foreign investor who wishes to acquire a U.S. dollar-denominated debt instrument (or bank account) in practice is not required to make that investment in a U.S. issuer.

Second, and as described in detail in an earlier Joint Committee on Taxation staff pamphlet, the United States for many years has been a net importer of financial capital. [FN22] Measured in nominal dollars, the amount of foreign-owned assets in the United States grew at an annual rate of more than 13 percent between 1981 and 2006. [FN23] In 2006 the portfolio assets of foreign investors invested in the United States exceeded $10 trillion; direct assets of foreign investors in the United States (e.g., ownership by a foreign parent company of a U.S. subsidiary) exceeded $2 trillion. [FN24] Foreign ownership of U.S. investments in 2006 exceeded the converse case (U.S. investments abroad) by $2.5 trillion. [FN25]

Third, many other countries also are net capital importers, or wish to reduce domestic interest costs by increasing the supply of lenders. As a result, many other jurisdictions do not today impose withholding tax on interest paid by resident companies to nonresident investors. In light of the ready substitutability in the global markets of debt obligations on which withholding tax is not imposed for those instruments that are subject to withholding tax, some observers have concluded that the imposition of withholding tax on interest paid to foreign portfolio investors is unlikely to raise revenue, but is likely to affect adversely the supply of lendable funds to domestic issuers (including, in the case of the United States, the U.S. Treasury). This reasoning may in part explain the decision of the United States (and other countries) not to impose withholding tax on portfolio interest income earned by nonresident investors.

As described earlier, however, the Code does impose 30-percent withholding tax on U.S.-source dividends, rents, royalties, and other amounts derived by nonresidents. Notwithstanding the broad international tax framework of source-based taxation of business income and residence-based taxation of portfolio income, there are a few possible explanations for the persistence of these withholding taxes under domestic law. Two practical explanations are first, that source-based withholding taxes generate some revenue [FN26] and, second, that the 30-percent statutory withholding rate is a tool that the U.S. Treasury Department can employ in negotiations over bilateral income tax treaties. On this second point, U.S. bilateral income tax treaties generally allow, as was described previously, reduced rates of U.S. withholding tax on dividends, rents, royalties, and non-portfolio interest derived by qualified residents of the other treaty countries in exchange for similar benefits for U.S. residents with investments in those countries. Where investment flows are disproportionate between the United States and a treaty partner, the United States may also be able to obtain other types of concessions from the treaty partner in exchange for offering to reduce the U.S. withholding tax rate.

A third explanation for the persistence of withholding taxes is the difficulty of enforcing residence-based taxation of foreign-source portfolio income. [FN27] This portfolio income may be truly foreign source as, for example, when a Mexican resident owns shares of stock in U.S. companies, either directly or perhaps through an entity organized in a tax haven jurisdiction. Alternatively, the portfolio income may be foreign source in formal terms only as, for example, when a U.S. resident forms a foreign corporation or other entity for investing into the United States. In either case, the residence country (Mexico in the first example and the United States in the second example) may not be able to enforce residence-based taxation under its regular income tax rules. In this circumstance, tax collected at the source may be the only tax imposed on the income. The enforcement challenges presented when U.S. residents derive portfolio income through foreign entities or accounts are the subject of much of the succeeding discussion in this pamphlet.

C. Withholding Tax Administration: Self-Certification

The U.S. withholding tax rules are administered through a system of self-certification. Thus, a nonresident investor seeking to obtain withholding tax relief for U.S.-source investment income typically must provide a certification, on IRS Form W-8, to the withholding agent in order to establish foreign status and eligibility for an exemption or reduced rate.

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[FN28]

There are four types of Form W-8, [FN29] three of which are designed to be filed by the beneficial owner of a payment of U.S.-source income: (1) the Form W-8BEN, which is filed by a beneficial owner of U.S.-source non-effectively-connected income, (2) the Form W-8ECI, which is filed by a beneficial owner of U.S.-source effectively-connected income, [FN30] and (3) the Form W-8EXP, which is filed by a beneficial owner of U.S.-source income that is an exempt organization or foreign government. [FN31] Each of these forms requires that the beneficial owner provide its name and address and certify that the beneficial owner is not a United States person. The Form W-8BEN also includes a certification of eligibility for treaty benefits (for completion where applicable). All certifications on Forms W-8 are made under penalties of perjury.

The United States imposes tax on the beneficial owner of income, not its formal recipient. For example, if a U.S. citizen owns securities that are held for her in "street" name at a brokerage firm, that U.S. citizen (and not the brokerage firm) is subject to tax on income from those securities. The distinction between nominal and beneficial ownership of course is important in determining liability for tax in the case of cross-border flows as well, but the complexity and opacity of some foreign law arrangements can make compliance more difficult. [FN32]

The fourth type of Form W-8 is the IRS Form W-8IMY, which is filed by a payee that receives a payment of U.S.-source income as an intermediary for the beneficial owner of that income. The intermediary's Form W-8IMY must be accompanied by a Form W-8BEN, W-8EXP, or W-8ECI, as applicable, [FN33] furnished by the beneficial owner, unless the intermediary is a "qualified intermediary," a "withholding foreign partnership" or a "withholding foreign trust." The rules applicable to qualified intermediaries are discussed in Section II below. A withholding foreign partnership or trust is a foreign partnership or trust that has entered into an agreement with the Internal Revenue Service to collect appropriate Forms W-8 from its partners or beneficiaries and act as a U.S. withholding agent with respect to those persons. [FN34]

Provision of the Form W-8 also establishes an exemption from the rules that apply to many U.S. persons governing information reporting on Form 1099 and backup withholding. [FN35] A withholding agent that makes payments of U.S.-source amounts to a foreign person is required to report those payments, including any amounts of U.S. tax withheld, to the IRS on Forms 1042 and 1042-S. [FN36]

D. Withholding Tax Enforcement Problems and Possible Solutions

Although the existence of source-based withholding taxes can be explained as a response to the difficulty of enforcing residence-based taxation of portfolio income, the withholding tax itself is difficult to enforce. This section describes several reasons for that difficulty.

1. Income categorization

As was described previously, the U.S. 30-percent withholding tax is imposed on discrete categories of income — dividends, rents, royalties, and non-portfolio interest, for example. The withholding tax treatment of a particular item of income derived by a nonresident may vary based on how the income is categorized. Particularly with the growth of financial derivatives, taxpayers have exploited problems of characterization. [FN37]

Perhaps the best-known example of structuring to avoid withholding tax is the use of instruments known as swaps to replicate actual ownership of stock while avoiding the withholding tax that would be imposed on dividends paid on the stock. A nonresident seeking exposure to the U.S. equity markets could purchase stock in U.S. companies. Dividends paid on this stock generally would be considered U.S.-source and therefore would be subject to withholding tax at a 30-percent (or reduced treaty) rate. [FN38] Instead of actually owning the stock, however, the non-U.S. investor could create synthetic ownership by holding an equity derivative contract.

For example, under a typical "total return swap," the investor would enter into an agreement with a counterparty under

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which returns to each party would be based on the returns generated by a notional investment in a specified dollar amount of stock. The investor would agree for a specified period to pay to the counterparty (a) interest calculated at a market rate (such as the London Interbank Offered Rate (LIBOR)) on the notional amount of stock and (b) any depreciation in the value of the stock, and the counterparty would agree for the specified period to pay the investor (c) any dividends paid on the stock and (d) any appreciation in the value of the stock. [FN39] This swap would be economically equivalent to a transaction in which the foreign investor actually purchased the stock from the counterparty, using funds borrowed from the counterparty, and at the end of the period sold the stock back to the counterparty and repaid the borrowing.

Although the equity swap just described has identical economic characteristics to a leveraged purchase of stock (except that the equity swap party has credit exposure to its swap counterparty), the tax treatment of the foreign investor would be different. Because the source of income from an equity swap (in tax terms, a notional principal contract) is (as described previously) determined by reference to the residence of the recipient of the income, amounts representing dividends in this example would be foreign source and therefore would not be subject to U.S. withholding tax. [FN40]

There may be non-tax reasons why foreign investors enter into equity swaps on U.S. stock rather than holding the underlying stock. For instance, U.S. securities law regulations forbid extending credit above certain levels for the purchase of stock, but these rules do not apply to swap transactions that replicate leveraged purchases. [FN41] Nonetheless, certain arrangements have been viewed as abusive. For example, a foreign investor might sell stock it owns to a U.S. counterparty shortly before a dividend is paid, simultaneously enter into a total return swap on the stock with the counterparty, and terminate the swap agreement and repurchase the stock from the counterparty shortly after the dividend is paid. [FN42] The IRS has sought data from large U.S. financial institutions to determine whether U.S. withholding tax should have been paid on certain swap transactions that those institutions facilitated. [FN43] Notwithstanding possible IRS successes in individual cases, the volume of swap transactions remains large. Financial engineering has made it difficult to collect withholding tax on cross-border dividend payments.

In response, some commentators argue that the U.S. withholding tax on nonresidents' U.S.-source dividend income should be abolished (or that attempts to collect that withholding tax are futile). [FN44] Arguments for why the dividend withholding tax should be abolished include the following. First, the dividend withholding tax impedes U.S. corporations' access to global capital. Second, taxpayers seek to avoid the dividend withholding tax, and this avoidance creates its own issues. Because portfolio interest can be paid to nonresidents free of withholding tax, U.S. corporations seeking foreign financing may find their decisions distorted by a tax preference for debt rather than equity financing. Debt financing, in turn, can result in a stripping of the U.S. tax base since interest payments, unlike dividend payments, are (subject to certain limitations) deductible. Moreover, the IRS must expend resources policing the distinction between notional principal contract income, which can be derived by nonresidents free of withholding tax, and dividend income, which cannot. Eliminating the dividend withholding tax would, in this view, free up resources for other enforcement efforts.

On the other hand, some policy makers and commentators have argued that the United States should not give up on dividend withholding tax. One alternative to giving up on the tax is to enact targeted changes to prevent avoidance of the tax. One targeted measure could be to change the rule under which the source of income from a notional principal contract is determined based on the residence of the recipient of the income. A source rule similar to the source rule for dividends would treat the source of notional principal contract income as the residence jurisdiction of the payor of the income. This rule, however, could create withholding on amounts that are not actually paid (because amounts representing dividends in swaps are netted against amounts representing interest and depreciation) and could be avoided by entering into derivative transactions in which amounts representing dividends are categorized as interest and therefore qualify for the portfolio interest exemption. [FN45]

Another targeted measure, included in bills introduced recently in the U.S. House of Representatives and the U.S. Senate, would impose the 30-percent gross basis withholding tax on dividend-equivalent amounts paid on swap contracts. [FN46] This measure may raise similar concerns to those that apply to a change in the source rule for notional principal

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contract income — that withholding tax could be imposed on amounts not actually paid and that the provision might be avoided through the use of other forms of derivative contracts (e.g., forward contracts in which anticipated dividend payments are reflected in the forward pricing).

A more thorough approach to the problem of avoiding withholding tax by deriving income in one category rather than another would be to impose a uniform withholding tax on all deductible payments, including portfolio interest. This approach is described in more detail below.

2. Treaty shopping

A second problem with enforcing withholding taxes arises from the availability of reduced rates of withholding tax under U.S. bilateral income tax treaties. Under the U.S. model tax treaty and in many actual U.S. tax treaties, the withholding tax rate on dividends is reduced to five percent when the beneficial owner of the dividends owns at least 10 percent of the voting stock of the company paying the dividends and is reduced to 15 percent in other cases; the withholding tax rate on interest that would not qualify for the U.S. portfolio interest exemption is reduced to zero (or, in the case of certain contingent interest, 15 percent); and the withholding tax on royalties is eliminated. [FN47] Several recent U.S. tax treaties go further than the U.S. model treaty and completely eliminate withholding tax when a subsidiary company makes dividend payments to its parent corporation (so-called "direct investment" dividends). [FN48]

Nonresidents receiving U.S.-source income subject to withholding tax have an incentive to take advantage of U.S. income tax treaties that reduce withholding tax. Treaty benefits, however, generally are allowed only to residents of the treaty countries. A taxpayer that is not a resident of a treaty country may attempt to benefit from a treaty by organizing an entity in a treaty jurisdiction and causing income to be routed through that entity.

For example, a corporation organized in Singapore (a non-treaty jurisdiction) that intends to make loans to a related U.S. corporation might form a corporation in Luxembourg (a treaty jurisdiction), and then arrange for the loans to be made by the Luxembourg corporation with funds ultimately supplied by the Singapore company. If the Luxembourg corporation is viewed under applicable U.S. law as the owner of the interest income paid by the U.S. affiliate, then interest on the loans will qualify for a zero or 15-percent rate of withholding tax under the U.S.-Luxembourg income tax treaty rather than the statutory 30-percent rate. This hypothetical example illustrates a practice referred to as treaty shopping.

There have been various efforts to restrict treaty shopping. The IRS has successfully litigated some cases, including a leading case involving "back-to-back" interest paid (as in the above example) from a U.S. company to a foreign affiliate in a treaty country that acted as a simple conduit for a loan from a non-treaty ultimate owner. [FN49] Similarly, the Treasury has negotiated extensive "limitation on benefits" provisions in treaties, and the problem has been addressed by proposed and enacted legislation and regulations.

All recent U.S. income tax treaties include comprehensive limitation on benefits provisions. These provisions are intended to ensure that only genuine residents of treaty countries are eligible for the benefits of a treaty. Limitation on benefits provisions therefore typically include rules denying treaty benefits unless one of several tests for a genuine connection to a treaty country is satisfied. Under a typical version of one of these tests (the ownership and base erosion test), at least 50 percent of the voting power and value of the person for whom eligibility for treaty benefits is at issue must be residents of the relevant treaty country and deductible payments to persons who are not residents of either treaty country must represent less than 50 percent of the person's income.

Limitation on benefits provisions have not prevented treaty shopping in all cases. The limitation on benefits provisions in some treaties more than 10 years old (the treaty with Luxembourg, for instance, under which, as an example, a Luxembourg company may qualify for treaty benefits even if its direct owner is a resident of a zero-tax jurisdiction so long as at least 50 percent of the company's principal share class is ultimately owned by Luxembourg *or* U.S. residents) are not as restrictive as the provisions in more recent treaties. Treaty shopping using the U.S. income tax treaties with Hungary and Poland, in fact, is limited only by relatively narrow provisions in those treaties defining residency and by considerations

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of the domestic laws of the treaty countries. Those two treaties have no rules comparable to comprehensive limitation on benefits provisions found in other treaties.

U.S. internal law, a recent legislative proposal, and Treasury regulations have also addressed certain concerns about treaty shopping. A Code provision denies treaty benefits to certain foreign persons for payments received through certain hybrid entities. [FN50] A proposal included in a bill sponsored by House Ways and Means Committee Chairman Rangel would deny treaty-based reductions in withholding tax for any payment to a subsidiary of a foreign parent corporation unless the payment would qualify for treaty benefits if paid directly to the parent corporation. [FN51] Treasury regulations promulgated in 1995 (the anti-conduit rules) recharacterize as transactions made directly between two parties certain multi-party financing transactions entered into principally to reduce withholding tax. [FN52]

In light of these treaty-based and domestic law provisions to limit withholding tax reductions to genuine residents of treaty countries, the extent of treaty shopping is unclear, in part because defining treaty shopping is itself subjective.

3. Self-certification nature of withholding tax rules

A third enforcement difficulty originates in the basic framework of the U.S. withholding tax rules. Those rules rely on certifications by recipients of income potentially subject to withholding and by withholding agents. As described previously, recipients of income potentially subject to withholding must certify their status so that the payors of the income can determine to what extent withholding is required. Recipients must, for example, certify whether they are U.S. residents or nonresidents and, if they are nonresidents, whether they are eligible for reduced rates of withholding tax allowed by a tax treaty. Withholding agents must certify that they have withheld the proper amount of tax, often with respect to very large volumes of income flows. Proper withholding, in turn, requires the withholding agent to determine whether a payee has U.S. or foreign status; whether a payee is the beneficial owner [FN53] of the income or is an intermediary receiving a payment on behalf of the owner; whether the payment can be reliably associated with proper documentation; and whether, in the absence of documentation, certain presumptions require full, reduced, or zero withholding or instead require backup withholding.

Problems with withholding can result from errors related to any aspect of this self-certification process. Moreover, the self-certification system can be difficult for the IRS to audit. Applicable Treasury regulations generally do not impose an "audit" or affirmative diligence obligation on the part of domestic withholding agents in determining the validity of a Form W-8, [FN54] and as a practical matter U.S. withholding agents cannot verify the accuracy of every Form W-8 they receive. As a consequence, U.S. investors may be able to portray themselves successfully as foreign persons, thereby escaping U.S. income taxation.

In a December 2007 report to the Senate Finance Committee, the Government Accountability Office ("GAO") found a number of potential problems with the self-certification process. [FN55] Withholding agents may not know the identity of beneficial owners of income when income is paid through foreign intermediaries. In particular, withholding agents may not be able to identify U.S. beneficial owners who ultimately control foreign corporations or trusts. [FN56] Consequently, these U.S. persons may incorrectly benefit from treaty-based reductions of withholding tax or exemptions from withholding tax altogether (because, for instance, the income in question is interest on a bank account or a bond). The problem of U.S. beneficial owners hiding behind foreign entities or accounts is central to the UBS case discussed elsewhere in this pamphlet and has been the focus of various efforts to address noncompliance with information reporting and withholding rules.

Relatedly, according to the GAO significant amounts of income have flowed to undisclosed recipients and undisclosed jurisdictions. For reasons that the IRS could not explain, according to the GAO, withholding taxes on these income flows have been imposed, in the aggregate, at rates significantly below 30 percent. Because beneficial ownership and residence information typically is the basis for reduced withholding tax rates, these reduced rates, according to GAO, suggest some amount of noncompliance. This noncompliance can be expected to have included evasion of U.S. tax by U.S. persons

who have derived portfolio income through foreign intermediaries.

Potential changes to the information reporting and withholding rules to address problems arising from the self-certification nature of the rules range from modest to sweeping. In its 2007 report the GAO recommended, among other steps, that the IRS improve its enforcement efforts by making better use of data that it already collects. In particular, the GAO suggested that the IRS determine the extent to which (1) income paid by withholding agents flows through foreign intermediaries that may be providing the IRS with unreliable documentation, and (2) reductions in withholding taxes collected from funds flowing to undisclosed jurisdictions and undisclosed recipients were proper. [FN57]

The IRS's qualified intermediary ("QI") program has been the major initiative undertaken by the IRS to deal with the compliance issues presented by self-certification. Under this program, the IRS contracts with foreign financial institutions to enforce U.S. withholding and reporting rules. The QI program is discussed in detail in Section II.

Professor Reuven Avi-Yonah has advocated a different approach. [FN58] Avi-Yonah's proposal is intended to address the principal concern of this pamphlet — the failure by individuals to report to the taxing authorities of their home countries income from portfolio investments derived through foreign intermediaries. Avi-Yonah argues that the United States should impose a uniform withholding tax on cross-border interest flows, other deductible payments such as royalties, and payments on derivative instruments. He suggests that this withholding tax should be imposed at a rate that would approximate the tax rate that would apply if the portfolio income were taxed on a true residence basis, a rate of 40 percent or higher. The withholding tax would be fully refundable if the beneficial owner of the income subject to withholding provided a certificate to the tax authorities in the country from which the income was derived attesting that the income was reported in the owner's home country.

Avi-Yonah's approach builds on (but goes further than) the European Union ("EU") Savings Taxation Directive. [FN59] That directive provides for (1) the automatic exchange of beneficial ownership and other information when a resident of one member state of the EU receives interest payments from an entity or other payor in another member state and (2) during a transitional period, imposition of a 20 percent (35 percent after June 2011) withholding tax on interest payments received by EU residents from payors located in Austria, Belgium, or Luxembourg unless the recipients of the payments agree to the exchange of information related to their accounts. [FN60] Avi-Yonah argues that the United States should use the EU Savings Taxation Directive as the basis for leading a coordinated effort at instituting his proposed uniform withholding tax in all member countries of the Organisation for Economic Co-operation and Development ("OECD").

Avi-Yonah's recommendations must be put in the context of the macroeconomic issues identified earlier. In particular, those recommendations might prove difficult for the United States to adopt unilaterally if withholding increases the cost of borrowing to domestic issuers, including the Federal government. Moreover, as applied to the United States those recommendations presumably would require that bearer bonds be prohibited, and arguably should require domestic withholding on interest as well. To date, at least, the United States has moved in the opposite direction, by emphasizing improved information reporting. It is worth noting, however, that repeal of the special rules for bearer bonds (under which the portfolio interest exemption is made available as long as certain foreign-targeting requirements are satisfied in connection with the original issuance) would also be consistent with the current IRS approach; the continued need for those rules is no longer entirely clear, in light of the absence of demand for actual bearer bonds and the global prevalence of electronic clearing systems.

Professor Michael J. Graetz and Itai Grinberg are not as pessimistic as Avi-Yonah about the ability of residence countries to collect tax on foreign portfolio income in the absence of refundable source-country withholding taxes. [FN61] Graetz have argued that source-based taxation of foreign portfolio income should be abolished and that, to address noncompliance with residence-based taxation of this income, the United States and other countries should instead engage in continued multilateral cooperation in information sharing. Graetz also have argued for unilateral efforts to address cross-border evasion. As an example of unilateral action, they view the United States' QI program as "a major step forward."

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II. QUALIFIED INTERMEDIARY PROGRAM

A. Background

In April of 1996, the IRS published proposed regulations under sections 1441 and 1442 addressing certain U.S.-source income paid to foreign persons. [FN62] Final regulations were issued in 1997, but their effective date was twice delayed, and they became effective only as of January 1, 2001. [FN63] These regulations substantially revised the withholding and reporting requirements for amounts paid to foreign persons and established the Qualified Intermediary ("QI") program. [FN64] As described in this Section II, the revised Treasury regulations were an attempt to balance the needs of tax administration and the procedures necessary to curb tax evasion with the need to minimize the barriers and burdens placed on the financial markets.

The basic strategy adopted by the QI regulations was for the IRS to rely explicitly on certain foreign intermediaries (QIs) to enforce compliance with U.S. tax information reporting requirements. These foreign intermediaries agree to assume responsibility for obtaining documentation from their customers and to substantiate the status of their customers as the beneficial owners of U.S.-source income. In turn, the IRS agrees to permit the QIs to certify on behalf of their foreign customers, without revealing to the IRS or to other U.S. withholding agents the identity of those foreign customers. Moreover, the IRS agrees to rely on third-party private auditors to audit the compliance of the QIs with the QI program; this condition was viewed as a practical necessity if foreign banks were to agree to participate in the QI program, because these foreign institutions feared that their non-U.S. customer base would not agree to allow a foreign taxing authority (the IRS) direct access (through an IRS audit) to customer account information.

At the time the QI program was adopted, the IRS explained its scope and purpose as follows in Announcement 2000-48:

> The QI system is a significant step forward for both taxpayers and the IRS. It does, however, represent a paradigm shift to greater self-regulation. Treasury and the IRS believe that it is appropriate to allow the greatest self-regulation under circumstances in which Treasury and the IRS have the greatest confidence that such self-regulation will be effective. In pursuit of that objective, Treasury and the IRS considered allowing QI status only for businesses operating in jurisdictions with which the United States has a bilateral tax treaty or tax information exchange agreement. In response to taxpayer comments, however, that approach was not adopted. Taxpayers requested that the QI system have the broadest scope possible, so that financial institutions can potentially act as qualified intermediaries in all jurisdictions in which they do business. In an attempt to balance these competing concerns, Treasury and the IRS intend to permit financial institutions to act as qualified intermediaries in accordance with the provisions of this announcement [and the model QI Agreement]. [FN65]

The Announcement went on to explain that, as part of this "paradigm shift," the IRS's cross-border withholding tax compliance effort essentially would be built around reliance on bank regulatory "know-your-customer" rules:

> Treasury and the IRS believe it is appropriate to permit the self-regulation envisioned by the QI system only under circumstances in which Treasury and the IRS have confidence that such self-regulation may be effective. Because Treasury and the IRS regard know-your-customer (KYC) rules as a vital component of adequate self-regulation, the IRS generally will not extend the QI system to any country that does not have KYC rules or has unacceptable KYC rules. The IRS will, however, permit a branch of a financial institution (but not a separate juridical entity affiliated with the financial institution) located in such a country to act as a qualified intermediary if the branch is part of an entity organized in a country that has acceptable KYC rules and the entity agrees to apply its home country KYC rules to the branch. As is the case with any violations of the QI agreement by the branch, failure to obtain adequate documentation will cause the entity to be in default of its agreement and may cause the agreement to be terminated. [FN66]

Prior to the issuance of the current withholding tax regulations and the QI program, withholding agents were subject to complex rules depending on the type of income and source of income of the payment. Inconsistent rules for determining

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whether a payee was a U.S. or foreign person applied to different types of income, and IRS guidance was sometimes unclear. The IRS and Treasury determined that, due to the substantial growth in cross-border flows and the desire to continue a net withholding system (rather than moving to a full withholding system with refundability), it was necessary to standardize and coordinate the procedures imposed on withholding agents for verifying U.S. or foreign status for Form 1099 reporting, compliance with backup withholding rules, and administration of the nonresident withholding provisions. Additionally, Treasury was under a congressional mandate to consider options for replacing the address/self-certification method of administering income tax treaty benefits. [FN67]

In developing the QI program, Treasury and the IRS gave particular attention to the problems raised under prior practice by payments made through foreign intermediaries. (As previously noted, payments made through an intermediary are treated as payments made directly to the beneficial owner for whom the intermediary is collecting the payments.) Prior Treasury regulations required different documentation depending on the type of payment, whether the intermediary remitted through a U.S. office, or whether the payee had a foreign address. In cases in which withholding certificates were required, the beneficial owner certification was required to be passed up through a chain of intermediaries to the U.S. withholding agent. These procedures were difficult to implement and enforce in many cases, making it difficult to collect tax from the ultimate beneficial owner of the payments.

A QI is defined as a foreign financial institution or a foreign clearing organization, other than a U.S. branch or U.S. office of such institution or organization, which has entered into a withholding and reporting agreement (a "QI agreement") with the IRS. [FN68] In exchange for entering into a QI agreement, the QI is able to shield the identities of its customers from the IRS and other intermediaries (for example, other financial institutions in the chain of payment that may be business competitors of the QI) in certain circumstances and is subject to reduced information reporting duties compared to those that would be imposed in the absence of the agreement. This ability to shield customer information is limited, however, with respect to U.S. persons, because the QI is required to furnish Forms 1099 to its U.S. customers if it has assumed primary withholding responsibility for these accounts, or to provide Forms W-9 to the withholding agent in cases in which the QI has not assumed such responsibility.

A foreign financial institution that becomes a QI is not required to forward beneficial ownership information with respect to its customers to a U.S. financial institution or other withholding agent of U.S.-source investment-type income to establish their eligibility for an exemption from, or reduced rate of, U.S. withholding tax. [FN69] Instead, the QI is permitted to establish for itself the eligibility of its customers for an exemption or reduced rate, based on information as to residence obtained under the "know-your-customer" rules imposed by the banking laws to which the QI is subject in its home jurisdiction. The QI certifies as to eligibility on behalf of its customers, and provides withholding rate pool information to the U.S. withholding agent as to the portion of each payment that qualifies for an exemption or reduced rate of withholding. As described below, a QI may also assume responsibility for both nonresident withholding and, in the case of U.S. customers, backup withholding.

The IRS has published a model QI agreement (described in more detail below) that financial institutions wishing to become QIs are generally expected to sign. [FN70] A prospective QI must submit an application to the IRS providing certain specified information, and any additional information and documentation requested by the IRS. The application must establish to the IRS's satisfaction that the applicant has adequate resources and procedures to comply with the terms of the QI agreement.

Before entering into a QI agreement that provides for the use of documentary evidence obtained under a country's know-your-customer rules, the IRS must receive (1) that country's know-your-customer practices and procedures for opening accounts and (2) responses to 18 related items. If the IRS has already received this information, a particular prospective QI need not submit it again. The IRS web site (www.irs.gov) lists 59 countries for which it has received such information and for which the know-your-customer rules are acceptable.

Although the QI program "gives the IRS an important line of sight into the activities of U.S. taxpayers at foreign banks and financial institutions," [FN71] QIs handle only a relatively small percentage of U.S.-source income flowing through

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foreign intermediaries. The Government Accountability Office (the “GAO”) has reported that, in 2003, only 12.5 percent of income reported as paid by withholding agents was reported by QIs; in fairness, however, the QI program at that point was only in its third year. [FN72] Of the remaining 87.5 percent, the GAO made no determination as to the amounts flowing through direct versus indirect (i.e., nonqualified intermediary) account holdings; nor did the GAO distinguish between portfolio and direct investment flows.

B. The Model QI Agreement

The model QI agreement describes in detail the QI's withholding and reporting obligations in numerous circumstances. Certain key aspects of the model agreement are described briefly below. [FN73]

Withholding and reporting

As a technical matter, all QIs are withholding agents for purposes of the nonresident withholding and reporting rules, and payors (required to withhold and report) for purposes of the backup withholding rules. However, under the QI agreement, a QI is not required to withhold on payments made to nonresident customers, or to report those payments on Form 1042-S, if the QI has not assumed primary responsibility for nonresident withholding and, instead, provides a U.S. withholding agent with a Form W-8IMY that certifies as to the status of its (unnamed) nonresident account holders. Similarly, a QI is not required to backup withhold on payments made to U.S. customers if the QI does not assume primary Form 1099 reporting and backup withholding responsibility and, instead, provides a U.S. payor with the Forms W-9 of its U.S. non-exempt recipient account holders (i.e., account holders that are U.S. persons not generally exempt from Form 1099 reporting and backup withholding). In either case, the QI must also provide the U.S. withholding agent (or U.S. payor) certain additional information about the withholding rates that should be applied to payments made to such account holders. These rates can be supplied with respect to “withholding rate pools” that aggregate payments of a single type of income (e.g., interest or dividends) that is subject to a single rate of withholding.

Alternatively, a QI may elect to assume primary nonresident withholding and reporting responsibility, primary backup withholding and Form 1099 reporting responsibility, or both. A QI that assumes such responsibility is subject to all of the related obligations imposed by the Code on U.S. withholding agents or payors.

In general, a QI is not required to disclose, either to a withholding agent or to the IRS, the identity of an account holder that is a foreign person or a U.S. person that is an exempt recipient (such as a corporation). [FN74] To the extent that a QI has not assumed primary Form 1099 reporting and backup withholding responsibility, the QI generally must provide to a withholding agent Forms W-9 obtained from each U.S. non-exempt recipient account holder (for example, an individual). If a U.S. non-exempt recipient has not provided a Form W-9, the QI must disclose the name, address, and taxpayer identification number (if available) to the withholding agent (and the withholding agent must apply backup withholding). However, no such disclosure is necessary if the QI is, under local law, prohibited from making the disclosure and the QI has followed certain procedural requirements (including providing for backup withholding, as described further below).

Documentation of account holders

QIs agree to review and maintain documentation regarding the status of their account holders in accordance with the terms of their QI agreement and, in the case of documentary evidence obtained from direct account holders, in accordance with “know-your-customer” rules applicable under the banking laws and regulations of the jurisdiction in which the QI is located.

A QI may treat an account holder as a foreign beneficial owner of an amount if the account holder provides a valid Form W-8 (other than a Form W-8IMY) or valid documentary evidence that supports the account holder's status as a for-

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eign person. With such documentation, a QI generally may treat an account holder as entitled to a reduced rate of withholding if all the requirements for the reduced rate are met and the documentation supports entitlement to a reduced rate. A QI may not reduce the rate of withholding if the QI knows that the account holder is not the beneficial owner of a reportable amount or payment.

If a foreign account holder is the beneficial owner of a payment, then a QI may shield the account holder's identity from U.S. custodians and the IRS. If a foreign account holder is not the beneficial owner of a payment (for example, because the account holder is a nominee), the account holder must provide the QI with a Form W-8IMY for itself along with specific information about each beneficial owner to which the payment relates. A QI that receives this information may shield the account holder's identity from a U.S. custodian, but not from the IRS. [FN75]

In general, if an account holder is a U.S. person, the account holder must provide the QI with a Form W-9 or appropriate documentary evidence that supports the account holder's status as a U.S. person. However, in cases in which a QI does not have sufficient documentation to determine whether an account holder is a U.S. or foreign person, the QI must apply certain presumption rules detailed in the QI agreement. These presumption rules may not be used to grant a reduced rate of nonresident withholding; instead they merely determine whether a payment should be subject to full nonresident withholding (at a 30 percent-rate), subject to backup withholding (at a 28 percent-rate), or treated as exempt from backup withholding.

In general, under these presumptions, amounts of U.S.-source investment income that are paid outside the United States to an account maintained outside the United States are presumed made to an undocumented foreign account holder. A QI must treat such an amount as subject to withholding at a 30-percent rate and report the payment to an unknown account holder on Form 1042-S. [FN76] However, U.S.-source deposit interest and interest or original issue discount on short-term obligations that is paid outside the United States to an offshore account is presumed made to an undocumented U.S. non-exempt recipient account holder and thus is subject to backup withholding at a 28-percent rate. [FN77] Importantly, both foreign-source income and broker proceeds are presumed to be paid to a U.S. exempt recipient (and thus are exempt from both nonresident and backup withholding) in cases in which such amounts are paid outside the United States to an account maintained outside the United States.

Foreign law prohibition of disclosure

The QI agreement includes procedures to address situations in which foreign law (including by contract) prohibits the QI from disclosing the identities of U.S. non-exempt recipients (such as individuals). Separate procedures are provided for accounts established with a QI prior to January 1, 2001, and for accounts established on or after January 1, 2001.

Established prior to January 1, 2001

For accounts established prior to January 1, 2001, if the QI knows that the account holder is a U.S. non-exempt recipient, the QI must (1) request from the account holder the authority to disclose its name, address, taxpayer identification number (if available), and reportable amounts; (2) request from the account holder the authority to sell any assets that generate, or could generate, reportable payments; or (3) request that the account holder disclose itself by mandating the QI to provide a Form W-9 completed by the account holder. The QI must make these requests at least two times during each calendar year and in a manner consistent with the QI's normal communications with the account holder (or at the time and in the manner that the QI is authorized to communicate with the account holder). Until the QI receives a waiver on all prohibitions against disclosure, authorization to sell all assets that generate, or could generate, reportable payments, or a mandate from the account holder to provide a Form W-9, the QI must backup withhold on all reportable payments paid to the account holder and report those payments on Form 1099 or, in certain cases, provide another withholding agent with all of the information required for that withholding agent to backup withhold and report the payments on Form 1099.

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Established on or after January 1, 2001

For any account established by a U.S. non-exempt recipient on or after January 1, 2001, the QI must (1) request from the account holder the authority to disclose its name, address, taxpayer identification number (if available), and reportable amounts; (2) request from the account holder, prior to opening the account, the authority to exclude from the account holder's account any assets that generate, or could generate, reportable payments; or (3) request that the account holder disclose itself by mandating the QI to transfer a Form W-9 completed by the account holder.

If a QI is authorized to disclose the account holder's name, address, taxpayer identification number, and reportable amounts, it must obtain a valid Form W-9 from the account holder, and, to the extent the QI does not have primary Form 1099 and backup withholding responsibility, provide the Form W-9 to the appropriate withholding agent promptly after obtaining the form. If a Form W-9 is not obtained, the QI must provide the account holder's name, address, and taxpayer identification number (if available) to the withholding agents from whom the QI receives reportable amounts on behalf of the account holder, together with the withholding rate applicable to the account holder. If a QI is not authorized to disclose an account holder's name, address, taxpayer identification number (if available), and reportable amounts, but is authorized to exclude from the account holder's account any assets that generate, or could generate, reportable payments, the QI must follow procedures designed to ensure that it will not hold any assets that generate, or could generate, reportable payments in the account holder's account.

Under both of these procedures, a U.S. non-exempt recipient may effectively avoid disclosure and backup withholding simply by investing in assets that generate solely foreign source income (such as bonds issued by a foreign government). Under present law, foreign source income generally is not subject to Form 1099 reporting and backup withholding or to U.S. nonresident withholding tax. [FN78] Thus, this feature of the QI agreement is arguably consistent with the present law framework for withholding and information reporting. Moreover, a U.S. investor seeking to avoid disclosure can hold foreign assets through an account with a foreign financial institution that is not a QI and, similarly, escape information reporting and backup withholding. On the other hand, the fact that QI status affords foreign financial institutions a number of significant benefits arguably justifies the imposition of enhanced reporting by those institutions (for example, with respect to foreign-source income) in order to assist the IRS in its enforcement efforts.

External audit procedures

The IRS generally will not audit a QI with respect to withholding and reporting obligations covered by a QI agreement if an approved external auditor conducts an audit of the QI. An external audit must be performed of the second and fifth full calendar years in which the QI agreement is in effect. In general, the IRS must receive the external auditor's report by June 30 of the year following the year being audited.

Certain requirements for the external audit are provided in the QI agreement. In general, however, the QI must permit the external auditor to have access to all relevant records of the QI, including information regarding specific account holders. In addition, the QI must permit the IRS to communicate directly with the external auditor, review the audit procedures followed by the external auditor, and examine the external auditor's work papers and reports.

In addition to the external audit requirements set forth in the QI agreement, the IRS has issued further guidance (the “QI audit guidance”) for an external auditor engaged by a QI to verify the QI's compliance with the QI agreement. [FN79] An external auditor must conduct its audit in accordance with the procedures described in the QI agreement. However, the QI audit guidance is intended to assist the external auditor in understanding and applying those procedures. The QI audit guidance does not amend, modify, or interpret the QI agreement.

Term of a QI agreement

A QI agreement expires on December 31 of the fifth full calendar year after the year in which the QI agreement first

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takes effect, although it may be renewed. Either the IRS or the QI may terminate the QI agreement prior to its expiration by delivering a notice of termination to the other party. However, the IRS will not terminate a QI agreement unless there is a significant change in circumstances or an event of default occurs, and the IRS determines that the change in circumstance or event of default warrants termination. In the event that an event of default occurs, a QI is given an opportunity to cure it within a specified time.

Discussion

Since the adoption of the QI regime in 2001, more than 7,000 QI agreements have been signed. As of July 2008, there were 5,660 active QI agreements involving financial institutions in 60 countries. [FN80] The QI program provides a significant benefit to foreign financial institutions—in particular, the ability to obtain a reduced rate or exemption from U.S. withholding tax for their non-U.S. customers without disclosing the identities of those customers to the IRS or competing financial institutions. At the same time, however, the contractual nature of the QI program provides the IRS with an important mechanism to enforce compliance with U.S. reporting and withholding rules. For example, a foreign financial institution that is a QI is contractually required to disclose the identity of its U.S. customers to the IRS, report the payment of certain amounts to those customers and, in some circumstances, apply backup withholding. These contractual requirements extend beyond the scope of the reporting and withholding that would otherwise be required under applicable Treasury regulations. Moreover, the fact that so many of the world's major financial institutions have entered into QI agreements places a non-QI financial institution at a competitive disadvantage and creates a significant incentive for existing QIs to maintain their QI status. The IRS's ability to terminate a QI agreement in the event of noncompliance, thereby placing a financial institution at such a disadvantage, is a powerful tool for enforcing compliance and ensuring cooperation by a QI when instances of noncompliance are discovered.

On the other hand, the ongoing investigation into the failure by UBS to comply with the terms of its QI agreement has demonstrated certain weaknesses in the QI program as presently implemented. The UBS investigation is described briefly below, followed by a description of certain modifications to the QI program presently under consideration by the IRS to address problems identified in the UBS and other enforcement proceedings and the voluntary disclosure procedures recently announced by the IRS for individual taxpayers with unreported offshore accounts and entities.

The UBS Case

UBS, based in Switzerland and one of the world's largest financial institutions, had voluntarily entered into a QI agreement with the IRS, effective January 1, 2001, under which UBS agreed to identify and document any customers who held U.S. investments or received U.S.-source income in accounts maintained with UBS. Alternatively, if a U.S. customer refused to be identified under the QI agreement, UBS was required to apply backup withholding tax at a 28-percent rate on payments made to the customer, and to bar the customer from holding U.S. investments.

According to a report issued by the Permanent Subcommittee on Investigations of the Committee on Homeland Security and Governmental Affairs of the U.S. Senate (the "PSI") on July 17, 2007 (prepared in connection with a hearing held that day), entitled *Tax Haven Banks and U.S. Tax Compliance* (the "2008 PSI Report"), many of UBS's U.S. clients refused to be identified, to have taxes withheld, or to sell their U.S. assets as required under the QI agreement. To retain these customers, UBS bankers assisted the customers in concealing their ownership of the assets held in offshore accounts by helping to create nominee and sham entities. These entities were set up in various jurisdictions, including Switzerland, Liechtenstein, Panama, the British Virgin Islands, and Hong Kong. The UBS bankers and their U.S. customers then claimed that the offshore accounts were owned by these nominee and sham entities and were not subject to the reporting requirements imposed by the QI agreement.

On July 1, 2008, a Federal district court in Florida granted the IRS permission to issue a John Doe summons to UBS seeking the names of as many as 20,000 U.S. citizens who were UBS customers for which reporting or withholding ob-

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ligations may not have been met.

At the 2008 PSI hearing, Mark Branson, Chief Financial Officer, UBS Global Wealth Management and Business Banking, acknowledged in his testimony that compliance failures may have occurred and stated that UBS would take actions to ensure that the types of activities identified in the 2008 PSI Report would not recur. As part of that effort, UBS will no longer provide offshore banking services to U.S. customers; instead, such customers will be provided services only through companies licensed in the United States. Moreover, UBS will no longer permit advisors based in Switzerland to travel to the United States to meet with U.S. customers. Finally, Mr. Branson indicated that UBS would comply with the John Doe summons as it relates to the UBS accounts held by U.S. residents.

Subsequent to the 2008 PSI hearing, there have been several developments including the United States and UBS entering into a deferred prosecution agreement, the filing of a petition to enforce the John Doe summons, and an expansion of the Justice Department's investigation to certain Swiss individuals that allegedly worked with UBS employees to help U.S. taxpayers set up offshore accounts and entities to avoid paying U.S. taxes. On February 18, 2009, the United States District Court for the Southern District of Florida accepted a deferred prosecution agreement between the United States and UBS. [FN81] Pursuant to this agreement, UBS waived indictment and consented to the filing of a one-count criminal information charging UBS in a conspiracy to defraud the United States and the IRS in violation of U.S. criminal law. As part of the agreement, UBS agreed to pay $780 million in fines, penalties, interest and restitution. To the extent UBS meets this, and all other, obligations under the deferred prosecution agreement, the government will recommend dismissal of the charge.

On February 19, 2009, following the acceptance of the deferred prosecution agreement, the government filed a petition to enforce the previously issued John Doe summons with the United States District Court for the Southern District of Florida. In this petition, the government requested that the court issue an order requiring UBS to disclose to the IRS the identities of the bank's U.S. customers with undeclared Swiss accounts. The lawsuit alleges that there may be as many as 52,000 undeclared accounts with approximately $14.8 billion in assets as of the mid-2000s.

On March 4, 2009, a subsequent PSI hearing on *Tax Haven Banks and U.S. Tax Compliance—Obtaining the Names of U.S. Clients with Swiss Accounts* (“the 2009 PSI hearing”) was held. At this hearing, the Acting Assistant Attorney General, Tax Division, U.S. Department of Justice, John DiCicco, discussed the content of the UBS deferred prosecution agreement. [FN82] Specifically, Mr. DiCicco stated that UBS acknowledged that, beginning in 2000 and continuing through 2007, it participated in a scheme to defraud the United States and the IRS through its cross-border business. UBS engaged in such activities through its private bankers and managers that actively facilitated the creation of accounts in the names of offshore companies, allowing U.S. taxpayers to conceal their ownership of, or beneficial interest in, the accounts in an effort to evade U.S. tax reporting and payment requirements. Furthermore, UBS admitted that it had failed to implement effective controls to detect and prevent the unlawful activity, that it had failed to initiate an effective investigation into credible allegations of such unlawful activity, and that it had failed to take effective action to stop such activities.

In addition to making the payment to the United States of $780 million, UBS also agreed to the following conditions:

- UBS will provide the United States with voluminous and detailed records concerning accounts held directly or through beneficial arrangements by United States persons. UBS has a continuing obligation to cooperate with the criminal investigation and any resulting prosecutions, and also to search for and turn over any additional records found concerning such accounts.
- UBS will terminate its U.S. cross-border business. As part of this process, the accounts of United States customers covered by the deferred prosecution agreement will be closed with any underlying assets liquidated. All resulting proceeds will be distributed to the U.S. owners in dollar-denominated instruments.
- UBS's challenge to the government's motion to enforce the John Doe summons, including the filing of an appeal from an adverse ruling, will not be considered a breach of the deferred prosecution agreement. Upon completion of that litigation, however, if the Court were to order UBS to produce the documents sought and hold UBS in contempt

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for failure to do so, UBS's noncompliance may be determined to be a material breach of the deferred prosecution agreement, permitting the government to proceed with the criminal prosecution of UBS.

• UBS's failure to comply with a term of the deferred prosecution agreement may, in the sole discretion of the government, be deemed a material breach, permitting the government to proceed with the criminal prosecution of UBS. If UBS fully complies with the deferred prosecution agreement, the criminal information will be dismissed.

• The deferred prosecution agreement only applies and provides protection for the bank as to the specific conduct set forth within the agreement.

At the 2009 PSI hearing, Mr. Branson again testified on behalf of UBS. In his testimony, he addressed the progress UBS has made with respect to the requirements under the deferred prosecution agreement. [FN83] Mr. Branson discussed the petition filed by the IRS to have the court enforce the John Doe summons. Mr. Branson also discussed how UBS has sought to comply with the summons without violating Swiss law. As Swiss law prohibits UBS from producing responsive information located in Switzerland, Mr. Branson explained that UBS has been able to produce only information responsive to the summons that is located in the United States. He stated his belief that UBS has now complied with the summons to the fullest extent possible without subjecting its employees to criminal prosecution in Switzerland. [FN84]

Mr. Branson went on to state his belief that further enforcement of the summons would be in violation of the original QI agreement and the income tax treaty between Switzerland and the United States. With respect to the QI agreement entered into between UBS and the IRS in 2001, it expressly recognized that UBS would open and maintain accounts covered by Swiss financial privacy laws for U.S. clients who chose not to provide a Form W-9, as long as those accounts held no U.S. securities. According to Mr. Branson, as UBS legitimately maintained those accounts consistent with the QI agreement, the summons seeks client information that the IRS itself agreed would be kept confidential. Additionally, the income tax treaty between Switzerland and the United States discusses those circumstances under which client names and account information located in Switzerland may be shared with U.S. authorities. Mr. Branson, therefore, expressed his belief that the John Doe summons is inconsistent with long-standing treaty obligations and this matter should, instead, be resolved through diplomatic measures.

According to an article published in the *New York Times* on March 18, 2009, the Justice Department has extended its investigation into UBS offshore tax fraud to include independent lawyers and accountants in Switzerland and the United States who worked with UBS. [FN85] Three individuals currently under investigation include Beda Singenberger, a Zurich based accountant who runs a boutique finance and trust company called Sinco Trust, as well as Matthias W. Rickenbach and Andreas M. Rickenbach, two brothers that are lawyers at Rickenbach & Partner, a law firm in Zurich and Geneva. A criminal case is being built against these individuals who are suspected of having traveled with Swiss UBS bankers to the U.S. to work with American clients to evade taxes.

2008 PSI Report

The 2008 PSI Report includes several recommendations for strengthening the QI program, based primarily on its investigation of the UBS matter and a similar investigation of the Liechtenstein Global Trust Group (discussed below). First, the report recommends that QIs should be required to file Forms 1099 for all U.S. persons who are clients (whether or not the client has U.S. securities or receives U.S.-source income) and for all accounts beneficially owned by U.S. persons, even if the accounts are held in the name of a foreign corporation, trust, foundation, or other entity.

The report also recommends that the IRS close what the report describes as a gap in the QI program by expressly requiring QIs to apply to their QI reporting obligations all information obtained through their know-your-customer procedures to identify the beneficial owners of accounts. The 2008 PSI Report claims that the rules of the QI program are distinct from the know-your-customer rules that apply for due diligence purposes under the internal laws of the country in which the QI is located, although a QI must apply such know-your-customer rules as a prerequisite for entering into the

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QI program. As a result, the 2008 PSI Report concludes, some QIs, including UBS, have apparently taken the position that information the QI acquires about a particular customer as a result of satisfying the QI's requirements under applicable know-your-customer rules does not necessarily affect the determination of that customer's status for purposes of the QI program. Thus, for example, the report states that such a QI may take the position that it can rely on a certification of non-U.S. status (technically a Form W-8BEN) proffered by a foreign nominee owner (e.g., a Liechtenstein foundation) to establish that the nominee in fact is the beneficial owner of an account for withholding and reporting purposes under the QI program, even if the QI knows, as a result of satisfying the applicable know-your-customer rules, that a U.S. person is the actual beneficial owner of the account.

The better reading of the model QI agreement is that the gap identified by the 2008 PSI Report does not in fact exist, although admittedly the model QI agreement might be revised to make the point more explicitly. Very simply, a QI is a "withholding agent" for all U.S. tax purposes. The QI agreement expands the obligations of withholding agents under the relevant Treasury regulations, [FN86] but does not override them. Under the regulations (and, indeed, under the model QI agreement itself [FN87]), a withholding agent may not accept a certification of non-U.S. status (a Form W-8BEN) if the withholding agent has *actual knowledge* that the beneficial owner of the relevant income (the taxpayer) is a U.S. person. There is no obvious basis for concluding that information obtained through know-your-customer rules is irrelevant for this purpose. Moreover, the relevant Treasury regulations also provide that a withholding agent effectively must compare a Form W-8BEN that it receives with other account information in its possession, and reject the Form W-8BEN if it is inconsistent with that information. [FN88]

As a result, a straightforward reading of the model QI agreement, in the context of the Treasury regulations under which the QI program exists, is that a foreign QI cannot accept a Form W-8BEN certification of non-U.S. status where it has actual knowledge (whether obtained through know-your-customer rules or otherwise) that the beneficial owner of the income in question is a U.S. person or where the certification is inconsistent with other account information. The gap, to the extent one exists, is with the consistent treatment of foreign corporations, in particular, as entities separate from their owners for both know-your-customer and withholding tax purposes, but this is a different (and larger) issue.

The 2008 PSI Report also recommends that the IRS broaden QI audits to require external auditors to report evidence of fraudulent or illegal activity. [FN89] The report also recommends that the Treasury Department penalize banks located in tax haven jurisdictions that impede U.S. tax enforcement or fail to disclose accounts held directly or indirectly by U.S. clients by terminating their QI status. The report further recommends that Congress amend section 311 of the Patriot Act to allow the Treasury Department to bar such banks from doing business with U.S. financial institutions.

Potential modifications under IRS consideration

During 2008, the IRS announced that a series of potential modifications to the QI program to address certain of the issues raised by the PSI report and the UBS investigation. These modifications are described further below. The modifications do not, however, purport to address compliance and enforcement issues relating to bank secrecy laws. Section III of this pamphlet addresses that subject.

Announcement 2008-98

On October 14, 2008, the IRS released Announcement 2008-98, 2008-44 I.R.B. 1087, which describes proposed amendments to the QI agreement and to the QI audit guidance. The announcement contains three proposed changes, which are proposed to be effective for calendar years beginning after December 31, 2009. The first proposed change relates to internal controls; it requires a QI to ensure that specific employees are responsible for oversight of the QI's performance under the QI agreement, and that those employees take steps to prevent, deter, detect, and correct failures in performance. In addition, the QI agreement will be amended to require a QI to notify the IRS whenever the QI becomes aware of a material failure of internal controls relating to its performance under the QI agreement, any employee allega-

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tions of such failures, or any investigation by regulatory authorities of such failures. The IRS does not anticipate automatically terminating a QI agreement as a result of any such notice; instead, the IRS expects prompt notification to allow the IRS and the QI to work together to remedy such failures.

The second proposed change relates to additional fact finding during the basic fact finding phase (phase 1) of a QI audit to enable the IRS to evaluate risk. The QI audit guidance will be amended to add an audit procedure testing certain accounts for characteristics that suggest that a U.S. person has authority over the account. Such information will allow the IRS in the follow up fact finding phase (phase 2) of the audit process to evaluate the risk of any failure of controls and, if necessary, to request that the external auditor perform additional audit procedures.

Furthermore, the QI audit guidance will be amended to add additional procedures for fact gathering by the external auditor relating to the IRS's evaluation of the risk of a material failure of internal controls. These procedures will include, for instance, identifying the persons charged with oversight of performance under the QI agreement and the authority given them to prevent, deter, detect, and correct such failures on the part of other operational personnel. The external auditor will be required to report any facts and circumstances observed in the course of its audit that reasonably relate to the evaluation by the IRS of the risk of a material failure of internal controls.

The third proposed change relates to oversight and review of the QI audit. The QI audit guidance will be amended to require a QI's external auditor to associate a U.S. auditor with the audit and to require the U.S. auditor to accept joint responsibility for the performance of the procedures under the QI audit guidance. It is intended that joining a U.S. auditor to the QI audit will assure appropriate application of U.S. withholding rules and enhance accuracy and accountability in the audit process.

In addition to announcing the proposed changes, Announcement 2008-98 solicited public comments regarding the proposed changes. The government asked that such comments be submitted by February 28, 2009. Several comments were received. In general, the commenters objected to the proposed changes on the grounds that the commenters believed the proposed changes would impose additional costs and burdens on QIs with no, or only marginal, benefit to the IRS. Nevertheless, in a few instances, commenters offered specific technical suggestions in the event the IRS decides not to abandon completely the proposed changes. These suggestions generally were intended to make the proposed changes more understandable and consistent with the existing model QI agreement and QI audit guidance.

IRS Commissioner's testimony

The IRS Commissioner indicated in congressional testimony before the PSI in July 2008, and more recently before the PSI and Senate Committee on Finance in March 2009, that the IRS may make several modifications to the QI program intended to further improve its effectiveness in enhancing compliance. [FN90]

In particular, in his 2008 PSI testimony, the Commissioner indicated that the IRS was considering changing the regulations to require QIs to look through trusts or certain other offshore entities to determine if U.S. taxpayers are the beneficial owners of the accounts. Additionally the IRS may require external auditors that conduct the audits required under the QI agreements to report to the IRS indications of fraud or other illegal acts. Currently, there is no requirement for external auditors to make such reports to the IRS. The Commissioner indicated that the IRS was engaged in discussions with the major accounting firms that perform QI audits to identify ways to enhance the detection and reporting of violations of the QI agreement.

As recommended by the 2008 PSI Report, the Commissioner testified in July 2008, and again at both March 2009 hearings, that the IRS and Treasury are also considering regulations that would expand the QI program to require information reporting on additional sources of income for accounts held by U.S. persons. This reporting could include foreign as well as U.S.-source income; QIs are currently required to report only certain U.S.-source income received by U.S. customers who are not otherwise exempt from information reporting and backup withholding.

The Commissioner's March testimonies also include two additional measures to enhance and strengthen the QI pro-

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gram that are currently under consideration by the IRS and Treasury. The first is to strengthen the QI documentation rules, and the second is to require withholding for accounts in cases in which documentation is considered insufficient. The Commissioner provided little detail on either of these measures.

Since the Commissioner's July 2008 testimony, IRS and Treasury Department officials have made several public statements indicating that proposed regulations to further improve the QI program may be forthcoming in the near future. Few details, other than the release of Announcement 2008-98, discussed above, about these proposed regulations are available. However, it is possible that these proposed regulations, whenever issued, may include some, or all, of the changes the Commissioner indicated are under consideration.

Voluntary disclosure procedures

On March 26, 2009, the IRS issued a statement, together with internal field guidance, announcing voluntary disclosure procedures that may be applied to individual taxpayers with unreported offshore accounts and entities. In return for engaging in this voluntary disclosure, these taxpayers can avoid criminal prosecution. In general, the guidance provides that taxpayers who make voluntary disclosures will be required to make all delinquent filings (e.g., FBAR and other information returns), pay back-taxes and interest for six years, and an accuracy or delinquency penalty for all six years. Additionally, such taxpayers will be required to pay a penalty equal to 20 percent of the highest asset value in any unreported bank account at any time during the six-year period. The penalty amount may be reduced to only five percent if the taxpayer did not open the account, there was no account activity while the taxpayer controlled the account, and all taxes have been paid on the account. The IRS's offer took effect March 23, 2009, and is available for only six months. [FN91]

III. BANK SECRECY

Introduction

In connection with the implementation of the QI program in 2000, the IRS issued Announcement 2000-48 describing the approach that it intended to take in determining whether financial institutions in a particular country would be permitted to become QIs. The Announcement describes the QI program as a "paradigm shift to greater self-regulation," and states that Treasury and IRS believe that it is appropriate to permit the self-regulation envisioned by the QI system only under circumstances in which Treasury and IRS have confidence that such self-regulation may be effective.

In that regard, Announcement 2000-48 indicated that the Treasury Department and the IRS considered restricting the QI program to institutions operating in jurisdictions with which the United States has a bilateral tax treaty or tax information exchange agreement. However, in response to taxpayer requests that the QI program permit financial institutions to act as QIs in all jurisdictions in which they do business, the IRS decided not to limit the program to institutions in treaty jurisdictions.

Instead, Treasury and the IRS determined that the key criterion for qualification of a jurisdiction as eligible for the QI program was the existence of "know-your-customer rules." Announcement 2000-48 described know-your-customer rules as "a vital component of adequate self-regulation" and states that the IRS generally will not extend the QI program to any country that does not have know-your-customer rules or that has unacceptable know-your-customer rules. [FN92] Thus, as described earlier, the IRS, in Rev. Proc. 2000-12, required that a financial institution applying to become a QI provide detailed information regarding the know-your-customer rules applicable in each jurisdiction in which the institution wished to act as a QI.

The IRS does not require that an institution applying to become a QI provide information regarding bank secrecy or other laws that could apply in a foreign jurisdiction to restrict disclosure of the institution's customers to the IRS or otherwise affect the IRS's ability to enforce the terms of the QI agreement. Instead, Announcement 2000-48 stated that the IRS expected to apply more rigorous oversight to financial institutions or their branches in jurisdictions that are tax

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havens or bank secrecy jurisdictions and show an unwillingness to cooperate with the United States to reform their practices relating to transparency and the provision of tax information.. In addition, the Announcement indicated that QIs should not assume that, merely because they have an agreement covering a business in a particular jurisdiction, such jurisdiction would not later be identified as a specified tax haven or secrecy jurisdiction. However, Announcement 2000-48 indicated that any enhanced audit requirements or stricter enforcement standards would be imposed only on agreements entered into or renewed after identification of the jurisdiction as a specified tax haven or secrecy jurisdiction.

Announcement 2000-48 further stated that the IRS expected that it would agree to renew a QI agreement or, in the case of new agreements that become effective on or after January 1, 2004, enter a new agreement for QIs in a particular country only if the IRS receives a certification from the Treasury Department that the country has effective rules and/or procedures for providing tax information to the United States for both civil tax administration and criminal tax enforcement purposes (including, for example, under an income tax treaty or a tax information exchange agreement), or has taken significant steps towards achieving such effective provision of information. As described further below, the actions taken by the Treasury Department and IRS in connection with the execution of a TIEA with Liechtenstein are consistent with this approach.

Liechtenstein

On July 17, 2008, the PSI released a report (prepared in connection with a hearing held that day) examining the business practices of the Liechtenstein Global Trust Group ("LGT") in Liechtenstein and UBS in Switzerland, both of which are alleged to have facilitated tax evasion by U.S. clients of those institutions. [FN93] The report describes practices employed by LGT, a leading Liechtenstein financial institution that is alleged to have assisted U.S. clients in hiding assets offshore during the period from 1998 to 2007. According to the report, those practices included maintaining U.S. client accounts that were not disclosed to U.S. tax authorities; advising U.S. clients to open accounts in the name of Liechtenstein foundations to hide their beneficial ownership of the account assets; advising clients on the use of complex offshore structures to hide ownership of assets outside of Liechtenstein; and establishing "transfer corporations" to disguise asset transfers to and from LGT accounts. According to the report, LGT also advised clients on how to structure their investments to avoid disclosure to the IRS under the QI program. [FN94]

The LGT inquiry originated with an investigation by German authorities into the role of LGT in facilitating the evasion of German tax. [FN95] On February 25, 2008, the German authorities announced that they would share the information they had obtained in regard to LGT with authorities in other countries whose residents had utilized Liechtenstein to engage in tax evasion. [FN96] On February 26, 2008, the IRS issued a news release stating that it was initiating enforcement actions involving more than 100 U.S. taxpayers to ensure that they properly reported income, and paid taxes, in connection with accounts in Liechtenstein. [FN97] The news release also stated that the tax authorities in Australia, Canada, France, Italy, New Zealand, Sweden, the United Kingdom, and the United States were working together to address the use of Liechtenstein accounts for tax evasion purposes.

Both the PSI report and news accounts of the IRS and other investigations into the conduct of LGT suggest that Liechtenstein's favorable treatment of foundations, together with its bank secrecy laws, was important to LGT's ability to shield client assets from discovery by U.S. and other tax authorities. [FN98] In Liechtenstein, according to these accounts, foundations are effectively taxed at a very low rate, [FN99] are permitted to benefit their founders and their founders' families, [FN100] and are permitted to open bank accounts in their own names outside Liechtenstein (which provides foundation owners with ready access to cash outside Liechtenstein). Efforts to trace the owners or activities of nonpublic foundations are typically precluded by Liechtenstein's bank secrecy laws. Although these foundations function effectively as foreign trusts, the U.S. clients of LGT who established these foundations apparently did not file Forms 3520 (Annual Return to Report Transactions with Foreign Trusts and Receipt of Foreign Gifts) or 3520-A (Annual Information Return of Foreign Trust with a U.S. Owner), and LGT did not disclose the existence of bank accounts opened by these

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foundations (whether at LGT or other financial institutions) to the IRS. The U.S. clients typically did not file the FBAR form to disclose the existence of these accounts to the Treasury Department, apparently taking the position that only the nominal owner of the accounts were required to file.

On December 8, 2008, the U.S. signed a tax information exchange agreement ("TIEA") with Liechtenstein. [FN101] Under the terms of this agreement, the United States may seek information from Liechtenstein on all types of U.S. federal taxes, and in both civil and criminal tax matters, without regard to whether Liechtenstein needs the information for its own tax purposes or whether the conduct being investigated would constitute a crime under its laws. According to the terms of the TIEA, however, Liechtenstein must change its banking secrecy laws that prevent it from complying with the agreement. Specifically, Article 13 of the TIEA states: "Legislation necessary to comply with and give effect to the terms of this Agreement shall be enacted by December 31, 2009, to the extent necessary." [FN102] As a result of Liechtenstein entering into this TIEA, the U.S. has agreed to extend Liechtenstein's treatment as an eligible QI jurisdiction until December 31, 2009; prior to this agreement, that status was set to expire on December 31, 2008.

A. Bank Secrecy: General Background

The degrees of protection afforded financial information range from the relative transparency in the United States to the traditional opacity of jurisdictions such as Switzerland, Liechtenstein or the Cayman Islands. The term "bank secrecy" generally refers to a legal standard, whether judicial or statutory in origin, which prevents governmental access to the financial information necessary to ascertain beneficial ownership and enforce tax, securities and financial regulations. The limitations may apply only to certain entities operating within the jurisdiction or may apply only to the sharing of information with a foreign jurisdiction, [FN103] and are often reinforced by civil or criminal penalties.

The difficulties in piercing the "bank secrecy" of tax haven jurisdictions are related to the centuries-long tradition against one jurisdiction assisting another jurisdiction with collection of its taxes. This doctrine, known as the "Revenue Rule," is rooted in common law and sovereign immunity. It is often referred to as the Lord Mansfield Rule, who stated "For no country ever takes notice of the revenue laws of another." [FN104] Although its vitality and scope have been questioned, most recently in *Pasquatino v. United States*, [FN105] the doctrine remains a cornerstone of all common law jurisdictions, as well as many others, and is abrogated only by state-to -state negotiations, in the form of multilateral or bilateral international agreements or treaties. [FN106] Tensions arise when the confidentiality of the information sought is in conflict with the other state's interest in obtaining information relevant to law enforcement.

In the United States, rights to financial privacy are generally governed by statute, both in tax matters and other financial information, and protect one from public dissemination of information. The government's need to have access to financial information to assist it in detecting and preventing money-laundering led to enactment of the Bank Secrecy Act of 1970, [FN107] which requires U.S. financial institutions to maintain records and submit reports on certain cash or cash equivalent transactions. Since 1974, federal statute has established controls over how federal agencies gather, maintain and use personal information, including financial information. [FN108] The Right to Financial Privacy Act ensures that the government will not have access to information without service of a valid subpoena, consent of an account holder or as provided in the Code. [FN109] Further prohibitions on the disclosure of tax return information were enacted in 1976. [FN110]

Because the United States taxes its citizens and residents on their worldwide income, [FN111] it frequently needs foreign-based financial information to verify the accuracy of reporting by U.S. taxpayers. Obtaining that information requires a balancing of the U.S. interest in tax enforcement with the interests of the other state in maintaining confidentiality. In *Société Internationale v. Rogers*, [FN112] the Supreme Court articulated a basic rule of comity, holding unanimously that a United States district court could not ignore the interests of the foreign state in determining whether it would compel production of foreign based documents. Since then, courts balancing these conflicting U.S. and foreign interests [FN113] have tended to give greater weight to the United States' interests in cases involving money laundering or drug

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dealing, than in those involving tax compliance. Thus, in *U.S. v. Bank of Nova Scotia*, the court enforced a grand jury subpoena served in the United States for records maintained in the Cayman Islands, despite claims that the bank secrecy laws of that jurisdiction would not permit production. [FN114] In that case, the records were sought in connection with prosecution of money laundering and possible drug dealing.

By contrast, in cases in which the only U.S. law enforcement interest was tax compliance, results have been mixed. Although the Ninth Circuit Court of Appeals has enforced a grand jury subpoena for Swiss business records in a tax fraud case, [FN115] the Seventh Circuit Court of Appeals refused to enforce IRS administrative summons for Greek bank records in a tax case. [FN116]

In balancing the conflicting interests of the U.S. and foreign interests, courts will examine whether there exists a reasonable alternative to obtaining the requested information. [FN117] Another alternative means of obtaining documents from a foreign jurisdiction is through negotiations between the states, usually in the context of an income tax treaty or a tax information exchange agreements. The information exchange procedures available under treaties are described in Section IV of this document. The remainder of this Section III describes the statutory and other unilateral measures available to the IRS under present law in connection with obtaining offshore information.

B. Unilateral Measures to Facilitate Production of Foreign-Based Documents

In response to the difficulties in compelling production of information across borders, a variety of statutory measures have been enacted to require greater voluntary disclosure, at the risk of incurring penalties or adverse findings. These include specific authority for the Tax Court to order foreign entities invoking its jurisdiction to provide all relevant information, [FN118] and a statutory exclusionary rule affecting admissibility of foreign based documents that had not been produced earlier in administrative or judicial proceedings. [FN119] Each is a valuable tool, but is limited to the situation in which an offshore transaction has been identified and selected for examination; they do not assist in identifying an offshore transaction. In the latter situation, the IRS can make use of its authority to issue so-called “John Doe” summons, although recent experience has shown that enforcement of these summonses can be particularly difficult when the information sought is located in jurisdictions with restrictive bank secrecy laws.

1. Section 7456(b)

Any party who initiates proceedings in the United States Tax Court may be subject to an order compelling production of offshore materials that are subject to that party's control. The term control is not limited to legal control. If the party establishes to the Court's satisfaction that it is unable to produce the materials in court, it may be ordered to make the documents available for inspection wherever situated. Although the Tax Court has attempted to rely on this provision to order production of materials, despite local law prohibitions against disclosure, it has met with limited success. The orders requiring production have been used to enforce government requests for documents as well as interrogatories, [FN120] and may require that the party appear personally at hearings or proceedings. The sanctions for failure to comply may include entry of a default judgment, striking pleadings, or adverse findings as to the issues to which the documents relate.

2. Section 982 exclusionary rules

In 1984, Congress enacted section 982, which limits the evidentiary value of foreign-based information by barring its admissibility in a civil proceeding if it was not timely produced to the IRS in response to a formal request for foreign based documents. The provision permits a defense of reasonable cause for non-production, but specifically precludes a defense that foreign law prohibits disclosure of such information. [FN121] The exclusionary rule has been upheld, [FN122] and is useful in prompting compliance with requests for information that are otherwise difficult to enforce. Nev-

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ertheless, the exclusion is only of value in denying a taxpayer's ability to use the information in defense of its own position. It does not compel a taxpayer to produce information in its possession that would be adverse to its position or that would help the IRS develop and support an issue identified in an examination.

3. John Doe summonses

The IRS has broad statutory authority to require production of information in the course of an examination. [FN123] A request for information in the form of an administrative summons is enforceable if the IRS establishes its good faith, as evidenced by the four factors enunciated by the Supreme Court in *United States v. Powell*. [FN124] The *Powell* factors require that the information is sought for a legitimate law enforcement purpose, is of a type that will shed light on the subject of the examination, is not already in the possession of the IRS and that the IRS has complied with all applicable statutory requirements such as service of process. Subsequent to *United States v. Powell*, the legitimacy of using an administrative summons in furtherance of an investigation into criminal violations was validated in *United States v. LaSalle National Bank*, [FN125] in which the Supreme Court determined that the dual civil and criminal purpose was legitimate, so long as there had not yet been a commitment to refer the case for prosecution.

The use of this summons authority to obtain information from third-parties is subject to greater procedural safeguards, [FN126] but otherwise the same good faith elements are analyzed to determine whether the summons should be enforced. When the existence of a possibly non-compliant taxpayer is known but not his identity, as in the case of holders of offshore bank accounts, or investors in particular abusive transactions, the IRS is able to issue a summons to learn the identity of the taxpayer, but must first meet significantly greater statutory requirements, to guard against fishing expeditions.

An effort to learn the identity of unnamed "John Does" requires that the United States seek judicial review in an *ex parte* proceeding prior to issuance of the summons. In its application and supporting documents, [FN127] the United States must establish that the information sought pertains to an ascertainable group of persons, that there is a reasonable basis to believe that taxes have been avoided, and that the information is not otherwise available. [FN128] The reviewing court does not determine whether the summons will ultimately be enforceable. Once a court has determined that the predicate for issuance of a summons is met, the summons is served, and the summoned party served may challenge enforcement of the summons, based on the *Powell* factors. It is not entitled to judicial review of the ex parte ruling that permitted issuance of the summons. [FN129]

If a taxpayer whose liability is the subject of the summons either initiates or intervenes in a proceeding to challenge the enforcement of the summons, the limitations period for the tax year under investigation is suspended during the pendency of the proceeding. [FN130] The taxpayer whose identity is at issue in a John Doe summons would not initiate or intervene in a proceeding, and may not know of the proceeding. Nevertheless, enforcement of a John Doe summons is likely to be subject to time-consuming challenges, possibly warranting an extension of the limitations period.

Under current law, the limitations period for the tax year under investigation is suspended beginning six months after the service of a John Does summons, and ends with the final resolution of the response to the summons. [FN131] The chronology of the UBS investigation (described previously in Section II) illustrates the time-consuming nature of the process. The basis for requiring six months to elapse between service of the summons, after a court has found that there is a likelihood of non-compliance by an ascertainable group of taxpayers, is less apparent.

Offshore Credit Card Program

The Offshore Credit Card Program ("OCCP"), initiated by the IRS in 2000, illustrates the type of situation in which the IRS has sought to use John Doe summonses. The OCCP was designed to identify taxpayers who hide unreported income in offshore bank accounts and access the funds through credits cards issued by those banks. Between 2000 and 2002, the IRS issued a series of "John Doe" summonses to a variety of financial and commercial businesses to obtain information and records relating to U.S. residents who held credit, debit, or other payment cards issued by offshore banks. The IRS

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used the information and records obtained through those efforts to trace the identities of people using the payment cards. [FN132] As of July 31, 2003, the OCCP had resulted in approximately 2,800 tax returns being selected for audit, a number of which had been referred to the Criminal Investigation Division for possible action. [FN133] Subsequently, in January 2003, the IRS announced the Offshore Voluntary Compliance Initiative ("OVCI") to encourage the voluntary disclosure of previously unreported income placed by taxpayers in offshore accounts and accessed through credit card or other financial arrangements similar to those targeted by the OCCP. Under this program, the IRS waived the civil fraud penalty and certain penalties relating to failure to file information and other returns, including the Report of Foreign Bank and Financial Accounts ("FBAR"), [FN134] but taxpayers remained liable for back taxes, interest, and certain accuracy-related and delinquency penalties. [FN135] The IRS reported that, as of July 31, 2003, it had received OVCI applications from 1,299 taxpayers who paid over $75 million in taxes and identified over 400 offshore promoters of abusive credit card or other financial arrangements. [FN136] Then IRS Commissioner Mark Everson discussed the limited success of the OVCI initiative at a PSI hearing on August 1, 2006. Within his testimony, he stated "In reality, we did not have a good idea of the potential universe of individuals covered by this initiative. As a result, the incentive for taxpayers to come forward and take advantage of this initiative was diminished due to the fact that we did not have the ability to identify immediately and begin examinations for all non-participating individuals." [FN137]

IV. ADDRESSING CONFLICTING INTERESTS: EXCHANGE OF INFORMATION UNDER TAX TREATIES

Tax treaties establish the scope of information that can be exchanged between treaty parties. Exchange of information provisions first appeared in the late 1930s, [FN138] and are included in most [FN139] current double tax conventions to which the United States is a party. More recently, the United States started executing specific, separate tax information exchange agreements ("TIEAs"). Presently, the United States is a party to more than 80 double tax conventions and TIEAs that provide for the exchange of information upon request, and is in negotiations for several additional agreements. In addition, the United States is a member of the Convention on Mutual Administrative Assistance in Tax Matters, which includes provisions on the exchange of tax information.

Model double tax conventions adopted by the United States and the Organization for Economic Co-operation and Development (the "OECD") each include exchange of information provisions. While the OECD has adopted a model TIEA, the model presently being used by the United States Treasury Department is not publicly available.

A. Exchange of Information Under Double Tax Conventions

1. U.S. Model Agreement

Article 26 of the 2006 United States Model Income Tax Convention (the "U.S. Model") establishes (in paragraph 1) the obligation of each State to obtain and provide information to the other and provides assurances (in paragraph 2) that information exchanged will be treated as secret in accordance with the same disclosure restraints as information obtained under the laws of the requesting State.

Paragraph 3 of Article 26 provides that the obligation to exchange information does not require either State to: (a) carry out administrative measures that are at variance with the laws or administrative practices of either State; (b) supply information not obtainable under the laws or administrative practice of either State; or, (c) disclose trade secrets or other information where the disclosure of such information would be contrary to public policy. Paragraph 4 of Article 26 provides that when information is requested by one State, the requested State is obligated to obtain the requested information as if the tax in question were the tax of the requested State, even if the requested State has no direct tax interest in the case to which the request relates.

Paragraph 5 provides that a requested State may not decline to provide information because that information is held by financial institutions, nominees or persons acting in an agency or fiduciary capacity. This provision effectively prevents a

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requested State from relying on paragraph 3 to argue that its domestic bank secrecy laws override the obligation to exchange information.

Paragraph 6 of the 2006 U.S. Model provides the form in which information is to be provided in order to ensure that the information exchanged may be introduced in judicial proceedings held in the requesting State.

Paragraph 7 of the 2006 U.S. Model provides for assistance in the collection of taxes to the extent necessary to ensure that only those persons entitled to treaty benefits actually enjoy such treaty benefits.

Paragraph 8 of the 2006 U.S. Model provides that the requested State shall allow representatives of the requesting State to enter the requested State for purposes of interviewing witnesses and examining books and records. However, such access is granted only with the consent of the person subject to examination.

Paragraph 9 of the 2006 U.S. Model provides that the competent authorities of each State may further agree to the details for the exchange of information under Article 26. Although not expressly stated, this paragraph is interpreted as authorizing the exchange of information on a routine basis, upon request with respect to a specific case, or spontaneously. In this context, a routine exchange of information covers income subject to withholding tax. A spontaneous exchange of information occurs when information discovered during a tax examination indicates possible noncompliance with the laws of the other State is delivered to the other State even thought there is no previous request.

2. OECD Model Agreement

The information exchange provisions in the OECD Model Tax Convention on Income and Capital, approved on July 17, 2008 (the “OECD Model”) generally correspond to the first five paragraphs of the 2006 U.S. Model. [FN140] At the time the OECD Model was approved, several member countries expressly reserved with respect to paragraph 5 of Article 26 (prohibiting a requested State from declining to supply information because that information is held by a bank, other financial institution, nominee or person acting in an agency or fiduciary capacity, or because it relates to ownership interests in a person). These members were Austria, Switzerland, Luxembourg and Belgium, all of which have bank secrecy laws. Notably, each of these countries has recently announced its intention to adopt OECD standards for the exchange of tax information and transparency in order to avoid being placed on a potential new G-20 blacklist of uncooperative tax havens. [FN141]

3. Recent developments

Shortly after the adoption the 2006 U.S. Model, the United States executed a double tax convention with Belgium in which the exchange of information provision exceeded the scope of the 2006 U.S. Model (the “Belgium Treaty”). [FN142] Historically, Belgium's bank secrecy rules prevented Belgian banks from providing information about their clients to tax authorities. Earlier negotiations between the United States and Belgium were abandoned because Belgium refused to make any concessions with respect to its bank secrecy rules. [FN143] The Belgium Treaty, which entered into force on December 28, 2007, included three innovative provisions related to the exchange of information which link continuity of certain treaty benefits to changes in Belgium's laws, including banking secrecy laws:

- The zero rate of withholding applicable to dividends under Article 10, paragraph 12(a)(i) (Dividends) will be discontinued after five years unless the Secretary certifies to the U.S. Senate that Belgium has satisfactorily met its obligations under Article 25 (Exchange of Information and Administrative Assistance);
- The zero rate of withholding applicable to dividends under Article 10, paragraph 12(a)(ii) (Dividends) may be discontinued if the United States gives written notice by June 30 of any year. However, such notice may not be given unless the United States has determined that Belgium's actions with respect to Articles 24 (Mutual Agreement Procedure) and 25 (Exchange of Information and Administrative Assistance) have materially altered the balance of benefits of the double tax treaty; and,
- The inclusion of paragraphs 5 through 8 (which, with the exception of the first sentence in paragraph 5, are not part

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of the 2006 US Model) [FN144] establish Belgium's obligations to change its tax legislation, as implied by the zero withholding rate provisions of Article 10, paragraph 12 (Dividends). [FN145]

However, paragraph 7 of the Protocol to the Belgium Treaty specifically provides that (a) banking records will only be exchanged upon request and (b) the requested State may decline to provide information that it does not already possess unless the request identifies both a specific taxpayer and a specific bank or financial institution. This effectively precludes the United States from learning the identity of U.S. taxpayers with Belgian interests under the Belgium Treaty. Instead, the United States would be required to rely on its domestic authority to issue a John Doe summons (discussed above in Part III).

B. TIEAs

TIEAs are bilateral agreements governing the mutual exchange of information. Typically these agreements are executed with countries with which the United States does not have a double tax convention. The agreement with Liechtenstein, signed on December 8, 2008, is the United States' most recent TIEA.

Enactment of the Caribbean Basin Economic Recovery Act [FN146] (the "Act") in 1983 provided the initial catalyst for so-called tax haven countries to conclude TIEAs with the United States. Commonly referred to as the Caribbean Basin Initiative ("CBI"), Title II of the Act authorized unilateral preferential trade and tax benefits for eligible Caribbean countries, [FN147] including duty-free treatment of eligible products, if the country entered into a TIEA with the United States. [FN148] Subsequently, in 1984 [FN149] and 1986, [FN150] additional incentives were enacted; the 1984 provisions were designed to encourage non-CBI countries to execute TIEAs with the United States. TIEAs are entered into by Treasury, without the advice and consent of the Senate, upon the determination by the President that the agreement as negotiated is in the national security interest of the United States. [FN151]

1. U.S. TIEA Program

Initiated in 1984, the goals of the U.S. tax information exchange program are (a) assuring the accurate assessment and collection of taxes, (b) preventing fiscal fraud and tax evasion, and (c) developing improved information sources for tax matters in general. With respect to the United States, taxes covered are limited to national taxes, such that state and local taxes are not covered. The objectives of the TIEA include the prosecution of tax crimes, as well as the pursuit of civil tax claims. A State must have adequate process for obtaining information; if the State is required to enact measures providing such process, then the entry into force of the TIEA may be delayed until such requirements have been met. The requirements of the TIEA override individual State's laws and practices pertaining to disclosure of information regarding taxes, although this provision may be eliminated from a TIEA if the internal laws of the other State do not allow for bank secrecy or undisclosed (bearer) ownership of securities or shares.

2. OECD Model TIEA

In 2002, the OECD released its Agreement on Exchange of Information on Tax Matters (the "OECD Model TIEA"), together with commentary (the "Commentary"). The OECD Model TIEA was developed by the OECD Global Forum Working Group on Effective Exchange of Information, which consisted of representatives from OECD Member countries as well as delegates from Aruba, Bermuda, Bahrain, Cayman Islands, Cyprus, Isle of Man, Malta, Mauritius, the Netherlands Antilles, the Seychelles and San Marino. [FN152] It is represents the standard of the effective exchange of information for purposes of the OECD's initiative on harmful tax practices, [FN153] while at the same time does not seek to prescribe the precise format for achieving this standard. [FN154]

Article 5 (Exchange of Information Upon Request) of the OECD Model TIEA sets forth the requirements for exchanging information upon request; notably, there are no provisions for automatic and spontaneous exchanges of information.

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In addition, it provides that information requested with respect to a criminal matter must be exchange without regard to whether the conduct under investigation would constitute a crime under the laws of the requested State. [FN155] Paragraph 4 of Article 5 is intended to prohibit banks, other financial institutions and any person acting in an agency or fiduciary capacity, including nominees and trustees from claiming the right of privilege as the basis for declining an information request - unless the provisions of Article 7 (Possibility of Declining a Request) apply. This paragraph also effectively prevents any claim that bank secrecy should be considered protected as a matter of public policy (*ordre public*) for purposes of Article 7 [FN156] — which as noted in the Commentary, should only be invoked in extreme cases, such as an information request motivated by political or racial persecution. [FN157]

3. Recent developments

The most recent TIEA completed by the United States is with Liechtenstein (the “Liechtenstein TIEA”). Signed on December 8, 2008, the Liechtenstein TIEA requires each State to provide information that is foreseeably relevant to either a civil or criminal tax matter. [FN158] Although Liechtenstein has publicly stated that it still retains the right for a Liechtenstein court to decide the legitimacy of the request from the United States, [FN159] there are no unique terms in the Liechtenstein TIEA that provide for any extraordinary review beyond the “foreseeably relevant” standard.

The Liechtenstein TIEA requires that any changes or additions to domestic laws as may be necessary to give effect to the agreement must be enacted by December 31, 2009. [FN160] Accordingly, the Liechtenstein TIEA is not effective until each State has notified the other that it has completed the necessary internal procedures (including enacted of legislation) required for entry into force. [FN161] Although there is no publicly-available list of the changes that must be made to the Liechtenstein laws for this purpose, some commentators have noted that bank secrecy laws must be changed in order to give effect to the Liechtenstein TIEA. This conclusion may be consistent with public statements by Treasury, which has said that the Liechtenstein TIEA is significant because it “pierces bank secrecy.” [FN162]

In concluding the Liechtenstein TIEA, the United States took the additional step of agreeing to a one-year extension of Liechtenstein's eligibility as a QI jurisdiction, until December 31, 2009. [FN163] The IRS will not enter into a QI agreement if it has not received a specified list of items regarding the know-your-customer practices and procedures in the jurisdiction in which the applicant is seeking QI status. [FN164] In this regard, the IRS publishes a list of those countries with approved know-your-customer rules; as of the last update on December 8, 2008, Liechtenstein was included on this list. [FN165] However, ongoing inclusion in this list is not guaranteed, and the IRS has publicly stated that QIs “should not assume that, because they have an agreement covering a business in a particular jurisdiction, such jurisdiction will not later be identified as a specified tax haven or secrecy jurisdiction.” [FN166] For this purpose, a “specified tax haven or secrecy jurisdiction” is a jurisdiction that shows an unwillingness to cooperate with the United States to reform their practices related to transparency and the provision of tax information. [FN167] Thus, this temporary QI extension raises the question whether Liechtenstein may have been at risk of being identified as a specified tax haven or secrecy jurisdiction and delisted as an approved QI jurisdiction. Similarly, it raises the question whether a direct correlation should be inferred from the fact that the temporary extension ends on the same date by which Liechtenstein is required to make the necessary changes to its in domestic law by December 31, 2009 in accordance with Article 13 (Implementing Legislation).

On March 12, 2009, Liechtenstein announced that it intends comply with the OECD standards on transparency and exchange of information, [FN168] and to negotiate new bilateral agreements “that may go beyond OECD standards so as to provide particularly for effective exchange of information to address the global issue of tax fraud and tax evasion as well as double taxation.” [FN169] The announcement further states that Liechtenstein is prepared “to develop comprehensive solutions to protect the legitimate tax claims of other jurisdictions according to their fiscal sovereignty and to balance legitimate interests of jurisdictions” albeit while maintaining “solid and modern bank secrecy laws.” [FN170]

C. Convention on Mutual Administrative Assistance in Tax Matters

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In addition to double tax conventions and TIEAs, the Convention on Mutual Administrative Assistance in Tax Matters provides the United States with mechanisms to ensure the exchange of tax information. This multilateral treaty entered into force in 1995 and the following States are also members: Azerbaijan, Belgium, Denmark, Finland, France, Iceland, Italy, Netherlands, Norway, Poland, Sweden, and the United Kingdom. [FN171] Germany has signed, but not ratified, this agreement. Ukraine has signed and ratified this agreement.

D. Administration of U.S. Treaty Network

In order to administer its obligations under the network of bilateral treaties, the United States has delegated the role of Competent Authority for the treaties to the IRS. The Competent Authority is responsible for resolving disputes with the other contracting state about the scope or interpretation of the treaty. With respect to exchange of information articles, the Competent Authority determines whether the agency should present a request for information to a treaty partner as well as how to respond to any requests that it receives from the treaty partner. All information exchanged flows through the offices of the Competent Authorities, [FN172] and is safeguarded by the domestic laws of each state as well as the secrecy clause in the exchange of information article. In the United States, the taxpayer specific information received from a treaty partner is within the scope of 'return information' for purposes of protecting it from disclosure. Nonspecific information received from a partner is also protected from publication if its disclosure would harm tax administration, as determined by the Competent Authority in consultation with his counterpart. [FN173] Since the entry into force of the first treaty to include an exchange of information article, the United States has exchanged information with its partners in a variety of ways. [FN174] The principal types of information exchanges are generally referred to as routine, spontaneous or specific exchanges. In addition, there are industry-wide exchanges with certain treaty partners, and simultaneous examinations or criminal investigations with other partners.

1. Routine exchange of information

A "routine exchange of information" is one in which the contracting states have agreed that a category of information will be shared with one another on an ongoing basis, without the need for a specific request for same, because it is of a type that is consistently relevant to the tax administration of the receiving jurisdiction. Information that is automatically shared under this authority may include information that is not taxpayer specific, such as news about changes in domestic tax legislation, or it may be comprise voluminous taxpayer filings, such as magnetic disks containing the information from Forms 1042-S, relating to U.S. source fixed or determinable income paid to persons claiming to be residents of the receiving treaty country. The type of information, when it will be provided and how frequently, are typically determined by the respective Competent Authorities after consultation. The information will then be automatically provided. OECD has developed standards for the electronic format of such exchanges, to enhance their utility to tax administration. [FN175]

The international steps taken to standardize the information exchanged and improve its usefulness are a positive development, but there remain numerous shortcomings, both practical and legal, in the routine exchange of information. Chief among them is the failure to include taxpayer identification numbers ("TINs"), despite the strong recommendation of the OECD that member states provide such information. [FN176] Ideally, the information received by the IRS should either include a TIN or be subject to a process referred to as "TIN perfection" to enable the IRS to correlate account data in the information received with a valid TIN in its taxpayer databases. [FN177] Such an undertaking is time-consuming and costly. Other practical hurdles that limit its value are the lack of timeliness of its production, the fact that the data may not readily conform to U.S. taxable periods, the need to translate the language of the documents and the currencies, and its voluminous nature. [FN178]

These practical limitations are further exacerbated by the legal barriers to using the information to pursue FBAR penalties. The treaty information may only be used for a purpose consistent with the treaty. The FBAR penalties arise under

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Title 31 of the United States Code and are not generally within the scope of the taxes covered by the tax treaties. As a result, the treaty secrecy clause prevents sharing the information with those who investigate FBAR penalties. If foreign account information received under the treaty can be associated with a specific taxpayer's income tax accounts, it becomes tax return information, subject to the provisions of section 6103. Under section 6103, the information may be disclosed for "tax administration" purposes, as determined on a case-by-case basis. Even if the penalties are covered by the treaty, domestic legislation could prevent use of the information. Despite the likelihood that the information would readily establish the applicability of the penalties, it cannot be used for that purpose. In the face of competing priorities, it is not surprising that the IRS has made little use of the information. An adequate cost/benefit study of various means of strategically using the information is needed.

2. Spontaneous exchange of information

A "spontaneous exchange of information" occurs when one contracting state is in possession of an item of information that it determines may be of interest to the other contracting state for the tax administration of that other state. In such an instance, the first state will spontaneously provide the information to the treaty partner. In the United States, such information would typically be identified by a revenue agent or other employee, who would forward the information to the U.S. Competent Authority offices to decide whether the information should be forwarded to the foreign jurisdiction. Information spontaneously provided by a treaty partner to the United States is generally reviewed by the Exchange of Information program analyst or Tax Attache who first receives it, who then forwards it to an appropriate field office for further action and follows up to determine the outcome of the exchange.

3. Specific exchange of information

A "specific exchange" is a formal request by one contracting state for information that is relevant to an ongoing investigation of a particular tax matter. These cases are generally taxpayer specific. Those familiar with the case prepare a request that explains the background of the tax case and the need for the information. That request is forwarded to the Competent Authority, who determines whether to issue the request. If he determines that it is an appropriate use of the treaty authority, he forwards it to his counterpart. When a contracting state receives a specific request for information, it is obligated to use its powers to obtain the information to the same extent that it would do so if it were a domestic case, even if the information obtained could not be used in a domestic case.

4. Other exchanges of information

In addition to the traditional exchanges of information described above, the treaty partners may also work together to gain expertise about specific industries and to facilitate sharing of information when there is a common interest in the information. In those instances, they may arrange a meeting of agents or officials familiar with a particular industry or economic sector to share experiences, know-how, investigative techniques, and observations about trends in that industry. These discussions do not generally address the cases of specific taxpayers. The United States has also joined in the multilateral effort to form the Joint International Tax Shelter Information Centre, in 2004. It now operates with offices in Washington, D.C., and London, England. In addition to the United States, the members are Australia, Japan, the United Kingdom and Canada. Each has a bilateral treaty with each other member. If there is sufficient commonality in an issue or a specific taxpayer, there are procedures to conduct a simultaneous examination which will involve significant cooperation between the participating tax administrations. Both the industry wide meetings and the simultaneous examinations occur under the auspices of the exchange of information program; they are not in lieu of formal exchanges. They establish a process by which extensive exchanges of information can occur, with the assistance of an Exchange of Information analyst or Tax Attache.

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In addition to exchanging information with its treaty partners, assistance is provided under the mutual assistance article in the tax treaties. The United States has specifically agreed to provide mutual assistance in collection of the taxes of five treaty partners: France, Canada, Sweden, Denmark, and the Netherlands. The United States does so under its "Mutual Assistance Collection Program" (MCAP). [FN179] It also provides assistance via the Mutual Legal Assistance in Criminal Matters Treaties (MLATs). Unlike the tax treaties, the role of Competent Authority for MLATs is delegated to the Department of Justice. [FN180]

5. Litigation in support of exchange of information program

In addition to the resources devoted to administer its Exchange of Information program, the United States has litigated extensively in support of the program against a variety of challenges to actions it took to honor its treaty obligations. These challenges have included suits seeking to obtain publication of information received under treaty exchanges, objections to enforcement of adminstrative summonses and finally, an attempt to claim that the disclosure to another tax administrator was negligent.

The IRS successfully defended its efforts to protect the secrecy of certain information in internal memoranda, including the identity of the treaty partner that had communicated with the IRS. [FN181] The need to safeguard the secrecy of the information in order to protect the working relationship of the treaty partners was sufficient reason to sustain the government position that documents from meetings of Competent Authorities are entitled to treaty protection. [FN182]

In efforts to obtain the domestic information responsive to a treaty partner's request for information, the IRS uses its authority to issue administrative summonses. Specific challenges to IRS efforts to obtain financial information requested by a treaty partner frequently centered on whether the *United States v. Powell* 'good faith' elements were satisfied, in particular the need to comply with all procedural constraints. The extent to which the United States was required to look behind the statement of its treaty partner that the information was needed in a tax matter in the foreign jurisdiction was hotly contested, with taxpayers arguing that the foreign authorities should be required to meet the standards that would apply if the investigation were conducted in the United States. As previously stated, in a domestic case, if a matter had already been referred to the Department of Justice for criminal prosecution, a third-party record keeper summons would not be enforced. [FN183] In *United States v. Stuart*, [FN184] the question presented involved a request from Canada for information relevant to an investigation in that jurisdiction. The target of the investigation argued that the Internal Revenue Service lacked good faith, because it did not attempt to ascertain whether the Canadian tax investigation that led to Canada's treaty request had reached a stage analogous to an IRS referral to the Justice Department for criminal prosecution before issuing an administrative summons. The Court held that the summons was enforceable without such inquiry, stating, "We hold that neither the 1942 Convention nor domestic legislation imposes this precondition to issuance of an administrative summons. So long as the summons meets statutory requirements and is issued in good faith, as we defined that term in *United States v. Powell*, 379 U.S. 48, 57-58 (1964), compliance is required, whether or not the Canadian tax investigation is directed toward criminal prosecution under Canadian law." Since that opinion, numerous treaty summonses have been enforced, with little controversy.

In a suit for damages based on allegedly negligent or false disclosures made by the IRS to the Japanese National Tax Administration ("NTA"), the trial court granted summary judgment for the United States, rejecting a taxpayer claim that the NTA was an unreliable protector of treaty information and that disclosure to that treaty partner constituted negligence. [FN185] The United States disclosed information pursuant to its treaty with Japan in the course of a simultaneous examination. Following the disclosures to the NTA, Japanese media reported that a joint examination of plaintiffs had been conducted by the IRS and the NTA. That fact was true, but the articles also contained information that was untrue. Although plaintiffs cited to numerous rumors of leaks by the NTA of information from Japanese domestic audits, and NTA's failure to maintain the confidentiality of taxpayer information, they provided no other examples of an alleged NTA leaks of US/Japan tax treaty information. Plaintiff provided expert testimony that tax information was often repor-

ted in the press in Japan, in support of its claim that the United States should have known that information provided to NTA would not be safe from further disclosure. The court concluded that the witnesses did not establish that the information made available to the press came from NTA, nor did they prove that the source of the reports was treaty information. In granting summary judgment for the United States, the court stated:

> Free and open disclosure best serves the purposes of tax treaties - - ensuring that taxpayers correctly report and pay their domestic and foreign taxes. To require the United States to guarantee the accuracy of all information conveyed to treaty partners, especially in the preliminary stages, would have a chilling effect on furthering the purposes of the treaty. The IRS would not propose simultaneous examinations for fear of lawsuits for any misinformation contained in the proposal. ... The Court holds that negligently providing incorrect information in the course of a simultaneous examination does not rise to the level of actionable conduct.

According to the opinion, the IRS temporarily suspended the exchange of information with Japan under the treaty on the basis of the complaints by plaintiffs as well as earlier allegations that information had been improperly disclosed in Japan, according to an internal email placed in the record and as explained by an IRS official at his deposition.

E. Attempts to Develop an International Consensus

In the current global financial crisis, greater attention to all means of restoring integrity and stability to financial institutions has led to greater scrutiny of efforts to reconcile the conflicts between jurisdictions with strict bank secrecy and those seeking information from those jurisdictions in order to enforce their own laws. At the upcoming conference of the leaders of the G-20 nations, the regulation of offshore financial centers and how to achieve international consensus on such regulation is expected to be on the agenda. In “The Turner Review: A Regulatory Response to the Global Banking Crisis”, the Financial Services Authority of the United Kingdom identifies the need for global regulation of offshore financial centers as one of the action items necessary to establish a stable and effective banking system. Otherwise, improved harmonization of the regulation of major financial institutions within the jurisdictions of the G-20 nations could increase incentives for use of offshore centers. [FN186] The extent to which multilateral and bilateral agreements can effect the changes necessary to pierce bank secrecy merits careful consideration.

1. OECD Initiatives

OECD's work on its standards of transparency and exchange of information (the “OECD Standards”) was initiated in 1996 by its Global Forum on Transparency and Exchange of Information (“the “Global Forum”).

The OECD Standards require:

- Exchange of information where it is “foreseeably relevant” to the administration and enforcement of the domestic laws of a requesting State;
- No restrictions on exchange caused by bank secrecy or domestic tax interest requirements;
- Availability of reliable information and powers to obtain it;
- Respect for taxpayer rights; and
- Strict confidentiality of information exchanged. [FN187]

The OECD Standards were adopted by the G20 Ministers of Finance in 2004, and by the UN Committee on Experts on International Cooperation in Tax Matters in 2008.

Also initiated in 1996 was the OECD's Harmful Tax Practices Project, which is carried out through the Forum on Harmful Tax Practices (“FHTP”). FHTP focuses on: (a) eliminating harmful tax practices of preferential tax regimes of OECD Member states; (b) identifying tax havens and pursuing their commitments to OECD Standards; and, (c) encouraging other non-OECD counties to associate themselves with FHTP work. [FN188] As of 2000, FHTP had identified more than 40 tax havens. By 2005, 35 were “committed jurisdictions,” i.e., jurisdictions that formally documented their commitment to the OECD Standards. While seven tax havens initially refused to become committed jurisdictions, the

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current list of uncooperative tax havens is now comprised of just three: Andorra, Monaco, and Liechtenstein. However, each of these countries has recently announced its intention to implement the OECD standards. It is expected that the list of uncooperative tax havens will be discussed at the upcoming G-20 meeting scheduled for April 2.

Some of the jurisdictions that have recently announced their intention to commit to the OECD Standards have bank secrecy rules. It appears from the press releases issued that none will abandon these rules. These jurisdictions include Austria, Belgium, Liechtenstein, Luxembourg and Switzerland. Rather, each has identified the parameters for lifting banking secrecy rules for purposes of exchanging information. For example, Switzerland will permit the exchange of information upon receipt of a specific, justified request; Austria will exchange information upon request if there is a criminal proceeding involving a tax matter. In contrast, Andorra's government has announced that it will repeal its bank secrecy laws by the end of 2009.

It is presently unknown if such measures will satisfy the G-20 at its April meeting and keep such jurisdictions off the list of uncooperative tax havens. It is also unknown what penalties may be imposed on such jurisdictions.

1. European Union Savings Directive

In its foundational documents, the European Union established access to information and transparency as an important principle. [FN189] Since then, it has attempted to address the perceived tax evasion facilitated by bank secrecy laws of its member states and others. In June 2003, the European Council issued a directive designed to ensure that all interest earned by a citizen of a member state from an account held in any other member state would be subject to a minimal direct tax (“Savings Directive”). A directive is a non-self-executing resolution of the European Council that member states must implement, whether by local legislation or regulatory action. [FN190] The Savings Directive ensures that interest income earned by a citizen of one jurisdiction from an institution in another jurisdiction is subject to tax by the appropriate member state by requiring both information reporting by the financial institution to the member state and automatic exchange of such information reports among the member states. Member states were required to implement the directive by July 1, 2005.

A special longer transition period was provided for the several member countries whose jurisdictions were the least transparent among the member states. Belgium, Luxembourg and Austria do not permit exchange of information without a specific request for information on a specific taxpayer. Instead of agreeing to automatic exchange of information, they agreed to act as a withholding agent with respect to accounts in their jurisdictions. They collect tax and pay over tax to the home jurisdiction of the account holder without identifying the account holders. They are nevertheless entitled to receive the automatic exchange of information about their own citizens from the other states. [FN191]

[FN1]. This document may be cited as follows: Joint Committee on Taxation, *Tax Compliance and Enforcement Issues With Respect to Offshore Accounts and Entities* (JCX-23-09), March 30, 2009. This document can be found at www.jct.gov.

[FN2]. U.S. persons may be subject in certain cases to a “backup withholding” tax with respect to payments of investment income. This backup withholding tax serves as a backstop to the regular information reporting and tax return filing requirements, and does not apply where the U.S. payee has provided an Internal Revenue Service Form W-9 to the payor or where the U.S. payee is a so-called “exempt recipient” (including a corporation, tax-exempt organization or governmental entity). See, generally, sections 3406 and 6041 through 6049 and the Treasury Regulations thereunder. Unless otherwise indicated, all section references herein are to sections of the Internal Revenue Code of 1986, as amended (the “Code”). A copy of Form W-9 is included in the Appendix hereto.

[FN3]. See Treas. Reg. sec. 1.1441-1(b).

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[FN4]. Secs. 871(h) and 881(c). Congress believed that the imposition of a withholding tax on portfolio interest paid on debt obligations issued by U.S. persons might impair the ability of U.S. corporations to raise capital in the Eurobond market (i.e., the global market for U.S. dollar-denominated debt obligations). Congress also anticipated that repeal of the withholding tax on portfolio interest would allow the U.S. Treasury Department direct access to the Eurobond market. See Joint Committee on Taxation, General Explanation of the Revenue Provisions of the Deficit Reduction Act of 1984, JCS-41-84 (December 31, 1984), at 391-392.

[FN5]. Sec. 871(h)(3). A 10-percent shareholder includes any person who owns 10 percent or more of the total combined voting power of all classes of stock of the corporation (in the case of a corporate obligor), or 10 percent or more of the capital or profits interest of the partnership (in the case of a partnership obligor). The attribution rules of section 318 apply for this purpose, with certain modifications.

[FN6]. Sec. 871(h)(4). Contingent interest generally includes any interest if the amount of such interest is determined by reference to any receipts, sales or other cash flow of the debtor or a related person; any income or profits of the debtor or a related person; any change in value of any property of the debtor or a related person; or any dividend, partnership distributions, or similar payments made by the debtor or a related person, and any other type of contingent interest identified by Treasury regulation. Certain exceptions also apply.

[FN7]. Sec. 881(c)(3)(C). A related person includes, among other things, an individual owning more than 50 percent of the stock of the corporation by value, a corporation that is a member of the same controlled group (defined using a 50-percent common ownership test), a partnership if the same persons own more than 50 percent in value of the stock of the corporation and more than 50 percent of the capital interests in the partnership, any United States shareholder (as defined in section 951(b) and generally including any U.S. person who owns 10 percent or more of the voting stock of the corporation), and certain persons related to such a United States shareholder.

[FN8]. Sec. 881(c)(3)(A).

[FN9]. An obligation is treated as in registered form if (i) it is registered as to both principal and interest with the issuer (or its agent) and transfer of the obligation may be effected only by surrender of the old instrument and either the reissuance by the issuer of the old instrument to the new holder or the issuance by the issuer of a new instrument to the new holder, (ii) the right to principal and stated interest on the obligation may be transferred only through a book entry system maintained by the issuer or its agent, or (iii) the obligation is registered as to both principal and interest with the issuer or its agent and may be transferred through both of the foregoing methods. Treas. Reg. sec. 5f.103-1(c).

[FN10]. Sec. 871(h)(2)(B) and (5).

[FN11]. Secs. 871(h)(2)(A) and 163(f)(2)(A).

[FN12]. Treas. Reg. sec. 1.1441-1(b)(4)(iii).

[FN13]. Treas. Reg. sec. 1.1441-1(b)(4)(ii).

[FN14]. Secs. 871(g)(1)(B), 881(a)(3); Treas. Reg. sec. 1.1441-1(b)(4)(iv).

[FN15]. Treas. Reg. sec. 1.1461-1(c)(2)(ii)(A), (B). However, Treasury regulations require a bank to report interest on Form 1042-S if the recipient is a resident of Canada and the deposit is maintained at an office in the United States. Treas. Reg. secs. 1.6049-4(b)(5), 1.6094-8. This reporting is required to comply with the obligations of the United States under the U.S.-Canada income tax treaty. T.D. 8664, 1996-1 C.B. 292. In 2001, the IRS and Treasury Department issued pro-

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posed regulations that would require annual reporting to the IRS of U.S. bank deposit interest paid to any foreign individual. 66 Fed. Reg. 3925 (Jan. 17, 2001). The 2001 proposed regulations were withdrawn in 2002 and replaced with proposed regulations that would require reporting with respect to payments made only to residents of certain specified countries (Australia, Denmark, Finland, France, Germany, Greece, Ireland, Italy, the Netherlands, New Zealand, Norway, Portugal, Spain, Sweden, and the United Kingdom). 67 Fed. Reg. 50,386 (Aug. 2, 2002). The proposed regulations have not been finalized.

[FN16]. Sec. 871(a)(2). In most cases, however, an individual satisfying this presence test will be treated as a U.S. resident under section 7701(b)(3), and thus will be subject to full residence-based U.S. income taxation.

[FN17]. Secs. 881(a), 631(b), (c).

[FN18]. Treas. Reg. sec. 1.863-7(b)(1).

[FN19]. Treas. Reg. sec. 1.863-7(b)(3).

[FN20]. Treas. Reg. sections 1.861-2(a)(7) (substitute interest), 1.861-3(a)(6) (substitute dividends).

[FN21]. E.g., Reuven S. Avi-Yonah, The Structure of International Taxation: A Proposal for Simplification, 74 Texas Law Review 1301, 1305-08 (1996); Michael J. Graetz and Itai Grinberg, "Taxing International Portfolio Income," 56 Tax Law Review 537, 540-41 (Summer 2003).

[FN22]. *Economic and U.S. Income Tax Issues Raised by Sovereign Wealth Fund Investment in the United States*, JCX-49-08 (June 17, 2008), at 3-20.

[FN23]. Id. at 14.

[FN24]. Id. at 17. In addition, foreign governments in 2006 held official reserve assets in the United States of $2.77 trillion, up from $1.25 trillion only four years earlier. Id.

[FN25]. Id. at 14.

[FN26]. For tax year 2005, foreign payees received $378.4 billion of U.S.-source income, as reported on Form 1042-S, and $333.2 billion (88.0 percent) of this income was exempt from withholding. (Since interest on bank deposits is wholly exempt from withholding, these figures exclude interest income paid by U.S. banking businesses to foreign depositors.) A total of $6.7 billion in withholding tax was collected on the remaining $45.3 billion of U.S.-source income subject to withholding. This amount of withholding tax represented approximately two percent of the total amount of U.S.-source income reported on Form 1042-S. IRS Statistics of Income Bulletin, Winter 2009, Publication 1136, at 100. This amount arguably is significant in absolute terms, but of course is a small fraction of total foreign investment in the United States. For example, using the 2006 figures cited earlier of some $12 trillion in foreign portfolio and direct private investments in the United States, if one were to assume (solely for illustrative purposes) a five percent presumptive return on those investments, those investments would generate some $600 billion in (presumptive) income. $6.7 billion in withholding tax amounts to a little over one percent of that amount.

[FN27]. See, e.g., Reuven S. Avi-Yonah, "Memo to Congress: It's Time to Repeal the U.S. Portfolio Interest Exemption," Tax Notes International, Dec. 7, 1998, at 1817; Graetz and Grinberg, note 16, at 578 (arguing against source-based withholding taxes and expressing the view that residence-based taxation of foreign portfolio income is possible through continued unilateral and multilateral enforcement and information exchange efforts). For a general discussion of the dif-

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ficulties in collecting residence-based taxes given globalization and technological developments such as electronic commerce and money, see Vito Tanzi, "Globalization, Technological Developments, and the Work of Fiscal Termites," 26 Brooklyn Journal of International Law 1261 (2001).

[FN28]. In general, the U.S. information reporting and backup withholding system as it applies to both domestic and foreign investors operates on the basis of offering investors an implicit choice: either the investor can furnish the requisite identifying information (e.g., a Form W-9 for domestic individual investors, or a Form W-8 for a foreign investor), or the investor can suffer withholding tax (technically, backup withholding tax in the case of a U.S. investor or, in most cases, an unidentified investor). While it is true that withholding tax protects government revenues (although not to the extent of the highest individual tax rate), it might be argued that noncompliance with these identification requirements can be evidence of more general noncompliance activity by the taxpayer, which in turn would be relevant to the IRS. As a result, it might be argued (for example) that interest should simply not be payable to a foreign account (or from a U.S. bank account) unless the requisite forms are provided. This approach would go far beyond current law, and might in turn be viewed as unduly intrusive into taxpayer privacy (with potentially adverse effects on U.S. borrowers' ability to raise funds). Alternatively, the backup withholding rate could be increased to the highest marginal tax rate applicable to individuals, or an even higher rate, in order to provide a greater incentive for compliance.

[FN29]. Copies of the Forms W-8 and their instructions are included in the Appendix hereto.

[FN30]. The Form W-8ECI requires that the beneficial owner specify the items of income to which the form is intended to apply and certify that those amounts are effectively connected with the conduct of a trade or business in the United States and includible in the beneficial owner's gross income for the taxable year.

[FN31]. The Form W-8EXP requires that the beneficial owner certify as to its qualification as a foreign government, an international organization, a foreign central bank of issue or a foreign tax-exempt organization, in each case meeting certain requirements.

[FN32]. A corporation (and not its shareholders) ordinarily is treated as the beneficial owner of the corporation's income; as a result, this problem technically is not one of withholding tax noncompliance as much as it is noncompliance with the rules governing U.S. owners of controlled foreign corporations or passive foreign investment companies. Similarly, a foreign complex trust ordinarily is treated as the beneficial owner of income that it receives, and a U.S. beneficiary or grantor is not subject to tax on that income unless and until he receives a distribution. However, as described by the Senate Permanent Subcommittee on Investigations, Committee on Homeland Security and Governmental Affairs, in its 2006 report, Tax Haven Abuses: the Enablers, the Tools and Secrecy, S. Hrg. 109-797, 109th Cong., 2d Sess. (August 1, 2006), arrangements such as "trust protectors" have been employed by U.S. taxpayers to achieve substantial control over assets held in offshore trusts. The UBS case, described later in this pamphlet, also involved the use of nominee and sham entities to conceal the assets and income of U.S. taxpayers.

[FN33]. In limited cases, the intermediary may furnish other documentary evidence of the status of the beneficial owner, rather than a Form W-8.

[FN34]. Rev. Proc. 2003-64, 2003-32 I.R.B. 306 (July 10, 2003), provides procedures for qualification as a withholding foreign partnership or withholding foreign trust and model withholding agreements.

[FN35]. See Treas. Reg. sec. 1.1441-1(b)(5).

[FN36]. Treas. Reg. sec. 1.1461-1(b), (c). Copies of Form 1042, Form 1042-S and their instructions are included in the

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Appendix hereto.

[FN37]. At the end of June 2008, the notional amount of interest rate derivatives (that is, the value of financial assets underlying the derivatives) outstanding worldwide was $458.3 trillion. Bank for International Settlements, Monetary and Economic Department, "OTC Derivatives Market Activity in the First Half of 2008" (November 2008), at 2.

[FN38]. Secs. 861(a)(2)(A), 871(a)(1)(A), 881(a)(1).

[FN39]. Amounts owed by each party under a total return swap typically are netted so that only one party makes an actual payment.

[FN40]. Treas. Reg. section 1.863-7(b)(1). For a fuller discussion of sourcing and other tax issues related to derivatives transactions, see Joint Committee on Taxation, Present Law and Analysis Relating to the Tax Treatment of Derivatives (JCX-21-08), March 4, 2008. For a presentation of various hypothetical equity and interest rate swaps and stock lending transactions and a discussion of whether and when imposition of withholding tax might be appropriate, see David P. Hariton, "Equity Derivatives, Inbound Capital, and Outbound Withholding Tax," 60 Tax Lawyer 313 (Winter 2007). As a policy matter, Hariton argues that the withholding tax on U.S.-source dividends should be eliminated.

[FN41]. See Hariton, note 32, at 324-25.

[FN42]. For an extensive discussion of swap transactions entered into by U.S. financial institutions, offshore hedge funds, and other taxpayers, see United States Senate, Permanent Subcommittee on Investigations, Committee on Homeland Security and Governmental Affairs, "Dividend Tax Abuse: How Offshore Entities Dodge Taxes on U.S. Stock Dividends," Staff Report, Sept. 11, 2008.

[FN43]. Anita Raghavan, "IRS Probes Tax Goal of Derivatives," Wall Street Journal, July 19, 2007, C1; Anita Raghavan, "Happy Returns: How Lehman Sold Plan to Sidestep Tax Man -- Hedge Funds Use Swaps to Avoid Dividend Hit; IRS Seeks Information," Wall Street Journal, Sept. 17, 2007, A1.

[FN44]. E.g., Hariton, note 32, at 346-50; Gregory May, "Flying on Instruments: Synthetic Investment and the Avoidance of Withholding Tax," Tax Notes, Dec. 9, 1996, at 1225.

[FN45]. Statement of Reuven S. Avi-Yonah, Irwin I. Cohn Professor of Law, University of Michigan Law School, Testimony Before the Subcommittee on Select Revenue Measures of the House Committee on Ways and Means, March 5, 2008, available at http://waysandmeans.house.gov/hearings.asp? formmode=printfriendly&id =6821 (last accessed March 25, 2009.

[FN46]. S. 506, 111th Cong., 1st Sess. (2009), section 108; H.R. 1265, 111th Cong., 1st Sess. (2009), section 108.

[FN47]. U.S. Model Income Tax Convention of November 15, 2006, Articles 10, 11, and 12.

[FN48]. See, for example, Article 10(3) of the income tax treaty between the United States and the United Kingdom. Other U.S. treaties that include a zero rate of withholding tax on direct dividends are the income tax treaties with Australia, Belgium, Denmark, Finland, Germany, Iceland, Japan, and Sweden.

[FN49]. *Aiken Industries, Inc. v. Commissioner*, 56 T.C. 925 (1971).

[FN50]. Section 894(c).

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[FN51]. H.R. 3970, 110th Cong., 1st Sess. (2007), section 3204. Rep. Doggett introduced a similar, though more restrictive, bill. H.R. 3160, 110th Cong. 1st Sess. (2007). The provision in H.R. 3970 would allow the treaty reduction in withholding tax if the parent corporation was eligible for the benefits of an income tax treaty with the United States. By contrast, if the rate of withholding tax applicable under the U.S. income tax treaty with the parent corporation's country of residence were higher than the rate under the U.S. income tax treaty with the subsidiary's country of organization, H.R. 3160 would apply the higher rate.

[FN52]. Treas. Reg. section 1.881-3; T.D. 8611 (Aug. 10, 1995).

[FN53]. The beneficial owner of income is, generally, the person who is required under U.S. tax principles to include the income in gross income on a tax return. A person is not a beneficial owner of income, however, to the extent that person is receiving the income as a nominee, agent, or a custodian, or to the extent that the person is a conduit whose participation in a transaction is disregarded. Foreign partnerships, foreign simple trusts, and foreign grantor trusts are not the beneficial owners of income paid to the partnership or trust. The beneficial owner of income paid to a foreign estate is the estate itself. See Treas. Reg. sec. 1.1441-1(c)(6) and the Instructions to Form 1042-S.

[FN54]. See, e.g., Treas. Reg. section 1.1441-1(b)(2)(vii)(A) (providing that a withholding agent generally can rely on a Form W-8 or similar documentation if, before the payment, the agent holds the documentation, can reliably determine how much of the payment relates to the documentation, and has no actual knowledge or reason to know that any of the information, certifications, or statements in or associated with the documentation are incorrect).

[FN55]. Government Accountability Office, Report to the Committee on Finance, U.S. Senate, "*Tax Compliance: Qualified Intermediary Program Provides Some Assurance that Taxes on Foreign Investors Are Withheld and Reported, but Can Be Improved*" (GAO-08-99), December 2007 (hereafter GAO Report).

[FN56]. As previously noted, a corporation (and not its shareholders) ordinarily is treated as the beneficial owner of the corporation's income. Similarly, a foreign complex trust ordinarily is treated as the beneficial owner of income that it receives, and a U.S. beneficiary or grantor is not subject to tax on that income unless and until he receives a distribution.

[FN57]. GAO Report at 15-16, 21.

[FN58]. Statement of Reuven S. Avi-Yonah, Irwin I. Cohn Professor of Law, University of Michigan Law School, Testimony Before the Subcommittee on Select Revenue Measures of the House Committee on Ways and Means, March 5, 2008, available at http://waysandmeans.house.gov/hearings.asp? formmode=printfriendly&id =6821 (last accessed March 25, 2009); Reuven S. Avi-Yonah, "Memo to Congress: It's Time to Repeal the U.S. Portfolio Interest Exemption," Tax Notes International, Dec. 7, 1998, at 1817.

[FN59]. Council Directive 2003/48/EC of 3 June 2003 on Taxation of Savings Income in the Form of Interest Payments, available at http:// eurlex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2003:157:0038:0048:en:PDF (last accessed March 25, 2009). To address avoidance of the Directive, the European Commission has proposed amendments that would, among other changes, extend the Directive to interest-equivalents and require payors to apply the Directive when payments are made to non-EU intermediaries on behalf of beneficial owners who reside in the EU. See Proposal for a Council Directive amending Directive 2003/48/EC on Taxation of Savings Income in the Form of Interest Payments, November 13, 2008, available at http:// ec.europa.eu/taxation_customs/resources/documents/taxation/personal_ tax/ savings_tax/savings_directive_review/COM(2008)727_en.pdf.

[FN60]. Rules similar to the rules for Austria, Belgium, and Luxembourg apply under EU savings agreements with An-

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dorra, Liechtenstein, San Marino, Monaco, and Switzerland and under bilateral agreements between individual EU states and the ten dependent and associated territories of the United Kingdom and the Netherlands (Anguilla, Aruba, the British Virgin Islands, the Cayman Islands, Guernsey, the Isle of Man, Jersey, Montserrat, the Netherlands Antilles and the Turks and Caicos Islands).

[FN61]. Michael J. Graetz & Itai Grinberg, "Taxing International Portfolio Income," 56 Tax Law Review 537, 578-86 (Summer 2003). (More broadly, Graetz and Grinberg argue that the United States should pursue a policy of national neutrality in the taxation of foreign portfolio income and therefore should allow a deduction, not a credit, for foreign taxes imposed on that income.)

[FN62]. 61 Fed. Reg. 17,614 (Apr. 22, 1996).

[FN63]. T.D. 8734 (Oct. 6, 1997). The regulations specific to QIs have subsequently been amended. See T.D. 8804 (Dec. 30, 1998) (delaying effective date and providing additional transition rules); T.D. 8856 (Dec. 30, 1999) (delaying effective date); and T.D. 8881 (May 16, 2000) (providing for withholding rate pools for QIs and changing model QI agreement regulations to conform with Rev. Proc. 2000-12, which includes a provision requiring a QI to disinvest in cases in which a non-exempt U.S. customer does not waive local bank secrecy laws).

[FN64]. Treas. Reg. sec. 1.1441-1(e)(5).

[FN65]. Announcement 2000-48, 2000-1 C.B. 1243.

[FN66]. Id. After December 31, 2006, however, branches located in countries without approved know-your-customer rules are no longer permitted to operate as QIs. See Notice 2006-35, 2006-14 I.R.B. 708.

[FN67]. See Tax Equity and Fiscal Responsibility Act of 1982, sec. 342.

[FN68]. The definition also includes: a foreign branch or office of a U.S. financial institution or U.S. clearing organization; a foreign corporation for purposes of presenting income tax treaty claims on behalf of its shareholders; and any other person acceptable to the Internal Revenue Service. Treas. Reg. sec. 1.1441-1(e)(5)(ii).

[FN69]. U.S. withholding agents are allowed to rely on a QI's Form W-8IMY without any underlying beneficial owner documentation. By contrast, non-QIs are required both to provide a Form W-8IMY to a U.S. withholding agent and to forward with that document Form W-8s or W-9s for each beneficial owner.

[FN70]. Rev. Proc. 2000-12, 2000-1 C.B. 387, *supplemented by* Announcement 2000-50, 2000-1 C.B. 998, and *modified by* Rev. Proc. 2003-64, 2003-2 C.B. 306, and Rev. Proc. 2005-77, 2005-2 C.B. 1176. The QI agreement applies only to foreign financial institutions, foreign clearing organizations, and foreign branches or offices of U.S. financial institutions or U.S. clearing organizations. However, the principles of the QI agreement may be used to conclude agreements with other persons defined as QIs. In addition, the IRS may choose to enter into a QI agreement that deviates from the model agreement.

[FN71]. Written Testimony of Douglas H. Shulman, Commissioner, Internal Revenue Service, Hearing on Tax Issues Related to Ponzi Schemes and an Update on Offshore Tax Evasion Legislation Before the S. Comm. on Fin., 111th Cong., Mar. 17, 2009 [hereinafter Shulman 2009 SFC Testimony].

[FN72]. Government Accountability Office, *Testimony of Michael Brostek Before the Committee on Finance, U.S. Senate: Tax Compliance: Offshore Financial Activity Creates Enforcement Issues for IRS*, GAO-09-478T (Mar. 17, 2009), at

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[FN73]. Additional detail can be found in Joint Committee on Taxation, *Selected Issues Relating to Tax Compliance With Respect to Offshore Accounts and Entities* (JCX-65-08), July 23, 2008.

[FN74]. This absence of a requirement to disclose a U.S. exempt recipient is consistent with the fact that exempt recipients are excluded from the scope of the general rules governing backup withholding and information reporting.

[FN75]. This rule restricts one of the principal benefits of the QI regime, nondisclosure of account holders, to financial institutions that have assumed the documentation and other obligations associated with QI status.

[FN76]. Form 1042-S is the IRS form on which a withholding agent reports a foreign person's U.S.-source income that is subject to reporting to the foreign person and to the IRS.

[FN77]. These amounts are statutorily exempt from nonresident withholding when paid to non-U.S. persons.

[FN78]. Non-U.S. investments can generate amounts subject to information reporting if they are not considered paid outside the U.S. under Treas. Reg. 1.6049-5(e). Payments are not considered paid outside the U.S. if the customer has transmitted instructions to an agent, branch, or office of the institution from inside the U.S. by mail, phone, electronic transmission, or otherwise, unless the transmission from the U.S. has taken place in isolated and infrequent circumstances.

[FN79]. Rev. Proc. 2002-55, 2002-2 C.B. 435.

[FN80]. See Written Testimony of Douglas H. Shulman, Commissioner, Internal Revenue Service, Hearing on Tax Haven Banks and U.S. Tax Compliance Before the Permanent Subcomm. on Investigations, S. Comm. on Homeland Sec. and Governmental Affairs, 110th Cong., July 17, 2008 [hereinafter Shulman 2008 Testimony]. The difference between signed agreements and active agreements is due to mergers, acquisitions, and terminations. As of July 2008, the IRS had issued 600 default letters and had terminated 100 QI agreements.

[FN81]. See *United States v. UBS AG*, 09-60033-CR-COHN (S.D. Fl.).

[FN82]. Written Testimony of John DiCicco, Acting Assistant Attorney General, Tax Division, U.S. Department of Justice, Hearing on Tax Haven Banks and U.S. Tax Compliance—Obtaining the Names of U.S. Clients with Swiss Accounts Before the Permanent Subcomm. on Investigations, S. Comm. On Homeland Sec. and Governmental Affairs, 111th Cong., Mar. 4, 2009.

[FN83]. Written Testimony of Mark Branson, Chief Financial Officer of UBS AG, Hearing on Tax Haven Banks and U.S. Tax Compliance — Obtaining the Names of U.S. Clients with Swiss Accounts Before the Permanent Subcomm. on Investigations, S. Comm. On Homeland Sec. and Governmental Affairs, 111th Cong., March 4, 2009.

[FN84]. The Swiss banking authority with the permission of the Swiss government had allowed UBS to agree to transfer approximately 250 names of United States resident account holders for which there is a reasonable suspicion of conduct constituting what Swiss law considers fraudulent acts to the Justice Department as part of the deferred prosecution agreement. See Lee Sheppard, *Don't Ask, Don't Tell, Part III: UBS's Sweet Deal*, 122 Tax Notes 1050 (2009).

[FN85]. Lynnley Browning, *U.S. Extends Its Inquiry of Offshore Tax Fraud*, N.Y. Times, Mar. 18, 2009, at B3.

[FN86]. Principally, Treasury Regulation sections 1.1441-1 and 1.1441-7.

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[FN87]. See Section 5.10 of the model QI agreement, as set forth in Rev. Proc. 2000-12, 2000-1 C.B. 387.

[FN88]. Treasury Regulation section 1.1441-7(b)(4).

[FN89]. A similar recommendation was made in a 2007 report prepared by the Government Accountability Office (the "GAO") on the QI program. The report generally found that the QI program provides some assurance that tax on U.S.-source income sent offshore is properly withheld and reported. However, the report offered four recommendations for the IRS to further improve the QI program. In addition to recommending that external auditors report fraud or illegal acts, the report recommended that the IRS: (1) measure U.S. withholding agents' reliance on self-certified documentation and use that data in its compliance efforts; (2) determine why some funds are reported to unknown jurisdictions and to unidentified recipients and take appropriate steps to recover withholding taxes that should have been paid and to better ensure that U.S. taxes are withheld; and (3) require electronic filing of forms in QI agreements whenever possible. Government Accountability Office, *Tax Compliance: Qualified Intermediary Program Provides Some Assurance that Taxes on Foreign Investors Are Withheld and Reported, but Can Be Improved*, GAO-08-99 (Dec. 19, 2007).

[FN90]. See Shulman 2008 Testimony, *supra*; Shulman 2009 SFC Testimony, *supra*; and Written Testimony of Douglas H. Shulman, Commissioner, Internal Revenue Service, Hearing on Tax Haven Banks and Offshore Compliance—Obtaining the Names of U.S. Clients with Swiss Accounts Before the Permanent Subcomm. on Investigations, S. Comm. on Homeland Sec. and Governmental Affairs, 111th Cong., Mar. 4, 2009 [hereinafter Shulman 2009 PSI Testimony].

[FN91]. Kristen A. Parillo & Jeremiah Coder, *IRS Reduces Penalties on Voluntarily Disclosed Offshore Accounts*, 2009 Tax Notes Today 57-2.

[FN92]. However, the IRS will permit a branch of a financial institution located in such a country to act as a QI if the branch is part of an entity organized in a country that has acceptable know-your-customer rules and the entity agrees to apply its home country know-your-customer rules to the branch.

[FN93]. Tax Haven Banks and U.S. Tax Compliance, Permanent Subcommittee on Investigations of the Committee on Homeland Security and Governmental Affairs of the U.S. Senate (July 17, 2008). The UBS matter is described in Section II of this document.

[FN94]. The QI program is discussed in detail in Section II of this document.

[FN95]. For additional background on this investigation, see Nicholas Kulish & Carter Dougherty, *Deutsche Post Chief Under Tax Inquiry*, N.Y. Times, Feb. 15, 2008, at C4; Randall Jackson, *The Mouse that Roared: Liechtenstein's Tax Mess*, 49 Tax Notes Int'l 707 (2008) [hereafter Jackson, *The Mouse that Roared*]; Mark Landler, *Liechtenstein Seeks Man Suspected of Selling Information that Led to Tax Scandal*, N.Y. Times, Mar. 13, 2008, at C3.

[FN96]. Jackson, *The Mouse that Roared, supra*.

[FN97]. News Release, Internal Revenue Service, IRS and Tax Treaty Partners Target Liechtenstein Accounts, IR-2008-26 (Feb. 26, 2008).

[FN98]. See 2008 PSI Report at 36-37; Jackson, *The Mouse that Roared, supra*.

[FN99]. Foundations are generally exempt from income taxes in Liechtenstein. However, they are subject to an annual capital tax, which is generally equal to the greater of 0.1 percent of the foundation's capital or CHF 1,000 (approximately

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U.S. $980). Other taxes may apply, including a stamp duty on formation (equal to no more than 1.0 percent of taxable capital) and a tax on the transfer of securities (equal to 0.15 percent for Liechtenstein securities and 0.30 percent for foreign securities).

[FN100]. Liechtenstein does not tax distributions to beneficiaries residing outside Liechtenstein.

[FN101]. Agreement Between the Government of the United States of America and the Government of the Principality of Liechtenstein on Tax Cooperation and the Exchange of Information Relating to Taxes.

[FN102]. In this regard, the Liechtenstein government released a statement on March 12, 2009 that it "accepts the OECD standards on transparency and information exchange in tax matters and supports the international measures against non-compliance with tax laws." Andrew Ross Sorkin, *Liechtenstein Pledges Tax Openness*, N.Y. Times Deal Book, Mar. 12, 2009.

[FN103]. "*Tax Co-operation: Towards a Level Playing Field*," 2008 Assessment by the Global Forum on Taxation, OECD, tabulates the numerous permutations by which information that is available to the host jurisdiction may or may not be shared with a requesting state.

[FN104]. *Holman v. Johnson*, 98 Eng. Rep. 1120 (K.B. 1775), cited in *AG of Canada v. R.J. Reynolds Tobacco Holdings, Inc*., 268 F.3d 103, *cert. denied*, 537 U.S. 1000 (2002).

[FN105]. 544 U.S. 349; 125 S. Ct. 1766; 161 L. Ed. 2d 619 (2005)

[FN106]. The United States has mutual assistance in collection agreements with five treaty partners, i.e., France, Canada, Sweden, Denmark, and the Netherlands.

[FN107]. 31 U.S.C. Secs. 5311-5314e, 5316-5332e; 12 U.S.C. secs. 1829b and 1951-1959e.

[FN108]. Privacy Act of 1974, 5 U.S.C. sec. 552a.

[FN109]. 12 U.S.C. 3402.

[FN110]. I.R.C. sec. 6103;

[FN111]. *Cook v. Tait*, 265 U.S. 47 (1924)

[FN112]. 357 U.S. 197 (1958)

[FN113]. The balancing test is summarized in the Restatement 3rd on Foreign Relations Law as follows: (a) A court or agency in the United States, when authorized by statute or rule of court, may order a person subject to its jurisdiction to produce documents, objects, or other information relevant to an action or investigation, even if the information or the person in possession of the information is outside the United States; (b) failure to comply with an order to produce information may subject the person to whom the order is directed to sanctions, including finding of contempt, dismissal of a claim or defense, or default judgment, or may lead to a determination that the facts to which the order was addressed are as asserted by the opposing party; and (c) in deciding whether to issue an order directing production of information located abroad, and in framing such an order, a court or agency in the United States should take into account the importance to the investigation or litigation of the documents or other information requested; the degree of specificity of the request; whether the information originated in the United States; the availability of alternative means of securing the in-

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formation; and the extent to which noncompliance with the request would undermine important interests of the United States, or compliance with the request would undermine important interests of the state where the information is located. Restatement 3d, Foreign Relations, sec. 441(1).

[FN114]. 691 F2d 1384 (11th Cir. 1982), *cert*. denied 462 U.S. 1119 (1983).

[FN115]. *United States v. Vetco*, 691 F.2d 1281 (9th Cir. 1981).

[FN116]. *United States v. First National Bank of Chicago*, 699 F. 2d 341 (7th Cir. 1983).

[FN117]. Restatement 3d, Foreign Relations, sec. 441(1)(c).

[FN118]. Sec. 7465(b)

[FN119]. Sec. 982

[FN120]. *Gerling International Insurance Co. v. Commissioner*, 839 F. 2d 131 (3rd Cir. 1988); *Hong Kong Shanghai Banking Corporation v. Commissioner*, 85 T.C. (1985)

[FN121]. Sec. 982(b)(2).

[FN122]. *Flying Tigers Oil Co. v. Commissioner*, 92 T.C. 1261 (1989).

[FN123]. Sec. 7602.

[FN124]. *United States v. Powell*, 379 U.S. 48 (1964).

[FN125]. 437 U.S. 298 (1978); codified in section 7609(c)

[FN126]. Sec. 7609.

[FN127]. Sec. 7609(h)(2) provides that the determination will be made *ex parte*, solely on the pleadings.

[FN128]. Sec. 7609(f).

[FN129]. *United States v. Samuels, Kramer & Co., and First Western Government Securities, Inc.*, 712 F.2d 1342 (9th Cir. 1983), which affirmed a lower court determination that the issuance of the John Doe summons was not subject to review, but reversed and remanded to permit a limited evidentiary hearing on whether the *Powell* standard was met.

[FN130]. Sec. 7609(e)(1).

[FN131]. Sec. 7609(e)(2).

[FN132]. News Release, Internal Revenue Service, IR-2003-95 (July 31, 2003); General Accounting Office, *Internal Revenue Service: Challenges Remain in Combating Abusive Tax Schemes*, GAO-04-50, at 10-11 (Nov. 19, 2003) [hereafter GAO, *Challenges Remain*].

[FN133]. News Release, Internal Revenue Service, IR-2003-95 (July 31, 2003).

[FN134]. News Release, Internal Revenue Service, IR-2003-48 (April 10, 2003). Taxpayers wishing to participate in the

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OVCI program were required to apply before April 15, 2003. The FBAR reporting requirements are discussed in Section II of this document.

[FN135]. Rev. Proc. 2003-11, 2003-1 C.B. 311; News Release, Internal Revenue Service, IR-2003-5 (Jan. 14, 2003); GAO, *Challenges Remain, supra*, at 12; General Accounting Office, *Testimony of Michael Brostek Before the Committee on Finance, U.S. Senate: Taxpayer Information: Data Sharing and Analysis May Enhance Tax Compliance and Improve Immigration Eligibility Decisions*, GAO-04-972T (Nov. 19, 2003).

[FN136]. News Release, Internal Revenue Service, IR-2003-95 (July 31, 2003).

[FN137]. Written Testimony of Commissioner of Internal Revenue Mark Everson Before Senate Committee on Homeland Security and Governmental Affairs' Permanent Subcommittee on Investigations Hearing on Offshore Abuses: The Enablers, The Tools and Offshore Secrecy, 109th Cong., August 1, 2006.

[FN138]. The United States' first double tax convention was entered into in 1932 with France; it did not contain an exchange of information provision. Article XV of the U.S.-Sweden Double Tax Convention, signed on March 23, 1939, included the United States' first the exchange of information provision. This was followed shortly by a second double tax convention with France, signed on July 25, 1939, which provided for the exchange of information in Article 26.

[FN139]. The 1973 income tax treaty between the USSR and the United States does not have an exchange of information provision. It still applies to the countries of Armenia, Azerbaijan, Belarus, Georgia, Kirgizstan, Moldova, Tajikistan, Turkmenistan, and Uzbekistan.

[FN140]. Paragraph 1 of the OECD Model provides, however, for the exchange of information imposed on behalf of each respective State, or “of their political subdivisions or local authorities.” In contrast, the U.S. Model is silent with respect to taxes imposed by political subdivisions and local authorities and the technical explanation specifically states that the Article 26 applies with respect to “taxes of every kind applied at the national level.” The OECD Model does not incorporate paragraphs 6 through 9 (described above) of the U.S. Model.

[FN141]. Randall Jackson, Kristen A. Parillo and David D. Stewart, *Tax Havens Agree to OECD Standards*, 53 Tax Notes Int'l 1027 (2009) [hereinafter, Tax Havens Agree].

[FN142]. The U.S. Model was adopted on November 15, 2006. The Convention Between the Government of the United States of America and the Government of the Kingdom of Belgium for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income was signed on November 26, 2006.

[FN143]. Marc Quaghebeur, *Belgium Uses Tax Treaties to Attract Investment*, 45 Tax Notes Int'l 1055, 1055 (March 19, 2007).

[FN144]. The provisions of paragraph 6 appear to correspond to commentary included in the technical explanation of the 2006 U.S. Model regarding the statute of limitations.

[FN145]. Marc Quaghebeur, *Belgian Parliament Ratifies Belgium-US Tax Treaty*, 46 Tax Notes Int'l 768, 776 (May 21, 2007).

[FN146]. P.L. No. 98-67.

[FN147]. See sec. 212(a)(1)(A) of the Act for the list of eligible countries. The list is updated by Rev. Rul. 2007-28,

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2007-1 C.B. 1039.

[FN148]. Alternatively, eligible CBI countries could qualify based on a double tax convention with the United States that contained an effective exchange of information program. Section 927(e)(3)(B).

[FN149]. Pursuant to the Deficit Reduction Act, P. L. No. 98-369, a foreign sales corporation established under section 927 could be organized in any foreign country (not just CBI eligible countries) provided that the country had concluded either a TIEA or a double tax convention with the United States meeting the requirements of section 274(h)(6)(A). Section 927(e)(3) (repealed for transactions after 9/30/2000 by P.L. 105-519); Treas. Reg. secs. 1.921-2(d) (A-7, part (i)) and 1.922-1(e) (A-5, part (ii)).

[FN150]. The Tax Reform Act of 1986, P.L. 99-514, added another incentive for eligible CBI countries by treating certain income derived from investments in that country as qualified possessions source investment income for purposes of the section 936 credit (allowing possession corporations a tax credit for U.S. taxes imposed on income earned by such corporations), provided that the eligible CBI country had concluded either a TIEA or a double tax convention with the United States meeting the requirements of section 274(h)(6)(A). Section 936(d)(4), flush language (repealed in 1996 by the Small Business Job Protection Act, P.L. 104-188, which provided for the 10-year phase out of the credit in section 936(j)).

[FN151]. Section 274(h)(3)(C); See also, *Barquero vs. United States*, 18 F.3d 1311, 1314-1315 (5th Cir. 1994); and *Treaties and Other International Agreements: the Role of the United States Senate, A Study Prepared for the Committee on Foreign Relations, United States Senate*, Congressional Research Service, Library of Congress (January, 2001), S. Prt. 106-71.

[FN152]. OECD Model TIEA, Introduction, paragraph 2.

[FN153]. OECD Model TIEA, Introduction, paragraph 3.

[FN154]. OECD Model TIEA, Introduction, paragraph 6.

[FN155]. Commentary to OECD Model TIEA, Article 5, paragraph 1, at (¶39-40).

[FN156]. Commentary to OECD Model TIEA, Article 5, paragraph 4, at (¶46).

[FN157]. Commentary to OECD Model TIEA, Article 7, paragraph 4, at (¶91).

[FN158]. Agreement Between the Government of the United States of America and the Government of the Principality of Liechtenstein on Tax Cooperation and the Exchange of Information Relating to Taxes, Article 1 [hereinafter, Lichtenstein TIEA].

[FN159]. Press Release, December 8, 2009, http:// www.presseportal.ch/de/pm/100000148/100574800/presse_informationsamt_ liechtenstein?pre=1

[FN160]. Lichtenstein TIEA, Article 13.

[FN161]. Lichtenstein TIEA, Article 15.

[FN162]. Charles Gnaedinger, *Liechtenstein, U.S. Sign Tax Information Exchange Agreement*, Tax Notes Today, December 9, 2008, citing Jesse Eggert, an attorney-adviser at the Treasury Department.

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[FN163]. Protocol to the Liechtenstein TIEA, set forth in the Appendix, paragraph 10.

[FN164]. Rev. Proc. 2000-12, 2000-1 C.B. 387, at Section 3.02.

[FN165]. See *http://www.irs.gov/businesses/international/article/0,, id=96618,00.html*.

[FN166]. I RS Announcement 2000-48, 2000-1 C.B. 1243.

[FN167]. Id.

[FN168]. See *infra* Section IV.E.1.

[FN169]. The Liechtenstein Declaration, March 12, 2009, *http:// www.oecd.org/dataoecd/27/21/42340216.pdf*.

[FN170]. Id.

[FN171]. The United States reserved as to several articles in that treaty, including the provisions that would require collection assistance.

[FN172]. In the United States, the requests are initially received by Tax Attaches, or, in the case of France or Canada, the Exchange of Information Team program analysts in Washington. I.R.M. par. 4.60.1.1(6)(b).

[FN173]. Sec. 6105.

[FN174]. In calendar year 2007, the United States made 1,429,499 disclosures of information to foreign countries under the exchange of information program. See Joint Committee on Taxation, Disclosure Report for Public Inspection Pursuant to Internal Revenue Code Section 6103(p)(3)(C) for Calendar Year 2007(JCX-47-08), June 3, 2008, at 3.

[FN175]. See Module 3 of "Manual On The Implementation of Exchange of Information Provisions for Tax Purposes", OECD Committee on Fiscal Affairs (23 January 2006).

[FN176]. *OECD Recommendation on the use of Tax Identification Numbers in an International Context* [C(97)29/FINAL], recommends at Article 4: "The information referred to in Article 2 of this Memorandum shall, as much as possible, be provided in a magnetic or electronic format following the Recommendation of the Council on the Use of the Revised OECD Standard Magnetic Format for Automatic Exchange of Information [C(97)30/FINAL] or any further updated format recommended by the Council. This information shall include, as much as possible, the Tax Identification Numbers in the residence and source country of the non-resident recipients of income[.]"

[FN177]. *Letter from Commissioner, IRS to Chairman, Senate Finance Committee* (June 12, 2006), 2006 TNT 115-17.

[FN178]. Id.

[FN179]. See, I.R.M. Pars. 11.3.25.5 and 11.3.25.6

[FN180]. See, I.R.M. Pars. 11.3.28.3.2.

[FN181]. *Tax Analysts v. IRS*, 152 F. Supp. 2d 1, 9 (D.D.C. 2001), rev'd in part on other grounds, 1 2002 WL 1300028 (D.C. Cir. 2002)). Congress enacted section 6105, which explicitly provides that information obtained under a treaty and not taxpayer-specific is nevertheless protected information.

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[FN182]. *Tax Analysts v. Internal Revenue Service*, 217 F. Supp. 2d 23 (D. D.C. 2002)

[FN183]. Sec. 7602(c); *United States v. LaSalle National Bank*, 437 U.S. 298 (1978).

[FN184]. 489 U.S. 353; 109 S. Ct. 1183; 103 L. Ed. 2d 388 (1989)

[FN185]. *Aloe Vera of America, Inc. v. United States*, 2007-1 U.S. Tax Cases Par 50,325; 99 AFTR 2d 895 (USDC D. AZ 2/2/2007).

[FN186]. *The Turner Review: A Regulatory Response to the Global Banking Crisis*, Financial Services Authority, United Kingdom, March 2009, at 7 and 74.

[FN187]. Overview of the OECD's Work on International Tax Evasion (A note by the OECD Secretariat) 3, (Mar. 23, 2009) [hereinafter 2009 OECD Overview].

[FN188]. 2009 OECD Overview at 3-4.

[FN189]. "Declaration on the right of access to information", *Treaty on European Union*, entered into force November 1, 1993, O.J. C. 191, 29 July 1992 [hereinafter Maastricht Treaty].

[FN190]. Maastricht Treaty, Art. 249

[FN191]. Council Directive 2003/48/EC of 3 June 2003, OJ L 157 (26-6-2003).

In Re:

Dear:

This letter is to inform you that the voluntary disclosure of your client, , has been preliminarily accepted. This acceptance is conditioned upon the information provided by being, and remaining, truthful, timely, and complete.

A voluntary disclosure will not automatically guarantee immunity from prosecution; however, a voluntary disclosure may result in prosecution not being recommended.

Please be aware that to make a voluntary disclosure complete, your client must fully cooperate with the IRS in determining the correct and appropriate tax liability and pay or make bona fide arrangements to pay in full, any tax, interest, and penalties determined by the IRS to be applicable. This required cooperation includes the production of all requested documents and the taxpayer submitting to an interview if requested by the examining agent.

Your client's voluntary disclosure will be forwarded for civil examination and the determination of the correct tax liability. A Revenue Agent will be contacting you regarding this matter.

This matter may be considered for the imposition of additional civil sanctions and/or criminal investigation should a subsequent determination be made that your client has not fully cooperated and/or has provided materially false information.

If you have any further questions, I can be contacted at .

Sincerely,

Special Agent in Charge

FEDERAL SENTENCING GUIDELINES MANUAL

Volume 1

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2008 EDITION

UNITED STATES SENTENCING COMMISSION

Effective November 1, 1987

Including

November 1, 2008 Amendments to Guidelines, Policy Statements, and Commentary -- Also-- Highlights of Guideline Amendments Supreme Court Decisions Affecting the Federal Sentencing Guidelines Statutory Index Index to Guidelines Manual

§5K2.16. Voluntary Disclosure of Offense (Policy Statement)

If the defendant voluntarily discloses to authorities the existence of, and accepts responsibility for, the offense prior to the discovery of such offense, and if such offense was unlikely to have been discovered otherwise, a downward departure may be warranted. For example, a downward departure under this section might be considered where a defendant, motivated by remorse, discloses an offense that otherwise would have remained undiscovered. This provision does not apply where the motivating factor is the defendant's knowledge that discovery of the offense is likely or imminent, or where the defendant's disclosure occurs in connection with the investigation or prosecution of the defendant for related conduct.

Historical Note: Effective November 1, 1991 (see Appendix C, amendment 420). Amended effective November 1, 2004 (see Appendix C, amendment 674).

§5K2.17. Semiautomatic Firearms Capable of Accepting Large Capacity Magazine (Policy Statement)

If the defendant possessed a semiautomatic firearm capable of accepting a large capacity magazine in connection with a crime of violence or controlled substance offense, an upward departure may be warranted. A “semiautomatic firearm capable of accepting a large capacity magazine” means a semiautomatic firearm that has the ability to fire many rounds without reloading because at the time of the offense (A) the firearm had attached to it a magazine or similar device that could accept more than 15 rounds of ammunition; or (B) a magazine or similar device that could accept more than 15 rounds of ammunition was in close proximity to the firearm. The extent of any increase should depend upon the degree to which the nature of the weapon increased the likelihood of death or injury in the circumstances of the particular case.

Commentary

Application Note:

1. “Crime of violence” and “controlled substance offense” are defined in §4B1.2 (Definitions of Terms Used in Section 4B1.1).

Historical Note: Effective November 1, 1995 (see Appendix C, amendment 531). Amended effective November 1, 2006 (see Appendix C, amendment 691).

§5K2.18. Violent Street Gangs (Policy Statement)

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If the defendant is subject to an enhanced sentence under 18 U.S.C. § 521 (pertaining to criminal street gangs), an upward departure may be warranted. The purpose of this departure provision is to enhance the sentences of defendants who participate in groups, clubs, organizations, or associations that use violence to further their ends. It is to be noted that there may be cases in which 18 U.S.C. § 521 applies, but no violence is

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Tax Penalties

IRS Should Evaluate Penalty Administration, Effect on Voluntary Compliance, GAO Says

The commissioner of internal revenue should direct his agency's Office of Servicewide Penalties to evaluate the administration of penalties and their effect on voluntary compliance, with a plan to focus its efforts, the Government Accountability Office said in a report released July 6.

The Internal Revenue Service commissioner also should use standard outreach methods to “again alert taxpayers of the need to disclose reportable loss transactions,” GAO said, noting that guidance on a new penalty for failure to disclose the transactions was timely but left some practitioners with questions.

The oversight office said although OSP does not comprehensively evaluate the administration of civil tax penalties or their impact on voluntary compliance, a plan could help it to do so.

Grassley Weighs In

Senate Finance Committee ranking Republican Charies Grassley (Iowa) July 6 issued a statement in response to the report urging the agency to follow GAO's recommendations.

“The IRS has a lot of discretion over assessing and rescinding tax penalties,” Grassley said. “This report shows the IRS rescinded about one-third of the penalties assessed in 2007. It assessed $29.5 billion in penalties and later rescinded $11.1 billion of that.”

The Iowa Republican noted that “it's impossible to know whether that amount was fair and justified because the IRS doesn't comprehensively evaluate tax penalty administration or the impact of penalties on voluntary tax compliance.

“The IRS promises to do a better job of evaluating tax penalties, and it needs to,” Grassley said. “Fair administration from one taxpayer to the next is critical to the integrity of the tax system.”

Efforts of Penalty Office Seen Falling Short

The GAO report found that although the IRS penalty office is charged with collecting information to evaluate penalties and penalty information and determining the effectiveness of penalties in promoting voluntary compliance, it currently does not do so on a broad scale due to resource constraints, methodological barriers, and limitations in available databases.

Rather, GAO found, OSP analysts focus on short-term issues, such as sudden spikes in assessments or abatements.

Despite the challenges, GAO said it believes planning could alleviate the problems the penalty office faces in fulfilling its broader mission. “A plan could help IRS focus its efforts and address the constraints to evaluating penalties,” the report said.

“In developing a plan, IRS could identify the analyses it should do and the resources needed to do them,” GAO said, noting OSP could then determine available resources and those that still might be needed to accomplish the task.

Plan Seen as Key to Improvement

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The report said a plan also could lay out feasible research for evaluating the effect of penalties on voluntary compliance. For example, GAO said, “fairness is believed to undergird voluntary compliance. Thus, analyses that determine whether penalties are being consistently applied across IRS would provide pertinent information.”

In looking at IRS's implementation of a penalty for failure to disclose reportable transactions, GAO noted guidance was issued within three months of enactment of the penalty. However, the oversight office said practitioners have asked for more targeted outreach about the penalty, particularly in difficult economic times.

Specifically, GAO said, practitioners are concerned about loss transactions “caused by the current economic climate in which many taxpayers may experience losses that could trigger the reportable transaction requirements.”

The report said that while IRS officials recognize the need to raise awareness, their planned outreach efforts would reach only a small portion of return preparers and taxpayers.

Daily Tax Report: All Issues > 2009 > July > 07/09/2009 > TaxCore® - Treasury Documents > Reports > Treasury Report, ‘Update on Reducing the Federal Tax Gap and Improving Voluntary Compliance’

Treasury Report, ‘Update on Reducing the Federal Tax Gap and Improving Voluntary Compliance’

Update on Reducing the Federal Tax Gap and Improving Voluntary Compliance

U.S. Department of the Treasury
July 8, 2009

I. Introduction

The Internal Revenue Service (IRS) collects 96 percent of the government's total receipts, approximately $2.7 trillion in FY 2008. The vast majority of those revenues come from taxpayers who voluntarily report and pay the taxes that they owe. The IRS has estimated the overall voluntary compliance rate to be approximately 84 percent.

Despite the voluntary compliance rate and vigorous enforcement by the IRS, a significant amount of revenue remains unreported and unpaid. In 2005, the IRS estimated this gross tax gap to be approximately $345 billion. After subtracting revenue obtained through enforcement actions and other late payments, the IRS estimated the net tax gap to be approximately $290 billion. These estimates, which remain the most recent estimates available, were conducted using data collected in tax year 2001 and before.

As a result of an increase in funding included in the IRS FY 2009 budget, the Department of the Treasury (Treasury) and the IRS have recently initiated intensive efforts to update the estimate of the tax gap on an ongoing basis, which will permit more regular and effective assessments. Consistent with its commitment to long-term fiscal soundness, the Administration is committed to working closely with Congress to narrow the tax gap, which imposes an unfair burden on every American who pays taxes in full. Ongoing updates of the tax gap estimate starting in 2011 will form the basis for regularly assessing progress towards that goal.

Building on reports previously released, this report is intended to provide a comprehensive overview of efforts to close the tax gap. This report is also intended to serve as a baseline for further work and discussion. After briefly discussing the nature and scope of the tax gap, this report summarizes previous Treasury and IRS tax gap reports and identifies the areas of strategic priority detailed in those reports. This report then summarizes the achievements, ongoing efforts, and new initiatives for achieving progress in each of those areas of strategic priority, organized according to the components of the strategy to reduce the tax gap detailed in prior reports.

As this report will make clear, the IRS and Treasury, working with Congress, are pursuing a wide range of initiatives, including a series of legislative proposals included in the Administration's FY 2010 budget. The Administration recognizes the particular value of those efforts and initiatives that improve voluntary compliance by making the tax filing process easier and more taxpayer-friendly. While aggressive enforcement activity can also help to narrow the tax gap, it is

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important to recognize that increased enforcement efforts require certain trade-offs. The Administration is committed to working closely with Congress to strike an appropriate balance to maximize revenue collection without imposing unreasonable compliance and enforcement burdens on the vast majority of individuals and businesses that fully and willingly pay what they owe.

II. The Tax Gap

The Tax Gap Map that follows illustrates the nature and scope of the tax gap based on data from 2001 and prior years. As this map shows, noncompliance takes three forms:

• Underreporting (not reporting one's full tax liability on a timely-filed return);

• Underpayment (not timely paying the full amount of tax reported on a timely-filed return); and

• Nonfiling (not filing required returns on time and not paying the full amount of tax that should have been shown on the required return).

The IRS has separate tax gap estimates for each of these three types of noncompliance. Underreporting (in the form of unreported receipts and overstated expenses) constitutes over 82 percent of the gross tax gap. The single largest subcomponent of underreporting involves the individual income tax, which represents more than 50 percent of the total tax gap. Underpayment constitutes nearly 10 percent, and nonfiling almost 8 percent of the gross tax gap.

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III. Prior Tax Gap Reports

In September 2006, Treasury's Office of Tax Policy issued a Comprehensive Strategy for Reducing the Tax Gap. [FN1] The 2006 report provided a primer on the components and measures of the tax gap and a seven-component strategy for reducing the tax gap. The components of that strategy are:

1. Reduce Opportunities for Evasion
2. Make a Multi-Year Commitment to Research
3. Continue Improvements in Information Technology
4. Improve Compliance Activities
5. Enhance Taxpayer Service
6. Reform and Simplify the Tax Law
7. Coordinate with Partners and Stakeholders

Following on this report, the Internal Revenue Service in August 2007 issued a more detailed report on Reducing the Federal Tax Gap: A Report on Improving Voluntary Compliance. [FN2] Emphasizing the same seven components outlined above, the 2007 report outlined specific projects and initiatives, legislative proposals, and other actions designed to attack the sources of noncompliance in each area. Four key principles guided the development of the strategy and continue to guide Treasury and IRS efforts to improve compliance:

• First, both unintentional taxpayer errors and intentional taxpayer evasion should be addressed.

• Second, sources of noncompliance should be targeted with specificity.

• Third, enforcement activities should be combined with a commitment to taxpayer service.

• Fourth, policy positions and compliance proposals should be sensitive to taxpayer rights and maintain an appropriate balance between enforcement activity and imposition of taxpayer burden.

The 2007 tax gap report also provided a detailed explanation of the composition of the tax gap. That explanation is reproduced in full in the appendix of this report.

IV. Update on Efforts to Reduce the Federal Tax Gap: Progress on Strategic

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Components

The prior tax gap reports detailed a seven-component strategy to reduce the tax gap and discussed and proposed specific actions to be taken within each component. This section of the report provides an update on those efforts, including a discussion of new proposals. The following section discusses the current IRS Strategic Plan, issued subsequent to the 2007 tax gap report, which covers FY 2009-2013, and outlines five long-term measures for evaluating the IRS' progress in achieving its goals, which directly relate to the tax gap strategy.

Component 1: Reduce Opportunities for Evasion

Implement and Expand Information Reporting Authorities

Previous reports have outlined the relationship between voluntary compliance and the degree to which income tax return items are “visible” to the IRS. Reporting compliance is highest where parties other than the taxpayer are required to file information reports and withhold taxes from payments made.

From the taxpayer's perspective, information reporting can lead to significant administrative simplification. Most Americans receive W-2 forms at the end of each year, which reduces the taxpayer's burden by eliminating the need to gather records or perform computations. W-2 recipients with no other major source of income can simply transcribe information from the W-2 form directly onto the tax return. For those taxpayers who e-file, the process is simplified even further, as the data from the W-2 can be electronically imported. At the same time, W-2 forms facilitate the ability of the IRS to detect non-compliance.

To improve compliance and minimize error, Treasury and IRS have been focused on implementing several new information reporting regimes recently authorized by Congress.

• **Credit and debit card payments to businesses**. Starting in January 2011, organizations that process credit and debit card payments for merchants must annually report the amount of these payments to the recipient businesses and to the IRS. Treasury and IRS are actively working on the implementing regulations and soliciting input and feedback from taxpayers, banks, and credit card processors.

• **Cost basis reporting**. Starting in January 2011, brokerage firms must annually report cost basis and holding period information to customers and to the IRS in addition to gross proceeds from securities transactions. These information reports will make it easier for taxpayers to compute the net amount of gain or loss and will have a significant effect on reducing misreported capital gains.

In addition, the Administration's budget for FY 2010 includes the following significant new information reporting proposals:

• **Paymentsto Corporations**. The FY 2010 budget proposals would require businesses to file information returns for payments to a corporation for any services (such as accounting services or consultancy services) or certain gains aggregating to $600 or more per year. This would end current practice under a longstanding regulatory regime that exempts certain payments to corporations from general requirements for information reporting. These information reports will serve as reminders to the corporate recipients to include these amounts in gross receipts and will make these amounts visible to the IRS for targeted compliance programs.

• **Rental Property Expense Payments**. The FY 2010 budget proposals would require taxpayers who receive rental income and deduct expenses on rental activities to file information returns for rental property expense payments to any service provider or contractor that performs work on rental properties. This would make the reporting requirements for taxpayers engaged in rental real estate activities consistent with the requirements for other business taxpayers.

• **Certain Government Payments for Property and Services**. Some government vendors fail to meet their tax filing and payment obligations, and compliance would likely increase significantly if those payments were automatically reported by the governmental entity making the payment. The FY 2010 budget proposals would therefore require Federal,

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state, and local governments to report information on non-wage payments made for the procurement of property or services. Exceptions are anticipated for certain categories of payments and recipients.

• **Private Separate Accounts of Life Insurance Companies**. The proposals would require life insurance companies to report account information for any contracts invested in a private separate account. The reporting of this information would help the IRS determine whether earnings on investments in separate accounts are taxable income to the holder or are tax-free or tax-deferred.

• **Requiring Certified Taxpayer Identification Numbers (TINs) from Contractors**. Without accurate taxpayer identifying information, the effectiveness of information reporting requirements is limited. Therefore, the FY 2010 budget proposal would require contractors to provide TINs to the businesses from which they receive payments, and require those businesses to verify the TINs. If a contractor failed to furnish an accurate certified TIN, the business paying the contractor would be required to withhold.

• **Increased Penalties for Failure to Properly Report Information**. Penalties for failure to properly report information have not been increased since they were first established in 1989. Increasing those penalties will provide a stronger incentive for compliance with information reporting requirements. Accordingly, the FY 2010 budget proposal would increase by 100 percent the current per-return penalties for failure to file most information returns and would substantially increase the maximum penalties that can be assessed in a calendar year. In addition, the proposal calls for adjusting the penalty amounts for inflation every five years.

Additional Fiscal Year 2010 Budget Proposals

In addition to the information reporting proposals outlined above, the Administration's FY 2010 budget proposes an expansive set of additional tools or requirements to reduce opportunities for evasion and other non-compliance.

Improving compliance by businesses:

• **E-filing by Certain Large Organizations**. Mandate electronic filing for all corporations and partnerships required to file Schedule M-3 (Net Income or Loss Reconciliation). Expand the current regulatory authority to require e-filing by other large organizations (such as certain large exempt organizations). This would provide tax return information in a more uniform electronic form, enhancing the ability of the IRS to focus more productively its audit activities.

• **Clarification of Liability for Federal Employment Taxes of Employee Leasing Companies and Their Clients.** Set forth standards for holding employee leasing companies jointly and severally liable with their clients for Federal employment taxes under certain circumstances. Providing standards for when an employee leasing company and its clients will be held liable for Federal employment taxes will facilitate the assessment, payment, and collection of those taxes.

Strengthening Tax Administration:

• **Assessment of Criminal Restitution as Tax**. Allow the IRS and Treasury to immediately assess, without issuing a statutory notice of deficiency, and collect as a tax debt court-ordered restitution in criminal tax cases. Since court-ordered restitution in criminal tax cases currently cannot be assessed as a tax, the IRS cannot use its existing assessment systems to collect and enforce the restitution obligations. This leads to unnecessary duplication of effort, delay, and confusion.

• **Offer-In-Compromise Application Rules**. Eliminate the current-law requirement that an initial offer-in-compromise include a nonrefundable payment of a portion of the taxpayer's offer. Eliminating this requirement would expand access to the offer-in-compromise program and thereby improve IRS' ability to collect the portion of a tax liability that the taxpayer can pay.

• **IRS Access to Information in the National Directory of New Hires (NDNH)**. Expand IRS access to the NDNH for

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general tax administration purposes, including data matching, verification of taxpayer claims during return processing, and preparation of substitute returns for non-compliant taxpayers. Access to the NDNH would increase IRS productivity by reducing the amount of IRS resources dedicated to obtaining and processing data without reducing the current levels of taxpayer privacy.

• **Repeated Willful Failure to File a Tax Return**. Create an aggravated failure-to-file criminal penalty for any person who willfully fails to file tax returns in any three years of five consecutive years if the aggregated tax liability is at least $50,000. Such failure to file would be classified as a felony with a penalty of a fine of not more than $250,000 ($500,000 for a corporation) or imprisonment of not more than five years, or both. These increased criminal penalties would help deter multiple willful failure-to-file tax returns.

• **Tax Compliance with Local Jurisdictions**. Treat Indian Tribal Governments (ITGs) that impose alcohol, tobacco, or fuel excise or income or wage taxes as States for purposes of information sharing to the extent necessary for ITG tax administration. Treating ITGs as States for information sharing purposes would allow greater sharing of information between the Federal government and ITGs and thereby support Federal and ITG compliance activities.

• **Statute of Limitations where State Tax Adjustment Affects Federal Tax Liability**. Create an additional exception to the general three-year statute of limitations for assessment of Federal tax liability resulting from adjustments to State or local tax liability. The statute of limitations would be extended only for items related to the State tax adjustment. The proposal would remove the current statute of limitations as a barrier to the effective use by the IRS of state and local tax adjustment reports when the reports are provided by the state or local revenue agency to the IRS with little time remaining to make assessments at the Federal level.

• **Investigative Disclosure**. Clarify that the taxpayer privacy laws do not prohibit Treasury and IRS officers and employees from identifying themselves, their organization, and the nature and subject of an investigation when contacting third parties in connection with a civil or criminal tax investigation. This clarification would facilitate investigations by IRS officers and employees while setting forth clear guidance for taxpayers.

• **Electronic Filing by Tax Return Preparers**. Permit regulations to require electronic filing by tax return preparers who file more than 100 tax returns in a calendar year. Electronic filing benefits taxpayers and the IRS because it decreases processing errors, expedites processing and payment of tax refunds, and allows the IRS to efficiently maintain up-to-date taxpayer records.

Expand Penalties

• **Bad Check Penalty**. Clarify, expand, and update the bad check penalty to cover all commercially acceptable instruments of payment, including electronic checks and other payment forms. At present, only checks and money orders are covered by the bad check penalty.

• **Penalties for Failure to Comply with Electronic Filing Requirements**. Establish a penalty for failure to comply with electronic filing requirements of $25,000 for a corporation or $5,000 for a tax-exempt organization. This penalty would not supersede existing penalties for failure to file in any format. Although there are additions to tax for the failure to file returns under current law, there is no specific penalty in the Internal Revenue Code for failure to comply with a requirement to file electronically.

Administration's Proposals and Efforts to Combat Under-Reporting of Offshore Income

The President has made addressing under-reporting of income earned or held through offshore accounts or entities a top priority for his Administration. The Administration has developed a comprehensive approach to combating offshore tax evasion by U.S. taxpayers that includes legislative proposals, efforts to increase exchange of tax information with other countries, and increased enforcement.

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Legislative Proposals

The Administration's budget for FY 2010 provides various legislative proposals to address offshore tax evasion, including:

• Reforming the existing IRS "Qualified Intermediary" (QI) program to require additional information reporting from QIs so that the IRS will receive the same level of information on U.S. taxpayers from QI participants that it does from U.S. financial institutions.

• Requiring withholding of tax, in appropriate circumstances, on payments made through intermediaries that are not QIs. This measure would discourage U.S. and foreign persons from attempting to avoid U.S. tax by providing incorrect self-certification to intermediaries or otherwise relying on the lack of information reporting required from foreign intermediaries that are not QIs.

• Denying the benefits of reduced withholding tax rates to certain foreign entities unless the entities identify their owners. This measure would help ensure that persons that are not entitled to an exemption from withholding tax or a reduced rate of withholding tax do not arrange to receive payments through entities that appear to qualify for such an exemption or reduced rate.

• Requiring taxpayers and financial institutions to report to the IRS on cross-border transfers of certain assets.

• Allowing the IRS to make certain legal presumptions to minimize the effect of nondisclosure on IRS investigations and enforcement proceedings when U.S. taxpayers fail to fully disclose their offshore accounts.

• Extending the statute of limitations and imposing increased penalties when certain required information returns are not filed.

Exchanging Tax Information with Other Countries

Access to information from other countries is critically important to combating offshore tax evasion. For this reason, the United States has been a leader in increasing information exchange in tax matters. We have worked through the Organisation for Economic Co-operation and Development (OECD) to establish standards on transparency and exchange of information for tax purposes, and have strongly encouraged countries to adopt these standards. The United States has been more active in broadening the scope of information that countries agree to exchange through tax treaties and in negotiating and implementing tax information exchange agreements (TIEAs).

The United States will continue to update existing tax treaties with insufficient exchange of information provisions. Treasury recently concluded negotiation of updated tax treaty information exchange provisions with two key countries, Luxembourg and Switzerland, and will work toward swift ratification and implementation of those new agreements. Treasury will also continue to enter into new TIEAs, such as the agreements that the United States recently signed with Liechtenstein and Gibraltar.

The United States also will begin expanding its focus with respect to exchange of tax information from advocating international adoption of OECD standards to assessing international implementation of the standards adopted. Consistent with recommendations made by the United States, the G-20 London Summit Declaration called on appropriate bodies to conduct and strengthen objective peer review processes. Accordingly, Treasury will work to establish a robust peer review process to assess implementation of the OECD standards through an expanded version of the OECD-organized Global Forum on Transparency and Exchange of Tax Information, which currently includes OECD members and more than 40 other jurisdictions. Peer review should act to improve international implementation of tax information exchange and thereby help to ensure that such exchange helps to support U.S. taxation of income earned or held through offshore accounts or entities.

Increasing Enforcement

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Finally, the President's FY 2010 budget also includes strong support for international enforcement. With the FY 2010 initiative funding, the IRS would hire nearly 800 additional employees dedicated to addressing a broad range of international tax enforcement concerns. The initiative will increase examinations of complex international structures, cross-border transactions, and offshore activity on both corporate and individual returns. The Administration's continued support of IRS enforcement is described in greater detail below.

Status Update

The following chart provides a status update on the full range of initiatives underway to reduce opportunities for evasion. In addition to the new initiatives detailed above, this chart catalogues the progress of initiatives previously reported in the 2006 and 2007 tax gap reports.

Action Items	Status
Work with Congress to enact legislative proposals included in the Administration's FY 2010 Budget	In process
Implement recently enacted tax gap legislative proposals	Cost basis and merchant card reporting implementation: • Issued announcement in January 2009 enabling merchant card and third party settlement organizations to begin TIN validation • Issued two notices in February 2009 requesting public comments on the two reporting requirements • Developing new forms, business requirements, compliance programs, and IT solutions • Preparing proposed regulations and draft forms for public comment in Summer 2009 • Participating in ongoing meetings with stakeholders to work through implementation issues Other proposals already implemented: • Revised collection due process for employment taxes • Increased preparer penalties • Implemented erroneous refund claim penalties
Develop regulations and other published guidance clarifying ambiguous areas of the law, targeting specific areas of noncompliance and preventing abusive behavior	Our goal is to release 85 percent of the items appearing on the 2008-2009 priority guidance plan by 9/30/09. Examples include rules in the following areas: • International restructurings • Repatriation of foreign earnings • Transfer pricing and cost sharing • Foreign tax credit generator transactions • Intermediary tax shelters • Withholding tax application to business income earned by foreign partners in US partnerships • Application of the excise tax on reinsurance of US risks by

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	foreign insurers not in business in the US • Corporate ‘inversions' • Preparer penalties • Welfare benefit funds • Transactions of interest that involve charitable remainder trusts and controlled foreign corporations • By 8/30/09, will release the priority guidance plan for 2009-2010

Component 2: Make a Multi-Year Commitment to Research

Measuring the Tax Gap

In 2005, the IRS released preliminary results of a major research effort to quantify the tax gap using data from tax year 2001 and before. The IRS in following years arrived at the estimate of the gross tax gap of $345 billion for tax year 2001. An update of the tax gap estimate based on more recent data is needed, and the IRS is working on delivering such an estimate in 2011. Updated estimates will help the IRS measure progress against its existing long-term goal of an 86 percent voluntary compliance rate for Tax Year 2009. [FN3]

To ensure that the Administration and Congress alike have access to more useful, up-to-date estimates of the tax gap, the Treasury and the IRS have begun to implement a long-term strategy to move away from occasional, large-scale efforts to estimate the tax gap and instead update tax gap estimates on an ongoing basis. The IRS's FY 2009 budget included funding to improve tax gap estimates, better measure non-compliance, and improve detection of non-compliance.

As part of the effort to update the tax gap estimate, the IRS is currently completing a reporting compliance study on Subchapter S corporations for 2003 and 2004 tax years, and plans to release the results later this year. The IRS is also currently conducting research on reporting compliance with the individual income tax for tax years 2006 and 2007, and will soon begin looking at tax year 2008 tax returns (filed in 2009). The data for these three years will provide the necessary baseline for regular updates to the individual income tax gap, which can begin in calendar year 2011.

The IRS is also conducting a pilot project to extend studies of individual income tax returns to include a small sample of returns with international addresses. While the research is still in exploratory stages, if representative compliance data for this population can be extrapolated, this approach could allow us to better estimate one portion of the international tax gap.

Finally, the IRS is currently preparing to launch a study of employment tax reporting and filing compliance, with field work beginning in October 2009. This study will also be conducted over multiple tax years, with the goal of eventually providing regular estimates of employment tax compliance levels and the drivers of non-compliance.

In addition to developing more recent data on which to base an updated estimate of the tax gap, the IRS will also continue to explore ways to improve research methodologies to better measure non-compliance and to improve its ability to target the sources of non-compliance.

Status Update

The following chart provides a status update on the research and measurement efforts currently underway or completed since the release of prior tax gap reports:

Action Items	Status
Undertake additional compliance studies, including S	• Completed S Corporation exams (analysis ongoing)

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Corporations and individuals	
	• Conducted TY2006 National Research Program (NRP) Form 1040 exams (analysis ongoing)
	• Conducting TY2007 NRP Form 1040 exams (ongoing)
	• Provide ongoing updates to level of tax gap attributable to underpayment (as shown in the Tax Gap Map, this amount is an actual amount, not an estimate)
Update tax gap estimates using new and existing data	• In process, as described above
Research the effect of service on taxpayer compliance	• Engaging in three significant research projects linking IRS service to compliance (in process)
Research the relationship between complexity, burden, and compliance	• Preparing survey of individual taxpayers to improve burden estimates (in process)
	• Engaging in three research projects focusing on relationships between complexity, burden, and compliance (in process)

Component 3: Continue Improvements in Information Technology

The IRS continues to focus on improving the technology infrastructure that supports its service and enforcement programs. Improved information technology capabilities will help make early detection and intervention efforts more effective, improve case selection, and allow the IRS to offer better, more user-friendly service to taxpayers.

Increasing E-File Rate

Electronic filing is a critical component of the effort to improve voluntary compliance and close the tax gap. By simplifying the filing process for taxpayers, decreasing processing errors, and expediting the processing and payment of tax refunds, electronic filing makes the tax-filing process less onerous for taxpayers and allows the IRS to update taxpayer records more efficiently.

Through sustained focus and outreach, the e-file rate has been steadily increasing for years. The 2008 e-file rate for individuals was 58 percent, up from 31 percent in 2001. Tax filing results thus far in 2009 already reflect a significant increase in this rate.

The Administration is committed to achieving an overall e-file rate of 80 percent. The IRS recent published an in-depth research study on ways to increase the e-file rate. [FN4] The study showed that approximately 85 percent of individual tax returns were filed by paid preparers, or by individuals via third-party software products. The study also showed that over 98 percent of paid preparer returns were completed using software, and yet a substantial number of tax returns are ultimately printed and mailed to the IRS. The Administration believes that in order to sustain progress toward the 80 percent goal, the Treasury should be authorized to require electronic filing from tax return preparers who file more than 100 tax returns in a calendar year. The President's FY 2010 budget includes the legislative proposal necessary to provide this authority.

Additionally, the IRS has been working on a modernized electronic filing (MeF) platform that provides real-time processing of tax returns and improves error detection. This new platform will improve detection of errors during the initial filing process, rather than after the fact, and will therefore reduce the number of filing errors that contribute to the tax gap. MeF is currently processing electronically filed tax returns for corporations, partnerships, excise tax filers, and exempt organizations. The number of tax returns filed through the MeF system increased 49 percent in 2008 to more than 3

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million accepted returns, and volumes are projected to reach 4 million accepted returns for 2009. Starting in 2010, the IRS plans to roll out Form 1040 and its family of related schedules on the MeF platform, which will extend the benefits of the MeF platform to individual taxpayers as well.

Core Taxpayer Account Database

The IRS has made significant progress in updating its core taxpayer account database, the Customer Account Data Engine. Moving away from its legacy technology, the IRS has devoted resources towards a new, relational database structure, which will enhance the flexibility, responsiveness, and timeliness of the IRS' service and enforcement functions. Nearly 40 million taxpayer accounts were processed using this modernized taxpayer account database in 2009. This new database is the most important element of the IRS' strategy for the next generation of taxpayer service and compliance applications that are needed to address the tax gap. The Administration's FY 2010 budget includes a program increase of $23 million to accelerate this important work.

Applying Enhanced Information Technology to Ongoing Operations

The IRS continues to deliver significant enhancements to the systems that support its core operations. For example, the Automated Underreporter (AUR) program, a mechanized system that helps to identify discrepancies in returns, sends notices to taxpayers when amounts reported on individual tax returns and amounts reported by third parties don't match. Improvements to the AUR program have enhanced workload selection and improved the overall productivity of the program. AUR case closures have increased from 2.0 million in 2004 to 3.5 million in 2008. The expansion of the AUR program has allowed the IRS to increase coverage in key areas of non-compliance.

Status Update

The following provides a status update on the full range of information technology initiatives underway or completed since the release of previous tax gap reports:

Action Items	**Status**
Use technology to improve high income and non-EITC exam workload selection and method of delivery and assess the effectiveness of the exam treatment stream on selected non-filer cases	• Implemented new selection and classification criteria based on NRP results
	• Implemented automated case screening and selection process
Expand Automated Underreporter (AUR) program to include additional income types	• Expanded use of automatic notices
Evaluate the AUR matching process, and implement an improved case scoring and selection concept to select the most productive cases.	• Reengineered AUR matching process to improve coverage, maximize resource utilization, and increase AUR closures
	• Implemented improved workload selection tools
Expand the AUR Soft Notice Test, which involves asking taxpayers to voluntarily self-correct for future years	• Developed system requirements
	• Performed test for approximately 30,000 taxpayers in FY2009 and expect to perform follow-up test of 30,000 addi-

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	tional taxpayers in FY2010
Develop enhancements to the Compliance Data Warehouse to improve workload identification and prioritization algorithms, allowing better evaluation of alternative treatment streams and ensuring Collection cases receive the most efficient and effective treatments	• Completed
Update the Collection inventory management system to improve functionality and navigation and provide capability to interface with other modernized systems	• Nationwide deployment in process
Automate lien delivery, recording, and release processes with state and local jurisdiction to improve the timeliness of lien filing, lien releases, and the payment of fees	• Not yet started (currently unfunded)
Test the use of statistical modeling techniques within TEGE to detect high- risk compliance patterns in order to use data to expand and improve examination selection	• In process
Develop and implement a set of compliance decision analytic tools that will support analysis of Tax Exempt and Government Entities (TE/GE) returns and other data to detect compliance trends and improve case and issue selection	• In process
Implement a new TE/GE electronic examination system (TREES) that will consolidate agent work papers to increase the accuracy and efficiency of the examination process	• Completed
Build and implement modernized e-file (MeF) receipt of electronic transmissions for additional tax forms	• Deployed Form 1120F replacement in January 2008 and Form 990 replacement in January 2009 • Developing first phase of the Form 1040 series for deployment in 2010

Component 4: Improve Compliance Activities

Multi-Year Investment in IRS Enforcement

The Administration's FY 2010 budget continues strong support of IRS enforcement, which will support a sustained focus in the areas of greatest risk. The budget request includes program increases of $332.2 million for investments in strong compliance programs, including a robust portfolio of international enforcement initiatives. The priorities include international enforcement, improving compliance programs dealing with businesses and high income individuals, expanding the use of document matching techniques to combat misreporting of income by business taxpayers, and improving collection operations, including the creation of two new Automated Collection System (ACS) sites.

The Administration's FY 2010 budget includes funding for an additional 15 tax specialists in Treasury's Office of Tax Policy. These new specialists will help to ensure that Treasury possesses capabilities sufficient to support rigorous analysis and implementation of revenue policy, including tax gap reduction.

The Administration's FY 2010 budget also outlines a multi-year investment to deal more effectively with the ever-increasing volume and complexity of international transactions. The initiative will add nearly 800 enforcement personnel

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to address the underreporting of tax associated with international transactions as well as domestic taxpayers involved with offshore activities.

The FY 2010 budget also contemplates a significant investment in enhancing and expanding the IRS' collection operation to address the tax gap attributable to underpayment of tax. From FY 2005 to FY 2008, the IRS achieved a 27.2 percent increase in collection efficiency, when over the same time period collection staffing decreased seven percent. The FY 2010 investment will allow the IRS to build on its efficiency gains, undertake pilot projects to further improve efficiency, and broaden overall collection coverage.

In total, the new enforcement personnel contemplated by the Administration's FY 2010 budget are estimated to generate $2.0 billion in additional annual enforcement revenue once the new hires reach full potential in FY 2012.

The IRS is constantly assessing the compliance landscape, and adapting and investing in its programs as needed to ensure an appropriate balance among its enforcement programs.

Status Update

Expanding on the new priorities and initiatives discussed above, the following chart provides a status update on the enforcement initiatives currently underway or completed since the release of prior tax gap reports:

Action Items	**Status**
Increase audit coverage and better target returns for examination	• Updated selection scores (DIF/Discriminate Information Function) based on NRP results
	• Increased Schedule C audits
	• Updating selection criteria based on results of NRP (in process)
	• Improving correspondence exam case selection methodologies (in process)
	• Began significant compliance hiring initiative in FY09
Enhance the ability to identify and address tax schemes of business and individuals involving offshore activity, address illegitimate use of tax havens to shelter income, and increase information matching and examination activity for individuals living abroad	• Working with Congress to secure requested FY 2010 funds for nearly 800 new international enforcement personnel. Funding request of $128M to increase international enforcement efforts.
	• Engaging in voluntary disclosure initiative for taxpayers with undeclared offshore accounts
	• Completed pilot phase of the Broker Compliance Initiative Project
	• Developing additional compliance initiative projects in the areas of private banking and offshore merchant accounts (in process)
	• Issued regulations relating to transfer pricing, foreign tax credits, and foreign trusts (regulations relating to cross border restructuring in process)
	• Implemented the Shelter Data Management System (SDM), and implementation of the larger Selection and Workload

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	Classification system is in process
	• Expanded the use of the OECD Abusive Transaction Database to identify emerging abusive transactions and issues
Enhance collection programs and increase the Federal Payment Levy Program (FPLP) using third-party data	• Working with Financial Management Service (FMS) and Centers for Medicare and Medicaid Services (CMS) to determine feasibility of adding Medicare payments
Work with other federal agencies regarding FPLP	• Expanded FPLP to include Defense Finance and Accounting Service salary payment files, Department of Defense Civilian Employees, HHS, EPA, and Department of Energy
	• Entered into agreements with DoD to add additional Federal wage and other payments
Improve compliance by tax preparers through implementation of the Service- wide Enforcement Preparers Strategy	• Announced IRS review of tax return preparers (recommendations to be made by end of 2009)
Improve collection selection criteria and filters for balance due and non-filer cases, including identifying and addressing potential high income non-filers	• Expanded the use of third-party information and research to enhance case selection
	• Refining decision analytics and developing new model to enhance case selection (in process)
	• Finalized Service-wide non-filer strategy
Litigate cases, work settlements, and design large scale resolution initiatives for tax shelter transactions to deter noncompliance	• Engaged in settlement initiatives including Son of Boss, LILO/SILO, Distressed Asset Trust (DAT), stock option transactions, and the overall Global Settlement Initiative
	• Litigated and continued to litigate unresolved cases
Initiate a project using Combined Annual Wage Reporting (CAWR) data to identify tax-exempt organizations that may not be properly reporting and paying employment tax	• Analyzed results and documented lessons for future CAWR initiatives
Increase criminal enforcement on abusive schemes, corporate fraud, employment tax, egregious non-filers, and Bank Secrecy Act violations	• Achieved average conviction rate over 90 percent for the combined component programs and publicity rates over 80 percent
Improve the alignment and allocation of Service-wide resources to identify, develop, and resolve challenges better in the global taxation arena	• Moved forward with significant international compliance initiatives (in process)
	• Used International Planning and Operations Council to identify opportunities to conduct cross-divisional exams and enhance cross-divisional identification and referral of emerging international compliance issues
	• Realigned international resources to improve integration and leverage expertise
	• Increased international examiner hiring (ongoing)

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	• Developing processes to evaluate referrals and identify and assess international and U.S. possessions compliance issues
Improve tax administration to deal more effectively with increased emphasis on globalization by all corporate and individual taxpayers	• Moved forward with significant international compliance initiatives (in process)
	• Expanded information sharing through increased membership and broader focus in the Joint International Tax Shelter Information Centre (JITSIC) by adding Japan, adding a London office, and adding China and Korea as observers
	• Introduced new Form M-3 for Form 1120F to gather information on foreign corporations
	• Revised Form 5471 for international transactions (in process)
	• Providing education and guidance to withholding agents of their responsibilities to withhold on Fixed, Determinable, Annual, Periodical (FDAP) payments to non-U.S. persons (ongoing)
Address offshore and cross-border compliance risks through enforcement and by issuing published guidance	• Completed project on foreign athletes and entertainers to ensure appropriate reporting and sourcing of income
	• Completed voluntary settlement initiative for embassy/consular employees and continuing to pursue enforcement activities on non-electors
	• Issued regulations on transfer pricing, foreign tax credits, cross-border restructuring, and other cross-border issues

Component 5: Enhance Taxpayer Service

Providing quality taxpayer service is critical to protecting the approximately $2.7 trillion that U.S. taxpayers report and remit. The tax code is complex, and effective taxpayer assistance is necessary to help taxpayers understand and comply with their obligations.

Providing Innovative Online Services

The demand for online services continues to grow dramatically. In FY 2008, IRS.gov received 2.2 billion web page visits, an increase of 74 percent from FY 2005. From January 1 to May 31, 2009, 48 million taxpayers used the “Where's My Refund?” web site, up from 24 million for the same period in 2005.

In FY 2008, the IRS launched a hybrid online/in-person service with its Facilitated Self-Assistance Research Project. This project provides a kiosk with web access at IRS Taxpayer Assistance Centers. The kiosk computers allow taxpayers to help themselves and to get additional help from an IRS assistor if needed. Through FY 2009, the IRS has installed kiosk services in 50 Taxpayer Assistance Centers.

Streamline Written Communications with Taxpayers

In 2008, the IRS created a Taxpayer Communications Task Group to study and improve the clarity, accuracy, and ef-

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fectiveness of written communications to taxpayers. Simple, clear communication makes it easier for taxpayers to comply with their obligations.

While the work of the group is ongoing, an early success was the elimination of nearly a dozen inserts in a notice informing businesses that they owe additional tax. This change to the CP 161 notice, which is mailed to business taxpayers who underpay their taxes, will halt the mailing of tens of millions of pieces of paper, reduce taxpayer and preparer burden, and save the government money.

Taxpayer Assistance Blueprint

The IRS continues to make progress in executing the initiatives outlined in its strategic plan for taxpayer service, the Taxpayer Assistance Blueprint (TAB). The TAB, which will be updated in the summer of 2009, outlines a series of initiatives aimed at enhancing IRS service options across all delivery channels: in person, on the Internet, and over the phone. The IRS has also embedded the philosophy and priorities of the TAB concept of improving service from the taxpayer perspective in every service improvement decision.

Status Update

The following chart provides an update on the status of the taxpayer service initiatives currently underway or completed since the release of prior tax gap reports:

Action Items	**Status**
Increase accuracy on toll-free telephone customer inquiries, processing functions, and paper adjustments	• Implementing and deploying Interactive Tax Law Assistant tool to provide accurate, efficient, and complete responses to basic tax law inquiries (in process)
	• Implementing and deploying Accessory Manager tools that provide standard research paths, consolidate account data, and automatically populate input fields (in process)
	• Implemented recommendations from the Correspondence Accuracy Improvement Study
Enhance IRS.gov	• Deployed interactive tax law decision support tool in FY 2009 filing season that includes enhanced FAQs
	• Preparing interactive probe and response capabilities (in process)
Improve the quality of volunteer-prepared returns through enhancements to the VITA program, including quality training and sample processing reviews	• Conducted on-site workshops to address quality concerns, and revised the volunteer return preparation training to use a process based training (PBT) approach for all volunteers.
	• Incorporating PBT concepts into online volunteer training application: Link & Learn Taxes (in process)
Enhance services to persons with limited English proficiency (LEP) through the Taxpayer Assistance Blueprint, development of a Multi-Lingual Strategic Plan, development of a Virtual	• Added enhancements including 'Where's My Refund?', 'How Much Was My Economic Stimulus Payment?', and the Economic Stimulus Calculator to the Spanish IRS.gov
Translation Office, and launch of a revised version of the Spanish IRS.gov webpage	• Undertook research efforts to pinpoint isolated community locations and identify actions to customize assistance

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	• Performed targeted outreach for LEP taxpayers
	• Expanded Virtual Translation Office to provide tax forms, publications, and education materials in Spanish and other IRS-priority languages
Improve quality and timeliness of taxpayer contacts by maintaining an enhanced integrated quality assurance process with internal and external partners	• Developed and deployed Site Coordinator's Training, mandating use of intake and interview sheets and quality reviews for all return preparation.
	• Continued partner and employee feedback via roundtable discussions and partner satisfaction surveys
	• Implemented a Quality Statistical Sample Cadre to perform on-site return reviews that incorporates a second level review
Improve services through programs at both the national and local level by expanding collaborations with organizations serving the disabled, Native American communities, and pre-existing rural infrastructures	• Increased availability of free tax return preparation and financial/EITC education through a network of national and local partners in hard-to-serve Native American communities as well as for low income disabled persons
	• Working with Department of Agriculture and Rural Funding Foundations to increase availability of tax-related services in rural communities
	• Established measures to gauge national and local penetration rates for the rural initiative and shared best practices with rural partners
Expand and enhance the Spanish Website to increase electronic options, including options for Spanish language delivery of applications currently only in English	• Added 'Where's My Refund?', 'How Much Was My Economic Stimulus Payment?', and the Economic Stimulus Calculator to the Spanish website
	• Expanded and enhanced taxpayer education information including tax responsibilities and eligibility requirements for various credits and other benefits
Provide Reporting Agents with access to e-Services	• Deployed access to Electronic Account Resolution (EAR) and Transcript Delivery System (TDS) for Reporting Agents
Implement Taxpayer Assistance Blueprint Phase 2, which includes a five-year strategic plan for taxpayer service based	• Embedded the TAB Guiding Principles within the FY 2009-2013 IRS Strategic Plan
on extensive research to understand taxpayer and stakeholder needs	• Issuing in summer 2009 the second annual Report to Congress, which will include examples of numerous taxpayer service improvements accomplished in 2008 and 2009
Implement Internet-Customer Account Services (I-CAS) Release 1, which will enable taxpayer to view account information	• Working toward electronic access to account information, once all data security issues are resolved and the core taxpayer account database complete
Implement I-CAS Release 2, which will enable taxpayers to change their address, file an extension, submit a Power of Attorney, and calculate a payoff amount on balances due via a secure Internet link	• Status is same as above

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Continue publicity efforts encouraging use of Online Payment Agreement (OPA)	• Issued new releases and other communications during filing seasons, including directions for accessing OPA from IRS.gov
	• Worked with tax software providers and other stakeholders to promote OPA
Enable taxpayers with disabilities to understand available tax credits and receive tax preparation assistance through partnerships with national and local organizations that serve this unique group of taxpayers	• Partnering with national and local organizations, including government entities, to increase return preparation services

Component 6: Reform and Simplify the Tax Law

Earlier this year, the President's Economic Recovery Advisory Board (PERAB) formed a Task Force on Tax Reform. The task force will, among other things, focus on tax simplification. The task force will report back to the board, and the full board is expected to report back to the President with options.

The following is a more detailed listing of specific action items that are underway by the IRS and Treasury to reform and simplify the tax law.

Initiatives	**Status**
Work with Congress to enact simplification legislative provisions	• Enacted simplifications to create uniform definition of a child
Continue Taxpayer Burden Reduction projects	• Released revised Forms 1120S and 2553, along with related regulation changes, to simplify an S Corporation election
	• Released revised Form 94X, along with related regulation changes, to reduce employment tax reporting errors
	• Released new Form 8857 for innocent spouse relief
Continue tax form and publication improvements	• Among other improvements, developed a multi-year prioritized plan of burden reduction activities to include forms redesign and simplification, defined the MeF platform for XML-enabled PDF Form 1040, and launched a hyperlinked Publication 17, Your Federal Income Tax, on IRS.gov

Component 7: Coordinate with Partners and Stakeholders *Tax Return Preparer Review* The IRS recently announced that, by the end of 2009, the Commissioner will propose a comprehensive set of recommendations concerning tax return preparers. The review seeks to identify ways to improve taxpayer compliance and to ensure strong and uniform ethical standards of conduct for tax preparers. Potential recommendations could focus on a new model for the regulation of tax return preparers, improved service and outreach for return preparers, education and training for return preparers, and enforcement related to return preparer misconduct. The tax return preparer review will begin with a fact-finding effort targeted at a large and diverse constituent community, including both licensed tax preparers—such as enrolled agents, lawyers and accountants—and unlicensed tax preparers and software vendors. The effort will also seek input and dialogue with consumer groups and taxpayers. *Enhanced Collaboration with Partners and Stakeholders* The IRS has strengthened its partnerships with other state and Federal agencies. Strong collaboration enables the IRS and its partner agencies to make more efficient and effective use of existing resources. For example, the IRS has undertaken initiatives to make better use of information from state agencies, including state audit reports, and has developed a coordinated strategy to com-

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bat employment tax schemes. Finally, the IRS has expanded its partnership with stakeholders to communicate more effectively with the numerous constituencies whose efforts might help raise the level of voluntary compliance. Examples include work with the Small Business Administration to educate new business owners on key tax topics, and expanded work with partners to communicate with military retirees on retirement-related tax issues. *Status Update* The following chart provides a status update on coordination efforts currently underway or completed since the release of prior tax gap studies:

Action Items	**Status**
Enhance the centralized process to maximize utilization of State Audit Reports (SARs) by IRS for federal assessments	• Established a system to establish baseline usability and productivity of incoming SARs
	• Continue to partner with states to implement enhancements (including automation of receipts) to improve usability of SARs
Implement a Questionable Employment Tax Practices (QETP) Initiative in partnership with the Department of Labor, National Association of State Workforce	• Implemented initiative with initial 20 states participating, with 25 percent participation increases targeted and achieved in FY08 and FY09
Agencies, Federation of Tax Administrators, and state workforce agencies to provide a collaborative national approach to combat employment tax schemes	• Incorporated data provided by the states into employment tax audit work streams
Further enhance the Fed/Fed program by facilitating and expanding partnerships with other Federal agencies to improve tax administration	• Expanded partnerships to include the Social Security Administration (SSA) and the Small Business Administration (SBA)
Engage all 50 states through the State Reverse File Match Initiative (SRFMI) - a process that matches IRS extracts received through the Governmental Liaison Data	• Engaged in 2008 pilot use of systemic SRFMI data received from 14 states, and increased state agency participation to 44 agencies in 2009
Exchange Program against state master files to identify individuals and businesses who filed a state return but not a federal return and to identify differences in federal and state income reporting	• Expansion in process
Determine tax administration benefits of utilizing state data warehouse concept	• Evaluating internal systems such as Compliance Data Warehouse and Integrated Production Model to determine feasibility
Develop an educational targeted outreach DVD for military personnel preparing for etirementr	• Distributed and integrated DVD into all military pre-retirement seminars to ensure retirees understand tax rules applicable to their retirement benefits
	• Working with Department of Labor to include a topic on withholding taxes as a requirement for all military retiree training conducted on military bases and developing a Life Cycle Brochure on this topic for distribution
Enhance outreach efforts to industry audiences about available Audit	• Determined what enhancements to current guides and what new guides are needed
Technique Guides and Tax Tips	• Continued to publicize availability of guides via national

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	and local liaison activities
Establish links to IRS.gov on industry, practitioner, educational, and governmental stakeholder websites	• Established Tax Centers (dedicated web space) with links to state and national organization websites
Develop and widely distribute educational fact sheets on areas of high noncompliance	• Distributed monthly fact sheets on wide variety of subject matters including avoiding incorrect self-employment deductions, wage compensation for S Corporation officers, and managing paper and electronic recordkeeping requirements
Develop a strategy to reach practitioners without affiliation to a professional organization	• Developed grass-roots delivery channel with national retail tax preparation firms, expanded outreach to colleges and universities to include graduates entering tax field
Leverage key partners such as the SBA and its SCORE program and Small Business Development Centers (SBDCs) to deliver small business workshops to the new business community	• Continued contact with traditional partners to maximize leveraged opportunities that provide education and outreach directly to business owners
	• Partnered with SCORE and SBDCs to enhance quality and consistency of leveraged Small Business Tax Workshops
	• Partnered with SBA to increase outreach through the National Women's Business Council in order to promote voluntary compliance and share information customized for new business owners
	• Increased the number of Small Business Tax Workshops
Deliver educational messages through existing relationships with universities and colleges	• Expanding participation of current Historically Black Colleges and Universities (HBCUs) in the VITA program (in process)
	• Increasing participation of Beta Alpha Psi, national scholastic and professional fraternity, in VITA program by 10% (in process)
	• Expanding the Cooperative Extension Services Network tax prep and education program in each of the four regions, HBCUs, tribal colleges and universities (in process)
Develop audio educational messages for toll-free wait times Customize outreach to specific industries to encourage voluntary compliance	• Developed text and appropriate placement of specific educational messages
	• Deploying audio educational messages (expected July 2009)
	• Launched industry specific communication and outreach to small businesses, industry stakeholders, and state licensing agencies
	• Performing outreach in all states to promote use of IRS's web-based Tax Centers designed to provide education and web resources for specific industries and professions (in process)
	• Provided educational materials to new and existing business

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	owners through partnerships with small business and industry stakeholders and state licensing agencies in all 50 states
Request feedback from internal and external stakeholders on existing outreach and educational programs to identify best practices and enhancements	• Convened IRS-wide task force to collect and review stakeholder feedback, shared recommendations with external stakeholders, and obtained additional feedback (implementation of recommendations ongoing)
Develop strategies to educate first-time business filers	• Implemented outreach strategy to first- time business filers including collaboration with small business and Industry partners to develop an outreach campaign to educate first time Schedule C filers, including common errors to avoid
Expand relationships and collaboration with foreign tax administrations to increase informal and formal communications on international tax administration matters	• Completed OECD project relating to international guidelines on attribution of profits to permanent establishments • Participating in OECD work on monitoring Transfer Pricing Guidelines, including international business restructurings (ongoing) > •Negotiated protocols to income tax treaties with Luxembourg and Switzerland to make the exchange of information provisions consistent with U.S. and OECD standards > •Continuing efforts to conclude tax information exchange agreements, including agreements recently signed with Liechtenstein and Gibraltar > •Participating in the Leeds Castle Group with the tax administration agencies of China, India, South Korea, the United Kingdom, Japan, Australia, Canada, France, and Germany (ongoing) > •Collaborating via the Joint International Tax Shelter Information Centre (JITSIC) with Canada, Australia, and the United Kingdom to identify and curb abusive tax avoidance transactions (ongoing) > •Participating with the OECD working group on Aggressive Tax Planning to design a database of various cross-border tax avoidance schemes (ongoing)

V. IRS Strategic Plan

Since the publication of the last tax gap report, the IRS published a new strategic plan for FY 2009-2013. The strategic plan outlines the service and enforcement goals of the IRS, along with the strategic foundations that underpin both. The plan recognizes that the IRS must excel at both service and enforcement: success is not an either/or proposition. The plan also outlines five long-term measures for evaluating the IRS's progress in achieving its goals, and which directly relate to the tax gap strategy. Those measures, some of which have been discussed above, include the following:

• Voluntary Compliance Rate. The Voluntary Compliance Rate, as explained earlier in this report, is highlighted in the strategic plan as a key long-term measure. The IRS's goal is to achieve an 86 percent voluntary compliance rate for Tax

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Year 2009, and is actively pursuing updates to the tax gap estimates that will allow progress against this goal to be measured.

• E-File Rate. The IRS has been tracking the rate of electronic filing for individual income tax returns since the inception of electronic filing in 1986, reporting the number of individual tax returns (Form 1040) that have been filed electronically in its published performance reports. The IRS is currently seeking to achieve an 80 percent e-file rate by 2012 for all major tax returns filed with the IRS.

• ACSI All Individual Taxpayer Score. The American Customer Satisfaction Index (ACSI) is a national indicator of customer satisfaction with the quality of products and services available to consumers in the United States. Each December, the ACSI issues a report on satisfaction of recipients of services from the Federal government. In 1999, the Federal government selected the ACSI to be a standard metric for measuring citizen satisfaction. Agency participation is voluntary but relatively extensive. Over 55 Federal government agencies have used the ACSI to measure citizen satisfaction of more than 110 services and programs. The IRS performance measure focuses on the satisfaction score associated with all individual income tax filers (paper and electronic filers). The IRS has a goal of achieving a satisfaction score of 72 for the 2012 tax year. As discussed above, a taxpayer-friendly tax filing process is essential to improving compliance.

• Nonrevenue Enforcement Activity. IRS has developed an index of enforcement activities that promote compliance yet do not focus primarily on tax revenue. IRS examines changes in this index in order to assess trends in its nonrevenue performance, which is similar to using the Consumer Price Index to assess trends in consumer prices. The nonrevenue enforcement activity index includes examination activity in the Tax Exempt and Government Entitles Division as well as Bank Secrecy Act investigations.

• Employee Engagement. A motivated, well-trained, and dedicated workforce is critical to the ultimate success of all IRS initiatives. The IRS for several years has been conducting an annual employee survey to obtain feedback on a wide range of workplace issues. The results are used to calculate an engagement index, which is compared with engagement scores from prior years and from other agencies.

Recognizing the importance of a well-trained workforce to the accomplishment of the goals and metrics outlined in the strategic plan, the IRS last summer launched a Workforce of Tomorrow Task Force. The Task Force's goal is to ensure that, five years from now, the IRS has a workforce equipped to serve America's taxpayers for the next fifteen years. The Task Force produced a roadmap of initiatives to address the IRS's greatest workforce challenges, which includes 58 recommendations that are currently being implemented. The IRS workforce is the foundation for the ultimate success of its efforts to implement its strategic plan and reduce the tax gap.

Conclusion

The tax gap imposes an unfair burden on law-abiding taxpayers, and the Department of the Treasury and the IRS are committed to narrowing the gap between what is owed and what is paid. This report has highlighted new initiatives to improve tax revenue collection, both through improved voluntary compliance and through effective enforcement. It has also provided status updates on a full range of initiatives currently underway or completed since the release of previous tax gap reports.

As outlined above, the plan to reduce the tax gap has multiple parts. Targeted changes in the tax laws, enhanced taxpayer service, and increased enforcement are all critical to this effort. As this report describes, progress has already been made with respect to key strategic priorities and initiatives, both those identified in prior tax gap reports and those developed since the issuance of the last report. In order to provide accurate and up-to-date assessments of progress, Treasury and IRS are deploying significant resources toward the long-term effort to produce regular, updated estimates of the tax gap, which will be used to assess progress toward closing the tax gap.

The Administration's FY 2010 budget proposes an expansive set of additional tools and requirements to reduce opportunities for evasion and other non-compliance. The Administration is committed to working closely with Congress to

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strike an appropriate balance to maximize revenue collection without imposing unreasonable compliance and enforcement burdens on the vast majority of individuals and businesses that fully and willingly pay what they owe.

APPENDIX: UNDERSTANDING THE TAX GAP [FN5]

The Internal Revenue Code places three primary obligations on taxpayers: (1) to file timely returns; (2) to make accurate reports on those returns; and (3) to pay the required tax voluntarily and timely. Taxpayers are compliant when they meet these obligations. Noncompliance — and the tax gap — results when taxpayers do not meet these obligations.

The tax gap is defined as the aggregate amount of true tax liability imposed by law for a given tax year that is not paid voluntarily and timely. True tax liability for any given taxpayer means the amount of tax that would be determined for the tax year in question if all relevant aspects of the tax law were correctly applied to all of the relevant facts of that taxpayer's situation. For a variety of reasons, this amount often differs from the amount of tax that a taxpayer reports on a return. The taxpayer might not understand the law, might make inadvertent mistakes, or might misreport intentionally.

To be paid voluntarily, a tax liability must be paid without direct IRS intervention. Taxpayers have the responsibility to determine and report their correct tax liability, and to make sure that amount is paid (whether through withholding, estimated tax payments, payments with a filed return, etc.). The IRS focuses its enforcement where it is needed most, but the overall rate of tax compliance in the United States is as high as it is because the vast majority of taxpayers meet their obligations with little or no involvement from the IRS. To be paid timely, a tax liability must be paid in full on or before the date on which all payments for the given tax year were legally due.

It is important to emphasize that IRS estimates of the tax gap are associated with the legal sector of the economy only. Although tax is due on income from whatever source derived, legal or illegal, the tax attributable to income earned from illegal activities is extremely difficult to estimate. Moreover, the government's interest in pursuing this type of noncompliance is, ultimately, to stop the illegal activity, not merely to tax it.

Although they are related, the tax gap is not synonymous with the "underground economy." Definitions of the "underground economy" vary widely. However, most people characterize it in terms of the value of goods and services that elude official measurement. Furthermore, there are some Items in the "underground economy" that are not included in the tax gap (such as tax due on illegal-source income), and there are contributors to the tax gap that no one would include in the "underground economy" (such as the tax associated with overstated exemptions, adjustments, deductions, or credits, or with claiming the wrong filing status). The greatest area of overlap between these two concepts is sometimes called the "cash economy," in which income (usually of a business nature) is received in cash, which helps to hide it from taxation.

Equally important, the tax gap does not arise solely from tax evasion or cheating. It includes a significant amount of noncompliance due to tax law complexity that results in errors of ignorance, confusion, and carelessness. This distinction is important even though, at this point, the IRS does not have sufficient data to distinguish clearly the amount of noncompliance that arises from willful, as opposed to unintentional, mistakes. Moreover, the line between intentional and unintentional mistakes is often a grey one, particularly in areas such as basis reporting, where a taxpayer may know that his or her reporting is inaccurate but does not have ready access to accurate information. This is an area where additional research is needed to improve understanding.

Measuring the Tax Gap

Historically, estimates of federal tax compliance were based on special studies, including the Taxpayer Compliance Measurement Program (TCMP), which covered income and self-employment taxes and groups of taxpayers, and consisted of line-by-line audits of random samples of returns. These studies provided the IRS with information on compliance trends and allowed the IRS to update audit selection formulas regularly. However, this method of data gathering was extremely burdensome on the taxpayers whose returns were selected. As a result of concerns raised by taxpayers,

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Congress, and other stakeholders, the last TCMP audits were done in 1988.

The IRS conducted several much narrower compliance studies between 1988 and 2001, but nothing that would provide a comprehensive perspective on the overall tax gap. Until recently, all of these subsequent estimates of the tax gap have been rough projections that basically assume no change in compliance rates among the major tax gap components even though the magnitude of these projections reflects growth in tax receipts in these major tax gap categories.

The NRP, which the IRS has used to estimate the most recent tax gap updates, arose out of a desire to find a less intrusive means of measuring tax compliance. The IRS used a focused statistical selection process that resulted in the selection of approximately 46,000 individual income tax returns for Tax Year (TY) 2001 — somewhat fewer than previous compliance studies, even though the population of individual tax returns had grown over time.

Like the compliance studies of the past, the NRP was designed to allow the IRS to meet certain objectives — to estimate the overall extent of reporting compliance among individual income tax filers and to update the audit-selection formulas. It also introduced several innovations designed to reduce the burden imposed on taxpayers whose returns were selected for the study.

The first NRP innovation was to compile a comprehensive set of data to supplement what was reported on the selected returns. The sources of the "case building" data included third-party information returns from payers of income (e.g., Form W-2 and Form 1099) and prior-year returns filed by taxpayers. Also, for the first time, the IRS added data on dependents obtained from various government sources, as well as data obtained from public records (e.g., current and prior addresses, real estate holdings, business registrations, and involvement with corporations). Together, these data reduced the amount of information requested from taxpayers, with some of the selected taxpayers not requiring any contact from the IRS. In effect, these data allowed the IRS to focus its efforts on return information that could not otherwise be verified. This pioneering approach was so successful it is being expanded in regular operational audit programs.

A second major NRP innovation was to introduce a "classification" process, whereby the randomly selected returns and associated case-building data were first reviewed by experienced auditors (referred to as classifiers) who identified not only which issues needed to be examined, but also the best way to handle each return in the sample. In this way, each return was either: (1) accepted as filed, without contacting the taxpayer at all (although, sometimes, minor adjustments were noted for research purposes); (2) selected for correspondence audit of up to three focused issues; or (3) selected for an in-person audit where there were numerous items that needed to be verified. In addition, the classifiers identified compliance issues that the auditor was required to evaluate, although the examiners had the ability to expand the audit to investigate other issues as warranted.

Other NRP innovations included streamlining the collection of data, providing auditors with new tools to detect noncompliance, and involving stakeholders (including representatives of tax professional associations) in the design and implementation of the study. Clearly, the NRP approach was much less burdensome on taxpayers than the old TCMP audits, which examined every line item on every return.

Tax Gap Estimates

As noted above, for the 2001 tax year, the overall gross tax gap was estimated to be approximately $345 billion, corresponding to a noncompliance rate of 16.3 percent. After accounting for enforcement efforts and late payments, the amount was reduced to $290 billion, corresponding to a net noncompliance rate of 13.7 percent.

Noncompliance takes three forms:

• Not filing required returns on time (nonfiling);
• Not reporting one's full tax liability on a timely filed return (underreporting); and,
• Not timely paying the full amount of tax reported on a timely return (underpayment).

The IRS has separate tax gap estimates for each of these three types of noncompliance. Underreporting (in the form of unreported receipts and overstated expenses) constitutes over 82 percent of the gross tax gap, up slightly from earlier es-

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timates. Underpayment constitutes nearly 10 percent and nonfiling almost 8 percent of the gross tax gap.

Nonfiling

The nonfiling gap is defined as the amount of true tax liability that is not paid on time by taxpayers who do not file a required return on time (or at all). It is reduced by amounts paid on time, such as through withholding, estimated payments, and other credits. The nonfiler population does not include legitimate nonfilers (i.e., those who have no obligation to file).

Underreporting

The underreporting gap is defined as the amount of tax liability not voluntarily reported by taxpayers who file required returns on time. For income taxes, the underreporting gap arises from three errors: underreporting taxable income, overstating offsets to income or to tax, and net math errors. Taxable income includes such items as wages and salaries, rents and royalties, and net business income. Offsets to income include income exclusions, exemptions, statutory adjustments, and deductions. Offsets to tax are tax credits. Net math errors involve arithmetic mistakes or transcription errors made by taxpayers that are corrected at the time the return is processed. In addition to developing an estimate of the aggregate underreporting gap, it is possible to break aspects of this estimate down into measures of the underreporting gap attributable to specific line items on the tax return.

Underpayment

The underpayment gap is the portion of the total tax liability that taxpayers report on their timely filed returns but do not pay on time. This arises primarily from insufficient remittances from taxpayers themselves. However, it also includes employer under-deposits of withheld income tax. In the case of withheld income tax, it is the responsibility of the employees to report the corresponding tax liability on timely filed returns, and it is the responsibility of their employers to deposit those withholdings with the government on time.

[FN1]. “Comprehensive Strategy for Reducing the Tax Gap,” U.S. Department of the Treasury, Office of Tax Policy, September 26, 2006.

[FN2]. “Reducing the Federal Tax Gap: A Report on Improving Voluntary Compliance,” Internal Revenue Service, Department of the Treasury, August 2, 2007.

[FN3]. The IRS's top-level measures, goals, and timelines are published in the Appendix to its strategic plan, available at http://www.irs.gov/pub// newsroom/long_term_measures.pdf

[FN4]. “Advancing E-file Study Phase 1 Report: Achieving the 80% E-file Goal Requires Partnering with Stakeholders on New Approaches to Motivate Paper Filers,” Internal Revenue Service, Department of the Treasury, September 30, 2008.

[FN5]. This section is reproduced from “Reducing the Federal Tax Gap: A Report on Improving Voluntary Compliance,” Internal Revenue Service, Department of the Treasury, August 2, 2007, pp. 6-9.

Society of Trust and Estate Practitioners - U.S., Inc.
Experience with the IRS Voluntary Disclosure Program for Foreign Bank Accounts and FBAR with Q&A
Thursday, 13 August 2009 Program Description
TIME: 12:15 - 1:30
SPEAKERS: Gideon Rothschild, JD, CPA and Neil A.J. Sullivan, CPA

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LOCATION: Moses & Singer, LLP, Chrysler Building, 405 Lexington Ave., Between 42nd St. and 43rd St., 12th Floor

TOPIC: Experience with the IRS Voluntary Disclosure Program for Foreign Bank Accounts and FBAR with Q&A

On June 12, 2009, IRS representatives gave surprising responses to 20 pages of questions presented by practitioners concerning FBAR reports (Form TD-F90-22.1). The IRS has extended the due date to September 23 for certain taxpayers. The presenters, who have represented numerous clients with foreign accounts, will share their experiences with you as well as answer your questions about FBAR reporting requirements.

Attendees are encouraged to bring questions and submit written comments and recommendations for submission to the IRS.

Members who are unable to attend this meeting but wish to send questions/comments for submission should send them to Jack Brister at jbrister @ere-cpa.com

CLE Credit: This program qualifies for One Hour CLE Credit for New York Lawyers

Thursday, 13 August 2009 **Program Outline & Index to reference materials**

1.0 **Voluntary Disclosure - Background**

1.1 Offshore Voluntary Compliance Initiative Rev Proc 2003-11

1.2 IRS Unveils Offshore Voluntary Compliance Initiative; Chance for 'Credit-Card Abusers' to Clear Up Their Tax Liabilities IR-2003-5, Jan. 14, 2003

1.3 IRS and FinCEN Announce Latest Efforts to Crack Down on Tax Avoidance IR-2003-48 10April03

1.4 Internal Revenue Bulletin - March 24, 2008 - Voluntary Compliance Initiative Covering Policies of Insurance and Reinsurance Issued by Foreign Insurers Announcement 2008-18.

1.5 Income from Abroad is Taxable IRS gov 5 Jun 09

1.6 Offshore Voluntary Compliance Initiative (OVCI) has Month to go People Need to Apply Directly IRS gov 01 Nov07

2 **Voluntary Disclosure — Current**

2.0a IRS memorandum_authorizing_penalty_framework Linda Stiff IRS gov 23Mar09

2.0b Statement from IRS Commissioner Doug Shulman on Offshore Income 26Mar09

2.1 AICPA e-alert re IRS six months FBAR Voluntary Disclosure policy until 23Sep09 3Apr09

2.2 Revised IRS Voluntary Disclosure Practice **TAX CRIMES - GENERAL** IRM 9.5.11.9 IRS gov 26Jun09

2.3 A voluntary disclosure occurs when the communication is truthful, timely, complete, and when the taxpayer shows a willingness to cooperate (and does in fact cooperate) with the IRS in determining his or her correct tax liability; and the taxpayer makes good faith arrangements with the IRS to pay in full, the tax, interest, and any penalties determined by the IRS to be applicable.

2.4 Contact IRS About Voluntary Disclosure list of telephone numbers by 50 states & 9 countries IRS gov 29Jul09

2.5 IRS letter-voluntary-disclosure-option-three page format-29Jul 2009 IRS gov.doc

2.6 NYS Voluntary Disclosure and Compliance Program 29Jul09

2.7 Voluntary Disclosure Q&A FAQ 1 to 51 IRS gov 31Jul09

3.0 Report of Foreign Bank & Financial Accounts Form TDF 90-22.1

3.0a Workbook on the Report of Foreign Bank and Financial Accounts (FBAR) IRS gov 19Feb09

3.1 Foreign Financial Accounts Reporting Requirements IRS gov 27 Feb 07

3.2 AICPA Update on New FBAR Form Reporting and Due Diligence Requirements

3.3 Foreign Trust Reporting Requirements IRS gov 2 Dec 08

3.4 Penalties CHART for non-filing Criminal & Civil per Workbook (FBAR) IRS gov 19Feb09.

3.5 FAQs Regarding Report of Foreign Bank and Financial Accounts (FBAR) - United States Person IRS gov 29Jun09

3.6 FAQs Regarding Report of Foreign Bank and Financial Accounts (FBAR) — Financial Accounts IRS gov 29Jun09

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3.7 FAQs Regarding Report of Foreign Bank and Financial Accounts (FBAR) - Filing Requirements 29Jun09

3.8 Report of Foreign Bank and Financial Accounts OVERVIEW & links IRS gov 30Jun09

3.9 Temporary Suspension of FBAR filing Requirements for Persons who are not Citizens IRA 05Jun09 Announcement 2009-51

3.10 September 23 Deadline for Some FBAR Filers IRS gov 14Jul09

3.11 One Year Moratorium -- FBAR Filing Requirements — Extended Filing Date for U.S. Persons Having Signature Authority Over, But No Financial Interest In, a Foreign Financial Account, and for U.S. Persons with Financial Interest In, or Signature Authority Over, Foreign Commingled Funds: Request for Public Comments on FBAR Filing Requirements Notice 2009-62 released 7Aug09

3.12 Attorneys want FBAR clarification from IRS- 11Aug09- Pensions & Investments

3.13 AICPA Journal of Accountancy FBAR Resources online 7Aug09 (extensive listing)

3.14 CPA Letter 11Aug09 Sign up for Aug. 20 teleconference on IRS' FBAR filing requirements and new offshore income Voluntary Disclosure

3.15 Foreign Bank Account Reports and More: Voluntary Disclosure - September 23 Deadline! August 20, 2009 11:00 AM — 12:30 PM EDT TELECONFERENCE with IRS sponsored by — ABA, AICPA & STEP

Part III - Administrative, Procedural, and Miscellaneous

Offshore Voluntary Compliance Initiative

Rev. Proc. 2003-11

SECTION 1. PURPOSE

.01 This revenue procedure describes the Internal Revenue Service's Offshore Voluntary Compliance Initiative for taxpayers that have underreported their United States income tax liability through financial arrangements that in any manner rely on the use of offshore payment cards (including credit, debit, or charge cards) issued by banks in foreign jurisdictions or offshore financial arrangements (including arrangements with foreign banks, financial institutions, corporations, partnerships, trusts, or other entities). This revenue procedure applies to tax years ending after December 31, 1998, and to tax years ending before that date to the extent provided in section 8 of this revenue procedure.

.02 The Service has determined that some taxpayers have used offshore payment cards or offshore financial arrangements to avoid United States income taxes. The Offshore Voluntary Compliance Initiative described in this revenue procedure affords taxpayers that have used these devices an opportunity to avoid certain penalties that would otherwise apply.

SECTION 2. SCOPE OF THE OFFSHORE VOLUNTARY COMPLIANCE INITIATIVE

.01 With respect to unreported income or false deductions associated with the use of offshore payment cards or offshore financial arrangements, the Service:

(1) will not impose the civil fraud penalty under section 6663, the fraudulent failure to file penalty under section 6651(f), and information return civil penalties for failure to comply with sections 6035, 6038, 6038A, 6038B, 6038C, 6039F, 6046, 6046A, and 6048; and

(2) will, in appropriate circumstances, impose the delinquency penalty under section 6651, the accuracy—related penalty under section 6662, or both penalties against taxpayers that participate in the Offshore Voluntary Compliance Initiative.

.02 The Financial Crimes Enforcement Network (FinCEN) will not impose civil penalties for failure to timely file a Report of Foreign Bank and Financial Accounts (FBAR) against eligible taxpayers that participate in the Offshore Voluntary Compliance Initiative. For more information, see FinCEN's website at www.fincen.gov and look under Regulatory/BSA Guidance.

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.03 The Service will treat the request to participate in the Offshore Voluntary Compliance Initiative as a request to make a voluntary disclosure pursuant to its Voluntary Disclosure Practice as described in IR-2002-135, Dec. 11, 2002. See also Treasury Directive 15-41, dated December 1, 1992 (delegating to the Service the authority to investigate the criminal FBAR penalty).

.04 Any contact or communication by the Service with a taxpayer regarding the taxpayer's request to participate in the Offshore Voluntary Compliance Initiative is not an examination of books and records for purposes of section 7605(b) or Rev. Proc. 94-68, 1994-2 C.B. 803. The Service may audit the returns of any taxpayer that participates in the Offshore Voluntary Compliance Initiative, and may propose adjustments for items that are not resolved under the Offshore Voluntary Compliance Initiative.

SECTION 3. APPLICATION PROCESS

.01 Taxpayers that want to participate in the Offshore Voluntary Compliance Initiative must, on or before April 15, 2003, send a written request to participate in the Offshore Voluntary Compliance Initiative to the National Offshore Voluntary Compliance Initiative Coordinator. Taxpayers may send the written request via the United States Postal Service to P.O. Box 480, Bensalern, PA 19020; by private delivery service to 11601 Roosevelt Blvd., Philadelphia, PA 19154, Attn.: DP S6005; or by email to VCI@irs.gov. The written request must:

(1) state that the taxpayer requests to participate in the Offshore Voluntary Compliance Initiative and is a taxpayer eligible to participate in the program, as described in section 4 of this revenue procedure;

(2) state the taxpayer's name, taxpayer identification number, current address, and daytime telephone number;

(3) state the name and employer identification number of any entity (including but not limited to corporations, partnerships, trusts, and estates) that the taxpayer caused to use offshore payment cards or offshore financial arrangements, or that was the source of funds that the taxpayer caused to be transferred to a foreign jurisdiction;

(4) state the name and office location of any Service official whom the taxpayer has previously contacted about making a voluntary disclosure; and

(5) include complete information regarding the taxpayer's introduction to offshore payment cards and offshore financial arrangements, including the following:

(a) the names, addresses, and telephone numbers of any parties who promoted or solicited the taxpayer's use of offshore payment cards or offshore financial arrangements;

(b) if known to the taxpayer, the names, addresses, and telephone numbers of any parties who advised or assisted the promoters or solicitors in marketing offshore payment cards or offshore financial arrangements; and

(c) all promotional materials, transactional materials, and other related correspondence and documentation that the taxpayer at any time received regarding offshore payment cards or offshore financial arrangements. Taxpayers that send a written request to participate in the Offshore Voluntary Compliance Initiative by email to VCI@irs.gov must send these materials by mail or private delivery service (to the addresses provided in subsection .01 above) within five days of the email. These taxpayers should include with the materials a copy of the email sent to VCI@irs.gov.

SECTION 4. TAXPAYERS THAT ARE ELIGIBLE TO PARTICIPATE IN THE OFFSHORE VOLUNTARY COMPLIANCE INITIATIVE

.01 A taxpayer that has used offshore payment cards or offshore financial arrangements is eligible to participate in the Offshore Voluntary Compliance Initiative if the taxpayer meets the following conditions:

(1) the taxpayer's written request to participate in the Offshore Voluntary Compliance Initiative is received before:

(a) the Service has initiated a civil examination or criminal investigation of the taxpayer, or has notified the taxpayer that it intends to commence such an examination or investigation;

(b) the Service has received information from a third party (e.g., informant, other governmental agency, or the me-

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dia) alerting the Service to the specific taxpayer's noncompliance;

(c) the Service has initiated a civil examination or criminal investigation that is directly related to the specific liability of the taxpayer; or

(d) the Service has acquired information directly related to the specific liability of the taxpayer from a criminal enforcement action (e.g., search warrant, grand jury subpoena);

(2) the taxpayer has not promoted, solicited, or, in any way, facilitated the participation of others (other than members of the taxpayer's immediate family, or of individuals from whom the taxpayer did not receive compensation of more than a nominal amount) in arrangements to avoid taxation by using offshore payment cards, offshore financial arrangements, or any other abusive transaction, domestic or offshore, such as arrangements based on arguments refuted by the Service in The Truth About Frivolous Tax Arguments found at www.irs.gov/pub/irs-utl/friv_tax.pdf;

(3) during the years in which the taxpayer seeks to participate in the Offshore Voluntary Compliance Initiative, the taxpayer has not derived income from illegal sources, such as income from drug trafficking; and

(4) during the years in which the taxpayer seeks to participate in the Offshore Voluntary Compliance Initiative, the taxpayer has not used the offshore payment cards or offshore financial arrangements to support or, in any way, facilitate illegal activities not related to taxes.

SECTION 5. ACKNOWLEDGMENT OF THE TAXPAYER'S REQUEST TO PARTICIPATE IN THE OFFSHORE VOLUNTARY COMPLIANCE INITIATIVE

.01 The Service will acknowledge receipt of the taxpayer's written request to participate in the Offshore Voluntary Compliance Initiative within 30 calendar days of receipt of the request. In its acknowledgment, the Service will advise whether the taxpayer has been preliminarily determined to be eligible to participate in the Offshore Voluntary Compliance Initiative or has been determined to be ineligible to participate in the Offshore Voluntary Compliance Initiative. A preliminary determination of eligibility will not prevent the Service from later determining that the taxpayer is not eligible to participate in the Offshore Voluntary Compliance Initiative due to a failure to comply with the conditions of section 4.01(2), (3), or (4), section 6, or section 7 of this revenue procedure.

SECTION 6. ADDITIONAL REQUIREMENTS THAT A TAXPAYER MUST SATISFY AFTER THE SERVICE PRELIMINARILY DETERMINES THAT THE TAXPAYER IS ELIGIBLE TO PARTICIPATE IN THE OFFSHORE VOLUNTARY COMPLIANCE INITIATIVE

.01 Within 150 calendar days of the date of the letter informing the taxpayer that the Service has preliminarily determined that the taxpayer is eligible to participate in the Offshore Voluntary Compliance Initiative, the taxpayer must send the following material to the National Offshore Voluntary Compliance Initiative Coordinator, via the United States Postal Service to P.O. Box 480, Bensalem, PA 19020, or by private delivery service to 11601 Roosevelt Blvd., Philadelphia, PA 19154, Attn.; DP S6005:

(1) copies of original and amended federal income tax returns for tax periods ending after December 31, 1998, that the taxpayer previously filed;

(2) copies of any powers of attorney (Forms 2848) granted by the taxpayer with respect to tax years in which the taxpayer requests to participate in the Offshore Voluntary Compliance Initiative;

(3) descriptions of offshore payment cards and foreign and domestic accounts of any kind (including the name and address of the bank or financial institution, the account number, and the date the account was opened), and descriptions of foreign assets in which the taxpayer has or had any ownership or beneficial interest or that are or were controlled by the taxpayer (i.e., the taxpayer has or had the practical ability to direct or influence the financial transactions or affairs of an account or entity, or the use or disposition of an asset, whether this ability was exercised directly or indirectly through a nominee, agent, power of attorney, letter of directions, letter of wishes, or any other device whatsoever) at any time after

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December 31, 1998;

(4) descriptions of entities of any kind (including but not limited to corporations, partnerships, trusts, and estates) and any nominees through which the taxpayer exercised control over foreign funds, assets, or investments at any time after December 31, 1998;

(5) descriptions of the source of any foreign funds, assets, or investments owned or controlled by the taxpayer at any time after December 31, 1998;

(6) all promotional materials, transactional materials, and other related correspondence and documentation regarding offshore payment cards or offshore financial arrangements received subsequent to the date the taxpayer submits the request to participate in the Offshore Voluntary Compliance Initiative;

(7) complete and accurate amended or delinquent original federal income tax returns of the taxpayer for all tax years ending after December 31, 1998, which are supported by an explanation of previously unreported income or incorrectly claimed deductions or credits (whether or not related to offshore payment cards or offshore financial arrangements);

(8) complete and accurate amended or delinquent original information returns required by sections 6035, 6038, 6038A, 6038B, 6038C, 6039F, 6046, 6046A, and 6048 for which the taxpayer requests relief from penalties; and

(9) complete and accurate FBARs for tax years ending after December 31, 1998. (FBAR forms are available by contacting FinCEN at 800-949-2732 and on FinCEN's website, www.fincen.gov.)

.02 Upon the Service's request, and within the period of time allowed by the Service in its request, the taxpayer must provide documentation of the matters described in section 6.01 paragraphs (3) through (5) of this revenue procedure, and information regarding all transactions conducted through the foreign accounts and entities.

.03 Upon the Service's request, and within the period of time allowed by the Service in its request, the taxpayer must provide executed consents or special consents to extend the time to assess tax for years that the taxpayer requests to participate in the Offshore Voluntary Compliance Initiative.

.04 At the time the taxpayer files the required amended or delinquent original returns, the taxpayer must fully pay the tax liabilities, including applicable penalties under sections 6651 and 6662, and interest, or make other financial arrangements acceptable to the Service for all years covered by the Offshore Voluntary Compliance Initiative. In addition, the taxpayer must fully pay all other unpaid, previously assessed liabilities, or make other financial arrangements acceptable to the Service. For purposes of this revenue procedure, other financial arrangements acceptable to the Service shall include the completion and submission of complete financial statements to the National Offshore Voluntary Compliance Initiative Coordinator at the time amended or delinquent returns are filed in compliance with section 6.01 of this revenue procedure. A complete financial statement shall include all assets, domestic and foreign, in which the taxpayer has an ownership or beneficial interest or over which the taxpayer has control, whether directly or indirectly, through a nominee, agent, power of attorney, letter of directions, letter of wishes, or any other device.

SECTION 7. FINAL DETERMINATION THAT A TAXPAYER IS ELIGIBLE TO PARTICIPATE IN THE OFFSHORE VOLUNTARY COMPLIANCE INITIATIVE

.01 After an eligible taxpayer meets the requirements of sections 3 and 6 of this revenue procedure, the taxpayer must execute a specific matters closing agreement in the form appended to this revenue procedure as Exhibit 1. In the closing agreement, the taxpayer must waive all defenses to the assessment and collection of tax, penalties, and interest under the Offshore Voluntary Compliance Initiative, including any defenses based on the expiration of the period of limitations on assessment or collection. The taxpayer must also agree that the failure to disclose information that would make the taxpayer ineligible to participate in the Offshore Voluntary Compliance Initiative, or the failure to fully and accurately provide the information required by sections 3 and 6 of this revenue procedure, constitutes a misrepresentation of a material fact under section 7121.

.02 Execution of the closing agreement by the Commissioner constitutes a final determination under section 7121 that

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the taxpayer is eligible to participate in the Offshore Voluntary Compliance Initiative.

SECTION 8. TREATMENT OF TAX YEARS ENDING PRIOR TO JANUARY 1, 1999

.01 For cases resolved under the Offshore Voluntary Compliance Initiative, the Service does not intend to solicit or secure information concerning an eligible participating taxpayer's federal income tax liabilities for tax years ending prior to January 1, 1999. Eligible participating taxpayers, however, must provide information about all aspects of the taxpayer's involvement with offshore payment cards or offshore financial arrangements, regardless of the year in which such activities began.

.02 If it comes to the Service's attention that substantial tax avoidance occurred in tax years ending prior to January 1, 1999, the Service reserves the right to examine such prior tax years and to assess tax, penalties, and interest, if the period of limitations on assessment and collection for those years is open. If any eligible participating taxpayer files complete and accurate amended or delinquent original returns for tax years ending prior to January 1, 1999, which are supported by an explanation of previously unreported income or incorrectly claimed deductions or credits (whether or not related to offshore payment cards or offshore financial arrangements), the Service will resolve the taxpayer's liability for those years for tax, penalties, and interest on the same basis that the Service will resolve liabilities for tax years ending after December 31, 1998, under the Offshore Voluntary Compliance Initiative.

SECTION 9. EFFECTIVE DATE

.01 This revenue procedure is effective on January 14, 2003.

SECTION 10. PAPERWORK REDUCTION ACT

.01 The collection of information contained in this revenue procedure has been reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act (44 U.S.C. § 3507) under control number 1545-1822. An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection of information displays a valid OMB control number.

.02 The collection of information in this revenue procedure is in Section 3 (APPLICATION PROCESS), Section 6 (ADDITIONAL REQUIREMENTS THAT A TAXPAYER MUST SATISFY AFTER THE SERVICE PRELIMINARILY DETERMINES THAT THE TAXPAYER IS ELIGIBLE TO PARTICIPATE IN THE OFFSHORE VOLUNTARY COMPLIANCE INITIATIVE), Section 7 (FINAL DETERMINATION THAT A TAXPAYER IS ELIGIBLE TO PARTICIPATE IN THE OFFSHORE VOLUNTARY COMPLIANCE INITIATIVE), and Section 8 (TREATMENT OF TAX YEARS ENDING PRIOR TO JANUARY 1, 1999). This information will be used to determine whether a taxpayer is eligible for the Offshore Voluntary Compliance Initiative and to apply the terms of the initiative. This information will also further the Service's understanding of how offshore payment cards and offshore financial arrangements have been promoted and solicited. Collection of the information described in this revenue procedure is required to obtain the benefits of the Offshore Voluntary Compliance Initiative. The likely respondents are individuals, corporations, partnerships, trusts, and other entities.

.03 The estimated total annual reporting burden is uncertain but estimated to be at least 100,000 hours. The estimated annual burden per respondent varies from 25 hours to 75 hours, depending on individual circumstances, with an estimated average of 50 hours. The number of respondents is uncertain but estimated to be in the thousands. The estimated frequency of responses is at least one per respondent.

.04 Books or records relating to a collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally tax returns and tax return information are confidential, as required by 26 U.S.C. § 6103.

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SECTION 11. CONTACT INFORMATION

.01 The principal author of this revenue procedure is Stuart Spielman of the Office of the Associate Chief Counsel (Procedure and Administration). For further information regarding this revenue procedure, please contact the Office of the National Offshore Voluntary Compliance Initiative Coordinator at 215-516-3537 (not a toll-free number) or visit www.irs.gov.

EXHIBIT 1

Department of the Treasury—Internal Revenue Service

Closing Agreement On Final Determination Covering Specific Matters

Under section 7121 of the Internal Revenue Code:
____________________ (Taxpayer's name)
____________________ (Taxpayer's address and identifying number)
WHEREAS, Taxpayer has underreported federal income taxes for [specify tax years] through financial arrangements that in some manner rely on the use of offshore payment cards (including credit, debit, or charge cards) issued by banks in foreign jurisdictions or offshore financial arrangements (including arrangements with foreign banks, financial institutions, corporations, partnerships, trusts, or other entities);
WHEREAS, Taxpayer has requested to participate in the Offshore Voluntary Compliance Initiative, which is described in Revenue Procedure 2003-11; and
WHEREAS, Taxpayer has agreed to all the terms and conditions of the Offshore Voluntary Compliance Initiative.

NOW IT IS HEREBY DETERMINED AND AGREED FOR FEDERAL TAX PURPOSES THAT:

1. For [Year 1], Taxpayer used offshore payment cards or offshore financial arrangements to avoid reporting income in the amount of [specify amount] and to claim false deductions in the amount of [specify amount]. [Insert only if applicable: For Year 1, Taxpayer had additional unreported income in the amount of [specify amount] and false deductions in the amount of [specify amount.]] For [Year 2], Taxpayer used offshore payment cards or offshore financial arrangements to avoid reporting income in the amount of [specify amount] and to claim false deductions in the amount of [specify amount]. [Insert only if applicable: For Year 2, Taxpayer had additional unreported income in the amount of [specify amount] and false deductions in the amount of [specify amount]] [Continue in this manner for all tax years.]

2. For [Year 1], penalties under sections [indicate sections] of the Internal Revenue Code apply to underpayments attributable to the unreported income and false deductions. For [Year 2], penalties under sections [indicate sections] apply to underpayments attributable to the unreported income and false deductions. [Continue in this manner for all tax years.]

3. Interest is due as provided by law on Taxpayer's underpayments of tax and penalties.

4. Taxpayer waives all defenses to the assessment and collection of tax, penalties, and interest described in the preceding paragraphs, including any defense based on the expiration of the period of limitations on assessment or collection.

5. This closing agreement does not prevent the Internal Revenue Service from auditing Taxpayer for [specify tax years] and proposing adjustments unrelated to offshore payment cards or to offshore financial arrangements. This closing agreement also does not prevent the Service from proposing adjustments related to offshore payment cards or to offshore financial arrangements if, subsequent to the date that this closing agreement is executed, the Service determines that Taxpayer, contrary to the provisions of Revenue Procedure 2003-11, failed to fully and accurately provide the information and materials required by sections 3 and 6 of the revenue procedure. Any examination or determination under this paragraph 5 does not constitute a second examination for purposes of section 7605(b) of the Code or Rev. Proc. 94-68, 1994-2 C.B. 803.

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6. Failure to disclose information that would make Taxpayer ineligible to participate in the Offshore Voluntary Compliance Initiative or failure to fully and accurately provide the information or material required by sections 3 and 6 of Revenue Procedure 2003-11 constitutes a misrepresentation of a material fact under section 7121 of the Code.

Instructions

This agreement must be signed and filed in triplicate. (All copies must have original signatures.) The original and copies of the agreement must be identical. The name of the taxpayer must be stated accurately. The agreement may relate to one or more years.

If an attorney or agent signs the agreement for the taxpayer, the power of attorney (or a copy) authorizing that person to sign must be attached to the agreement. If the agreement is made for a year when a joint income tax return was filed by a husband and wife, it should be signed by or for both spouses. One spouse may sign as agent for the other if the document (or a copy) specifically authorizing that spouse to sign is attached to the agreement.

If the fiduciary signs the agreement for a decedent or an estate, an attested copy of the letters testamentary or the court order authorizing the fiduciary to sign, and a certificate of recent date that the authority remains in full force and effect must be attached to the agreement. If a trustee signs, a certified copy of the trust instrument or a certified copy of extracts from that instrument must be attached showing:

(1) the date of the instrument;

(2) that it is or is not of record in any court;

(3) the names of the beneficiaries;

(4) the appointment of the trustee, the authority granted, and other information necessary to show that the authority extends to Federal tax matters; and

(5) that the trust has not been terminated, and that the trustee appointed is still acting. If a fiduciary is a party, Form 56, Notice Concerning Fiduciary Relationship, is ordinarily required.

If the taxpayer is a corporation, the agreement must be dated and signed with the name of the corporation, the signature and title of an authorized officer or officers, or the signature of an authorized attorney or agent. It is not necessary that a copy of an enabling corporate resolution be attached.

Use additional pages if necessary, and identify them as part of this agreement.

Please see Revenue Procedure 68-16, C.B. 1968-1, page 770, for a detailed description of practices and procedures applicable to most closing agreements.

This agreement is final and conclusive except:

(1) the matter it relates to may be reopened in the event of fraud, malfeasance, or misrepresentation of material fact;

(2) it is subject to the Internal Revenue Code sections that expressly provide that effect be given to their provisions (including any stated exception for Code section 7122) notwithstanding any other law or rule of law; and

(3) if it relates to a tax period ending after the date of this agreement, it is subject to any law, enacted after the agreement date, that applies to that tax period.

By signing, the above parties certify that they have read and agreed to the terms of this document.

Your signature ____________________

Date Signed ____________________

Spouse's signature (if a joint return was filed) ____________________

Date Signed ____________________

Taxpayer's representative ____________________

Date Signed ____________________

Taxpayer (other than individual) ____________________

By ____________________

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Date Signed ____________________
Title ____________________
Commissioner of Internal Revenue
By ____________________
Date Signed ____________________
Title ____________________

IRS Unveils Offshore Voluntary Compliance Initiative; Chance for 'Credit-Card Abusers' to Clear Up Their Tax Liabilities

IR-2003-5, Jan. 14, 2003

WASHINGTON — Internal Revenue Service officials today announced the launch of an initiative aimed at bringing taxpayers who used "offshore" payment cards or other offshore financial arrangements to hide their income back into compliance with tax law.

Under the Offshore Voluntary Compliance Initiative, eligible taxpayers who step forward will not face civil fraud and information return penalties. However, taxpayers will still have to pay back taxes, interest and certain accuracy or delinquency penalties.

Eligible taxpayers who come forward will also avoid criminal prosecution based upon application of the revised voluntary disclosure practice. A taxpayer who does not come forward now, however, will be subject to payment of taxes, interest, penalties and potential criminal prosecution.

"It's time for those involved in abusive avoidance schemes to make things right," said Acting IRS Commissioner Bob Wenzel. "Our investigators have gathered valuable information about offshore payment cards and offshore financial arrangements in recent months. With today's action, the IRS is sending the clear signal that those involved in these offshore schemes should come forward now on their own."

The Voluntary Compliance Initiative reflects an attempt to bring taxpayers back into compliance quickly while simultaneously gathering more information about the promoters of these offshore schemes. As part of the request to participate, the taxpayer must provide full details on those who promoted or solicited the offshore financial arrangement. The last day a taxpayer can apply is April 15, 2003.

The IRS will use this information to pursue promoters and to obtain information about taxpayers who have avoided tax through the use of offshore payment cards or other offshore financial arrangements and who do not come forward under the Voluntary Compliance Initiative.

"We are striking the proper balance with this initiative. It's sound tax administration, and it will help root out tax evasion," Wenzel said. "Those who misused offshore credit and other payment cards will be able to pay their fair share. Just as importantly, it will help the IRS get the people promoting these deals."

In addition to the names of those who promoted these offshore financial arrangements, taxpayers deemed eligible to participate in the Voluntary Compliance Initiative must provide the details on all aspects of the scheme used to avoid paying the proper tax liability.

Those who promoted or solicited others to avoid tax by using offshore payment cards and other domestic and offshore abusive schemes are not eligible to participate in the Voluntary Compliance Initiative. Complete details on this initiative and eligibility can be found in Revenue Procedure 2003-11, which has also been issued today.

The Voluntary Compliance Initiative grows out of the two-year-old "John Doe" summons investigation. Since October 2000, the IRS has issued a series of summonses to a variety of financial and commercial businesses to obtain information on U.S. residents who held credit, debit or other payment cards issued by offshore banks.

Investigators have been using records from these summonses to trace the identities of those whose use of these payment cards may be related to hiding taxable income. The investigation itself has entailed combing through data on mil-

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lions of transactions.

The results of the investigation have been promising. In its initial steps, the IRS has identified thousands of offshore payment card holders for potential examination. Dozens of cases have already been referred to Criminal Investigation for possible action.

An early estimate suggested possibly more than 1 million payment cardholders could be involved. After reviewing records in recent months obtained from the "John Doe" effort, the IRS has reduced its estimate of the number of abusive cardholders. This later information includes duplicate cards issued to the same individual, inactive or small-dollar accounts, people using the cards because of bad credit, persons traveling abroad and a wide range of other non-tax reasons for holding the cards. While an exact figure of the number of taxpayers involved remains uncertain, IRS officials believe the use of offshore credit, debit and charge cards to evade payment of U.S. taxes involves a substantial number of taxpayers.

"The John Doe summonses are providing us with the information we need," Wenzel said. "It's helping us separate honest taxpayers with legitimate needs from those whose goal is tax evasion. The information clearly highlights a major abusive area that must be addressed."

It is not illegal to have a credit, debit or other payment card issued by an offshore financial institution. However, such cards can provide easy access to offshore funds and accounts in tax haven or bank secrecy countries that allow income to be hidden. U.S. citizens must pay tax on their worldwide income.

Access to information is critical to ensuring the full and fair enforcement of the tax laws. In addition to techniques such as the use of these John Doe summonses, the United States has a broad network of bilateral treaties and agreements with countries throughout the world that allow the IRS to obtain information relevant to the tax liabilities of U.S. taxpayers. Information requested from other countries under these treaties and agreements is an important means by which the IRS identifies taxpayers who attempt to hide income offshore to avoid their tax obligations.

Under the Voluntary Compliance Initiative, eligible taxpayers will have to file or amend their returns and pay interest and certain civil penalties, as well as the tax. The interest and penalties depend on the amount of the unpaid tax liability, the years involved, whether a return was inaccurate or if a return should have been filed and was not.

For example, a taxpayer who understated his income to avoid $100,000 in taxes in 1999 would wind up paying $149,319 to the government. This includes the tax liability plus $29,319 in interest and an additional accuracy-related penalty of $20,000.

If a taxpayer did not step forward, his tax liability generally would include the civil fraud penalty of $75,000, and therefore higher interest of $42,758. The total amount due would be $217,758, without considering probable additional civil penalties for failure to file certain information returns.

The accuracy-related penalty, cited in the above examples, is equal to 20 percent of the tax underpayment. The civil fraud penalty is up to 75 percent of the unpaid tax liability attributable to fraud.

To apply for the Voluntary Compliance Initiative, taxpayers must notify the IRS in writing and provide their name, taxpayer identification number, current address, daytime phone number and certain promoter information as specified in the Revenue Procedure.

The IRS voluntary disclosure practice, which assists agency investigators in determining whether a case is recommended for criminal prosecution, was updated in December (see News Release IR-2002-135).

As part of the Voluntary Compliance Initiative, the IRS will also be closely monitoring the filing of amended returns. If, in order to circumvent this initiative, taxpayers simply file an amended return without complying with the other required provisions, they run the risk of having the civil fraud penalty and other information return penalties applied.

Written requests for the Voluntary Compliance Initiative can be sent to the following mail addresses:

Regular mail:

National Offshore Voluntary Compliance Initiative Coordinator P.O. Box 480 Bensalem, PA 19020

Overnight/Special Delivery:

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National Offshore Voluntary Compliance Initiative Coordinator 11601 Roosevelt Blvd. Philadelphia, PA 19154 DP S6005

Those seeking information by telephone should call: 215-516-3537 (not toll-free). In addition, a special e-mail address has been set up for taxpayers. All e-mail queries should be sent to VCI@irs.gov.

- Statements by Sens. Charles Grassley and Max Baucus
- Statement by Assistant Secretary Pam Olson
- Fact Sheet 2002-12, IRS Sets New Audit Priorities
- Offshore Credit Card Program and John Doe Summonses

Subscribe to IRS Newswire.

IRS and FinCEN Announce Latest Efforts to Crack Down on Tax Avoidance Through Offshore Accounts

IR-2003-48, April 10, 2003

WASHINGTON — Officials of the Internal Revenue Service and the Financial Crimes Enforcement Network (FinCEN) announced today they have signed a memorandum of agreement under which FinCEN delegates its enforcement authority for Foreign Bank and Financial Account reporting to the IRS.

The agreement marks the latest step in the IRS effort to seek out people with undisclosed accounts overseas. In January, the IRS announced an initiative to encourage the voluntary disclosure of unreported income by people who have used offshore payment cards or other offshore financial arrangements improperly to avoid paying taxes. People have only until April 15, 2003 to apply for benefits of the Offshore Voluntary Compliance Initiative (OVCI).

Under the Bank Secrecy Act, U.S. residents or a person in and doing business in the United States must file a report with the U.S. Treasury if he or she has a financial account in a foreign country with a value exceeding $10,000 at any time during the calendar year. Taxpayers comply with this law by noting the account on their tax return and by filing Form 90-22.1, the Foreign Bank and Financial Account Report (FBAR). Willfully failing to file an FBAR report can be punished under both civil and criminal law.

The FBAR penalty will be waived for taxpayers who participate in OVCI.

“This delegation of authority results from increased cooperation between the IRS and other Treasury bureaus to improve compliance with the law,” said acting Commissioner Bob Wenzel. “Our nation will benefit not only from improved compliance with the tax laws, but also our determination to make certain that those with accounts in foreign countries meet their reporting requirements.”

“Unlike other Bank Secrecy Act reports, FBARs are filed mainly by individuals and are more closely related to tax enforcement,” said FinCEN Director, James F. Sloan. “Placing oversight of FBARs with the IRS is a natural fit that should enhance compliance and enforcement.”

A provision of the USA PATRIOT Act required the Secretary of the Treasury to study methods to improve compliance with reporting requirements. Today's agreement delegating enforcement to the IRS grows out of this effort.

For more than two years, IRS investigators have been focused on the use of offshore bank payment cards to avoid reporting income. This investigation continues, and agents assigned to examine income tax returns will also recommend assertion of the FBAR penalties where appropriate.

Since OVCI was announced, the IRS has already collected millions of dollars from the compliance project. Under the initiative, eligible taxpayers who step forward will not face civil fraud, information return or FBAR penalties. However, taxpayers will still have to pay back taxes, interest and certain accuracy or delinquency penalties.

To apply to OVCI, taxpayers must notify the IRS in writing and provide their name, taxpayer identification number, current address, daytime phone number and certain promoter information.

Written requests for the OVCI can be sent to the following mail addresses:

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Regular Mail:

National Offshore Voluntary Compliance Initiative Coordinator P.O. Box 480 Bensalem, PA 19020

Overnight/Special Delivery: National Offshore Voluntary Compliance Initiative Coordinator 11601 Roosevelt Blvd. Philadelphia, PA 19154 DP S6005

Those seeking information by telephone should call: 215-516-3537 (not toll-free). In addition, a special e-mail address, vci@irs.gov, has been set up for taxpayers.

Additional information on the Offshore Voluntary Compliance Initiative is available on this site.

Subscribe to IRS Newswire

Internal Revenue Bulletin: 2008-12
March 24, 2008
Announcement 2008-18
Voluntary Compliance Initiative Covering Policies of Insurance and Reinsurance Issued by Foreign Insurers and Foreign Reinsurers

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- Section 4. Notification Procedures for Participating Taxpayers.
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- Section 6. Non-participating Taxpayers.
- Section 7. Contact Information.

Section 1. Overview and Purpose of the Voluntary Compliance Initiative.

This announcement describes a voluntary compliance initiative by the Internal Revenue Service (IRS) regarding the foreign insurance excise tax. The purpose of this voluntary compliance initiative is to encourage foreign insurers, reinsurers, and other agents, solicitors and brokers to comply with their obligations under section 4371 through 4374 of the Internal Revenue Code (the Code), and in particular, with their obligations described in Revenue Ruling 2008-15, 2008-12 I.R.B.

Revenue Ruling 2008-15 generally clarifies the foreign insurance excise tax consequences under section 4371 *et seq*. of the Code with respect to premiums paid by one foreign insurer or reinsurer to another, including the consequences where the first-mentioned foreign insurer or reinsurer qualifies for an exemption from the foreign insurance excise tax under an income tax treaty with the United States and the second foreign insurer or reinsurer does not qualify for such an exemption.

In order to ensure that all participants in the industry are aware of these tax consequences and their associated reporting and record-keeping obligations, and have a reasonable period of time to come into compliance with them, the IRS is announcing herein that, unless otherwise noted, it will not examine issues arising under the situations set forth in Rev. Rul. 2008-15 in respect of reinsurance premiums paid by one foreign insurer or reinsurer to another prior to October 1, 2008, the first day of the quarterly excise tax period beginning six months after this announcement is published in the Internal Revenue Bulletin. The specific terms of this voluntary compliance initiative are as follows.

Section 2. Eligibility for the Voluntary Compliance Initiative.

.01 Eligible Foreign Person. Any foreign insurer or reinsurer, as defined in section 4372(a), or any other foreign person liable for the tax imposed by section 4371 of the Code ("eligible foreign person"), is eligible to participate if such person has failed to file timely one or more Form 720 returns (*Quarterly Federal Excise Tax Return*) and pay or remit any foreign insurance excise taxes due with respect to premiums paid or received during any quarterly tax period ending prior to October 1, 2008. An eligible foreign person also includes any foreign insurer or reinsurer that has failed to satisfy the treaty-based return disclosure requirements of Treas. Reg. § 301.6114-1(c)(viii), if applicable, with respect to claiming an exemption from foreign insurance excise tax under a U. S. income tax treaty during any such period.

.02 Ineligible Failures to File. Notwithstanding that a foreign insurer or reinsurer is an eligible foreign person, certain failures by that person to file a Form 720 return and pay excise tax will not fall within the scope of the initiative. Accordingly, such failures to file and pay occurring during any quarterly tax period ending prior to October 1, 2008, will not be protected from examination as described in Section 5 below, regardless of whether the foreign insurer or reinsurer is a participating taxpayer, as described in Section 3 below, in this voluntary compliance initiative. The failures to file that are not covered by this initiative include:

a. In the case of a foreign insurer or reinsurer that has entered into a closing agreement with the IRS based on Appendix A of Rev. Proc. 2003-78, 2003-2 C.B. 1029, or any predecessor revenue procedure, any failure to pay foreign insurance excise tax with respect to premiums received on policies issued by that foreign insurer or reinsurer that do not qualify for an exemption from tax under the income tax treaty with the country in which it is resident because that foreign insurer or reinsurer has reinsured, in whole or in part, a policy of reinsurance with a foreign reinsurer not entitled to an exemption from tax under that treaty or any other treaty; and

b. In the case of a foreign insurer or reinsurer that has entered into a closing agreement with the IRS based on Appendix B of Rev. Proc. 2003-78, 2003-2 C.B. 1029, any failure to pay foreign insurance excise tax with respect to premiums received on policies issued by that foreign insurer or reinsurer where, as part of a conduit arrangement, the foreign insurer or reinsurer reinsures, in whole or in part, a policy of insurance or reinsurance with any person not entitled to an exemption from tax under that treaty or any other treaty.

Section 3. Participation Requirements.

.01 Participating Taxpayers. A participating taxpayer under this voluntary compliance initiative is any eligible foreign person that timely files the applicable Form 720 return or returns and pays any foreign insurance excise taxes due with respect to premiums paid or received on or after October 1, 2008, or, if applicable, who timely discloses in accordance with section 6114 of the Code its treaty-based return position that it is entitled to an exemption under an income tax treaty with the United States with respect to such premiums. If a participating taxpayer does not make any premium payment for policies of reinsurance covering contracts described in section 4371 of the Code during the quarterly tax period beginning on October 1, 2008, and is not otherwise obligated to file a Form 720 return to disclose a treaty-based return position, it may still participate in this compliance initiative if it timely files a blank Form 720 return with the notation described in Section 4 below.

.02 Recordkeeping Requirements. A taxpayer will not be considered a participating taxpayer, however, if it does not also comply with the record-keeping requirements in Treas. Reg. § 46.4371-4 with respect to premiums paid or received on or after October 1, 2008, which includes maintaining the appropriate records "for at least 3 years from the date any part of the tax became due or the date any part of the tax is paid, whichever is later, in such manner as to be readily accessible to authorized internal revenue officers or employees".

.03 Determination of Date of Receipt. For purposes of determining whether foreign insurance excise taxes are due with respect to premiums received by a foreign insurer or reinsurer, a premium will be treated as received on or after October 1, 2008, if the date on which the liability for the foreign insurance excise tax attaches, within the meaning of Treas. Reg. §46.4374-1(b), occurs on or after October 1, 2008. For example, if an insured pays to a participating taxpayer, prior to

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October 1, 2008, a premium on a covered policy that is exempt from foreign insurance excise tax under section 4371 of the Code by reason of an income tax treaty, and the participating taxpayer makes a premium payment reinsuring the risk covered by such policy with a person not entitled to the benefits of an income tax treaty on or after October 1, 2008, liability for the foreign insurance excise tax with respect to the premium paid to the participating taxpayer will generally attach as of the date that the second premium is paid by the participating taxpayer, and will, therefore, be treated as received by the participating taxpayer on or after October 1, 2008.

Section 4. Notification Procedures for Participating Taxpayers.

A participating taxpayer under this voluntary compliance initiative must file its Form 720 return described in Section 3 above with the Cincinnati Service Center at the following address:

Department of Treasury Internal Revenue Service Center Cincinnati, OH 45999-0009

In addition to filing its Form 720 return with the Cincinnati Service Center, a participating taxpayer must also notify the IRS of its election to participate by including a notation, as described below, on the Form 720 return.

A participating taxpayer must notate in red print at the top of the Form 720 return the following statement:

Election to participate in FET Voluntary Compliance Initiative pursuant to Announcement 2008-18.

Section 5. Terms for Participating Taxpayers.

Except as provided in Section 2.02, the IRS agrees not to examine any participating taxpayer (whether a foreign insurer, reinsurer, agent, solicitor or broker) with respect to tax liabilities arising under the four situations set forth in Rev. Rul. 2008-15, or any similar fact pattern, to the extent that premiums are paid or received by the participating taxpayer during any quarterly tax period prior to October 1, 2008.

Section 6. Non-participating Taxpayers.

A non-participating taxpayer under this voluntary compliance initiative is defined as an eligible foreign person who is not a participating taxpayer.

The IRS may: (a) conduct examinations of a non-participating taxpayer covering *any and all* excise taxes due under section 4371 of the Code for any open tax periods, including tax periods beginning prior to October 1, 2008; and, (b) determine and assess the correct excise taxes due under section 4371 of the Code, including interest, additions to tax, and, if applicable, penalties under section 6712 of the Code for failure to disclose a treaty-based return position under section 6114 of the Code and the regulations thereunder, and penalties under section 7270 of the Code for failure to comply with section 4374 of the Code.

Section 7. Contact Information.

Various personnel from the Office of Large and Mid-Sized Business Unit, the Office of Small Business/Self Employed Business Unit, and the Office of the Associate Chief Counsel (international), participated in drafting this announcement. For further information regarding this announcement, contact Charles E. Jenkins with the Office of Large and Mid-Sized Business Unit (Pre-Filing and Technical Guidance) via e-mail at *charles.e.jenkins@irs.gov*, or Jody Angelo with the Office of Small Business/Self Employed Business Unit (Excise Policy) via e-mail at *jody.j.angelo@irs.gov*.

Income from Abroad is Taxable

Many United States (U.S.) citizens and resident aliens receive income from foreign sources. There have been recent reports about the interest of the Internal Revenue Service (IRS) in taxpayers with accounts in Liechtenstein. The interest of

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the IRS, however, extends beyond accounts in Liechtenstein to accounts anywhere in the world. Consequently, the IRS reminds you to report your worldwide income on your U.S. tax return.

If you are a U.S. citizen or resident alien, you must report income from all sources within and outside of the U.S. This is true whether or not you receive a Form W-2 Wage and Tax Statement, a Form 1099 (Information Return) or the foreign equivalents. See Publication 525, Taxable and Nontaxable Income for more information.

Additionally, if you are a U.S. citizen or resident alien, the rules for filing income, estate and gift tax returns and for paying estimated tax are generally the same whether you are living in the U.S. or abroad.

Hiding Income Offshore

Not reporting income from foreign sources may be a crime. The IRS and its international partners are pursuing those who hide income or assets offshore to evade taxes. Specially trained IRS examiners focus on aggressive international tax planning, including the abusive use of entities and structures established in foreign jurisdictions. The goal is to ensure U.S. citizens and residents are accurately reporting their income and paying the correct tax.

Foreign Financial Accounts

In addition to reporting your worldwide income, you must also report on your U.S. tax return whether you have any foreign bank or investment accounts. The Bank Secrecy Act requires you to file a Form TD F 90-22.1, Report of Foreign Bank and Financial Accounts (FBAR), if:

- You have financial interest in, signature authority, or other authority over one or more accounts in a foreign country, and
- The aggregate value of all foreign financial accounts exceeds $10,000 at any time during the calendar year.

More information on foreign financial account reporting requirements is in News Release FS-2007-15, Foreign Financial Accounts Reporting Requirements and Publication 4261, Do You have a Foreign Financial Account?

Consequences for Evading Taxes on Foreign Source Income

You will face serious consequences if the IRS finds you have unreported income or undisclosed foreign financial accounts. These consequences can include not only the additional taxes, but also substantial penalties, interest, fines and even imprisonment.

Reporting Promoters of Off-Shore Tax Avoidance Schemes

The IRS encourages you to report promoters of off-shore tax avoidance schemes. Whistleblowers who provide allegations of fraud to the IRS may be eligible for a reward by filing Form 211, Application for Award for Original Information, and following the procedures outlined in Notice 2008-4, Claims Submitted to the IRS Whistleblower Office under Section 7623.

Offshore Voluntary Compliance Initiative has Month to go; People Need to Apply Directly to Receive Penalty Relief

IR-2003-35, March 17, 2003

WASHINGTON — Internal Revenue Service officials today reminded people that time is running short for those who have used offshore payment cards or other offshore financial arrangements to avoid U.S. taxes and who want to take advantage of the Offshore Voluntary Compliance Initiative (OVCI). Individuals need to apply directly to OVCI to receive the initiative's penalty relief.

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People need to come forward and request to participate in the OVCI by April 15, 2003. To request participation, taxpayers must notify the IRS in writing and provide their name, taxpayer identification number, current address, daytime phone number and certain promoter information.

"Time is running out for offshore tax evaders," said acting Commissioner Bob Wenzel. "April 15 is the last chance to come forward under this program and make things right. If these people don't act now, there's a much higher price to be paid later."

Once taxpayers have been deemed eligible to participate, they have 150 days to provide all required documents and information to the IRS. Full details on terms, eligibility and how to apply can be found in the Revenue Procedure 2003-11.

"Those who are involved with abusive offshore practices need to come forward, identify themselves and tell the IRS the names of those who sought to sell them on these schemes," said Wenzel. "They need to avoid the temptation of trying to slip by or they will face the consequences."

In monitoring the filing of amended and delinquent returns, the IRS has detected taxpayers who appear to have used offshore payment cards and other offshore financial arrangements. These taxpayers, however, are filing their returns without requesting participation in the OVCI.

IRS officials are closely screening such returns to determine which civil penalties are warranted. Since in these circumstances, the taxpayer has not requested participation in the OVCI, the taxpayer will not receive the initiative's penalty relief. In appropriate circumstances, the taxpayer will face the full range of civil penalties, including the civil fraud penalty. The civil fraud penalty is 75 percent of the unpaid tax liability attributable to fraud.

In response to inquiries, the IRS has clarified its position regarding the OVCI and prior year tax returns. Although the initiative only requires taxpayers to file amended or delinquent returns for the last three years (1999-2001), it also offers taxpayers the same terms if they choose to bring earlier years into the initiative. Eligible taxpayers who choose to bring the years 1996-1998 into the initiative will not be examined for any earlier years.

Since announcing the OVCI in mid-January, the IRS has received numerous questions on the Initiative. To assist potential applicants and their tax advisers, the IRS has updated the Frequently Asked Questions.

- Updated Questions (These links to dated information were deleted May 16, 2005.)
- General Questions
- Eligibility
- Request Period
- 150-day Submission Period

Written requests for the OVCI can be sent to the following mail addresses:

Regular Mail:

National Offshore Voluntary Compliance Initiative Coordinator P.O. Box 480 Bensalem, PA 19020

Overnight/Special Delivery:

National Offshore Voluntary Compliance Initiative Coordinator 11601 Roosevelt Blvd. Philadelphia, PA 19154 DP S6005

Those seeking information by telephone should call: 215-516-3537 (not toll-free). In addition, a special e-mail address has been set up for taxpayers.

Subscribe to IRS Newswire

Voluntary Disclosure

Taxpayers with unreported income relating to offshore transactions who wish to voluntarily disclose the information to

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the IRS can find information on the process.

For a complete understanding of the voluntary disclosure procedures, see Internal Revenue Manual (IRM) 9.5.11.9

Taxpayers wanting to participate in the IRS voluntary disclosure process should call the phone number associated with the state in which they reside. See Contact IRS About Voluntary Disclosure. (Updated 7/29/09)

Some questions and answers on the voluntary disclosure process and undisclosed offshore accounts (7/31/2009).

Related Items:

- Memorandum on Routing of Voluntary Disclosure Requests
- Memorandum on SB/SE and LMSB Offshore Examination Cases
- Memorandum Authorizing Application of Penalty Framework
- Questions and Answers (revised 7/31/09) HTML PDF
- September 23 Deadline for Some FBAR Filers
- Voluntary Disclosure Optional Format Letter (Updated 7/29/09)
- IRS Commissioner's Statement on Offshore Income

March 23, 2009

MEMORANDUM FOR COMMISSIONER, LARGE AND MID-SIZE BUSINESS DIVISION COMMISSIONER, SMALL BUSINESS/SELF-EMPLOYED DIVISION

FROM:	Linda E. Stiff Deputy Commissioner for Services and Enforcement
SUBJECT:	Authorization to Apply Penalty Framework to Voluntary Disclosure Requests Regarding Unreported Offshore Accounts and Entities

The purpose of this memorandum is to set forth a penalty framework to be applied to voluntary disclosure requests containing offshore issues. The outlined framework will be applied to all such requests that have been submitted to the IRS and are not yet resolved, and will remain in effect for six months from the date of this memorandum. All voluntary disclosure requests are mandatory work.

As Criminal Investigation (CI) makes preliminary determinations that taxpayers are eligible to make voluntary disclosures, it will forward voluntary disclosure requests with offshore implications to the Philadelphia Offshore Identification Unit (POIU) for civil processing. Those requests will be distributed to and worked by examiners who specialize in offshore examinations. All resulting closing agreements will be reviewed and executed as prescribed by existing delegation orders.

Effective as of the date of this memorandum, you are authorized to execute agreements to resolve the tax liabilities related to offshore issues of taxpayers who make voluntary disclosure requests in the following manner:

(1) Assess all taxes and interest due going back six years (exception: where an account/entity was formed or acquired within the six year look back period, taxes and interest will be assessed starting with the earliest year in which an account was opened/acquired or entity formed). Require the taxpayer to file or amend all returns, including information returns and Form TD F 90-22.1, Report of Foreign Bank and Financial Accounts, commonly known as an “FBAR”,

(2) Assess either an accuracy or delinquency penalty on all years (no reasonable cause exception may be applied), and

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(3) In lieu of all other penalties that may apply, including FBAR and information return penalties, assess a penalty equal to 20% of the amount in foreign bank accounts/entities in the year with the highest aggregate account/asset value.

If, (a) the taxpayer did not open or cause any accounts to be opened or entities formed, (b) there has been no activity in any account or entity (no deposits, withdrawals, etc.) during the period the account/entity was controlled by the taxpayer, and (c) all applicable U.S. taxes have been paid on the funds in the accounts/entities (where only account/entity earnings have escaped U.S. taxation), then the penalty in (3) is reduced to 5%.

The terms outlined herein are only applicable to taxpayers that make voluntary disclosure requests, and who fully co-operate with the IRS, both civilly and criminally.

cc: Acting Chief Counsel Senior Advisor to the Commissioner Commissioner, Tax Exempt and Government Entities Chief, Criminal Investigation

Statement from IRS Commissioner Doug Shulman on Offshore Income

March 26, 2009

My goal has always been clear — to get those taxpayers hiding assets offshore back into the system. We recently provided guidance to our examination personnel who are addressing voluntary disclosure requests involving unreported offshore income. We believe the guidance represents a firm but fair resolution of these cases and will provide consistent treatment for taxpayers. The goal is to have a predictable set of outcomes to encourage people to come forward and take advantage of our voluntary disclosure practice while they still can.

In the guidance to our people, we draw a clear line between those individual taxpayers with offshore accounts who voluntarily come forward to get right with the government and those who continue to fail to meet their tax obligations. People who come in voluntarily will get a fair settlement. We set up a penalty framework that makes sense for them — they need to pay back-taxes and interest for six years, and pay either an accuracy or delinquency penalty on all six years. They will also pay a penalty of 20 percent of the amount in the foreign bank accounts in the year with the highest aggregate account or asset value. Just to be clear, this is 20 percent of the highest asset value of an account anytime in the past six years. This gives taxpayers — and tax practitioners — certainty and consistency in how their case will be handled.

We have instructed our agents to resolve these taxpayers' cases in a uniform, consistent manner. Those who truly come in voluntarily will pay back taxes, interest and a significant penalty, but can avoid criminal prosecution.

At the same time, we have also provided guidance to our agents who have cases of unreported offshore income when the taxpayer did not come in through our voluntary disclosure practice. In these cases, we are instructing our agents to fully develop these cases, pursuing both civil and criminal avenues, and consider all available penalties including the maximum penalty for the willful failure to file the FBAR report and the fraud penalty.

We believe this is a firm, but fair resolution of these cases. It will make sure that those who hid money offshore pay a significant price, but also allow them to avoid criminal prosecution if they come in voluntarily. As we continue to step up our international enforcement efforts, this is a chance for people to come clean on their own. Our guidance to the field is for the next six months only, after which we will re-evaluate our options.

For taxpayers who continue to hide their head in the sand, the situation will only become more dire. They should come forward now under our voluntary disclosure practice and get right with the government.

FBAR Penalties Reduced for Six Months - IRS Voluntary Disclosure Framework

IRS recently provided a framework for voluntary disclosure requests regarding offshore issues, such as previously undisclosed foreign financial accounts and entities, (March 23, 2009 IRS memo to LMSB and SBSE, see March 26, 2009, IRS Commissioner statement at http://www.irs.gov/newsroom/article/0,,id=206014,00.html). This IRS policy is in place for six months until September 23, 2009. Taxpayers making voluntary disclosures of offshore non-compliance can avoid

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many civil and criminal penalties that would otherwise apply, such as the account balance FBAR non-disclosure penalty provisions, and other provisions pertaining to various information returns including Form 926, Form 3520, Form 3520-A, Form 5471, Form 5472 and Form 8865. IRS is promising not to pursue criminal penalties and to only impose limited civil penalties. For more information, see http://tax.aicpa.org/Resources/International/IRS+March+2009+Statements+on+Voluntary+Compliance+Penalty+Framework+for+Unreported+Offshore+Accounts.htm

Also, for more information and AICPA resources on the FBAR, click here. There is also more information and links about the 2009 voluntary compliance initiative compiled by one of the AICPA International Tax TRP members at http://www.vernonjacobs.com/voluntary-compliance.html.

Revised IRS Voluntary Disclosure Practice

TAX CRIMES - GENERAL

IRM 9.5.11.9

Voluntary Disclosure Practice

(1) It is currently the practice of the IRS that a voluntary disclosure will be considered along with all other factors in the investigation in determining whether criminal prosecution will be recommended. This voluntary disclosure practice creates no substantive or procedural rights for taxpayers, but rather is a matter of internal IRS practice, provided solely for guidance to IRS personnel. Taxpayers cannot rely on the fact that other similarly situated taxpayers may not have been recommended for criminal prosecution.

(2) A voluntary disclosure will not automatically guarantee immunity from prosecution; however, a voluntary disclosure may result in prosecution not being recommended. This practice does not apply to taxpayers with illegal source income.

(3) A voluntary disclosure occurs when the communication is truthful, timely, complete, and when:

a. the taxpayer shows a willingness to cooperate (and does in fact cooperate) with the IRS in determining his or her correct tax liability; and

b. the taxpayer makes good faith arrangements with the IRS to pay in full, the tax, interest, and any penalties determined by the IRS to be applicable.

(4) A disclosure is timely if it is received before:

a. the IRS has initiated a civil examination or criminal investigation of the taxpayer, or has notified the taxpayer that it intends to commence such an examination or investigation;

b. the IRS has received information from a third party (e.g., informant, other governmental agency, or the media) alerting the IRS to the specific taxpayer's noncompliance;

c. the IRS has initiated a civil examination or criminal investigation which is directly related to the specific liability of the taxpayer; or

d. the IRS has acquired information directly related to the specific liability of the taxpayer from a criminal enforcement action (e.g., search warrant, grand jury subpoena).

(5) Any taxpayer who contacts the IRS in person or through a representative regarding voluntary disclosure will be directed to Criminal Investigation for evaluation of the disclosure. Special agents are encouraged to consult Area Counsel, Criminal Tax on voluntary disclosure issues.

(6) Examples of voluntary disclosures include:

a. a letter from an attorney which encloses amended returns from a client which are complete and accurate (reporting legal source income omitted from the original returns), which offers to pay the tax, interest, and any penalties determined by the IRS to be applicable in full and which meets the timeliness standard set forth above. This is a voluntary disclosure because all elements of (3), above are met.

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b. a disclosure made by a taxpayer of omitted income facilitated through a barter exchange after the IRS has announced that it has begun a civil compliance project targeting barter exchanges; however the IRS has not yet commenced an examination or investigation of the taxpayer or notified the taxpayer of its intention to do so. In addition, the taxpayer files complete and accurate amended returns and makes arrangements with the IRS to pay in full, the tax, interest, and any penalties determined by the IRS to be applicable. This is a voluntary disclosure because the civil compliance project involving barter exchanges does not yet directly relate to the specific liability of the taxpayer and because all other elements of (3), above are met

c. a disclosure made by a taxpayer of omitted income facilitated through a widely promoted scheme regarding which the IRS has begun a civil compliance project and already obtained information which might lead to an examination of the taxpayer; however, the IRS has not yet commenced an examination or investigation of the taxpayer or notified the taxpayer of its intent to do so. In addition, the taxpayer files complete and accurate returns and makes arrangements with the IRS to pay in full, the tax, interest, and any penalties determined by the IRS to be applicable. This is a voluntary disclosure because the civil compliance project involving the scheme does not yet directly relate to the specific liability of the taxpayer and because all other elements of (3), above are met.

d. A disclosure made by an individual who has not filed tax returns after the individual has received a notice stating that the IRS has no record of receiving a return for a particular year and inquiring into whether the taxpayer filed a return for that year. The individual files complete and accurate returns and makes arrangements with the IRS to pay the tax, interest, and any penalties determined by the IRS to be applicable in full. This is a voluntary disclosure because the IRS has not yet commenced an examination or investigation of the taxpayer or notified the taxpayer of its intent to do so and because all other elements of (3), above, are met.

(7) Examples of what are not voluntary disclosures include:

a. a letter from an attorney stating his or her client, who wishes to remain anonymous, wants to resolve his or her tax liability. This is not a voluntary disclosure until the identity of the taxpayer is disclosed and all other elements of (3) above have been met.

b. a disclosure made by a taxpayer who is under grand jury investigation. This is not a voluntary disclosure because the taxpayer is already under criminal investigation. The conclusion would be the same whether or not the taxpayer knew of the grand jury investigation.

c. a disclosure made by a taxpayer, who is not currently under examination or investigation, of omitted gross receipts from a partnership, but whose partner is already under investigation for omitted income skimmed from the partnership. This is not a voluntary disclosure because the IRS has already initiated an investigation which is directly related to the specific liability of this taxpayer. The conclusion would be the same whether or not the taxpayer knew of the ongoing investigation.

d. a disclosure made by a taxpayer, who is not currently under examination or investigation, of omitted constructive dividends received from a corporation which is currently under examination. This is not a voluntary disclosure because the IRS has already initiated an examination which is directly related to the specific liability of this taxpayer. The conclusion would be the same whether or not the taxpayer knew of the ongoing examination.

e. a disclosure made by a taxpayer after an employee has contacted the IRS regarding the taxpayer's double set of books. This is not a voluntary disclosure even if no examination or investigation has yet commenced because the IRS has already been informed by the third party of the specific taxpayer's noncompliance. The conclusion would be the same whether or not the taxpayer knew of the informant's contact with the IRS.

Contact IRS About Voluntary Disclosure

The IRS stresses that acceptance into a voluntary disclosure arrangement depends on the individual facts and circumstances involved in each case. Taxpayers with unreported income should immediately discuss with their tax professional

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their options to get right with the government, including taking advantage of coming in voluntarily.

A voluntary disclosure occurs when the communication is truthful, timely, complete, and when: A taxpayer shows a willingness to cooperate (and does in fact cooperate) with the IRS in determining his/her correct tax liability.

For a complete understanding of the voluntary disclosure procedures, see Internal Revenue Manual (IRM) 9.5.11.9

Taxpayers cannot rely on the fact that other similarly situated taxpayers may not have been recommended for criminal prosecution. Also, a voluntary disclosure will not automatically guarantee immunity from prosecution; however, a voluntary disclosure may result in prosecution not being recommended. This practice does not apply to taxpayers with illegal source income.

Tax professionals or individuals who want to make a voluntary disclosure, may call the phone number below associated with the State in which the taxpayer resides. Or taxpayers may send a letter to the IRS providing all of the requested information and mailing the signed letter to the appropriate address listed below.

*These phone numbers are for the purpose of making voluntary disclosures **ONLY**.*

Alabama	404-338-7540	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Atlanta Field Office 401 W. Peachtree Street, N. W. Suite 600, STOP 400-D Atlanta, GA 30308
Alaska	907-271-6911	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Seattle Field Office 800 Fifth Avenue, Suite 3950 Seattle, WA 98104
Arizona	602-207-8964	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Phoenix Field Office 4041 N. Central Avenue Suite 112, MS 9000 Phoenix, AZ 85012-5000
Arkansas	615-250-5005	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Nashville Field Office 801 Broadway, Suite 400 Nashville, TN 37203
California - Northern	510-637-1031	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Oakland Field Office 1301 Clay Street, Suite 1780S Oakland, CA 94612
California - Southern	714-347-9226	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Los Angeles Field Office 801 Civic Center Drive West Room 218, MS 8000 Santa Ana, CA 92701
Colorado	303-603-4936	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Denver Field Office PO Box 1767 Denver, CO 80201
Connecticut	617-316-2073	IRS Criminal Investigation Attn: Volun-

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		tary Disclosure Coordinator Boston Field Office 1 Montvale Avenue, Room 205 Stoneham, MA 02180
Delaware	215-861-1392	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Philadelphia Field Office 600 Arch Street, Room 6224 Philadelphia, PA 19106
District of Columbia	202-874-0155	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Washington DC Field Office P.O. Box 1038 Baileys Crossroads, VA 22041
Florida - Northern	727-568-2561	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Tampa Field Office 9450 Koger Blvd, Suite 101 St. Petersburg, FL 33702
Florida - Southern	954-423-7245	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Miami Field Office 7850 SW 6th Court Plantation, FL 33324
Georgia	404-338-7540	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Atlanta Field Office 401 W. Peachtree Street, N. W. Suite 600, STOP 400-D Atlanta, GA 30308
Hawaii	808-539-2843	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Seattle Field Office 800 Fifth Avenue, Suite 3950 Seattle, WA 98104
Idaho	303-603-4936	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Denver Field Office PO Box 1767 Denver, CO 80201
Illinois	312-566-4503	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Chicago Field Office 230 South Dearborn, Room 1400 Chicago, IL 60604
Indiana	312-566-4503	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Chicago Field Office 230 South Dearborn, Room 1400 Chicago, IL 60604
Iowa	402-233-7452	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator St. Louis Field Office 1616 Capital Avenue, Suite

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		460 MS 9000 Omaha, NE 68102
Kansas	402-233-7452	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator St. Louis Field Office 1616 Capitol Avenue, Suite 460 MS 9000 Omaha, NE 68102
Kentucky	615-250-5005	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Nashville Field Office 801 Broadway, Suite 400 Nashville, TN 37203
Louisiana	504-558-1535	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator New Orleans Field Office P.O. Box 2230 New Orleans, LA 70176-2230
Maine	617-316-2073	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Boston Field Office 1 Montvale Avenue, Room 205 Stoneham, MA 02180
Maryland	202-927-9351	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Washington DC Field Office P.O. Box 1038 Baileys Crossroads, VA 22041
Massachusetts	617-316-2073	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Boston Field Office 1 Montvale Avenue, Room 205 Stoneham, MA 02180
Michigan	313-234-2410	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Detroit Field Office 985 Michigan Ave, Room 251 Detroit, Michigan 48226
Minnesota	651-767-3254	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator St. Paul Field Office 30 East 7th Street, Stop 9000 St. Paul, MN 55101
Mississippi	504-558-1535	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator New Orleans Field Office P.O. Box 2230 New Orleans, LA 70176-2230
Missouri	402-233-7452	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator St. Louis Field Office 1616 Capitol Avenue, Suite 460 MS 9000 Omaha, NE 68102
Montana	303-603-4936	IRS Criminal Investigation Attn: Volun-

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		tary Disclosure Coordinator Denver Field Office PO Box 1767 Denver, CO 80201
Nebraska	402-233-7452	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator St. Louis Field Office 1616 Capitol Avenue, Suite 460 MS 9000 Omaha, NE 68102
Nevada	801-799-6763	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Las Vegas Field Office 50 S. 200 E. PO Box 1466 Salt Lake City, UT 84111
New Hampshire	617-316-2073	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Boston Field Office 1 Montvale Avenue, Room 205 Stoneham, MA 02180
New Jersey	732-761-3381	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Newark Field Office P.O. Box 741 Springfield, NJ 07081
New Maxico	505-837-9033	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Phoenix Field Office 4041 N. Central Avenue Suite 112, MS 9000 Phoenix, AZ 85012-5000
New York	212-436-1588	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator New York Field Office 290 Broadway, 4th Floor New York, NY 10007
North Carolina	919-856-4283 ext 408	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Charlotte Field Office 310 New Bern Ave, Suite 210 Raleigh, NC 27601
North Dakota	701-239-5143 ext 292	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator St. Paul Field Office 30 East 7th Street, Stop 9000 St. Paul, MN 55101
Ohio	614-744-3130	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Cincinnati Field Office P.O. Box 973 Cincinnati, OH 45201
Oklahoma	214-413-5979	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Dallas Field Office 1100 Commerce Street, Room 1222 Dallas, TX 75242

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Oregon	503-326-3207	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Seattle Field Office 800 Fifth Avenue, Suite 3950 Seattle, WA 98104
Pennsylvania - Eastern	215-861-1392	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Philadelphia Field Office 600 Arch Street, Room 6224 Philadelphia, PA 19106
Pennsylvania - Western	412-395-6771	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Pittsburgh Field Office P.O. Box 534 Pittsburgh, PA 15230
Rhode Island	617-316-2073	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Boston Field Office 1 Montvale Avenue, Room 205 Stoneham, MA 02180
South Carolina	919-856-4283 ext 408	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Charlotte Field Office 310 New Bern Ave, Suite 210 Raleigh, NC 27601
South Dakota	605-330-4449 ext 266	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator St. Paul Field Office 30 East 7th Street, Stop 9000 St. Paul, MN 55101
Tennessee	615-250-5005	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Nashville Field Office 801 Broadway, Suite 400 Nashville, TN 37203
Texas - Dallas	214-413-5979	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Dallas Field Office 1100 Commerce Street, Room 1222 Dallas, TX 75242
Texas - Houston	281-721-8341	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Houston Field Office 8701 S. Gessner, Stop 9000 HAL Houston, TX 77074
Texas - San Antonio	512-499-5261	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator San Antonio Field Office One International Centre 100 NE Loop 410, Suite 400 San Antonio, TX 78216
Utah	801-799-6763	IRS Criminal Investigation Attn: Volun-

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		tary Disclosure Coordinator Las Vegas Field Office 50 S. 200 E. PO Box 1466 Salt Lake City, UT 84111
Vermont	617-316-2073	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Boston Field Office 1 Montvale Avenue, Room 205 Stoneham, MA 02180
Virginia	703-647-5502	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Washington DC Field Office P.O. Box 1038 Baileys Crossroads, VA 22041
Washington	206-464-4916	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Seattle Field Office 800 Fifth Avenue, Suite 3950 Seattle, WA 98104
West Virginia	412-395-6771	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Pittsburgh Field Office P.O. Box 534 Pittsburgh, PA 15230
Wisconsin	414-231-2448	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator St. Paul Field Office 30 East 7th Street, Stop 9000 St. Paul, MN 55101
Wyoming	303-603-4936	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Denver Field Office PO Box 1767 Denver, CO 80201
INTERNATIONAL		
Puerto Rico	954-423-7872	IRS Criminal Investigation Attn: Voluntary Disclosure Coordinator Miami Field Office 7850 SW 6th Court Plantation, FL 33324
South America	011-571-383-2769	IRS Criminal Investigation International Section, SE:CI:OPS:I 1111 Constitution Avenue, NW Room 2547 Washington, DC 20224 Attn: International Voluntary Disclosure Coordinator
Caribbean	246-227-4143	IRS Criminal Investigation International Section, SE:CI:OPS:I 1111 Constitution Avenue, NW Room 2547 Washington, DC 20224 Attn: International Voluntary Disclosure Coordinator
Mexico & Central America	011-52-55-50-80-29-01	IRS Criminal Investigation International

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		Section, SE:CI:OPS:I 1111 Constitution Avenue, NW Room 2547 Washington, DC 20224 Attn: International Voluntary Disclosure Coordinator
Canada	613-688-5292	IRS Criminal Investigation International Section, SE:CI:OPS:I 1111 Constitution Avenue, NW Room 2547 Washington, DC 20224 Attn: International Voluntary Disclosure Coordinator
Germany, Switzerland, Italy, Russian Federation, Eurasia, Eastern Europe, and Southern Europe	011-49-69-7535-3647 or 3638	IRS Criminal Investigation International Section, SE:CI:OPS:I 1111 Constitution Avenue, NW Room 2547 Washington, DC 20224 Attn: International Voluntary Disclosure Coordinator
United Kingdom, France, Western Europe, Africa, and Middle East	011-4420-7894-0036 or 0037	IRS Criminal Investigation International Section, SE:CI:OPS:I 1111 Constitution Avenue, NW Room 2547 Washington, DC 20224 Attn: International Voluntary Disclosure Coordinator
Far East, Australia, & South Pacific Islands	011-852-2841-2361	IRS Criminal Investigation International Section, SE:CI:OPS:I 1111 Constitution Avenue, NW Room 2547 Washington, DC 20224 Attn: International Voluntary Disclosure Coordinator
Iraq	011-964-770-443-0356	IRS Criminal Investigation International Section, SE:CI:OPS:I 1111 Constitution Avenue, NW Room 2547 Washington, DC 20224 Attn: International Voluntary Disclosure Coordinator

Offshore Voluntary Disclosures — Optional Format

If taxpayer has domestic issues only, please have them contact their local Criminal Investigation office for a traditional voluntary disclosure.

<DATE>

Internal Revenue Service
Criminal Investigation
ATTN: Voluntary Disclosure Coordinator
<CITY Field Office>
<Address>

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<CITY, ST ZIP CODE>
Re: Taxpayer Name
Tax Identification Number
Taxpayer Date of Birth
Taxpayer Address

Dear Voluntary Disclosure Coordinator:

To assist in a timely determination of my acceptance into the Voluntary Disclosure, Program, (*for Voluntary Disclosures involving offshore accounts or assets)* I have addressed *all* of the following items:

- Please include your:
  - Complete name:
  - Social Security Number:
  - DOB:
  - Address:
  - Passport Number (and Country):
  - Current Occupation
- Taxpayer Representative and his/her contact information.
- Explain the source of the funds.
- Disclose if you or any related entities are currently under audit or criminal investigation by the Internal Revenue Service or any other law enforcement authority.
  - Has the IRS notified you that it intends to commence an examination or investigation? **Yes No**
  - Are you under criminal investigation by any law enforcement authority? **Yes No**
  - If yes, please explain.
- Do you believe that the IRS has obtained information concerning your tax liability? **Yes No**
  - If yes, please specify.
- Please check the box to estimate the annual range of the highest aggregate *value* of your offshore accounts/assets.

Highest Aggregate Account/Asset Value	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**
$0 to $100,000						
$100,000 to $1,000,000						
$1,000,000 to $2,500,000						
$2,500,000 to $10,000,000						
Greater than $10,000,000						
Greater than $100,000,000						

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• Please check the box to estimate the potential total unreported *income* from the offshore account(s) during each disclosure period. If known, please enter exact amounts/assets.

Estimated Total Unreported Income	2003	2004	2005	2006	2007	2008
$0 to $100,000						
$100,000 to $1,000,000						
$1,000,000 to $2,500,000						
$2,500,000 to $10,000,000						
Greater than $10,000,000						

• For accounts or assets where you have control or are a beneficial owner of the account or asset, list any and all financial institutions and the country where the institution is located. For accounts, please also list the dates the accounts were opened and/or closed. Provide your point of contact at each financial institution.

• Explain the purpose for establishing the offshore account or assets. For example: Holocaust Compensation or Restitution; inherited account; account established prior to World War II, etc.; if tax non-compliance — please explain.

• List each person or entity affiliated with the account, their formal structure (i.e., if a corporation, foundation, or trust), and the nature of their relationship to the account (i.e. owner, power of attorney, parent entity of corporate account holder, etc.).

• Explain all face to face meetings, and any other communications you had regarding the accounts or assets with the financial institution(s). Also include face to face meetings or communications regarding the accounts or assets with independent advisors/investment managers not from the financial institution(s) where the funds are held. Provide the names, locations and dates of these meetings and/or communications.

To be included with all letters:

By signing this document, I certify that I am willing to continue to cooperate with the Internal Revenue Service, including in assessing my income tax liabilities and making good faith arrangements to pay all taxes, interest, and penalties associated with this voluntary disclosure.

Under penalties of perjury, I declare that I have examined this document and accompanying statements, and to the best of my knowledge and belief, they are true, correct, and complete.

____________________	____________________	____________________
Signature of Taxpayer	Print Name	Date

IRS reserves the right to make further contacts with the taxpayer to clarify his/her submission.

Under the Tax Department's new Voluntary Disclosure and Compliance program, eligible taxpayers who owe back taxes can avoid monetary penalties and possible criminal charges by:

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• telling the Department what taxes they owe;
• paying those taxes; **and**
• entering an agreement to pay all future taxes.

It's easy to apply. Just follow the prompts, answer a few questions, and submit your application electronically. Once we receive your application, we'll review it and contact you.

This program differs from our Voluntary Compliance Initiative (VCI). The VCI required taxpayers who engaged in abusive tax avoidance transactions to apply by February 2, 2009.

Voluntary Disclosure: Questions and Answers

July 31, 2009 — modified A6, A21 and A22
June 24, 2009 — modified A26 and added Q&A 31-51
May 6, 2009 — posted Q&A 1-30

Q1. Why did the IRS issue internal guidance regarding offshore activities now?

A1. The IRS has had a voluntary disclosure practice in its Criminal Manual for many years. Once IRS Criminal Investigation has determined preliminary acceptance into the voluntary disclosure program, the case is referred to the civil side of IRS for examination and resolution of taxes and penalties. Recent IRS enforcement efforts in the offshore area have led to an increased number of voluntary disclosures. Additional taxpayers are considering making voluntary disclosures but are reportedly reluctant to come forward because of uncertainty about the amount of their liability for potentially onerous civil penalties. In order to resolve these cases in an organized, coordinated manner and to make exposure to civil penalties more predictable, the IRS has decided to centralize the civil processing of offshore voluntary disclosures and to offer a uniform penalty structure for taxpayers who voluntarily come forward. These steps were taken to ensure that taxpayers are treated consistently and predictably.

Q2. What is the objective of these steps?

A2. The objective is to bring taxpayers that have used undisclosed foreign accounts and undisclosed foreign entities to avoid or evade tax into compliance with United States tax laws. Additionally, the information gathered from taxpayers making voluntary disclosures under this practice will be used to further the IRS's understanding of how foreign accounts and foreign entities are promoted to United States taxpayers as ways to avoid or evade tax. Data gathered will be used in developing additional strategies to inhibit promoters and facilitators from soliciting new clients.

Q3. Why should I make a voluntary disclosure?

A3. Taxpayers with undisclosed foreign accounts or entities should make a voluntary disclosure because it enables them to become compliant, avoid substantial civil penalties and generally eliminate the risk of criminal prosecution. Making a voluntary disclosure also provides the opportunity to calculate, with a reasonable degree of certainty, the total cost of resolving all offshore tax issues. Taxpayers who do not submit a voluntary disclosure run the risk of detection by the IRS and the imposition of substantial penalties, including the fraud penalty and foreign information return penalties, and an increased risk of criminal prosecution.

Q4. What is the IRS's Voluntary Disclosure Practice?

A4. The Voluntary Disclosure Practice is a longstanding practice of IRS Criminal Investigation of taking timely, accurate, and complete voluntary disclosures into account in deciding whether to recommend to the Department of Justice that a taxpayer be criminally prosecuted. It enables noncompliant taxpayers to resolve their tax liabilities and minimize their chances of criminal prosecution. When a taxpayer truthfully, timely, and completely complies with all provisions of the voluntary disclosure practice, the IRS will not recommend criminal prosecution to the Department of Justice.

Q5. How do I make a voluntary disclosure and where should I submit my voluntary disclosure?

A5. A voluntary disclosure is made by following the procedures described in I.R.M. 9.5.11.9. Tax professionals or individuals who want to initiate a voluntary disclosure, should call their local CI office. Taxpayers with questions may call

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the IRS Voluntary Disclosure Hotline at (215)516-4777, visit www.irs.gov, or contact their nearest CI office.

Q6. What form should my voluntary disclosure take?

A6. [Revised July 31, 2009] You may either contact the nearest Special Agent in Charge, IRS Criminal Investigation, stating that you wish to make a voluntary disclosure, or provide a letter outlining Information needed to assist the IRS in determining your acceptance into the voluntary disclosure program. You should also include a power of attorney (Form 2848), if you are represented by a third party, and daytime contact information for you or your representative. If you have already completed the amended or delinquent returns, those should be submitted with the letter, but it is not necessary to include them with the initial submission if you are unable to do so.

Q7. I'm currently under examination. Can I come in under voluntary disclosure?

A7. No. If the IRS has initiated a civil examination, regardless of whether it relates to undisclosed foreign accounts or undisclosed foreign entities, the taxpayer will not be eligible to come in under the IRS's Voluntary Disclosure Practice.

Q8. I have an offshore merchant account upon which I have not reported all of the income. Can I come in under the IRS's voluntary disclosure practice?

A8. Yes. Taxpayers with unreported income from an offshore merchant account can make a voluntary disclosure.

Q9. I have properly reported all my taxable income but I only recently learned that I should have been filing FBARs in prior years to report my personal foreign bank account or to report the fact that I have signature authority over bank accounts owned by my employer. May I come forward under the voluntary disclosure practice to correct this?

A9. The purpose for the voluntary disclosure practice is to provide a way for taxpayers who did not report taxable income in the past to voluntarily come forward and resolve their tax matters. Thus, If you reported and paid tax on all taxable income but did not file FBARs, do not use the voluntary disclosure process.

For taxpayers who reported and paid tax on all their taxable income for prior years but did not file FBARs, you should file the delinquent FBAR reports according to the instructions (send to Department of Treasury, Post Office Box 32621, Detroit, MI 48232-0621) and attach a statement explaining why the reports are filed late. Send copies of the delinquent FBARs, together with copies of tax returns for all relevant years, by September 23, 2009, to the Philadelphia Offshore Identification Unit at:

Internal Revenue Service 11501 Roosevelt Blvd. South Bldg., Room 2002 Philadelphia, PA 19154 Attn: Charlie Judge, Offshore Unit, DP S-611

The IRS will not impose a penalty for the failure to file the FBARs.

Q10. What if the taxpayer has already filed amended returns reporting the additional unreported income, without making a voluntary disclosure (i.e., quiet disclosure)?

A10. The IRS is aware that some taxpayers have attempted so-called “quiet” disclosures by filing amended returns and paying any related tax and interest for previously unreported offshore income without otherwise notifying the IRS. Taxpayers who have already made “quiet” disclosures may take advantage of the penalty framework applicable to voluntary disclosure requests regarding unreported offshore accounts and entities. Those taxpayers must send previously submitted documents, including copies of amended returns, to their local CI office by September 23, 2009. (See Q&A 5).

Taxpayers are strongly encouraged to come forward under the Voluntary Disclosure Practice to make timely, accurate, and complete disclosures. Those taxpayers making “quiet” disclosures should be aware of the risk of being examined and potentially criminally prosecuted for all applicable years.

The IRS has identified, and will continue to identify, amended tax returns reporting increases in income. The IRS will be closely reviewing these returns to determine whether enforcement action is appropriate.

Q11. Is a taxpayer who sought relief under the IRS's Voluntary Disclosure Practice before this internal guidance was issued, eligible for the terms described in this internal guidance?

A11. Yes. If a taxpayer sought relief under the IRS's Voluntary Disclosure Practice before this internal guidance was issued he or she may be eligible, as long as the voluntary disclosure has not yet resulted in an assessment.

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Q12. How does the penalty framework work? Can you give us an example?

A12. Assume the taxpayer has the following amounts in a foreign account over a period of six years. Although the amount on deposit may have been in the account for many years, it is assumed for purposes of the example that it is not unreported income in 2003.

Year	Amount on Deposit	Interest Income	Account Balance
2003	$1,000,000	$50,000	$1,050,000
2004		$50,000	$1,100,000
2005		$50,000	$1,150,000
2006		$50,000	$1,200,000
2007		$50,000	$1,250,000
2008		$50,000	$1,300,000

(NOTE: This example does not provide for compounded interest, and assumes the taxpayer is in the 35-percent tax bracket, files a return but does not include the foreign account or the interest income on the return, and the maximum applicable penalties are imposed.)

If the taxpayer comes forward and has their voluntary disclosure accepted by the IRS, they face this potential scenario:

They would pay $386,000 plus interest. This includes:

- Tax of $105,000 (six years at $17,500) plus interest,
- An accuracy-related penalty of $21,000 (i.e., $105,000 × 20%), and
- An additional penalty, in lieu of the FBAR and other potential penalties that may apply, of $260,000 (i.e., $1,300,000 × 20%).

If the taxpayer didn't come forward and the IRS discovered their offshore activities, they face up to $2,306,000 in tax, accuracy-related penalty, and FBAR penalty. The taxpayer would also be liable for interest and possibly additional penalties, and an examination could lead to criminal prosecution.

The civil liabilities potentially include:

- The tax and accuracy-related penalty, plus interest, as described above,
- FBAR penalties totaling up to $2,175,000 for willful failures to file complete and correct FBARs (2003- $100,000, 2004 - $100,000, 2005 - $100,000, 2006 - $600,000, 2007 - $625,000 and 2008 - $650,000).
- The potential of having the fraud penalty (75 percent) apply, and
- The potential of substantial additional information return penalties if the foreign account or assets is held through a foreign entity such as a trust or corporation and required information returns were not filed.

Note that if the foreign activity started more than six years ago, the Service may also have the right to examine additional years.

Q13. What years are included in the 6-year period?

A13. A taxpayer is expected to file correct delinquent or amended tax returns for tax year 2008 back to 2003.

Q14. What are some of the criminal charges I might face if I don't come in under voluntary disclosure and the IRS finds me?

Q14. Possible criminal charges related to tax returns include tax evasion (26 U.S.C. § 7201), filing a false return (26 U.S.C. § 7206 (1)) and failure to file an income tax return (26 U.S.C. § 7203). The failure to file an FBAR and the filing of a false FBAR are both violations that are subject to criminal penalties under 31 U.S.C. § 5322.

A person convicted of tax evasion is subject to a prison term of up to five years and a fine of up to $250,000. Filing a false return subjects a person to a prison term of up to three years and a fine of up to $250,000. A person who fails to file

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a tax return is subject to a prison term of up to one year and a fine of up to $100,000. Failing to file an FBAR subjects a person to a prison term of up to ten years and criminal penalties of up to $500,000.

Q15. What are some of the civil penalties that might apply if I don't come in under voluntary disclosure and the IRS finds me? How do they work?

A15. The following is a summary of potential reporting requirements and civil penalties that could apply to a taxpayer, depending on his or her particular facts and circumstances.

- A penalty for failing to file the Form TD F 90-22.1 (Report of Foreign Bank and Financial Accounts, commonly known as an "FBAR"). United States citizens, residents and certain other persons must annually report their direct or indirect financial interest in, or signature authority (or other authority that is comparable to signature authority) over, a financial account that is maintained with a financial institution located in a foreign country if, for any calendar year, the aggregate value of all foreign accounts exceeded $10,000 at any time during the year. Generally, the civil penalty for willfully failing to file an FBAR can be as high as the greater of $100,000 or 50 percent of the total balance of the foreign account. See 31 U.S.C. § 5321(a)(5). Nonwillful violations are subject to a civil penalty of not more than $10,000.
- A penalty for failing to file Form 3520, Annual Return to Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts. Taxpayers must also report various transactions involving foreign trusts, including creation of a foreign trust by a United States person, transfers of property from a United States person to a foreign trust and receipt of distributions from foreign trusts under section 6048. This return also reports the receipt of gifts from foreign entities under section 6039F. The penalty for failing to file each one of these information returns, or for filing an incomplete return, is 35 percent of the gross reportable amount, except for returns reporting gifts, where the penalty is five percent of the gift per month, up to a maximum penalty of 25 percent of the gift.
- A penalty for failing to file Form 3520-A, Information Return of Foreign Trust With a U.S. Owner. Taxpayers must also report ownership interests in foreign trusts, by United States persons with various interests in and powers over those trusts under section 6048(b). The penalty for failing to file each one of these information returns or for filing an incomplete return, is five percent of the gross value of trust assets determined to be owned by the United States person.
- A penalty for failing to file Form 5471, Information Return of U.S. Person with Respect to Certain Foreign Corporations. Certain United States persons who are officers, directors or shareholders in certain foreign corporations (including International Business Corporations) are required to report information under sections 6035, 6038 and 6046. The penalty for failing to file each one of these information returns is $10,000, with an additional $10,000 added for each month the failure continues beginning 90 days after the taxpayer is notified of the delinquency, up to a maximum of $50,000 per return.
- A penalty for failing to file Form 5472, Information Return of a 25% Foreign-Owned U.S. Corporation or a Foreign Corporation Engaged in a U.S. Trade or Business. Taxpayers may be required to report transactions between a 25 percent foreign-owned domestic corporation or a foreign corporation engaged in a trade or business in the United States and a related party as required by sections 6038A and 6038C. The penalty for failing to file each one of these information returns, or to keep certain records regarding reportable transactions, is $10,000, with an additional $10,000 added for each month the failure continues beginning 90 days after the taxpayer is notified of the delinquency, up to a maximum of $50,000 per return.
- A penalty for failing to file Form 926, Return by a U.S. Transferor of Property to a Foreign Corporation. Taxpayers are required to report transfers of property to foreign corporations and other information under section 6038B. The penalty for failing to file each one of these information returns is ten percent of the value of the property transferred, up to a maximum of $100,000 per return, with no limit if the failure to report the transfer was intentional.
- A penalty for failing to file Form 8865, Return of U.S. Persons With Respect to Certain Foreign Partnerships. United States persons with certain interests in foreign partnerships use this form to report interests in and transactions of the foreign partnerships, transfers of property to the foreign partnerships, and acquisitions, dispositions and changes

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in foreign partnership interests under sections 6038, 6038B, and 6046A. Penalties include $10,000 for failure to file each return, with an additional $10,000 added for each month the failure continues beginning 90 days after the taxpayer is notified of the delinquency, up to a maximum of $50,000 per return, and ten percent of the value of any transferred property that is not reported, subject to a $100,000 limit.

• Fraud penalties imposed under sections 6651(f) or 6663. Where an underpayment of tax, or a failure to file a tax return, is due to fraud, the taxpayer is liable for penalties that, although calculated differently, essentially amount to 75 percent of the unpaid tax.

• A penalty for failing to file a tax return imposed under section 6651(a)(1). Generally, taxpayers are required to file income tax returns. If a taxpayer fails to do so, a penalty of 5 percent of the balance due, plus an additional 5 percent for each month or fraction thereof during which the failure continues may be imposed. The penalty shall not exceed 25 percent.

• A penalty for failing to pay the amount of tax shown on the return under section 6651(a)(2). If a taxpayer fails to pay the amount of tax shown on the return, he or she may be liable for a penalty of .5 percent of the amount of tax shown on the return, plus an additional .5 percent for each additional month or fraction thereof that the amount remains unpaid, not exceeding 25 percent.

• An accuracy-related penalty on underpayments imposed under section 6662. Depending upon which component of the accuracy-related penalty is applicable, a taxpayer may be liable for a 20 percent or 40 percent penalty.

Q16. Why did the IRS pick 6 months?

A16. The March 23, 2009 memorandum communicating the approved penalty framework for resolving the civil side of offshore voluntary disclosures is effective for 6 months because the Service intends to re-evaluate the framework at that time. Six months is a reasonable time to close out a number of voluntary disclosures, evaluate our experience and the feedback from the practitioner community, and decide whether or how to continue the practice going forward.

Q17. What happens at the end of 6 months? Will I get a better deal if I wait to see what the IRS does at the end of 6 months?

A17. Taxpayers should not wait until the end of the 6-month period to make their voluntary disclosures as there is no guarantee that the taxpayer will still be eligible or that the current penalty terms will be available after 6 months.

Taxpayers who wait until the end of the 6-month period run the risk that they will be disqualified from the Voluntary Disclosure Practice. The IRS has stepped up its enforcement efforts, including the use of John Doe summonses, to identify taxpayers using offshore accounts and entities to avoid tax. In addition, the IRS continues to receive information from whistleblowers and other taxpayers making voluntary disclosures. If the IRS receives specific information about a taxpayer's noncompliance before the taxpayer attempts to make a voluntary disclosure, the disclosure will not be timely and the taxpayer will not be eligible for the criminal and civil penalty relief available under the voluntary disclosure practice. Finally, taxpayers run a substantial risk that the uniform penalty structure described in the internal guidance will not be available past the 6-month deadline or that the terms will be less beneficial to taxpayers.

Q18. What should I do if I am having difficulty obtaining my records from overseas?

A18. Our experience with offshore cases in recent years is that taxpayers are successful in retrieving copies of statements and other records from foreign banks when they genuinely attempt to do so. If assistance is needed, the agent assigned to a case will work with the taxpayer in preparing a request that should be acceptable to the foreign bank. The penalty framework described in the March 23 memorandum will apply to all voluntary disclosures in process within the 6-month timeframe, so difficulty in completing a voluntary disclosure started during that period will not disqualify a cooperative taxpayer from the penalty relief. The key is to notify the Service of your intent to make a voluntary disclosure as soon as possible, and in any event, by Sept. 23, 2009.

Q19. Are entities, such as corporations, partnerships and trusts eligible to make voluntary disclosures?

A19. Yes, entities are eligible to participate in the IRS's Voluntary Disclosure Practice.

Q20. Does the twenty percent penalty apply to entities? Does the twenty percent penalty apply only to cash and

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securities held in foreign accounts or entities or to tangible and intangible assets as well?

A20. The twenty percent penalty applies to entities. The twenty percent penalty applies to all assets (or at least the taxpayer's share) held by foreign entities (e.g., trusts and corporations) for which the taxpayer was required to file information returns, as well as all foreign assets (e.g., financial accounts, tangible assets such as real estate or art, and intangible assets such as patents or stock or other interests in a U.S. business) held or controlled by the taxpayer.

Q21. Are taxpayers required to complete a questionnaire as part of the voluntary disclosure practice?

A21. [Revised July 31, 2009] There is no specific questionnaire for taxpayers to complete. However, taxpayers may submit their offshore voluntary disclosure using an optional format letter (as referenced in Question 6)

Q22. Is there a list of questions taxpayers are expected to answer as part of the voluntary disclosure process?

A22. [Revised July 31, 2009] There is no standard list of questions for these cases. The Service may require an interview with the taxpayer making a voluntary disclosure, depending on the facts of each case. However, see the response to FAQ 21 for the link to an optional format letter.

Q23. When determining the highest amount in each undisclosed foreign account for each year or the highest asset balance of all undisclosed foreign entities for each year, what exchange rate should be used?

A23. Convert foreign currency by using the foreign currency exchange rate at the end of the year. In valuing currency of a country that uses multiple exchange rates, use the rate that would apply if the currency in the account were converted into United States dollars at the close of the calendar year. Each account is to be valued separately.

Q24. Will I have to file or amend my old tax returns?

A24. Yes. Any tax return not filed during the previous 6-year period that was otherwise required to be filed by law, must be filed by the taxpayer. In addition, any inaccurate returns for any of the 6 years must be amended by the taxpayer.

Q25. Besides federal income tax returns, what forms or other returns must be filed?

A25. The following forms must be filed:

- Copies of original and amended federal income tax returns for tax periods covered by the voluntary disclosure;
- Complete and accurate amended federal income tax returns (or original returns, if not previously filed) of the taxpayer for all tax years covered by the voluntary disclosure;
- An explanation of previously unreported or underreported income or incorrectly claimed deductions or credits related to undisclosed foreign accounts or undisclosed foreign entities, including the reason(s) for the error or omission;
- If the taxpayer is a decedent's estate, or is an individual who participated in the failure to report the foreign account or foreign entity in a required gift or estate tax return, either as executor or advisor, complete and accurate amended estate or gift tax returns (original returns, if not previously filed) necessary to correct the underreporting of assets held in or transferred through undisclosed foreign accounts or foreign entities;
- Complete and accurate amended information returns required to be filed by the taxpayer, including, but not limited to, Forms 3520, 3520-A, 5471, 5472, 926 and 8865 (or originals, if not previously filed) for all tax years covered by the voluntary disclosure, for which the taxpayer requests relief; and
- Complete and accurate Form TD F 90.22-1, Report of Foreign Bank and Financial Accounts, for foreign accounts maintained during calendar years covered by the voluntary disclosure.

Q26. If I had an FBAR reporting obligation for years covered by the voluntary disclosure, what version of the Form TD F 90-22.1 should I use to report my interests in foreign accounts?

A. **[Revised June 24, 2009]** Taxpayers should use the current version of Form TD F 90-22.1, (revised in October 2008), to file delinquent FBARs to report foreign accounts maintained in prior years. The taxpayer may, however, rely on the instructions for the prior version of the form (revised in July 2000) for purposes of determining who must file to report foreign accounts maintained in 2008 and prior calendar years.

Although the FBAR was revised in October 2008, IRS News Release IR-2009-58 (June 5, 2009) and IRS Announcement 2009-51 permit the use of the definition of "United States person" in the prior version of the FBAR in determining who must file FBARs that are due on June 30, 2009. Accordingly, for all FBARs that are due in the current and prior

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years, the term “United States person” means (1) a citizen or resident of the United States; (2) a domestic partnership; (3) a domestic corporation; or (4) a domestic estate or trust.

Q27. If I don't have the ability to full pay can I still participate in the IRS's Voluntary Disclosure Practice?

A27. Yes. The March 23, 2009 guidance requires the taxpayer to fully pay all taxes and interest for all years covered, and the Voluntary Disclosure penalty, as well as all other unpaid, previously assessed liabilities, when the signed closing agreement is returned to the Service. However, it is possible for a taxpayer who is unable to make full payment at that time to submit a request that includes other payment arrangements acceptable to the IRS.

The burden will be on the taxpayer to establish inability to pay, to the satisfaction of the IRS, based on full disclosure of all assets and income sources, domestic and offshore, under the taxpayer's control. Assuming that the IRS determines that the inability to fully pay is genuine, the taxpayer must work out other financial arrangements, acceptable to the IRS, to resolve all outstanding liabilities, in order to be entitled to the penalty relief set forth in the March 23, 2009 guidance.

Q28. If the taxpayer and the IRS cannot agree to the terms of the closing agreement, will mediation with Appeals be an option with respect to the terms of the closing agreement?

A28. No. The penalty framework and the agreement to limit tax exposure to the most recent 6 years are package terms. If any part of the penalty framework is unacceptable to the taxpayer, the case will be examined and all applicable penalties may be imposed. Any tax and penalties imposed by the Service on examination may be appealed, but not the Service's decision on the terms of the closing agreement applying the penalty framework.

Q29. I have a client who may be eligible to make a voluntary disclosure. What are my responsibilities to my client under Circular 230?

A29. The IRS expects taxpayers to seek qualified legal advice and representation in connection with considering and making a voluntary disclosure. If a taxpayer seeks the advice of a tax practitioner but nonetheless decides not to make a voluntary disclosure despite the taxpayer's noncompliance with Untied States tax laws, Circular 230, section 10.21, requires the practitioner to advise the client of the fact of the client's noncompliance and the consequences of the client's noncompliance as provided under the Code and regulations.

Q30. Can I talk to the IRS without revealing my client's identity?

A30. Hypothetical situations present a potential for misunderstanding that exists when there is no assurance that the hypothetical contains all relevant facts. In addition, tax practitioners should be aware that posing a situation as a hypothetical does not satisfy the requirements of making a voluntary disclosure. If the IRS receives information relating specifically to the taxpayer's undisclosed foreign accounts or undisclosed foreign entities while the hypothetical question is pending, the taxpayer may become ineligible to make a voluntary disclosure.

If practitioners have questions about the terms of the voluntary disclosure program, they should contact the IRS Voluntary Disclosure Hotline at (215) 516-4777, visit www.irs.gov, or contact their nearest CI office with questions.

Questions and answers 31 through 51 were added June 24, 2009.

Q31. How can the IRS propose adjustments to tax for a six-year period without either an agreement from the taxpayer or a statutory exception to the normal three-year statute of limitations for making those adjustments?

A31. Going back six years is part of the resolution offered by the IRS for resolving offshore voluntary disclosures. The taxpayer must agree to assessment of the liabilities for those years in order to get the benefit of the reduced penalty framework. If the taxpayer does not agree to the tax, interest and penalty proposed by the voluntary disclosure examiner, the case will be referred to the field for a complete examination. In that examination, normal statute of limitations rules will apply. If no exception to the normal three-year statute applies, the IRS will only be able to assess tax, penalty and interest for three years. However, if the period of limitations was open because, for example, the IRS can prove a substantial omission of gross income, six years of liability may be assessed. Similarly, if there was a failure to file certain information returns, such as Form 3520 or Form 5471, the statute of limitations will not have begun to run. If the IRS can prove fraud, there is no statute of limitations for assessing tax.

Q32. If a taxpayer's violation includes unreported individual foreign accounts and business accounts (for an act-

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ive business), does the 20 percent offshore penalty include the business accounts?

A32. Yes. Assuming that there is unreported income with respect to all the accounts, they all will be included in the penalty base. No distinction is to be drawn based on whether the account is a business account or a savings or investment account.

Q33. If the lookback period is 2003-2008, what does the taxpayer do if the taxpayer held foreign real estate, sold it in 2002, and did not report the gain on his 2002 return? Does the taxpayer compute the 20 percent on the highest aggregate balance in 2003-2008? What, if anything, does IRS expect the taxpayer to do with respect to 2002?

A33. Gain realized on a foreign transaction occurring before 2003 does not need to be included as part of the voluntary disclosure. If the proceeds of the transaction were repatriated and were not offshore after January 1, 2003, they will not be included in the base for the 20 percent offshore penalty. On the other hand, if the proceeds remained offshore after January 1, 2003, and the income in the account was not reported, they will be included in the base for the penalty.

Q34. If, after making a voluntary disclosure, a taxpayer disagrees with the 20 percent offshore penalty, what can the taxpayer do?

A34. If any part of the penalty structure is unacceptable to a taxpayer, that case will follow the standard audit process. All relevant years and issues will be subject to a complete examination. At the conclusion of the examination, all applicable penalties (including information return and FBAR penalties) will be imposed. Those penalties could be substantially greater than the 20 percent penalty. If the case is unagreed, the taxpayer will have recourse to Appeals.

Q35. Will examiners have any discretion to settle cases? For example, if a penalty for failing to file a Form 5471 for 6 years is $10,000 per year, will that be compared to 20 percent of the corporation's asset value? Would the lesser amount apply?

A35. Voluntary disclosure examiners do not have discretion to settle cases for amounts less than what is property due and owing. These examiners will compare the 20 percent offshore penalty to the total penalties that would otherwise apply to a particular taxpayer. Under no circumstances will a taxpayer be required to pay a penalty greater than what he would otherwise be liable for under existing statutes. If the taxpayer disagrees with the IRS's determination, as set forth in the closing agreement, the taxpayer may request that the case be referred for a standard examination of all relevant years and issues. At the conclusion of this examination, all applicable penalties, including information return penalties and FBAR penalties, will be imposed. If, after the standard examination is concluded the case is closed unagreed, the taxpayer will have recourse to Appeals. See Q&A 34.

Q36. Re: Q&A 12 Does interest run on any of the penalties? If so, which ones and from what date does interest accrue?

A36. With regard to the accuracy-related and delinquency penalties, interest runs from the due date of the return in question. With regard to all other penalties, interest runs from the date of assessment of the penalty.

Q37. Re: Q&A 20 A taxpayer owns valuable land and artwork located in a foreign jurisdiction. This property produces no income and there were no reporting requirements regarding this property. Must the taxpayer report the land and artwork and pay a 20 percent penalty?

A37. Q&A 20 relates to income producing property for which no income was reported. Under those circumstances, no distinction is made between assets held directly and assets held through an entity in computing the 20 percent offshore penalty. However, if the taxpayer owns nonincome producing property in the taxpayer's own name, there has been no U.S. taxable event and no reporting obligation to disclose. The taxpayer will be required to report any current income from the property or gain from its sale or other disposition at such time in the future as the income is realized. Because there has as yet been no tax noncompliance, the 20 percent offshore penalty would not apply to those assets. If the foreign assets were held in the name of an entity such as a trust or corporation, there would have been an information return filing obligation that may need to be disclosed. See Q&A 42.

Q38. If a taxpayer transferred funds from one unreported foreign account to another between 2003 and 2008,

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will he have to pay a 20 percent offshore penalty on both accounts?

A38. No. If the taxpayer can establish that funds were transferred from one account to another, any duplication will be removed before calculating the 20 percent penalty. However, the burden will be on the taxpayer to establish the extent of the duplication.

Q39. How is the 20 percent offshore penalty computed if the taxpayer has multiple accounts or entities where the highest value of some accounts is not in the same year? Are separate penalties determined at the rate of 20 percent for each account or entity value?

A39. The values of accounts and other assets are aggregated for each year and the penalty is calculated at 20 percent of the highest year's aggregate value.

Q40. A taxpayer has two offshore accounts. No FBARs were filed. The taxpayer reported all income from one account but not the other. Mechanically, how does the taxpayer report this? Does the taxpayer report both accounts as a voluntary disclosure or bifurcate it into a delinquent FBAR filing for the reported account and a voluntary disclosure for the unreported account?

A40. Because the annual FBAR requirement is to file a single report reporting all foreign accounts meeting the reporting requirement, it is not possible to bifurcate the corrected filing. The taxpayer should make a voluntary disclosure for the omitted income and include the delinquent FBARs with respect to both accounts. The account with no income tax issue is unrelated to the taxpayer's tax noncompliance, so no penalty will be imposed with respect to that account. See Q&A 9.

Q41. If, in addition to other noncompliance, a taxpayer has failed to file an FBAR to report an account over which the taxpayer has signature authority but no beneficial interest (e.g., an account owned by his employer), will that foreign account be included in the base for calculating the taxpayer's 20 percent offshore penalty?

A41. No. The account on which the taxpayer has mere signature authority will be treated as unrelated to the tax noncompliance the taxpayer is voluntarily disclosing. The taxpayer may cure the FBAR delinquency for the account the taxpayer does not own by filing the FBAR with an explanatory statement by September 23, 2009. See Q&A 9. The answer might be different (1) if the account over which the taxpayer has signature authority is held in the name of a related person, such as a family member or a corporation controlled by the taxpayer; (2) if the account is held in the name of a foreign corporation or trust for which the taxpayer had a Title 26 reporting obligation; or (3) if the account was related in some other way to the taxpayer's tax noncompliance. In these cases, the taxpayer will be liable for the 20 percent offshore penalty if there is unreported income on the account. On the other hand, if there is no unreported income with respect to the account, no penalty will be imposed under the rationale of Q&A 40.

Q42. Q&A 9 states that a taxpayer who only failed to file an FBAR should not use this process. What about a taxpayer who only has delinquent Form 5471s or Form 3520s but no tax due? Does that taxpayer fall outside this voluntary disclosure process?

A42. A taxpayer who has failed to file tax information returns, such as Form 5471 for controlled foreign corporations (CFCs) or Form 3520 for foreign trusts but who has reported and paid tax on all their taxable income with respect to all transactions related to the CFCs or foreign trusts, should file delinquent information returns with the appropriate service center according to the instructions for the form and attach a statement explaining why the information returns are filed late. (The Form 5471 should be submitted with an amended return showing no change to income or tax liability.) Send copies of the delinquent information returns, together with copies of tax returns for all relevant years, by September 23, 2009, to the Philadelphia Offshore Identification Unit at:

> Internal Revenue Service 11501 Roosevelt Blvd. South Bldg., Room 2002 Philadelphia, PA 19154 Attn: Charlie Judge, Offshore Unit, DP S-611

The IRS will not impose a penalty for the failure to file the information returns.

Q43. Re: Q&A 9 A taxpayer recently learned that they have an FBAR filing obligation but they do not have sufficient time to gather the information necessary to property file the FBAR by the June 30, 2009 due date. How

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should the taxpayer proceed?

A43. Taxpayers who reported and paid tax on all their 2008 taxable income but only recently learned of their FBAR filing obligation and have insufficient time to gather the necessary information to complete the FBAR, should file the delinquent FBAR report according to the instructions (send to Department of Treasury, Post Office Box 32621, Detroit, MI 48232-0621) and attach a statement explaining why the report is filed late. Send a copy of the delinquent FBAR, together with a copy of the 2008 tax return, by September 23, 2009, to the Philadelphia Offshore Identification Unit at the address in Q&A 9.

In this situation, the IRS will not impose a penalty for the failure to file the FBAR.

Additionally, if all 2008 taxable income with respect to a foreign financial account is timely reported and a United States person only recently learned they have a 2008 FBAR obligation and there is insufficient time to gather the necessary information to complete the FBAR, the United States person may follow the procedures set forth above and no penalty will be imposed.

For 2008 tax returns due after September 23, 2009, the tax return does not need to accompany the 2008 FBAR.

Q44. Re: Q&A 12 The due date for the 2008 FBAR is June 30, 2009. Should a taxpayer file a 2008 FBAR in the normal manner or should a taxpayer submit it with the voluntary disclosure request?

A44. Except as described in Q&A 43, the taxpayer should timely file the 2008 FBAR in the normal manner by the June 30, 2009 deadline and submit an additional copy with the taxpayer's voluntary disclosure.

Q45. If a taxpayer is uncertain about whether he is required to file an FBAR with respect to a particular foreign account, how can the taxpayer get help with this question?

A45. Help with questions about FBAR filing requirements is available on the FBAR Hotline at 1-800-800-2877. When the call is answered, select option 2. You can also submit written questions about the FBAR rules by e-mail addressed to FBARQuestions@irs.gov. The instructions to the FBAR form are available at www.irs.gov. Do not call the Voluntary Disclosure Hotline with questions about whether you have an FBAR filing requirement. The purpose of the Voluntary Disclosure Hotline is to answer questions about how to make voluntary disclosures and what penalties apply, assuming a taxpayer was required to file.

Q46. A taxpayer moved to the U.S. in 2007 and is now a permanent resident of the U.S. The taxpayer had a requirement to file an FBAR for one year but failed to do so. Is the taxpayer subject to a penalty equal to 20 percent of the account?

A46. First, the taxpayer should confirm that the taxpayer had an FBAR filing requirement. Assuming that the taxpayer was required to report the interest earned on the account during the year the taxpayer was in the U.S. and failed to do so, the taxpayer is subject to a penalty based on the high account balance during the year. The penalty may be limited to five percent if the taxpayer did not avoid U.S. tax with respect to the deposits and if the account was passively held during the year the taxpayer was in the U.S. if there was no unreported taxable income related to the unreported foreign accounts that would have been reported on the FBAR, the taxpayer will not be subject to the 20 percent offshore penalty. In that case, the taxpayer should file delinquent FBARs attaching a statement explaining why the FBAR was not timely filed. For more information, see Q&A 9.

Q47. If parents have a jointly owned foreign account on which they have made their children signatories, the children have an FBAR filing requirement but no income. Should the children just file delinquent FBARs as described by Q&A 9 and have the parents submit a voluntary disclosure? Will both parents be penalized 20 percent each? Will each have a 20 percent penalty on 50 percent of the balance?

A47. Only one 20 percent offshore penalty will be applied with respect to voluntary disclosures relating to the same account. In the example, the parents will be jointly required to pay a single 20 percent penalty on the account. This can be through one parent paying the total penalty or through each paying a portion, at the taxpayers' option. For those signatories with no ownership interest in the account, such as the children in these facts, they may file delinquent FBARs with no penalty as described in Q&As 9 and 41. However, any joint account owner who does not make a voluntary dis-

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closure may be examined and subject to all appropriate penalties.

Q48. If there are multiple individuals with signature authority over a trust account, does everyone involved need to file delinquent FBARs? If so, could everyone be subject to a 20 percent offshore penalty?

A48. Only one 20 percent offshore penalty will be applied with respect to voluntary disclosures relating to the same account. The penalty may be allocated among the taxpayers making the disclosures in any way they choose. The reporting requirements for filing an FBAR, however, do not change. Therefore, every individual who is required to file an FBAR must file one.

Q49. Re: Q&A 10 Some taxpayers have made quiet disclosures by filing amended returns. Will the IRS audit these taxpayers? If so, will they be eligible for the 20 percent offshore penalty? Is the IRS really going to prosecute someone who filed an amended return and correctly reported all their income?

A49. The IRS is reviewing amended returns and could select any amended return for examination. If a return is selected for examination, the 20 percent offshore penalty would not be available. When criminal behavior is evident and the disclosure does not meet the requirements of a voluntary disclosure under IRM 9.5.11.9, the IRS may recommend criminal prosecution to the Department of Justice. Taxpayers who have already made quiet disclosures but have not yet been selected for examination may take advantage of the penalty framework applicable to voluntary disclosure requests regarding unreported offshore accounts and entities, provided they otherwise meet the criteria for voluntary disclosure set forth in IRM 9.5.11.9. Those taxpayers must send previously submitted documents, including copies of amended returns, to their local CI office by September 23, 2009. See Q&As 4 and 10 for more information.

Q50. What is the distinction between filing amended returns to correct errors and filing a voluntary disclosure?

A50. An amended return is the proper vehicle to correct an error on a filed return, whether a taxpayer receives a refund or owes additional tax. A voluntary disclosure is a truthful, timely and complete communication to the IRS in which a taxpayer shows a willingness to cooperate (and does in fact cooperate) with the IRS in determining the taxpayer's correct tax liability and makes arrangements in good faith to fully pay that liability. Filing correct amended returns is normally a part of the process of making a voluntary disclosure under IRM 9.5.11.9.

Taxpayers and practitioners trying to decide whether to simply file an amended return with a Service Center or to make a formal voluntary disclosure under the process described in IRM 9.5.11.9 and the March 23, 2009 memoranda should consider the nature of the error they are trying to correct. Taxpayers with undisclosed foreign accounts or entities should consider making a voluntary disclosure because it enables them to become compliant, avoid substantial civil penalties and generally eliminate the risk of criminal prosecution. Making a voluntary disclosure also provides the opportunity to calculate, with a reasonable degree of certainty, the total cost of resolving all offshore tax issues. It is anticipated that the voluntary disclosure process is appropriate for most taxpayers who have underreported their income with respect to offshore accounts and assets. However, there will be some cases, such as where a taxpayer has reported all income but failed to file the FBAR (Q&A 9), or only failed to file Information returns (Q&A 42), where it remains appropriate for the taxpayer to simply file amended returns with the applicable Service Center (with copies to the Philadelphia office listed in Q&A 9).

Q51. If the Service has served a John Doe summons seeking information that may identify a taxpayer as holding an undisclosed foreign account or undisclosed foreign entity, does that make the taxpayer ineligible to make a voluntary disclosure in accordance with the March 23, 2009 guidance?

A51. No. The mere fact that the Service served a John Doe summons does not make every member of the John Doe class ineligible to participate. However, once the Service obtains information under a John Doe summons that provides evidence of a specific taxpayer's noncompliance with the tax laws, that particular taxpayer may become ineligible. For this reason, a taxpayer concerned that a party served with a John Doe summons will provide information about them to the Service should apply to make a voluntary disclosure as soon as possible.

Part I Filer Information

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TABLE

TABULAR OR GRAPHIC MATERIAL SET FORTH AT THIS POINT IS NOT DISPLAYABLE

Part II Information on Financial Account(s) Owned Separately

TABLE

TABULAR OR GRAPHIC MATERIAL SET FORTH AT THIS POINT IS NOT DISPLAYABLEFile this form with: U.S. Department of the Treasury, P.O. Box 32621, Detroit, MI 48232-0621

This form should be used to report a financial interest in, signature authority, or other authority over one or more financial accounts in foreign countries, as required by the Department of the Treasury Regulations (31 CFR 103). No report is required if the aggregate value of the accounts did not exceed $10,000. **See Instructions For Definitions.**

PRIVACY ACT AND PAPERWORK REDUCTION ACT NOTICE

Pursuant to the requirements of Public Law 93-579 (Privacy Act of 1974), notice is hereby given that the authority to collect information on TD F 90-22.1 in accordance with 5 USC 552a (e) is Public Law 91-508; 31 USC 5314; 5 USC 301 ; 31 CFR 103.

The principal purpose for collecting the information is to assure maintenance of reports where such reports or records have a high degree of usefulness in criminal, tax, or regulatory investigations or proceedings. The information collected may be provided to those officers and employees of any constituent unit of the Department of the Treasury who have a need for the records in the performance of their duties. The records may be referred to any other department or agency of the United States upon the request of the head of such department or agency for use in a criminal, tax, or regulatory investigation or proceeding. The information collected may also be provided to appropriate state, local, and foreign law enforcement and regulatory personnel in the performance of their official duties. Disclosure of this information is mandatory. Civil and criminal penalties, including in certain 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. Disclosure of the Social Security number is mandatory. The authority to collect is 31 CFR 103. The Social Security number will be used as a means to identify the individual who files the report.

The estimated average burden associated with this collection of information is 20 minutes per respondent or record keeper, depending on individual circumstances. Comments regarding the accuracy of this burden estimate, and suggestions for reducing the burden should be directed to the Internal Revenue Service, Bank Secrecy Act Policy, 5000 Ellin Road C-3-242, Lanham MD 20706.

Part II *Continued*—Information on Financial Account(s) Owned Separately

Complete a Separate Block for Each Account Owned Separately

This side can be copied as many times as necessary in order to provide information on all accounts.

TABLE

TABULAR OR GRAPHIC MATERIAL SET FORTH AT THIS POINT IS NOT DISPLAYABLE

Part III Information on Financial Account(s) Owned Jointly

Complete a Separate Block for Each Account Owned Jointly

This side can be copied as many times as necessary in order to provide information on all accounts.

TABLE

TABULAR OR GRAPHIC MATERIAL SET FORTH AT THIS POINT IS NOT DISPLAYABLE

Part IV Information on Financial Account(s) Where Filer has Signature or Other Authority but No Financial In-

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terest in the Account(s)

Complete a Separate Block for Each Account

This side can be copied as many times as necessary in order to provide information on all accounts.

TABLE

TABULAR OR GRAPHIC MATERIAL SET FORTH AT THIS POINT IS NOT DISPLAYABLE

Part V Information on Financial Account(s) Where Corporate Filer Is Filing a Consolidated Report

Complete a Separate Block for Each Account

This side can be copied as many times as necessary in order to provide information on all accounts.

TABLE

TABULAR OR GRAPHIC MATERIAL SET FORTH AT THIS POINT IS NOT DISPLAYABLE

General Instructions

Who Must File this Report. Each 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, must report that relationship each calendar year by filing this report with the Department of the Treasury on or before June 30, of the succeeding year.

Exceptions

An officer or employee of a bank which is currently examined by Federal bank supervisory agencies for soundness and safety need not report that he has signature or other authority over a foreign bank, securities or other financial account maintained by the bank, if the officer or employee has NO personal financial interest in the account.

An officer or employee of a domestic corporation whose equity securities are listed upon any United States national securities exchange or which has assets exceeding $10 million and has 500 or more shareholders of record need not file such a report concerning signature or other authority over a foreign financial account of the corporation, if he has NO personal financial interest in the account and he has been advised in writing by the chief financial officer or similar responsible officer of the corporation that the corporation has filed a current report, which includes that account. An officer or employee of a domestic subsidiary of such a domestic corporation need not file this report concerning signature or other authority over the foreign financial account if the domestic parent meets the above requirements, he has no personal financial interest in the account, and he has been advised in writing by the responsible officer of the parent that the subsidiary has filed a current report which includes that account. If a United States subsidiary is named in a consolidated FBAR of the parent, the subsidiary will be deemed to have filed a report for purposes of this exception. An officer or employee of a foreign subsidiary more than 50% owned by such a domestic corporation need not file this report concerning signature or other authority over the foreign financial account if the employee or officer has no personal financial interest in the account, and he has been advised in writing by the responsible officer of the parent that the parent has filed a current report which includes that account.

General Definitions

United States Person. The term “United States person” means a citizen or resident of the United States, or a person in and doing business in the United States. See 31 C.F.R. 103.11(z) for a complete definition of “person.” The United States includes the states, territories and possessions of the United States. See the definition of United States at 31 C.F.R.

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103.11(nn) for a complete definition of United States. A foreign subsidiary of a United States person is not required to file this report, although its United States parent corporation may be required to do so. A branch of a foreign entity that is doing business in the United States is required to file this report even if not separately incorporated under U.S. law.

Financial Account. This term includes any bank, securities, securities derivatives or other financial instruments accounts. Such accounts generally also encompass any accounts in which the assets are held in a commingled fund, and the account owner holds an equity interest in the fund (including mutual funds). The term also means any savings, demand, checking, deposit, time deposit, or any other account (including debit card and prepaid credit card accounts) maintained with a financial institution or other person engaged in the business of a financial institution. Individual bonds, notes, or stock certificates held by the filer are not a financial account nor is an unsecured loan to a foreign trade or business that is not a financial institution.

Account in a Foreign Country. A "foreign country" includes all geographical areas located outside the United States. See "United States Person" above 31 C.F.R. 103.11(nn) for a definition of United States. The geographical location of the account, not the nationality of the financial entity institution in which the account is found determines whether it is in an account in a foreign country. Report any financial account (except a military banking facility) that is located in a foreign country, even if it is held at an affiliate of a United States bank or other financial institution. Do not report any account maintained with a branch, agency, or other office of a foreign bank of other institution that is located in the United States.

Military Banking Facility. Do not consider as an account in a foreign country, an account in an institution known as a "United States military banking facility" (or "United States military finance facility") operated by a United States financial institution designated by the United States Government to serve U.S. Government installations abroad, even if the United States military banking facility is located in a foreign Country, is not an account in a foreign country.

Financial Interest. A financial interest in a bank, securities, or other financial account in a foreign country means an interest described in one of the following three paragraphs:

1. 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.

2. A United States person has a 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) a person acting as an agent, nominee, attorney, or in some other capacity on behalf of the U.S. person; (b) a corporation in which the United States person owns directly or indirectly more than 50 percent of the total value of shares of stock or more than 50 percent of the voting power for all shares of stock; (c) a partnership in which the United States person owns an interest in more than 50 percent of the profits (distributive share of income, taking into account any special allocation agreement) or more than 50 percent of the capital of the partnership; or (d) a trust in which the United States person either has a present beneficial interest, either directly or indirectly, in more than 50 percent of the assets or from which such person receives more than 50 percent of the current income.

3. A United States person has a 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 trust, or a person acting on behalf of a trust, that was established by such United States person and for which a trust protector has been appointed. 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.

Correspondent or "nostro" accounts (international interbank transfer accounts) maintained by banks that are used solely for the purpose of bank-to-bank settlement need not be reported on this form, but are subject to other Bank Secrecy Act filing requirements. This exception is intended to encompass those accounts utilized for bank-to-bank settlement purposes only.

Signature or Other Authority Over an Account. A person has signature authority over an account if such person can

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control the disposition of money or other property in it by delivery of a document containing his or her signature (or his or her signature and that of one or more other persons) to the bank or other person with whom the account is maintained. Other authority exists in a person who can exercise comparable power over an account by communication with the bank or other person with whom the account is maintained, either directly or through an agent, nominee, attorney, or in some other capacity on behalf of the U.S. person, either orally or by some other means.

Filing Information—Do NOT file with your Federal Income Tax Return

When and where to file. This report must be filed on or before June 30 of the year following the calendar year reported. The report is required annually. File by mailing this report to the Department of the Treasury, Post Office Box 32621, Detroit, MI 48232-0621, or by hand-carrying it to any local office of the Internal Revenue Service for forwarding to the Department of the Treasury, Detroit, MI. Tax attaches are located in the U.S. embassies in some countries. A filer can receive instructions for verifying that a report has been filed by calling the Detroit Computing Center Hotline at 1-800-800-2877.

Extensions of time to file federal tax returns do not extend the time for filing this report. **There is no extension of time available for filing this report.** If a delinquent FBAR is filed, also attach a statement explaining the reason for the late filing. See “When and where to file” (above) for filing instructions.

An amendment of a previously filed FBAR is accomplished by checking the “Amended” box in the upper right hand corner of the first page of the form, making the needed additions or corrections, and then stapling it to a copy of the original form. Please also attach a statement explaining the changes. See “When and where to file” (above) for filing instructions.

Record Keeping Requirements. If this Report is required, certain records must be retained. Such records must contain the name in which each such account is maintained, the number or other designation of such account, the name and address of the foreign bank or other person with whom such account is maintained, the type of such account, and the maximum value of each account during the reporting period. Retaining filed copies of this report will help to meet these requirements. The records must be retained for a period of five years and must kept at all times available for inspection as provided by law.

Explanations for Specific Items

Part I

Item 1. The Report of Foreign Bank and Financial Accounts (FBAR) is an annual report. Enter the calendar year being reported.

Amendment of a previously filed FBAR is accomplished by checking the “Amended” box in the upper right hand corner of the first page of the form, making the needed additons and corrections, and then stapling it to a copy of the original report. See “When and where to file” (above) for filing instructions.

Item 2. Check the appropriate box describing the filer. A corporation which owns directly or indirectly more than a 50 percent interest in one or more other entities required to file this Report will be permitted to file a consolidated report on TD F 90-22.1, on behalf of itself and such other entities.

Check box “d” in Item 2 and complete Part V. Consolidated reports should be signed by an authorized official of the parent corporation. Trusts and other entities, including tax-exempt organizations, should check box “e” and describe the filer on the line following box “e.”

Item 3. A filer should provide the filer's taxpayer identification number. Generally this is the filer's U.S. social security number (SSN) or employer identification number (EIN). Numbers should be entered with no spaces, dashes, or other punctuation throughout this report. If the filer does not possess such U.S. identification, the filer should complete Item 4.

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Item 4. Complete Item 4 only if the filer has no U.S. taxpayer identification number. Item 4 requires the filer to provide the information about an official foreign government document evidencing the filer's nationality or residence. The filer should write in the document number followed by the country of issuance. The filer may check off the type of document. If “other”' is checked, the filer should write in the type of document. For example, an individual who is not a U.S. citizen would provide a passport number, the name of the country of issuance, and check off “passport.”

Item 5. Enter the date of birth of the filer using the month, day, and year convention.

Items 6, 7 and 8. Enter the name of the filer. An organization should enter its name in the Last Name space.

Items 9, 10, 11, 12 and 13. Enter the address of the filer. An individual filer residing in the United States should enter the street address of filer's United States residence, not a post office box. An individual filer residing outside the United States should enter the filer's United States mailing address. If the filer has no U.S. mailing address the filer may provide a foreign address. An organization should enter its United States mailing address.

Item 14. If the filer has a financial interest in 25 or more foreign financial accounts, the filer should check the yes box, sign and date the report (Items 44, 45 and 46) and leave blank Part II (Continuation of Separate Accounts) or Part III (Joint Accounts) of the report. If the group of entities covered by a consolidated report has a financial interest in 25 or more foreign financial accounts, the reporting parent corporation need only complete Part V (for consolidated reporting) Items 34 through 42, for the identity information of the account owners, but need not complete the account information. Detailed information about each account, including all information called for on this report, must be recorded and retained for five years from June 30 of the year following the calendar year reported. Any person who reports 25 or more foreign financial accounts must provide all the information omitted from Part II, III or V as appropriate.

Part II

Item 15. Provide the maximum value of the account during the calendar year being reported. The maximum value of an account is the largest amount of currency or non-monetary assets that appear on any quarterly or more frequent account statement issued for the applicable year. If periodic account statements are not issued, the maximum account asset value is the largest amount of currency and non-monetary assets in the account at any time during the year. Convert foreign currency by using the official exchange rate at the end of the year. In valuing currency of a country that uses multiple exchange rates, use the rate which would apply if the currency in the account were converted into United States dollars at the close of the calendar year. The value of stock, other securities, or other non-monetary 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. For purposes of Item 15, if the filer had a financial interest in more than one account, each account is to be valued separately in accordance with the foregoing two paragraphs. If the filer had a financial interest in one or more but fewer than 25 accounts, and is unable to determine whether the maximum value of these accounts exceeded $10,000 at any time during the year, complete Part II, III, or V for each of these accounts and enter “value unknown” in Item 15 for these accounts.

Item 16. Indicate the type of account. If “Other” is selected describe the account.

Item 17. Provide the name of the financial institution with which the account is held.

Item 18. Provide the account number which the financial institution uses to designate the account.

Item 19-23. Provide the complete mailing address of the financial institution where the account is located. If the foreign state or postal code is not known leave them blank.

Part III

Item 24. Enter the number of joint owners for the account. If the exact number is not known, provide an estimate. In determining the number of joint owners, the filer is not counted.

Items 25-33. Enter this identity information about the joint owner. If there is more than one joint owner, enter the

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identity information about the principal joint owner. The filer may leave blank items for which no information is available. A spouse having a joint financial interest in an account with the filing spouse should be included as a joint account owner in Part III of this report. The filer should write (spouse) on Line 26 after the last name of the joint spousal owner. If the only reportable accounts of the filer's spouse are those reported as joint accounts, the filer's spouse need not file a separate report. If the accounts are owned jointly by both spouses, the filer's spouse should also sign the report. See the instructions for Item 44. If the filer's spouse has a financial interest in other accounts that are not jointly owned with the filer or has signature or other authority over other accounts, the filer's spouse should file a separate report for all accounts including those owned jointly with the other spouse.

Part IV—No Financial Interest in Account

Items 34-42. You must provide the name, address, and identifying number of the owner of a foreign financial account over which you had signature or other authority but no financial interest in the account. If there is more than one owner of the account over which you have authority, providethe information in Items 34-43 for the primary owner for which you have authority. If you complete the account information for more than one account of the same owner, you need identify the owner only once. Write “Same Owner” in Item 34 for the succeeding accounts of the same owner.

Item 43. Enter filer's title for the position which gives him authority over the account.

Part V—Consolidated Report for Corporate Parent & Subsidiary Corporations

A corporation which owns directly or indirectly more than a 50 percent interest in one or more other entities required to file this report will be permitted to file a consolidated report on TD F 90-22.1, on behalf of itself and such other entities. Check box “d” in Item 2 in Part I and complete Part V.

Items 34-42. You must provide the corporate name, identifying number and address of the owner of the foreign financial account as shown on the books of the financial institution.

If you complete the account information for more than one account of the same owner you need identify the owner only once. Write “Same Owner” in Item 34 for the succeeding accounts of the same owner.

Signatures

This report must be signed by the person named in Part I. If the report is being filed on behalf of a partnership, corporation, fiduciary or other legal entity, it must be signed by an authorized individual. Consolidated reports should be signed by an authorized official of the parent corporation. Enter the title of the individual signing for a legal entity, such as a corporation, which is shown as the filer. A spouse included as a joint owner, who elects not to file a separate report in accordance with the instructions in Part III, must also sign this report. See the instructions for Part III.

Enter the title of the individual signing for a legal entity, such as a corporation, which is shown as the filer. Leave “Filer's Title” blank if the filer is only reporting as an individual. An individual filing because of a financial interest in his individual accounts is filing as an individual. An individual filing because of signature or other authority over a foreign financial account is filing as an individual. If the filer only has signature authority over the account, he should enter his title in Part IV Item 43, Filer's Title with this Owner, to show his relationship to the account. Enter the actual date signed.

Workbook on the Report of Foreign Bank and Financial Accounts (FBAR)

- Introduction
- Objectives
- Purpose of the FBAR

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- Who Must File the FBAR?
- Definition of a United States Person
- Definition of Foreign Financial Accounts
- Definition of Financial Interest
- Definition of Signature Authority
- Definition of Other Account Authority
- Reporting for Joint Accounts
- Recordkeeping
- Exemptions from Filing
- Penalties
- Putting It All Together
- Exercises

Introduction

The Bank Secrecy Act (BSA) gave the Department of Treasury authority to establish recordkeeping and filing requirements for United States persons with financial interests in or signature authority, or other authority over financial accounts maintained with financial institutions in foreign countries. This provision of the law requires that a Form TD F 90-22.1, Report of Foreign Bank and Financial Accounts (FBAR) be filed if the aggregate balances of such foreign accounts exceed $10,000 at any time during the year. (See Exhibit 1, Form TD F 90-22.1)

On April 10, 2003, the Financial Crimes and Enforcement Network (FinCEN) delegated enforcement authority to the Internal Revenue Service (IRS). The IRS is now responsible for:

- Investigating possible civil violations.
- Assessing and collecting civil penalties.
- Issuing administrative rulings.

Objectives

- Learn the purpose of the FBAR regulation.
- Determine who must file the FBAR.
- Determine the FBAR filing requirements.
- Understand the civil and criminal penalties that may be applicable for noncompliance with the FBAR filing requirements.
- Determine who is exempt from the FBAR filing requirements.

Purpose of the FBAR

The FBAR rules were established because of the utility of the information required in criminal, tax, and other regulatory matters and in the conduct of intelligence or counterintelligence activities including analysis to protect against international terrorism. The reports filed as a result of this regulation provide leads to investigators that facilitate the identification and tracking of illicit funds or unreported income, as well as providing additional prosecutorial tools to combat money laundering and other crimes.

Who Must File the FBAR?

A United States person must file an FBAR report if that person has financial interest in, signature authority or other authority over any financial account(s) in a foreign country and the aggregate value of these account(s) exceeds $10,000 at

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any time during the calendar year.

The account value is the largest amount of currency and/or monetary instruments that appear on any quarterly or more frequently issued account statement for the applicable year. If a periodic account statement is not issued, the maximum account value is the largest amount of currency and/or monetary instruments in the account at any time during the year. If the account value exceeds $10,000 on any account statement at any time during the calendar year an FBAR must be filed.

Definition of a United States Person

A “United States person” is:

- A citizen or resident of the United States.
- A person in, and doing business in, the United States.

The term “person” includes individuals and all forms of business entities, trusts, and estates.

Definition of Foreign Financial Accounts

Foreign financial accounts are accounts that are located outside of the:

- United States
- Northern Mariana Islands
- District of Columbia
- American Samoa
- Guam
- Puerto Rico
- U.S. Virgin Islands
- Trust Territories of the Pacific Islands and include:
- Bank accounts such as savings accounts, checking accounts, and time deposits.
- Securities accounts such as mutual funds, brokerage accounts, and securities derivatives accounts.
- Accounts where the assets are held in a commingled fund and the account owner holds an equity interest in the fund.
- Any other account(s) maintained in a foreign financial institution or with a person doing business as a financial institution.

Definition of Financial Interest

Financial interest includes accounts for which the U.S. person is the owner of record or has legal title, whether the account is maintained on his or her own benefit or for the benefit of others including non-United States persons.

Financial interest also includes accounts where the owner of record or holder of legal title is a person acting as an agent, nominee, or in some other capacity on behalf of a U.S. person.

Example: John, a U.S. citizen who resides in Mexico, granted his brother Paul, a U.S. citizen, a Power of Attorney to access his Mexican bank accounts. Paul is the owner of record.

John has a financial interest in the account. Paul is acting only as an attorney on behalf of John. Paul also has a financial interest in the account, since he is the owner of record. Both John and Paul must file an FBAR.

Example: Given the information in the above example, if Paul is a Mexican citizen, must he file the FBAR?

No, Paul is not considered to be a U.S. person.

Financial interest in an account also includes a corporation in which a U.S. person directly or indirectly owns more than 50 percent of the total value of the shares of stock.

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Example: A Florida corporation that owns 100% of a foreign company that has foreign financial accounts has to file an FBAR because the corporation is a U.S. person and the owner of record or holder of legal title is a corporation that directly owns more than 50% of the total value of the shares of stock.

Example: A U.S. person who owns 75% of the Florida corporation in the previous example has to file an FBAR because he indirectly owns more than 50% of the total value of shares of stock of the foreign corporation.

Financial interest also includes an account where the owner of record or holder of legal title is:

- a partnership in which the U.S. person owns interest in more than 50% of the profits.
- a trust in which the U.S. person either has a present beneficial interest in more than 50% of the assets or receives more than 50% of the current income.

Definition of Signature Authority

A U.S. person has account signature authority if that person can control the disposition of money or other property in the account by delivery of a document containing his signature to the bank or other person with whom the account is maintained.

Definition of Other Account Authority

A person with other authority over an account is one who can exercise power that is comparable to signature authority over an account by direct communication, either orally or by some other means to the bank or other person with whom the account is maintained.

Example: A person who has the power to direct how an account is invested but cannot make disbursements or deposits to the account does not have to file an FBAR because the person has no power of disposition.

Reporting for Joint Accounts

If two persons jointly maintain an account, or if several persons each own a partial interest in an account, then each U.S. person has a financial Interest in that account and each person must file an FBAR.

A spouse having a joint financial interest in an account with the filing spouse should be included as a joint account owner in Part III of the FBAR. The filer should write (spouse) on line 26 after the last name of the joint spousal owner. If the only reportable accounts of the filer's spouse are those reported as joint owners, the filer's spouse need not file a separate report. If the accounts are owned jointly by both spouses, the filer's spouse should also sign the report. It should be noted that if the filer's spouse has a financial interest in other accounts that are not jointly owned with the filer or has signature or other authority over other accounts, the filer's spouse should file a separate report for all accounts including those owned jointly with the other spouse.

Recordkeeping

FBAR records should be kept for five years from the due date of the report which is June 30 of the following calendar year. The records should contain the following:

- Name maintained on each account.
- Number or other designation of the account.
- Name and address of the foreign bank or other person with whom the account is maintained.
- Type of account.
- Maximum value of each account during the reporting period.

Exemptions from Filing

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The following types of accounts and persons are exempt from the FBAR filing requirement.

• Accounts held in a military banking facility operated by a United States financial institution designated by the United States Government to serve U.S. Government installations located abroad.

• Officers or employees of a bank under the supervision of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, the Office of Thrift Supervision, or the Federal Deposit Insurance Corporation are exempt from filing the FBAR, if that officer or employee has NO personal financial interest in the account.

• Officers or employees of a domestic corporation whose equity securities are listed on national securities exchanges, or which has assets exceeding $10 million and 500 or more shareholders of record, need not file an FBAR concerning the other signature authority over a foreign financial account of the corporation, if:

1. the officer or employee has NO personal financial interest in the account, and
2. has been advised in writing by the chief financial officer of the corporation that the corporation has filed a current report which includes that account.

Penalties

The following chart highlights the civil and criminal penalties that may be asserted for not complying with the FBAR reporting and recordkeeping requirements.

Violation	Civil Penalties	Criminal Penalties	Comments
Negligent Violation	Up to $500	N/A	31 U.S.C. § 5321(a)(6)(A) 31 C.F.R. 103.57(h).
Non-Willful Violation	Up to $10,000 for each negligent violation	N/A	31 U.S.C. § 5321(a)(5)(B)
Pattern of Negligent Activity	In addition to penalty under § 5321(a)(6)(A) with respect to any such violation, not more than $50,000	N/A	31 U.S.C. 5321(a)(6)(B)
Willful - Failure to File FBAR or retain records of account	Up to the greater of $100,000, or 50 percent of the amount in the account at the time of the violation.	Up to $250,000 or 5 years or both	31 U.S.C. § 5321(a)(5)(C) 31 U.S.C. § 5322(a) and 31 C.F.R. § 103.59(b) for criminal. The penalty applies to all U.S. persons.
Willful - Failure to File FBAR or retain records of account while violating certain other laws	Up to the greater of $100,000, or 50 percent of the amount in the account at the time of the violation.	Up to $500,000 or 10 years or both	31 U.S.C. § 5322(b) and 31 C.F.R. § 103.59(c) for criminal The penalty applies to all U.S. persons.
Knowingly and Willfully Filing False FBAR	Up to the greater of $100,000, or 50 percent of the amount in the account at the time of the violation.	$10,000 or 5 years or both	18 U.S.C. § 1001, 31 C.F.R. § 103.59(d) for criminal. The penalty applies to all U.S. persons.
L1-4Civil and Criminal Penalties may be imposed together. 31 U.S.C. § 5321(d).			

Putting It All Together

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In this lesson you fearned:

• What is the purpose of the FBAR regulation.

• Who must file the FBAR.

• What are the FBAR filing requirements.

• What civil and criminal penalties may be assessed for noncompliance with FBAR filing and recordkeeping requirements.

• Who is exempt from the FBAR filing requirement.

Exercises

1) True or False

All foreign accounts of U. S. persons must be reported to the Department of Treasury.

2) Which of the following is a U.S. person? (Circle all that apply)

a. a citizen

b. a domestic corporation

c. a domestic partnership

d. a domestic trust or estate

e. all of the above

3) True or False

A savings account may be a type of foreign financial account.

4) True or False

An FBAR is not required if the foreign account generates neither interest nor dividend income.

5) True or False

If a person has a foreign account in the year 2008 that requires reporting, the FBAR is due April 15, 2009.

6) How long should account holders keep a copy of the filed FBAR?

a. 3 years

b. 5 years

c. 7 years

d. 10 years

7) Does a U.S. person need to file an FBAR for his Eurodollar account in the Cayman Islands?

8) A N.Y. corporation owns a foreign company that has foreign accounts. The corporation will file an FBAR for the foreign company's accounts. Does a shareholder who owns 65% of the company's stock need to file an FBAR?

9) True or False

Accounts in U.S. military banking facilities, operated by a United States financial institution to serve U.S. Government installations abroad, are not reportable on a FBAR.

(See Exhibit 2 for answers to exercises.)

Exhibit 1

Form TD F 90-22, Report of Foreign Bank and Financial Accounts (PDF)

Exhibit 2, Answers to Exercises

1) False

Only foreign accounts with an aggregate value of more than $10,000 at any time during the calendar year must be reported.

2) e.

All of the choices are a U.S. person. A United States person is:

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- A citizen or resident of the United States
- A domestic partnership
- A domestic corporation
- A domestic estate or trust

3) True

A "financial account" includes bank, securities, securities derivatives, or other financial instruments accounts. The term also means any savings, demand checking, deposit, or any other account maintained with a financial institution.

4) False

An FBAR must be filed whether or not the foreign account generates any income.

5) False

The FBAR is due by June 30, 2009. The FBAR is due by June 30 of the subsequent year after the account holder meets the more than $10,000 threshold.

6) b.

Copies of the FBAR must be kept for a period of five years.

7) Yes

The Cayman Islands account is a foreign account.

8) Yes

An FBAR must be filed by any owner that directly or indirectly owns more than 50 percent of the total value of the shares of stock.

9) True

Accounts in U.S. military banking facilities, operated by a United States financial institution to serve U.S. Government installations abroad, are not reportable.

Rate the Small Business and Self-Employed Web Site

Foreign Financial Accounts Reporting Requirements

FS-2007-15, February 2007

With the globalization of the economy, more and more people in the U.S. have foreign financial accounts. While there are many legitimate reasons to own foreign financial accounts, there are also responsibilities that go along with owning such accounts. Foreign account owners must remember that they may have to report their accounts to the government, even if the accounts do not generate any taxable income.

Who is required to report their foreign accounts to the government, and how do they do so? The Bank Secrecy Act requires U.S. persons who own a foreign bank account, brokerage account, mutual fund, unit trust, or other financial account to file a Form TD F 90-22.1, Report of Foreign Bank and Financial Authority (FBAR), if:

1. The person has financial interest in, signature authority, or other authority over one or more accounts in a foreign country, and
2. The aggregate value of all foreign financial accounts exceeds $10,000 at any time during the calendar year.

A U.S. person is:

- A citizen or resident of the United States, or
- Any domestic legal entity such as a partnership, corporation, estate or trust.

A foreign country includes all geographical areas outside the United States, the Commonwealth of Puerto Rico, the Commonwealth of the Northern Mariana Islands, and the territories and possessions of the United States (including Guam, American Samoa, and the United States Virgin Islands). An account in an institution known as a United States "military banking facility" is not considered to be an account in a foreign country.

The FBAR is not an income tax return and should not be mailed with any income tax returns. The FBAR must be

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mailed on or before June 30 of the following year to: U.S. Department of the Treasury, P.O. Box 32621, Detroit, MI 48232-0621.

Unlike with federal income tax returns, requests for an extension of time to file an FBAR are not granted.

A person having signature or other authority over, but no financial interest in, a foreign financial account may be excepted from filing an FBAR if they are an officer or employee of a federally-regulated bank or a federally-regulated publicly traded corporation. See the FBAR instructions for more information about this exception.

Why is it important to file the FBAR? The FBAR is required because foreign financial institutions that do not conduct business in the United States may not be subject to the same reporting requirements that domestic financial institutions are subject to (such as the requirement to file a Form 1099 to report interest paid to an account holder). Although there are legitimate purposes for having a foreign account, the FBAR is a tool to help the U.S. government identify persons who may be using foreign financial accounts to circumvent U.S. law.

Such individuals may be participating in economic crimes such as income tax evasion or embezzlement, or they may be trying to fund other illegal activity like drug trafficking or even terrorist activities.

Also, there are serious consequences for foreign account holders who choose not to honor their FBAR filing requirements. Account holders who do not comply with the FBAR reporting requirements may be subject to civil penalties, criminal penalties or both.

For an FBAR violation occurring after Oct. 22, 2004, the maximum civil penalty for a willful violation of the FBAR reporting and recordkeeping requirements is the greater of $100,000 or 50% of the balance in the account at the time of the violation. Non-willful violations can result in a penalty as high as $10,000 for each violation. Criminal violations of the FBAR rules can result in a fine and/or five years in prison.

More information on FBAR filing exceptions can be obtained on this Web site, the Money Services Businesses' Web site at www.msb.gov and the Financial Crimes Enforcement Network's Web site at www.fincen.gov. Help in completing Form TD F 90-22.1 is available at 1-800-800-2877, option 2. The form is available online at www.irs.gov and www.msb.gov or may be ordered by telephone at 1-800-829-3676. Questions regarding the FBAR may also be sent to FBARquestions@irs.gov.

September 23 Deadline for Some FBAR Filers

Some taxpayers, whose circumstances are described below, recently learned that they have an FBAR filing obligation but they do not have sufficient time to gather the information necessary to properly file the FBAR by the June 30, 2009 due date. For all others, however, the due date remains June 30.

On June 24, 2009, the IRS offered the following advice.

Taxpayers who reported and paid tax on all their 2008 taxable income, but only recently learned of their FBAR filing obligation and have insufficient time to gather the necessary information to complete the FBAR, should file the delinquent FBAR report according to the instructions and attach a statement explaining why the report is filed late. Send it to the address below:

U.S. Department of the Treasury P.O. Box 32621 Detroit, MI 48232-0621

Additionally, send a copy of the delinquent FBAR, together with a copy of the 2008 tax return, by September 23, 2009, to the Philadelphia Offshore Identification Unit, at the following address:

Internal Revenue Service 11501 Roosevelt Blvd. South Bldg., Room 2002 Philadelphia, PA 19154 Attn: Charlie Judge, Offshore Unit, DP S-611

In this situation, the IRS will not impose a penalty for the failure to file the FBAR.

Additionally, if all 2008 taxable income with respect to a foreign financial account is timely reported and a United States person only recently learned they have a 2008 FBAR obligation and there is insufficient time to gather the necessary information to complete the FBAR, the United States person may follow the procedures set forth above and no pen-

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alty will be imposed.

For 2008 tax returns due after September 23, 2009, the tax return does not need to accompany the 2008 FBAR.

Related Items:

- Voluntary Disclosure
- Voluntary Disclosure: Questions and Answers (revised June 24, 2009)

Part III — Administrative, Procedural, and Miscellaneous

FBAR Filing Requirements — Extended Filing Date for U.S. Persons Having Signature Authority Over, But No Financial Interest In, a Foreign Financial Account, and for U.S. Persons with Financial Interest In, or Signature Authority Over, Foreign Commingled Funds: Request for Public Comments on FBAR Filing Requirements

Notice 2009-62

I. Background and Purpose

The Report of Foreign Bank and Financial Accounts, Form TD F 90-22.1 (hereinafter referred to as "FBAR"), provides necessary information for certain governmental agencies. Information on the FBAR may be used in criminal, tax, or regulatory investigations or proceedings, or in the conduct of intelligence or counterintelligence activities, including analysis, to protect against international terrorism. This governmental need for information is balanced with the administrative concerns presented by the filing of the information by U.S. persons.

In October 2008, the IRS revised the FBAR and the accompanying instructions. On June 5, 2009, the IRS issued Announcement 2009-51, 2009-25 I.R.B. 1105, which stated that the IRS is temporarily suspending the filing requirement of the FBAR for those persons who are not U.S. citizens, residents, or domestic entities. On May 6, 2009 and June 24, 2009, the IRS posted questions and answers (Q&As-9 and -43, respectively) on its public website (www.irs.gov) that provide relief to certain persons who only recently learned of their obligation to file an FBAR by setting forth conditions and procedures for filing Form TD F 90-22.1 by September 23, 2009. More information concerning this relief is available at http://www.irs.gov/newsroom/article/0,,id=210027,00.html. This Notice provides additional administrative relief for (i) persons with no financial interest in a foreign financial account but with signature or other authority over the foreign financial account (hereinafter referred to as "signature authority"), and (ii) persons with a financial interest in, or signature authority over, a foreign financial account in which the assets are held in a commingled fund (hereinafter referred to as "foreign commingled funds"). The Department of the Treasury intends to issue regulations clarifying the FBAR filing requirements pertaining to those persons with respect to these foreign financial accounts, and solicits comments related to these FBAR filing requirements in this Notice.

II. Extended Filing Date for Specified Persons

A. Current FBAR Instructions

The current instructions to the FBAR provide, with certain exceptions, that U.S. persons that have signature authority over, but no financial interest in, a foreign financial account are required to file an FBAR. These persons must report the account on an FBAR even if the foreign financial account is reported on an FBAR filed by the owner of the account (or other person that has a financial interest in the account).

The current instructions to the FBAR also provide that a foreign financial account that must be reported on an FBAR includes any bank, securities, securities derivatives, or other financial instruments account. The FBAR instructions fur-

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ther provide that those accounts “generally also encompass any accounts in which the assets are held in a commingled fund and the account owner holds an equity interest in the fund (including mutual funds).”

The current instructions to the FBAR also provide that Form TD F 90-22.1 with respect to a given calendar year must be filed with the Department of the Treasury on or before June 30 of the succeeding year. Thus, except as provided in the prior relief granted by the IRS on its public website and the relief granted in this Notice, FBARs with respect to the 2008 calendar year should have been filed on or before June 30, 2009.

B. Extended Date for Filing an FBAR

In light of the additional time needed for the Department of the Treasury to address issues pertaining to FBAR filing requirements and the need to provide administrative relief for (i) persons with signature authority over, but no financial interest in, a foreign financial account, and (ii) persons with a financial interest in, or signature authority over, a foreign commingled fund, this Notice provides that those persons have until June 30, 2010, to file an FBAR for the 2008 and earlier calendar years with respect to these foreign financial accounts. Thus, eligible persons that avail themselves of the administrative relief provided in this Notice may need to file FBARs for the 2008, 2009 and earlier calendar years on or before June 30, 2010, to the extent provided in future guidance.

The FBAR filing extension provided by this Notice applies to FBARs with respect to 2008 and earlier calendar years. For (i) persons with signature authority over, but no financial interest in, a foreign financial account, and (ii) persons with a financial interest in, or signature authority over, a foreign commingled fund, the FBAR filing extension provided in this Notice supplements the filing extension to September 23, 2009, previously provided by the IRS on its public website.

III. Request for Public Comments

The Department of the Treasury is interested in receiving comments on the following issues affecting a person's FBAR filing obligation.

The Department of the Treasury requests comments regarding when a person with signature authority over, but no financial interest in, a foreign financial account should be relieved of filing an FBAR for the account. For example comments are requested regarding whether relief from filing would be appropriate if a person with a financial interest in the account has filed an FBAR.

The Department of the Treasury requests comments discussing in what circumstances the exception from FBAR filing currently available for officers and employees of banks and certain publicly-traded domestic companies might be expanded to apply to all officers and employees with only signature authority over, and no financial interest in, an employer's foreign financial account, including circumstances in which an individual has been advised that an FBAR has been filed with respect to a foreign financial account for which that person has signature authority. The Department of the Treasury also requests comments discussing how the bank and publicly-traded company exception (including the requirement of notification that an FBAR was filed by a U.S. person with a financial interest in the account) might apply to officers and employees with only signature authority over accounts owned by clients of their employer.

The Department of the Treasury requests comments concerning when an interest in a foreign entity (e.g., a corporation, partnership, trust, or estate) should be subject to FBAR reporting. For example, comments are requested regarding the possibility of applying the principles of sections 1297 and 1298(b) of the Internal Revenue Code to determine when an interest in a foreign entity should be subject to FBAR reporting. Comments are also requested regarding whether the passive asset and passive income thresholds of 50 percent and 75 percent, respectively, are appropriate and whether the tests should apply conjunctively.

The Department of the Treasury also requests comments on whether a U.S. person should be relieved from an FBAR filing requirement with respect to a foreign commingled fund in other circumstances, such as when filing would be du-

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plicative of other reporting.

Interested persons should submit comments and suggestions with respect to the guidance on FBAR reporting in this Notice by October 6, 2009, to:

Internal Revenue Service Attn: CC:PA:LPD:PR (Notice 2009-62) Room 5203 P.O. Box 7604 Ben Franklin Station Washington, D.C. 20044

or hand deliver comments Monday through Friday between the hours of 8 a.m. and 4 p.m. to:

Courier's Desk Internal Revenue Service Attn: CC:PA:LPD:PR (Notice 2009-62) 1111 Constitution Avenue, N.W. Washington, D.C. 20224

A copy of those comments should also be sent to:

Financial Crimes Enforcement Network Department of the Treasury P.O. Box 39 Vienna, VA 22183

Alternatively, the public may submit comments electronically via e-mail to the following address: Notice.Comments@irscounsel.treas.gov with a copy to regcomments@fincen.gov. Respondents should include " Notice 2009-62" in the subject line of any comment submitted.

All comments submitted by the public will be made available for public inspection and copying in their entirety.

IV. Effective Date

This Notice applies to FBARs (Form TD F 90-22.1) with respect to calendar year 2008 and prior calendar years.

V. Contact Information

For further information regarding the relief relating to signature authority, contact Terra-Lynn Zentara at (202) 283-7659 (not a toll-free call). For further information regarding foreign commingled funds, contact Joseph Henderson at (202) 622-3446 (not a toll-free call).

Pensions & Investments

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Attorneys want FBAR clarification from IRS

By Doug Halonen
Source: Pensions & Investments
Date: August 11, 2009

Groom Law Group plans to ask the IRS to clarify a recent announcement postponing until at least June 30, 2010, a requirement for pension plans to report for the first time investments in offshore hedge funds and private equity firms, said Jennifer Eller, an ERISA attorney for the firm.

The agency said the filing extension for the Treasury Department's Report of Foreign Bank and Financial Accounts form, or FBAR, applied to some offshore investments made by plans but not by plans holding securities owned through a foreign custody account, Ms. Eller said in an interview.

Ms. Eller said the extension the IRS provided was "very helpful." But without further clarification, sponsors, custodi-

ans and trustees might have to look through every foreign financial account to determine which might still be subject to the original Sept. 23 FBAR filing deadline, Ms. Eller said. “It's almost as much work as what you would have to do to make a full filing,” Ms. Eller said.

The IRS had no comment, said Bruce Friedland, an IRA spokesman.

The FBAR reporting obligation has been in effect since the early 1970s. But until recently it had been believed to not apply to pension investments, only to investments by U.S.-based individuals and corporations with more than $10,000 in offshore accounts.

Through changes in the instructions to the FBAR form — and a series of frequently asked questions and statements from IRS officials starting late last year — Treasury beefed up the obligation in a way that appeared to require pension plans, plan investment committee members and plan trustees to file individual FBAR reports on the investments with offshore managers.

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FBAR Resources

Updated August 7, 2009

TD F 90-22.1, *Report of Foreign Bank and Financial Accounts* (FBAR), must be filed by U.S. persons having a financial interest in or signature authority or other authority over any financial account in a foreign country if the aggregate value of these accounts exceeds $10,000 at any time during the calendar year.

June 30 is the deadline for filing the current year FBAR.

The following is a collection of *JofA* news, analysis and feature articles and AICPA and IRS resources dealing with the newly revised FBAR.

NEWS

IRS Extends FBAR Filing Date for 2008 Filings

Aug. 7, 2009

The IRS announced Friday in Notice 2009-62 that it is extending for certain taxpayers the due date for filing calendar year 2008 Form TD F 90-22.1, *Report of Foreign Bank and Financial Accounts* (FBAR). Because the Treasury Department is still working out various FBAR filing issues, it has decided to give certain taxpayers until June 30, 2010, to file FBARs for 2008 and earlier calendar years.

IRS Releases Streamlined Offshore Voluntary Disclosure Form

July 31, 2009

On July 29, the IRS posted to its Web site a three-page “optional format” short form for taxpayers to use when disclosing applying for the Voluntary Disclosure Program.

New Voluntary Compliance FAQs

June 25, 2009

On June 24, the IRS released new voluntary compliance FAQs, including instructions for taxpayers who only recently learned of their FBAR filing obligation and guidance on delinquent information returns.

Reminder: Foreign Bank Account Report (FBAR) Forms Must Be Received by the IRS by June 30

June 6, 2009

FBAR forms must be received (not just mailed) by June 30; however, the IRS has let non-U.S. taxpayers off the hook for now by reverting to the old definition of "U.S. person."

FBAR Penalties Reduced for Six Months

April 22, 2009

The IRS created a framework for voluntary disclosure requests containing offshore issues, such as previously undisclosed foreign financial accounts and entities. The policy will remain in place for six months until Sept. 23, 2009.

ARTICLES

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

June 10, 2009

The revised version of the FBAR form surprised many practitioners. This article discusses the new reporting requirements and new traps for the uninitiated.

FBAR Voluntary Disclosure Questions Answered

June 11, 2009

The IRS has answered 51 "frequently asked questions" (FAQs) about its voluntary disclosure and settlement option for previously unreported offshore financial accounts and entities and income from them. The six-month window for making disclosures under the program ends Sept. 23.

RESOURCES

AICPA-ABA Teleconference on Aug. 20 on FBAR Issues

Aug. 10, 2009

The AICPA's Tax Section and PFP Section are cosponsoring with the ABA Section of International Law a 90-minute teleconference on Aug. 20 at 11 a.m. on FBAR reporting and the IRS Offshore Income Voluntary Disclosure Program.

AICPA/ABA Teleconference on FBAR Issues

June 25, 2009

On Friday, June 12, the AICPA Tax Section and PFP Section cosponsored with the ABA a teleconference on FBAR reporting. The teleconference featured a panel of IRS FBAR experts. Listen to the audio here (95 minutes).

Chart of Information Needed From Clients

June 24, 2009

A handy document for gathering from clients the information needed to file FBAR, produced by the AICPA's FBAR

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Task Force. (Opens in Microsoft Word.)

FBAR Reporting Requirements - Issues to Consider

June 24, 2009
This report from Eisner LLP outlines FBAR reporting requirements. (Opens as a PDF.)

IRS Voluntary Compliance Questions

June 8, 2009
The information below includes questions that IRS Criminal Investigation special agents have asked some taxpayers participating in the IRS Offshore Voluntary Compliance program. Practitioners might want to document the facts as fully as possible in a detailed summary when submitting under the program.

GUIDANCE

FBAR Procedural

Announcement 2009-51, temporarily reverting to old definition of “United States person”
New TD F 90-22.1 FBAR and instructions
IRS reminder of June 30 FBAR deadlines
IRS information on FBAR reporting
FBAR FAQs
Publication 4261, Do You Have a Foreign Financial Account?
IRS's Beth Elfrey discusses FBAR changes
IRS's Beth Elfrey discusses new FBAR
IRS OPR information on professional responsibility and FBAR
IRS headliner on FBAR reporting by persons with only signature authority
IRS Appeals Coordinated Issue information
FBAR definition of “in and doing business in” the United States
FBAR workbook and penalty chart
IRS memo on FBAR job aid and counsel review of penalty cases
Internal Revenue Manual sections on FBAR law and penalties
Internal Revenue Manual FBAR examination procedures
BSA Compliance Examiners memo on money transmitter FBAR requirements
IRS FBAR requirements webpage

Voluntary Compliance Initiative

Rev. Proc. 2003-11 on Offshore Voluntary Compliance Initiative

Other Procedural

Bank Secrecy Act information
Bank Secrecy Act requirements
IRS Criminal Investigation 2009 business plan
The life and times of a Currency Transaction Report
Civil penalties under Title 31

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Currency reporting and money laundering statistics

Voluntary disclosure

IRS voluntary disclosure main webpage
FAQs on voluntary disclosure (updated June 24, 2009)
IRS memo authorizing application of penalty framework to voluntary disclosure requests
IRS memo on routing voluntary disclosure requests
Internal Revenue Manual sections on voluntary disclosure
IRS voluntary disclosure contact information
Offshore voluntary disclosures form - optional format

Offshore income

Commissioner Shulman's statement on offshore income
IRS memo on proper development of offshore examination cases
Income from abroad is taxable

Sign up for Aug. 20 teleconference on IRS' FBAR filing requirements and new offshore income voluntary disclosure program

CPA Letter Daily | 08/11/2009

The AICPA, the American Bar Association and the Society for Trust and Estate Practitioners are sponsoring a teleconference with the Internal Revenue Service about its new offshore income voluntary disclosure program (and filing requirements for FBAR Form TDF 90-22.1). Voluntary disclosure will reduce penalties for overlooked prior year filings. File 2008 and earlier FBARs free of penalty for filers who qualify -- available up to Sept. 23. Teleconference: Aug. 20, 11 a.m. to 12:30 p.m. ET. Get more information or a registration form ($20 for AICPA Tax and PFP Section members; $30 for others). Submit questions in advance of the teleconference here.

The ABA Section of International Law Committee on International Taxation

In cooperation with the Section of Real Property Trust & Estate Law American Institute of Certified Public Accountants & Society of Trust and Estate Practitioners Present

Foreign Bank Account Reports and More: Voluntary Disclosure - September 23 Deadline!

August 20, 2009

11:00 AM - 12:30 PM EDT **TELECONFERENCE**

Click here to register online or see the attachment

UPDATE: Avoid pitfalls & penalties filing NEW FBAR Form TDF 90-22.1 for offshore accounts. **Learn NEW Voluntary Disclosure to reduce penalties for overlooked prior year filings & caveats. File 2008 and earlier FBARs**

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free of <u>penalty for filers who qualify — available up to September 23, 2009</u>.

Comprehend <u>CLARIFIED reporting requirements</u> for *"U.S. 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"*.

Clarify what is (and is not) a "foreign financial account": *hedge funds, mutual funds, pension plans, estates, trusts and tiered entities*; <u>avoid Draconian failure to file penalties</u> — (a) $10,000 for a non-willful violation and (b) $100,000 or up to 50% of the account balance for a willful violation; lexicon 31 U.S.C not 26 U.S.C. and related issues.

Apply & comply - catch up filing prior years' FBARs, and **Forms 3520, 3520-A, 5471, 5472, 926, & 8865**.

Expert panel of practitioners and IRS shall provide detailed guidance and examples for you to apply and comply to <u>Voluntarily Disclose by the September 23 Deadline</u>!

PANEL:

- **Leigh-Alexandra Basha**, *Partner/Chair-International Private Wealth Services,* ***Holland*** *& Knight*
- **John C McDougal**, *IRS Counsel (SBSE)*
- **Neil AJ Sullivan**, *CPA, TEP, International Tax Compliance Strategy*

<u>REGISTRATION FORM</u>

International Tax Committee Hot Topic Briefing August 20, 2009

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AICPA Update on New FBAR Form, Reporting, and Due Diligence Requirements

<u>Update on New Foreign Bank Account Form, Reporting and Due Diligence Requirements</u>

The AICPA FBAR Task Force recently met with IRS FBAR (Report of Foreign Bank and Financial Accounts) offi-

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cials and learned of developments with the new form, reporting rules, and due diligence requirement. See below an update on:

1. Income Tax Return Questions and Notification to Clients of the New FBAR Form and Requirements for 2009
2. IRS FAQs on FBAR
3. Expanded Scope of FBAR
3. Preparer “Due diligence” Penalties for FBAR per IRS OPR
4. Penalty Enforcement for FBAR - $10,000 per Return Penalties
5. AICPA Resources/Tax Guides on FBAR Available

1. Income Tax Return Questions: AICPA reminds tax practitioners that when gathering information for Form 1040s (and Form 1041s, 1065s, 1120s, etc.), to ask clients about the existence of foreign bank accounts and disclose the information in Question 7, Part III of Form 1040, Schedule B, Interest and Ordinary Dividends, **even if the client has no reportable interest or dividends and would not otherwise fill out the Schedule B**, Line 3 Other Information, Schedule G of Form 1041, Line 9 of Schedule B of Form 1065, and Line 6a of Schedule N of Form 1120. (See related tax organizer e-alert item.) Taxpayers who are currently filing Form 5471, Form 8858, Form 8865 or Form 3520 may also be subject to FBAR reporting requirements. (See related Form 5471 penalty e-alert item) If the questions on Schedule B of the Form 1040 Part III are left blank, it may be considered an incomplete return and the statute of limitations will remain open.

Practitioner Should Notify Clients of FBAR: Tax practitioners with clients with foreign bank accounts should notify clients of their responsibility to file the “Report of Foreign Bank and Financial Accounts” (Treasury Form TD F 90-22.1, referred to as FBAR) on or before June 30, 2009. IRS has released a new Form TD F 90-22.1, http://www.irs.gov/pub/irs-pdf/f90221.pdf, which should be used for all 2008 filings in 2009 and later years. Significant changes have been made to the form so the practitioner should read the instructions carefully. Practitioners should also check their tax return software programs to make sure the new version of the form is being used for all FBARs filed in 2009 or later, even if the FBAR is being filed for a prior year. We note that the return must be RECEIVED by June 30, not mailed by that date, and recommend sending it in Certified Mail, Return Receipt Requested as proof of the receipt date.

2. FAQs: IRS frequently asked questions (FAQs) on the FBAR are at http://www.irs.gov/businesses/small/article/0,,id=148845,00.html.

3. Expanded Scope of FBAR: According to the new form instructions, beginning for the 2008 tax year, the new FBAR requirements apply to persons in and doing business in the U.S. Therefore, a non-resident alien working in the U.S. (as an employee or independent contractor) may be subject to the new 2009 FBAR filing requirement because that individual is “in and doing business” in the U.S. and has signing or other authority over foreign financial accounts.

A foreign corporation that is in and doing business in the United States is also considered a U.S. person.

Previously, nonresidents did not have to file, but with this 2009 form, persons in, and doing business in, the United States must file FBARs, whether or not they are nonresidents. This means that many nonresidents who do business in the U.S. (Canadians, for example) may have to disclose their foreign bank account information.

The IRS website - http://www.irs.gov/businesses/small/article/0,, id=204798,00.html and http://www.irs.gov/businesses/small/article/0,, id=148845,00.html has more information on the “doing business in the U.S.” requirement, including that it will be determined based on an analysis of the facts and circumstances of each case, and that it is generally required if the person is conducting business within the United States on a regular and continuous basis.

The IRS website indicates that persons who are merely visiting or who sporadically conduct business in the United States are not in and doing business in the United States for FBAR reporting purposes and provides the following examples of persons who are not considered to be in and doing business in the United States for FBAR reporting purposes and do NOT need to file FBARs:

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• Persons who are not citizens or residents and who are engaged in a business but who only occasionally visit the United States to meet customers or business associates.

• Artists, athletes, and entertainers who are not citizens or residents of the United States and who only occasionally come to the United States to participate in exhibits, sporting events, or performances.

• A person who is not a United States citizen or resident and who visits the United States to manage his personal investments, such as rental property, and conducts no other business.

The AICPA Tax Division will continue to discuss this issue and our concerns with this new requirement with the IRS.

4. Preparer Due Diligence Requirement: According to the IRS Office of Professional Responsibility in a posting on their website at http:// www.irs.gov/pub/irs-utl/fbar_document.doc, failure to timely file required tax or information returns, including FBARs, must be disclosed by practitioners on Form 8554, Application for Renewal of Enrollment to Practice Before the Internal Revenue Service.

In addition, a practitioner must comply with FBAR rules as part of his or her due diligence obligation under Section 10.22 of Circular 230. IRS further states: "Due diligence does not require that the practitioner "audit" their client. However, it does require that a practitioner make reasonable inquiries when a client provides information that suggests possible participation in overseas transactions/accounts subject to FBAR requirements. A practitioner may rely on information provided by a client in good faith. However, they may not ignore implications learned from information provided or actually known. The practitioner is also required to advise a client of potential penalties likely to apply to a position taken, such as failing to abide by FBAR requirements. The practitioner must make reasonable inquiries if information appears incorrect, inconsistent with an important fact or factual assumption, or is incomplete."

5. Penalty Enforcement for FBAR: The IRS has announced that it intends to enforce penalties for FBAR noncompliance — as far back as 6 years, the statute of limitations under the *Bank Secrecy Act*, Title 31 USC. It might be possible to negotiate for one year of penalties if compliance is started. Effective March 24, 2008, IRS has delegated the authority (Delegation Order 4-35, http://www.irs.gov/pub/foia/ig/spder/do_4-35_rev_1.pdf) to handle such enforcement to various government officials.

6. AICPA Resources on FBAR: The AICPA Tax Division's International Tax Resource Panel's Reporting Requirements Task Force has developed two guides on foreign income reporting and the TD F 90-22.1 (guide 1 and guide 2). For more details on this, see prior e-alert /NR/rdonlyres/E7DB3712-A36E-4ED9-8B69-39168FFE5A60/0/ealert053008.pdf or update at /Resources/International/Foreign+Bank+and+Financial+Account+Information+Needs+to+be+Reported+and+Filed+by+June+30.htm

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Foreign Trust Reporting Requirements

International Tax Gap Series

August 2008

Although there are legitimate reasons why a U.S. person might create a foreign trust, or have transactions with a foreign trust, they can have tax consequences and result in filing responsibilities as well. Regardless of your motivation, failure to meet these reporting and filing requirements can result in very significant penalties.

General Rules

In general, the reporting rules apply to a U.S. person who:

- Creates a foreign trust
- Transfers any money or property to a foreign trust
- Receives a distribution from a foreign trust
- Is treated as the U.S. owner of a foreign trust.

Tax consequences can apply to the U.S. owners and U.S. beneficiaries of foreign trusts, and to the foreign trust itself.

Reporting Requirements and Tax Consequences

Information Returns

Form 3520 - Annual Return to Report Transactions with Foreign Trusts and Receipt of Certain Foreign Gifts

Who must file Form 3520? There are several situations in which a Form 3520 (or statement with similar information) is required to be filed. The most common circumstances are where a U.S. person:

- Creates or transfers money or property to a foreign trust
- Receives (directly or indirectly) any distributions from a foreign trust
- Receives certain gifts or bequests from foreign entities

Form 3520 Instructions have more detailed information about who must file a Form 3520: when, where, and possible penalties for late or incomplete filing.

Form 3520-A - Annual Information Return of Foreign Trust with a U.S. Owner. This form provides information about the foreign trust. its U.S. beneficiaries, and any U.S. person who is treated as an owner of any portion of the foreign trust.

Who Must File Form 3520-A? Each U.S. person treated as an owner of any portion of a foreign trust under the grantor trust rules is responsible for ensuring that the foreign trust files Form 3520-A and furnishes the required annual statements to its U.S. owners and U.S. beneficiaries.

Instructions to Form 3520-A have more detailed information about who must file a Form 3520-A; when, where, and possible penalties for late or incomplete filing.

Other Possible Reporting Requirements

Form 1040. Schedule B, Part III, Foreign Accounts and Trusts must be completed if you receive a distribution from, or were grantor of, or a transferor to a foreign trust

TDF 90-22.1; Report of Foreign Bank and Financial Accounts — You might have to file this form if you have a financial interest in or signature authority over an account associated with a foreign trust.

Form 709 Gift Tax Return. A U.S. person who transfers money or property to a foreign trust may be required to file Form 709 United States Gift (Generation Skipping Transfer) Tax Return. See the Instructions for Form 709 for further information.

Form 1040NR — A foreign trust, which is not taxed to a U.S. owner as a grantor trust, may be obligated to file a Form 1040NR to pay U.S. tax on certain U.S. sourced income. See Publication 519 and the Instructions for Form 1040NR for additional information.

Income Tax Consequences

- U.S. owner of a foreign trust - In general, the U.S. owner of a foreign trust is taxed on the income of that trust. A U.S. person is treated as the owner of a foreign trust under the grantor trust rules of Internal Revenue Code sections 671-679, **which includes someone who transfers assets to a** foreign trust **which has a** U.S. beneficiary **of any portion of the trust.** *Each U.S. owner should receive a Foreign Grantor Trust Owner Statement (Form 3520-A, page 3), which includes information about the foreign trust income they must report.
- U.S. beneficiary of a foreign trust — In general, the U.S. beneficiary of a foreign trust will report their share of foreign trust income to the extent it is not reported by the transferors to the trust under the grantor trust rules. The U.S. beneficiary should receive a Foreign Grantor Trust Beneficiary Statement (Form 3520-A, or a Foreign Non Grantor Trust Beneficiary Statement which includes information about the taxability of distributions they have received and foreign trust income they must report.
- U.S. transferor of assets to a non grantor foreign trust - Internal Revenue Code section 684 requires the recognition of gain on certain transfers of appreciated assets to a foreign trust. See the Instructions for Form 3520-A for additional information.

Compliance Issue

Citizens and residents of the United States are taxed on their worldwide income. To help prevent the use of foreign trusts and other offshore entities for tax avoidance or deferral, Congress has enacted several specific provisions in the Internal Revenue Code. Some provisions trigger recognition of gains that would otherwise be deferred. Others deny deferral of tax on income moved offshore.

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A specialized industry has developed in attempting to circumvent these provisions. The promoters of offshore schemes often advance technical arguments which purport to show that their scheme is legal. These arguments are used to provide some comfort to their clients, who are then induced to enter into a scheme which usually involves concealing the true ownership and control of assets and income.

The filing and reporting responsibilities discussed here also apply to the beneficial owners of foreign trusts as well. The term beneficial ownership applies to the true owner of an entity, asset, or transaction as opposed to any stated ownership provided in documents or oral representations. The beneficial owner is the one that receives or has the right to receive proceeds or other advantages as a result of the ownership. It is common practice in offshore financial secrecy jurisdictions to interpose entities, individuals, or both as stated owners. The beneficial or true owner is contractually acknowledged in side agreements, statements or by other devises. For more information about offshore tax schemes just click on the following link: Abusive Offshore Tax Avoidance Schemes

Additional Information about any of the foreign trust reporting requirements and related income tax consequences is available by clicking on the relevant links throughout the article.

Return to:

The International Tax Gap Series

Penalties

The following chart highlights the civil and criminal penalties that may be asserted for not complying with the FBAR reporting and recordkeeping requirements.

Violation	Civil Penalties	Criminal Penalties	Comments
Negligent Violation	Up to $500	N/A	31 U.S.C. § 5321(a)(6)(A) 31 C.F.R. 103.57(h).
Non-Willful Violation	Up to $10,000 for each negligent violation	N/A	31 U.S.C. § 5321(a)(5)(B)
Pattern of Negligent Activity	In addition to penalty under § 5321(a)(6)(A) with respect to any such violation, not more than $50,000	N/A	31 U.S.C. 5321(a)(6)(B)
Willful - Failure to File FBAR or retain records of account	Up to the greater of $100,000, or 50 percent of the amount in the account at the time of the violation.	Up to $250,000 or 5 years or both	31 U.S.C. § 5321(a)(5)(C) 31 U.S.C. § 5322(a) and 31 C.F.R. § 103.59(b) for criminal. The penalty applies to all U.S. persons.
Willful - Failure to File FBAR or retain records of account while violating certain other laws	Up to the greater of $100,000, or 50 percent of the amount in the account at the time of the violation.	Up to $500,000 or 10 years or both	31 U.S.C. § 5322(b) and 31 C.F.R. § 103.59(c) for criminal The penalty applies to all U.S. persons.
Knowingly and Willfully Filing False FBAR	Up to the greater of $100,000, or 50 percent of the amount in the account at the time of the violation.	$10,000 or 5 years or both	18 U.S.C. § 1001, 31 C.F.R. § 103.59(d) for criminal. The penalty applies to all U.S. persons.
L1-4Civil and Criminal Penalties may be imposed together. 31 U.S.C. § 5321(d).			

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FAQs Regarding Report of Foreign Bank and Financial Accounts (FBAR) - United States Person

1. What is a United States person?
2. Who is considered to be doing business in the United States for FBAR reporting purposes?
3. Would a foreign athlete or entertainer that occasionally visits the U.S. in order to compete or perform in an event, be considered a United States person for FBAR purposes?
4. A person is a non-resident alien and only visits the United States to manage his personal interests, such as rental property. Does that person have to file an FBAR?
5. A non resident alien who doesn't meet the 183 day test is a partner in a US partnership where the US partnership deals with rentals: must he file an FBAR?
6. An American citizen, X, gives a person who is a citizen or resident of the U.S. power of attorney to X's Canadian bank accounts. X files an FBAR form annually. Does the power of attorney also need to file an FBAR?
7. A fiduciary who is a U.S. person has control as a trustee for an IRA with a foreign account. Should an FBAR be filed?
8. Is a single member LLC, which is a disregarded entity for US tax purposes, a United States person for FBAR purposes?

Q. What is a United States person?

A "United States person" includes a citizen or resident of the United States, or a person in and doing business in the United States. The term "person" includes individuals and all forms of business entities, trusts, and estates.

Q. Who is considered to be doing business in the United States for FBAR reporting purposes?

A. Whether a person is considered, for FBAR purposes, to be in, and doing business in the United States is determined based on an analysis of the facts and circumstances of each case. Generally, a person is not considered to be in, and doing business in the United States unless that person is conducting business within the United States on a regular and continuous basis. Persons who are merely visiting the United States or who sporadically conduct business in the United States, are not in, and doing business in, the United States for FBAR reporting purposes. For example, a person who is not a citizen or resident of the United States and who is engaged in a business but who only occasionally visits the United States to meet customers or business associates would not be in, and doing business in the United States for FBAR reporting purposes.

Q. Would a foreign athlete or entertainer that occasionally visits the U.S. in order to compete or perform in an event, be considered a United States person for FBAR purposes?

A. Artists, athletes, and entertainers who are not citizens or residents of the United States and who only occasionally come to the United States to participate in exhibits, sporting events, or performances, do not have to file FBARs.

Q. A person is a non-resident alien and only visits the United States to manage his personal interests, such as rental property. Does that person have to file an FBAR?

A. A person who is not a United States citizen or resident and who visits the United States to manage his personal investments, such as rental property, and conducts no other business, is not considered to be in, and doing business in, the United States for FBAR reporting purposes and does not have to file FBARs.

Q. A non resident alien who doesn't meet the 183 day test is a partner in a US partnership where the US partnership deals with rentals; must he file an FBAR?

A. With the October 2008 revision to the FBAR form and instructions, FBARs are now required by nonresidents who are in, and doing business in, the United States. Whether a person is a nonresident alien for tax purposes has no bearing on the person's FBAR reporting obligation. The domestic partnership may have to file FBARs if it has a financial interest in, or signature authority (or other authority that is comparable to signature authority), over a financial account that is located in a foreign country. Whether a person is considered to be in, and doing business in, the United States is determined based on an analysis of the facts and circumstances of each case. Generally, a nonresident is not considered to be in, and doing business in the United States for FBAR reporting purposes if he only holds a partnership interest in a domestic

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partnership.

Q. An American citizen, X, gives a person who is a citizen or resident of the U.S. power of attorney to X's Canadian bank accounts. X files an FBAR form annually. Does the power of attorney also need to file an FBAR?

A. Yes, because the power of attorney has signature or other authority over the accounts and because he is a U.S. person.

Q. A fiduciary who is a U.S. person has control as a trustee for an IRA with a foreign account. Should an FBAR be filed?

A. Yes, because the fiduciary is a U.S. person.

Q. Is a single member LLC, which is a disregarded entity for US tax purposes, a United States person for FBAR purposes?

A. Yes, the tax rules concerning disregarded entities do not apply with respect to the FBAR reporting requirement. FBARs are required under Title 31, not under any provision of the Internal Revenue Code.

References/Related Topics

- FAQs Regarding Report of Foreign Bank and Financial Accounts (FBAR) - Filing Requirements
- FAQs Regarding Report of Foreign Bank and Financial Accounts (FBAR) - Financial Accounts
- Report of Foreign Bank and Financial Accounts

FAQs Regarding Report of Foreign Bank and Financial Accounts (FBAR) - Financial Accounts

1. What is a financial account?
2. What's meant by the term “commingled funds”?
3. What does “maximum value of account” mean (for Box 15 on the FBAR)?
4. How do you determine the “highest value” in the account during the previous calendar year?
5. Is an FBAR required if the account generates neither interest nor dividend income?
6. Is an FBAR required for accounts maintained with financial institutions located in a foreign country if the accounts hold noncash assets, such as gold?
7. Does the term “other authority over a financial account” mean that a person, who has the power to direct how an account is invested, but who cannot make disbursements to the accounts, has to file an FBAR?
8. A N.Y. corporation owns a foreign company that has foreign accounts. The corporation will file an FBAR for the foreign company's accounts. Do the primary owners of the U.S. Company also have to file?
9. A company has over 25 foreign accounts. What should they enter in Part II of the FBAR?
10. If a United States person holds a partnership interest in a hedge fund that is located in the United States but that owns foreign financial accounts, must the United States person report his interest in a hedge fund on an FBAR, assuming the United States person does not hold more than a 50% partnership interest in the hedge fund?
11. What are the exceptions to the FBAR filing requirement?

Q. What is a financial account?

A. A “financial account” includes any bank, securities, securities derivatives or other financial instruments accounts. The term includes any savings, demand, checking, deposit, or any other account maintained with a financial institution or other person engaged in the business of a financial institution. Individual bonds, notes, or stock certificates held by the filer are not a financial account nor is an unsecured loan to a foreign trade or business that is not a financial institution.

Q. What's meant by the term “commingled funds”?

A. The reference to “commingled fund” appears in the definition, in the instructions for the FBAR, for the term “financial account.” The instructions state that the term “financial account” generally encompasses accounts in which the assets are held in a commingled fund and the account owner holds an equity interest in the fund. An example of such a commingled fund account would be a mutual fund account.

Q. What does “maximum value of account” mean (for Box 15 on the FBAR)?

A. The maximum value of account is the largest amount of currency and non-monetary assets that appear on any

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quarterly or more frequent account statements issued for the applicable year. If periodic account statements are not issued, the maximum account value is the largest amount of currency or non-monetary assets in the account at any time during the year. Convert foreign currency by using the official exchange rate at the end of the year. The value of stock, other securities or other non-monetary assets in an account reported on TD F 90-22.1 (PDF) is the fair market value at the end of the calendar year. If the asset is withdrawn from the account, the value is the fair market value at the time of the withdrawal.

Q. How do you determine the "highest value" in the account during the previous calendar year?

A. The FBAR instructions state that the maximum value of an account is the largest amount (not the average amount) that appears on periodic account statements that are issued at least quarterly. If the financial institution does not issue periodic account statements, then the maximum value is the largest amount of cash and non-monetary assets that were in the account at any time during the year.

Q. Is an FBAR required if the account generates neither interest nor dividend income?

A. Yes, an FBAR must be filed whether or not the foreign account generates any income.

Q. Is an FBAR required for accounts maintained with financial institutions located in a foreign country if the accounts hold noncash assets, such as gold?

A. Yes. An account with a financial institution that is located in a foreign country is a financial account for FBAR purposes whether the account holds cash or non-monetary assets.

Q. Does the term "other authority over a financial account" mean that a person, who has the power to direct how an account is invested, but who cannot make disbursements to the accounts, has to file an FBAR?

A. No, an FBAR is not required because the person has no power of disposition of money or other property in the account.

Q. Must a U.S. person file an FBAR on a Eurodollar account in the Cayman Islands?

A. Yes, the Cayman Islands account is a foreign account.

Q. A N.Y. corporation owns a foreign company that has foreign accounts. The corporation will file an FBAR for the foreign company's accounts. Do the primary owners of the U.S. Company also have to file?

A. Yes, if any owner directly or indirectly owns more than 50 percent of the total value of the shares of stock, that owner will have to file an FBAR.

Q. A company has over 25 foreign accounts. What should they enter in Part II of the FBAR?

A. If the filer holds a financial interest in more than 25 accounts, check the yes box in item 14 and indicate the number of accounts in the space provided. Do not complete any further items in Part II or Part III of the report. Sign the form in item 44/45 and enter the date signed in item 46. Any person who lists more than 25 accounts in item 14 must provide all the information called for in Part II and Part III when requested by the Department of the Treasury.

Q. If a United States person holds a partnership interest in a hedge fund that is located in the United States but that owns foreign financial accounts, must the United States person report his interest in a hedge fund on an FBAR, assuming the United States person does not hold more than a 50% partnership interest in the hedge fund?

A. Generally, no. If the hedge fund is located in the United States, a financial interest in the hedge fund is not an interest in a foreign financial account for FBAR reporting purposes, even though the hedge fund may have foreign operations. If the domestic partnership has a financial interest in a foreign financial account, then it may have to file an FBAR. If a United States person who is an officer, employee, or partner of the partnership has a financial interest in, or signature or other authority over a foreign financial account, then that person may also have to file an FBAR. If a partner owns an interest in more than 50 percent of the profits of the partnership (distributive share of income, taking into account any special allocation agreement) or more than 50 percent of the capital of the partnership, then that partner has a financial interest, for FBAR reporting purposes, in the foreign financial accounts of the partnership and may have to file an FBAR.

Q. What are the exceptions to the FBAR filing requirement?

A. Accounts in U.S. military banking facilities, operated by a United States financial institution to serve U.S. Govern-

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ment installations abroad, are not considered as accounts in a foreign country. For this reason, these accounts do not have to be reported on an FBAR.

An officer or employee of a bank which is subject to the Supervision of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, the Office of Thrift Supervision, or the Federal Deposit Insurance Corporation need not report that he has signature or other authority over a foreign bank, securities or other financial account maintained by the bank, if the officer or employee has NO personal financial interest in the account.

An officer or employee of a domestic corporation whose equity securities are listed on a national securities exchange or which has assets exceeding $10 million and 500 or more shareholders of record, need not file a report concerning the other signature authority over a foreign financial account of the corporation, if he has NO personal financial interest in the account and he has been advised, in writing, by the chief financial officer of the corporation that the corporation has filed a current report, which includes that account.

References/Related Topics

- FAQs Regarding Report of Foreign Bank and Financial Accounts (FBAR) - Filing Requirements
- FAQs Regarding Report of Foreign Bank and Financial Accounts (FBAR) - United States Person
- Report of Foreign Bank and Financial Accounts

FAQs Regarding Report of Foreign Bank and Financial Accounts (FBAR) - Filing Requirements

1. What is an FBAR?
2. Who must file an FBAR?
3. What is a foreign country?
4. What constitutes signature or other authority over an account?
5. Is an FBAR required by a US resident with elderly parents in Canada who has a power of attorney on accounts in Canada, but never exercised it?
6. How do foreign account holders report their accounts to the IRS?
7. Form 1040NR does not require a Schedule B. If the person filing the form has foreign accounts, must he now attach a Schedule B to his return?
8. When is the FBAR due?
9. Where are FBAR forms available?
10. Is there a help line for questions about completing the form?
11. Where do account holders file the FBAR?
12. How does an FBAR filer amend a previously filed FBAR?
13. What is the statute of limitations for assessing civil penalties for violations of the FBAR requirements?
14. Can cumulative FBAR penalties exceed the amount in a taxpayer's foreign accounts?
15. How long should account holders retain records of the foreign accounts?
16. What happens if an account holder is required to file an FBAR and fails to do so?
17. For filing FBARs for prior years, should the current FBAR form be used or should the previous version of the form be used?
18. Does more than one form need to be filed for a husband and wife owning a joint account?
19. Does the IRS have an email address to send questions regarding the FBAR?

Q. What is an FBAR?

A. An FBAR is a Report of Foreign Bank and Financial Account. The form number is TD F 90-22.1 (PDF).

Q. Who must file an FBAR?

A. Any United States person who has a financial interest in or signature authority, or other authority over any financial account in a foreign country, if the aggregate value of these accounts exceeds $10,000 at any time during the calendar year

Q. What is a foreign country?

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A. A “foreign country” includes all geographical areas outside the United States, the Commonwealth of Puerto Rico, the Commonwealth of the Northern Mariana Islands, and the territories and possessions of the United States (including Guam, American Samoa, and the United States Virgin Islands).

Q. What constitutes signature or other authority over an account?

A. A person has signature authority over an account if such person can control the disposition of money or other property in it by delivery of a document containing his or her signature (or his or her signature and that of one or more other persons) to the bank or other person with whom the account is maintained.

Other authority exists in a person who can exercise power that is comparable to signature authority over an account by direct communication to the bank or other person with whom the account is maintained, either orally or by some other means.

Q. Is an FBAR required by a US resident with elderly parents in Canada who has a power of attorney on accounts in Canada, but never exercised it?

A. Yes, if the power of attorney gives the U.S. resident signature authority, or other authority comparable to signature authority, over the financial accounts. Whether or not such authority is ever exercised is irrelevant to the FBAR filing requirement.

Q. How do foreign account holders report their accounts to the IRS?

A. The holders report their foreign accounts by completing boxes 7a and 7b on Form 1040 Schedule B and completing Form TD F 90-22.1 (PDF).

Q. Form 1040NR does not require a Schedule B. If the person filing the form has foreign accounts, must he now attach a Schedule B to his return?

A. At present, there is no requirement to attach a Form 1040 Schedule B to Form 1040NR. A person filing a Form 1040NR is not required to attach Schedule B to his return.

Q. When is the FBAR due?

A. The FBAR is due by June 30th of the year following the year that the account holder meets the $10,000 threshold. The granting, by IRS, of an extension to file Federal income tax returns does not extend the due date for filing an FBAR. There is no extension available for filing the FBAR.

If an account holder does not have all the available information to file the return by June 30th, they should file as complete a return as they can and amend the document when the additional or new information becomes available.

Q. Where are FBAR forms available?

A. FBAR forms are available:

- On the IRS.gov (PDF) Web site.
- On the Department of the Treasury's Financial Crimes Enforcement Network Web site for Money Services Businesses.
- By calling IRS at (800) 829-3676.

Q. Is there a help line for questions about completing the form?

A. You can get answers to questions concerning the FBAR form by calling (800) 800-2877, option 2.

Q. Where do account holders file the FBAR?

A. Send completed forms to:

U.S. Department of the Treasury
P.O. Box 32621
Detroit, MI 48232-0621

The FBAR is not to be filed with the filer's Federal tax return.

Q. How does an FBAR filer amend a previously filed FBAR?

A. FBAR filers can amend a previously filed FBAR by:

- Checking the Amended box in the upper right hand corner of the first page of the form;

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- Making the needed additions or correction;
- Stapling it to a copy of the original FBAR; and
- Attaching a statement explaining the changes.

Q. What is the statute of limitations for assessing civil penalties for violations of the FBAR requirements?

A. Civil penalties can be assessed anytime up to six years after the date of the violation.

Q. Can cumulative FBAR penalties exceed the amount in a taxpayer's foreign accounts?

A. Yes, under the penalty provisions found in 31 U.S.C. 5314(a)(5), it is possible to assert civil penalties for FBAR violations in amounts that exceed the balance in the foreign financial account.

Q. How long should account holders retain records of the foreign accounts?

A. Records of accounts required to be reported on an FBAR must be retained for a period of five years. Failure to maintain required records may result in civil penalties, criminal penalties, or both.

Q. What happens if an account holder is required to file an FBAR and fails to do so?

A. Failure to file an FBAR when required to do so may potentially result in civil penalties, criminal penalties, or both. If you learn you were required to file FBARs for earlier years, you should file the delinquent FBAR reports and attach a statement explaining why the reports are filed late. No penalty will be asserted if the IRS determines that the late filings were due to reasonable cause. Keep copies, for your record, of what you send.

Q. For filing FBARs for prior years, should the current FBAR form be used or should the previous version of the form be used?

A. The current FBAR form (revised in October 2008) may be used to report a financial interest in, or signature or other authority over, financial accounts that were maintained in years prior to 2008. However, since the changes to the current FBAR form reflect a change in the reporting requirements, the instructions for the prior version of the FBAR form (revised in July 2000) may be relied upon for the purpose of determining the filing requirements for properly reporting financial accounts maintained in calendar years prior to 2008.

Q. Does more than one form need to be filed for a husband and wife owning a joint account?

A. No, if the names and social security numbers of the joint owners are fully disclosed on the filed FBAR. A spouse having a joint financial interest in an account with the filing spouse should be included as a joint account owner in Part III of the FBAR. The filer should write (spouse) on line 26 after the last name of the joint spousal owner. If the only reportable accounts of the filer's spouse are those reported as joint owners, the filer's spouse need not file a separate report. If the accounts are owned jointly by both spouses, the filer's spouse should also sign the report. It should be noted that if the filer's spouse has a financial interest in other accounts that are not jointly owned with the filer or has signature or other authority over other accounts, the filer's spouse should file a separate report for all accounts including those owned jointly with the other spouse.

Q. Does the IRS have an email address to send questions regarding the FBAR?

A. You can send questions concerning the FBAR to FBARquestions@irs.gov. The email system does not accept actual FBAR reports.

References/Related Topics

- FAQs Regarding Report of Foreign Bank and Financial Accounts (FBAR) - United States Person
- FAQs Regarding Report of Foreign Bank and Financial Accounts (FBAR) - Financial Accounts
- Report of Foreign Bank and Financial Accounts

Report of Foreign Bank and Financial Accounts

Do You Have a Foreign Financial Account?

If you own or have authority over a foreign financial account, including a bank account, brokerage account, mutual fund, unit trust, or other types of financial accounts, then you may be required to report the account yearly to the Internal Revenue Service. Under the Bank Secrecy Act, each United States person must file a Report of Foreign Bank and Financial Accounts (FBAR), if

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1. The person has a financial interest in, or signature authority (or other authority that is comparable to signature authority) over one or more accounts in a foreign country, and

2. The aggregate value of all foreign financial accounts exceeds $10,000 at any time during the calendar year.

A United States person is not prohibited from owning foreign accounts. The FBAR is required because foreign financial institutions may not be subject to the same reporting requirements as domestic financial institutions. The FBAR is a tool to help the United States government identify persons who may be using foreign financial accounts to circumvent United States law. Investigators use FBARs to help identify or trace funds used for illicit purposes or to identify unreported income maintained or generated abroad.

Definition of Terms

A "United States person" includes a citizen or resident of the United States, or a person in and doing business in the United States. Whether a person is considered, for FBAR purposes, to be in, and doing business in the United States is determined based on an analysis of the facts and circumstances of each case. Generally, a person is not considered to be in, and doing business in the United States unless that person is conducting business within the United States on a regular and continuous basis. Persons who are merely visiting the United States or who sporadically conduct business in the United States, are not in, and doing business in, the United States for FBAR reporting purposes.

A foreign country includes all geographical areas outside the United States, the Commonwealth of Puerto Rico, the Commonwealth of the Northern Mariana Islands, and the territories and possessions of the United States (including Guam, American Samoa, and the United States Virgin Islands).

Reporting and Filing Information

A person who holds a foreign account may have a reporting obligation even though the account produces no taxable income. Checking the appropriate block on Form 1040 Schedule B, and filing Form TD F 90-22.1, Report of Foreign Bank and Financial Accounts, satisfies the account holder's reporting obligation.

A foreign account holder must mail the Form TD F 90-22.1 on or before June 30 of the following year to:

U.S. Department of the Treasury
P.O. Box 32621
Detroit, MI 48232-0621.

The FBAR is not to be filed with the filer's Federal income tax return.

The granting, by IRS, of an extension to file Federal income tax returns does not extend the due date for filing an FBAR. There is no extension available for filing the FBAR.

Account holders who do not comply with the FBAR reporting requirements may be subject to civil penalties, criminal penalties, or both.

Exceptions to the Reporting Requirement

There are exceptions to the reporting requirement. These exceptions include:

1. Accounts in U.S. military banking facilities operated by a United States financial institution to serve U.S. Government installations abroad are not considered to be accounts in a foreign country for purposes of the reporting requirement.

2. An officer or employee of a bank that is subject to the supervision of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, the Office of Thrift Supervision, or the Federal Deposit Insurance Corporation, is not required to report having signature or other authority over a foreign account if the officer or employee has no personal interest in the account.

3. An officer or employee of a domestic corporation whose equity securities are listed on a national securities exchange or which has assets exceeding $10 million and 500 or more shareholders of record, is not required to report having signature or other authority over a foreign account if the person has no personal financial interest in the account, and the officer or employee has been advised in writing by the chief financial officer of the corporation that the corporation has filed a current report that includes the foreign account.

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FBAR Assistance

Help in completing Form TD F 90-22.1 (PDF) is available at (800) 800-2877, option 2. The form is available online at IRS.gov and MSB or by telephone at (800) 829-3676. Questions regarding the FBAR can be sent to FBARquestions @irs.gov.

References/Related Topics

- Workbook on the Report of Foreign Bank and Financial Accounts (FBAR)
- FAQs regarding Report of Foreign Bank and Financial Accounts (FBAR)
- Bank Secrecy Act
- Small Business Video and Audio Presentations

Rate the Small Business and Self-Employed Web Sjte

Date: 6/5/09

Part IV — Items of General Interest

Temporary Suspension of FBAR filing Requirements for Persons who are not Citizens, Residents, or Domestic Entities

Announcement 2009-51

The Internal Revenue Service is temporarily suspending the reporting requirement with respect to foreign bank accounts (Form TD F 90.22-1 (Report of Foreign Bank and Financial Accounts)) due on June 30, 2009, for those persons who are not citizens, residents, or domestic entities. The revised Form TD F 90.22-1 (October 2008) was issued with a change in the instructions to the definition of "United States person." The IRS has received a number of questions and comments from the public concerning the new filing requirement that may require additional guidance.

To reduce the burden on the public with respect to FBARs due on June 30, 2009, all persons may rely on the definition of "United States person" found in the instructions for the prior version of the FBAR (the July 2000 version) to determine whether they have an obligation to file an FBAR. The definition of "United States person" from the prior version is as follows:

> **United States Person** The term "United States person" means (1) a citizen or resident of the United States, (2) a domestic partnership, (3) a domestic corporation, or (4) a domestic estate or trust.

The definition of the term "United States person" from the instructions for the prior version of the FBAR form may be relied upon for purposes of determining who must file an FBAR. All other requirements of the current version of the FBAR form and instructions (revision October 2008) are still in effect. The current version of the form must be used when filing an FBAR.

The substitution of the definition of "United States person" from the instructions for the prior version of the FBAR applies only with respect to FBARs due on June 30, 2009. Additional guidance will be issued with respect to FBARs due in subsequent years.

The Service invites interested persons to submit comments regarding the revised FBAR form and instructions (revision October 2008). Please submit comments by August 31, 2009 to: Internal Revenue Service, CC:PA:LPD:PR (Announcement 2009-51), room 5203, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044. Submissions also may be hand delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to: CC:PA:LPD:PR (Announcement 2009-51), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue N.W., Washington, DC. Alternatively, taxpayers may submit electronic comments directly to the IRS e-mail address: notice.comments@irscounsel.treas.gov (attention: Announcement 2009-51).

The principal author of this announcement is Adrienne Mikolashek of the Office of Associate Chief Counsel (Procedure and Administration). For further information regarding this announcement contact Adrienne Mikolashek at 202-622-4940 not a toll-free call).

Part I

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TABLE

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This form should be used to report a financial interest in, signature authority, or other authority over one or more financial accounts in foreign countries, as required by the Department of the Treasury Regulations (31 C m 103). No report is required if the aggregate value of the accounts did not exceed $10,000. **See Instructions For Definitions,**

PRIVACY ACT AND PAPERWORK REDUCTION ACT NOTICE

Pursuant to the requirements of Public Law 93-579 (Privacy Act of 1974), notice is hereby given that the authority to collect information on TD F 90' 22.1 in accordance with 5 USC 552a (e) is Public Law e1-50e; 31 4Jno5314; 5 USC 301; 31 CFR 103.

The principal purpose for collecting the information is to assure maintenance of reports where such reports or records have a high degree of usefulness in criminal, tax, or regulatory investigations or proceedings. The information collected may be provided to those officers and employees of any constituent unit of the Department of the Treasury who have a need for the records in the performance of their duties. The records be referred to any other department or agen of the United States upon the request the head of such department or agency for use in a criminal, tax, or regulatory investigation or proceeding. The information collected may also be provided to appropriate state, local, and foreign law enforcement and regulatory personnel in the performance of their official duties. Disclosure of this information is mandatory. Civil and criminal penalties, including in certain 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. Disclosure of the Social Security number is mandatory. The authority to collect is 31 CFR 103. The Social Security number will be used as a means to identify the individual who files the report.

The estimated average burden associated with this collection of information is 20 minutes per respondent or record keeper, depending on individual circumstances. Comments regarding the accuracy of this burden estimate, and suggestions for reducing the burden should be directed to the Internal Revenue Service, Bank Secrecy Act Policy, 5000 Ellin Road C-3-242. Lanham MD 20706.

TABLE

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Part III

TABLE

TABULAR OR GRAPHIC MATERIAL SET FORTH AT THIS POINT IS NOT DISPLAYABLE

Part IV

TABLE

TABULAR OR GRAPHIC MATERIAL SET FORTH AT THIS POINT IS NOT DISPLAYABLE

General Instructions

Who Must File this Report. Each 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, must report that relationship each calendar year by filing this report with the Department of the Treasury on or before dune 30, of the succeeding year.

Exceptions

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An officer or employee of a bank which is currently examined by Federal bank supervisory agencies for soundness and safety need not report that he has signature or other authority over a foreign bank, securities or other financial account maintained by the bank, if the officer or employee has NO personal financial interest in the account.

An officer or employee of a domestic corporation whose equity securities are listed upon any United States national securities exchange or which has assets exceeding $10 million and has 500 or more shareholders of record need not file such a report concerning signature or other authority over a foreign financial account of the corporation, if he has NO personal financial interest in the account and he has been advised in writing by the chief financial officer or similar responsible officer of the corporation that the corporation has filed a current report, *which* includes that account. An officer or employee of a domestic subsidiary of such a domestic corporation need not file this report concerning signature or other authority over the foreign financial account if the domestic parent meets the above requirements, he has no personal financial interest in the account, and he has been advised in writing by the responsible officer of the parent that the subsidiary has filed a current report which includes that account. If a United States subsidiary is named in a consolidated FBAR of the parent, the subsidiary will be deemed to have filed a report for purposes of this exception. An officer or employee of a foreign subsidiary more than 5096 owned by such edomestin corporation need not file this report concerning signature or other authority over the foreign financial account if the employee or officer has no personal financial interest in the account, and he has been advised in writing by the responsible officer of the parent that the parent has filed a current report which includes that account.

General Definitions

United States Person. The term “United States person” meanaa citizen or resident of the United States, or a person in and doing business in the United States. See 31 C.F.R. 103.11(z) for a complete definition of “person.” The United States includes the states, territories and possessions of the United States, See the definition of United States at 31 C.F.R. 103.11(nn) for a complete definition of United States. 8foreign subsidiary of a United States person is not required to file this report, although its United States parent corporation m be required to do so. A branch of a foreign entity that is doing business in the United States is required to file this report even if not separately incorporated under U.S. law.

Financial Account. This term includes any bank, o*ouhUom, securities derivatives or other financial instruments accounts. Such accounts generally also encompass any accounts in which the assets are held in a commingled fund, and the account owner holds an equity interest in the fund (including mutual funds). The term also means any savings, demand, checking, deposit, time deposit, or any other account (including debit card and prepaid credit card accounts) maintained with a financial institution or other person engaged in the business of a financial institution. Individual bonds, notes, or stock certificates held by the filer are not a financial account nor is an unsecured loan to a foreign trade or business that is not a financial institution.

Account in a Foreign Co

all geographical areas located outside the United States. See “United States Person” above 31 C.F.B. 103,11(nn)fora definition of United States. The geographical location of the account, not the nationality of the financial entity institution in which the account is found determines whether it is in an account in afornign country. Report any financial account (except a military banking facility) that is located in a foreign ouuntry, even if it is held at an affiliate of a United States bank or other financial institution. Do not report any account maintained with a branch, agency, or other office of a foreign bank of other institution that is located in the United States.

Military Banking Facility. Do not consider as an account in a foreign uovntry, an account in an institution known as a “United States military banking facility” (or “United States i! bmi!) omoia! institution designated by the United States Government to serve U.S. Government installations abroad, even if the United States military banking facility is located in a foreign Country, is not an account in a foreign country.

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Financial Interest. A financial interest in a bank, securities, or other financial account in ofomign country means an interest described in one of the following three paragraphs:

1. 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.

2. A United States person has a financial interest in each bonh, aeouhtioo, or other financial account in a foreign country for which the owner of record or holder of legal title is: (a) a person acting as an agent, nominee, attorney, or in some other capacity on behalf of the U.S. person; (b) a corporation in which the United States person owns directly or indirectly more than 50 percent of the total value of shares of stock or more than 50 percent of the voting power for all shares of stock; (c) eportnanahip in which the United States person owns an interest in more than 50 percent of the profits (distributive share of income, taking into account any special allocation agreement) or more than 50 percent of the capitel of the partnership; or (d) etruot in which the United States person either has a present beneficial interest, either directly or indirectly, in more than 50 percent of the assets or from which such person receives more than 50 percent of the current income.

3. A United States person has a 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 trust, or a person acting on behalf of a trust, that was established by such United States person and for which a trust protector has been appointed. A trust protector iaa 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.

Correspondent or "nostro" accounts (international interbank transfer accounts) maintained by banks that are used solely for the purpose of bank-to-bank settlement need not be reported on this form, but are subject to other Bank Secrecy Act filing requirements. This exception is intended to encompass those accounts utilized for bank-to-bank settlement purposes only.

Signature or Other Authority Over an Account. A person has signature authority over an account if such person can control the disposition of money or ether property in it by delivery of a document containing his or her signature (or his or her signature and that of one or more other persons) to the bank or other person with whom the account is maintained. Other authority exists in a person who can exercise comparable power over an account by communication with the bank or other person with whom the account is maintainmj, either directly or through an agent, nominee, attorney, or in some other capacity on behalf of the Q.S. person, either orally or by some other means.

Filing Information-Do NOT file with your Federal Income Tax Return

When and where to file. This report must be filed on or before June 30 of the year following the calendar year reported. The report is required annually. File by mailing this report to the Department of the Treasury, Post Office Box 32621 Detroit, K4! 48282-0021, or by hand-carrying it to any local office of the Internal Revenue Service for forwarding to the Department of the Treasury, Detroit, MI. Tax attaches are located in the US. embassies in some countries. A filer can receive instructions for verifying that a report has been filed by calling the Detroit Computing Center Hotline at 1-800-800-2877.

Extensions of time to file federal tax returns do not extend the time for filing this report. **There is no extension of time available for filing this report.** If a delinquent FBAR is filed, also attach a statement explaining the reason for the late filing. See "When and where to file" (above) for filing instructions.

An amendment of a previously filed FBAR is accomplished by checking the "Amended" box in the upper right hand corner of the first page of the form, making the needed additions or corrections, and then stapling it to a copy of the original form. Please also attach a statement explaining the changes. See "When and where to file" (above) for filing instructions. **Record Keeping Requirements**. If this Report is required, certain records must be retained. Such records

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must contain the name in which each such account is maintained, the number or other designation of such account, the name and address of the foreign bank or other person with whom such account is maintained, the type of such account, and the maximum value of each account during the reporting period. Retaining filed copies of this report will help to meet these reguirementsi The records must be retained for a period of five years and must kept at all times available for inspection as provided by law.

Explanations for Specific Items

Part I

Item 1. The Report of Foreign Bank and Financial Accounts (FBAR) is an annuel report. Enter the calendar year being reported.

Amendment of a previously filed FBAR is accomplished by checking the “Amended” box in the upper right hand corner of the first page of the form, making the needed additons and ooneoiona, and then stapling it to a copy of the original report. See “When and where to file” (above) for filing instructions.

Item 2. Check the appropriate box describing the filer. A corporation which owns directly or indirectly more than a 50 percent interest in one or more other entities required to file this Report will be permitted to file a consolidated report on TD F 90-22.1, on behalf of itself and such other entitiesi

Check box “d” in Item 2 and complete Part V. Consolidated reports should be signed by an authorized official of the parent corporation. Trusts and other entities, including tax-exempt organizations, should check box “e” and describe the filer on the line following box “e.”

Item 3. A filer should provide the filer's taxpayer identification number. Generally this is the filer's U.S. social security number (SSN) or employer identification number (EIN). Numbers should be entered with no spaces, dooheo, mother punctuation throughout this report. If the filer does not possess such U.S. identification, the filer should complete Item 4.

Item 4. Complete Item 4 only if the filer has no U.S. taxpayer identification number. Item 4 requires the filer to provide the information about an official foreign government document evidencing the filer's nationality or residence. The filer should write in the document number followed by the country of issuance. The filer may check off the type of document. If “othmv^' is checked, the filer should write in the type of document. For example, an individual who is not a U.S. citizen would providoa passport numbar, the name of the country of issuance, and check off “passport.”

Item 5. Enter the date of birth of the filer using the month, day, and year convention.

Items 6, 7 and 8. Enter the name of the filer. Ap organization should enter its name in the Last Name space,

Items 9, 10, 11, 12 and 13. Enter the address of the filer. An individual filer residing in the United States should enter the street address of filer's United States residence, not a post office box. An individual filer residing outside the United States should enter the filer's United States mailing address. If the filer has no U.S. mailing address the filer may provide a foreign address. An organization should enter its United States mailing address.

Item 14. If the filer has afinenoia! interest in 25 or more foreign financial accounts, the filer should check the yes box, sign and date the report (Items 44, 45 and 46) and leave blank Part II (Continuation of Separate Accounts) or Part III (Joint Accounts) of the report. If the group of entities covered by a consolidated report has a financial interest in 25 or more foreign financial accounts, the reporting parent corporation need only complete Part V (for consolidated reporting) Items 34 through 42, for the identity information of the account owners, but need not complete the account information. Detailed information about each account, including all information called for on this naport, must be recorded and retained for five years from June 30 of the year following the Calendar year reported. Any person who reports 25 or more foreign financial accounts must provide all the information omitted from Part II, III or V as appropriate.

Part II

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Item 15. Provide the maximum value of the account during the calendar year being reported. The maximum value of an account is the largest amount of currency or non-monetary assets that appear on any quarterly or more frequent account statement issued for the applicable year. If periodic account statements are not issued, the maximum account asset value is the largest amount of currency and non-monetary assets in the account at any time during the year. Convert foreign currency by using the official exchange rate at the end of the year. In valuing currency of a country that uses multiple exchange rates, use the rate which would apply if the currency in the account were converted into United States dollars at the close of the calendar year. The value of stock, other securities, or other non-monetary 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. For purposes of Item 15, if the filer had a financial interest in more than one account, each account is to be valued separately in accordance with the foregoing two paragraphs. If the filer had a financial interest in one or more but fewer than 25 accounts, and is unable to determine whether the maximum value of these accounts exceeded $10.000 at any time during the year, complete Part II, III, or V for each of these accounts and enter "value unknown" in Item 15 for these accounts.

Item 16. Indicate the type of account. If "Other" is selected describe the account.

Item 17. Provide the name of the financial institution with which the account is held.

Item 18. Provide the account number which the financial institution uses to designate the account.

Item 19-23. Provide the complete mailing address of the financial institution where the account is located. If the foreign state or poatal code is not known leave them blank,

Part III

Item 24. Enter the number of joint owners for the account. If the exact number is not known, provide an estimatei In determining the number of joint owners, the filer is not counted.

Items 25-33. Enter this identity information about the joint owner. If there is more than one joint owner, enter the identity information about the principal joint owner. The filer may leave blank items for which no information is available. A spouse having a joint financial interest in an account with the filing spouse should be included as a joint account owner in Part III of this report. The filer should write (spouse) on Line 26 after the last name of the loint upounal mwner. \f\he only reportable accounts of the filer's spouse are those reported as joint accounts, the filer's spouse need not file a separate report. If the accounts are owned jointly by both spouses, the filer's spouse should also sign the report. See the instructions for Item 44. If the filer's spouse has a financial interest in other accounts that are not jointly owned with the filer or has signature or other authority over other accounts, the filer's spouse should file a separate report for all accounts including those owned jointly with the other spouse.

Part IV—'No Financial Interest in Account

Items 34-42. You must provide the name, address, and identifying number of the owner of a foreign financial account over which you had signature or other authority but no finunnial interest in the account. If there is more than one owner of thaccount over which you have authority, providethe information in items 34-43 for the primary owner for which you have authority. If you complete the account information for more than one account of the same owner, you need identify the owner only once. Write "Same Owner" in Item 34 for the succeeding accounts of the same owner.

Item 43. Enter filer's title for the position which gives him authority over the account,

Part V-Consolidated Report for Corporate Parent & Subsidiary Corporations

Aoonpooation which owns directly or indirectly more than a 50 percent interest in one or more other entities required to file this report will be permitted to file a consolidated report on TO F 90-22.1, on behalf of itself and such other entit-

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ies. Check box “d” in Item 2 in Part } and complete Part V.

Items 34-42. You must provide the corporate name, identifying number and address of the owner of the foreign financial account as shown on the books of the financial institution.

If you complete the account information for more than one account of the same owner you need identify the owner only once. Write “Same Owner” in Item 34 for the succeeding accounts of the same owner.

Signatures

This report must be signed by the person named in Part I. If the report is being filed on behalf of a partnership, corporation, fiduciary or other legal entity, it must be signed by an authorized individual. Consolidated reports should be signed by an authorized official of the parent corporation. Enter the title of the individual signing for a legal entity, such as acorpon[9]ion, which is shown as the filer. A spouse included as a joint owner, who elects not to file a separate report in accordance with the instructions in Part ill, must also sign this report. See the instructions for Part III.

Enter the title of the individuol signing for a legal entity, such as a corporation, which is shown as the filer. Leave “Filer's Title” blank if the filer is only reporting as an individual. An individual filing because of a financial interest in his individual accounts is filing as an individual. An individual filing because of signature or other authority over a foreign financial account is filing as an individual. If the filer only has signature authority over the account, he should enter his title in Part IV Item 43, Filer's Title with this Owner, to show his relationship to the account. Enter the actual date signed.

WASHINGTON ITEMS **The Climate of Current Thinking on New Developments**

Chief Counsel's Office Provides Guidance on the Foreign Bank and Financial Accounts Report (FBAR) Penalty

In CCA 200603026, the Chief Counsel's Office provided important guidance regarding the 31 USC §5321(a)(5) civil FBAR penalty for willful violations with respect to Offshore Credit Card Program and Last Chance Compliance Initiative cases. CCA 200603026 is the most significant guidance that the Chief Counsel's Office has released to the public since the IRS assumed responsibility for overseeing and enforcing FBARs under the Bank Secrecy Act (BSA) in April, 2003. *See* IRS News Release (IR-2003-48).

CCA 200603026 raised two issues of note, each with subordinate questions, and posited four scenarios for which guidance was sought. These issues concerned (1) the proper interpretation of the willfulness standard which determines whether a failure to file a report is subject to civil and criminal penalties, and (2) the status as offshore accounts of offshore credit card accounts that are not associated with bank accounts for deposits.

With respect to the first issue of “willfulness,” there were two questions. The first question was whether the phrase “willful violation (or willfully causes any violation)” has the same definition and interpretation under 31 USC §§5321 (the civil penalty) and 5322 (the criminal penalty). The Chief Counsel's Office answered that the phrase had the same meaning in both statutes.

The Chief Counsel's Office concluded that both §§5321(a)(5) and 5322(a) contain a similar “willfulness” requirement. Section 5321(a)(5) provides that “[t]he Secretary of the Treasury may impose a civil money penalty on any person who willfully violates, or any person willfully causing any violation of, any provision of section 5314.” Section 5322 provides that “[a] person willfully violating this subchapter [the Bank Secrecy Act] . . . or a regulation prescribed or order issued under this subchapter . . . shall be fined not more than $250,000, or imprisoned for not more than five years, or both.” The word “willful” is used in both of these sections. The Chief Counsel's Office explained that under principles of statutory construction, the same word used in related sections should be consistently construed.

The Chief Counsel's Office noted that there are no cases in which the issue presented is construing “willful” in the civil penalty context. Therefore, it relied on Justice Blackmun's dissent in *Ratzlaf v. U.S.*, 510 U.S. 135 (1994), a Supreme

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Court case that addressed the standard for willfulness in the context of a criminal violation of a structuring provision of the BSA, to find that in the case of the FBAR penalty, in order for there to be a voluntary intentional violation of a known legal duty, the account holder merely would have to have knowledge that he had a duty to file an FBAR, since knowledge of the duty to file an FBAR would entail knowledge that it is illegal not to file the FBAR. A corollary of this principle is that there is no willfulness if the accountholder has no knowledge of the duty to file the FBAR.

The Chief Counsel's Office concluded that cases involving willful FBAR violations generally will have to rely on circumstantial evidence, and that willfulness can be inferred where an entire course of conduct establishes the necessary intent.

A second question with respect to the willfulness issue was whether the criteria for assertion of the civil FBAR penalty are the same as the burden of proof that the IRS has when asserting the civil fraud penalty under §6663 (i.e., clear and convincing evidence). The Chief Counsel's Office found that although there are no cases that address this issue with respect to the civil FBAR penalty, the IRS expects that the clear and convincing evidence standard will apply because of the inherent difficulty of proving, or disproving, a state of mind (willfulness) at the time of a violation.

Another issue addressed by the Chief Counsel's Office was whether either a “secured” offshore credit card account or a credit card account in which large advance payments were made, resulting in positive balances in the account, can be a financial account for FBAR reporting purposes. The definition for “financial accounts” is contained in the instructions for filing the FBAR report. However, the instructions do not mention credit cards.

The Chief Counsel's Office explained that a secured credit card account can be secured by a separate deposit account, including a deposit account with a trust. The credit limit for a secured credit card account would typically be tied to the balance in the deposit account that is securing the credit card account. In such a situation, the deposit account would clearly be a “financial account” for FBAR purposes.

The Chief Counsel's Office also found that a debit card account is a financial account. If a card agreement requires that advance payments be made to cover anticipated charges, then the card is a debit card, not a credit card, and a debit card would be a financial account for FBAR purposes.

The Chief Counsel's Office advised that, generally, a credit card account would not be a financial account, because it is unclear whether the term “financial accounts” was intended to include credit card accounts. Therefore, it would generally not be appropriate to assert the FBAR penalty for a willful failure to report a credit card account with a foreign bank.

However, the Chief Counsel's Office advised that if by making advance payments, the card holder was using the credit card account as a debit card or a checking account, then one could argue, depending on the facts and circumstances, that the credit card account was a financial account for purposes of the FBAR penalty. Even if it is shown that a credit card account is a financial account, the IRS still would need to show that the accountholder willfully failed to report the account.

With respect to a deposit with a trust associated with the credit card account, although a card holder generally would not be required to file an FBAR with respect to the credit card account, the trust account (which if held as collateral for the credit card and earns interest for the card holder) does act as a deposit account and, therefore, can be considered a “financial account.” Further, the existence of this type of credit card account would be circumstantial evidence of the existence of the trust account, and the credit card statements would be helpful in estimating the minimum amount deposited in the trust account.

• For a more detailed discussion of this matter, see Tarr & Drucker, 634 T.M., *Civil Tax Penalties*.

Part 4. Examining Process

Chapter 26. Bank Secrecy Act

Section 7. Penalties

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4.26.7 Penalties

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- 4.26.7.6 Forfeiture Authority
- 4.26.7.7 Injunctive Relief
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4.26.7.1 (11-17-2006) Overview

1. The Bank Secrecy Act (BSA) as amended and related regulations at 31 CFR Part 103 provide for civil and criminal penalties as well as forfeiture of assets. BSA penalties depend on the type of entity, the type of activity involved, and the degree of intent. Apparent violations are found through examination or information from informants.
2. Although, generally, the BSA examiner does not propose penalties arising from the violations, the elements of each violation must be known in order to determine which facts are relevant to the examination process.

4.26.7.2 (11-17-2006) Penalty Authority

1. BSA civil examinations are conducted by BSA regulators. Final authority to assess civil penalties rests with the Secretary of the Treasury, 31 USC 5321, and is delegated to the Financial Crimes Enforcement Network (FinCEN), 31 CFR 103.56. Authority for IRS to examine certain financial institutions for compliance with 31 CFR 103 is delegated to the IRS, 31 CFR 103.56(b)(8). See Exhibit 4.26.1-1.
2. 31 CFR 103.56(c)(2) provides IRS Criminal Investigation (CI) with jurisdiction to investigate all criminal violations except those of 31 CFR 103.23 (Reports of Transportation of Currency or Monetary Instruments, CMIR). Customs investigates violations of the CMIR. 31 CFR 103.56(c)(1). Courts impose criminal penalties.

4.26.7.3 (11-17-2006) Civil Penalties

1. 31 USC 5321 provides overall civil penalty provisions for any violation of the BSA and for violations of certain related statutes. It provides authority for assessing penalties when regulations for those penalties have not been issued. The penalties apply to violations of the BSA itself, the regulations under the BSA, or any geographic targeting or special measures order issued by Treasury, as well as penalties for taking certain actions, such as structuring, with the intent to evade BSA reporting or recordkeeping requirements.
2. 31 CFR 103.57, which was issued under the authority of 31 USC 5321, is the primary penalty regulation. It addresses civil penalties arising from violations of the BSA reporting and recordkeeping requirements as well as structuring penalties.
3. Other Code provisions and regulations provide for civil penalties for violations of special BSA requirements. For example, 31 USC 5330 and 31 CFR 103.41(e) provide for civil penalties for failure to register a money services business.

4.26.7.3.1 (11-17-2006) Negligence

1. For each negligent violation of any requirement of the BSA, the penalty may not exceed $500. It is assessed only against financial institutions and nonfinancial trades or businesses. 31 USC 5321(a)(6); CFR 10357(H). A chart of negligent violations follows.

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C1-4**Negligent Violation Penalties**

Violation	Persons Subject to Penalty	Penalty	Authority
Negligent violation of any provision of the BSA or any regulation prescribed under the BSA	• Any financial institution or non-financial trade or business	Not more than $500	31 USC 5321(a)(6) 32 CFR 103.57(h)
Pattern of negligent violations of any provision of the BSA or any regulation prescribed under the BSA	• Any financial institution or non-financial trade or business	not more than $50,000	31 USC 5321(a), 31 CFR 103.57(h)

4.26.7.3.2 (11-17-2006) Willfulness

1. A penalty may be assessed upon a partner, director, officer or employee as well as the business for certain willful violations identified in section 5321(a) and against any person with respect to an FBAR reporting and recordkeeping violation. Where the violation is willful the penalty depends upon the type of violation. A chart of willful violation penalties follows:

C1-4**Willfulness Related Penalties**

Violation	Persons Subject to Penalty	Penalty	Authority
Failure to comply with any recordkeeping requirement for a financial institution except 31 CFR 103.32.	• Any domestic financial institution, and	Not to exceed $1,000.	31 USC 5321(a)(1), 31 CFR 103.57(c)
	• Any partner, director, officer, or employee.		
Failure to comply with requirements to report transportation of monetary instrument (CMIR) found in 31 USC 5316, 31 CFR 103.23.	Any person	Up to the amount of the currency or monetary instruments transported, mailed or shipped less any amount forfeited under the authority of 31 CFR 103.58.	31 USC 5321(a)(2), 31 CFR 103.57(f)
Failure to comply with any reporting requirement for financial institutions, including report retention requirements. Exceptions:	• Any domestic financial institution and	Not to exceed the greater of the amount involved in the transaction (not to exceed $100,000) or $25,000.	31 USC 5321(a)(1), 31 CFR 103.57(f)
• Failure to report a foreign account (FBAR) 31 USC 5314, 31 CFR 103.24.	• Any partner, director, officer, or employee.		

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• Failure to report a transaction with a foreign financial agency 31 U.S.C. 5315, 31 C.F.R. 103.25.			
Structuring transactions, or taking other actions in violation of 31 U.S.C. 5324 — that is, structuring transactions for the purpose of evading the requirement by financial institutions to file certain reports (such as CTRs) or to otherwise cause or attempt to cause a financial institution to not file certain reports, to file certain incorrect reports, or to not maintain certain records.	Any person.	• Not to exceed the amount of coins and currency involved in the transaction with respect to which such penalty is imposed. The amount of any civil penalty assessed shall be reduced by the amount of any forfeiture in connection with the transaction for which the penalty was imposed.	31 U.S.C. 5321(a)(4); 31 C.F.R. 103.57(e)
In the case of any person willfully violating, or willfully causing any violation of, any provision of section 5314- (Failure to report the existence of a foreign financial account or any identifying information required to be provided with respect to an account) or maintain related records under 31 CFR 103.32.	Any person.	For willful violations occurring prior to October 23, 2004, a penalty not to exceed the greater of	31 USC 5321(a)(5), 31 CFR 103.57(g)
		• An amount equal to the balance of the account at the time of the violation (not to exceed $100,000) or	
		• $25,000.	
		For willful violations occurring after October 22, 2004, the maximum penalty is increased to the greater of	
		• $100,000, or	

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		• 50 percent of the amount equal to the balance of the account at the time of the violation.	
Failure to report a transaction with a foreign financial agency required by 31 C.F.R. 103.25.	Specified financial institutions that are required to provide such reports by a regulation promulgated pursuant to 31 C.F.R. 103.25(a).	For willful violations occurring prior to October 23, 2004, a penalty not to exceed the greater of: • The amount (not to exceed $100,000) of the transaction or • $25,000. For willful violations occurring after October 22, 2004, the maximum penalty is increased to the greater of • $100,000, or • 50 percent of the amount of the transaction.	31 U.S.C. 5321(a)(5), 31 C.F.R. 103.57(g)
Failure to comply with a geographic targeting order issued under 31 USC 5326, 31 CFR 103.26.	• Any domestic financial institution and	The penalties are the same as those for recordkeeping and reporting violations in general.	31 USC 5321(a), 31 CFR 103.57
	• Any partner, director, officer, or employee.		
Failure to comply with any special measures order issued under 31 USC 5318A.	• Any domestic financial institution and	An amount equal to not less than 2 times the amount of the transaction but not more than $1,000,000.	31 USC 53219(a)(7), 31 CFR 103.57
	• Any partner, director, officer, or employee.		
Failure to comply with the information sharing rules required by Sec. 314 of the USA PATRIOT Act and found at 31 CFR 103 Subpart H.	• Any financial institution defined 31 CFR 103.110 and director, officer, or employee.	$25,000 per day.	31 USC 5321(a)(1), 31 CFR 103.57
Failure to establish a compliance program under 31 USC 5318(h) and various regulations appearing at 31 CFR Subpart I.	• Any financial institution required to establish a program and	$25,000	31 USC 5321(a)(1), 31 CFR 103.57
	• Any partner, director, of-		

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	ficer or employee.		
Failure to comply with due diligence requirements for banks, brokers and some other financial institutions set forth at 31 USC 5318(i) and at 31 CFR 103.181 - 183.	• Any financial institution or agency included in 31 USC 5218(i)	An amount equal to not less than 2 times the amount of the transaction, but not more than $1,000,000.	31 USC 5321(a)(7), 31 CFR 103.57

4.26.7.3.3 (11-17-2006) Failure to comply with MSB Registration

1. The failure to comply with the MSB registration requirement includes failure to retain a copy of the registration or agent list.
2. A person who fails to register as required by 31 CFR 103.41 is subject to a penalty of $5,000 per day whether or not the failure to register was willful.

Violation	Persons Subject to Penalty	Penalty	Authority
Failure to comply with any requirements of 31 USC 5330 or 31 CFR 103.41, that is registration of money services businesses. This includes failure to retain a copy of the registration or agent list.	Any person who is required to comply.	$5,000 per day	31 USC 5330(e), 31 CFR 103.41(e)
	The instructions to the registration form, FinCEN Form 107, define 'owner or controlling person' for purposes of responsibility to register to include, for a corporation, 'the largest single shareholder.' The instructions also provide that if two or more persons own equal numbers of shares of a corporation, they can enter into an agreement to determine who will register the corporation. See the instructions to Form 107 for additional information.		

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4.26.7.4 (11-17-2006) Determining Intent under the BSA

1. Civil penalties vary depending on intent. The BSA examiner must thoroughly document facts on the issue of intent. See IRM 4.26.9.
2. There is no overall definition of intent in the BSA. The common law (case law) definitions of negligence and intent must be used to establish which penalties may be appropriate for particular violation.

4.26.7.4.1 (11-17-2006) Negligence

1. Negligence is usually defined as the failure to use the care that a reasonable person would use in the same or similar circumstances.
2. There are two principal areas where a reasonable person would exercise care with respect to financial reporting and recordkeeping:
   - A reasonable businessman would normally exercise care to learn about legal requirements in his area of business.
   - A reasonable businessman would also exercise care to see that his business had sufficient internal controls to meet those requirements.
3. When care is not exercised in one or both of these areas, there is a case for negligence.

4.26.7.4.2 (11-17-2006) Civil Willfulness

1. Civil willfulness under the BSA is more than negligence.
2. Civil willfulness is established by evidence showing voluntary intentional violation of a known legal duty. If a person does not know of the legal duty but it can be shown that the person made conscious efforts to avoid learning of the duty, willfulness may be imputed under the concept of "willful blindness."

4.26.7.4.3 (11-17-2006) Establishing Willfulness

1. Two factors in establishing willfulness are:
   A. Knowledge of the law, and
   B. Knowledge of the facts.

4.26.7.4.3.1 (11-17-2006) Knowledge of the Law

1. An apparent violator's knowledge about applicable legal requirements may be an indicator of willfulness if those requirements are not met. Knowledge may be established in several ways.
2. Notification by IRS:
   - The Letter 1052 describes the requirements of most businesses in general. When receipt of the Letter 1052 has been acknowledged, knowledge is established.
   - Special mailings are good evidence of knowledge if controls have been set up for returned mail.
   - Educational visits where the financial institution signs that it has received information concerning BSA are proof of knowledge.
   - A prior compliance examination may prove knowledge.
3. Actions of the apparent violator:
   - The apparent violator previously filed reports.
   - The apparent violator may state that he was aware of the law.
   - The apparent violator's actions, such as structuring transactions to avoid the filing of Currency Transaction Reports

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(CTRs), may show that he was aware of the law.

4. Education by principals for whom the violator is acting as an agent. Many financial institutions have training programs to inform their agents about BSA reporting and recordkeeping requirements.

5. Education by the business community:

• Many businesses belong to business organizations, which have newsletters and handbooks relating to BSA requirements.

• Many businesses have legal and accounting professionals who may be advising them about their BSA responsibilities.

4.26.7.4.3.2 (11-17-2006) Knowledge of Facts

1. A showing of willfulness of the apparent violator that causes a failure to report or keep records is based on the facts and circumstances of each case.

2. Failure to Report: Evidence of willful failure to report may include:

A. Presentation of retained copies of reports that do not appear on the Currency and Banking Retrieval System (CBRS) database as filed.

B. Filings on some transactions but not on others, especially where the unreported transactions involved the same individual(s).

C. Failure to comply with AML requirements that leads to reporting or recordkeeping violations

3. Failure to Record: Evidence of willful failure to record includes:

A. Documentary evidence that the same individual conducted multiple transactions within a very short period of time so that it would have been clear to anyone that the transactions were related and triggered a recordkeeping requirement.

B. Evidence that the records were false and that the violator must have known, for example retention of a photocopied identification document, which differs from the information provided on the form.

C. Failure to comply with requirements that leads to reporting or recordkeeping violations

4. Evidence of personal relationships between the financial institution and the individual on whom the facts were not reported or recorded is also useful.

4.26.7.5 (11-17-2006) Criminal Penalties for Violation of Bank Secrecy Act

1. 31 USC 5322 and 31 CFR 103.59 provide for most Federal BSA criminal penalties. 18 USC 1960 provides for criminal penalties for certain money services businesses for failure to comply with the state licensing requirements or with the registration requirement for money services businesses under 31 USC 5330 and 31 CFR 103.41.

2. See CI's Law Enforcement Manual (LEM) for further information.

4.26.7.6 (11-17-2006) Forfeiture Authority

1. BSA criminal and civil forfeiture authority was moved by Sec. 372 of the USA PATRIOT Act from Title 18 to 31 USC 5317(c). 31 USC 5317(c) (2) provides for civil forfeiture proceedings. Any property involved in a violation of Section 5313 [currency reporting requirements], 5316 [exporting and importing monetary instruments], or 5324 [structuring] or any conspiracy to commit such violation, and any property traceable to any such violation or conspiracy, may be seized and forfeited to the United States. 31 CFR 103.58 provides regulatory authority for forfeiture in the case of a violation of 31 USC 5316 and 31 CFR 103.23 [exporting and importing monetary instruments]. The Secretary of the Treasury has discretionary authority to remit or mitigate the forfeiture.

2. Amounts seized and forfeited reduce penalties assessed for violation of the reporting requirements regarding exporting and importing monetary instruments, 31 USC 5321(a)(2), 31 CFR 103.57(d) and the structuring prohibitions, 31 USC

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5321(a)(4), 31 CFR 103.57(e).

4.26.7.7 (11-17-2006) Injunctive Relief

1. Authority to enjoin a BSA violation or to enforce compliance with the BSA is provided at 31 USC 5320. An injunction may be sought in cases in which the financial institution has taken inadequate steps to remedy a violation, or to remedy weaknesses in its anti-money laundering compliance program.
2. Authority for injunctive relief is specifically provided at 31 CFR 103.41(e) for failure to comply with the registration rules of 31 USC 5330 or the regulations under it at 31 CFR 103.41.

4.26.7.8 (11-17-2006) Rewards for Informants

1. An individual who provides original information that leads to recovery of a criminal fine, civil penalty, or forfeiture that exceeds $50,000 for a violation of the Bank Secrecy Act may be eligible for a reward, 31 USC 5323 and 31 CFR 103.62.
2. The reward may not exceed the lesser of $150,000 or 25% of the net amount collected. Generally officers and employees of the United States, state, or local governments are not eligible to collect the reward.

Section 16. Report of Foreign Bank and Financial Accounts (FBAR)

4.26.16 Report of Foreign Bank and Financial Accounts (FBAR)

- 4.26.16.1 FBAR Law Overview
- 4.26.16.2 FBAR Authorities
- 4.26.16.3 FBAR Filing Criteria
- 4.26.16.4 FBAR Penalties
- Exhibit 4.26.16-1 Pre-October 23, 2004 Normal FBAR Civil Penalty Mitigation Guidelines
- Exhibit 4.26.16-2 Normal FBAR Penalty Mitigation Guidelines for Violations Occurring After October 22, 2004
- Exhibit 4.26.16-3 Last Chance Compliance Initiative (LCCI) Penalty Mitigation Guidelines for FBAR Violations Occurring before October 23, 2004
- Exhibit 4.26.16-4 Last Chance Compliance Initiative (LCCI) Penalty Mitigation Guidelines for FBAR Violations Occurring After October 22, 2004.

4.26.16.1 (07-01-2008) FBAR Law Overview

1. The Report of Foreign Bank and Financial Accounts, TD F 90-22.1, (FBAR), is required when a U.S. Person has a financial interest in or signature authority over one or more foreign financial accounts with an aggregate value greater than $10,000. If a report is required, certain records must also be kept.
2. In April 2003, the IRS was delegated civil enforcement authority for the FBAR.
3. IRM 4.26.16covers FBAR law. FBAR procedures are covered in IRM 4.26.17.

4.26.16.2 (07-01-2008) FBAR Authorities

1. FBAR issues can be researched at:
   A. 31 U.S.C. § 5314 the United States Code,
   B. 31 C.F.R. Part 103, the Code of Federal Regulations, and
   C. Instructions to the FBAR.
2. FBAR relevant authorities are listed on the SB/SE FBAR web site at ht-

tp://sbse.web.irs.gov/FR/BSA/ProgTechGuidance.htm#fbar. If additional research sources are needed:

A. Statutory material may be found using commercial legal research services on the IR web home page research center. This is preferable to using the official version of the United States Code because the web site is updated more frequently.

B. Regulations may be found using commercial legal research services or at http://www.gpoaccess.gov/ecfr. The Electronic Code of Federal Regulations (ECFR) is updated frequently.

C. The best source for the most current version of the FBAR and its instructions is IRS Forms and Publications at http:// publish.no.irs.gov/catlg.html

3. The public can obtain the FBAR and instructions as follows:

A. On the internet at http://www.irs.gov.

B. In some libraries and IRS Forms Distribution centers

4.26.16.2.1 (07-01-2008) FBAR Statutory Authority

1. Statutory authority for the FBAR is 31 U.S.C. § 5314.

2. Section 5314 directs the Secretary of the Treasury to require a resident or citizen of the United States, or a person in and doing business in the United States, to keep records and/or file reports when making transactions or maintaining a relationship with a foreign financial agency.

3. 31 U.S.C. § 5321(a)(5) establishes civil penalties for violations of the FBAR reporting and recordkeeping requirements. See IRM 4.26.16.4 FBAR Penalties for a discussion of penalties.

4.26.16.2.2 (07-01-2008) FBAR Regulatory Authority

1. Regulatory authority for the FBAR is 31 C.F.R. §§ 103.24 and 103.27. Section 103.32 provides for FBAR records and Section 103.56 tasks the IRS with FBAR enforcement. Section 103.24 states that each person subject to the jurisdiction of the United States (except a foreign subsidiary of a U.S. person) who has a financial interest in, or signature or other authority over, a bank, securities, or other financial account in a foreign country must report that relationship to the Commissioner of the Internal Revenue for each year in which the relationship exists. The U.S. person must provide information as specified in the required reporting form.

2. The FBAR must be filed on or before June 30 for foreign financial accounts aggregating more than $10,000 in the previous calendar year. 31 C.F.R. § 103.27(c)

3. Any person required to file the FBAR must keep certain records of the account for five years. Records may need to be maintained for a longer period by persons who have been formally charged with a criminal tax violation. 31 C.F.R. § 103.32

4. The authority to enforce the provisions of 31 U.S.C. § 5314 and 31 C.F.R. §§103.24 and 103.32 has been redelegated from the Financial Crimes Enforcement Network (FinCEN) to the Commissioner of the Internal Revenue Service by a Memorandum of Understanding (MOU) between FinCEN and IRS. The MOU is referenced in 31 C.F.R. § 103.56(g). This includes authority to:

A. Investigate possible civil violations of these provisions;

B. Assess and collect civil FBAR penalties;

C. Employ the summons power of subpart F of part 103;

D. Issue administrative rulings under subpart G of part 103; and,

E. Take any other action reasonably necessary for the enforcement of these and related provisions, including pursuit of injunctions.

4.26.16.2.3 (07-01-2008) FBAR Instructional Authority

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1. The instructions for the FBAR provide additional guidance and contain some rules not found in the FBAR statute or regulations. For example, the instructions identify exceptions to the filing requirement for certain corporate officers and employees having signature or other authority over a foreign financial account.

2. The instructions in some instances are clarified by reference to the regulations. For example, terms in the instructions such as "United States" are defined in the regulations.

4.26.16.3 (07-01-2008) FBAR Filing Criteria

1. In order to determine whether or not the FBAR is required, all of the following must apply:

A. The filer is a U.S. person;

B. The U.S. person has a financial account(s);

C. The financial account is in a foreign country;

D. The U.S. person has a financial interest in the account or signature or other authority over the foreign financial account; and,

E. The aggregate amount(s) in the account(s) valued in dollars exceed $10,000 at any time during the calendar year.

4.26.16.3.1 (07-01-2008) U.S. Person

1. A U.S. person is defined by reference to three sources. 31 U.S.C. 5314 and 31 C.F.R. 103.24 identify persons who may be subject to the FBAR reporting requirement. The FBAR instructions identify a smaller group of persons who must file FBARs than could have been required, under the statute and regulations, to file.

A. "The Secretary of the Treasury shall require a resident or citizen of the United States or a person in, and doing business in, the United States, to keep records, file reports..." and that "The Secretary may prescribe a reasonable classification of persons subject to or exempt from a requirement under this section or a regulation under this section". 31 U.S.C. § 5314

B. Each person subject to the jurisdiction of the United States (except a foreign subsidiary of a U.S. person)...shall provide information specified in a reporting form prescribed by the Secretary. 31 C.F.R. § 103.24

C. The instructions to the July 2000 FBAR (the current version) define "United States person" as "a citizen or resident of the United States, a domestic partnership, a domestic corporation or a domestic estate or trust."

D. "United States" includes the states, territories, and possessions of the United States. 31 C.F.R. 133.11(nn)

E. Examiners should use the definition of "United States person" found in the FBAR instructions when determining whether a person has an obligation to file the FBAR.

4.26.16.3.1.1 (07-01-2008) ??(IT,IB,D091028)

1. A citizen of the United States has a U.S. birth certificate or naturalization papers. Documents to substantiate citizenship, however, would not normally be requested as part of the FBAR examination.

2. A "resident" of the United States is a permanent resident. "Permanent resident" is not defined in the FBAR instructions, regulations, or statute. The definition of "resident alien" found in IRC § 7701(b) is not applicable for FBAR purposes. The plain meaning of the term "resident" (in this context, someone who is living in the U.S. and not planning to permanently leave the U.S.) should be used for FBAR examination purposes. Although IRC § 7701(b) is not applicable, an individual can establish that he is not a resident for FBAR purposes if he can show that none of the following three criteria apply:

A. The green-card test - Individuals who at any time during the calendar year have been lawfully granted the privilege of residing permanently in the U.S. under the immigration laws automatically meet the definition of resident

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alien under the green-card test; or

B. Individuals who are not lawful permanent residents are defined as resident aliens under the substantial-presence test if they are physically present in the U.S. for at least 183 days during the current year, or they are physically present in the U.S. for at least 31 days during the current year and meet the specifications contained in IRC § 7701(b) (3); or

C. The person files a first year election on his income tax return to be treated as a resident alien under IRC § 7701(b) (4).

Therefore, if none of the three criteria listed above apply, then the person is not a resident for FBAR purposes.

3. For FBAR purposes, the definition of "person" also includes a corporation, trust, or partnership.

A. A certificate of incorporation from a state of the United States establishes that the corporation is a U.S. person.

B. A foreign subsidiary (a subsidiary that is not incorporated in the United States) of a U.S. person is not subject to the FBAR filing requirements under 31 C.F.R. § 103.24. The U.S. parent is, however, considered to have a financial interest in any foreign financial account owned by its subsidiary and will file the FBAR on such an account.

4. A corporation that owns directly or indirectly more than a 50 percent interest in one or more other entities is permitted to file a consolidated FBAR, on behalf of itself and the other entities. The consolidated report must include a list of the entities. An authorized official of the parent corporation should sign the consolidated report.

4.26.16.3.2 (07-01-2008) Financial Account

1. A financial account includes a:

A. Bank account, such as a savings, demand, checking, deposit, time deposit, or any other account maintained with a financial institution or other person engaged in the business of a financial institution. A bank account set up to secure a credit card account is an example of a financial account. An insurance policy having a cash surrender value is an example of a financial account.

B. Securities, securities derivatives, or other financial instruments account.

C. Other financial accounts generally encompass any accounts in which the assets are held in a commingled fund and the account owner holds an equity interest in the fund. A mutual fund account is an example of such an account.

D. Individual bonds, notes, or stock certificates held by the filer are not a financial account.

4.26.16.3.3 (07-01-2008) Foreign Financial Account

1. Generally, an account in a foreign country includes all geographical areas located outside the United States.

2. The location of an account, not the nationality of the financial institution with which the account is held, determines whether the account is in a foreign country. Any financial account (except accounts maintained with a U.S. military banking facility) that is located in a foreign country should be reported, even if the account is held with a branch of a United States financial institution located abroad.

A. The FBAR is not required for an account maintained with a branch, agency, or other office that is located in the United States even though the financial institution itself may be foreign.

B. The United States includes the states of the United States, the District of Columbia, the Indian lands (as defined in the Indian Gaming Regulatory Act), and the territories and insular possessions of the United States. Examples include the Commonwealth of Puerto Rico, the United States Virgin Islands, Guam. American Samoa and the Commonwealth of the Northern Marianna Islands.

C. An account is not considered foreign if held in an institution known as a "United States military banking facility" (or "United States military finance facility") operated by a United States financial institution designated by the United States Government to serve U.S. Government installations abroad, even if the United States military banking facility is located in a foreign country.

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3. The existence of a foreign financial account may be discovered during an income tax or Bank Secrecy Act (BSA) examination. Examples of such occurrences include:

A. When inspecting a tax return as a part of pre-contact analysis (for example, Form 1040 Schedule B Part III has questions pertaining to foreign accounts).

B. When conducting an income probe performed during an income tax examination.

C. When interviewing a taxpayer.

D. When conducting a BSA examination of a business, such as a money transmitter, that may routinely transmit funds overseas. Note that such businesses may or may not have a financial interest in, or authority over, a financial account located in a foreign country even though they transmit funds to an account overseas

4.26.16.3.4 (07-01-2008) Financial Interest

1. 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 own benefit or for the benefit of others including non-United States 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 United States persons has a financial interest in that account and, generally, each person must file the FBAR. Under the individual reporting requirement, persons who file a joint tax return must file separate FBARs. In the past however, FinCEN has accepted a single FBAR for an account jointly held by husband and wife. IRS is continuing this practice.

2. A United States person also has a 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. a person acting as an agent, nominee, attorney, or in some other capacity on behalf of the U.S. person; or

B. a corporation, whether foreign or domestic, in which the United States person owns directly or indirectly more than 50 percent of the total value of shares of stock; or

C. a partnership, whether foreign or domestic, in which the United States person owns an interest in more than 50 percent of the profits (distributive share of income); or,

D. a trust, whether foreign or domestic, in which the United States person either has a present beneficial interest in more than 50 percent of the assets or from which such person receives more than 50 percent of the current income.:

3. A bank is not required to file the FBAR to report a financial interest in an international interbank transfer account (commonly called a “nostro” account). This exception appears in 52 Fed. Reg. 11436, 11438 (April 8, 1987).

4.26.16.3.5 (07-01-2008) Signature or Other Authority Over an Account

1. A person having signature or other authority over a foreign financial account must file the FBAR even if the person has no financial interest in the account.

2. A person has signature authority over an account if that person can control the disposition of money or other property in it by delivery of a document containing his signature (or his signature and that of one or more other persons) to the financial institution where the account is maintained. A person has other authority if the person can exercise power comparable to signature authority over an account by communication to the financial institution where the account is maintained, either orally or by some other means.

3. The following are exceptions to the FBAR reporting requirement:

A. An officer or employee of a bank that is subject to the supervision of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, the Office of Thrift Supervision, or the Federal Deposit Insurance Corporation need not file the FBAR reporting that he has signature or other authority over a foreign bank, securities, or other financial account maintained by the bank, if the officer or employee has NO personal financial interest in the account.

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B. An officer or employee of a domestic corporation whose equity securities are listed on a national securities exchange or which has assets exceeding $10 million and 500 or more shareholders of record need not file the FBAR concerning his signature or other authority over a foreign financial account of the corporation, if he has NO personal financial interest in the account and he has been advised in writing by the chief financial officer of the corporation that the corporation has filed a current FBAR, which includes that account.

C. An officer or employee of either a domestic subsidiary of a domestic corporation or a foreign subsidiary that is more than 50% owned by a domestic corporation which has securities listed on a national securities exchange or which has assets exceeding $10 million and 500 or more shareholders of record, need not report that he has signature or other authority over a foreign financial account of the subsidiary if he has NO personal financial interest in the account and has been advised in writing by the chief financial officer of the parent corporation that the corporation has filed a current FBAR which includes that account.

D. An employee or officer of a wholly owned domestic subsidiary of a domestic parent corporation whose equity securities are listed on a national securities exchange or which has assets exceeding $10 million and 500 or more shareholders of record, need not file the FBAR concerning his signature or other authority over a foreign financial account of another domestic or foreign subsidiary of the same domestic parent if he has NO personal financial interest in the account and has been advised in writing by the chief financial officer of the parent corporation that the corporation has filed a current FBAR which includes that account.

4.26.16.3.6 (07-01-2008) Account Valuation

1. The FBAR is required for each calendar year during which the aggregate amount(s) in the account(s) exceeded $10,000 valued in U.S. dollars at any time during the calendar year. The maximum value of an account is the largest amount of currency and non-monetary assets that appear on any quarterly or more frequent account statement issued for the applicable year. For example, if the statement closing balance is $9,000 but at any time during the year a balance of $15,000 appears on a statement, the maximum value is $15,000.

2. If periodic account statements are not issued, the maximum account asset value is the largest amount of currency and non-monetary assets in the account at any time during the year.

3. Convert foreign currency by using the official exchange rate in effect at the end of the year in question for converting the foreign currency into U. S. dollars. In valuing currency of a country that uses multiple exchange rates, use the rate that would apply if the currency in the account were converted into U. S. dollars at the close of the calendar year. The official Treasury Reporting Rates of Exchange for the previous quarter year can be obtained at http://fms.treas.gov/intn.html#rates or by calling the Department of the Treasury, Financial Management Service International Funds Team at (202) 874-7994. As these rates are published quarterly, the rates should be accessed during the first quarter of the following year to obtain the previous December 31 valuation. The rates posted on the FMS website are the current exchange rates. Historical exchange rates will be needed to determine the value in a foreign account in prior years. For historical exchange rates, call FMS at (202) 874-8001 or (202) 874-8004. These phone numbers may be subject to change. Check the FMS website (http:// www.fms.treas.gov) for the most current information.

4. The value of stock, other securities, or other non-monetary assets in an account reported on the FBAR is the fair market value at the end of the calendar year, or if withdrawn from the account earlier in the year, at the time of the withdrawal.

5. If the filer had a financial interest in more than one account, each account is valued separately in accordance with the previous paragraphs.

6. If a person had a financial interest in one or more but fewer than 25 accounts and is unable to determine whether the maximum value of these accounts exceeded $10,000 at any time during the year, the FBAR instructions state that the person is to complete Part II of the FBAR and if needed, the continuation page(s) for each of these accounts. If the

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maximum aggregate value of the accounts was not in excess of $10,000, then there would be no FBAR violation if the person did not file the FBAR, whether or not the person knew the value of the accounts at the time the FBAR was due. This is because section 103.27(c) of the Title 31 regulations only requires FBARs to be filed when the value of the accounts exceeds $10,000 during a calendar year. For rules regarding a person with a financial interest in 25 or more accounts, see IRM 4.26.16.3.9.

4.26.16.3.7 (07-01-2008) Filing

1. The determination to file the FBAR is made annually. For example, the FBAR may be required to report an account for one year but not for the subsequent years if the aggregate account balances in the subsequent years do not exceed $10,000.
2. The FBAR must be filed for each year that the person has a financial interest in or authority over the foreign financial account when the balance exceeds the $10,000 threshold.
3. The FBAR must be filed on or before June 30 each calendar year.
4. The FBAR is filed by mailing it to the U.S. Department of the Treasury, Post Office Box 32621, Detroit, MI 48232-0621.
5. The FBAR should not be filed with the filer's federal income tax return.
6. The FBAR is considered filed when it is received in Detroit, not when it is postmarked.

4.26.16.3.7.1 (07-01-2008) Filing Extension

1. Extensions of time to file federal income tax returns do not extend the time for filing FBARs. There is no statutory or regulatory provision specifically granting an extension of time for filing FBARs.
2. IRC section 7508 Time for performing certain acts postponed by reason of service in combat zone or contingency operation does not grant U.S. persons that are U.S. Armed Forces members any extension to file the FBAR.

4.26.16.3.7.2 (07-01-2008) Amending a Filed FBAR

1. The FBAR instructions (for the July 2000 revision of the form) do not address filing amended FBARs. The following instructions may be given to anyone who needs to file an amended FBAR. To amend a previously filed FBAR:
   A. Write “Amended” at the top of a new form.
   B. Add/correct the information about the account.
   C. Staple it to a copy of the original form.
   D. Mail the amended FBAR to the filing address shown on the form - Department of the Treasury, Post Office Box 32621, Detroit, MI 48232-0621.

4.26.16.3.7.3 (07-01-2008) Filing Verification

1. Filed FBARs are entered onto the Detroit Computing Center's Currency and Banking Retrieval System (CBRS) database. Filing can be checked by IRS personnel with CBRS passwords.
2. A CBRS printout of a filed FBAR establishes that any retained FBAR was actually filed and that the retained FBAR has the same information as the filed FBAR. CBRS printouts should be obtained for both the filer's name and his TIN.
3. Filers can request verification of the FBARs that they filed 60 days after the date of filing. A request for verification of FBAR filing must be made in writing and should include the filer's name, Taxpayer Identification Number, and filing period. There is a $5.00 fee for verifying five or fewer forms and a $1.00 fee for each additional form. If copies are needed, the additional fee is $0.15 per copy. Checks or money orders should be made payable to the United States

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Treasury. The payment should be mailed to:

??(IT,IB,D091028)

4.26.16.3.8 (07-01-2008) FBAR Recordkeeping

1. If the FBAR is required, certain records must be retained by the filer. 31 C.F.R. 103.32. Each person having a financial interest in or signature or other authority over any such account must keep the following records:

A. Name in which the account is maintained;

B. Number or other designation of the account;

C. Name and address of the foreign bank or other person with whom the account is maintained;

D. Type of account; and,

E. Maximum value of each account during the reporting period.

2. Retaining a copy of the FBAR is not required. However, a copy of the current FBAR form contains most of the required information. Additional records that must be retained include the address of the foreign financial institution where the account is maintained and its maximum value (not just a range of values) during the year reported.

3. The records must be kept for five years and be available at all times for inspection as provided by law. In the computation of the five years, disregard any period beginning with a date on which the taxpayer is indicted or information filed on account of the filing of a false or fraudulent Federal income tax return or failing to file a Federal income tax return, and ending with the date on which final disposition is made of the criminal proceeding.

4. An examiner should request any retained copies of FBARs as well as the records for the underlying account(s). Note that persons are not required to keep copies of FBARs filed. Retained FBARs should always be compared to information in the filed FBAR that is recorded in the CBRS database.

4.26.16.3.9 (07-01-2008) Recordkeeping for Filers Having 25 or More Accounts

1. Any person who has a financial interest in 25 or more foreign financial accounts can note the number of accounts in item 20 on the current FBAR form and is not required to complete the remainder of Part II. However, the person must provide the information called for in Part II when requested by government authorities.

2. If a group of entities covered by a consolidated FBAR has a financial interest in 25 or more foreign financial accounts, the reporting corporation only notes that fact on the FBAR. A listing of all the entities which hold the accounts must be attached to the FBAR. The reporting corporation must provide the information called for in Part II for each account when requested by the secretary or his delegate.

4.26.16.4 (07-01-2008) FBAR Penalties

1. The IRS has been delegated authority to assess FBAR civil penalties.

2. There are civil penalties for negligence, pattern of negligence, non-willful, and willful violations.

3. Whenever there is an FBAR violation, the examiner will either issue the FBAR warning letter, Letter 3800, or determine a penalty. See IRM 4.26.17 for the Letter 3800procedures.

4. Penalties should be asserted only to promote compliance with the FBAR reporting and recordkeeping requirements. In exercising their discretion, examiners should consider whether the issuance of a warning letter and the securing of delinquent FBARs, rather than the assertion of a penalty, will achieve the desired result of improving compliance in the future.

5. FBAR civil penalties have varying upper limits, but no floor. The examiner has discretion in determining the amount of the penalty, if any. Examiner discretion is necessary because the total amount of penalties that can be applied under the statute can greatly exceed an amount that would be appropriate in view of the violation.

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6. Examiners are expected to exercise discretion, taking into account the facts and circumstances of each case, in determining whether penalties should be asserted and the total amount of penalties to be asserted. Because FBAR penalties do not have a set amount, IRS has developed penalty mitigation guidelines to assist examiners in the exercise of their discretion in applying these penalties. The mitigation guidelines are only intended as an aid for the examiner in determining an appropriate penalty amount. The examiner must still consider whether a warning letter or a penalty amount that is less than what would be called for under the mitigation guidelines would be more appropriate given the facts and circumstances of a particular case. For example, if an individual failed to report the existence of five small foreign accounts with a combined balance of $20,000 for all five accounts but the income from each account was properly reported and the taxpayer made no effort to conceal the existence of the account, it may be more appropriate to issue a warning letter rather than assert penalties under the mitigation guidelines.

7. FBAR penalties are determined per account, not per unfiled FBAR, for each person required to file. Penalties apply for each year of each violation. As noted above, however, examiners are expected to exercise discretion, taking into account the facts and circumstances of each case, in determining whether penalties should be asserted and the total amount of penalties to be asserted.

8. There may be multiple FBAR civil penalty assessments arising from one account. FBAR civil penalties can apply to each person with a financial interest in, or signature or other authority over, the foreign financial account. Thus there may be multiple penalty assessments if there is more than one account owner or if a person other than the account owner has signature or other authority over the foreign account. Each person can be liable for the full amount of the penalty.

4.26.16.4.1 (07-01-2008) FBAR Penalty Authority

1. As of April 8th 2003, IRS was delegated the authority to assess and collect FBAR civil penalties. 31 C.F.R. § 103.56(g). The delegation includes the authority to investigate possible FBAR civil violations, provided in Treasury Directive No. 15-41 (Dec. 1, 1992), and the authority to assess and collect the penalties for violations of the reporting and recordkeeping requirements.

2. When performing these functions, the IRS is not acting under Title 26 but, instead, is acting under the authority of Title 31. Provisions of the Internal Revenue Code generally do not apply to FBARs.

3. Criminal investigation has been delegated the authority to investigate possible criminal violations of the Bank Secrecy Act. 31 C.F.R. §103.56 (c)(2)

4.26.16.4.2 (07-01-2008) FBAR Penalty Structure

1. A civil money penalty may be imposed for an FBAR violation even if a criminal penalty is imposed for the same violation. 31 U.S.C. § 5321(d). (d).

4.26.16.4.3 (07-01-2008) BSA Negligence Penalties

1. There are two negligence penalties which apply generally to all BSA provisions. 31 U.S.C. § 5321(a)(6)

A. A negligence penalty up to $500 may be assessed against a business for any negligent violation of the BSA, including FBAR violations.

B. An additional penalty up to $50,000 may be assessed for a pattern of negligent violations.

2. Generally, these two negligence penalties only apply to trades or businesses, not to individuals. The FBAR penalties under section 5321(a) (5) and the FBAR warning letter, Letter 3800, should be adequate to address most FBAR violations that are identified. The FBAR warning letter may be issued in the cases where the revenue agent determines none of the 5321(a)(5) FBAR penalties are warranted. If the revenue agent believes, however, that assertion of a sec-

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tion 5321(a)(6) negligence penalty is warranted in a particular case, the revenue agent should contact a Bank Secrecy Act Program Analyst for guidance.

4.26.16.4.3.1 (07-01-2008) Negligence

1. Actual knowledge of the reporting requirement is not required to find negligence. If a financial institution or non-financial trade or business exercising ordinary business care and prudence for its particular type of business should have known about the FBAR filing and record keeping requirements, failure to file or maintain records is negligent. Therefore, standards of practice for a particular type of business are relevant in determining whether someone committed a negligent violation of 31 U.S.C. § 5314. If the failure to file the FBAR or to keep records is due to reasonable cause, and not due to the negligence of the person who had the obligation to file or keep records, the negligence penalty should not be asserted.
2. Negligent failure to file does NOT exist when, despite the exercise of ordinary business care and prudence, the business was unable to file the FBAR or keep the required records.
3. Use general negligence principles in determining whether or not to apply the negligence penalty. Treas. Reg. 1.6664-4, Reasonable Cause and Good Faith Exception to § 6662 penalties, may serve as useful guidance in determining the factors to consider. Although this tax regulation does not apply to FBARs, the information it contains may still be helpful in determining whether the FBAR violation was due to reasonable cause and not due to negligence.

4.26.16.4.3.2 (07-01-2008) BSA Simple Negligence Penalty

1. The $500 simple negligence penalty applies only to financial institutions for violations occurring prior to October 27, 2001. 31 U.S.C. § 5321 (a) (6) (A). For violations occurring after October 26, 2001, the negligence penalty applies to all businesses.
2. Currently, regulation 31 C.F.R. § 103.57(h) does not reflect the statutory change making the penalty applicable to all businesses. However, section 5321(a)(6)(A) provides the authority to assert the penalty against any business for violations occurring after October 26, 2001.

4.26.16.4.3.3 (07-01-2008) BSA Simple Negligence Penalty - Application to Financial Institutions

1. The simple negligence penalty of 31 C.F.R. 103.57(h) applies to financial institutions as they are defined in the regulations at 31 C.F.R. 103.11(n) for violations occurring prior to October 27, 2001.
2. These financial institutions are defined to include "each agent, agency, branch, or office within the United States of any person doing business, whether or not on a regular basis or as an organized business concern, in one or more of following capacities:"
   - A bank (except bank credit card systems);
   - A broker or dealer in securities;
   - A money services business as defined in 31 C.F.R. 103.11 (uu);
   - A telegraph company;
   - A casino or card club;
   - A person subject to supervision by any state or federal bank supervisory authority; or,
   - A futures commission merchant or an introducing broker in commodities.

4.26.16.4.3.4 (07-01-2008) BSA Simple Negligence Penalty Amount

1. For each negligent violation of any requirement of the Bank Secrecy Act committed after October 27, 1986, a civil penalty may be assessed not to exceed $500.

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2. Generally, the full amount of this $500 penalty is assessed. Although 31 U.S.C. 5321(a)(6) permits discretion to assert a lower amount, there are no mitigation guidelines for this penalty.

4.26.16.4.3.5 (07-01-2008) BSA Pattern of Negligence Penalty

1. 31 U.S.C. § 5321(a)(6)(B) provides for a civil money penalty of not more than $50,000 on a business that engages in a pattern of negligent BSA violations including violations of the FBAR rules. This penalty is in addition to any $500 negligence penalty.

2. The pattern of negligence penalty has applied to financial institutions since 1986. For violations occurring after October 26, 2001, the penalty applies to all trades or businesses. This penalty does not apply to individuals.

3. For purposes of determining the pattern of negligence penalty, use the definitions in 31 C.F.R. § 103.11(n) for the term "financial institution" and not the definition of "financial institution" in 31 U.S.C. § 5312(a)(2).

4.26.16.4.3.6 (07-01-2008) BSA Pattern of Negligence Penalty - Amount

1. If any trade or business engages in a pattern of negligent violations of any provision [including the FBAR requirements] of the BSA, a civil penalty of not more than $50,000 may be imposed. This is in addition to the simple negligence $500 penalty. 31 U.S.C. § 5321(a)(6)(B). The examiner is given discretion to determine the penalty amount up to the $50,000 ceiling.

2. There are no mitigation guidelines for this penalty. The pattern of negligence penalty should only be asserted in egregious cases.

4.26.16.4.4 (07-01-2008) Non-Willfulness Penalty

1. For violations occurring after October 22, 2004, a new penalty applies to individuals as well as businesses. 31 U.S.C. § 5321(a)(5)(A). A penalty, not to exceed $10,000, may be imposed on any person who violates or causes any violation of the FBAR filing and recordkeeping requirements.

2. The penalty should not be imposed if:

A. The violation was due to reasonable cause, and

B. The balance in the account was properly reported on an FBAR. This means that the examiner must receive the delinquent FBARs from the nonfiler in order to avoid application of the non-willfulness penalty.

3. The ceiling allows the examiner discretion in determining the penalty. Mitigation guidelines have been developed as a guide to examiners in asserting the appropriate non-willfulness penalty amount. See the discussion of the mitigation guidelines below. *See Exhibit 4.26.16-1* through 4. As with the FBAR penalty for willful violations, examiners are to use discretion, taking into account the facts and circumstances of each case, in determining whether a warning letter or penalties that are less than the total amounts provided for in the mitigation guidelines are appropriate. The sole purpose for the FBAR penalties is to serve as a tool to promote compliance with respect to the FBAR reporting and recordkeeping requirements.

4. A filing violation occurs on June 30th of the year following the calendar year to be reported (that is, on the due date for filing the FBAR).

5. A recordkeeping violation occurs on the date when the records are requested by the IRS examiner if the records are not later provided.

4.26.16.4.5 (07-01-2008) FBAR Willfulness Penalty

1. There are two different statutory ceilings for willful penalty violations of the FBAR requirements, depending on whether or not the violation occurred before October 23, 2004. As stated previously, a filing violation occurs on June

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30th of the year following the calendar year to be reported. A recordkeeping violation occurs on the date when the records are requested by the IRS examiner if the records are not provided.

2. Because the willfulness penalty statute has a substantial ceiling amount, IRS has developed guidelines for the exercise of the examiner's discretion in arriving at the amount of a willfulness penalty.

4.26.16.4.5.1 (07-01-2008) FBAR Willfulness Penalty - Authority

1. A civil money penalty may be imposed on any person who willfully violates or causes any violation of any provision of section 5314 (the FBAR FBAR requirements). 31 U.S.C. § 5321(a)(5)(A)

2. The ceiling applicable for violations occurring before October 23, 2004 is the greater of an amount (not to exceed $100,000) equal to the balance in the account at the time of the violation or $ 25,000.

3. For violations occurring after October 22, 2004 the ceiling is the greater of $100,000 or 50% of the balance in the account at the time of the violation.

4. At the time of this writing, the regulations at 31 C.F.R. § 103.57 have not been revised to reflect the change in the willfulness penalty ceiling. However, the statute is self-executing and the new penalty ceilings apply.

4.26.16.4.5.2 (07-01-2008) FBAR Willfulness Penalty - Application

1. The willfulness penalty applies to any person who has willfully violated the FBAR reporting or recordkeeping provisions.

2. It applies to individuals as well as financial institutions and non-financial trades or businesses for all years.

4.26.16.4.5.3 (07-01-2008) FBAR Willfulness Penalty - Willfulness

1. The test for willfulness is whether there was a voluntary, intentional violation of a known legal duty.

2. A finding of willfulness under the BSA must be supported by evidence of willfulness.

3. The burden of establishing willfulness is on the Service.

4. If it is determined that the violation was due to reasonable cause, the willfulness penalty should not be asserted.

5. Willfulness is shown by the person's knowledge of the reporting requirements and the person's conscious choice not to comply with the requirements. In the FBAR situation, the only thing that a person need know is that he has a reporting requirement. If a person has that knowledge, the only intent needed to constitute a willful violation of the requirement is a conscious choice not to file the FBAR.

6. Under the concept of “willful blindness”, willfulness may be attributed to a person who has made a conscious effort to avoid learning about the FBAR reporting and recordkeeping requirements. An example that might involve willful blindness would be a person who admits knowledge of and fails to answer a question concerning signature authority at foreign banks on Schedule B of his income tax return. This section of the return refers taxpayers to the instructions for Schedule B that provide further guidance on their responsibilities for reporting foreign bank accounts and discusses the duty to file Form 90-22.1. These resources indicate that the person could have learned of the filing and recordkeeping requirements quite easily. It is reasonable to assume that a person who has foreign bank accounts should read the information specified by the government in tax forms. The failure to follow-up on this knowledge and learn of the further reporting requirement as suggested on Schedule B may provide some evidence of willful blindness on the part of the person. For example, the failure to learn of the filing requirements coupled with other factors, such as the efforts taken to conceal the existence of the accounts and the amounts involved may lead to a conclusion that the violation was due to willful blindness. The mere fact that a person checked the wrong box, or no box, on a Schedule B is not sufficient, by itself, to establish that the FBAR violation was attributable to willful blindness.

7. Willfulness can rarely be proven by direct evidence, since it is a state of mind. It is usually established by drawing

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a reasonable inference from the available facts. The government may base a determination of willfulness in the failure to file the FBAR on inference from conduct meant to conceal sources of income or other financial information. For FBAR purposes, this could include concealing signature authority, interests in various transactions, and interests in entities transferring cash to foreign banks.

8. The following examples illustrate situations in which willfulness may be present:

A. A person admits knowledge of, and fails to answer, a question concerning signature authority over foreign bank accounts on Schedule B of his income tax return. When asked, the person does not provide a reasonable explanation for failing to answer the Schedule B question and for failing to file the FBAR. A determination that the violation was willful likely would be appropriate in this case.

B. A person files the FBAR, but omits one of three foreign bank accounts. The person had closed the omitted account at the time of filing the FBAR. The person explains that the omission was due to unintentional oversight. During the examination, the person provides all information requested with respect to the omitted account. The information provided does not disclose anything suspicious about the account, and the person reported all income associated with the account on his tax return. The willfulness penalty should not apply absent other evidence that may indicate willfulness.

C. A person filed the FBAR in earlier years but failed to file the FBAR in subsequent years when required to do so. When asked, the person does not provide a reasonable explanation for failing to file the FBAR. In addition, the person may have failed to report income associated with foreign bank accounts for the years that FBARs were not filed. As with example a. above, a determination that the violation was willful likely would be appropriate in this case.

D. A person received a warning letter informing him of the FBAR filing requirement, but the person continues to fail to file the FBAR in subsequent years. When asked, the person does not provide a reasonable explanation for failing to file the FBAR. In addition, the person may have failed to report income associated with the foreign bank accounts. As with examples a. and c. above, a determination that the violation was willful likely would be appropriate in this case.

4.26.16.4.5.4 (07-01-2008) FBAR Willfulness Penalty - Evidence

1. Documents that may be helpful in establishing willfulness include:

A. Copies of documents from the administrative case file (including the Revenue Agent Report) for the income tax examination that show income related to funds in a foreign bank account was not reported.

B. A copy of the signed income tax return with Schedule B attached (showing whether or not the box pertaining to foreign accounts is checked or unchecked).

C. Copies of statements for the foreign bank account.

D. Notes of the examiner's interview with the foreign account holder/taxpayer about the foreign account.

E. Any documents that would support fraud (see IRM 4.10.6.2.2 for a list of items to consider in asserting the fraud penalty).

F. Correspondence with the account holder's tax preparer that may address the FBAR filing requirement.

G. Documents showing criminal activity related to the non-filing of the FBAR (or non-compliance with other BSA provisions).

H. Promotional material (from the promoter or offshore bank).

I. Statements for debit or credit cards from the offshore bank (which could show if the account holder was using funds from the offshore account to cover everyday living expenses in a manner that would conceal the source of the funds).

J. Printouts from CBRS that show that the FBAR was not filed.

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K. Copies of any FBARs (or CBRS printouts of FBARs) that were previously filed by the account holder.

L. Copies of tax returns (or RTVUEs/BRTVUs) for at least three years prior to the opening of the offshore account and for all years after the account was opened. (To show any significant drop in reportable income after the account was opened, three years prior to the opening of the account would be requested in order to give the examiner a better idea of what the account holder typically would have reported as income prior to opening the foreign account).

M. Copies of Information Document Requests with items that were not provided by the account holder highlighted and explanations given as to why the requested information was not provided.

N. Copies of debit or credit card agreements and fee schedules with the foreign bank (which may show a significantly higher cost than typically associated with cards from domestic banks).

O. Copies of debit and credit card statements prior to the opening of the foreign account (to show that the account holder did or did not routinely use such cards for everyday living expenses, keeping in mind these statements may be difficult to obtain if the foreign account was opened many years ago).

P. Copies of any investment management or broker's agreement and fee schedules with the foreign bank (which may show significantly higher costs than costs associated with domestic investment management firms or brokers).

Q. The account holder's written explanation of why the FBAR was not filed (if the account holder wishes to provide such a statement). Otherwise, note in the workpapers whether the account holder was given an opportunity to provide such a statement.

R. Copies of any previous warning letters issued to the account holder.

S. Copies of any prior Revenue Agent Reports that may show a history of noncompliance.

T. An explanation, in the workpapers, as to why the examiner believes that the account holder's failure to file the FBAR was willful.

U. Two sets of cash Ts (a reconciliation of the taxpayer's sources and uses of funds) with one set showing any unreported income in foreign accounts that was identified during the examination and the second set excluding the unreported income in foreign accounts.

4.26.16.4.5.5 (07-01-2008) FBAR Wilfulness Penalty - Calculation

1. For violations occurring prior to October 23, 2004, a penalty up to the greater of $25,000 or the amount in the account (up to $100,000) may be asserted for willfully violating the FBAR requirements, 31 U.S.C. § 5321 (a)(5).

2. For violations occurring after October 22, 2004, a willfulness penalty may be imposed up to the greater of $100,000 or 50% of the amount in the account at the time of the violation, 31 U.S.C. § 5321 (a)(5).

3. There may be both a reporting and a recordkeeping violation regarding each account. The amount of the penalty is calculated per account and per violation. There is no reduction in the amount of the account due to multiple financial interests in the account. For example, the entire balance of an account owned by two persons is the amount used to calculate the amount of the penalty for each. The value of the account is not reduced by half because there are two owners. But see sections 4.26.16.4(3) and (4).

4. The date of a filing violation is June 30th of the year following the calendar year for which the accounts are being reported. This date is the last possible day for filing the FBAR so that the close of the day with no filed FBAR represents the first time that a violation has occurred. The amount [balance] in the account at the close of June 30th is the amount to use in calculating the filing violation.

5. The date that the examiner first requests records is the date of the violation for failure to keep records. The date of the violation should be tied to the date of the request, and not a later date to avoid the taxpayer manipulating the amount in the account after receiving a request for records. The balance in the account at the close of the day on which the records are first requested is the amount to use in calculating the recordkeeping penalty violation.

4.26.16.4.5.6 (07-01-2008) FBAR Wilfulness Penalty Amount - Mitigation Inapplicable

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1. When the person does not meet the threshold conditions for mitigation (see IRM 4.26.16.4.6.1), then the mitigation guidelines found in the Exhibits to this IRM section should not be used.

2. For violations occurring prior to October 23, 2004:

A. Small Accounts: For cases when the balance in the account, as of the due date for filing the FBAR (or, if the violation is for failure to keep required records, as of the date the Service first requests the records), does not exceed $25,000, then the penalty is $25,000. This $25,000 penalty is available, for example, when the account has been closed by the following June 30th and the balance is zero.

B. Large Accounts: For cases when the balance in the account, as of the due date for filing the FBAR (or, if the violation is for failure to keep required records, as of the date the Service first requests the records) exceeds $25,000, then the maximum penalty is the lesser of: $100,000 or the balance in the account, as of the due date for filing the FBAR (or, if the violation is for failure to keep required records, as of the date the Service first requests the records).

3. For violations occurring after October 22, 2004:

A. Small Accounts: For cases when the balance in the account, as of the due date for filing the FBAR (or, if the violation is for failure to keep required records, as of the date the Service first requests the records), does not exceed $ 100,000, then the penalty is $100,000. This $100,000 penalty is available, for example, when the account has been closed by the following June 30th and the balance is zero.

B. Large Accounts: For cases when the balance in the account, as of the due date for filing the FBAR (or, if the violation is for failure to keep required records, as of the date the Service first requests the records) exceeds $100,000, then the penalty is 50% of the balance in the account on that date. This is the maximum penalty for these accounts.

4.26.16.4.6 (07-01-2008) Mitigation

1. The statutory penalty computation provides a celling on the FBAR penalty. The actual amount of the penalty is left to the discretion of the examiner.

2. The Service has adopted guidelines to promote consistency by Service employees in exercising this discretion for similarly situated persons.

3. FBAR cases closed under the Last Chance Compliance Initiative (LCCI) use different mitigation guidelines from those used for other FBAR cases. *See Exhibit 4.26.16-1.* through 4.

4.26.16.4.6.1 (07-01-2008) Mitigation Threshold Conditions

1. For most FBAR cases, the Service has determined that if a person meets four threshold conditions then the person may be subject to less than the maximum FBAR penalty depending on the amounts in the person's accounts. There are four threshold conditions which vary slightly depending on the date of the violation.

2. For violations occurring prior to October 23, 2004, the four threshold conditions are:

A. The person has no history of past FBAR penalty assessments;

B. 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;

C. The person cooperated during the examination (i.e., the Service did not have to resort to a summons to obtain non-privileged information; the taxpayer responded to reasonable requests for documents; meetings, and interviews; or the taxpayer back-filed correct reports); and,

D. The Service 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.

3. For violations occurring after October 22, 2004, the first condition was expanded to add no history of criminal tax or BSA convictions for the preceding ten years as well as no history of past FBAR penalty assessments. Otherwise, the four conditions are the same.

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4.26.16.4.6.2 (07-01-2008) Mitigation of the Non-willful FBAR Penalty

1. IRS has developed penalty mitigation guidelines for the computation of the non-willfulness penalty regarding FBAR violations occurring after October 22, 2004. *See Exhibit 4.26.16-2*.

2. The same mitigation threshold requirements apply as discussed above in this Section.

3. There are three penalty levels depending on the highest amount in the account during the period for which the FBAR should have been filed.

4. If the aggregate balance of all accounts held during the year does not exceed $50,000, then the penalty for each violation is $500, not to exceed a total of $5,000 in penalties.

5. If the aggregate balance of the accounts is over $50,000, but less than $250,000, the penalty is, per violation, the lesser of $5,000 or ten per cent of the highest balance in the account during the year for which the account should have been reported.

6. For violations regarding an account exceeding $250,000, the penalty per violation is the statutory maximum of $10,000.

4.26.16.4.6.3 (07-01-2008) Mitigation Levels for Willful FBAR Penalties

1. If the person satisfies the four threshold conditions for general mitigation, then the mitigation guidelines apply.

2. The mitigation guidelines for willful violations occurring prior to October 23, 2004 provide for four levels of mitigation. *See Exhibit 4.26.16-1*.

A. Level I Willful Violations Occurring Before October 23, 2004 - A Level I penalty applies if the maximum aggregate balance for all required but unreported foreign accounts does not exceed $20,000. For Level I cases, the penalty will be 5% of the maximum balance during the calendar year for each of the unreported foreign accounts that should have been reported.

B. Level II Willful Violations Occurring Before October 23, 2004 - A Level II penalty applies if the Level I penalty does not apply and the maximum balance during the year for a required but unreported foreign account is not more than $250,000. The balance in each account is analyzed separately to determine the applicable penalty for that account. For an account that falls within Level II, the penalty will be 10% of the maximum balance during the year for each of the unreported foreign accounts that should have been reported. Thus, the maximum Level II penalty is $25,000 per account.

C. Level III Willful Violations Occurring Before October 23, 2004 — A Level III penalty applies if the maximum balance during the year for an unreported foreign account that should have been reported is greater than $250,000 but not more than $1 million. The balance in each account is analyzed separately to determine the applicable penalty for that account. For an account that falls within Level III, the penalty will be the lesser of: (a) 10% of the maximum amount of the foreign account that should have been reported, or (b) the amount in the account as of the last day for filing the FBAR, unless this amount is less than $25,000, in which case the penalty is $25,000.

D. Level IV Willful Violations Occurring Before October 23, 2004 - A Level IV penalty applies if the maximum balance during the year for an unreported foreign account that should have been reported was greater than $1 million. The balance in each account is analyzed separately to determine the applicable penalty for that account. For Level IV, the penalty will be the lesser of: (a) $100,000 or (b) the amount in the account as of the last day for filing the FBAR, unless this amount is less than $25,000, in which case the penalty is $25,000.

3. Mitigation guidelines for willfulness penalties occurring after October 22, 2004:

A. Level I Willful Violations Occurring After October 22, 2004 - If the maximum aggregate balance for all accounts to which the violations relate did not exceed $50,000, Level I applies to all accounts. Determine the maximum balance during the calendar year for each account. Add the various maximums to find the maximum aggregate balance. The Level I penalty is the greater of $1,000 per violation or 5% of the maximum account balance during the

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calendar year for each Level I account.

B. Level II Willful Violations Occurring After October 22, 2004 - If Level I does not apply and if the maximum account balance to which the violations relate at any time during the calendar year did not exceed $250,000, Level II applies to that account. The Level II penalty assessed for each account is the greater of $5,000 per violation or 10% of the maximum account balance during the calendar year for each Level II account.

C. Level III Willful Violations Occurring After October 22, 2004 - If the maximum account balance to which the violations relate at any time during the calendar year exceeded $250,000 but did not exceed $1,000,000, Level III applies to that account. The Level III penalty assessed for each account is the greater of 10% of the maximum account balance during the calendar year for each Level III account or 50% of the closing balance in the account as of the last day for filing the FBAR.

D. Level IV Willful Violations Occurring After October 22, 2004 - If the maximum account balance to which the violations relate at any time during the calendar year exceeded $1 million, Level IV, the statutory maximum, applies to that account. The Level IV penalty is the statutory maximum applied to each account. It is the greater of $100,000 or 50% of the closing balance in the account as of the last day for filing the FBAR.

4.26.16.4.6.4 (07-01-2008) FBAR Penalty - LCCI Mitigation Guideline Conditions

1. The penalty mitigation guidelines for cases closed under the Last Chance Compliance Initiative (LCCI) are different from the general mitigation guidelines.

2. For violations occurring prior to October 23, 2004, there are two criteria, both of which must be met, for application of the LCCI mitigation guidelines:

A. The person must meet all of the conditions necessary to qualify for the Last Chance Compliance Initiative, and

B. The person must not have been previously assessed the FBAR penalty.

3. For violations occurring after October 22, 2004, there are four conditions necessary for application of the LCCI mitigation guidelines:

A. The person meets all of the conditions necessary to qualify for the Last Chance Compliance Initiative;

B. The person has no history of criminal tax or BSA convictions for the preceding ten years and has no history of prior FBAR penalty assessments;

C. 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; and,

D. The person cooperated during the examination.

4. Generally, the FBAR penalty is only asserted for one year in LCCI cases.

5. One of the conditions for the LCCI initiative is that the FBAR penalty must be fully paid when asserted. If it is not fully paid, the taxpayer has not met the conditions for LCCI and the case becomes a general FBAR case with penalties for all years.

4.26.16.4.6.5 (07-01-2008) FBAR Penalty - LCCI Mitigation Levels

1. There are two mitigation levels in LCCI cases for violations occurring prior to October 23, 2004. Both levels depend on the highest aggregate balance on the same day for all unreported accounts. This calculation differs from the way the general rule aggregation is calculated. Under the general rule, if one account is closed and all the funds are transferred to a new account both accounts are included in the aggregate amount, even though it is the same cash. Under the LCCI calculation, the amount would only be included once, because it is not available in each account on the same day.

2. Once the conditions have been met, the level of mitigation for violations occurring before October 23, 2004 are determined as follows:

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A. Persons are eligible for Level I if the aggregate highest balance on the same day for all unreported accounts during the year of examination was less than $20,000. The Level I mitigated penalty is 5% of the maximum balance during the calendar year for each of the unreported foreign accounts that should have been reported.

B. Persons are eligible for Level II if the highest aggregate balance on the same day for all unreported accounts was equal to or greater than $20,000. The mitigated penalty for Level II is 10% of the maximum balance during the calendar year for each of the unreported foreign accounts that should have been reported, up to the regulatory limits.

3. For violations occurring after October 22, 2004, there are mitigation levels for each willful and non-willful violation. Each depends on the LCCI aggregate amount which is arrived at differently than the pre-October 22, 2004 cases. The maximum balance at any time during the calendar year for each account is determined. Then the various maximums are added to find the maximum aggregate balance.

4. There are three levels of LCCI mitigated penalties for non-willful (NW) violations occurring after October 22, 2004:

A. Level I Non-Willful Violations After October 22, 2004 - If the maximum aggregate balance for all accounts to which the violations relate did not exceed $50,000 at any time during the year, the Level I NW mitigated penalty applies. The Level I NW penalty is $500 for each violation, not to exceed an aggregate penalty of $5,000 for all violations.

B. Level II Non-Willful Violations After October 22, 2004 - If Level I NW penalty does not apply and if the maximum balance of the account to which the violations relate at any time during the calendar year did not exceed $250,000, Level II NW penalty applies to that account. The Level II NW Penalty is $5,000 for each Level II NW account violation, not to exceed ten per cent of the maximum balance in the account during the year.

C. Level III Non-Willful Violations After October 22, 2004 - If Level I NW penalty does not apply and if the maximum balance of the account to which the violations relate at any time during the calendar year was more than $250,000, the Level III NW penalty applies to that account. The Level III NW penalty is $10,000 for each Level III NW account violation, the statutory maximum for non-willful violations.

5. There are four levels of LCCI FBAR mitigated willfulness penalties applicable to violations occurring after October 22, 2004:

A. Level I Willful Violations after October 22, 2004 - If the maximum aggregate balance for all accounts to which the violations relate did not exceed $50,000, Level I applies to all accounts. Determine the maximum balance at any time during the calendar year for each account that involves violations. Add the various maximums to find the maximum aggregate balance. The Level I mitigated penalty is the greater of $1,000 per violation or 5% of the maximum balance during the calendar year for each Level I account.

B. Level II Willful Violations after October 22, 2004 - If Level I does not apply and if the maximum balance of the account to which the violations relate at any time during the calendar year did not exceed $250,000, Level II applies to that account. The Level II penalty assessed for each account is the greater of $5,000 per violation or 10% of the maximum balance during the calendar year for each Level II account.

C. Level III Willful Violations After October 22, 2004 - If the maximum balance of the account to which the violations relate at any time during the calendar year exceeded $250,000 but did not exceed $1,000,000, Level III applies to that account. The Level III penalty assessed for each account is the greater of 10% of the maximum amount during the year for each Level III account or 50% of the closing balance in the account as of the last day for filing the FBAR.

D. Level IV Willful Violations After October 22, 2004 - If the maximum balance of the account to which the violations relate at any time during the calendar year exceeded $1 million, Level IV, the statutory maximum, applies to that account. The Level IV penalty assessed for each account is the greater of $100,000 or 50% of the closing balance in the account as of the last day for filing the FBAR.

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4.26.16.4.7 (07-01-2008) FBAR Penalties - Examiner Discretion

1. The examiner may determine that the facts and circumstances of a particular case do not justify asserting a penalty. If there was an FBAR violation but the examiner determines that a penalty is not appropriate, the examiner should issue the FBAR warning letter, Letter 3800.

2. When a penalty is appropriate, IRS has established penalty mitigation guidelines to aid the examiner in applying penalties in a uniform manner. The examiner may determine that a penalty under these guidelines is not appropriate or that a lesser penalty amount than the guidelines would otherwise provide is appropriate or that the penalty should be increased (up to the statutory maximum). The examiner must make such a determination with the written approval of the examiner's manager and document the decision in the workpapers.

3. Factors to consider when applying examiner discretion may include, but are not limited to, the following:

A. Whether compliance objectives would be achieved by issuance of a warning letter;

B. Whether the person who committed the violation had been previously issued a warning letter or has been assessed the FBAR penalty;

C. The nature of the violation and the amounts involved; and

D. The cooperation of the taxpayer during the examination.

4. Given the magnitude of the maximum penalties permitted for each violation, the assertion of multiple penalties and the assertion of separate penalties for multiple violations with respect to a single FBAR form, should be considered only in the most egregious cases.

Exhibit 4.26.16-1 (07-01-2008) Pre-October 23, 2004 Normal FBAR Civil Penalty Mitigation Guidelines

The Willfulness Penalty (31 U.S.C. § 5321(a)(5)) and Mitigation:

Section 5321(a)(5) of the Bank Secrecy Act generally provides for a civil penalty of up to the amount in the account at the time of the violation (but no more than $100,000) for a willful violation of the FBAR reporting and recordkeeping requirements. The time of the violation for failing to file a report is the end of the due date for filing the report. Although section 5321 sets the maximum amount for the penalty, the Secretary may assess a lower amount. The Service has established guidelines for imposing the FBAR penalty in an amount below the maximum amount in cases where, generally, the person has not engaged in criminal conduct, does not have prior FBAR penalty assessments, and is cooperating with the Service.

The criteria for qualifying for mitigation of the FBAR civil penalty are:

1. No history of past FBAR penalty assessments;

2. No money in the foreign account was from an illegal source or used for a criminal purpose (based on available information — the revenue agent is not required to conduct a criminal investigation);

3. The person is cooperating with the Service; and,

4. A civil fraud penalty was not asserted against the person for an underpayment of tax that was connected to the person's failure to file the FBAR.

The maximum FBAR penalty is limited to the amount in the foreign account at the time of the violation up to $100,000, except in cases where the maximum amount in the account at the time of the violation was less than $25,000 (in which case the maximum penalty amount is $25,000). The mitigation guidelines are based on the maximum amount in the account during the year in question.

Mitigation Guidelines for Pre-October 23, 2004 (Four Levels Based on the Amount in the Foreign Account):

Level I - If the highest aggregate balance for all unreported accounts does not exceed $20,000, the penalty is 5% of the maximum balance during the year for each of the unreported accounts.

Level II - If the maximum balance of an unreported account does not exceed $250,000, the penalty is 10% of the maximum amount during the year for each unreported account. The maximum Level II penalty is $25,000.

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Level III - If the maximum balance of an unreported account is greater than $250,000 but does not exceed $1 million, the penalty is the lesser of:

A. 10% of the maximum amount in each unreported account during the year, or

B. The amount in the account as of the last day for filing the FBAR, unless this amount is less than or equal to $25,000 (in which case the penalty is $25,000, the maximum penalty in such cases, under section 5321).

Level IV - If the maximum balance of an unreported account is greater than $1 million. The amount of the penalty is the lesser of:

A. $100,000 for each unreported account or

B. The amount in the account as of the last day for filing the FBAR unless this amount is less than $25,000 (in which case the penalty is $25,000).

Exhibit 4.26.16-2 (07-01-2008) Normal FBAR Penalty Mitigation Guidelines for Violations Occurring After October 22, 2004

The Bank Secrecy Act (BSA) allows the Secretary of the Treasury some discretion in determining the amount of penalties for violations of the FBAR reporting and record keeping requirements. There is a penalty ceiling but no minimum amount. This discretion has been delegated to the FBAR examiner.

- The examiner may determine that the facts and circumstances of a particular case do not justify a penalty.
- If there was an FBAR violation but no penalty is appropriate, the examiner should issue the FBAR warning letter, Letter 3800.

When a penalty is appropriate, IRS has established penalty mitigation guidelines so that the penalties determined through the examiner's discretion are uniform. The examiner may determine that:

- A penalty under these guidelines is not appropriate, or
- A lesser amount than the guidelines would otherwise provide is appropriate.

The examiner must make this determination with the written approval of the examiner's manager. The examiner's workpapers must document the circumstances that make mitigation of the penalty under these guidelines appropriate. To qualify for mitigation, the person must meet four criteria:

1. The person has no history of criminal tax or BSA convictions for the preceding ten years and has no history of prior 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; and,
4. IRS did not determine a fraud penalty against the person for an underpayment of income tax for the year in question due to the failure to report income related to any amount in a foreign account

Normal FBAR Penalty Mitigation Guidelines for Violations Occurring After October 22, 2004 - Per Person Per Year

L1-2**Non-Willful (NW) Penalties**

To Qualify for Level I-NW - Determine Aggregate Balances	If the maximum aggregate balance for all accounts to which the violations relate did not exceed $50,000 at any time during the year, Level I — NW applies to all violations. Determine the maximum balance at any time during the calendar year for each account. Add the individual maximum balances to find the maximum aggregate balance.

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Level I-NW Penalty is	$500 for each violation, not to exceed an aggregate penalty of $5,000 for all violations.
To Qualify for Level II-NW - Determine Account Balance	If Level I-NW does not apply and if the maximum balance of the account to which the violations relate at any time during the calendar year did not exceed $250,000, Level II-NW applies to that account.
Level II-NW Penalty is	$5,000 for each Level II-NW account violation, not to exceed 10% of the maximum balance in the account during the year
To Qualify for Level III-NW	If Level I-NW does not apply and if the maximum balance of the account to which the violations relate at any time during the calendar year was more than $250,000, Level III-NW applies to that account.
Level III-NW is	$10,000 for each Level III-NW account violation, the statutory maximum for non-willful violations.
Willfulness Penalties	
To Qualify for Level I - Determine Aggregate Balances	If the maximum aggregate balance for all accounts to which the violations relate did not exceed $50,000, Level I applies to all accounts. Determine the maximum balance at any time during the calendar year for each account. Add the individual maximum balances to find the maximum aggregate balance.
Level I Penalty is	The greater of $1,000 per violation or 5% of the maximum balance during the year of the account to which the violations relate for each violation.
To Qualify for Level II — Determine Account Balance	If Level I does not apply and if the maximum balance of the account to which the violations relate at any time during the calendar year did not exceed $250,000, Level II applies to that account.
Level II Penalty is per account	The greater of $5,000 per violation or 10% of the maximum balance during the calendar year for each Level II account.
To Qualify for Level III	If the maximum balance of the account to which the violations relate at any time during the calendar year exceeded $250,000 but did not exceed $1,000,000, Level III applies to that account.
Level III Penalty is per account.	The greater of (a) or (b): (a) 10% of the maximum balance during the calendar year for each Level III account, or (b) 50% of the closing balance in the account as of the last day for filing the FBAR.
To Qualify for Level IV	If the maximum balance of the account to which the violations relate at any time during the calendar year exceeded $1 million, Level IV, the statutory maximum, applies to that account.
Level IV Penalty is per account the statutory maximum	The greater of (a) or (b): (a) $100,000, or (b) 50% of the clos-

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ing balance in the account as of the last day for filing the FBAR.

Exhibit 4.26.16-3 (07-01-2008) Last Chance Compliance Initiative (LCCI) Penalty Mitigation Guidelines for FBAR Violations Occurring before October 23, 2004

LCCI FBAR Mitigation Penalty Level Calculation

Calculate the aggregate highest balance on the same day **during the tax year under examination for all unreported accounts.**

- **If the amount is less than $20,000, use the level 1 guideline below.**
- **If the amount is $20,000 or more, use the level 2 guidelines below.**

LCCI FBAR Level 1 Mitigation Penalty Calculation

(To be used when the highest balance for all unreported accounts is less than $20,000).

Step 1 - Calculate "preliminary mitigation penalty" amount:

For each account, multiply the maximum value of the account during the year of examination by 5%.

For each account, determine the great of: a) the amount (not to exceed $100,000) equal to the balance in the account at the time of the violation (the opening balance of the account on 7/1 of the subsequent year), or b) $25,000.

Note:

This is the statutory maximum limit to any FBAR penalty.

Step 3

Compare the amount calculated in Step 1 to the amount determined in step 2.

Step 4

If the amount calculated in Step 1 is less than the amount determined in step 2, then asses the amount calculated in Step 1.

Step 5

If the amount calculated in Step 1 is greater than the amount determined in step 2, then assess the amount determined in step 2.

LCCI FBAR Level 2 Mitigation Penalty Calculation

(To be used when the highest balance for all unreported accounts isat least $20,000)

Step 1 - Calculate "preliminary mitigation penalty" amount:

For each account, multiply the maximum value of the account during the year of examination by 10%.

Step 2 - Determine "maximum limits" of the penalty:

For each account, determine the greater of a) the amount (not to exceed $100,000) equal to the balance in the account at the time of the violation (the opening balance of the account on 7/1 of the subsequent year), or b) $25,000.

Note:

This is the statutory maximum limit to any FBAR penalty.

Step 3

Compare the amount calculated in Step 1 to the amount determined in step 2.

Step 4

If the amount calculated in step 1 is less than the amount determined in Step 2, then assess the amount calculated in Step 1.

Step 5

If the amount calculated in Step 1 is greater than the amount determined in Step 2, then assess the amount determined in Step 2.

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Exhibit 4.26.16-4 (07-01-2008) Last Chance Compliance Initiative (LCCI) Penalty Mitigation Guidelines for FBAR Violations Occurring After October 22, 2004.

The Bank Secrecy Act (BSA) allows the Secretary of the Treasury some discretion in determining the amount of penalties for violations of the FBAR reporting and record keeping requirements. There is a penalty ceiling but no minimum amount. This discretion has been delegated to the FBAR examiner.

- The examiner may determine that the facts and circumstances of a particular case do not justify a penalty.
- If there was an FBAR violation but no penalty is appropriate, the examiner should issue the FBAR warning letter, Letter 3800.

When a penalty is appropriate, IRS has established penalty mitigation guidelines so that the penalties determined through the examiner's discretion are uniform. The examiner may determine that:

- A penalty under these guidelines is not appropriate, or
- A lesser amount than the guidelines provide is appropriate.

The examiner must make this determination with the written approval of the examiner's manager. The examiner's workpapers must document the circumstances that make mitigation of the penalty under these guidelines appropriate.

To qualify for mitigation, the person must meet all four criteria:

1. The person must meet all of the conditions necessary to qualify for the Last Chance Compliance Initiative (LCCI);
2. The person has no history of criminal tax or BSA convictions for the preceding ten years and has no history of prior FBAR penalty assessments;
3. 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; and,
4. The person cooperated during the examination.

As a part of the LCCI program, the FBAR penalty is only imposed for the same year that the fraud penalty is asserted under the LCCI guidelines. The FBAR penalty must be paid in full at the time of the LCCI agreement.

C1-2**Last Chance Compliance Initiative (LCCI) Penalty Mitigation Guidelines for FBAR Violations Occurring After October 22, 2004**

L1-2**Non-Willful (NW) Penalties**	
To Qualify for Level I-NW — Determine Aggregate Balances	If the maximum aggregate balance for all accounts to which the violations relate did not exceed $50,000 at any time during the year, Level I-NW applies to all violations. Determine the maximum balance at any time during the calendar year for each account. Add the individual maximum balances to find the maximum aggregate balance.
Level I-NW Penalty is	$500 for each violation, not to exceed an aggregate penalty of $5,000 for all violations.
To Qualify for Level II-NW — Determine Account Balance	If Level I-NW does not apply and if the maximum balance of the account to which the violations relate at any time during the calendar year did not exceed $250,000, Level II-NW applies to that account.
Level II-NW Penalty is	$5,000 for each Level II-NW account violation, not to exceed ten per cent of the maximum balance in the account during the year
To Qualify for Level III-NW	If Level I-NW does not apply and if the maximum balance of

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	the account to which the violations relate at any time during the calendar year was more than $250,000, Level III-NW applies to that account.
Level III-NW is	$10,000 for each Level III-NW account violation, the statutory maximum for non-willful violations.
Willfulness Penalties	
To Qualify for Level I - Determine Aggregate Balances	If the maximum aggregate balance for all accounts to which the violations relate did not exceed $50,000, Level I applies to all accounts. Determine the maximum balance at any time during the calendar year for each account. Add the individual maximum balances to find the maximum aggregate balance.
Level I Penalty is	The greater of $1,000 per violation or 5% of the maximum balance of the account during the year to which the violations relate for each violation.
To Qualify for Level II — Determine Account Balance	If Level I does not apply and if the maximum balance of the account to which the violations relate at any time during the calendar year did not exceed $250,000, Level II applies to that account.
Level II Penalty is per account	The greater of $5,000 per violation or 10% of the maximum balance during the calendar year for each Level II account.
To Qualify for Level III	If the maximum balance of the account to which the violations relate at any time during the calendar year exceeded $250,000 but did not exceed $1,000,000, Level III applies to that account.
Level III Penalty is per account:	The greater of (a) or (b): (a) 10% of the maximum amount during the year for each Level III account or (b) 50% of the closing balance in the account as of the last day for filing the FBAR.
To Qualify for Level IV	If the maximum balance of the account to which the violations relate at any time during the calendar year exceeded $1 million, Level IV, the statutory maximum, applies to that account.
Level IV Penalty is the statutory maximum.	The greater of (a) or (b): (a) $100,000 or (b) 50% of the closing balance in the account as of the last day for filing the FBAR.

Section 17. Report of Foreign Bank and Financial Accounts (FBAR) Procedures

4.26.17 Report of Foreign Bank and Financial Accounts (FBAR) Procedures

- 4.26.17.1 FBAR Procedures Overview
- 4.26.17.2 FBAR Procedures Starting the Case - Related Statute Memorandum
- 4.26.17.3 FBAR Case File Procedures

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• 4.26.17.4 Closing the FBAR Case
• 4.26.17.5 FBAR Special Procedures

4.26.17.1 (05-05-2008) FBAR Procedures Overview

1. The Report of Foreign Bank and Financial Accounts (FBAR) requires procedures that are very different from both other Bank Secrecy Act (BSA) cases and tax cases, although FBAR violations are often found in these other cases.
2. A separate FBAR file must always be set up if there appears to be an FBAR violation, regardless of whether or not a penalty is asserted.
3. If the examiner notes that a Foreign Bank and Financial Accounts Report TD-F 90-22.1 (FBAR) apparently should have been filed during a tax, Form 8300 or BSA examination, the examiner will determine:
   A. Whether the FBAR was required; and if so
   B. Whether the FBAR was filed; and if so
   C. Whether the records required by the FBAR instructions and 31 C.F.R. 103.32 were retained.
4. FBAR law and examination requirements are detailed in IRM 4.26.16. This section (IRM 4.26.17) provides the procedures to apply to an FBAR examination.
5. When an FBAR issue arises in the course of an Offshore Voluntary Compliance Initiative (OVCI) or Last Chance Compliance Initiative (LCCI) or other special initiative, the examiner should use the FBAR procedures for those initiatives.

4.26.17.2 (01-01-2007) FBAR Procedures Starting the Case - Related Statute Memorandum

1. Information relevant to a Title 26 (Internal Revenue Code) case that is also relevant to an FBAR case may be obtained during a tax examination or a Form 8300 examination.
   A. For example, bank account information is a necessary part of an income probe, and may reveal the existence of a foreign account requiring the filing of an FBAR.
   B. The examiner should not ask interview questions or request documents that are only relevant to the FBAR examination without first obtaining a related statute memorandum signed by the examiner's Territory Manager.
   C. Neither interviews nor Information Document Requests (IDRs) in a Title 26 case should request documents only needed for the FBAR examination, such as the FBAR itself, prior to a related statute determination signed by the examiner's Territory Manager.
   D. If the source of the FBAR information is a Title 26 examination, including a Form 8300 examination, the information acquired is return information protected by IRC Section 6103. The examiner must obtain a related statute determination, signed by a Territory Manager before using the return information in an FBAR case.
   E. A related statute determination is a good faith determination with respect to the present case, that the apparent FBAR violation was in furtherance of an apparent Title 26 violation.
   F. A related statute determination is necessary to allow the examiner to use the information obtained from a Title 26 examination in the FBAR examination.
   G. Without a related statute determination, Title 26 information cannot be used in the Title 31 FBAR examination. Any such use could subject the persons making the disclosure to penalties for violating the disclosure provisions protecting Title 26 return information.
   H. The Related Statute Memorandum (RSM) also serves as an input document for the FBAR database maintained at the Detroit Computing Center.
2. For an in depth discussion of the related statute determination, its basis in IRC Section 6103, the factors in making the determination, and its effect, see IRM 4.26.14, Disclosure.

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4.26.17.2.1 (01-01-2007) Obtaining Related Statute Determination

1. In obtaining a related statute determination, the examiner will prepare the Foreign Bank and Financial Accounts Report Related Statute Memorandum - Form 13535 (RSM).
   A. The RSM should be completed in full after discussion with the group manager.
   B. Each year requires a separate RSM to facilitate tracking of the statute of limitations.
   C. A separate RSM is required for each person required to file an FBAR, even if a joint tax return has been filed.
   D. The RSM is used as the initial input document for the monitoring of FBAR cases. All the information required in the RSM will be used to track the FBAR case and provide information to the Department of the Treasury and Congress in required annual reports.
2. The examiner will forward the FBAR file with the RSM through the group manager, who will initial to indicate concurrence and forward to the examiner's Territory Manager.
3. The Territory Manager will:
   A. Determine whether the apparent FBAR violations are in furtherance of an apparent Title 26 violation and sign the determination portion of the related statute memorandum. The Territory Manager does not have to be certain that there was an FBAR violation and that the violation was made in furtherance of a Title 26 violation. The Territory Manager can make a determination based on apparent violations, but this determination must be made in good faith.
   B. Return the file with the related statute determination through the examiner's group manager to the examiner.

4.26.17.2.2 (05-05-2008) Procedures Following The Related Statute Determination

1. Following the Related Statute determination, if the Territory Manager has determined that the apparent FBAR violations are not in furtherance furtherance of an apparent violation of Title 26, the examiner places the RSM determination in the Title 26 case file. This terminates the examiner's FBAR responsibilities. The examiner will not conduct an FBAR examination.
2. If the Territory Manager has determined that the apparent violations in the FBAR case are in furtherance of an apparent violation of Title 26 in the tax case, the evidence acquired in the Title 26 case can be used in the FBAR case and the FBAR case can begin. If the FBAR case is opened, the examiner will fax the RSM determination to the Detroit Computing Center (DCC) at Fax 313-234-2278. The original RSM determination and the Fax Transmission Report are retained in the case file.
3. DCC will enter the RSM information into the FBAR database which starts the monitoring of the FBAR case for statute purposes.
4. The examiner will download the FMD, Form 13536, from the IRS Forms and Publications intranet web site and complete the entity information.
5. The examiner will set up the FBAR case file, place the original RSM in the case file and proceed with the FBAR examination. The examiner will update the FMD as needed and forward the updated FMD to DCC to keep the database up to date. The FMD is sent to DCC when the case is closed from the group.

4.26.17.2.3 (05-05-2008) Cases where No Related Statute Memorandum (RSM) Needed

1. If the examiner is conducting an examination under the BSA, a related statute determination is not needed to examine for FBAR compliance. This is because no information from a tax examination or other 6103 protected source is involved.
2. The examiner should request and provide pertinent information necessary to determine compliance with BSA reporting and record keeping requirements, which include those relating to the FBAR. Examiners should utilize the FBAR lead sheet and make sufficient inquiries to detect potential FBAR violations in all BSA cases. Without a related

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statute determination, however, the examiner is precluded from accessing Title 26 data, such as the Information Document Retrieval System (IDRS).

3. The examiner uses the Title 31 FBAR Lead Sheet to document the examination steps taken during the FBAR portion of the BSA examination. Examination steps include determining if there is a requirement to file the FBAR and maintain required records and if the requirements were met. FBAR law and evidence is discussed in IRM 4.26.16.

4. If there appears to be no FBAR violation, a separate case file is not set up. If there appears to be an FBAR violation, a separate FBAR case file must be set up. FBAR cases cannot be included in the regular BSA case file. They are tracked on a separate database. FBAR penalties are assessed by IRS and the separate case file is necessary to support asserting penalties or issuing a warning letter. Non-FBAR related BSA penalties are referred to FinCEN for assessment using procedures set out in IRM 4.26.8, Special Procedures.

5. To start the FBAR case when there is no RSM:

A. The examiner will download the FMD, Form 13536, from the IRS Forms and Publications intranet web site, and use it as an input document for the Detroit Computing Center (DCC).

B. The examiner will complete the entity information and as much as possible of the other information requested on the FMD.

C. The examiner will note in an attached memorandum that this FMD is to be used as an originating document, like a related statute memorandum, by DCC, and that there is no RSM because there is no Title 26 information being used.

D. The examiner will fax the FMD and the attached memorandum explaining the reason that there is no RSM to the DCC FBAR Database at Fax 313-234-2278. The original FMD and the Fax Transmission Report are retained in the FBAR case file.

E. DCC will enter the information from the FMD received from the examiner on the FBAR database.

F. The examiner will update the FMD as needed, but will not forward it to DCC until the case is closed out of the group.

4.26.17.3 (05-05-2008) FBAR Case File Procedures

1. Whether the examiner is assigned an FBAR case with no other BSA or tax issues, or the examiner uncovered apparent FBAR violations in the course of a tax or BSA examination, the examiner will set up a separate FBAR case file that may include:

A. Agent Activity Record — FBAR time on this record is charged to Activity Code 545.

B. Related Statute Determination if appropriate.

C. FBAR lead sheet and work papers.

D. A brief summary memorandum explaining the FBAR violation(s) if any.

E. Copy of any delinquent FBAR(s) annotated in red on the top “Secured by Examination”, if available.

2. When the case is closed, the examiner will include in the file:

A. FBAR Monitoring Document (FMD), providing closing information for the FBAR database and

B. closing documents as appropriate.

3. Closing documents may include:

A. Letter 3800, Waming Letter for Apparent Foreign Bank and Financial Accounts Report Violations (copy)

B. Letter 3709, FBAR 30 Day Letter (transmitting Agreement for Assessment and Collection, F-13449) (copy)

C. Form 13449, Agreement to Assessment and Collection of Penalties Under 31 U.S.C. Sections 5321(a)(5) and 5321(a)(6) (original)

D. Notice 1330, Information on Making FBAR Penalty Payment By Check (copy)

E. Power of Attorney document (original)

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4. DCC will include as appropriate:

A. Form 13448, Penalty Assessments Certification Summary (Title 31 FBAR) (internal document)

B. Letter 3708, Notice and Demand for Payment of FBAR Penalty (copy)

C. Notice 1330, Information on Making FBAR Penalty Payment By Check (copy)

4.26.17.3.1 (05-05-2008) Working the FBAR Case

1. The examiner conducting the FBAR examination will:

A. Set up work papers on the FBAR issues in FBAR file. Each issue identified in IRM 4.26.16.3, FBAR Filing Criteria, should be addressed in determining if a U.S. person was required to file an FBAR, whether the FBAR was filed when required, and whether required records were kept. If facts have been derived from other cases (such as a related income tax case), the examiner must make copies for the FBAR case file of any documents needed for the FBAR case.

B. Review FBAR issues with the taxpayer/BSA entity along with other examination issues and make a decision concerning violations and penalties.

2. Other procedural items include:

A. A person may authorize a representative to receive information with respect to the FBAR examination by using IRS Form 2848, Power of Attorney and Declaration of Representative, if a related statute determination has been made. In an FBAR case that does not involve a related income tax case, a general power of attorney (POA) must be used (see IRM 4.26.8.2). The power of attorney (general or Form 2848) is retained in the case file. The FMD should always be updated with POA information. Whenever a Form 13449 is sent to DCC for penalty assessment, a copy of any POA should accompany it.

B. FBARs are due to be filed by June 30 of the calendar year succeeding the year reported. An extension for filing a tax return is not valid for the FBAR. There are no procedures at present for granting extensions of time to file FBARs.

C. A BSA summons, TD F 90-22.31, rather than a Title 26 summons must be used if information that is purely BSA information is sought. For BSA summons procedures see IRM 4.26.8.3. For information that can be used in both a Title 26 and an FBAR case, a Title 26 summons is valid.

D. A waiver of the statute of limitations for the Title 26 case will not waive the statute of limitations on the FBAR case. The statute of limitations on assessment of the FBAR penalties is found in 31 U.S.C. 5321(b)(1). It is six years from the date of the transaction. In the case of filing violations, the date of the transaction is the due date for filing the FBAR; that is, June 30 of the calendar year following the year to be reported. In the case of a recordkeeping violation, the date of the transaction is the date that the examiner first requests the records required by 31 C.F.R. 103.32. Generally, section 103.32 does not require records to be maintained for more than five years. If a waiver of the statute of limitations on assessment of the FBAR penalty is needed, consult the BSA FBAR Analyst for assistance.

3. Assistance in working the FBAR case is available from:

A. Technical Services FBAR specialists: A list of these specialists is available on the SB/SE BSA web site at http:// SBSE.web.irs.gov/FR/BSA/default.htm.

B. SB/SE Counsel: Local counsel is available for FBAR questions. SB/SE Counsel has also designated SB/SE Counsel Area FBAR Coordinators. A list of these specialists is available on the SB/SE Counsel web site at http:// counsel.web.irs.gov/sbse/admin/.

C. BSA FBAR Analyst: A list of BSA Analysts is on the BSA web site at http://SBSE.web.irs.gov/FR/BSA/default.htm.

4.26.17.4 (01-01-2007) Closing the FBAR Case

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1. Closing procedures vary depending on the results of the examination.

2. In all cases, the examiner will support the determination in a summary memorandum with references to the work papers. The summary memorandum should show all years opened and the determination reached for each year. If several years are opened but a penalty is asserted only with respect to one year, the summary memorandum should provide an explanation such as "This is an LCCI case. Under LCCI guidelines an FBAR penalty will be asserted with respect to only one year" or "It is the examiner's judgment that a penalty with respect to only two years is appropriate in view of the facts and circumstances of the case."

3. In all cases, the examiner will complete an FBAR Monitoring Document (FMD) Form 13536 for each year.

4. There are different closing procedures depending on whether there is no violation, a violation without penalty, negligence or a nonwillful violation, a willful violation, or a referral to Criminal Investigation.

4.26.17.4.1 (05-05-2008) Closing the FBAR Case - No Violation

1. If no FBAR violation is found, the examiner will:
   A. Complete a summary memorandum and FBAR Monitoring Document (FMD).
   B. Close the FBAR case file to the group manager.
2. The group manager will:
   A. Review the FBAR case file for both technical and procedural issues and note this on the activity record.
   B. Indicate on the FMD the date closed from the group.
   C. Forward on a 3210 the FBAR file to Internal Revenue Service, P.O. Box 33113, Detroit, MI 48232-0113.
3. Detroit Computing Center (DCC) will:
   A. Enter the information from the FMD into the FBAR database.
   B. Note on the FBAR database in the comments field when and if a follow-up FBAR examination is needed.
   C. Place the case file in the FBAR historic files.

4.26.17.4.2 (05-05-2008) Closing the FBAR Case - Warning Letter

1. The examiner may, after discussion with the group manager, issue an FBAR Warning letter, Letter 3800, if there is a violation of the FBAR requirements but no penalty is being asserted.
   A. The examiner may determine that there was a violation but that penalties are not warranted in view of the facts and circumstances of the case.
   B. A Letter 3800 is also issued when there is evidence of a negligent violation by an individual (not a business) prior to October 23, 2004.
   C. Letter 3800 is not used in Last Chance Compliance Initiative (LCCI) cases for the years when the FBAR penalties are forgiven as a part of the LCCI agreement.
2. If Letter 3800 is issued, the closing procedures are:
   A. The examiner will issue Letter 3800 and a copy to the person apparently in violation of the FBAR requirements and retain a copy in the file.
   B. This person will return any delinquent or corrected FBAR(s) and a copy of the warning letter to the examiner.
   C. Delinquent forms will be processed in accordance with instructions in this chapter. *See IRM 4.26.17.4.8*.
   D. The examiner will also complete a summary memorandum and FBAR Monitoring Document (FMD) and close the FBAR case file to the group manager.
3. The group manager will:
   A. Review the FBAR case file for both technical and procedural issues and note this on the activity record.
   B. Indicate on the FMD the date closed from the group.
   C. Forward on a 3210 the FBAR file to Internal Revenue Service, P.O. Box 33113, Detroit, MI 48232-0113.

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4. Detroit Computing Center (DCC) will:

A. Enter the information from the FMD into the FBAR database.

B. Note on the FBAR database when a follow-up FBAR examination is needed.

C. Remove the original FBARs for entry on CBRS and retention in the Federal Records System.

D. Place the case file in the FBAR historic files.

4.26.17.4.3 (05-05-2008) Closing the FBAR Case with Penalties

1. If the examiner, after discussion with the group manager, determines that it is appropriate to assert an FBAR penalty and that a referral to Criminal Investigation is not appropriate or has been declined, the examiner will assert penalties in accordance with the FBAR penalty guidelines. See IRM 4.26.16 for the FBAR penalty computation rules and penalty mitigation guidelines.

2. Once the penalties have been determined and just before the examiner is ready to issue Letter 3709, the FBAR 30 Day Letter, and Form 13449, FBAR Agreement to Assessment and Collection, the examiner will submit the FBAR case file to an SB/SE Counsel Area FBAR Coordinator.

3. Each of the eight SB/SE Division Counsel Areas has at least one Counsel FBAR Area Coordinator. A current listing of the Area Coordinators can be accessed on the SB/SE Counsel "Contacts" web page at: http:// counsel.web.irs.gov/sbse/admin/. The examiner may also call local counsel for the name of the appropriate FBAR coordinator or for other assistance with respect to FBAR cases.

4. Review by Counsel is not required:

A. In special program agreement situations such as LCCI. This will allow the special rules of those programs to prevail. However special programs which do not require a special agreement, such as related offshore income tax cases, do require Counsel review of a related FBAR case.

B. When the examiner has determined that there is no FBAR issue or in cases where the examiner has determined that the issuance of Letter 3800, the FBAR Warning Letter, is appropriate.

5. Counsel will:

A. Render its legal advice within 45 days. If coordination with an Associate Chief Counsel is necessary and will cause a delay, Counsel will inform the FBAR examiner of the potential delay. Counsel will work with the examiner to establish a shorter time frame for review if expedited review is needed. b) Prepare a written memorandum of review of the FBAR case. If Counsel recommends issuance of Letter 3709, the FBAR 30-day letter, the review will be designed to assist Appeals in the event the case is appealed. If Counsel does not recommend issuance of Letter 3709, the review will state the reasons for the disagreement. If the disagreement is based upon inadequate factual development, the review should recommend areas for further examination.

6. After the Counsel review has been received and agreed that penalties are appropriate, the examiner will:

A. Issue Letter 3709, the FBAR 30 day letter, and

B. Transmit with Letter 3709 the Form 13449, FBAR Agreement to Assessment and Collection. Although Form 13449 is shown as an Agreement, it also functions as the examiner's report of FBAR violations. It is the basis for the FBAR penalty assessment(s).

C. Provide the customer Notice 1330, Information on Making FBAR Penalty Payment by Check, and retain a copy in the file. This notice advises that the payment will be recorded electronically and that the person submitting payment will not receive a copy of the cancelled check.

D. Discuss payment. Payment on the FBAR penalty must be evidenced by a separate check or money order made out to the United States Treasury showing the FBAR account number and year. Separate checks or money orders should be written for FBAR and tax payments. When a receipt is desired, payment should be made by money order or cashiers check. The examiner should not issue a tax receipt form, such as Form 809.

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E. No interest accrues on FBAR penalties prior to assessment, therefore only the penalty amount would be owed if full payment is made ??(IT,IB,D091028) filer. Under 31 U.S.C. § 3717(b), interest begins to accrue on the date the FBAR notice of penalty assessment is mailed but no interest is owed on payments received within thirty days from the date a notice of the penalty amount due is first mailed to the filer. In addition to interest, a six percent delinquency penalty applies to amounts remaining unpaid ninety days from the date a notice of the penalty amount due is first mailed to the filer. The applicable interest rate is found at http:// fms.treas.gov/cvfr/index.html. This rate is updated at least annually but may be updated quarterly if certain criteria, identified in § 3717(a)(2), are met.

4.26.17.4.4 (05-05-2008) Closing the FBAR Case With Penalties Agreed

1. If the person apparently violating the FBAR requirements agrees to assessment of the penalties, the person returns to the examiner:

A. Delinquent FBARs

B. Signed and dated Form 13449, FBAR Agreement to Assessment and Collection

C. Possibly partial or full payment.

2. The examiner will:

A. Place the signed Agreement Form 13449 in the FBAR case file.

B. Process delinquent forms in accordance with instructions in this chapter. *See IRM 4.26.17.4.8*.

C. Complete a summary memorandum and FBAR Monitoring Document (FMD).

D. Forward the FBAR case for closure to the group manager.

3. The group manager will:

A. Review the FBAR case file for both technical and procedural issues and note this on the activity record.

B. Indicate the date the case was closed from the group.

C. Forward on a 3210 the FBAR file to Internal Revenue Service, P.O. Box P.O. Box 33113, Detroit, MI 48232-0113.

4. DCC will:

A. Enter the information from the FMD to the FBAR database.

B. Note on the FBAR database that a follow-up FBAR civil examination referral is needed.

C. Forward the penalty assessment information to the Field Director, Compliance Services, Cincinnati, Small Business/Self-Employed or her designee. This designated official completes the assessment using Form 13448, Penalty Assessments Certification Summary. Form 13448 is for internal use only. It validates the assessment; i.e., it documents the Service's determination that the penalty assessed is legally due and payable. It functions in the same way as Form 23C in the Campuses. A copy of Form 13448 is placed in the case file.

D. If the penalty has been paid in full, place the case file in the FBAR historic files.

E. If the penalty is not paid in full, issue the Letter 3708. The Letter 3708 should be sent certified mail with a return receipt requested. Enter the interest rate on Letter 3708 according to the interest rate currently published by the Financial Management Service (FMS) at http:// fms.treas.gov/cvfr/index.html. A copy of the Letter 3708 is sent to the Power Of Attorney (POA) as appropriate. DCC should check the FMD to determine if there is a POA. A copy of the dated Letter 3708 should be placed in the case file.

F. Forward the collection information to FMS and place the case file in the FBAR historic files.

4.26.17.4.5 (01-01-2007) Closing the FBAR Case - Payment

1. (1) If there is any payment, the examiner will:

A. Photocopy the check or money order.

B. Copy Form 13449, front and back and paper clip the check or money order to the copy.

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C. Complete Form 3210 describing all documents.

D. Forward by certified mail the payment, copy of Form 13449, and Form 3210 to the FBAR Payment post office box used exclusively for FBAR payments: Internal Revenue Service, P.O. Box 33115, Detroit, MI 48232-0115. This is not the same post office box used for forwarding the file.

E. If any payment is made, the examiner will not execute a Payment Posting Voucher, Form 3244 for any payments received. If Form 3244 is inadvertently executed, the examiner will be responsible for tracing the payment to ensure that it is refunded from the tax module. The examiner will then need to obtain another payment which will be sent to DCC for posting to the FBAR database as above.

2. Detroit Computing Center (DCC) will record and process the payment utilizing as appropriate:

A. Form 13448, Penalty Assessments Certification Summary (Title 31 FBAR) (internal document)

B. Letter 3708, Notice and Demand for Payment of FBAR Penalty (copy)

C. Notice 1330, Information on Making FBAR Penalty Payment by Check

4.26.17.4.6 (01-01-2007) Closing the FBAR Case Unagreed

1. If an FBAR penalty is proposed but not agreed to, the examiner waits 45 days to see if the person will appeal as provided in Letter 3709.

2. In order to appeal:

A. The person against whom an FBAR penalty is proposed must mail a written protest in duplicate to the examiner that is postmarked before the designated response date, which is listed in the Letter 3709.

B. The protest must contain all the information required in Letter 3709.

C. An appeal requires 180 days remaining on the assessment statute of limitations. The statute of limitations on assessment of a failure to file penalty is six years from the date when the FBAR should have been filed (which is June 30th of the year following the year for which the foreign financial account is being reported).

3. If there is no response from the person against whom an FBAR penalty is proposed, the penalty is assessed and the collection process begins.

4. The examiner will:

A. Complete a summary memorandum and FBAR Monitoring Document.

B. Forward the FBAR case for closure to the group manager.

5. The group manager will:

A. Review the FBAR case file for both technical and procedural issues and note this on the activity record.

B. Indicate the date the case is closed from the group.

C. Forward the FBAR file on a 3210 to Internal Revenue Service, P.O. Box 33113, Detroit, MI 48232-0113.

6. Detroit Computing Center will:

A. Enter the information from the FMD to the FBAR database.

B. Note on the FBAR database that a follow-up FBAR civil examination is needed.

C. Forward the penalty assessment information to the Field Director, Compliance Services, Cincinnati, Small Business/Self-Employed.

D. This designated official completes the assessment using Form 13448, Penalty Assessments Certification Summary. Form 13448 is for internal use only. It validates the assessment, i.e., it documents the Service's determination that the penalty assessed is legally due and payable. It functions in the same way as Form 23C in the Campuses. A copy of Form 13448 is placed in the case file.

E. If the penalty has been paid in full, the case file can now be placed in the FBAR historic files.

F. If the penalty has not been paid in full, DCC will issue the Letter 3708, Notice and Demand for Payment. The letter 3708 should be sent by certified mail, return receipt requested. A copy should be placed in the case file. DCC

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enters the interest rate on Letter 3708 according to the interest rate currently published by the Financial Management Service (FMS) at http://fms.treas.gov/cvfr/index.html. DCC then places the case file in the FBAR historic files and forwards the collection information to the FMS.

4.26.17.4.7 (01-01-2007) Closing the FBAR Case Appealed

1. If the person apparently violating the FBAR requirements appeals and there is no related Title 26 case or the related Title 26 case is agreed, the following procedures apply.

2. The examiner will:

A. Ensure that any documents needed in any related cases or in the FBAR case are copied so that there is a fully documented case file for each.

B. Note on the Transmittal Letter that the case is an FBAR category case, UIL 9999.99-01, in the Appeals Coordinated Issue (ACI) Program. The Appeals Officer must contact the Appeals FBAR Coordinator prior to scheduling the initial conference. The coordinator can be reached at (818) 242-8143 x3014.

C. Forward, through the group manager, an FMD to DCC so that the appeal can be entered on the FBAR database.

3. The group manager will:

A. Review the FBAR case file for both technical and procedural issues and note this on the activity record.

B. Indicate the date the case is closed from group.

C. Complete and forward the FMD to the DCC, at Internal Revenue Service, P.O. Box 33113, Detroit, MI 48232-0113.

D. Forward the case to Appeals following regular case processing procedures.

4. DCC will record the appeal on the FBAR database and continue to monitor the statute of limitations. DCC will contact Appeals when the statute of limitations has less than a year to expire and thereafter on a regular basis.

5. Appeals Officers will follow procedures outlined in "Foreign Bank and Financial Accounts Requirements Guidance for Appeal Officers" available on the Appeals web site. Appeals will close the FBAR case through DCC following the closing procedures for examiners found in this section.

6. In addition to the above procedures which are to be used in all appealed cases, where there is a related Title 26 case, the examiner, the group manager, and Appeals will discuss whether the examiner should hold the FBAR case until the Title 26 case is closed or forwarded to Appeals. The different statutes of limitation are important in this discussion.

4.26.17.4.8 (05-05-2008) Delinquent FBAR Processing

1. Examiners should secure delinquent or amended FBAR forms, unless a criminal referral is contemplated. In the case of a criminal referral, the the examiner should not solicit delinquent or amended forms, but should accept them if offered.

2. The examiner will date stamp the original delinquent FBAR form with the date received and label at the top IN RED: "Secured by BSA Examination."

3. A copy of the delinquent form should be made and placed in the case file.

4. Original FBAR forms are to be mailed to:

Internal Revenue Service
CTR Operations
Edit and Error Resolution Mailroom
PO Box 32621
Detroit, MI 48232

5. DCC will post these delinquent FBAR forms with a Saturday Julian date. This will clearly identify them as forms

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secured by BSA examiners and will stop all correspondence from DCC.

6. If the entity refuses to provide delinquent FBARs or delays past 30 days after receipt of Letter 3800, the examiner and manager will make a determination concerning the appropriate penalty. Failure to provide delinquent FBARs is a failure to cooperate which may prevent mitigation of penalty amounts.

4.26.17.5 (01-01-2007) FBAR Special Procedures

1. Procedures used in an FBAR examination are substantially different from those used in an income tax examination because generally, none of the provisions of Title 26 apply to FBAR examination.

2. Some of the special procedures that may be encountered in an FBAR examination include procedures for:

A. A Related Statute Memorandum

B. Securing a Power of Attorney

C. A BSA Summons

D. The Criminal Referral Process

E. Waiving Statute of Limitations

F. Bankruptcy

4.26.17.5.1 (01-01-2007) Related Statute Determination

1. Related Statute Determination is discussed in IRM 4.26.14.

4.26.17.5.2 (01-01-2007) FBAR Power of Attorney

1. A power of attorney is a document that evidences the creation of a relationship between two people who are designated as the “principal” and and the “agent”. The principal designates the agent in the document, and the agent is authorized to act on the principal's behalf - to stand in the shoes of the principal - for whatever business the power of attorney permits.

2. During the course of the FBAR compliance examination:

A. The person under examination may request representation.

B. A representative may ask to submit Form 2848 to represent the person under examination.

3. Form 2848 was developed to meet requirements relating to tax. It is generally inappropriate for BSA examinations, including FBAR examinations.

4. The BSA examiner can accept a general power of attorney valid under state law and, in cases where a related statute determination has been made, the examiner can accept a Form 2848.

5. Regardless of the type of power of attorney, the original power of attorney should be retained in the FBAR examination file.

4.26.17.5.2.1 (01-01-2007) FBAR Power of Attorney —Related Statute Memorandum Exception

1. Where a related statute determination has been made, a Form 2848 may be accepted.

2. In this case, Line 3 on the Form 2848 reflects either income tax in the first column or 1040 in the second column. For clarity, “FBAR Examination” may be added.

4.26.17.5.2.2 (01-01-2007) FBAR General Power of Attorney

1. The examiner will not draft a general power of attorney but can direct the person under examination to have his or her representative provide a general power of attorney.

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2. The power of attorney should state that it is for the limited purpose of representation of the person during the FBAR examination. All representatives should be named. The same topics generally need to be covered as on a Form 2848. For example, whether or not communications need to be made in duplicate should be addressed.

4.26.17.5.3 (01-01-2007) FBAR Title 31 Summons

1. The examiner must use the BSA summons, TD F 90-22.31, not the Title 26 summons in FBAR examinations that do not have a concurrent Title 26 examination. The BSA summons is only available in hard copy. It is used to summon and require an individual to appear and give testimony and/or produce the books, papers, records, and other data identified as essential to the civil enforcement requirements of the Currency and Foreign Transactions Reporting Act, as amended (31 U.S.C. 5311-5324); section 21 of the Federal Deposit Insurance Act (12 U.S.C. 1829b); and Title 1 of Public Law 91-508 (12 U.S.C. 1951, et seq.)

2. Summons authority, completion, issuance, and special disclosure rules are covered in IRM 4.26.8.

4.26.17.5.3.1 (01-01-2007) FBAR Title 31 Summons Approval

1. A cover memorandum is prepared for the summons package. The memorandum:
   A. Provides a brief history of the case;
   B. Describes the potential FBAR violations; and,
   C. States whether or not the party being summoned will comply with the summons.
2. The memorandum is addressed from the examiner through his/her group manager and SB/SE Division local Counsel to the examiner's Territory Manager.
3. SB/SE Division local Counsel will review the summons:
   A. If disapproved, Counsel and the examiner will work together to resolve the problems.
   B. If approved, Counsel will prepare and send to the Territory Manager a memorandum approving issuance of the Title 31 summons.
4. Only after receipt of the SB/SE Division local Counsel Approval memorandum will the Territory Manager sign (issue) the FBAR summons.
5. The Territory Manager then returns the summons package to the BSA examiner for service of the summons. Procedures for service of the summons are covered in IRM 4.26.8.

4.26.17.5.3.2 (01-01-2007) FBAR Title 31 Summons Enforcement

1. The examiner will report immediately to the examiner's manager, the Territory Manager, and the SB/SE Division local Counsel any refusal to comply or any proceeding brought by the summoned party to quash a summons.
2. The examiner will, in cases where there is a refusal or a proceeding:
   A. Consider recommending enforcement action when the person summoned neglects or refuses to comply.
   B. Review the summons handbook, IRM 25.5.10, for considerations in summons enforcement. The examiner will not refer a summons for enforcement in the situations given in IRM 25.5.10, for example: (i) the summoned party or their representative has contacted the Service and indicated a willingness to comply with the summons but has requested a reasonable extension of time within which to comply or (ii) the summoned party has appeared and denied under oath the possession or control of the documents called for in the summons, unless there is a good reason to believe the contrary.
3. SB/SE Division local Counsel will consider the summons enforcement request.
   A. If SB/SE Division local Counsel believes the summons can be enforced, they will forward the summons enforcement request to the appropriate US Attorney's office.

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B. If SB/SE Division local Counsel believes the summons cannot be enforced, they will notify the examiner.

4.26.17.5.3.3 (01-01-2007) FBAR Title 31 Summons Enforcement Request

1. The examiner will prepare requests for enforcement of an FBAR Title 31 summons using the memorandum report format, to include the following information:

A. The name and full address of the person being summoned;

B. A summary of the pertinent facts in the investigation;

C. Exactly what the Service employee is seeking to obtain;

D. The relevancy of the records sought, including the relevancy of records pertaining to third parties;

E. The need or importance of such evidence to the success or completion of the investigation;

F. If a corporation was summoned, a statement of whether service of the summons has been made on a responsible officer and, if not, why not;

G. The circumstances surrounding contacts with the person summoned, explaining the defense(s) claimed for refusing to comply with the summons, and the circumstances under which the person summoned claimed the defense(s);

H. A transcript (if recorded) or memorandum of interview of the questions asked to the person summoned and the person's responses;

I. A description of any problems involving the imminent expiration of the statutes of limitation;

J. A statement as to any known criminal investigations by other federal agencies of the individual, and, in the case of a corporation, its officers or employees; and,

K. A statement as to any other known requests for summons or subpoena enforcement against the person or related parties.

2. The summons enforcement request memorandum is to be signed by the examiner's Territory Manager. The original and one copy of the summons are transmitted through SB/SE Division local Counsel to the U.S. Attorney's office in which the venue lies.

4.26.17.5.4 (05-05-2008) FBAR Title 31 Criminal Referrals

1. IRS CI has authority to examine for criminal FBAR violations.

A. Treasury Directive 15-41 (December 1, 1992) delegates to the Commissioner of Internal Revenue the authority to initiate investigations of any person, including banks and brokers or dealers in securities, for possible criminal violations of 31 C.F.R. part 103 (except violations of section 103.23).

B. Treasury Directive 15-42 (January 21, 2002), further delegates to the Commissioner investigatory authority over violations of 18 U.S.C. 1956 and 1957 where the underlying conduct is subject to investigation under Title 26 or under the Bank Secrecy Act, or 31 U.S.C. 5311-5332 (other than violations of 31 U.S.C. 5316).

2. Criminal FBAR penalties appear at 31 U.S.C. 5322 and 31 C.F.R. 103.59.

3. Acceptance by Criminal Investigation of an FBAR referral for criminal investigation depends on the evidence establishing willfulness and sometimes other criteria.

A. Willfulness is a question of intent. Willfulness involves the intentional, voluntary violation of a known legal duty.

B. Criminal sentencing in FBAR cases depends on the Federal Sentencing Guidelines. Federal Sentencing Guidelines for money laundering cases including criminal FBAR reporting or recordkeeping violations appear in the U.S. Sentencing Guidelines, section 2S1.3. The relevant statutes require monetary reporting without regard to whether the funds were lawfully or unlawfully obtained.

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4.26.17.5.4.1 (05-05-2008) FBAR Title 31 Criminal Referrals and the Fraud Technical Advisor

1. A Fraud Technical Adviser (FTA) can assist the examiner in determining whether or not there was a willful violation and provide the examiner with information concerning referrals to Criminal Investigation.
2. If the examiner considers that the case warrants referral for possible criminal investigation, the examiner, with the approval of the group manager, will involve an FTA as soon as possible.
3. If the decision to involve the FTA is made, the examiner will fill out the Fraudulent Intent Referral Memorandum (FIRM), Form 13639. The FIRM documents the involvement of the FTA, the plan for developing the case further, and the referral recommendations of the FTA.
4. Any related income tax case submitted for fraud development should follow regular fraud development procedures including completion of Form 11661.
5. If the FTA considers that additional development is warranted, the FTA will provide a written plan of action.
6. If the FTA considers that criminal investigation is not appropriate:
   A. The FTA will so advise the examiner and provide a written explanation of the reason that criminal referral is not appropriate and recommendations respecting civil penalties.
   B. The examiner may then proceed with the FBAR case under FBAR civil procedures.
7. If there are firm indications of willful FBAR violations that warrant referral to Criminal Investigation, the FTA will advise the examiner and the examiner's manager of this determination.
8. The examiner will prepare Form 2797, Referral Report of Potential Criminal Fraud Cases, with a detailed explanation of the FBAR violations. The FTA will assist in the preparation of Form 2797 if requested by the examiner. When preparing Form 2797 for an FBAR referral, the examiner will follow the instructions attached to the form and:
   A. Note that “filer” means the person required to file the FBAR regardless of whether or not the person filed.
   B. Insert FBAR Violation in Item 2f.
   C. Note that Item 3d of the Form 2797 must show that CBRS was checked for FBAR filings, if an FBAR referral to Criminal Investigation is being made.
   D. Document on the Form 2797 Referral to CI and in the work papers the date that the entity was educated about filing and the filing compliance status at the date of the referral.
   E. Omit items 4, 8, and 9.
9. If there is a related tax case, the examiner will:
   A. Prepare a separate Form 2797 for any related tax case, if warranted.
   B. Submit related tax and FBAR referrals to CI at the same time if possible.
   C. Follow procedures established for criminal referrals in IRM 25.1.3.
   D. If a related statute determination is made, a copy of the related statute determination memorandum must be attached to Form 2797.

4.26.17.5.4.2 (01-01-2007) FBAR Title 31 Criminal Referrals and CI

1. If the referral of the FBAR case to Criminal Investigation is declined, the examiner follows the procedures where material violations exist and civil penalties are asserted.
2. If referral to Criminal Investigation is accepted, the examiner will:
   A. Place the Transmittal memorandum that indicates acceptance in the retained FBAR file.
   B. Complete the FBAR Monitoring Document (FMD) showing CI acceptance.
   C. Forward the FMD through the Group Manager to DCC so that the FBAR database can be updated.
3. DCC will:
   A. Enter the information from the FMD to the FBAR database.
   B. Note on the FBAR database that a follow-up FBAR civil examination is needed following the close of the crim-

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inal case.

C. Track the FBAR statute of limitations and advise the examiner's manager when there is less than a year on the statute and then at monthly intervals.

4. Criminal investigation will:

A. Discuss statute problems with the examiner and his manager.

B. Advise the examiner through the FTA about the final disposition of the case.

4.26.17.5.4.3 (01-01-2007) FBAR Procedures After the Criminal Case

1. After completion of the criminal case, the examiner will:

A. Forward any delinquent or corrected FBARs to DCC.

B. Commence any appropriate civil FBAR penalty action.

C. If no civil penalty action is appropriate, the examiner will forward the FBAR case file to Detroit Computing Center (DCC) for placement in the historic files.

2. DCC will then:

A. Update the database.

B. Process any attached FBARs.

C. Place the case file in the historic files.

4.26.17.5.5 (05-05-2008) FBAR Statute of Limitations

1. Title 26 statutes of limitations do not apply to FBAR cases.

2. The statute of limitations on assessment of civil FBAR penalties is six years from the date of the violation.

3. The statute of limitations on bringing suit to collect the assessment of civil penalties is two years from the date of assessment or the date any judgment becomes final in any criminal action under section 5322.

4. The statute of limitations on FBAR criminal penalties is five years from the date the offense is committed.

4.26.17.5.5.1 (01-01-2007) FBAR Statute on Assessment

1. The period of limitation on assessment of FBAR civil penalties is found in 31 U.S.C. 5321(b)(1). Section 5321(b)(1) provides that the Secretary of the Treasury may assess a civil penalty under subsection (a) at any time before the end of the six year period beginning on the date of the transaction with respect to which the penalty is assessed.

2. The date of the transaction for report filing violations is June 30th of the year following the calendar year for which the foreign financial account should be reported.

3. The date of the transaction for recordkeeping purposes is the date that the examiner first requests the records required to be maintained under 31 C.F.R. § 103.32. Note that section 103.32 generally only requires that records be maintained for five years.

4. The date that the FBAR civil penalty is assessed is the date that the IRS designated official delegate stamps the assessment form. The assessment certification form is IRS Form 13448. The designated official is the Operations Officer, Cincinnati Compliance Services, CTR Operations or his/her delegate.

4.26.17.5.5.2 (01-01-2007) FBAR Statute on Collection

1. The period of limitation on collection of FBAR penalties is found in 31 U.S.C. 5321(b)(2). The Secretary may commence a civil action to recover a civil penalty assessed under subsection (a) at any time before the end of the two year period beginning on the later of:

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A. The date the penalty was assessed; or,

B. The date any judgment becomes final in any criminal action under section 5322 in connection with the same transaction with respect to which the penalty is assessed.

2. The date the FBAR penalty is assessed is the date that the IRS designated official stamps IRS Form 13448.

4.26.17.5.5.3 (01-01-2007) Waiving the FBAR Statutes of Limitation

1. FBAR civil statutes of limitation on assessment and collection may be waived.

2. The Service currently does not have any special procedures for soliciting waivers of the statute of limitations on assessment of the FBAR penalty.

3. A person may voluntarity waive the statute of limitations for assessing FBAR penalties.

4.26.17.5.5.4 (01-01-2007) FBAR Statute of Limitation on Criminal Offenses

1. (1) The period of limitation for FBAR criminal penalties is the general criminal statute of limitations found at 18 U.S.C. 3282. This section provides that except as otherwise expressly provided by law, no person shall be prosecuted, tried, or punished for any non-capital offense, unless the indictment is found or the information is instituted within five years next after such offense shall have been committed.

4.26.17.5.6 (01-01-2007) FBAR Bankruptcy Procedures

1. Bankruptcy may occur prior to or subsequent to assessment of an FBAR penalty.

2. If, prior to assessment of the FBAR penalty, the IRS examiner is notified of a (potential) bankruptcy with respect to the person against whom a penalty is proposed, the examiner should:

A. Notify IRS local insolvency unit as soon as possible.

B. Proceed through the examination and assessment process.

C. Send a copy of the first notice of bankruptcy to Internal Revenue Service, Detroit Computing Center, P.O. Box 33113, Detroit, MI 48232-0113, and phone: 313-234-1273.

3. After assessment, if the debtor reports an FBAR penalty as a debt in the bankruptcy petition and schedules, clerks of bankruptcy courts will send notices to: U.S. Treasury, Financial Management Service Birmingham Debt Management Operations Center, P.O. Box 830794, Attn: Debt Service Branch, Birmingham, AL 35283-0794. The Financial Management Service will forward bankruptcy notices to: Internal Revenue Service, Detroit Computing Center, P.O. Box 33113, Detroit, MI 48232-0113. DCC will then provide the bankruptcy account information to the FBAR Penalty Insolvency Bankruptcy Specialist in Insolvency Territory 16.

4. In the pre-assessment bankruptcy cases, the Territory Insolvency Specialist will:

A. Determine if a proof of claim is warranted and if so.

B. Prepare and mail a proof of claim.

5. Post-Assessment FBAR penalty bankruptcy cases will be handled by the Financial Management Service and the IRS insolvency unit.

FBAR—FOREIGN BANK ACCOUNT REPORTING OBLIGATIONS: A PRIMER FOR THE PRACTITIONER

BY KEVIN E. PACKMAN AND ANDREW H. WEINSTEIN [FNa1]

Cross-border investing and multinational clients are both increasingly commonplace. A major concern may turn out to be the reporting requirements imposed on taxpayers with an interest in “a foreign financial account.” And this concern will be substantially heightened if the Joint Committee's recommendations, which would essentially “delegate” the re-

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sponsibility to a tax preparer, ever become law.

While it is generally understood that U.S. persons are obligated to file income tax returns with the IRS on an annual basis, it is not as well understood that such persons may have additional reporting requirements if they have an interest in a foreign financial account. Form TD F 90-22.1, the "Report of Foreign Bank and Financial Accounts" and more commonly known as the FBAR, must be filed by U.S. persons on an annual basis if at any point during the calendar year they have an ownership interest in or signature authority over a financial account (or several such accounts) in a foreign country, with an aggregate value in excess of $10,000 (the "FBAR requirements"). Failure to file the report is punishable by both civil and criminal penalties.

Even though many professionals may be aware of the need to file the FBAR, there is much confusion surrounding the breadth of the reporting requirement. For example, multiple persons may be responsible for filing an FBAR to report the existence of the same financial account. Additionally, there are questions regarding who qualifies as a U.S. person, what constitutes signature authority over a financial account, and what is classified as a foreign account.

Notwithstanding any ambiguity regarding the FBAR requirements, the responsibility to file an FBAR currently falls on the taxpayer. If, however, Section E of the report by the Joint Committee on Taxation entitled "Additional Options to Improve Tax Compliance" (the "JCT Report") should be enacted, tax practitioners will be placed squarely on the front line. [FN1] The JCT Report proposals would put the responsibility for determining whether a taxpayer has an FBAR filing requirement on tax preparers, by extending to the FBAR the Section 6695(g) due diligence requirement, which currently imposes the responsibility on preparers to determine a taxpayer's eligibility for the earned income tax credit as well as the amount of the credit permitted. Consequently, preparers would have to become intimately familiar with the FBAR requirements. Practitioners would be liable for (1) discussing with taxpayers the FBAR filing requirement as well as the civil and criminal penalties for failure to file the FBAR, and (2) documenting taxpayers' responses to such discussion as well as retaining such documentation for the Service's possible use in an audit.

ORIGIN OF THE FBAR REQUIREMENTS

The FBAR is a by-product of the Bank Secrecy Act (BSA), which was first enacted in 1970. [FN2] Congress created the BSA because of concern that financial institutions in tax haven jurisdictions were being used by U.S. persons to hide the proceeds of their illegal activities, evade tax, and for other criminal purposes. BSA section 5314 required Treasury to create forms that financial institutions and individuals would have to file that ultimately could be used by the government to track the movement in cash in the economy and crack down on nonfilers. The BSA specifically imposed responsibility on Treasury to promulgate regulations that would promote compliance and be useful in criminal, tax, regulatory, intelligence, and counter-terrorism matters, as well as to counter money laundering. 31 C.F.R. section 103.24 contains the requirement for an FBAR to be filed:

"(a) Each person subject to the jurisdiction of the United States (except a foreign subsidiary of a U.S. 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 the Internal Revenue for each year in which such relationship exists, and shall provide such information as shall be specified in a reporting form...."

Originally, authority to investigate possible FBAR compliance issues was delegated to the Service, [FN3] and the authority for civil enforcement of FBAR violations was delegated to the Financial Crimes Enforcement Network ("FinCEN"). [FN4] FinCEN is an arm of the Treasury Department that has responsibility to oversee and implement policies to detect and prevent money laundering and terrorist financing. According to the "overview" on its website, "FinCEN is a network, a means of bringing people and information together to fight the complex problem of money laundering. Since its creation in 1990, FinCEN has worked to maximize information sharing among law enforcement agencies and its other partners in the regulatory and financial communities. Working together is critical in succeeding against today's criminals. No organization, no agency, no financial institution can do it alone. Through cooperation and

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partnerships, FinCEN's network approach encourages cost-effective and efficient measures to combat money laundering domestically and internationally.” [FN5]

The FBAR is filed with the IRS Detroit Service Center, and the information on the return is entered into an FBAR database that is administered by both the Service and FinCEN. Once entered, the information can be accessed by multiple governmental authorities for purposes of tracking the flow of money.

Early in 2003, FinCEN delegated its enforcement authority for FBARs to the Service. [FN6] The delegation was the culmination of a study imposed on Treasury by the USA PATRIOT Act to find ways to improve compliance with reporting requirements. The IRS now has the ability to investigate noncompliance with the FBAR, assess and collect civil penalties associated with such noncompliance, and use the full investigative arsenal available to it.

WHO IS SUBJECT TO THE FBAR REQUIREMENTS?

The FBAR requirements apply to any “U.S. person,” which includes all U.S. citizens and resident aliens. Nonresident aliens are not required to file an FBAR. Consequently, an individual who otherwise would qualify as a nonresident alien must be careful to avoid being classified as a resident alien under the substantial presence test of Section 7701(b)(3) and thus subjected to the FBAR requirements (and related penalties for failure to comply).

The substantial presence test provides that an individual becomes a resident if he or she is physically present in the U.S. for 183 or more days during the current tax year. [FN7] An individual not physically present in the U.S. for 183 days or more during the current tax year, still may satisfy the substantial presence test under a three-year look-back. [FN8] The rule requires the individual to be physically present in the U.S. during the current tax year for at least 31 days, and for a total of 183 days over a three-year period that includes the two preceding calendar years.

To determine if the 183-day count is satisfied, a separate multiplier is applied to each of the three years. For the current year, the multiplier is 1 and each day is counted as a full day. For the immediately preceding calendar year, the multiplier is 1/3 (e.g., 60 days in the U.S. × 1/3 = 20 days). For the next preceding calendar year, the multiplier is 1/6 (e.g., 60 days in the U.S. × 1/6 = 10 days). Thus, even if the individual was actually present in the U.S. for 183 days or more during the two preceding calendar years, the individual may not be deemed a U.S. resident alien for the current tax year.

In fact, if an individual is physically present in the U.S. for no more than 121 days every year, the individual will not meet the substantial presence test and will be classified as a nonresident alien. For example, in order to determine 2007 residency, if the individual was present in the U.S. for 121 days in each of 2005, 2006, and 2007, the formula would yield 121 days in 2007, 40.3 days in 2006 (121 days/3); and 20.16 days in 2005 (121 days/6) for a total of 181.46 days in 2007.

For purposes of the FBAR requirements, a U.S. person also includes all U.S. estates, trusts, partnerships, and corporations. Thus, if any of these domestic entities has an interest in or authority over a financial account worth more than $10,000, the entity must file an FBAR. Similarly, it is possible that the authorized representative of any of these domestic entities will have a personal filing requirement as a result of the affiliation with the entity (discussed in greater detail, below).

LLCs are not specifically classified as U.S. persons under the FBAR requirements. Nevertheless, since these entities are taxed as corporations, partnerships, or to the entity owner (i.e., a single-member LLC treated as a disregarded entity), it would appear as though the members of such entities would have a reporting requirement based on the entity's classification for income tax purposes. In the absence of specific IRS guidance, members of an LLC would be well advised to take the conservative approach and file an FBAR if the LLC otherwise meets the FBAR requirements.

U.S. jurisdictions. For purposes of proving residency in a U.S. possession, territory, or commonwealth (“U.S. jurisdictions”). Section 937 and the Regulations thereunder specify that time spent in a U.S. jurisdiction is deemed to be time spent outside of the U.S. [FN9] Additionally, time spent in a U.S. jurisdiction will not qualify as time spent in the U.S. for purposes of the substantial presence test. [FN10] By contrast, for FBAR purposes each U.S. jurisdiction is deemed to

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be part of the U.S. Consequently, contrary to what would be expected pursuant to Sections 937 and 7701, financial accounts in U.S. jurisdictions are not deemed to be foreign accounts and thus are not subject to FBAR reporting.

Notwithstanding the fact that U.S. jurisdictions are deemed to be part of the U.S. for purposes of the FBAR requirements, there is some confusion between the FBAR instructions and the IRS website. The instructions define "foreign country" as one outside the U.S., Guam. Puerto Rico, and the Virgin Islands. "Frequently Asked Questions Regarding FBARs" on the IRS website, however, also include the Northern Mariana Islands and American Samoa. [FN11] An additional difference between the instructions and the IRS website is that the FBAR directions do not limit the "Virgin Islands" to the U.S. Virgin Islands, whereas the IRS website does.

In spite of the conflict between the directions and IRS website, it would appear as though the intent is to exempt accounts in any U.S. jurisdiction from FBAR reporting. This would be consistent with Sections 937 and 7701 and the associated Regulations.

WHAT TYPES OF ACCOUNTS HAVE TO BE REPORTED?

Generally, any type of account that holds liquid assets or marketable securities will be a "financial account" for purposes of the FBAR requirements. Thus, everything from a cash account to a foreign mutual fund, such as an exchange traded fund, is classified as a financial account.

The breadth of this statement is perhaps best illustrated by a posting on the Asset Protection Blog. [FN12] The posting contained an e-mail from Treasury which stated its position on FBAR financial accounts as follows: "[T]he premium payments for insurance policies with cash surrender value or other investment features constitute deposits within the meaning of Form TD 90-22.1. Therefore, if a life insurance policy is a whole life or other policy with investment value, then it is an 'other financial account' subject to reporting." When Treasury takes the position that the payment of life insurance premiums can be classified as a deposit, and thus as a financial account for purposes of the FBAR, it should be evident to taxpayers that *any* financial activity in the foreign arena should be reviewed carefully for compliance with the FBAR filing requirement.

Only financial accounts actually located in a foreign jurisdiction are subject to FBAR reporting. [FN13] For example, an investment account with Credit Suisse's New York office would not require an FBAR but an account with one of Credit Suisse's European offices would. Similarly, a whole life insurance policy with ING would not automatically generate a reporting requirement since such a policy could be obtained from its U.S. subsidiary ReliaStar. If, however, the underlying investment account associated with the insurance is held in Europe, there would be such a filing requirement.

Taxpayers should be aware that the Regulations state that all records that are required to be reported on an FBAR must be kept for five years. [FN14] Failure to keep the records for the stated period may result in civil penalties, criminal penalties, or both.

Signature or Other Authority

If an individual can order the distribution or disbursement of funds or other property from the institution where the funds or property are maintained, by signing a document providing such direction (or in conjunction with one other person signing the document), that individual has signature authority over the financial account. Similarly, if an individual can exercise the same control verbally or via other means of communication, the individual has other authority over a financial account.

These powers should not be confused with the power of investment. Individuals who can make investment decisions but who do not have the ability or discretion to make disbursements do not have an FBAR reporting requirement. Notwithstanding the foregoing, the JCT Report would treat a U.S. person as having signature or other authority over a foreign account if the U.S. person creates a trust with a foreign protector. Specifically, the JCT Report will attribute any duties and powers held by the foreign protector to the U.S. person.

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In summary, an individual who holds a power of attorney or who is a custodian of an account for a minor would appear to have the ability to exercise sufficient powers that would cause the attorney-in-fact or custodian to have an FBAR reporting duty. Similarly, a trustee, personal representative, president of a corporation, president of a general partner or managing member of an LLC, to name but a few individuals by title, could be deemed to have signature authority or other authority over a financial account held by the entity and thus a reporting obligation.

Financial Interest

The definition of what constitutes a financial interest for purposes of the FBAR is based on who owns the interest. For example, a foreign pension account satisfying the FBAR requirements and which is owned by an employer or a foreign government would not have to be reported by a U.S. person, since the U.S. person does not have any ownership over the pension account. If, however, the employer maintains individual accounts for each employee, similar to a Section 401(k) account, the employee would have a filing requirement.

Essentially, an individual has a financial interest in every account for which the individual is the owner of record or has legal title, whether the account is for the owner's benefit or for the benefit of another. There can be many situations in which several persons have an obligation to file a report with respect to the same account. For example, if the account is owned by more than one person, such as a joint account or an account held by tenants in common, each person has a financial interest for purposes of the FBAR. Similarly, if a U.S. person who owns a foreign bank account gave a power of attorney to another U.S. person to sign over the account, both the owner of the account and the individual exercising the power of attorney would have a reporting requirement. Multiple filings also would be required from the trustees of a trust with several trustees if the trust has an interest in a foreign financial account.

Individuals serving as shareholders, partners, and trustees also may be deemed to hold a financial interest in an account if the account is owned by or the individual with legal title is any of the following:

1. A person acting as an agent, nominee, attorney, or in some other capacity on behalf of the U.S. person.
2. A corporation in which the U.S. person owns more than 50% of the total stock either directly or indirectly.
3. A partnership in which the U.S. person owns an interest in more than 50% of the profits.
4. A trust in which a U.S. person has either a present interest in more than 50% of the assets or from which the U.S. person receives more than 50% of the income.

Thus, while the domestic entity that has a financial interest that otherwise meets the FBAR requirements will have to file an FBAR, it also is possible that the shareholders, officers, or directors of foreign corporations, partners in foreign partnerships, grantors of foreign trusts, or beneficiaries of a foreign trust or estate also will have to file the FBAR.

The JCT Report would extend the definition of "financial interest" to include (1) an account held by a corporation in which a U.S. person owns, directly or indirectly, more than 50% percent of the value or voting power of the corporation, (2) a partnership in which a U.S. person owns an interest either directly or indirectly in more than 50% of the profits or capital of the partnership, and (3) an account held by a trustee for a U.S. person who had a beneficial interest either directly or indirectly in more than 50% of the trust's assets.

An officer or employee of a U.S. corporation that is listed on a trading exchange, which has in excess of 500 shareholders and $10 million in assets, does not have to file an FBAR to reflect that the individual has signature authority or other authority over the financial investments if the individual has no personal financial interest in the account and has been advised in writing by the corporation's CFO that the corporation has filed an FBAR to report the investments.

Similarly, an officer or employee of a U.S. subsidiary of a U.S. corporation that is listed on a trading exchange, which has in excess of 500 shareholders and $10 million in assets, does not have to file an FBAR to reflect that the individual has signature authority or other authority over the financial investments of the subsidiary if the individual has no personal financial interest in the account and has been advised in writing by the corporation's CFO that the subsidiary corporation has filed an FBAR to report the investments. This exemption for officers and employees of a U.S. subsidiary is not

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in the FBAR instructions. Rather, the IRS answered the question as to whether the exemption for such individuals existed on its website. The Service stated that "the question was resolved in an interpretive ruling published prior to a 1988 revision of Appendix A in 31 Code of Federal Regulations (CFR) Part 103. In October 1988, the interpretive ruling was removed from Appendix A but was not revoked." [FN15]

An officer or employee of a bank that is subject to the supervision of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, the Office of Thrift Supervision, or the Federal Deposit Insurance Corporation, does not need to file an FBAR if he or she has signature authority or other authority over the accounts so long as the individual does not have a personal financial interest in the account.

DUE DATES FOR FILING AN FBAR

If a U.S. person has a foreign account that satisfies the FBAR requirements, the FBAR is due on June 30 of the following year (with no extensions). The form is filed with the Detroit Service Center. The duty to file the FBAR is independent of the obligation to file an income tax return even though the FBAR is cross referenced on Form 1040, Schedule B, Part III.

A foreign account that satisfies the FBAR requirements must be reported even if the account does not generate taxable income. Thus, a taxpayer who fails to file an FBAR because the account generates no taxable income will be subject to penalty.

The IRS has six years within which to assess a civil penalty related to an FBAR violation. It is unclear, however, whether the statute will toll if the FBAR is not filed. [FN16]

PENALTIES FOR FAILURE TO FILE

A taxpayer who fails to file an FBAR may be subject to both civil and criminal penalties under Title 31 of the United States Code. The same violation may be punishable by both a civil and criminal penalty. [FN17]

Civil Penalties

Prior to the Americans Jobs Creation Act of 2004 (AJCA), civil penalties were imposed on willful violations of the reporting requirement. The minimum penalty was $25,000 and the maximum penalty was $100,000. After the AJCA, there is now a penalty of up to $10,000 for a non-willful failure to file the FBAR. [FN18] If, however, the amount of the transaction or the balance of the foreign account is reported on the taxpayer's Form 1040, the penalty may be eliminated as a result of the reasonable cause exception. [FN19] Nevertheless, Form 1040. Schedule B, Part III instructs a taxpayer who indicates that he or she has a financial account in a foreign country to review the FBAR. To satisfy the reporting necessitated for the reasonable cause exception, the taxpayer must be certain to include on the Form 1040 any income generated by the foreign account and to the extent possible a detailed explanation of the transaction.

For a willful violation of the FBAR reporting requirement, the penalty is now a fine equal to the greater of $100,000 or 50% of the amount of the transaction or of the balance of the account at the time of the offense. [FN20] Violations that are deemed to be willful are not subject to the reasonable cause exception. [FN21] In the event the suggestions in the JCT Report are enacted in their present form, it would appear that the availability of the reasonable cause exception would be severely curtailed absent documentation of extenuating circumstances (such as the taxpayer's tax preparer advising the taxpayer that the FBAR was not required).

The Service has created internal "Guidelines for Calculation of FBAR Civil Penalty for Willful Violations." According to commentators, [FN22] IRS personnel are to apply the Guidelines and, if certain prerequisites are satisfied, the IRS agent is to use discretion to impose a less severe penalty under the statute. The prerequisites require that:

1. The taxpayer has no prior FBAR reporting violations.

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2. None of the money passing through the foreign account was used for a criminal purpose or came from such activity.
3. The taxpayer cooperated during the examination.
4. The IRS did not impose a civil fraud penalty against the taxpayer for the year in question as a result of the taxpayer's failing to report income related to the account.

While the commentators go into significant detail to explain the manner in which the penalty is to be calculated under the Guidelines, it should be understood that these Guidelines were issued prior to the AJCA and there is no official pronouncement from the Service discussing the existence of such Guidelines, their application, or whether they remain valid under current law. We understand that, as a matter of practice, these Guidelines are being applied with respect to certain voluntary disclosures.

Criminal Penalties

While the AJCA did not change any aspect of the criminal penalties, such penalties are premised on the violation's being willful. Thus, if the failure to file the FBAR is deemed to be a criminal violation, the penalty can include a fine of up to $250,000, imprisonment for up to five years, or both. [FN23] If the failure to file is deemed to be part of a criminal activity (i.e., it occurs during the violation of another law or is part of an illegal activity involving more than $100,000 in a 12-month period), the maximum fine increases to $500,000 and the possibility of imprisonment increases to up to ten years. [FN24] There is, of course, a possibility that both the $500,000 penalty and ten-year jail term will be applicable. [FN25]

To establish willfulness, the government must prove that the taxpayer had knowledge of the reporting requirement and in spite of such knowledge chose to ignore the requirement. [FN26] Some courts, however, have held that the government may prove willfulness by demonstrating that the taxpayer consciously or recklessly disregarded the law. [FN27]

In recent guidance, the IRS Chief Counsel's Office stated that “willful violation” should be interpreted in the same way for either a civil or criminal penalty. CCA 200603026 goes on to state that “in order for there to be a voluntary intentional violation of a known legal duty, the accountholder would have to have knowledge that he had a duty to file an FBAR, since knowledge of the duty to file an FBAR would entail knowledge that it is illegal not to file the FBAR. A corollary of this principle is that there is no willfulness if the accountholder has no knowledge of the duty to file the FBAR.”

Thus, the IRS appears to interpret the willfulness requirement differently from some courts. The CCA also observes that the Service must prove willfulness by the same clear and convincing evidence required when imposing a civil fraud penalty under Section 6663.

In certain situations, a taxpayer may be able to avoid a penalty. For example, if the taxpayer can show that the violation was not willful, it may be possible to avoid a penalty if the account was properly reported on the Form 1040 and the taxpayer can show reasonable cause. [FN28] Further, the Service occasionally creates a short-term amnesty program permitting delinquent taxpayers or those in noncompliance to avoid certain penalties.

The first such program was the Offshore Voluntary Compliance Initiative (OVCI), which expired on 4/15/03 but under which FinCEN granted a complete waiver of civil penalties for those taxpayers who complied with the program's terms and conditions. [FN29] Concurrent with OVCI and continuing beyond the program was the Last Chance Compliance Initiative (LCCI) within which the Service offered certain identified taxpayers an opportunity to minimize their exposure to penalties. The LCCI, however, did not offer complete amnesty from civil penalties as did the OVCI.

CONCLUSION

While the FBAR requirements include some ambiguities and could be clearer, the major issue for taxpayers and their advisors is the general level of ignorance with respect to both the filing requirement itself and the substantial and ongoing penalties that may follow noncompliance. It is not advisable to continue violating the statute in hopes that the IRS will provide an additional amnesty program in the future.

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Practice Notes

• U.S. financial institutions with international branches could provide a great service to their U.S. clientele by advising them of the need to file an FBAR any time foreign assets are purchased. The taxpayer's financial advisor, as well as the institution, will be aware of when the taxpayer's account holds foreign investments.

• Practitioners should immediately begin preparation of an FBAR checklist in the event the JCT Report proposals are implemented.

• The FBAR was last revised in July 2000. Treasury and the IRS intend to release a revised form in the near future.

[FNa1]. *KEVIN E. PACKMAN is an associate, and ANDREW H. WEINSTEIN is a senior international tax partner, with the law firm of* ***Holland*** *& Knight LLP in Miami. They have previously written for THE JOURNAL.*

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[FN1]. The purpose of the JCT Report, which was prepared on 8/3/06 but not released for distribution by the Senate Committee on Finance until 10/19/06, was to discuss options that may help bring about a reduction in the tax gap. Section E of the Report pertains to offshore bank accounts and trusts.

[FN2]. 12 U.S.C. sections 1951-1959 and 31 U.S.C. sections 5311-5330.

[FN3]. Treasury Directive 15-41, 12/1/92.

[FN4]. 31 C.F.R. section 103.56(b).

[FN5]. www.fincen.gov.

[FN6]. IR-2003-48, 4/10/03.

[FN7]. Section 7701(b)(3)(A).

[FN8]. Reg. 301.7701(b)-1(c).

[FN9]. Reg. 1.937-1(c)(3)(iii)(A).

[FN10]. Section 7701(a)(9); Reg. 301.7701(b)-1(c)(2)(ii).

[FN11]. www.irs.gov/businesses/small/article/0,,id=148845.00.html.

[FN12]. www.apbook.com, 11/12/05.

[FN13]. A financial account located in a U.S. military banking facility in a foreign country and operated to serve the U.S. military is *not* required to be reported on an FBAR.

[FN14]. 31 C.F.R. section 103.32.

[FN15]. www.irs.gov/businesses/small/article/0,,id=139727,00.html.

[FN16]. 31 U.S.C. section 5321(b)(1).

[FN17]. 31 U.S.C. section 5321(d).

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[FN18]. 31 U.S.C. section 5321(a)(5)(B)(i), as amended by AJCA section 821.

[FN19]. 31 U.S.C. section 5321(a)(5)(B)(ii), as amended by AJCA section 821.

[FN20]. 31 U.S.C. section 5321(a)(5)(C).

[FN21]. 31 U.S.C. section 5321(a)(5)(C)(ii).

[FN22]. Toscher and Stein, "FBAR Enforcement is Comingl." www.taxlitigator.com/articles/FBar.htm.

[FN23]. 31 U.S.C. section 5322(a).

[FN24]. 31 U.S.C. section 5322(b).

[FN25]. *Id*.

[FN26]. See, e.g., U.S. v. Eisenstein, 731 F.2d 1540 (CA-11, 1984).

[FN27]. See, e.g., U.S. v. London, 66 F.3d 1227 (CA-1, 1995).

[FN28]. 31 U.S.C. section 5321(a)(5)(B)(ii), as amended by AJCA section 821.

[FN29]. Rev. Proc. 2003-11, 2003-1 CB 311. See generally Ostrander. "The Offshore Credit Card and Financial Arrangement Probe: Fraught With Danger for Taxpayers," 99 JTAX 113 (August 2003).

SHOP TALK

Update on FBAR Developments—New Enforcement Efforts Likely

This column provides an informal exchange of ideas, questions, and comments arising in everyday tax practice. Readers are invited to write to the editors: Sheldon I. Banoff, Suite 1900, 525 West Monroe Street, Chicago, Illinois 60661-3693, Sheldon.Banoff@kattenlaw.com, and Richard M. Lipton, 130 East Randolph Drive, Chicago, Illinois 60601, Richard.M.Lipton@BakerNet.com.

In "FBAR—Foreign Bank Account Reporting Obligations: A Primer for the Practitioner," 106 JTAX 44 (January 2007), Kevin E. Packman and Andrew H. Weinstein, respectively an associate and a senior international tax partner with the law firm of **Holland** & Knight LLP in Miami, discussed the origins and scope of the FBAR filing requirement, as well as the penalties for failure to comply. Messrs. Packman and Weinstein write to us as follows regarding post-publication statements made by IRS personnel or Members of Congress affecting the FBAR.

1. Nina Olson, the National Taxpayer Advocate, released her 2006 Report on 12/31/06. In the report, Olson suggested three alternatives for closing the tax gap. The second pertained to improving third-party reporting, premised on the idea that increased reporting from foreign institutions will lead to an increase in U.S. taxpayer compliance. While the FBAR itself (Form TD F 90-22.1) is not an income tax return, and does not generate income such that improved compliance would help reduce the tax gap, the penalties associated with noncompliance could generate significant revenue.

2. During a panel discussion at the Florida Bar's 25th Annual International Tax Conference held January 25th and 26th, Frank Ng, IRS Deputy Commissioner (International), Large and Midsize Business Division, said "international tax compliance is now really a major emphasis for the Service." When the conversation turned to the FBAR and IRS enforcement, K. Steven Burgess, Director of Examination for Service's Small Business/Self-Employed Division, stated that IRS does have discretion when imposing penalties for noncompliance. Penalties for noncompliance prior to the Americans

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Jobs Creation Act of 2004 include penalties of up to $100,000 per account for each year that the account was unreported. Subsequent to the AJCA, there is a penalty of up to $10,000 for a non-willful violation, and the maximum willful violation penalty is the greater of $100,000 or 50% of the balance of the account at the time of the violation. Because the IRS does have discretion when imposing penalties, the penalties may differ based on the taxpayer's particular facts and circumstances.

Rodney L. Hare, an SB/SE Territory Manager for the South Atlantic Area, indicated that if the foreign account is referred to on the taxpayer's Form 1040 but an FBAR is not filed, the IRS will follow a facts and circumstances approach to determine penalties. The Service may simply issue a warning letter, but the Form 1040 otherwise has to be complete, including interest from the foreign accounts.

Finally, Hare was asked a question dealing with the lack of extensions on FBARs. He stated that because the FBAR is a Title 31 filing requirement rather than a Title 26 requirement, the June 30 deadline for the FBAR is the same as for any other Title 31 filing. When he was asked why the FBAR was simply not changed to a Title 26 filing requirement, Hare stated that making such a change was not easy to do. Under Title 31, other government agencies like the FBI have access to the documentation, which is not the case with Title 26 filings. Additionally, the statute of limitations on the FBAR is six years, again because it is a Title 31 filing.

3. The Stop Tax Haven Abuse Act (S.681) was introduced by Senator Carl Levin (D-Mich.), the Chairman of the Permanent Subcommittee on Investigations, Senator Norm Coleman (R-Minn.), the ranking Republican on the committee and Senator Barack Obama (D-Ill.), a member of the committee, on 2/17/07. The legislation is designed to deter the use of tax havens for tax evasion. It also suggests FBAR-related changes to Title 31.

Section 101 of the bill provides a presumption that any taxpayer who has an account in one of the 34 jurisdictions deemed to be secretive has sufficient income within the account to trigger an FBAR reporting. Section 104 requires any bank or securities firm that knows from its anti-money-laundering due diligence that the beneficial owner of one of its foreign-owned financial accounts is a U.S. taxpayer, to file, in its role as withholding agent, a Form 1099 reporting account income of that beneficial owner to the IRS.

Section 205 of the bill is designed to enhance enforcement of the FBAR by (a) clarifying the authority of IRS agents investigating FBAR violations to use tax information in the investigations and (b) simplifying the calculation of FBAR penalties by tying the penalty to the highest balance in the account during the reporting period.

4. On 2/27/07, the IRS issued a Fact Sheet designed to remind U.S. taxpayers with foreign accounts that there are responsibilities associated with such ownership. While the Fact Sheet briefly explains who is required to file the FBAR and when, it also summarizes the penalties for failure to comply as well as states that there are no extensions provided.

The IRS states that “the FBAR is required because foreign financial institutions that do not conduct business in the United States may not be subject to the same reporting requirements that domestic financial institutions are subject to (such as the requirement to file a Form 1099 to report interest paid to an account holder). Although there are legitimate purposes for having a foreign account, the FBAR is a tool to help the U.S. government identify persons who may be using foreign financial accounts to circumvent U.S. law.”

Whether the Stop Tax Haven Abuse Act becomes law or not, it is clear that Congress and the IRS are focused on reducing the tax gap. While compliance with the FBAR filing requirements will not generate revenue, failure to comply most certainly will generate revenue. Between statements made by IRS personnel regarding the increase in international compliance and the February 2007 Fact Sheet, it should be clear that FBAR enforcement is on the uptick. Taxpayers and tax preparers should realize that these are not isolated attempts to increase compliance.

In our January 2007 article, we summarized the report prepared by the Joint Committee on Taxation entitled “Additional Options to Improve Tax Compliance.” The purpose of the JCT Report, which was prepared on 8/3/06 but not released for distribution by the Senate Committee on Finance until 10/19/06, was to discuss options that may help bring about a reduction in the tax gap. Section E of the JCT Report was dedicated to offshore bank accounts. The report's proposals would put the responsibility for determining whether a taxpayer has an FBAR filing requirement on tax preparers,

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by extending to the FBAR the Section 6695(g) due diligence requirement, which currently imposes the responsibility on preparers to determine a taxpayer's eligibility for the earned income tax credit as well as the amount of the credit permitted.

Shop Talk thanks Messrs. Packman and Weinstein for their input and asks our readers for their experiences with FBAR reporting.

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HOP TALK

Significant New FBAR Developments From IRS and the Tax Court

EDITED BY SHELDON I. BANOFF, J.D., AND RICHARD M. LIPTON, J.D.

This column provides an informal exchange of ideas, questions, and comments arising in everyday tax practice. Readers are invited to write to the editors: Sheldon I. Banoff, Suite 1900, 525 West Monroe Street, Chicago, Illinois 60661-3693, Sheldon.Banoff@kattenlaw.com, and Richard M. Lipton, 130 East Randolph Drive, Chicago, Illinois 60601, Richard.M.Lipton@BakerNet.com.

The requirement to file the non-tax information return known as an FBAR ("Report of Foreign Bank and Financial Accounts," TD F 90.22-1) is an obligation most taxpayers and many practitioners are unaware of. See Packman and Weinstein, "FBAR—Foreign Bank Account Reporting Obligations: A Primer for the Practitioner," 106 JTAX 44 (January 2007), and Shop Talk, "Update on FBAR Developments—New Enforcement Efforts Likely," 106 JTAX 318 (June 2007) .

The FBAR must be filed by all U.S. persons who have a financial account, signature authority, or other authority over foreign financial accounts if in the aggregate at any time during the calendar year the balances of all of the accounts are at least $10,000. Each of the respective terms is defined quite broadly and multiple persons can have a filing obligation to report the existence of the same accounts.

Kevin E. Packman and Andrew H. Weinstein, respectively a senior associate and a senior international tax partner with the law firm of **Holland** & Knight LLP in Miami, have provided us with the following broad overview of several new developments affecting taxpayers, including a revised FBAR form released on 9/30/08. In addition, a new Tax Court case considered FBAR jurisdictional issues. The steps leading up to these developments include:

- *IRS outreach*. In June 2007, the Service as part of its IRS National Phone Forum hosted three webinars dealing with the FBAR. On 11/25/07, an e-mail was issued to those who participated, which contained a series of answers approved by IRS Counsel to questions asked by those who participated. This seems to be the greatest extent of IRS guidance on the FBAR filing obligation, and yet it does not appear that the IRS has published this list of questions and answers on its website. We will make copies available; please contact us by e-mail (kevin.packman@hklaw.com).
- *Investigations*. The Service announced in IR-2008-26, 2/26/08, that it was taking enforcement action against more than 100 U.S. taxpayers "to ensure proper income reporting and tax payment in connection with accounts in Liechtenstein," joining forces with seven major treaty partners to crack down on tax evasion in connection with that principality. The news release indicated that IRS was "working together [with other member countries of the Organization for Economic Cooperation and Development's Forum on Tax Administration] following revelations that Liechtenstein accounts are being used for tax avoidance and evasion." Then on 7/1/08 the IRS filed a John Doe summons against UBS to obtain the names of up to 20,000 U.S. taxpayers who held accounts with the institution, and who failed to report the accounts. A headline in the 10/1/08 edition of the *International Herald Tribune* reported that "Switzerland said to be sharing client data in UBS tax case."
- *Notices and delegations*. In Delegation Order 4-35, 3/24/08, the IRS delegated numerous FBAR responsibilities among its divisions. On 6/17/08, the IRS issued IR-2008-79, entitled "IRS Reminds Taxpayers to Report Certain For-

eign Bank and Financial Accounts by June 30." IRS Commissioner Doug Shulman was quoted as saying "[t]here are responsibilities that go along with owning such foreign bank and financial accounts [and] [f]oreign account owners must remember that they may have to report their accounts to the government, even if the accounts do not generate any taxable income." On 6/18/08, the IRS also released a "Memorandum for BSA Compliance Examiners and Managers," which provides guidance to examiners on how to audit for FBAR compliance. (The BSA is the Bank Secrecy Act, 31 U.S.C. sections 5311-5330.)

• *Internal Revenue Manual*. Section 4.26.16 of the IRM was added as of 7/1/08, and parts of section 4.26.17 were revised on 5/5/08.

• *Audits*. When auditing taxpayers, the IRS is using at least two approaches to determine FBAR compliance with its information document requests (IDRs). The first approach is a simple innocuous request for "[c]opies of all bank statements for all foreign accounts (including but not limited to checking, savings, certificate of deposits, etc.), in which the taxpayer is a beneficiary or has control over (i.e., signature authority, as trustee, nominee, etc.) for the [specified] period...." The second approach is much more aggressive and appears similar to a subpoena with a definitional section. The FBAR related questions run several pages. Taxpayers should understand that if dealing with the IRS alone, they could inadvertently make an admission that will later be used against them in a criminal matter. They also should realize that the innocuous questions can be followed up with the more aggressive approach.

ABA Tax Section. The FBAR also was a topic of discussion at the Fall meeting of the Section of Taxation held in San Francisco. A panel of the Civil and Criminal Penalties Committee on 9/12/08 discussed the following issues:

• *UBS and LGT*. Taxpayers who have failed to file FBARs and report the income associated with their foreign accounts should not assume that just because their accounts are not held at UBS or LGT (the Liechtenstein Global Trust Group), they will be immune from IRS enforcement. IRS Deputy Chief of Criminal Investigation Victor Song stated that "just because you see a couple of banks that are making the press doesn't mean ... that it's limited to two banks." Song indicated that the IRS has trained 800 law enforcement officers around the world and the implication was that the Service will find noncompliant taxpayers. The IRS is getting good information from its treaty partners through spontaneous exchanges of information. The whistleblower law is also bringing a lot of new information to the Justice Department and IRS.

• *Enforcement*. Practitioners should expect the IRS to increase imposition of FBAR penalties because the IRS has been criticized for not previously penalizing those taxpayers who failed to comply with the law following the 2003 Offshore Voluntary Compliance Initiative. The IRS recognizes that increased use of the FBAR penalties is a useful tool to encourage compliance.

• *Focus*. Mr. Song noted that there are two new senior prosecutors, one who will deal with FBAR and other offshore banking issues, and the other who will deal with national security issues, including some immigration issues. There are currently eight international attaches overseas. Not only are their staffs being increased but they are being educated on the law so that they can enforce it. IRS is working to educate foreign prosecutors and foreign investigators on these issues because the issues are global. The Commissioner is very interested in this topic. Both civil and criminal agents are being trained to understand the available tools to uncover noncompliance and to specialize in areas of law. This includes training in treaties and MLATs (Mutual Legal Assistance Treaties).

• *Prosecutions*. Recognizing the Service's workload, and its inability to police all taxpayers, prosecutors are encouraging the IRS to look for facts with jury appeal. Offshore accounts are attractive to juries, especially when these accounts are coupled with efforts to conceal large sums of money. Because Congress has provided new enforcement tools, we should expect the IRS to publicize cases that will include FBAR violations. There is now an agent in the Detroit Service Center whose job is to review all late-filed FBARs. The relevant information can be provided to the DOJ the very next day. Even though the IRS may have included FBARs in a voluntary disclosure, the DOJ does not necessarily have to follow the IRS policy. While DOJ may file some major cases to deliver the message that hiding money offshore does not pay, prosecutors should continue to focus on the facts. By prosecuting a taxpayer who is trying to get

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it right, the DOJ may cause a disincentive for taxpayers to come into compliance. There was no answer given as to how the DOJ will tread or discretion as to what factors it will look to before deciding to prosecute. The new agent based in Detroit is certainly a cause for concern, especially with a stealth disclosure.

• *Voluntary disclosure*. There is no FBAR-related voluntary compliance initiative likely to be offered. There was a suggestion that it "would be nice if the IRS could quickly get names of taxpayers on a DOJ target list to give us a clear answer if this is a good voluntary case or not.... It would also be good if the IRS had a clear position on how much the maximum penalty will be on a voluntary FBAR disclosure." The IRS response was that they utilize a balanced approach, and review the facts of each case. An additional comment was made that there are so many penalties that there needs to be assurance of reasonable determinations. The IRS is being urged by the ABA Tax Section to use discretion, but so far the Service's position is that there has to be reasonable cause to avoid penalties. IRS says to expect stiffer penalties than before, but IRS is being careful because of limited resources and because the law is not always clear. This is definitely an evolving issue. The uncertainty is scaring off some voluntary disclosures because penalties can exceed account balances. Both the IRS and DOJ want increased taxpayer compliance, and both offer voluntary disclosure programs. Therefore, making criminal cases from those filings is not consistent with the carrot-and-stick approach. It would be better for the government agencies to focus on egregious cases, rather than on taxpayers who have proceeded through bona-fide voluntary disclosures.

The revised FBAR. On 9/30/08, and with no pronouncement, the IRS posted a revised FBAR on its website, which is to be used for all filings after 2008. While we provide a brief summary of some of the noteworthy revisions, we do encourage everyone to spend time reviewing the new FBAR and the accompanying instructions. A complete analysis of the new FBAR and its instructions are beyond the scope of this column.

(1) *Multiple parts*. Similar to Form 3520 ("Annual Return to Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts"), there are now multiple parts to the FBAR, and taxpayers only need to complete the relevant sections. Part I always will be completed, as it contains the filer's information; Part II is completed by those reporting a financial interest in a foreign account; Part III by those reporting a joint interest in a foreign account; Part IV by those filers who need to report signature authority or other authority over foreign accounts; and Part V is completed by those corporations filing a consolidated FBAR.

(2) *U.S. person*. The instructions reflect that the definition of "U.S. person," and thus who is required to file the FBAR, includes "a citizen or resident of the United States, or a person in and doing business in the United States." Reference is made to 31 CFR section 103.11(z) for a complete definition of U.S. person. As a result of the expanded definition, question 4 now requires a person in and doing business in the U.S. to report that person's foreign identification number. The instructions explain that only if the filer does not have a Social Security number should the filer report an official foreign government document number evidencing the filer's nationality or residence (i.e., foreign passport number).

(3) *Filing due date*. The instructions reiterate that the FBAR must be filed by June 30 of the year following the calendar year to be reported, and there are no extensions. Whereas the FBAR must be filed with the Detroit Service Center, filers now have the option of hand delivering the FBAR to any local IRS office. For those filers located outside of the U.S., tax attaches are located in the U.S. embassies in certain foreign countries. Finally, filers are advised that they can contact the Detroit Computing Center Hotline at 800-800-2877.

(4) *Amended/late filings*. There is now a box to be checked if the filer is submitting an amended FBAR. Whether the FBAR is filed late or is an amendment, the instructions advise the filer (and thereby practitioners) to attach a statement explaining why the FBAR is filed late, or the reason for the changes to the previously filed FBAR. If submitting an amended FBAR, the original FBAR must be attached.

(5) *Financial accounts*. The definition of financial account found in the instructions has been expanded to make clear that it also encompasses debit card or prepaid credit card accounts.

(6) *Financial interest*. The definition of financial interest also has been expanded. Under the prior definition, a U.S.

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person who created a trust, or was deemed to own a trust (for example under the grantor trust rules), could be classified as having a financial interest if the trust owned foreign accounts. Now, the U.S. person will be deemed to have a financial interest if the trust that owns foreign accounts has a "trust protector." Trust protector is defined as 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." As we mentioned in our January 2007 article, the trust protector's powers could rise to the level that the trust protector could have his or her own filing requirement under signature or other authority.

(7) *Account valuations*. Prior versions of the FBAR asked the filer to check one of four boxes reflecting the value of the foreign accounts, with each box reflecting a range of values. The new FBAR requires the filer to report the "maximum value" of the account. Foreign currencies are to be converted at the end of the year, and there are specific instructions provided for valuing assets, including how to report accounts with an unknown valuation.

(8) *Signature or other authority*. In the new Part IV, to be completed when an individual is reporting signature or other authority over foreign accounts, the filer also must report the name, address, and identifying number of the owner of the foreign account (in addition to the address of the foreign financial institution where the account is held). While much of this information was previously requested in prior drafts of the FBAR, we have heard instances in which filers would simply report that no U.S. person had a financial interest, and not report the identifying information of the account owner. The instructions make it clear that this information is now required.

Tax Court. On 10/2/08, the Tax Court released its decision in *Williams*, 131 TC No. 6, in which it stated it did not have jurisdiction to address the taxpayer's liability for FBAR penalties. The IRS had issued a notice of deficiency to the taxpayer, including penalties and additions to tax for the years 1993-2000. The taxpayer sought a deficiency redetermination for the years at issue as well as for the 2001 tax year. In addition, the taxpayer sought to have the court abate interest that may be assessed as well as the FBAR penalties.

The Tax Court began its review by noting that the FBAR filing and penalty are authorized by Title 31, not Title 26. It then found that civil penalties for violations of the FBAR filing requirements are permitted by section 5321(a) of Title 31. The court noted that section 5321(b)(1) permits Treasury to assess those penalties, and to "commence a civil action to recover" the penalties. Treasury has delegated its authority to the IRS. Because FBAR penalties are not subject to the deficiency procedures of Title 26, and the Tax Court's jurisdiction is conferred on it by Title 26, the court found it did not have jurisdiction to address the propriety of the FBAR penalty.

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Weinstein, Andrew H (MIA - X27755)

From:	*SBSE National Phone Forum [NationalPhoneForum@irs.gov]
Sent:	Sunday, November 25, 2007 7:43 PM
To:	Packman, Kevin E (MIA - X22261)
Subject:	IRS National Phone Forum - Foreign Bank and Financial Account Reporting (FBAR) Question and Answers
Follow Up Flag:	Follow up
Flag Status:	Red

FBAR Questions

SB/SE Counsel Approved 10-22-07

The following are the questions and answers from the FBAR Phone Forum. We recently received them back from Counsel. We apologize for any inconvenience this delay may have caused.

Absence of a Signature

In an absence of signature or other authority over an account of the trust is a beneficiary of a trust exempt from filing on the foreign financial account(s) of the trust?

No. A beneficiary may have an obligation to file an FBAR even though he has no authority over the foreign accounts of the trust. The beneficiary should file an FBAR if the beneficiary is a U.S. person and either has a present beneficial interest in more than 50 percent of the assets of the trust or receives more than 50 percent of the current income of the trust. See the definition for "financial interest" in the instructions to the FBAR.

Aggregate

• In the slide (page 4) stating "if the aggregate value of these accounts exceeds $10,000 at any time during the calendar year" - Does it mean the **total value of ALL the accounts** exceeds $10,000 or the **largest value of EACH account** over $10,000 during the year?

For purposes of determining whether an FBAR needs to be filed, the largest value during the year is determined separately for each account (including the accounts that did not exceed $10,000) and added together. See the instructions for Item 22, Account Valuation, for the FBAR form.

• If a U.S. citizen has two foreign bank accounts with the following max. balances:

$12,000

$1,000

Do both accounts have to be included on the FBAR form?

Yes.

• When is the aggregate value determined? For instance, if 2 foreign accounts exist and the ending monthly balances when added together do not exceed $10,000 at any time during the year, is there a filing requirement if during some month the balances in the 2 accounts exceeded $10,000 for 1 day.

The maximum value of the account when there are monthly statements is the largest amount that appears on the statement, not the ending balance. See the instructions for Item 22, Account Valuation, for the FBAR form.

• If a person holds a foreign account and the balance of the account fluctuates during the year and for argument purpose the amount goes over 10,000 and comes down by the end of the year. Would this person need to file forms subject to FBAR requirement.

Yes. The maximum value of the account is the largest amount during the year. See the instructions for Item 22, Account Valuation, for the FBAR form.

Bank Subsidiary

Employees of a Bank who have authority over foreign accounts with no personal interest in the account are exempt from filing the report. Are Employees of a "Bank Subsidiary" (that is not a bank. but is a subsidiary of a large domestic bank that is subject to bank Regulatory authority), also exempt from filing the report?

Yes, provided that the employees otherwise qualify for the exception for officers and employees of banks described in the FBAR instructions.

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Canadian Citizen — Resident of US and Form 8891

• If a Canadian citizen is a resident of the U.S. and has filed the Form 8891 each year for their various RRSPs, is an FBAR to be filed along with the 8891 each year?

Yes. Even though both the FBAR and IRS Form 8891 contain similar information about the Canadian retirement accounts, they serve different purposes. The Form 8891 contains information that is needed by IRS, including information that is not reported on an FBAR. Unlike the Form 8891, the FBAR is intended to be made available to other government agencies, including state and federal law enforcement agencies. Internal Revenue Code restrictions on disclosure of tax return information generally prevent the use of the Form 8891 for this purpose.

• If the filing of 8891 has been done the past 2-3 years, but no FBAR has been filed, how should I proceed with various clients filing needs? The FBAR filing requirement for RRSPs seems to be a duplication of the reporting process. Therefore is there any thought into allowing RRSPs to be an exception to the rule if a 8891 is properly filed?

No one is considering such an exception at this time. Even though both the FBAR and IRS Form 8891 contain similar information about the Canadian retirement accounts, they serve different purposes. The Form 8891 contains information that is needed by IRS, including information that is not reported on an FBAR. Unlike the Form 8891, the FBAR is intended to be made available to other government agencies, including state and federal law enforcement agencies. Internal Revenue Code restrictions on disclosure of tax return information generally prevent the use of the Form 8891 for this purpose.

Canadian Registered Retirement Plan

My taxpayer has had a Canadian Registered Retirement plan. He has not had any contributions to it for many years, however, he began receiving distributions from it in 2006. He filed form 8891 reporting the distribution and account balance with his 2006 individual income tax return. Is it also necessary to file TD F 90-22.1? This is his only foreign account and since the 8891 was filed, it would seem redundant. I believe he filed the TD F 90-22.1 in 2005, but may not have filed in previous years.

Yes, both forms should be filed. Even though both the FBAR and IRS Form 8891 contain similar information about the Canadian retirement accounts, they serve different purposes. The Form 8891 contains information that is needed by IRS, including information that is not reported on an FBAR. Unlike the Form 8891, the FBAR is intended to be made available to other government agencies, including state and federal law enforcement agencies. Internal Revenue Code restrictions on disclosure of tax return information generally prevent the use of the Form 8891 for this purpose.

CFC

Does a CFC have to file a TD-F 90-22.1 or only the shareholders? IF so what is the support for this position? Do attribution rules apply? If so in what way and what is the support for this position?

Presently, if the controlled foreign corporation (the CFC) was not incorporated in the United States, it does not have to file FBARs since only domestic corporations have to file FBARs. This is expected to change with the next revision to the FBAR form. In the current draft for the next revision, foreign corporations that are in, and doing business in, the United States will also have to file FBARs. A shareholder who is a United States person may have to file FBARs depending on the shareholder's ownership interest in the CFC. If a shareholder owns directly or indirectly more than 50 percent of the total value of shares of stock in the CFC, the shareholder has to file FBARs, even if the CFC does not have to file. Concerning indirect ownership interests, the attribution rules in the Internal Revenue Code are not applicable with respect to FBARs. The FBAR instructions, however, provide guidance on whether an individual has a financial interest in a foreign account held by a partnership, corporation, estate, or trust.

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Community Property State and Joint Ownership

• Does the spouse of a person with an interest in / signature authority over a Foreign Bank Account by reason of residing in a community property state have a separate (for her only) FBAR filing requirement? The spouse with the interest in / signature authority over a Foreign Bank Account does file the FBAR. The account is not listed with the foreign financial institution as jointly owned.

No. If the spouse is not a joint owner of his or her spouse's account except by virtue of the state's community property laws, and does not have signature authority or other authority comparable to signature authority over the account, there is no filing requirement.

• Say the wife has her own foreign bank account, but lives in a community property state, should the FBAR indicate the account is jointly owned by the spouse?

No. If the husband is not a joint owner of the account except by virtue of the states' community property laws, and the husband does not have signature authority or other authority comparable to signature authority over the account, the wife should not indicate on the FBAR that the account is jointly owned with the husband.

Corporation

• Can you please explain how FBAR reporting should be done where a corporation owns a foreign bank account? Can the corporation file the FBAR form as the entity having a financial interest in the account? Individual employees of the corporation would have signature authority over the account, but cannot personally benefit from the account. Would the corporation's reporting cover those individual employees?

The domestic corporation should file an FBAR to report the corporation's financial interest in the foreign bank account but the employees who are United States citizens or residents also have an obligation to file FBARs if they have signature authority or other authority that is comparable to signature authority over the bank account.

There is an exception for officers and employees of domestic corporations that are listed on a national securities exchange or that have assets exceeding $10 million and at least 500 shareholders. In order for the exception to apply, the officer or employee must have no personal interest in the account and must have been advised in writing by the chief financial officer of the corporation that the corporation has filed a current report which includes the account.

• I have a client that is an S-corporation (Company A). Company A's stock ownership is as follows: 6% John Doe (the father), 6% Jane Doe (the mother), 44% Bill Doe (John and Jane's son) and 44% Bob Doe (John and Jane's son). Company A owns 100% of the stock of Company B (which is a Qualified Subchapter S Subsidiary of Company A). Company B has a bank account in Montreal, Canada. The value of the account exceeded $10,000 for 2006.

Who is required to file a Form TD F 90-22.1 for 2006? Company A? Company B? John Doe? Jane Doe? Bill Doe? Bob Doe? All six of them?

S corporation status has no effect on the FBAR reporting requirements. Companies A and B would have to file FBARs but Company A can file a consolidated FBAR for both corporations. The shareholders do not have to file FBARs. Although any shareholder who owns directly or indirectly more than 50% of the value of the stock of either of the two corporations would have to file FBARs, the attribution rules in the Internal Revenue Code do not apply to FBARs. The FBAR instructions provide guidance on whether an individual has a financial interest in a foreign account held by a partnership, corporation, estate, or trust.

• You are an officer of a corporation that is not a large public company. The corporation files the FBAR and indicates on the FBAR that you have signature authority over a financial account. Am I correct in understanding that both the corporation and the officer should have filed FBARs? Is this situation similar to the joint account situation where only one FBAR was filed even though two were technically required? So is it safe to infer that penalties would not be assessed and that going forward separate FBARs should be filed?

Yes, both the corporation and the officer should have filed FBARs. The officer can file delinquent FBARs, attach-

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ing a statement explaining the circumstances, and file current FBARs, keeping copies for his records. No penalty will be assessed if there was reasonable cause for not filing the FBAR. Reasonable cause is determined based on the facts and circumstances of each case.

• Our parent company owns more than 50% of several US entities and we file a consolidated 1120 return. We have more than 25 foreign bank accounts in which we have financial interest. On many of these accounts we also have signature authority. What is the proper way to report this? If the accounts are included in the consolidated report as a result of the financial interest, do we also have to report them separately as a result of having signature authority?

The corporation can file a consolidated FBAR to report the accounts but officers and employees who are United States citizens or residents also have an obligation to file FBARs if they have signature authority or other authority that is comparable to signature authority over the account. There is an exception for officers and employees of domestic corporations that are listed on a national securities exchange or that have assets exceeding $10 million and at least 500 shareholders. In order for the exception to apply, the officer or employee must have no personal interest in the account and must have been advised in writing by the chief financial officer of the corporation that the corporation has filed a current report which includes the account.

• Do US shareholders that own over 50% of a corporation file a form TDF 90-22.1? Therefore the corporation, the 2 employees that can transfer the funds from the US bank account to pay the suppliers (check signers), and the two 50% shareholders need to file a form TDF 90-22.1 for the accounts? So 5 forms for the same bank accounts need to be filed.

A shareholder will only have to file FBARS as a shareholder if he or she owns directly and indirectly more than 50% percent of the total value of shares of the corporation. If a shareholder owns exactly 50% of the total value of the shares, then the shareholder does not have to file FBARs as a shareholder. The FBAR reporting requirement can result in multiple FBARs that report the same bank account.

Corporate Foreign Account

If a U.S. person has signature authority over a corporate foreign account, but doesn't own 50% of the corporation do they need to file the FBAR?

Yes, even though the corporation files an FBAR to report the foreign account, a United States person who has signature authority or other authority comparable to signature authority also has to file an FBAR to report the same account. There is an exception for officers and employees of domestic corporations that are listed on a national securities exchange or that have assets exceeding $10 million and at least 500 shareholders. In order for the exception to apply, the officer or employee must have no personal interest in the account and must have bee advised in writing by the chief financial officer of the corporation that the corporation has filed a current report which includes the account.

Issues Respecting Decedents

• If a taxpayer is deceased and the Personal Representative of the Estate discovers that an FBAR was never filed for the deceased when preparing the FBAR for the Estate, and believes that the taxpayer had foreign financial accounts that may have had an aggregate amount above $10,000, (the documentation of such accounts is not readily available) what is the P.R.'s responsibility and what steps should the personal representative take?

The personal representative should file an FBAR for the estate but will not be expected to file FBARs that the decedent should have filed.

• What steps would the personal representative take if unable to locate the documents from the foreign accounts?

The personal representative should take reasonable steps to obtain the information needed to complete the FBAR, including contacting the foreign financial institution. The personal representative can file the FBAR with the information the personal representative was able to obtain and attach an explanation as to why the FBAR is not complete,

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keeping copies for his records.

• Who is responsible for the penalties for the deceased taxpayers non-filing?

If penalties were assessed against the deceased taxpayer, the penalties are debts against the estate. No penalty will be assessed if there is reasonable cause for the nonfiling and delinquent FBARs are filed.

Domestic company making legitimate loan to foreign company/individual

What about a domestic company that makes a legitimate loan (market value rates and terms) to a foreign company or individual?

Generally, a loan by a domestic company to a foreign company or individual is not a financial account for FBAR reporting purposes. An exception would be if the foreign company or individual routinely entered into such loans, or accepted deposits, with the general public or otherwise acted as a bank or other financial institution with respect to such loans.

Due Diligence

When we, as preparers, question our clients and get a negative response to the “Foreign investment” questions on Sch B - Form 1040, how do you suggest we prove “due diligence”? Can a question be added below those to questions so that the Preparer can indicate that the client has responded negatively?

If the preparer is not reasonably expected to know that the taxpayer has a foreign financial account and the preparer asks the taxpayer if the taxpayer had a foreign financial account this should be sufficient, in most cases, to show due diligence. There are no plans to add another question to the Schedule B with respect to foreign accounts.

Expansion of the Large Corp exception to include Universities

I would like to know whether Treasury is looking at an expansion of the Large Corp exception to include Universities and their employees. The current exception requires shareholders (>500) as well as domestic corporation status in order for the employees to be exempt from filing.

Universities are becoming more and more involved on a global level. We have “European Campuses” or “Semester Abroad” programs and hundreds of students in “Exchange” programs. Many Universities have multiple foreign bank accounts and the definition of “signature authority” is often 15 to 20 people who administer the foreign programs, wire funds, set budgets, and process payments, as well as the Dean of the College offering the program, the Controller, Asst. Treasurer, Treasurer and President. Basically, anyone who can expend money from that “Fund”.

I'm sure that this is the reason that employees of Large Corps are excluded... What about large Universities??

There is no exception to the FBAR reporting requirement for officers and employees of large universities. The officers and employees of the universities who are United States citizens and residents will have to file FBARs if they have signature authority or other authority comparable to signature authority over the foreign financial accounts, even if they have no personal financial interest in the accounts.

Fax Signatures

• Does the IRS accept a fax signature on the FBAR?

No.

• Should you file the FBAR with fax signature if pressed for time, then follow up with

Amended FBAR with an original signature later and an explanation of why the signature was obtained late?

Yes.

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Filing Requirements

- Is a U.S. Citizen who is permanently living outside of the U.S. required to file the form?

Yes.

- We have a client who has a domestic corporation in which there are two foreign directors and a foreign corporation which holds a financial interest in said domestic company. The 2 foreign directors also hold interest in the same foreign corporation. There is also an officer who we believe has access to at least one of the foreign accounts, but as of yet we do not know if he holds any financial interests in them. Who is required to file the FBAR, if they meet the over 10,000 aggregate total?

If the domestic corporation has a financial interest in foreign accounts, then the domestic corporation is required to file an FBAR. If the client owns directly and indirectly more than 50% percent of the total value of shares of the corporation, then the client is required to file an FBAR. If an officer or employee is a citizen or resident of the United States and has signature authority or other authority comparable to signature authority over foreign financial accounts of the corporation, then that person is required to file FBARs.

Financial Interest

- Is ownership in a foreign country such as a trust, real estate, collectables, and inheritance considered financial interest under FBAR?

An ownership interest in real estate or collectibles is not a financial account for FBAR purposes and is not reported on an FBAR.

A trust is generally not a foreign account for FBAR purposes, it can be if, for example, it is an investment trust similar in function to a mutual fund with account owners holding an equity interest in the trust. This would not include trusts set up under a will to manage the interests of the beneficiaries in the decedent's estate. If the trust is a domestic trust, it is subject to the FBAR reporting requirements. Whether the trust is domestic or foreign, if a beneficiary is a citizen or resident of the United States and has either a present beneficial interest in more than 50 percent of the assets of the trust or receives more than 50% of the current income of the trust, then the beneficiary is also subject to the FBAR reporting requirements.

If a citizen or resident of the United States inherits an interest in a foreign financial account, then that person is subject to the FBAR reporting requirements with respect to his or her inherited interest in the foreign financial account.

- Does the exemption for officers in a large corporation extend to smaller non-publicly traded corporations? At what level of the corporation would an individual be responsible for filing FBAR forms? For example would a controller be responsible, manager or CEO? How many forms per corporation need to be filed?

The exception for officers and employees of large corporations does not apply to non-publicly traded corporations unless the corporations have over $10 million in assets and at least 500 shareholders.

Only the officers and employees who have signature authority or authority comparable to signature authority must file FBARs for the corporation's financial accounts. If their supervisors do not have this authority, they do not file FBARs.

The corporation files FBARs for its financial accounts and each officer or employee with signature authority or other authority comparable to signature authority files an FBAR for the accounts they have authority over.

Fixed deposit account

How is a ‘Fixed Deposit’ account that acquires a new account number at each renewal handled?

We will need more time to answer this question.

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Form 1099-INT

A U.S. bank account issued a U.S. Form 1099-INT. However, the banker's name and address on Form 1099-INT indicated foreign branch. Does this bank account subject to FBAR filing requirement, assuming the balance is over $10K? If so, how do I report this on Form TD F 90-22.1, line 25?

Generally, if the account is maintained with a branch of a U.S. bank that is located in a foreign country, then the bank customer should file an FBAR. For FBAR reporting purposes, Puerto Rico, the Virgin Islands, the Northern Mariana Islands, and the territories and possessions of the United States are not considered to be foreign countries. In addition, an account with a United States military banking facility that serves U.S. Government installations overseas is not reported on an FBAR even though the account may be located in a foreign country.

Foreign Entity for Depository

What is actually considered a foreign entity for depository? Military clients often answer the question that they do have an account on base overseas, however I am assuming this is just an extension of a U.S. banking system established in the U.S. Is this a correct assumption, that there would be no filing requirements even if they deposited greater than $10000 into this on base bank.

An account with a United States military banking facility that serves U.S. Government installations overseas is not reported on an FBAR even though the account may be located in a foreign country. The military clients may wish to confirm that their accounts are with a military banking facility as described in the FBAR instructions. If so, then they do not have to file FBARs for the accounts.

Foreign Life Insurance

A second question pertains to an internet posting in 2005. The posting contains an email response from Elizabeth Witzgall and states that Treasury's position is that paying the premium on a foreign life insurance policy that has a cash value component is a “deposit” within the meaning of FBAR. Thus, the cash value account of a foreign life insurance policy would essentially be a financial account. If this is indeed a valid posting on the website, why has this not been reflected on the FBAR instructions or on the FBAR FAQ IRS Website? Needless to say, the insurance lobby should understand the issue.

The definition for financial account in the FBAR instructions includes “savings, demand, checking, deposit, time deposit, or any other account maintained with a financial institution or other person engaged in the business of a financial institution. Since a cash surrender value insurance policy can be used to store cash and withdraw it at a later time, it is treated as a financial account with a financial institution for FBAR purposes. If the policy is located overseas, and the cash surrender value exceeds $10,000, the policy holder should report the policy on an FBAR. This only applies to policies located overseas, policies acquired in the United States from an insurance agent located in the United States are not policies located overseas.

Foreign Life Insurance Accounts

Are foreign life insurance products considered other financial instruments? If a US Citizen is a beneficiary of a Canadian insurance policy required to file an FBAR if the proceeds exceed $10,000? Example: Canadian insurance policy pays annual dividends of an amount under $50. Should we then be inquiring details about the insurance?

The U.S. citizen does not have to report being the beneficiary of a foreign life insurance policy. If, on the other hand, the U.S. citizen is a policy holder of a life insurance policy located in a foreign country, and the cash surrender value of the policy exceeds $10,000, the U.S. citizen is required to report the policy on an FBAR.

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Foreign Postmark

Would a foreign postmark on June 30th (or July 2 this year) count as timely filed?

Unlike with tax returns, FBARs are considered filed on the day that they are received, not the date that they are mailed.

Foreign Trust

A US person is deemed to have a financial interest in a foreign account when the person has a beneficial interest in 50% or more of the assets in a foreign trust or receives 50% or more of the current income. If the foreign trust is a wholly discretionary trust, how does one measure the percentages? Is it solely determined retrospectively based upon distributions that were actually made?

A beneficiary files an FBAR to report his interest in the foreign financial accounts that are held by the trust. It does not matter if the trust itself is foreign. If the trust is a domestic trust, it also has an obligation to file FBARs.

If the beneficiary's interest in the assets or income of a trust that holds foreign financial accounts cannot be determined, the beneficiary should file an FBAR. If you have a question as to how the terms of a particular trust agreement affect a beneficiary's obligation to file FBARs, you may request a written ruling from IRS.

Gold Bullion

Is an account that is holding ‘gold bullion’ considered a reportable account?

Yes. An account with a financial institution that is located in a foreign country is a reportable account whether the account holds cash or non-monetary assets.

Interest-bearing Securities Issued by Foreign Country

Interest-bearing securities issued by Foreign Country. Fiscal Agent and Financial agent of the securities is a US Bank. Is there a potential FBAR requirement for one who invest in these securities?

No. Investments in interest-bearing securities, such as savings bonds, that are issued by a foreign government and that are acquired through a bank located in the United States are not reported on FBARs.

IRA Account

- Assume an Individual Retirement Account with a custodian domiciled in the United States. Assume that the owner of the account is an individual who is a citizen of the United States and who is domiciled in the United States. Assume that the IRA account owns an interest in an off-shore hedge fund. Question 1: Is an FBAR report required? Question 2: Who is required to file the report? - the custodian? - the owner? - both the custodian and the owner?

  The IRA is an account located in the United States. The owner of the IRA does not have to report the interest in the foreign hedge fund that is held in the IRA located in the United States. If the custodian does not have signature authority (or other authority comparable to signature authority) over the hedge fund account, but instead, is only holding units of the hedge fund as an investment in the IRA, and does not control the hedge fund, then the custodian does not have to file an FBAR either.

- With so many clients now using International Funds (e.g. Vanguard Target Retirement Funds, or other similar funds) for IRA and/or 401k Investments, will they be required to report on an FBAR form? And to answer the question on the Schedule B - Form 1040?

  No FBAR is required for mutual funds that are located in the United States even though the funds invest in the securities of companies located in foreign countries. If, however, the mutual funds are located in a foreign country, then an FBAR is required even if the funds only invest in the securities of companies located in the United States. It

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is the location of the mutual fund, not the types of investments made by the fund that determines whether a mutual fund investor should file an FBAR. If the client's mutual fund is located in a foreign country, then the client is subject to the FBAR reporting requirement with respect to the mutual fund account and must treat the mutual fund account as a foreign financial account for purposes of answering the Schedule B question.

• Does having the ability to vote (due to an IRA or 401k holding) during an annual meeting of a company in which a client invests (less than $10K) globally cause a requirement to file a FBAR form?

No.

• If a taxpayer has an IRA type account in a foreign country, does it need to be reported on an FBAR? If that is the case, which item should be checked in box 21 of the 90-22.1?

IRA accounts located in the United States are not reported on an FBAR. IRA type accounts that are located in a foreign country are financial accounts that are reported on an FBAR.

If the IRA-type account is not a bank or securities account, then check item c., Other, on the FBAR form and write a short description, in the space provided, of the type of account that it is.

Line of Credit

Is a Line of Credit considered a personal or business loan (debt) account that's not required to be reported?

Yes, a line of credit is not reported on an FBAR.

LLC

Why would a domestic legal entity of an LLC not be included as a US person?

The definition in the FBAR instructions for “United States person” was not updated to include LLCs and other types of legal entities that may not have existed or that were not as common when the FBAR instructions were first published. The next version of the FBAR will include all legal entities in the definition of “United States person.” Because LLCs share characteristics of both corporations and partnerships, we believe that the instructions may be interpreted to include such organizations in the definition of “United States person.” For this reason, we advise that LLCs file FBARs. The next version of the FBAR form should make it clear that LLCs are subject to the FBAR reporting and recordkeeping requirements.

Matching Program

Is there a matching program between Schedule B interest and FBAR account disclosure?

The information reported on an FBAR can be used by IRS for tax compliance purposes. Beyond this, we do not feel it is appropriate to discuss here whether there is such a matching program. The purpose for this conference call is to answer questions about the FBAR filing requirements.

Mexico Real Estate

• Mexico does not allow a U.S. person to own real estate in Mexico. Therefore, when a U.S. citizen buys real estate in Mexico they buy the property through a Foreign Bank Trust. Is this the equivalent of a foreign trust and a U.S. beneficiary? Does this give rise to a 3520 or 3520-A?

If the U.S. citizen has an interest in a foreign trust, he should file a form 3520 or 3520-A. If a person has a question as to whether he should file a form 3520 or 3520A to report an interest in Foreign Bank Trust located in Mexico, he should consult a tax professional. An ownership interest in real estate is not an interest in a foreign account for FBAR reporting purposes.

• What about a foreign trust in Mexico that owns real estate for a US citizen? Does this require a form TDF

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90-22.1? US citizens cannot own certain real estate, so a trust is set up to purchase, mortgage, own the property.

No. An ownership interest in real estate is not an interest in a foreign financial account for FBAR reporting purposes.

Military

What about government and military employees stationed overseas? I assume the same rules apply if they open a bank account in the local area and have a balance greater than 10k at any point in time, correct?

Yes, generally, they would have to file FBARs if they opened a foreign bank account but there is an exception for certain banks operating on the military installation.

An account with a United States military banking facility that serves U.S. Government installations overseas is not reported on an FBAR even though the account may be located in a foreign country. The military clients may wish to confirm that their accounts are with a military banking facility as described in the FBAR instructions. If so, then they do not have to file FBARs for the accounts.

Money Laundering

Would you please discuss the how this reporting has uncovered money laundering? It doesn't seem that the individuals it is aimed to catch would actually file this form.

The reporting requirement was intended to discourage the use of foreign accounts by U.S. persons for money laundering and other illegal purposes since the civil and criminal penalties for failing to comply are substantial.

Non-Resident

• A husband, who is a U.S. citizen, is living in a foreign country and married to a foreign national of that country. She is not a U.S. citizen and has never filed a U.S. tax return either with her husband or by herself. She has no social security number or tax identification number. She has never been to the United States. She has bank accounts with funds greater than $10,000. Does she have to file the TD F 90-22.1? Their kids who also have never been to the United States and have no social security number or taxpayer identification number, but who are U.S. citizens, also have bank accounts that exceed $10,000.. Do they have to file TD F 90-22.1

• 2) A U.S. Sub Chapter S. Corporation whose ownership consists of two U.S. citizens formed an off shore Business Trust(Corp)in the British Virgin Islands. The Foreign Corporations only bank accounts are in the United States .All administrative work is performed within the United States. The British Virgin Island Corporation is owned 80% by the U.S. Sub S. Corp and 20% by individuals with no one of these individuals owning 10%. The individuals are all passive investors. Does the foreign Corporation have to file a TD F 90-22.1? What about the U.S. Domestic Sub S. Corp.

For the first scenario, the wife, who is not a U.S. citizen or resident, does not have to file FBARs but the children, who are U.S. citizens, do have to file with respect to their financial interests in foreign bank accounts.

For the second scenario, if the foreign corporation's only financial accounts are the bank accounts located in the United States, and the foreign corporation is not acting as a financial institution (such as a mutual fund company) then neither the investors nor the domestic corporation is required to file an FBAR to report a financial interest in the bank accounts.

• Definition of US person for FBAR filing: An individual who is not a US citizen satisfies the substantial presence test for being a resident alien. They however file a 1040NR as a nonresident by using a treaty tie breaker or closer connection exception. Are they subject to the FBAR filing requirements?

Although the definition for “resident alien” in section 7701(b) of the Internal Revenue Code is not applicable with

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respect to the FBAR reporting requirements, individuals can establish that they are not residents for FBAR reporting purposes if they can show that they are not "resident aliens" for income tax purposes. In this case, the taxpayer who files as a nonresident alien does not have to file an FBAR. Please note that the filing instructions will change with the next version of the FBAR to require persons in, and doing business in the United States to file FBARs.

• If someone is on a J visa, for example, so they are considered a nonresident for income tax purposes under 7701(b), even though they may be living in the US for two years, for example, are they required to file an FBAR? I know one speaker mentioned that the visa did not matter, but the visas in question (Neville's question) were H and L visas. Those individuals would be residents under 7701(b), whereas a J or F visa holder would usually be a nonresident under 7701(b).

Although the definition for "resident alien" in section 7701(b) of the Internal Revenue Code is not applicable with respect to the FBAR reporting requirements, individuals can establish that they are not residents for FBAR reporting purposes if they can show that they are not "resident aliens" for income tax purposes. In this case, the taxpayer who files as a nonresident alien does not have to file an FBAR. Please note that the filing instructions will change with the next version of the FBAR to require persons in, and doing business in the United States to file FBARs.

• A follow up question on the definition of US resident. If an individual is a resident alien under substantial presence test of IRC sec 7701(b), but under an income tax treaty residency tie-breaker provision he is a nonresident for US income tax purposes, will he be required to file an FBAR?

Although the definition for "resident alien" in section 7701(b) of the Internal Revenue Code is not applicable with respect to the FBAR reporting requirements, individuals can establish that they are not residents for FBAR reporting purposes if they can show that they are not "resident aliens" for income tax purposes. In this case, the taxpayer who files as a nonresident alien does not have to file an FBAR. Please note that the filing instructions will change with the next version of the FBAR to require persons in, and doing business in the United States to file FBARs.

Other Financial Instruments

"Other Financial Instruments" was not adequately defined in the seminar. Does that term include an investment in a foreign stock traded on a U.S. exchange or a mutual fund from a U.S. mutual fund company which is invested in foreign securities?

Although investments in brokerage accounts and mutual funds located in the United States are accounts that can hold financial instruments (such as stock certificates and bond notes), the accounts are not foreign accounts for FBAR reporting purposes. It is the location of the account, not the type of securities held in the account that determines whether an FBAR should be filed.

Ownership Attribution

Is there ownership attribution? If so, what are the ownership attribution rules and what is the support for the rules?

The attribution rules in the Internal Revenue Code are not applicable with respect to FBARs. The FBAR instructions, however, provide guidance on whether an individual has a financial interest in a foreign account held by a partnership, corporation, estate, or trust.

Partnership

When you say indirectly control more than 50% stock or interests in partnerships, does this include accounts owned by Spouse, Children, Siblings etc?

No, the attribution rules found in the Internal Revenue code are not applicable with respect to the requirement to file FBARs.

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• An individual holds a foreign financial account in his or her name and this account has less than $10,000 during the calendar year. The individual also has signature authority over a foreign account held by a partnership where the individual is a partner owning a less than 5% interest in capital and profits. The partnership will file the FBAR form for its foreign account. Is the individual also required to file an FBAR? If so, what accounts should be included on the FBAR?

The individual would file an FBAR for the partnership account because he has signature authority over the account, not because he is a partner with less than a 5% interest in the partnership. The individual would also include, in the FBAR, his personal foreign financial account. This will result in the partnership's foreign account appearing on two FBARs: the one filed by the partnership and the one filed by the individual who had signature authority over the partnership's foreign account.

• A partnership has an escrow account with a foreign bank. The escrow account has a main account and many sub-accounts because a new sub-account is established each time funds are received from a separate transaction. A partner in the partnership, owning a less than 5% interest in capital and profits, has signature authority over the foreign bank account. This signature authority gives him or her access to the main account and all of the sub-accounts without having to sign new papers each time a sub-account is formed. The partnership will file the FBAR and report the foreign account and all of the sub-accounts. Is the partner required to file the FBAR? If so, does he or she report only the main account or the main account and all of the sub-accounts?

The partner should file an FBAR to report his signature authority over the partnership's foreign financial account. This will result in the partnership's foreign account appearing on two FBARs: the one filed by the partnership and the one filed by the partner who had signature authority over the partnership's foreign account. The partner and the partnership need only report the main account. The aggregate value of the account includes the value of each subaccount.

• If a U.S. person holds partnership interests with FMV > $10,000, but the ownership is less than 50% of the profits, is an FBAR required?

No, the U.S. person does not have to report an ownership interest in the foreign financial accounts of a domestic partnership in this case. The U.S. person would only have to file an FBAR to report a financial interest in the partnership's foreign financial accounts if the U.S. person owned an interest in more than 50 percent of the partnership's profits. It is the aggregate value of the foreign financial accounts in question (the accounts held by the partnership), not the fair market value of the partner's partnership interest, that determines whether an FBAR is required.

Partnership serving as Investment Manager

We are a domestic partnership acting as an investment manager for about 12 domestic mutual funds. Our domestic partnership has employees which have signatory authority over these mutual funds. The mutual funds have financial interests in foreign bank accounts through a domestic custodian. In order for the signatories to move monies from these foreign bank accounts they must contact our domestic custodian. Then our custodian must contact a sub-custodian located in the foreign country of the foreign bank account. Should we recommend the filing of the FBAR for the signatories?

Yes, the employees of the partnership who have signature authority should file FBARs to report the foreign accounts for which they have signature authority.

Penalties and Abatement

• About the penalty - For US Persons who have foreign bank accounts, but absolutely have no knowledge about FBAR over the years, if they file TD F 90-22.1 for 2006, do they also need to file from 2001 to 2005? If so, **how to waive the penalty** and what kind of documents need to be attached?

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The U.S. persons should file any FBARs that were required during the past 6 years and attach an explanation as to why the FBARs are delinquent. They should also keep copies for their records.

No penalty will be assessed if there was reasonable cause for not filing the FBAR. Reasonable cause is determined based on the facts and circumstances of each case.

• Summary of the penalties

For violations occurring after October 22, 2004, civil penalties can be as high as the greater of $100,000 or 50% of the amount in the foreign account at the time of the violation for each willful violation. For violations occurring after October 22, 2004, civil penalties can be as high as $10,000 for each nonwillful violation that is not corrected and for which there was no reasonable cause. There are also criminal penalties for willful violations.

You can view a table of FBAR penalties by clicking on the following link: http://www.irs.gov/businesses/small/article/0,,id=159757,00.html

• What criteria does IRS use to determine whether an individual is subject to criminal prosecution for failure to file TD-F 90-22.1 for two or more consecutive years?

As with tax cases, referrals of FBAR cases for criminal investigation are based on the facts and circumstances of each case. If a revenue agent believes that a case should be referred for criminal investigation, he will first discuss this with his group manager. The criteria that IRS uses in determining whether to pursue a criminal investigation is not made available to the public. See IRM 4.25.5.4 for IRS's procedures with respect to criminal referrals of FBAR cases.

• Have penalties been assessed to taxpayers that are not involved in criminal activity (or willfillness) to date? (clerical error, not aware of filing requirement.)

Yes but a determination with respect to penalties is made taking into account the facts and circumstances of each case. No penalty will be assessed if there was reasonable cause for not filing the FBAR. Reasonable cause is determined based on the facts and circumstances of each case.

Pension Issues

Does this other financial account include foreign pensions if the person is not yet receiving it and just has this established in a foreign country either by self saving or by a company pension plan?

No, financial accounts for FBAR purposes do not include foreign pension accounts maintained by employers. A foreign retirement account maintained by the employee (such as an IRA-type account) would, however, be a foreign financial account that should be reported on an FBAR filed by the employee.

Qualifying PFIC

Does a US individual owner of a qualifying electing fund (QEF) or a Passive Foreign Investment Company (PFIC) that files an IRS form 8621 need to file TDF 90-22.1?

Yes. Even though both the FBAR and the Form 8621 may contain similar information about the shareholder's interest in a Passive Foreign Investment Company (PFIC) or a Qualified Electing Fund (QEF), they serve different purposes. The Form 8621 contains information that is needed by IRS, including information that is not reported on an FBAR. Unlike the Form 8621, the FBAR is intended to be made available to other government agencies, including state and federal law enforcement agencies. Internal Revenue Code restrictions on disclosure of tax return information prevent the use of the Form 8621 for this purpose.

The shareholder's interest in the PFIC or the QEF is an interest in an account in which the assets are held in a commingled fund and the account owner holds an equity interest in the fund. Such interests are reportable as financial accounts for FBAR purposes.

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Schedule B, F 1040

• If client has foreign bank account but does not meet filing criteria that year, should you still file the Sch B, 1040 and indicate yes they have a foreign bank account, even if they won't need to file the FBAR.

No. The instructions for Form 1040 Schedule B identify situations, such as the one described in the question, for which an FBAR would not be required. For such situations, the instructions advise taxpayers to check the “no” box on Schedule B to indicate that they do not have a foreign bank account. See the 2006 Instructions for Schedules A & B (Form 1040), page B-2.

• Can you please cite your authority for the schedule B filing requirement if interest/dividend income < $1,500 but has a foreign account?

The authority for the requirement to answer the Schedule B question about foreign accounts regardless of the amount of interest or dividend income reported on the tax return is in the regulations under section 5314 of Title 31. Section 5314 provides the authority to require that FBARs be filed and, although section 5314 is not part of the Internal Revenue Code, it provides clear authority for IRS to ask the question about foreign accounts on Schedule B. Section 103.24 of the Title 31 regulations requires United States persons to both file FBARS and to report to IRS the fact that they have a financial interest in or signature or other authority over a foreign financial account. This requirement is met by answering the Schedule B questions in accordance with the Schedule B instructions.

Statute of Limitations

Also the code section for the statute of limitations was mentioned, can you send me the code section?
The 6-year statute of limitations for assessing civil penalties for an FBAR violation is in 31 U.S.C. 5321(b)(1).

Stock

• Does holding an individual stock (such as BNSF) - which may or may not pay dividends - and which invests a portion of its funds into foreign countries require filing of a FBAR form?

Generally, no. Only shareholders who own directly or indirectly more than 50 percent of the total value of the corporation's stock need to file FBARs to report a financial interest in the foreign financial accounts held by the corporation.

• If a U.S. person owns stock in a corporation but that person holds less than 50% of the value of the stock, is an FBAR required?

No.

Report of Foreign Bank and Financial Accounts

Do You Have a Foreign Financial Account?

If you own or have authority over a foreign financial account, including a bank account, brokerage account, mutual fund, unit trust, or other types of financial accounts, then you may be required to report the account yearly to the Internal Revenue Service. Under the Bank Secrecy Act, each United States person must file a Report of Foreign Bank and Financial Accounts (FBAR), if

1. The person has a financial interest in, or signature authority (or other authority that is comparable to signature authority) over one or more accounts in a foreign country, and
2. The aggregate value of all foreign financial accounts exceeds $10,000 at any time during the calendar year.

A United States person is not prohibited from owning foreign accounts. The FBAR is required because foreign financial institutions may not be subject to the same reporting requirements as domestic financial institutions. The FBAR is a

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tool to help the United States government identify persons who may be using foreign financial accounts to circumvent United States law. Investigators use FBARs to help identify or trace funds used for illicit purposes or to identify unreported income maintained or generated abroad.

Definition of Terms

A "United States person" includes a citizen or resident of the United States, or a person in and doing business in the United States. Whether a person is considered, for FBAR purposes, to be in, and doing business in the United States is determined based on an analysis of the facts and circumstances of each case. Generally, a person is not considered to be in, and doing business in the United States unless that person is conducting business within the United States on a regular and continuous basis. Persons who are merely visiting the United States or who sporadically conduct business in the United States, are not in, and doing business in, the United States for FBAR reporting purposes.

A foreign country includes all geographical areas outside the United States, the Commonwealth of Puerto Rico, the Commonwealth of the Northern Mariana Islands, and the territories and possessions of the United States (including Guam, American Samoa, and the United States Virgin Islands).

Reporting and Filing Information

A person who holds a foreign account may have a reporting obligation even though the account produces no taxable income. Checking the appropriate block on Form 1040 Schedule B, and filing Form TD F 90-22.1, Report of Foreign Bank and Financial Accounts, satisfies the account holder's reporting obligation.

A foreign account holder must mail the Form TD F 90-22.1 on or before June 30 of the following year to:

U.S. Department of the Treasury P.O. Box 32621 Detroit, MI 48232-0621.

The FBAR is not to be filed with the filer's Federal income tax return. The granting, by IRS, of an extension to file Federal income tax returns does not extend the due date for filing an FBAR. There is no extension available for filing the FBAR.

Account holders who do not comply with the FBAR reporting requirements may be subject to civil penalties, criminal penalties, or both.

Exceptions to the Reporting Requirement

There are exceptions to the reporting requirement. These exceptions include:

1. Accounts in U.S. military banking facilities operated by a United States financial institution to serve U.S. Government installations abroad are not considered to be accounts in a foreign country for purposes of the reporting requirement.
2. An officer or employee of a bank that is subject to the supervision of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, the Office of Thrift Supervision, or the Federal Deposit Insurance Corporation, is not required to report having signature or other authority over a foreign account if the officer or employee has no personal interest in the account.
3. An officer or employee of a domestic corporation whose equity securities are listed on a national securities exchange or which has assets exceeding $10 million and 500 or more shareholders of record, is not required to report having signature or other authority over a foreign account if the person has no personal financial interest in the account, and the officer or employee has been advised in writing by the chief financial officer of the corporation that the corporation has filed a current report that includes the foreign account.

FBAR Assistance

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Help in completing Form TD F 90-22.1 (PDF) is available at (800) 800-2877, option 2. The form is available online at IRS.gov and MSB or by telephone at (800) 829-3676. Questions regarding the FBAR can be sent to FBARquestions @irs.gov.

References/Related Topics

- Workbook on the Report of Foreign Bank and Financial Accounts (FBAR)
- FAQs regarding Report of Foreign Bank and Financial Accounts (FBAR)
- Bank Secrecy Act
- Small Business Video and Audio Presentations

Rate the Small Business and Self-Employed Web Site

Page Last Reviewed or Updated: June 30, 2009

FAQs Regarding Report of Foreign Bank and Financial Accounts (FBAR) - Financial Accounts

1. What is a financial account?
2. What's meant by the term “commingled funds”?
3. What does “maximum value of account” mean (for Box 15 on the FBAR)?
4. How do you determine the “highest value” in the account during the previous calendar year?
5. Is an FBAR required if the account generates neither interest nor dividend income?
6. Is an FBAR required for accounts maintained with financial institutions located in a foreign country if the accounts hold noncash assets, such as gold?
7. Does the term “other authority over a financial account” mean that a person, who has the power to direct how an account is invested, but who cannot make disbursements to the accounts, has to file an FBAR?
8. A N.Y. corporation owns a foreign company that has foreign accounts. The corporation will file an FBAR for the foreign company's accounts. Do the primary owners of the U.S. Company also have to file?
9. A company has over 25 foreign accounts. What should they enter in Part II of the FBAR?
10. If a United States person holds a partnership interest in a hedge fund that is located in the United States but that owns foreign financial accounts, must the United States person report his interest in a hedge fund on an FBAR, assuming the United States person does not hold more than a 50% partnership interest in the hedge fund?
11. What are the exceptions to the FBAR filing requirement?

Q. What is a financial account?

A. A “financial account” includes any bank, securities, securities derivatives or other financial instruments accounts. The term includes any savings, demand, checking, deposit, or any other account maintained with a financial institution or other person engaged in the business of a financial institution. Individual bonds, notes, or stock certificates held by the filer are not a financial account nor is an unsecured loan to a foreign trade or business that is not a financial institution.

Q. What's meant by the term “commingled funds”?

A. The reference to “commingled fund” appears in the definition, in the instructions for the FBAR, for the term “financial account.” The instructions state that the term “financial account” generally encompasses accounts in which the assets are held in a commingled fund and the account owner holds an equity interest in the fund. An example of such a commingled fund account would be a mutual fund account.

Q. What does “maximum value of account” mean (for Box 15 on the FBAR)?

A. The maximum value of account is the largest amount of currency and non-monetary assets that appear on any quarterly or more frequent account statements issued for the applicable year. If periodic account statements are not issued, the maximum account value is the largest amount of currency or non-monetary assets in the account at any time during the year. Convert foreign currency by using the official exchange rate at the end of the year. The value of stock,

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other securities or other non-monetary assets in an account reported on TD F 90-22.1 (PDF) is the fair market value at the end of the calendar year. If the asset is withdrawn from the account, the value is the fair market value at the time of the withdrawal.

Q. How do you determine the "highest value" in the account during the previous calendar year?

A. The FBAR instructions state that the maximum value of an account is the largest amount (not the average amount) that appears on periodic account statements that are issued at least quarterly. If the financial institution does not issue periodic account statements, then the maximum value is the largest amount of cash and non-monetary assets that were in the account at any time during the year.

Q. Is an FBAR required if the account generates neither interest nor dividend income?

A. Yes, an FBAR must be filed whether or not the foreign account generates any income.

Q. Is an FBAR required for accounts maintained with financial institutions located in a foreign country if the accounts hold noncash assets, such as gold?

A. Yes. An account with a financial institution that is located in a foreign country is a financial account for FBAR purposes whether the account holds cash or non-monetary assets.

Q. Does the term "other authority over a financial account" mean that a person, who has the power to direct how an account is invested, but who cannot make disbursements to the accounts, has to file an FBAR?

A. No, an FBAR is not required because the person has no power of disposition of money or other property in the account.

Q. Must a U.S. person file an FBAR on a Eurodollar account in the Cayman Islands?

A. Yes, the Cayman islands account is a foreign account.

Q. A N.Y. corporation owns a foreign company that has foreign accounts. The corporation will file an FBAR for the foreign company's accounts. Do the primary owners of the U.S. Company also have to file?

A. Yes, if any owner directly or indirectly owns more than 50 percent of the total value of the shares of stock, that owner will have to file an FBAR.

Q. A company has over 25 foreign accounts. What should they enter in Part II of the FBAR?

A. If the filer holds a financial interest in more than 25 accounts, check the yes box in item 14 and indicate the number of accounts in the space provided. Do not complete any further items in Part II or Part III of the report. Sign the form in item 44/45 and enter the date signed in item 46. Any person who lists more than 25 accounts in item 14 must provide all the information called for in Part II and Part III when requested by the Department of the Treasury.

Q. If a United States person holds a partnership interest in a hedge fund that is located in the United States but that owns foreign financial accounts, must the United States person report his interest in a hedge fund on an FBAR, assuming the United States person does not hold more than a 50% partnership interest in the hedge fund?

A. Generally, no. If the hedge fund is located in the United States, a financial interest in the hedge fund is not an interest in a foreign financial account for FBAR reporting purposes, even though the hedge fund may have foreign operations. If the domestic partnership has a financial interest in a foreign financial account, then it may have to file an FBAR. If a United States person who is an officer, employee, or partner of the partnership has a financial interest in, or signature or other authority over a foreign financial account, then that person may also have to file an FBAR. If a partner owns an interest in more than 50 percent of the profits of the partnership (distributive share of income, taking into account any special allocation agreement) or more than 50 percent of the capital of the partnership, then that partner has a financial interest, for FBAR reporting purposes, in the foreign financial accounts of the partnership and may have to file an FBAR.

Q. What are the exceptions to the FBAR filing requirement?

A.Accounts in U.S. military banking facilities, operated by a United States financial institution to serve U.S. Government installations abroad, are not considered as accounts in a foreign country. For this reason, these accounts do not have to be reported on an FBAR.

An officer or employee of a bank which is subject to the Supervision of the Comptroller of the Currency, the Board of

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Governors of the Federal Reserve System, the Office of Thrift Supervision, or the Federal Deposit Insurance Corporation need not report that he has signature or other authority over a foreign bank, securities or other financial account maintained by the bank, if the officer or employee has NO personal financial interest in the account.

An officer or employee of a domestic corporation whose equity securities are listed on a national securities exchange or which has assets exceeding $10 million and 500 or more shareholders of record, need not file a report concerning the other signature authority over a foreign financial account of the corporation, if he has NO personal financial interest in the account and he has been advised, in writing, by the chief financial officer of the corporation that the corporation has filed a current report, which includes that account.

References/Related Topics

- FAQs Regarding Report of Foreign Bank and Financial Accounts (FBAR) - Filing Requirements
- FAQs Regarding Report of Foreign Bank and Financial Accounts (FBAR) - United States Person
- Report of Foreign Bank and Financial Accounts

Page Last Reviewed or Updated: June 29, 2009

FAQs Regarding Report of Foreign Bank and Financial Accounts (FBAR) - United States Person

1. What is a United States person?
2. Who is considered to be doing business in the United States for FBAR reporting purposes?
3. Would a foreign athlete or entertainer that occasionally visits the U.S. in order to compete or perform in an event, be considered a United States person for FBAR purposes?
4. A person is a non-resident alien and only visits the United States to manage his personal interests, such as rental property. Does that person have to file an FBAR?
5. A non resident alien who doesn't meet the 183 day test is a partner in a US partnership where the US partnership deals with rentals; must he file an FBAR?
6. An American citizen, X, gives a person who is a citizen or resident of the U.S. power of attorney to X's Canadian bank accounts. X files an FBAR form annually. Does the power of attorney also need to file an FBAR?
7. A fiduciary who is a U.S. person has control as a trustee for an IRA with a foreign account. Should an FBAR be filed?
8. Is a single member LLC, which is a disregarded entity for US tax purposes, a United States person for FBAR purposes?

Q. What is a United States person?

A "United States person" includes a citizen or resident of the United States, or a person in and doing business in the United States. The term "person" includes individuals and all forms of business entities, trusts, and estates.

Q. Who is considered to be doing business in the United States for FBAR reporting purposes?

A. Whether a person is considered, for FBAR purposes, to be in, and doing business in the United States is determined based on an analysis of the facts and circumstances of each case. Generally, a person is not considered to be in, and doing business in the United States unless that person is conducting business within the United States on a regular and continuous basis. Persons who are merely visiting the United States or who sporadically conduct business in the United States, are not in, and doing business in, the United States for FBAR reporting purposes. For example, a person who is not a citizen or resident of the United States and who is engaged in a business but who only occasionally visits the United States to meet customers or business associates would not be in, and doing business in the United States for FBAR reporting purposes.

Q. Would a foreign athlete or entertainer that occasionally visits the U.S. in order to compete or perform in an event, be considered a United States person for FBAR purposes?

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A. Artists, athletes, and entertainers who are not citizens or residents of the United States and who only occasionally come to the United States to participate in exhibits, sporting events, or performances, do not have to file FBARs.

Q. A person is a non-resident alien and only visits the United States to manage his personal interests, such as rental property. Does that person have to file an FBAR?

A. A person who is not a United States citizen or resident and who visits the United States to manage his personal investments, such as rental property, and conducts no other business, is not considered to be in, and doing business in, the United States for FBAR reporting purposes and does not have to file FBARs.

Q. A non resident alien who doesn't meet the 183 day test is a partner in a US partnership where the US partnership deals with rentals; must he file an FBAR?

A. With the October 2008 revision to the FBAR form and instructions, FBARs are now required by nonresidents who are in, and doing business in, the United States. Whether a person is a nonresident alien for tax purposes has no bearing on the person's FBAR reporting obligation. The domestic partnership may have to file FBARs if it has a financial interest in, or signature authority (or other authority that is comparable to signature authority), over a financial account that is located in a foreign country. Whether a person is considered to be in, and doing business in, the United States is determined based on an analysis of the facts and circumstances of each case. Generally, a nonresident is not considered to be in, and doing business in the United States for FBAR reporting purposes if he only holds a partnership interest in a domestic partnership.

Q. An American citizen, X, gives a person who is a citizen or resident of the U.S. power of attorney to X's Canadian bank accounts. X files an FBAR form annually. Does the power of attorney also need to file an FBAR?

A. Yes, because the power of attorney has signature or other authority over the accounts and because he is a U.S. person.

Q. A fiduciary who is a U.S. person has control as a trustee for an IRA with a foreign account. Should an FBAR be filed?

A. Yes, because the fiduciary is a U.S. person.

Q. Is a single member LLC, which is a disregarded entity for US tax purposes, a United States person for FBAR purposes?

A. Yes, the tax rules concerning disregarded entities do not apply with respect to the FBAR reporting requirement. FBARs are required under Title 31, not under any provision of the Internal Revenue Code.

References/Related Topics

- FAQs Regarding Report of Foreign Bank and Financial Accounts (FBAR) - Filing Requirements
- FAQs Regarding Report of Foreign Bank and Financial Accounts (FBAR) - Financial Accounts
- Report of Foreign Bank and Financial Accounts

Page Last Reviewed or Updated: June 29, 2009

Holland+Knight

FBAR — What You Should Have Learned, and Why You Need to Care

Recent Headlines

- June 10 — An aide to the Homeland Security and Governmental Affairs Permanent Subcommittee on Investigations told BNA that Senate investigators have issued subpoenas in connection with an investigation into alleged tax evasion by U.S. citizens with accounts at Liechtenstein banks.
- May 21 WSJ — “Combating offshore tax avoidance and evasion are high priorities for the IRS,” says IRS Commissioner Doug Shulman. “Recent events show there is no safe hiding place for the proceeds of tax avoidance and evasion. Anyone with hidden income and gains would be well-advised to make a prompt and complete disclosure to the IRS.”

• February 21 — Chairman Carl Levin of the committee stated that they would investigate, and knew that more than 100 U.S. taxpayers had accounts in Liechtenstein banks.

• March 31 - The Justice Department agreed that billionaire California real estate developer Igor M. Olenicoff should not serve jail time for failing to disclose tens of millions of dollars in overseas accounts on his 2002 tax returns, according to a government sentencing position. Olenicoff, who was No. 215 on Forbes Magazine's list of the 400 richest Americans for 2006, pleaded guilty in December 2007 to one count of filing a false 2002 tax return.

• May 13 — Bradley Birkenfeld, former UBS private banker, and Liechtenstein businessman Mario Staggl indicted for assisting Igor Olenicoff in avoiding payment in over $200 million hidden off shore.

• May 29 — Birkenfeld agrees to plead guilty.

• June 19 — hearing for Birkenfeld to change plea.

Overview

- Report of Foreign Bank and Financial Account
  - Mandated by Bank Secrecy Act (31 USC 5314)
  - Treasury Department Form (TD F 90-22.1)
  - June 30 (Detroit Service Center)
- Filing Requirements
  - US Person with a
    - Financial Interest (or)
    - Signature Authority (or)
    - Other Authority
  - Foreign Financial Account
  - $10,000 (in aggregate)

Who is a US Person?

- Individual (i.e., citizen and resident aliens)
- Domestic Trusts & Estates
  - PR/executor files on behalf of estate. If non compliance by decedent, no liability for PR/executor.
  - If unable to obtain complete records, file with what you have, and note the steps taken to gather information.
- Domestic Corporations
- Domestic Partnerships

Resident Aliens may have a filing requirement

Substantial Presence Test

- 2008 — count whole days (i.e., 90 days = 90 days)
- 2007 — count 1/3 days (i.e., 90 days = 30 days)
- 2006 — count 1/6 days (i.e., 60 days = 10 days)
  - Total for 2008 is 130 days. Because less than 183, not a resident alien and no filing requirement

Who is Not A US Person?

- Non Resident Alien (NRA)
  - The filing obligation is tied to being a US income tax resident.

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— Pay attention to Visa (J or F are not residents).
— Check treaty tie breaker provisions
• Limited Liability Company (LLC)
— LLC is taxed as partnership or corporation. Thus, likely filing requirement at entity level.
— All US members may have their own filing obligation.

What is a Financial Interest?

• Owner of Record/Title Holder
— US beneficial owner of a bearer share entity or IBC.
— US Grantor of foreign trust with US Beneficiaries has filing requirement even if not a beneficiary (i.e. IRC 679). Grantor is the owner.
— Notwithstanding, no need to have a personal beneficial interest
• Constructive Ownership:
— Hold title as an Agent, Custodian, Nominee, Attorney in Fact
— Owns more than 50% of the shares of a Foreign corporation
— Owns more than 50% of the profits of a Foreign partnership
— Has a beneficial interest in more than 50% of the assets or income in a Foreign trust.

Not all Financial Interests Need to be Reported

• Foreign: anywhere outside of the US, its possessions and territory
— Royal Bank of Canada in New York — no requirement
— Bank of America in Toronto — requirement
— US mutual fund with foreign investments — no requirement
— Foreign mutual fund with all US investments - requirement
• Financial Account: any "savings, demand, checking, deposit, time deposit, or any other account maintained with a financial institution..."
— IRA vs. Pension/401K account — if individually controlled — requirement
— IRS says the cash value of a foreign life insurance policy classifies as an account
— A foreign line of credit / Gold bullion held in an account

Exceptions to Filing Requirement

• NRAS
• If foreign account is in a US military facility or operated by US institution for the military.
• Officers/employees of public US corporations (more than $10 M and at least 500 SHs) if no personal financial interest.
• Officers/employees of federally-regulated bank if no personal financial interest.

What is Signature Authority?

• US Person can control the disposition of funds by signing a paper, even if more than one person's signature is required
Examples
• US hedge fund or investment manager. While investment decisions do not require a filing, moving money in and out of accounts, may.

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• US trustee of foreign trust.
• Officer of a US corporation with less than $10M or 500 SHs
• University employees — semester abroad accounts.

What is Other Authority?

US Person can control the disposition of funds by verbal means (any means other than signing a paper)
— Email?
— Telephone call?
— Fax?
• Example — US Protector of Foreign Trust with veto power. This may qualify as 'other authority'

How are accounts valued?

$10,000 is met if
— At any time of the year
— **aggregate value of all** foreign accounts
— in excess of $10,000
— Regardless of whether accounts generated income or dividends
— If non liquid asset, 12/31 value.
— If asset sold during year, value at date of sale.
— All values must be converted for US purposes

Miscellaneous Filing Issues

• Joint Account — if H/W on all accounts, only one return required.
— Not in instructions, but accepted by IRS.
• US corporation — may file a consolidated return if more than 25 accounts.
• Records — required by regulations to be held for 5 years
• Deadline — Must be received by June 30, no extensions
• Form 1040, Schedule B, Part III (check the box)
• Form 1041, Question 3, Other Information (if Trust/Estate)
• Form 3520 references FBAR filing obligation.
• No CFC attribution rules

Enforcement — Civil Penalties

• Non-Willful: penalty of up to $10,000
• Willful: maximum penalty is the greater of $100,000 or 50% of the balance of the account at the time of the violation.
— IRS has discretion when imposing penalties. Thus, penalties may differ based on the taxpayer's particular facts and circumstances.
— If check the box on Form 1040, incorporate foreign income on Form 1040 and otherwise forget to file FBAR, facts and circumstances (warning, reasonable cause)
• Because FBAR is Title 31, IRC cannot use a lien or levy to collect on a penalty. They are limited to Title 31 collection methods. [civil suit to collect monetary fine - 31 USC §5321(b)(2)]

Enforcement — Criminal Penalties

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Requires Willfulness.

- Up to $250,000 fine, imprisonment for up to 5 years, or both.
- Up to $500,000 fine, imprisonment for up to 10 years, or both.
  — Failure to file must have been part of a criminal activity (i.e., it occurs during the violation of another law or is part of an illegal activity involving more than $100,000 in a 12-month period)

IRS Enforcement

- Prior to 2003, FINCEN in charge of enforcement. Subsequent to 4/10/03, IRS in charge.
- 2007 — approx. 322,000 FBARs filed
- 2006 — 287,358 FBARs filed
- 2004 — 219,105 FBARs filed
- 2003 — 204,689 FBARs files
- 2001 — 177,151 FBARs filed
- 2000 — 174,528 FBARs filed
- 1991 — 116,600 FBARs filed
- Treasury estimates at least 1 million people have an FBAR obligation

Enforcement — Statute of Limitations

Civil — 6 years to assess penalty; 2 years following assessment to collect
— 31 USC 5321(b)(1) and (b)(2)

- Criminal - 5 years to assess penalty.
  — 18 USC 3282(a)
- Fraud — SOL remains open on the underlying tax.
  — Saying no on Form 1040 FBAR question can be evidence of tax evasion.

Enforcement — Judicial

- FBARs — constitutional (US Supreme Court)
  — California Bankers Assn. v Schultz, 416 US 21 (1974)
- Failure to check the box — an affirmative act in tax evasion, SOL remains open, continuing violation.
  — US Dept of Justice Criminal Tax Manual — saying no on the Form 1040 can be the basis for a tax evasion prosecution. 12.08(6)(g)
  — Concealing the existence of a foreign account is evidence of fraud.
  — US v Olenicoff, (C.D. California, 3/31/08). Said no on Schedule B for 1998 - 2004 tax returns reflecting no foreign accounts, despite transferring well over $100 million into such accounts during those years. Avoided jail, but paid $52 million to resolve civil tax liabilities.

Non Compliance — What to Do?

- 6694 Issue?
- Nothing — conspiracy?
- File delinquent returns
- 5th Amendment — testimonial in nature
- Voluntary Disclosure

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Miscellaneous — Use of FBARs

• FBAR is not a tax filing.
— IRC 6103 confidentiality and disclosure not applicable
— Any governmental agency may access (IRS, Customs, DEA, FBI, etc)
— May also be provided to appropriate state, local, and foreign law enforcement and regulatory personnel in the performance of their official duties.

FBAR Assistance

• FBAR Frequently Asked Questions www.irs.gov/businesses/small/article/0,, id=148845,00.html
• IRS FBAR HOTLINE -- 800-800-2877, option 2.
• IRS FBAR EMAIL -- FBARquestions@irs.gov

From: Vischer Bernard [mailto:Bernard.Vischer@swlegal.ch]
Sent: Tuesday, April 28, 2009 12:25 AM
To: Packman, Kevin E (MIA - X22261)
Subject: RE: Thank You

Dear Kevin,

1) a criminal offence is a misdemeanour if the maximun sentence is of 3 years imprisonment; if the offence can be sanctioned with imprisonment for more than 3 years it is a crime. This distinction is relevant for instance in connection with money laundering, as only crimes are regarded as predicate offenses of money laundering. However, this distinction does not apply to tax evasion/fraud. Tax evasion is not a criminal offence at all: it is rather a breach of an administrative provision which can only be sanctioned with a financial penalty.

2) As regards the negotiations between Switzerland and the US in respect of a revision of the treaty. I do not think I can tell you more than you already know. The negotiation teams will meet tomorrow in Bern to start negotiations and we will therefore perhaps hear more about it later this week.

As you probably know, this negotiations were called by the US Treasury after the Swiss Government announced on 13 March 2009, that it withdraws its qualification against the OECD's recommendation in article 26 of its Model Double Taxation Agreement in respect of tax evasion and therefore is prepared to renegotiate the existing double taxation treaties to include also exchange of information with the requesting states in case of alleged tax evasion (and not only in cases of tax fraud).

In its announcement, the Swiss Government stated however that it will endeavour to have the following safeguards included in the double taxation treaties:

- administrative assistance on a case by case basis only (no fishing expeditions);
- reasonable transitory provisions;
- administrative assistance limited to the type of taxes covered by the double taxation treaty;
- applicability of OECD's subsidiary principle;
- provision against discriminatory practices.

The statements attributed to Mr Merz in the WSJ and the NYT must therefore probably be understood as a an endeavour to obtain reasonable transitory provisions, not only for UBS' clients, but for all US clients of Swiss banks.

Good luck for your conference.

Best regards.

Bernard

From: kevin.packman@hklaw.com [mailto:kevin.packman@hklaw.com]
Sent: mardi, 28. avril 2009 01:36
To: Vischer Bernard

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Subject: RE: Thank You

Bernard,

1) If I recall, tax evasion is a misdemeanor, and tax fraud is a crime in Switzerland. Can you define what classifies as each in Switzerland?

2) Is there anything new you can share with me with regard to the tax treaty? Today's Wall Street Journal reports that if the US drops the UBS prosecution, then the Swiss government will agree to the provisions in the new treaty.

Thank you so much for your assistance.

Kevin E. Packman | Holland & Knight

Partner, Private Wealth Services

701 Brickell Avenue, Suite 3000 | Miami FL 33131

Phone 305.349.2261 | Fax 305.679-6416

kevin.packman@hklaw.com | www.hklaw.com

Add to address book | View professional biography

From: Vischer Bernard [mailto:Bernard.Vischer@swlegal.ch]

Sent: Tuesday, March 10, 2009 11:42 AM

To: Duncan E. Osborne; Weinstein, Andrew H (MIA - X27755); Vischer Bernard

Cc: Packman, Kevin E (MIA - X22261)

Subject: RE: Thank You

Dear Andrew, dear Duncan,

Thank you very much for your kind words. I truly enjoyed meeting you and getting a better feeling of the US perspective of the matter through discussions with you.

You may be interested to hear that, while I was with you, the Swiss Federal Administrative Tribunal handed down its decision rejecting the clients' appeal against the exchange of information on their accounts with UBS, confirming thus that the conditions for assistance to the IRS under the Swiss-US tax treaty were fulfilled in respect of the information obtained by the IRS under the deferred prosecution agreement.

Best regards.

Bernard

From: Markus Zwicky [mailto:m.zwicky@zwlawyers.com]

Sent: Tuesday, April 28, 2009 10:48 AM

To: Packman, Kevin E (MIA - X22261)

Subject: Swiss Tax Situation with Banking Secrecy and Assistance in Tax Fraud or Tax Evasion

Dear Kevin

Enclosed two documents: A summary of the issue and my small easy-reading overview over the matter prepared for Washington and on the CD, in which you will find a summary of some prevailing documents between the USA and Switzerland in the very last paragraph. Please write or call if you'd like anything more or other.

Best regards

MZ

Tax evasion vs. tax fraud according to Swiss Law

Sources of law:

Law about the direct federal tax: DBG: SR 642.11, weblink: http:// www.admin.ch/ch/d/sr/6/642.11.de.pdf (german), http:// www.admin.ch/ch/f/rs/6/642.11.fr.pdf (french);

Law about fiscal harmonization: StHG: SR 642.14, weblink: http:// www.admin.ch/ch/d/sr/6/642.14.de.pdf (german), http:// www.admin.ch/ch/f/rs/6/642.14.fr.pdf (french);

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Swiss Penal Code: StGB: SR 311.0, weblink: http:// www.admin.ch/ch/d/sr/3/311.0.de.pdf (german), http:// www.admin.ch/ch/f/rs/3/311.0.fr.pdf (french).

Definitions:

Tax evasion (Steuerhinterziehung): DBG 175; StHG 56.

Tax fraud (Steuerbetrug): DBG 186; StHG 59.

Swiss penal code:

To define whether there is a misdemeanor, a crime or a capital crime, the Swiss Penal Code (StGB) uses as parameter the threat of punishment:

	StGB	**Punishment**
Misdemeanor	103	Fine up to CHF 10'000.00; more according to leges speciales
Crime	10 II	Fiscal punishment or imprisonment up to 3 yrs.
Captial Crime	10 III	Imprisonment, minimum 3 yrs.

According to this factsheet, tax evasion is a misdemeanour and tax fraud a crime, the breach of the banking secrecy is a crime.

The Role of the Banking Secrecy in Switzerland

Dr. Markus Zwicky

Zwicky Windlin & Partner, Zug, Switzerland www.zwlawyers.com

Background of Banking Secrecy

Banking secrecy has an old and widespread tradition in Switzerland and goes back to the origins of banking on what is today the territory of the Swiss Confederation.

The most notable banking tradition was developed in the city of Geneva before its joining the Swiss Confederation in 1815. Previously, the tradition of banking already was well established for the French kings and nobility, leading to the necessity of confidentiality between the Calvinist borrowers and the catholic nobility.

On the central Swiss and Germanic city side confidentiality was a vital necessity due to the tradition within small autocratic cities and rural cantons to avoid any disclosure or displaying of personal wealth, altogether in a more regional rural and merchant's context.

After the French revolution and again after the revolution of 1848 and 1918 Switzerland was a country chosen by the various waves of wealthy refugees. It was self-understood that depositing assets in Swiss banks was a private matter to be disclosed, if ever, only by the depositing party.

Before 1934 there was no specific banking law regulation providing confidentiality or secrecy. However, cantonal laws applied which provided for the basis of secrecy obligations in a professional context for everyone. The basis for such confidentiality and secrecy was established in the light of personality rights, corporate and employment law obligations, and the constitutional right to property. In 1907 Swiss Civil law was unified, establishing harmonized laws for civil law rights pertaining to the personality (Art. 28 Swiss Civil Code, hereinafter CC), and with the Swiss Code of Obligations in 1911 also in light of corporate obligations (i.e in employment law or obligations of staff members, Swiss Code of Obligation, hereinafter CO).

The reasons leading to the stipulation of an explicit banking secrecy are to be seen in the context of the political situ-

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ation of the years between 1930 and 1939.

Pressure had been built up by the socialist French government and by fascist German government, both governments eager to avoid the migration of wealth and both also ready to penalize any individual who owned money outside their respective jurisdiction. Other countries were building up similar strong regulations in a world recovering from the first great economic depression. Switzerland chose to resist such foreign pressure by stipulating a straightforward legal regime of banking secrecy.

As a consequence, the Federal Banking Act of 1934 was enacted, in which a strict banking secrecy was established.

Content of the Banking Secrecy

The Swiss banking secrecy is a contractual obligation of the Bank against the customer. The bank commits to keep confidential the identity and all details of the customer towards third parties. Therefore, the primary consequence of a breach of banking secrecy is a civil law claim of the bank's client against the banking institution.

However, in addition to the contractual stipulations between banks and customers, the Swiss banking secrecy has also been subject to public fines. It is established in Art. 47 of the Federal Banking Act of 1934, which reads as follows:

1. Any person who, in his or her capacity as a member of a juridical enactment, employee, power-of-attorney holder, liquidator or commissioner of a bank, mandate holder for the Banking Commission, or a member of a juridical body or an employee of an authorized audit company, has revealed a secret that was brought into his/her knowledge in the course of such practice or employment, any person who has made another to violate professional secrecy, shall be punished by prison for a maximum period of six months or by a fine not exceeding 50'000.00 Swiss Francs.
2. Should the offending party have acted in negligence, the punishment will consist of a fine not exceeding CHF 30'000.00 Swiss Francs.
3. A breach of secrecy shall be punished even when the practice of employment has terminated or the holder of the secret should no longer be working for a banking institution.
4. Any further Federal and Cantonal legislation ruling on the obligation to inform authorities and testify in court shall be reserved.

The banking secrecy therefore is a private right of the individual customer towards the bank irrespective of the status or background of the money carried to the bank. The secrecy is unconditional. However, there are various exceptions that lead to the consequence that such banking secrecy is revealed. Especially, court proceedings dealing with prevailing personal rights (family, inheritance) and prevailing public rights (criminal prosecution) shall prevail.

Against wide-spread rumours and different from how displayed as a favourite cliché among many novels of leading writers, the anonymous numbered accounts have been history for a long time. Opening a bank account is regularly only possible in person and usually upon referral only. Every customer opening a bank account must state his/her identity, hand in passport copies and must confirm in writing that he/she is the beneficial owner of the funds deposited. This document (the form “A”) is an important document in the process of establishing a bank account. Stating inaccurate information may constitute a criminal offense of forgery and/or fraud.

Furthermore, Switzerland has strict regulations on controlling funds to avoid money laundry. Any person being active as professional financial intermediary (which banks are) must compile information on his/her customer and must register in a self-regulatory organisation if the amounts tendered are of a certain importance, namely CHF 2 Mio in annual transactions per intermediary or CHF 5 Mio in assets held per intermediary (Regulation of the Swiss Financial Market Supervisory Board on Professional Financial Intermediary in the Sense of the Swiss Anti Money Laundry Code of 20 August 2002, Art. 6 and 7).

Parallel Secrecy Obligations

Swiss Employment Law stipulates secrecy as an employees' obligation in Art. 321a al. 4 CO:

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" In the course of an employment relationship the employee shall not make use of or inform others of any facts to be kept secret, such as, in particular, manufacturing or business secrets that come to his/her knowledge while in the employer's service. Also, after termination of the employment relationship (Art. 334 et seq.), he/she shall continue to be bound to secrecy to the extent required to safeguard the employers' legitimate interests."

Art. 162 of the Swiss Criminal Code stipulates as follows:

" Anyone who has disclosed a trade secret or any confidential business information that should have been kept secret due to obligations stipulated by the law or by contract,

anyone who has made use of this information to his/her benefit or that of a third party,

shall be, if reported to prosecution, punished by prison or by fine."

Art 320 of the Swiss criminal code again reads as follows:

" Anyone who has disclosed a secret obtained in his/her capacity as political office or civil servant or who has obtained such information due to his/her activity in office or in service shall be punished by prison up to three years or fine. The sanction shall be imposed even after termination of service. No punishment shall occur if the disclosure was done with knowledge of the superior body."

Banking Secrecy in Case of Tax Evasion or Tax Fraud

As a matter of principle, banks and their employees must maintain and respect the banking secrecy irrespective of the actions or omissions of their customers. The only exceptions are stipulated in the reporting duties towards the self-regulatory bodies in connection with the Anti Money Laundry Act and in case of a subpoena issued by a competent Swiss judge either in his/her own competence or by means of enforcement of a foreign judgement.

Although Swiss Federal and cantonal law may stipulate different principles or procedures, in case of taxation the issued of tax evasion and tax fraud are dealt with parallel. Tax fraud has never been considered, and isn't considered, as a crime, but as a malfeasance.

Switzerland will not grant judicial assistance if a matter that is being examined is mere tax evasion. By definition, taxes are being evaded if the attempt to minimize an individual tax exposure is obtained by mere omission of reporting duties and declarations. Tax evasion is accomplished if the tax is finally levied based upon the insufficient information, or if a refund or tax amnesty has been granted as a result of such respective information missing (Art 175 Swiss Code on Direct Taxes, fines; § 204 Zug Code of Taxation, fines in the amount of the omitted tax of down to one third of such an amount).

Tax fraud however is accomplished by submitting forgeg, modified or untruthful documents with the objective to misguide or deceive the tax authorities in their process of levying the tax. This means that a illegitimate activity must have been positively committed by the individual who is subject of the prosecution (Art. 186 Swiss Code on Direct Taxes, prison or fines up to CHF 30'000.00; § 229 Zug Code of Taxation, prison up to two years or fines).

In consequence, tax evasion is usually an administrative proceeding before the administration of the cantonal tax authority in charge of levying the tax. As in the case of tax fraud illegitimate activity is realized, such activity is subject to criminal prosecution. Only such criminal prosecution, however, is subject to judicial assistance to other countries. This derives from the principle of "double jeopardy", meaning that the incriminating incident must be considered a malfeasance or crime in both the requesting jurisdiction as much as in Switzerland. This is the case in matters of tax fraud. The prosecuting judge in Switzerland will immediately lift the bank secrecy and will carry out a full investigation to completion, co-operating with the requesting authority within the framework of the respective international treaties.

Switzerland has clearly stipulated these circumstances with many neighbouring and other countries. In the case of Germany, the extent and technicalities of cooperation is stipulated by federal regulation (Regulation on the Swiss-German Double Taxation Agreement of 30 April 2003, Art. 9, exchange of information in case of fraud). A detailed legal framework for the procedure between US and Swiss authorities has been concluded and ratified (Regulation on the Swiss-

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American Double Taxation Agreement of 15 June 1998, Art. 20c and Art 20d, exchange of information). There is a detailed treaty between Switzerland and the US on reciprocal assistance in criminal matters (Treaty between Switzerland and the US on reciprocal judicial assistance of 25 May 1973) and there are provisions in the double taxation agreement (Double Taxation Agreement Switzerland US of 2 October 1996, Art. 26 and notes).

Professional Responsibility and the Report of Foreign Bank and Financial Accounts

There have been some questions about professional responsibility and the Report of Foreign Bank and Financial Accounts (FBAR). The FBAR, TD F 90-22.1, is not a tax return. It is an information report required under the Bank Secrecy Act (BSA), 31 U.S.C. 5314, and related regulations 31 C.F.R. 103.24, 103.27. Related records are required under 31 C.F.R.103.24 and 103.32. This report, however, is referenced in US tax returns. These tax returns request information about the existence of foreign financial accounts in which the filer of the tax return has a financial interest or over which the filer has signature or other authority. If the response to the leading question is "yes," then the tax return filer is prompted to file an FBAR.

In 2003 IRS was delegated responsibility for assessing penalties for failure to file this report. In 2004, Congress substantially increased penalties for failure to file the FBAR and created a non-willfulness penalty of up to $10,000 for individuals as well as other entities. As a result, there has been increased interest in compliance.

We understand that FBAR non-filers are blaming their preparers for the failure to file — stating that they have reasonable cause for failure to file because the practitioners did not ask about or explain the foreign financial account part of the return. Accordingly, practitioners have expressed concerns about their legal responsibilities respecting this form.

Practitioners must comply with the FBAR filing rules. For example, failure to timely file required tax or information returns, including FBARs, must be disclosed on Form 8554, Application for Renewal of Enrollment to Practice Before the Internal Revenue Service.

A practitioner must comply with FBAR rules as part of his or her due diligence obligation under Section 10.22 of Circular 230:

> **§10.22 Diligence as to accuracy.**
>
> Each attorney, certified public accountant, enrolled agent, or enrolled actuary shall exercise due diligence:
>
> (a) In preparing or assisting in the preparation of, approving, and filing returns, documents, affidavits, and other papers relating to Internal Revenue Service matters;
>
> (b) In determining the correctness of oral or written representations made by him to the Department of the Treasury; and
>
> (c) In determining the correctness of oral or written representations made by him to clients with reference to any matter administered by the Internal Revenue Service

Due diligence does not require that the practitioner "audit" their client. However, it does require that a practitioner make reasonable inquiries when a client provides information that suggests possible participation in overseas transactions/accounts subject to FBAR requirements. A practitioner may rely on information provided by a client in good faith. However, they may not ignore implications learned from information provided or actually known. The practitioner is also required to advise a client of potential penalties likely to apply to a position taken, such as failing to abide by FBAR requirements. The practitioner must make reasonable inquiries if information appears incorrect, inconsistent with an important fact or factual assumption, or is incomplete.

Additional inquiries about the FBAR filing requirements may be resolved by reading "FAQs regarding Report of Foreign Bank and Financial Accounts (FBAR)," and other FBAR information available on the IRS web site at www.irs.gov. Specific questions and comments may be emailed to the following address: FBARquestions@irs.gov. Questions concerning your ethical obligations in this area may be addressed to the Office of Professional Responsibility at: opr @irs.gov.

Confidentiality of Client Information

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A. General Rule (*Model Rule 1.6(a)*) — a lawyer shall not:

1. *Reveal* information
2. Relating to the representation of a client
3. Unless:
   a. Client gives informed consent, OR
   b. Disclosure is impliedly authorized in order to carry out representation (even without client consent), OR
   c. Disclosure is permitted under certain exceptions (see below).
4. This prohibition includes disclosures that could reasonably lead to the discovery of protected information by a third person.

B. Exceptions (*Model Rule 1.6(b)*)

1. A lawyer may reveal information if the lawyer reasonably believes it necessary to:
   a. *Prevent* reasonably certain death or substantial bodily harm
   b. *Prevent* the client from committing a crime or fraud
      i. Reasonably certain to result in substantial injury to the financial interest or property of another
      ii. Client has used lawyer's services in furtherance of the crime or fraud
   c. *Prevent, mitigate* or *rectify* substantial injury to the financial interest or property of another
      iii. Reasonably certain to result/has resulted from the client's commission of a crime or fraud
      iv. Client has used lawyer's services in furtherance of the crime or fraud
   d. Establish a claim or defense
      v. On behalf of the lawyer in a controversy between lawyer and client, OR
      vi. To a criminal charge or civil claim against the lawyer based upon the client's conduct, OR
      vii. To respond to allegations in any proceeding concerning the lawyer's representation of the client
   e. Secure legal advice about the lawyer's compliance with ethics rules
   f. Comply with a law or court order

C. Current Clients (*Model Rule 1.8*)

1. A lawyer shall not *use* information relating to representation of a client to the disadvantage of the client unless.
   a. The client gives informed consent
   b. Permitted/required by the Rules

D. Former Clients (*Model Rule 1.9*)

1. With respect to a former client, a lawyer shall not:
   a. *Use* information relating to the representation to the disadvantage of the former client, except:
      i. As permitted/required by the Rules with respect to a current client
      ii. When the information has become generally known
   b. *Reveal* information relating to the representation except as the Rules would permit/require with respect to a current client.
2. Applies to representation by the lawyer individually, as well as representation by the lawyer's present or former firm.

E. Prospective Clients (*Model Rule 1.18*)

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1. Defined as "[a] person who discusses with a lawyer the possibility of forming a client-lawyer relationship with respect to a matter."
2. Even when no client-lawyer relationship ensues, a lawyer who has had discussions with a prospective client shall not *use* or *reveal* information learned in the consultation, except as Rule 1.9 would permit with respect to information of a former client.

F. Organizations as Clients (*Model Rule 1.13*)

1. If a lawyer for an organization knows that an officer, employee or other person associated with the organization:
  a. Is engaged in an action, intends to act or refuses to act in a matter related to the representation:
    i. that is a violation of a legal obligation to the organization, or a violation of law that reasonably might be imputed to the organization, *and*
    ii. that is likely to result in substantial injury to the organization,
  b. The lawyer shall refer the matter to higher authority in the organization, unless the lawyer reasonably believes that it is not in the best interest of the organization to do so.
2. In the situation described above, a lawyer may reveal information (regardless of whether Rule 1.6 permits such disclosure) if:
  a. Despite the lawyer's efforts, the highest authority that can act on behalf of the organization does not address the issue in a timely and appropriate manner, *and*
  b. The lawyer reasonably believes that the violation is reasonably certain to result in substantial injury to the organization,
3. Disclosure is only appropriate to the extent the lawyer reasonably believes disclosure is necessary to prevent substantial injury to the organization.
  a. This Rule does not apply with respect to information relating to a lawyer's representation of an organization to investigate an alleged violation of law, or to defend the organization or an officer, employee or other constituent associated with the organization against a claim arising out of an alleged violation of law.

G. Candor Toward the Tribunal

1. If a lawyer, the lawyer's client, or a witness called by the lawyer, has offered material evidence and the lawyer comes to know of its falsity, the lawyer shall take reasonable remedial measures, including, if necessary, disclosure to the tribunal.
2. A lawyer who represents a client in an adjudicative proceeding and who knows that a person intends to engage, is engaging or has engaged in criminal or fraudulent conduct related to the proceeding shall take reasonable remedial measures, including, if necessary, disclosure to the tribunal.
3. These duties to the tribunal continue to the conclusion of the proceeding, and apply even if compliance requires disclosure of information otherwise protected by Rule 1.6.

Rule 1.9 Duties To Former Clients

(c) A lawyer who has formerly represented a client in a matter or whose present or former firm has formerly represented a client in a matter shall not thereafter:

(1) use information relating to the representation to the disadvantage of the former client except as these Rules would permit or require with respect to a client, or when the information has become generally known; or

(2) reveal information relating to the representation except as these Rules would permit or require with respect to a client.

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Rule 1.18 Duties To Prospective Client

(a) A person who discusses with a lawyer the possibility of forming a client-lawyer relationship with respect to a matter is a prospective client.

(b) Even when no client-lawyer relationship ensues, a lawyer who has had discussions with a prospective client shall not use or reveal information learned in the consultation, except as Rule 1.9 would permit with respect to information of a former client.

. . .

Rule 1.13 Organization As Client

(a) A lawyer employed or retained by an organization represents the organization acting through its duly authorized constituents.

(b) If a lawyer for an organization knows that an officer, employee or other person associated with the organization is engaged in action, intends to act or refuses to act in a matter related to the representation that is a violation of a legal obligation to the organization, or a violation of law that reasonably might be imputed to the organization, and that is likely to result in substantial injury to the organization, then the lawyer shall proceed as is reasonably necessary in the best interest of the organization. Unless the lawyer reasonably believes that it is not necessary in the best interest of the organization to do so, the lawyer shall refer the matter to higher authority in the organization, including, if warranted by the circumstances to the highest authority that can act on behalf of the organization as determined by applicable law.

(c) Except as provided in paragraph (d), if

(1) despite the lawyer's efforts in accordance with paragraph (b) the highest authority that can act on behalf of the organization insists upon or fails to address in a timely and appropriate manner an action, or a refusal to act, that is clearly a violation of law, and

(2) the lawyer reasonably believes that the violation is reasonably certain to result in substantial injury to the organization,

then the lawyer may reveal information relating to the representation whether or not Rule 1.6 permits such disclosure, but only if and to the extent the lawyer reasonably believes necessary to prevent substantial injury to the organization.

(d) Paragraph (c) shall not apply with respect to information relating to a lawyer's representation of an organization to investigate an alleged violation of law, or to defend the organization or an officer, employee or other constituent associated with the organization against a claim arising out of an alleged violation of law.

. . .

Advocate

Rule 3.3 Candor Toward The Tribunal

(a) A lawyer shall not knowingly:

. . .

(3) offer evidence that the lawyer knows to be false. If a lawyer, the lawyer's client, or a witness called by the lawyer, has offered material evidence and the lawyer comes to know of its falsity, the lawyer shall take reasonable remedial measures, including, if necessary, disclosure to the tribunal. A lawyer may refuse to offer evidence, other than the testimony of a defendant in a criminal matter, that the lawyer reasonably believes is false.

(b) A lawyer who represents a client in an adjudicative proceeding and who knows that a person intends to engage, is engaging or has engaged in criminal or fraudulent conduct related to the proceeding shall take reasonable remedial measures, including, if necessary, disclosure to the tribunal.

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(c) The duties stated in paragraphs (a) and (b) continue to the conclusion of the proceeding, and apply even if compliance requires disclosure of information otherwise protected by Rule 1.6.

Center *for* Professional Responsibility

Model Rules of Professional Conduct

Client-Lawyer Relationship

Rule 1.6 Confidentiality Of Information - Comment

[1] This Rule governs the disclosure by a lawyer of information relating to the representation of a client during the lawyer's representation of the client. See Rule 1.18 for the lawyer's duties with respect to information provided to the lawyer by a prospective client, Rule 1.9(c)(2) for the lawyer's duty not to reveal information relating to the lawyer's prior representation of a former client and Rules 1.8(b) and 1.9(c)(1) for the lawyer's duties with respect to the use of such information to the disadvantage of clients and former clients.

[2] A fundamental principle in the client-lawyer relationship is that, in the absence of the client's informed consent, the lawyer must not reveal information relating to the representation. See Rule 1.0(e) for the definition of informed consent. This contributes to the trust that is the hallmark of the client-lawyer relationship. The client is thereby encouraged to seek legal assistance and to communicate fully and frankly with the lawyer even as to embarrassing or legally damaging subject matter. The lawyer needs this information to represent the client effectively and, if necessary, to advise the client to refrain from wrongful conduct. Almost without exception, clients come to lawyers in order to determine their rights and what is, in the complex of laws and regulations, deemed to be legal and correct. Based upon experience, lawyers know that almost all clients follow the advice given, and the law is upheld.

[3] The principle of client-lawyer confidentiality is given effect by related bodies of law: the attorney-client privilege, the work product doctrine and the rule of confidentiality established in professional ethics. The attorney-client privilege and work-product doctrine apply in judicial and other proceedings in which a lawyer may be called as a witness or otherwise required to produce evidence concerning a client. The rule of client-lawyer confidentiality applies in situations other than those where evidence is sought from the lawyer through compulsion of law. The confidentiality rule, for example, applies not only to matters communicated in confidence by the client but also to all information relating to the representation, whatever its source. A lawyer may not disclose such information except as authorized or required by the Rules of Professional Conduct or other law. See also Scope.

[4] Paragraph (a) prohibits a lawyer from revealing information relating to the representation of a client. This prohibition also applies to disclosures by a lawyer that do not in themselves reveal protected information but could reasonably lead to the discovery of such information by a third person. A lawyer's use of a hypothetical to discuss issues relating to the representation is permissible so long as there is no reasonable likelihood that the listener will be able to ascertain the identity of the client or the situation involved.

Authorized Disclosure

[5] Except to the extent that the client's instructions or special circumstances limit that authority, a lawyer is impliedly authorized to make disclosures about a client when appropriate in carrying out the representation. In some situations, for example, a lawyer may be impliedly authorized to admit a fact that cannot properly be disputed or to make a disclosure that facilitates a satisfactory conclusion to a matter. Lawyers in a firm may, in the course of the firm's practice, disclose to each other information relating to a client of the firm, unless the client has instructed that particular information be confined to specified lawyers.

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Disclosure Adverse to Client

[6] Although the public interest is usually best served by a strict rule requiring lawyers to preserve the confidentiality of information relating to the representation of their clients, the confidentiality rule is subject to limited exceptions. Paragraph (b)(1) recognizes the overriding value of life and physical integrity and permits disclosure reasonably necessary to prevent reasonably certain death or substantial bodily harm. Such harm is reasonably certain to occur if it will be suffered imminently or if there is a present and substantial threat that a person will suffer such harm at a later date if the lawyer fails to take action necessary to eliminate the threat. Thus, a lawyer who knows that a client has accidentally discharged toxic waste into a town's water supply may reveal this information to the authorities if there is a present and substantial risk that a person who drinks the water will contract a life-threatening or debilitating disease and the lawyer's disclosure is necessary to eliminate the threat or reduce the number of victims.

[7] Paragraph (b)(2) is a limited exception to the rule of confidentiality that permits the lawyer to reveal information to the extent necessary to enable affected persons or appropriate authorities to prevent the client from committing a crime or fraud, as defined in Rule 1.0(d), that is reasonably certain to result in substantial injury to the financial or property interests of another and in furtherance of which the client has used or is using the lawyer's services. Such a serious abuse of the client-lawyer relationship by the client forfeits the protection of this Rule. The client can, of course, prevent such disclosure by refraining from the wrongful conduct. Although paragraph (b) (2) does not require the lawyer to reveal the client's misconduct, the lawyer may not counsel or assist the client in conduct the lawyer knows is criminal or fraudulent. See Rule 1.2(d). See also Rule 1.16 with respect to the lawyer's obligation or right to withdraw from the representation of the client in such circumstances, and Rule 1.13(c), which permits the lawyer, where the client is an organization, to reveal information relating to the representation in limited circumstances.

[8] Paragraph (b)(3) addresses the situation in which the lawyer does not learn of the client's crime or fraud until after it has been consummated. Although the client no longer has the option of preventing disclosure by refraining from the wrongful conduct, there will be situations in which the loss suffered by the affected person can be prevented, rectified or mitigated. In such situations, the lawyer may disclose information relating to the representation to the extent necessary to enable the affected persons to prevent or mitigate reasonably certain losses or to attempt to recoup their losses. Paragraph (b)(3) does not apply when a person who has committed a crime or fraud thereafter employs a lawyer for representation concerning that offense.

[9] A lawyer's confidentiality obligations do not preclude a lawyer from securing confidential legal advice about the lawyer's personal responsibility to comply with these Rules. In most situations, disclosing information to secure such advice will be impliedly authorized for the lawyer to carry out the representation. Even when the disclosure is not impliedly authorized, paragraph (b)(4) permits such disclosure because of the importance of a lawyer's compliance with the Rules of Professional Conduct.

[10] Where a legal claim or disciplinary charge alleges complicity of the lawyer in a client's conduct or other misconduct of the lawyer involving representation of the client, the lawyer may respond to the extent the lawyer reasonably believes necessary to establish a defense. The same is true with respect to a claim involving the conduct or representation of a former client. Such a charge can arise in a civil, criminal, disciplinary or other proceeding and can be based on a wrong allegedly committed by the lawyer against the client or on a wrong alleged by a third person, for example, a person claiming to have been defrauded by the lawyer and client acting together. The lawyer's right to respond arises when an assertion of such complicity has been made. Paragraph (b)(5) does not require the lawyer to await the commencement of an action or proceeding that charges such complicity, so that the defense may be established by responding directly to a third party who has made such an assertion. The right to defend also applies, of course, where a proceeding has been commenced.

[11] A lawyer entitled to a fee is permitted by paragraph (b)(5) to prove the services rendered in an action to collect it. This aspect of the rule expresses the principle that the beneficiary of a fiduciary relationship may not exploit it to the det-

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riment of the fiduciary.

[12] Other law may require that a lawyer disclose information about a client. Whether such a law supersedes Rule 1.6 is a question of law beyond the scope of these Rules. When disclosure of information relating to the representation appears to be required by other law, the lawyer must discuss the matter with the client to the extent required by Rule 1.4. If, however, the other law supersedes this Rule and requires disclosure, paragraph (b)(6) permits the lawyer to make such disclosures as are necessary to comply with the law.

[13] A lawyer may be ordered to reveal information relating to the representation of a client by a court or by another tribunal or governmental entity claiming authority pursuant to other law to compel the disclosure. Absent informed consent of the client to do otherwise, the lawyer should assert on behalf of the client all nonfrivolous claims that the order is not authorized by other law or that the information sought is protected against disclosure by the attorney-client privilege or other applicable law. In the event of an adverse ruling, the lawyer must consult with the client about the possibility of appeal to the extent required by Rule 1.4. Unless review is sought, however, paragraph (b)(6) permits the lawyer to comply with the court's order.

[14] Paragraph (b) permits disclosure only to the extent the lawyer reasonably believes the disclosure is necessary to accomplish one of the purposes specified. Where practicable, the lawyer should first seek to persuade the client to take suitable action to obviate the need for disclosure. In any case, a disclosure adverse to the client's interest should be no greater than the lawyer reasonably believes necessary to accomplish the purpose. If the disclosure will be made in connection with a judicial proceeding, the disclosure should be made in a manner that limits access to the information to the tribunal or other persons having a need to know it and appropriate protective orders or other arrangements should be sought by the lawyer to the fullest extent practicable.

[15] Paragraph (b) permits but does not require the disclosure of information relating to a client's representation to accomplish the purposes specified in paragraphs (b)(1) through (b)(6). In exercising the discretion conferred by this Rule, the lawyer may consider such factors as the nature of the lawyer's relationship with the client and with those who might be injured by the client, the lawyer's own involvement in the transaction and factors that may extenuate the conduct in question. A lawyer's decision not to disclose as permitted by paragraph (b) does not violate this Rule. Disclosure may be required, however, by other Rules. Some Rules require disclosure only if such disclosure would be permitted by paragraph (b). See Rules 1.2(d), 4.1(b), 8.1 and 8.3. Rule 3.3, on the other hand, requires disclosure in some circumstances regardless of whether such disclosure is permitted by this Rule. See Rule 3.3(c).

Acting Competently to Preserve Confidentiality

[16] A lawyer must act competently to safeguard information relating to the representation of a client against inadvertent or unauthorized disclosure by the lawyer or other persons who are participating in the representation of the client or who are subject to the lawyer's supervision. See Rules 1.1, 5.1 and 5.3.

[17] When transmitting a communication that includes information relating to the representation of a client, the lawyer must take reasonable precautions to prevent the information from coming into the hands of unintended recipients. This duty, however, does not require that the lawyer use special security measures if the method of communication affords a reasonable expectation of privacy. Special circumstances, however, may warrant special precautions. Factors to be considered in determining the reasonableness of the lawyer's expectation of confidentiality include the sensitivity of the information and the extent to which the privacy of the communication is protected by law or by a confidentiality agreement. A client may require the lawyer to implement special security measures not required by this Rule or may give informed consent to the use of a means of communication that would otherwise be prohibited by this Rule.

Former Client

[18] The duty of confidentiality continues after the client-lawyer relationship has terminated. See Rule 1.9(c)(2). See

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Rule 1.9(c)(1) for the prohibition against using such information to the disadvantage of the former client.

SURVEY OF THE ATTORNEY-CLIENT PRIVILEGE AND WORK PRODUCT DOCTRINE IN TAX CONTROVERSIES AND LITIGATION [FNf1]

Jerald David August Fox Rothschild LLP West Palm Beach, FL/Philadelphia, PA

TAX PRACTITIONER-CLIENT PRIVILEGE SECTION 7525.

Despite the long-standing precedent which does not recognize an accountant-client privilege for federal tax controversies, communications between an accountant and a client occurring after July 22, 1998 may be privileged under the Federal accountant-client privilege contained in 26 U.S.C. Section 7525.

A. Affirmative Obligation.

The accountant/return preparer is under an affirmative obligation to prepare and file true and accurate returns. Mistakes which are the product of negligence or intentional disregard of rules and regulations subject the preparer to civil liability. §§ 6694, 6701, 7407. Criminal liability is imposed on return preparers under the Internal Revenue Code (26 U.S.C.) as well as the general federal crimes provisions (18 U.S.C.) who knowingly file false returns or aid and assist a client to file a false return. § 7206(2) (aid or assist in false return); § 7207 (false document, statement). 18 U.S.C. § 371 (conspiracy to evade); § 2 (aiding and abetting in commission of felony); 1001 (false statement).

B. Section 7525.

The section was enacted after the Supreme Court's decision in Arthur Young, Arthur Young, 465 U.S. at 817 which declined to create a new "accountant-client privilege" between a corporation and its independent auditor. Section 7525(a)(1) confers a privilege on tax advice in the form of confidential communications "between a taxpayer and any federally authorized tax practitioner" to the same extent that such communications would be protected between a taxpayer and an attorney, but carries several significant limitations.

1. First, it does not apply to a tax practitioner's "work product" in preparing a return or to "communications between a tax practitioner and a client simply for the preparation of a tax return." U.S. v. KPMG, LLP, 316 F. Supp. 2d 30, 35 (D.D.C. 2004) (the court found that a tax opinion prepared by an accountant was not privileged because the analysis in the opinion letter was "prepared in connection with preparation of a tax return."). The relevant tax return nexus was found because the opinion related to a transaction to be disclosed on the taxpayer's tax return. Despite this narrow reading of the privilege, a tax opinion delivered by either an attorney or an accountant may be protected under the work-product doctrine, described below. See U.S. v. Adlman, 134 F.3d 1194 (2nd Cir. 1998) (reversing and remanding lower court's decision to reject claim of work product privilege by reason that the tax opinion prepared by an accounting firm was prepared in anticipation of litigation).

2. Second, the privilege does not apply to communications regarding "tax shelter" transactions (i.e., transactions with a significant purpose of tax avoidance). See 26 U.S.C. § 7525 (The Federal statutory accountant-client privilege does not apply to communications regarding "corporate" tax shelters prior to October 22, 2004, and to any tax shelter after October 22, 2004).

3. Third, the privilege may be asserted only by a taxpayer or an accountant in a non-criminal proceeding before the IRS or brought in Federal court.

C. Applicability.

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1. Investor Lists. The Federal accountant-client privilege does not appear to protect investor lists maintained by accounting firms to market "tax shelters." In U.S. v. BDO Seidman, 337 F.3d 802 (7th Cir. 2003), the court held that investors could not have an expectation of confidentiality at the time of investment because the investors should have known that the accounting firm was required to disclose their names. See also U.S. v. Arthur Anderson, 2003-2 U.S.T.C. ¶ 50,624 (D. Ill. 2003) (following the reasoning in BDO Seidman). The reasoning in BDO Seidman was adopted in substance in Doe v. KPMG, LLP, 325 f. Supp. 746 (D. Tex. 2004), where an accounting firm notified the investors of the possibility of identity disclosure.

2. Opinion Letters. In U.S. v. KPMG LLP, 237 F. Supp. 2d 35 (D.D.C. 2002) the court held that certain documents and opinion letters discussing the tax consequences of the transactions were not protected under the tax practitioner privilege because the communications were for the purpose of preparing tax returns.

II. ATTORNEY WORK PRODUCT DOCTRINE.

Related but yet distinctly separate from the attorney-client privilege is the immunity given for an attorney's work product.

A. Generally.

It is broader than the attorney-client privilege since it is not limited to confidential communications between an attorney and client. The work product doctrine protects documents prepared "in anticipation of litigation" by or for another party, or by or for that other party's representative. See Hickman v. Taylor, 329 U.S. 495 (1947); F.R.C.P. 26(b)(3). Although the IRS may be able to compel production of a document by establishing a substantial need for the document, an attorney's mental impression will be entitled to substantial protection, more so than factual information also contained in documents prepared in anticipation of litigation. See, e.g., Upjohn v. U.S., 449 U.S. 383 (1981) (Supreme Court noted that an attorney's mental impressions "cannot be disclosed simply on a showing of substantial need and inability to obtain the equivalent without undue hardship).

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B. Two Types of Work Product.

There are two types of work product, fact work product and opinion work product.

1. Fact Work Product. Fact work product encompasses such items as correspondence, interview notes, and general fact memoranda. For example, if a memorandum discusses business records, the memorandum is non-discoverable work product because the IRS could presumably summon the underlying business records. Similarly, witness statements are generally non-discoverable work product because the party seeking discovery could depose the witness itself.

Documents that are not created in anticipation of litigation, such as general business records, are not fact work product and are discoverable.

2. Opinion Work Product. “At its core, the work product doctrine shelters the mental processes of the attorney, providing a privileged area within which he can analyze and prepare his clients case.” U.S. v. Chevron Texaco Corp., 241 F. Supp. 2d 1065, 1081 (N.D. Cal. 2002). This includes, for example, materials reflecting analyses of the law, analyses of an adversary's position, potential legal theories, strategies for handling the controversy, and analyses of different forums. In general, the question of what constitutes opinion work product is construed broadly in favor of protecting such materials. For example, it may include the order in which an attorney organizes certain documents because the organization of the documents can show the attorney's mental impressions concerning a case.

C. Nature of the Privilege.

The purpose of the privilege is “to preserve a zone of privacy in which a lawyer can prepare and develop legal theories and strategy ‘with an eye toward litigation’ free from unnecessary intrusion by his adversaries.” U.S. v. Adlman, 134 F.3d 1194, 1196 (2d Cir. 1998) (citing Hickman v. Taylor, 329 U.S. 495, 510-11 (1947)), “to prevent a litigant from taking a free ride on the research and thinking of his opponent's lawyer and to avoid the resulting deterrent to a lawyer's committing his thoughts to paper.” Frederick, 182 F.3d at 500.

D. Origin.

The privilege first was articulated by the Supreme Court in Hickman v. Taylor, 329 U.S. 495, 67 S. Ct. 685, 91 L. Ed. 451 (1947), and, later, was codified in Federal Rule of Civil Procedure 26(b)(3) which provides:

(3) Trial Preparation Materials. . . . a party may obtain discovery of documents and tangible things otherwise discoverable under subdivision (b)(1) of this rule and prepared in anticipation of litigation or for trial by or for another party or by or for that other party's representative . . . only upon a showing that the party seeking discovery has substantial need of the materials in the preparation of the party's case and that the party is unable without undue hardship to obtain the substantial equivalent of the materials by other means.

In ordering discovery of such materials when the required showing has been made, the court shall protect against disclosure of the mental impressions, conclusions, opinions, or legal theories of an attorney or other representative of a party concerning the litigation.

E. Substantial Need.

As the rule indicates, unlike the attorney-client privilege, the work product privilege is a qualified privilege which may be overcome by a showing of “substantial need.” Fed. R. Civ. P. 26(b)(3). The burden of establishing “substantial need” rests on the party seeking to overcome the privilege; and, when “opinion work product” consisting of “mental

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impressions, conclusions, opinions or legal theories" of attorneys is involved, the burden of establishing "substantial need" is greater than it is with respect to documents that are merely obtained by a party. Upjohn, 449 U.S. at 401-2 ("we think a far stronger showing of necessity and unavailability by other means . . . would be necessary to compel disclosure" of opinion work-product.).

1. Nearly Absolute Protection. Some courts have accorded "nearly absolute" protection to work product consisting of opinions or theories. In re Grand Jury Subpoena, 220 F.R.D. 130, 145 (D. Mass. 2004) (collecting cases).

2. In Response to IRS Summonses. In Upjohn, the Supreme Court made it clear that the work product privilege may be invoked in response to IRS summonses.

[T]he obligation imposed by a tax summons remains 'subject to the traditional privileges and limitations.' . . . Nothing in the language of the IRS summons provisions or their legislative history suggests an intent on the part of Congress to preclude application of the work-product doctrine. Rule 26(b)(3) codifies the work-product doctrine, and the Federal Rules of Civil Procedure are made applicable to summons enforcement proceedings by Rule 81(a)(3).

F. In Anticipation of Litigation Requirement.

Courts have applied two different tests in determining whether a document was prepared "in anticipation of litigation."

1. Primary Purpose Test. Under the "primary purpose" test, documents are held to be prepared in anticipation of litigation "as long as the primary motivating purpose behind the creation of a document was to aid in possible future litigation." In U.S. v. El Paso Co., 682 F.2d 530 (5th Cir. 1982), cert. denied, 466 U.S. 944 (1984), the corporate taxpayer wanted to keep tax accrual workpapers and similar documents out of the hands of the IRS, which was auditing its returns. The Fifth Circuit, applying the strict standard of U.S. v. Davis, 636 F.2d 1028 (5th Cir. 1981) held that the documents had to be produced because they were created in the ordinary course of business.

2. Because Of Test. Under the more inclusive "because of" test, the relevant inquiry is whether the document was prepared or obtained "because of" the prospect of litigation. U.S. v. Adlman, 134 F.3d 1194 (2d Cir. 1998). In Adlman, after making a detailed analysis of the two tests, the Second Circuit found the "because of" test "more consistent with both the literal terms and the purposes of [Rule 26(b)(3)]".

a. Adiman v. U.S. 134 F.3d 1194 (2d Cir. 1998). There a divided three-judge panel led by Circuit Judge Leval concluded that the phrase "in anticipation of litigation" as used in Fed. Rul. Civ. P. 26(b)(3) could be read broadly enough to encompass a memo prepared to assess the desirability of a business transaction, which, if undertaken, would give rise to litigation. "Where a document was created because of anticipated litigation, and would not have been prepared in substantially similar form but for the prospect of that litigation, if falls within Rule 26(b)(3)," Judge Leval wrote:

"The document in question was a legal memorandum prepared by an outside accounting firm for an in-house corporate legal officer. The subject of the memo was the application of the tax rules governing corporate reorganizations to a combination of subsidiaries aggressively recast as a taxable sale of the shares of one subsidiary to another to enable the corporation to recognize a large capital loss on the shares. Because the corporation, Sequa Corp., was under continuous audit, it was reasonably foreseeable that the IRS would challenge the desired result. Adlman had previously failed in his attorney-client privilege claim."

b. Other Circuits. Most circuits apply this test, which is called the "because of" test, but none has stretched it as far as Judge Leval did in Adlman. (In re Grand Jury Proceedings, 604 F.2d 798 (3rd Cir. 1979); National Union Fire Ins. Co. v. Murray Sheet Metal Co., Inc., 967 F.2d 980 (4th Cir. 1992); Binks Mfg. Co. v. National Presto Indus., Inc., 709 F.2d 1109 (7th Cir. 1983); Simon v. G.D. Searle & Co., 816 F.2d 397, (8th Cir. 1987) (holding that individual case litigation reserves prepared by company's attorney were protected opinion work product), cert. denied, 484 U.S. 917 (1987); Senate of Puerto Rico v. U.S. Dep't of Justice, 823 F.2d 574 (D.C. Cir. 1987); In re

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Sealed Case, 146 F.3d 881, 884 (D.C. Cir. 1998); Maine v. Dept. of the Interior, 298 F.3d 60, 68, 70 (1st Cir. 2002). (The work product privilege does not apply to "'documents that are prepared in the ordinary course of business or that would have been created in essentially similar form irrespective of the litigation."') (quoting Adlman, 134 F.3d at 1202); see also U.S. v. Chevron, 241 F. Supp. 2d 1065, 1082 (N.D. Cal. 2002) (adopting Second Circuit's approach in Adlman and rejecting the "primary motivating test." Holding that '[e]xcept where a document would have been generated in the normal course of business even if no litigation was anticipated, the work product doctrine can reach documents prepared 'because of litigation' even if they were prepared in connection with a business transaction or also served a business purpose.')

G. Waiver of Work Product Privilege.

Since the work product privilege serves a purpose different from the attorney-client or tax practitioner privileges, the kind of conduct that waives the privilege also differs.

1. Generally. Protection is forfeited by disclosures in circumstances where the attorney cannot reasonably expect to limit the future use of the otherwise protected materials. Westinghouse Elec. Corp. v. Republic of the Philippines, 951 F.2d 1414 (3rd Cir. 1991). The [attorney-client] privilege . . . is designed to protect confidentiality, so that any disclosure outside the magic circle is inconsistent with the privilege; by contrast, work product protection is provided against "adversaries," so only disclosing material i a way inconsistent with keeping it from an adversary waives work product protection." U.S. v. Massachusetts Institute of Technology, ("MIT"), 129 F.3d 681 (1st Cir. 1997).

2. Disclosure. Only disclosures that are inconsistent with keeping the information from an adversary constitute a waiver of the work product privilege. Gutter, 1988 WL 2017926 (S.D. Fl. 1998) ("While disclosure to outside auditors may waive the attorney-client privilege, it does not waive the work product privilege"). 129 F.3d at 687 (collecting cases). See Jaffe Pension Plan, 237 F.R.D. 183 ("[T]he work product privilege may be waived by disclosures to third parties 'in a manner which substantially increases the opportunity for potential adversaries to obtain the information."') (citation omitted); In re Raytheon Sec. Litig., 218 F.R.D. at 360 (D. Mass. 2003) ("[D]isclosure of a document to third persons does not waive the protection unless it has substantially increased the opportunity for potential adversaries to obtain the information.").

a. Not automatic waiver. Voluntary disclosure to third parties does not automatically waiver work product protection. Most courts considering the question have held that disclosure of information to an independent auditor does not waive the work product privilege because it does not substantially increase the opportunity for potential adversaries to obtain the information. In re JDS Uniphase Corp. Sec. Litig., 2006 WL 2850049 (N. D. Cal. 2006) (work product protection not waived when protected board minutes were disclosed to the independent auditor); Jaffe Pension Plan, 237 F.R.D. at 183 (Because an independent auditor does not have an adversarial relationship with the client. "[d]isclosing documents to an auditor does not substantially increase the opportunity for potential adversaries to obtain the information."); Frank Betz Assocs., Inc. v. Jim Walter Homes Inc., 226 F.R.D. 533, 535 (D.S.C. 2005) (disclosure to independent auditor of documents supporting reserve for copyright infringement litigation did not waive work product protection); Merrill Lynch & Co., Inc. v. Allegheny Energy, Inc., 229 F.R.D. 441 (S.D.N.Y. 2004) (even though an auditor "must maintain an independent role," disclosure to auditor not a waiver of work product privilege because no likelihood that the independent auditors were a conduit to an adversary or that accounting rules would "mandate public disclosure" of the documents); Gutter, 1998 WL 2017926 (S.D. Fl. 1998) (work product privilege not waived by disclosure to auditor of letters estimating cost of litigation since the accountants are not considered a conduit to a potential adversary" and "there is an expectation that confidentiality of such information will be maintained by the recipient."); In re Pfizer Inc. Sec. Litig., 1993 WL 561125 (S.D.N.Y. 2003) (no waiver of work product privilege because auditor "not reasonably viewed as a conduit to a

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potential adversary.").

b. Not Related to Facilitation of its Trial Preparation. Where a party discloses work product for reasons not related to the facilitation of its trial preparation, the work product protection may be waived. Waiver is found where the disclosure substantially increases the opportunity for potential adversaries to obtain information. F.S.A. 2000420007 (July 12, 2000). In F.S.A. 200042007, the IRS ruled that a taxpayer waived the attorney-client privilege and the work product protection when it turned over to the IRS several boxes of documents, which included documents marked as being protected by the attorney-client privilege. The taxpayer allowed IRS examiners approximately 18 months of unrestricted access to the documents and failed to raise, at any time during this period, the attorney-client privilege or work-product protection. The taxpayer contested use of the documents after receiving an assessment, claiming that the documents had been inadvertently provided to the IRS examiners. The IRS, however, took the position that the taxpayer had failed to take precautions to prevent inadvertent disclosure and thus had effectively waived any protection applicable to the documents.

c. To Gain an Advantage. When party reveals part of a privileged communication to gain an advantage in litigation, the party waives the privilege for all other communications on the same subject matter. In re Sealed Case, 676 F.2d 793, 809 (D.C. Cir. 1982) (Court found that by voluntarily and selectively submitting report of investigative counsel to the SEC the company fully waived the privilege. This waiver included any documentation necessary to evaluate the report.). In In re Sealed Case, outside counsel for the defendant conducted an internal investigation into possible illegal foreign payments and submitted a final report to the SEC. The grand jury subpoenaed and received all but 38 of these documents. Id. at 803-04. The court of appeals held that the privilege had been waived for of all the documents, including the 38 that had been withheld. It rejected the corporation's argument that disclosure would prompt corporations to avoid voluntary cooperation with the government, and found that the corporation had "attempted to manipulate its privilege, by withholding vital documents while making a great pretense of full disclosure of their contents." Id. at 825. However, the court did state that the SEC or any other government agency could expressly agree to limitations on further disclosure consistent with their legal responsibilities. Id. at 824.

d. Disclosure to the Government. Most courts have rejected or at least applied a narrow construction of selective waiver doctrine, and have held that selective disclosure of a document to the government constitutes complete waiver of the privilege. See e.g., Permian Corp. v. U.S., 665 F.2d 1214, 1219-20 (D.C. Cir. 1981). Since the D.C. Circuit first rejected selective waiver, the First, Second, Third, Fourth and Sixth Circuits have rejected the selective waiver doctrine to varying degrees. See, e.g., Westinghouse Elec. Corp. v. Republic of the Philippines, 951 F.2d 1414 (3rd Cir. 1991) (In the interest of fairness, full subject matter waiver will result from a partial disclosure in two instances: testimonial revelation and self-serving disclosure.). In Westinghouse the Court held that disclosure of work product during this investigation fully waived any attorney-client or work product protection, even with respect to third parties in civil litigation. Court reasoned that protection is not required to encourage these types of disclosures to a government agency since the corporation will turn over the exculpating documents willingly, privileged or not, in order to obtain lenient treatment. Court thus refused to apply selective waiver to reports disclosed to the government.

An individual or entity may not disclose documents to a federal government agency that is a potential adversary in litigation and then assert the work product privilege in seeking to protect the disclosure of the same documents in litigation involving that or another federal agency. Evergreen Trading, LLC v. U.S., — Fed. Cl. ___, 1007 WL 4553061 (Fed. Cl.)

H. Overcoming the Work Product Privilege.

As already noted, the work product doctrine creates only a qualified privilege that may be overcome by a showing of

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(1) “substantial need” for the protected documents, and (2) an inability to otherwise obtain the information contained therein or its substantial equivalent without “undue hardship.” Fed. R. Civ. P. 26(b)(3).

1. Substantial Need. While establishing that protected documents relate to a legitimate IRS investigation may satisfy the “relevancy” requirement of section 7602, it is insufficient to establish the “substantial need” showing necessary to overcome the work product privilege. See Davis v. Emery Air Freight Corp., 212 F.R.D. 432, 436 (D. Me. 2003) (“the fact that the documents sought might be relevant to [plaintiff's] claims is not enough under Rule 26(b)(3) ”).

2. Undue Hardship. That is especially true in the case of opinion work product, which consists of the “mental impressions, conclusions, opinions or legal theories” of attorneys, where the party seeking the materials must meet a heightened burden. See Upjohn, 449 U.S. at 401-2 (“a far stronger showing of necessity and unavailability by other means . . . would be necessary to compel disclosure” of attorneys' notes and memoranda regarding oral statements of witnesses which “reveal the attorneys' mental processes in evaluating the communications”); see also Fed. R. Civ. P. 26(b)(3) (“In ordering discovery . . . the court shall protect against disclosure of the mental impressions, conclusions, opinions, or legal theories of an attorney or other representative of a party concerning the litigation.”).

III. DISCOVERY BY IRS OF TAX ACCRUAL WORKPAPERS AND FIN 48 OPINIONS AND WORKPAPERS

A. Section 6001.

Every person liable for any tax imposed by this title, or for the collection thereof, shall keep such records, render such statements, make such returns, and comply with such rules and regulations as the Secretary may from time to time prescribe. Whenever in the judgment of the Secretary it is necessary, he may require any person, by notice served upon such person or by regulations, to make such returns, render such statements, or keep such records, as the Secretary deems sufficient to show whether or not such person is liable for tax under this title. The only records which an employer shall be required to keep under this section in connection with charged tips shall be charge receipts, records necessary to comply with section 6053(c), and copies of statements furnished by employees under section 6053(a).

B. Section 7602.

Section 7602 of the Internal Revenue Code authorizes the Secretary of the Treasury to summon and “examine any books, papers, records, or other data which may be relevant or material” to a particular tax inquiry.

1. Section 7602. For the purpose of ascertaining the correctness of any return, making a return where none has been made, determining the liability of any person for any internal revenue tax or the liability at law or in equity of any transferee or fiduciary of any person in respect of any internal revenue tax, or collecting any such liability, the Secretary is authorized— (1) To examine any books, papers, records, or other data which may be relevant or material to such inquiry; (2) To summon the

[FNf1]. This outline was previously presented in conjunction with the ALI-ABA Video Webcast “New Proposed Tax Preparer Regulations & Enhanced Circular 230 Enforcement” — July 11, 2008.

[NOTE]

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From: Packman, Kevin E (MIA - X22261)
Sent: Monday, June 08, 2009 10:37 AM
To: Weinstein, Andrew H (MIA - X27755)

Subject: RE: FBAR Reminder & Update

From the OPR Website

Professional Responsibility and the Report of Foreign Bank and Financial Accounts

There have been some questions about professional responsibility and the Report of Foreign Bank and Financial Accounts (FBAR). The FBAR, TD F 90-22.1, is not a tax return. If is an information report required under the Bank Secretary Act (BSA), 31 U.S.C. 5314, and related regulations 31 C.F.R. 103.24, 103.27. Related records are required under 31 C.F.R.103.24 and 103.32. This report, however, is referenced in US tax returns. These tax returns request information about the existence of foreign financial accounts in which the filer of the tax return has a financial interest or over which the filer has signature or other authority. If the response to the leading question is "yes," then the tax return filer is prompted to file an FBAR.

In 2003 IRS was delegated responsibility for assessing penalties for failure to file this report. In 2004, Congress substantially increased penalties for failure to file the FBAR and created a non-willfulness penalty of up to $10,000 for individuals as well as other entities. As a result, there has been increased interest in compliance.

We understand that FBAR non-filers are blaming their preparers for the failure to file — stating that they have reasonable cause for failure to file because the practitioners did not ask about or explain the foreign financial account part of the return. Accordingly, practitioners have expressed concerns about their legal responsibilities respecting this form.

Practitioners must comply with the FBAR filing rules. For example, failure to timely file required tax or information returns, including FBARs, must be disclosed on Form 8554, Application for Renewal of Enrollment to Practice Before the Internal Revenue Service.

A practitioner must comply with FBAR rules as part of his or her due diligence obligation under Section 10.22 of Circular 230:

§10.22 Diligence as to accuracy.

Each attorney, certified public accountant, enrolled agent, or enrolled actuary shall exercise due diligence:

(a) in preparing or assisting in the preparation of, approving, and filing returns, documents, affidavits, and other papers relating to Internal Revenue Service matters;

(b) In determining the correctness of oral or written representations made by him to the Department of the Treasury; and

(c) In determining the correctness of oral or written representations made by him to clients with reference to any matter administered by the Internal Revenue Service

Due diligence does not require that the practitioner "audit" their client. However, it does require that a practitioner make reasonable inquiries when a client provides information that suggests possible participation in overseas transactions/accounts subject to FBAR requirements. A practitioner may rely on information provided by a client in good faith. However, they may not ignore implications learned from information provided or actually known. The practitioner is also required to advise a client of potential penalties likely to apply to a position taken, such as failing to abide by FBAR requirements. The practitioner must make reasonable inquiries if information appears incorrect, inconsistent with an important fact or factual assumption, or is incomplete.

Additional inquiries about the FBAR filing requirements may be resolved by reading "FAQs regarding Report of Foreign Bank and Financial Accounts (FBAR)," and other FBAR information available on the IRS web site at www.irs.gov. Specific questions and comments may be emailed to the following address: FBARquestions@irs.gov. Questions concerning your ethical obligations in this area may be addressed to the Office of Professional Responsibility at: opr @irs.gov.

Kevin E. Packman | **Holland** & Knight Partner, Private Wealth Services 701 Brickell Avenue, Suite 3000 | Miami FL 33131 Phone 305.349.2261 | Fax 305.679-6416 kevin.packman@hklaw.com | www.hklaw.com

FRAUD & NEGLIGENCE

Advising a Client With Secret Offshore Accounts—Current Filing and Reporting Problems

Author: By Scott D. Michel

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SCOTT D. MICHEL is a partner in the Washington, D.C., law firm of Caplin & Drysdale, Chartered, with a specialty in criminal tax cases. A past chair of the Committee on Civil and Criminal Tax Penalties of the ABA Tax Section, he has written and lectured frequently on criminal tax issues.

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A practitioner's legal and ethical responsibilities to the client and to the judicial system are tested when the client's past conduct collides with annual reporting and disclosure obligations for foreign bank accounts. Often the only acceptable approach is the explicit assertion of the privilege against self-incrimination, which may itself provide an incriminating lead to an inquisitive investigator.

EDITED BY ROBERT S. FINK, LL.M.

For a U.S. taxpayer, the act of opening a foreign bank account triggers multiple annual reporting and disclosure obligations. Many people who open such accounts do so without the benefit of competent advice and then wrongfully fail to make the proper disclosures to the IRS and the Treasury. As illustrated by the not atypical hypothetical described below, when such a client later consults a tax advisor, the practitioner must tread carefully in protecting the client's legal interest to the fullest extent possible while at the same time ensuring that the client—and the advisor as well—commit no new offenses.

BANKING IN PARADISE

In the spring of 1996, Richard Smith had a marvelous vacation on the tropical island of Azure. While he was there, he attended a free seminar on offshore banking and investing, where he heard about the many benefits of having an Azure bank account, including the island's strict bank secrecy laws. Smith opened an account at an Azure bank and deposited funds over the next three years. The bank invested his money and provided him with a “debit” card to use for “untraceable” cash advances and purchases. While Smith was careful to report all of his domestic income on his tax returns for 1996 and 1997, he did not disclose the existence of the Azure account or report the income earned in the account.

In January 1999, Smith received a routine civil audit notice for 1996 and 1997 from the IRS. Nervous about his Azure account, he consulted his lawyer. She took some comfort in the fact that Smith was not skimming cash out of his business, but she was concerned that the offshore account might surface during the audit. As she considered the agent's initial request for information, Smith sent her a draft copy of his 1998 return. She noted that i response to the standard question asking whether the taxpayer had any foreign accounts, Smith had falsely answered “no.”

Smith's lawyer knew that she could not advise him to file a false tax return. She also knew, however, that disclosing the foreign account and reporting offshore earnings on Smith's 1998 return might lead the Service to his false statements and underreporting of income on prior returns. She also was aware that Smith was exposed to criminal sanctions for failing to file annual Treasury Department forms concerning his foreign account. She pondered her options.

The annual reporting requirements for foreign bank accounts and the severe sanctions for noncompliance with those obligations create recurring problems for any tax practitioner who, like Smith's lawyer, encounters a client with a previously undisclosed foreign account. In addition to the client's issues, the practitioner faces the difficult question of what advice ethically can be given to a client who has failed in prior years to disclose a foreign financial account when the time comes to file the current tax return.

DISCLOSURE REQUIREMENTS

The tax and banking laws obligate U.S. taxpayers to disclose any foreign financial account under their control in a variety of ways. First, the Code requires U.S. citizens and residents to report their worldwide income. Thus, if a U.S. taxpayer has a bank or brokerage account in a foreign country and that account earns interest, dividends, or capital gains, that income, and a disclosure of its source, must appear on the Form 1040.

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A person who opens an account in a tax haven country with the intention not to report it to the IRS typically attempts to evade this requirement by using a nominee entity. Financial advisors in tax havens often promote "bearer share" corporations for this purpose. Such a corporation belongs to whomever physically possesses the stock certificates, so there is no official record of ownership. In Smith's case, for example, an Azure solicitor created the "RS Corporation" under Azure law, put himself and his office staff on the corporation's board of directors, opened the account in the corporation's name, and then gave Smith the stock certificates.

There is no question, however, that Smith is the "beneficial owner" of the account in the name of the RS Corporation. He is the sole signatory on the account. He presumably filled out a form at the bank identifying himself as the beneficial owner. The money in the account is his to use as he pleases. The debit card issued on the account is in his name. It is beyond dispute under U.S. tax law that the obligation to report income earned on a financial account attaches to the beneficial owner of the funds in the account, regardless of the name in which the account is held. [FN1] There is no question that Smith should have disclosed the account and reported its earnings on his prior returns.

U.S. taxpayers are also subject to additional requirements, derived from the Bank Secrecy Act of 1970 (BSA), to report their interest in or authority over any foreign financial accounts. When it enacted BSA, Congress was concerned that wealthy Americans with secret foreign bank accounts were able to evade income taxes and conceal assets, that foreign financial accounts were often linked to other serious criminal activity, and that U.S. law enforcement agencies encountered roadblocks when investigating such offenses because "wrongdoers cloak their activities in the shield of foreign financial secrecy." [FN2] Congress therefore directed the Treasury to adopt regulations requiring disclosure of foreign accounts. [FN3] Pursuant to this mandate, federal regulations require each person subject to U.S. jurisdiction to make a report on yearly tax returns of any "financial interest in, or signature or other authority over, a bank, securities or other financial account in a foreign country." [FN4] The regulations further require the disclosure of information relating to such accounts on a separate form issued by the Treasury.

The result of the BSA's directive is a dual disclosure requirement. First, since the promulgation of the regulations, Form 1040 has contained a question asking about foreign financial accounts. On the 1998 return, the question appears on Schedule B and reads as follows: "At any time during [the calendar year], did you have an interest in or a signature or other authority over a financial account in a foreign country, such as a bank account, securities account, or other financial account? See [the instructions] for exceptions and filing requirements for Form TD F 90-22.1." The form contains boxes labeled "yes" and "no" for the taxpayer's response. If the answer is "yes," the form requires the taxpayer to "enter the name of the foreign country."

The instructions accompanying Form 1040 make plain that, in general, a "yes" answer to the foreign bank account question is required if the taxpayer (1) at any time during the year had *an interest in* or *signatory* or *other authority over* a financial account in a foreign country, or (2) owns more than 50% of the stock in any corporation that owns one or more such accounts. There are exceptions to the disclosure requirement, such as for accounts valued at less than $10,000 during the entire year or accounts owned by a publicly traded or otherwise large corporation where the company has disclosed the account.

The second disclosure requirement, alluded to in the question on the Form 1040, is Treasury Department Form 90-22.1, "Report Of Foreign Bank And Financial Accounts" (known as an FBAR, for "foreign bank account report"). That form requires the disclosure of detailed information about the taxpayer's foreign accounts, including the filer's identity and social security number, and a list of all foreign accounts, with account numbers. The FBAR instructions and definitions describe what constitutes a "financial account," a "financial interest," or "signature or other authority," but in the typical case like Richard Smith's the obligation to file the FBAR is clear. Even if Smith's account is technically "owned" by the RS Corporation, his signature authority over the account by itself triggers the disclosure obligation, regardless of the nature of his financial interest, as does his financial interest, standing alone, without regard to the identity of the signatory.

If a taxpayer has a disclosable interest in a foreign account at any time during the tax year, the FBAR describing that

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account is due on June 30 of the following calendar year, and no extensions are possible. Form 90-22.1 is filed not with the IRS but with the Treasury's computing center in Detroit.

SANCTIONS FOR NONCOMPLIANCE

Both the willful failure to comply with the disclosure requirements for foreign financial accounts and the willful failure to report earnings on such accounts constitute serious criminal offenses and may also trigger severe civil penalties.

The most likely basis for a criminal prosecution against a taxpayer who provides a false answer to the foreign bank account question is Section 7206(1). That statute punishes any taxpayer who "[w]illfully makes and subscribes any return, statement, or other document, which contains or is verified by a written declaration that it is made under the penalties of perjury, and which he does not believe to the true and correct as to every material matter." A taxpayer who knowingly checks and foreign bank account box "no" when the correct answer is "yes" obviously would violate this provision. The Justice Department lists such conduct in its Criminal Tax Manual as a basis for a prosecution under Section 7206(1), and the government has prosecuted individuals in such cases. [FN5]

A taxpayer may not avoid these sanctions by failing to answer the foreign bank account question. A willful failure to answer "yes" or "no" could violate Section 7206(1) if the taxpayer signing such a return knew that the return was not "true and correct as to every material matter." [FN6] There is at least one reported case in which the government prosecuted a taxpayer under Section 7206(1) for failing to respond to the foreign bank account question. [FN7] Moreover, in other regulatory contexts, the government has obtained false-statement felony convictions against individuals who leave blank a request for information on a federal filing. In such cases, a willful nonresponse is considered a false statement. [FN8]

Other criminal tax sanctions could apply to the knowing noncompliance with the foreign bank account disclosure requirements. A taxpayer's omission from his return of taxable interest, dividends, or capital gains earned on a foreign account is a separate offense under Section 7206(1) or, if the government can prove a tax deficiency, tax evasion under Section 7201. If more than one individual is involved, the government can— and often does—bring tax-related conspiracy charges. [FN9]

In addition to criminal tax charges, the BSA imposes criminal penalties for the willful failure to file an FBAR. [FN10] Any such failure is a misdemeanor, and it is elevated to a felony if the person fails to file the form "while violating another law of the United States or as part of a pattern of illegal activity involving transactions of more than $100,000 in a 12 month period." [FN11] Thus, any knowing failure to file an FBAR that occurs in the context of tax, currency, or money-laundering offenses can be prosecuted as a separate felony. [FN12] The government has prosecuted individuals under the BSA for failing to file the FBAR. [FN13]

Whether the government brings criminal charges or not, a taxpayer who fails to disclose a foreign financial account or who omits income from such an account on a tax return will be subject to various civil penalties. The Treasury can impose a civil penalty for each willful failure to file an FBAR equal to the greater of the balance in the foreign account (not to exceed $100,000) or $25,000. [FN14] The IRS can invoke the full panoply of civil tax penalties that may apply when a taxpayer omits income from a return, including the negligence or substantial understatement penalties of 20% or the fraud penalty of 75%. [FN15]

ADVISING THE CLIENT ON CURRENT FILINGS

Before he consulted his lawyer, Richard Smith violated a number of federal statutes. He made false statements on his 1996 and 1997 tax returns by checking "no" in response to the foreign bank account question. He omitted interest, dividend, and capital gains earned on the Azure account from the taxable income reported on those returns. He failed twice to file the required FBAR.

There is little that Smith's lawyer can do about her client's prior conduct. Filing amended 1996 and 1997 returns or the

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delinquent FBARs after the initiation of an IRS audit for those years would constitute an admission of Smith's prior false statements and create evidence that the IRS could use against him in the audit and, more important, in a criminal investigation. [FN16] Smith and his lawyer can hope that the revenue agent will complete the audit without coming across information that would lead to discovery of the Azure account. If, however, the agent asks the right questions, Smith has only two lawful avenues open to him—either he can respond truthfully to the agent's inquiries, which would presumably result in providing information about or leads to the foreign account, or he can assert his Fifth Amendment rights and otherwise decline to cooperate with the audit. Either course may prompt the agent to refer the case to the Criminal Investigation Division.

Smith's lawyer faces an equally daunting challenge in how to advise Smith with respect to his current filing obligations. Smith must file a timely, truthful and complete 1998 tax return, and he is required to file a current FBAR. His lawyer cannot ethically advise him to disregard those legal obligations. Nevertheless, providing the government with the information required by these forms could be criminally incriminating for Smith. The tensions among Smith's current filing requirements relating to the foreign account, his self-interest in avoiding disclosure of past violations, and his lawyer's professional responsibility, create a delicate and troublesome set of tactical issues for Smith and his lawyer.

The Form 1040

If Smith makes a full disclosure on his Form 1040, he will be providing the IRS with a clear lead to his Azure account. The revenue agent conducting the audit is likely to ask for a copy of the 1998 return, and the disclosure of a bank account in a tax haven will surely prompt further inquiry. There is no question that the government could use any disclosures made on the return against Smith. [FN17] With the extensive powers of U.S. law enforcement authorities to obtain foreign evidence, even in tax haven jurisdictions, the details of the account may well be discovered. [FN18] To the extent consistent with her ethical responsibilities, Smith's lawyer ought not recommend a full disclosure on the return.

Yet, Smith's lawyer cannot advise him to check “no” in response to the foreign bank account question, or to leave the answer blank. [FN19] If she did that, she might be entering into a conspiracy with Smith to violate Section 7206(1), and she might have aided and abetted his conduct by doing so. Not only would this compound Smith's legal problems, but his lawyer might be subject to potential investigation, criminal prosecution, incarceration, and disbarment.

Thus, Smith must answer the question, and his counsel must advise him on an answer that does the least amount of damage without having him engage in additional criminal conduct. After exhausting all available extensions (perhaps Smith's audit will have ended by October), the only acceptable vehicle for such an approach is Smith's Fifth Amendment privilege against self-incrimination.

Smith may decline to answer the foreign bank account question by claiming his Fifth Amendment privilege. An individual taxpayer may assert the privilege against self-incrimination to avoid making particular disclosures on the tax return. [FN20] To be valid, a claim of privilege must be explicit on the face of the return and in response to specific questions or line items when the requested information would provide testimonial self-incrimination. [FN21] Thus, Smith's lawyer could advise him to place an asterisk next to the foreign bank account question, footnote his answer with an explicit claim of privilege, and then leave the “yes” and “no” boxes blank.

Obviously, Smith's assertion of his Fifth Amendment privilege in response to the foreign bank account question will be a “red flag” if the 1998 tax return is audited or surfaces during the ongoing examination. But Smith's counsel can offer no other ethical alternative to having her client admit to his control over the Azure account, which would be more than just a “red flat”—it would constitute an admission that could be used against Smith in a criminal prosecution. If the examining agent asks for the return, it is far better for Smith that it contains no information that could prejudice him in the event such an inquiry is (or has already) begun.

Smith's right to assert his Fifth Amendment privilege to avoid disclosure of his foreign bank account is subject to a potentially important limitation. Most courts considering the issue have held that while a taxpayer can assert the Fifth

Amendment privilege in response to a line item, such as his occupation or the source of income, the taxpayer may not use the privilege to withhold the *amount* of his taxable income. [FN22] Thus, while Smith may decline on Fifth Amendment grounds to disclose his authority over or interest in his Azure account, most courts would hold that he must report the amount of income earned on the account on his 1998 tax return. He can rely on his privilege against self-incrimination as a basis for declining to identify the source of that income. [FN23]

The FBAR

As discussed above, the Form 1040 is not the only annual reporting requirement relevant to Smith's Azure account. He and his counsel still must deal with his obligation to file Form 90-22.1.

The FBAR presents different, yet just as problematic, issues for Smith's counsel. It would be extremely risky to have Smith fill out a truthful and complete form. Although the FBAR goes to a Treasury Department computing center in Detroit rather than the IRS, the disclosure of Smith's Azure account on the form would give the government a clear road map to details about the account, including the account number and evidence of the account balance. These leads would permit an investigator or prosecutor to seek records relating to the Azure account, and the form itself could be used as evidence against Smith. Because Smith is a potential target of a criminal investigation, his lawyer certainly should not advise him to supply the information called for on the FBAR. Even if a criminal investigation were not yet pending, there would be too great a risk that the FBAR would be uncovered.

Since Smith would be ill advised to file a complete, accurate, and truthful FBAR, his lawyer must consider other options. She may consider that Smith's Fifth Amendment privilege can be invoked to justify declining to file the form altogether, or that Smith can assert the privilege on the FBAR to prevent the government from obtaining evidence that can be used against him.

One could argue that Smith's Fifth Amendment privilege should excuse him from the filing requirement because the mere act of filing the FBAR could constitute testimonial self-incrimination. Only those people with the requisite authority or interest in a foreign bank account must file an FBAR. Thus, the mere act of filing constitutes what the courts call a “testimonial act”—that is, a nonverbal admission that the person who filed the form is in fact required to do so because he has a foreign financial account. The act of filing the form, without regard to its contents, would provide a lead to a prosecutor or investigator about Smith's connection with a foreign account. Depending on what other information the government might have obtained, Smith's filing of an FBAR by itself could well be an important “link in the chain” of evidence necessary to charge him with a crime.

Yet, two courts of appeals have rejected the Fifth Amendment privilege as a basis for the nonfiling of Bank Secrecy Act forms. In *Sturman*, 951 F2d 1466, 34 Fed Rules Evid Serv 704, 1991 WL 213802 *Sturman,, cert. den.*, the government charged the principal defendant with, among other offenses, three felony counts of failing to file the FBAR as to otherwise undisclosed foreign accounts. In *Dichne*, 612 F2d 632, 59 ALR Fed 424 *Dichne,, cert. den.*, the defendant failed to file the BSA-required form reporting currency that he carried across the U.S. border. [FN24]

Both defendants argued that the applicable filing requirements violated their Fifth Amendment privilege because the information provided on the forms would incriminate them with respect to other crimes. They asserted that the BSA filing obligations were unconstitutional, relying on Supreme Court cases that struck down, on Fifth Amendment grounds, selected reporting obligations that compelled a targeted group to acknowledge its participation in a criminal offense. The most prominent such case in the tax area is *Marchetti*, 390 US 39, 88 S Ct 697, 19 L Ed 2d 889, 43 Ohio Ops 2d 215, 68-1 USTC ¶15800, 21 AFTR 2d 539 *Marchetti*, in which the Supreme Court invalidated federal requirements that gamblers disclose their unlawful wagering activity by posting a stamp at their principal place of business, filing additional forms, and reporting their wagering income. At the time, gambling was unlawful in nearly every state, and the Court found that “every portion of the [reporting and payment] requirements had the direct and unmistakable consequence of incriminating” those required to comply with them. [FN25] As in *Marchetti*, the defendants in *Sturman* and *Dichne* ar-

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gued that, merely by filing BSA forms, they would be providing evidence that might incriminate them in various crimes.

Both the *Sturman* and *Dichne* courts rejected the defendants' arguments because, In contrast to *Marchetti*, the conduct disclosed by filing the required form was not itself illegal. The Sixth Circuit in *Sturman* recognized that the FBAR filing requirement “applies to all persons making foreign deposits, most of whom do so with legally obtained funds.” The court concluded that the required disclosures did not subject the defendants to a “real danger of self-incrimination,” and therefore held that the FBAR did not meet the *Marchetti* test because not “every element” of the reporting requirement would have incriminated the defendant. Similarly, in *Dichne* the Second Circuit observed that there is nothing unlawful in transporting currency in excess of the reporting requirement. Other courts have reached similar results. [FN26]

While the analysis in *Sturman* and *Dichne* is questionable in some respects, [FN27] the courts have plainly decided to tolerate some potential for self-incrimination rather than sanction a system where individuals may simply ignore the BSA filing requirements. In light of these authorities, Smith's lawyer would be wise to find a mechanism to try to protect her client's interest other than simply failing to file the FBAR.

While the cases are clear that one who fails to file an FBAR risks potentially serious penalties, they do not foreclose the option of claiming the Fifth Amendment on the FBAR itself. As noted above, where a particular disclosure on a federal tax return might incriminate a taxpayer, it is permissible for the taxpayer to decline to provide the information and to assert the Fifth Amendment privilege on the face of the return. The FBAR should be no different. Thus, while Smith is required to file an FBAR, he should not have to provide details on the form that might lead to the discovery of, or provide evidence of, other criminal offenses. This raises the question of how Smith could validly assert his privilege against self-incrimination on the face of the FBAR.

The FBAR asks for specific information relating to the taxpayer and his account, including name, address, social security number, and the name of his bank, the bank account number, and an approximate balance in the account. One approach would be for Smith to file a blank FBAR accompanied by a statement that identifies him, provides his social security number, and asserts his Fifth Amendment privilege as to whether he is even required to file the form. Another approach would be analogous to the one used on Smith's 1998 tax return, providing his identifying information but asserting his privilege in response to particular questions about his foreign accounts.

Either form clearly would comply with the Filing requirement by identifying Smith and providing his social security number. An FBAR that asserts Smith's privilege as to the underlying obligation to file provides the broadest possible protection. Claiming the privilege as to the obligation to file the FBAR would be no different than refusing on Fifth Amendment grounds to respond to an inquiry from an auditor or investigator as to whether Smith had a foreign account. Moreover, such a “Fifth Amendment” FBAR could not be used as evidence against Smith in a subsequent prosecution—a court could not properly allow the government to introduce the form against Smith in a criminal case as evidence of his control over a foreign account when he explicitly claimed his privilege against self-incrimination as to that very fact. [FN28]

For Smith's lawyer, advising her client to file a Fifth Amendment FBAR in this manner is more sensible than advising him not to file the form on Fifth Amendment grounds. While she may find it tempting to relitigate the Fifth Amendment issue, the dispute would arise in the context of a prosecution of her client in which she would likely be a witness—on her client's claim of reliance on professional advise—or a codefendant. Moreover, her advise as to the FBAR is part of the overall strategy of dealing with current filing issues; Smith still must file a tax return, and he cannot simply fail to answer the foreign bank account question. He has no choice but to assert his Fifth Amendment privilege on his tax return as to his control over a foreign account and as to the source of the income earned on the account. The tax return will provide just as much of a lead (and probably one more likely be discovered) as the filing of a Fifth Amendment FBAR. Because Smith eventually must file a tax return, his lawyer clearly would be taking an unnecessary risk for herself and her client by instructing him to ignore the filing requirement for the FBAR. [FN29]

There is no question that even a Fifth Amendment FBAR discloses information to the government that it may not otherwise have obtained. It clearly provides an incriminating lead by acknowledging that Smith has enough of a relationship

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with a foreign account that he felt compelled to file the FBAR, even if the form itself cannot be used as evidence against him. Although the Fifth Amendment assertion on a tax return or the FBAR may do nothing more than confirm the suspicion of an IRS auditor or criminal investigator that Smith has an offshore account, in certain cases that might be significant. It may seem unfair to require Smith to file the form in this context, but the case law compels the conclusion that he must do so. Under existing precedent, however, no prosecutor or court could legitimately quarrel with a decision to file the FBAR with the broadest possible assertion of Smith's Fifth Amendment privilege.

CONCLUSION

Because of annual disclosure requirements, taxpayers engaged in ongoing concealment of foreign accounts are forced to “return to the scene of the crime” every year. This provokes a tricky set of issues for tax practitioners advising these clients, especially those already under IRS scrutiny. In such cases, lawyers must reconcile their professional responsibility to protect the client's interest with their legal and ethical obligations not to counsel, condone, or join in an unlawful cover up. Although there are no ideal answers, through the judicious and careful use of the taxpayer's Fifth Amendment privilege, the practitioner can recommend a course of action that complies with the tax and BSA reporting requirements, while disclosing the least amount of information that could damage the client.

Practice Notes

A client comes to you with a problem: the IRS has started an audit, and the client has secret foreign bank accounts that he has never reported on his tax returns. Now it's time to file his current tax return, and if the client makes a full disclosure on that return, he will provide evidence of his prior misconduct. How can the client use the Fifth Amendment privilege to protect himself as much as legally possible? What ethical advise can the practitioner provide?

[FN1]. See, e.g., *Chu*, TC Memo 1996-549, RIA TC Memo ¶96549; *Hang*, 95 TC 74, Tax Ct Rep (CCH) 46725, Tax Ct Rep Dec (P-H) 95.6, 1990 WL 98703; *Serianni*, 80 TC 1090, Tax Ct Rep (CCH) 40162, 1983 WL 14842, *aff'd* 765 F2d 1051, 54 USLW 2079, 85-2 USTC ¶9551, 56 AFTR 2d 85-5559; *Hook*, 58 TC 267, 1972 WL 2439.

[FN2]. See H. Rep't No. 91-975, 91st Cong., 2d Sess., reprinted in U.S. Code Cong. & Ad. News 4394, 4397-8 (1970).

[FN3]. 31 U.S.C. section 5314.

[FN4]. 31 C.F.R. section 103.24.

[FN5]. U.S. Department of Justice, Criminal Tax Manual, §12.08[6][g]. See, e.g., *Mueller*, 74 F3d 1152, 96-1 USTC ¶50190, 77 AFTR 2d 96-893, 1996 WL 34481; *Harvey*, 869 F2d 1439, 89-1 USTC ¶9266, 63 AFTR 2d 89-1212, 1989 WL 28324; *Franks*, 723 F2d 1482, 84-1 USTC ¶9118, 53 AFTR 2d 84-595, *cert. den*. See also *Hajecate*, 683 F2d 894, 83-1 USTC ¶9192, 51 AFTR 2d 83-1282 *en banc,, cert. den*. (dismissing charges under 18 U.S.C. section 1001 for false answer to FBAR question under now defunct “exculpatory no” doctrine but holding that government was free to prosecute under Section 7206(1)).

[FN6]. The failure to answer the foreign bank account question would also be a violation of Section 7203, which makes it a misdemeanor willfully to fail to supply any information required under the Code. The government usually prosecutes such an offense as a felony, however, where the individual involved engaged in other allegedly fraudulent activity. See *Spies*, 317 US 492, 63 S Ct 364, 87 L Ed 418, 43-1 USTC ¶9243, 30 AFTR 378.

[FN7]. In *Polidori*, TC Memo 1996-514, RIA TC Memo ¶96514, the taxpayer “left the blocks corresponding to” the foreign bank inquiry blank. The taxpayer eventually pled guilty to a violation of Section 7206 (1), and the court upheld the

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civil fraud penalty because the taxpayer had concealed his interest in the foreign accounts. See also Franks, *supra* note 5 (disclosing some but not all foreign accounts is a violation of Section 7206(1)).

[FN8]. See *Mattox*, 689 F2d 531 (failing to answer a question on the form for federal workers' compensation benefits equivalent to making a false statement); *Irwin*, 654 F2d 671, *cert. den*. (similar holding); *McCarthy*, 422 F2d 160, 73 BNA LRRM 2607, 62 CCH LC ¶10692, *cert. dism*. (similar holding).

[FN9]. 18 U.S.C. section 371.

[FN10]. 31 U.S.C. section 5322.

[FN11]. *Id*., section 5322(b).

[FN12]. The fact that Form 90-22.1 is referred to in the foreign bank account question on Schedule B of Form 1040 is sufficient evidence to permit a jury to infer willfulness. See *Sturman*, 951 F2d 1466, 34 Fed Rules Evid Serv 704, 1991 WL 213802, *cert. den*.

[FN13]. See *Clines*, 958 F2d 578, 1992 WL 35344, *cert. den*.; Sturman, *supra* note 12.

[FN14]. 31 C.F.R. section 103.47(g)(2).

[FN15]. Sections 6662, 6663.

[FN16]. If the IRS had not yet contacted Smith, his counsel may have more comfortably advised him to disclose the foreign bank account on his 1998 return because he might have been eligible for the Service's voluntary disclosure policy. Under that policy, the IRS usually does not recommend prosection of a taxpayer who has filed false returns in the past, or failed to file returns, and who comes forward, prior to the initiation of an IRS inquiry and otherwise without promoting, to correct his tax affairs. The policy applies only to taxpayers with legal source income, and it requires making reasonable efforts to pay the outstanding liability and continuing cooperation by the taxpayer in any subsequent inquiry. The policy is not legally binding on the IRS, and it does not cover FBARs. See Internal Revenue Manual section 9781, Special Agent's Handbook section 342.142.

[FN17]. See, e.g., *Garner*, 424 US 648, 96 S Ct 1778, 47 L Ed 2d 370, 76-1 USTC ¶9301, 76-1 USTC ¶16218, 37 AFTR 2d 76-1042-A; *Hornstein*, 176 F2d 217, 49-2 USTC ¶9326, 38 AFTR 292; *Dinnell*, 428 F Supp 205, 77-2 USTC ¶9490, 40 AFTR 2d 77-5764, *aff'd without opn*. 568 F2d 779.

[FN18]. Notwithstanding Azure's bank secrecy laws, the U.S. government likely could obtain access to the records relating to Smith's account. The government has been increasingly active in negotiating treaties or information exchange agreements that provide for the disclosure of information for use in tax cases notwithstanding local bank secrecy. See, e.g., Income Tax Treaty Between Switzerland and the United States, Art. XXVI. If the bank at which the account is held has a branch in the U.S., moreover, a grant jury subpoena can reach the records. See, e.g., *Bank of Nova Scotia*, 691 F2d 1384, *cert. den*. (upholding enforcement of subpoena), contempt sanction upheld 740 F2d 817, 84-2 USTC ¶9802, *cert. den*. The government also can compel Smith to consent to the disclosure of the bank records. See *Doe*, 487 US 201, 108 S Ct 2341, 101 L Ed 2d 184, 56 USLW 4708, 88-2 USTC ¶9545, 25 Fed Rules Evid Serv 632, 62 AFTR 2d 88-5744, 1988 WL 61708; Criminal Tax Manual, *supra* note 5, §41.06.

[FN19]. It also is not an option for a taxpayer to avoid filing Schedule B, with its foreign bank account question, by having no reportable interest or dividends. The tax return instructions make plain that a taxpayer must file a Schedule B even

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if there is no interest or dividend income but the taxpayer nonetheless would be required to answer "yes" to the foreign bank account question. Moreover, Smith cannot avoid criminal exposure by giving a partial answer, i.e., answering "yes" and simply not putting down the country, thereby avoiding the disclosure of an account in a tax haven. Such an approach would amount to intentionally withholding required information and would be just as much an offense as no answer at all. It also could prompt further inquiry.

[FN20]. See *Verkuilen*, 690 F2d 648, 82-2 USTC ¶9618, 11 Fed Rules Evid Serv 1417, 50 AFTR 2d 82-5937; *Neff*, 615 F2d 1235, 80-1 USTC ¶9397, 6 Fed Rules Evid Serv 169, 45 AFTR 2d 80-1217, *cert. den*. The privilege will not justify the failure to file a tax return, or any false, incomplete, or misleading statements on the return. See, e.g., *Sullivan*, 274 US 259, 47 S Ct 607, 71 L Ed 1037, 1 USTC ¶236, 6 AFTR 6753, 51 ALR 1020; *Raborn*, 575 F2d 688, 78-1 USTC ¶9262, 41 AFTR 2d 78-1077; *Milder*, 459 F2d 801, 72-1 USTC ¶9407, 29 AFTR 2d 72-1084, *cert. den*. See generally Timbie and Michel, "Strategies for Filing a Tax Return While Under a Criminal Tax Investigation," 2 J. Asset Protection 34 (Sep/Oct 1996).

[FN21]. See Garner, *supra* note 17; *Jordan*, 508 F2d 750, 75-1 USTC ¶9154, 35 AFTR 2d 75-524, *cert den*.

[FN22]. Compare *Goetz*, 746 F2d 705, 84-2 USTC ¶9947, 55 AFTR 2d 85-390, *Brown*, 600 F2d 248, 79-1 USTC ¶9322, 43 AFTR 2d 79-1004, *cert. den*., and *Johnson*, 577 F2d 1304, 78-2 USTC ¶9642, 42 AFTR 2d 78-5624 (Fifth Amendment privilege not available as to amount of income), with Verkuilen, *supra* note 20, and *Barnes*, 604 F2d 121, *cert. den*. (suggesting that privilege may be asserted as to amount).

[FN23]. Another option open to a taxpayer under scrutiny as to an issue that flows into a current filing year is to avoid both an incriminating admission and an explicit assertion of the Fifth Amendment privilege by filing an admittedly incomplete return. Such a return would identify the items that are incomplete and explain that the taxpayer is currently under investigation and cannot provide the information without damaging his adversarial position.

A lawyer's good faith advice that a client file such a return probably could not be the basis of a criminal prosecution, but since neither the courts nor the IRS have ever approved this strategy, it carries some risk that the advice may be considered unethical. (It also may not work—a broad disclaimer may draw more scrutiny than a narrow assertion of the Fifth Amendment as to a specific item.) Moreover, while the strategy might be useful in finessing the reporting of income earned on a foreign account, it does not solve the problem presented by the foreign bank account question, which still must be answered. If the taxpayer declines to check the foreign bank account box in the context of such a disclaimer, that would provide just as much of a lead as his explicit assertion of the Fifth Amendment privilege.

[FN24]. At that time, anyone transporting more than $5,000 in currency into or out of the U.S. was required to file an appropriate form. This provision was amended in 1986 to increase the amount to $10,000. P.L. No. 99-570, section 1358(c), codified at 31 U.S.C. section 5316(a)(1).

[FN25]. See also *Grosso*, 390 US 62, 88 S Ct 709, 19 L Ed 2d 906, 43 Ohio Ops 2d 226, 68-1 USTC ¶15801, 21 AFTR 2d 554, the companion case to *Marchetti*, 390 US 39, 88 S Ct 697, 19 L Ed 2d 889, 43 Ohio Ops 2d 215, 68-1 USTC ¶15800, 21 AFTR 2d 539. The Marchetti reporting requirements violated the Fifth Amendment because "the very filing itself necessarily admitted illegal gambling activity." *Selective Service System v. Minnesota Public Interest Research Group*, 468 US 841, 104 S Ct 3348, 82 L Ed 2d 632, 18 Ed Law Rep 115.

[FN26]. See, e.g., *Mickens*, 926 F2d 1323, 32 Fed Rules Evid Serv 614, 1991 WL 24307, *cert. den*. (currency reporting requirements upheld because information disclosed on reporting form did not necessarily reflect criminal activity); *Kimball*, 711 F Supp 1031, 1989 WL 48048 (similar holding); *Scanio*, 705 F Supp 768, 1988 WL 147642 (similar holding); *San Juan*, 405 F Supp 686, 76-1 USTC ¶9183, 37 AFTR 2d 76-810, *rev'd on other grounds* 545 F2d 314 (sustaining con-

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viction for failing to file BSA-required currency reports over Fifth Amendment claim in part because of traditional tolerance of broad government authority to regulate trans-border conduct).

[FN27]. The Sixth Circuit found, in part, that the FBAR does not carry a risk of self-incrimination because it does not disclose the source of the funds in the account. *Sturman*, 951 F2d 1466, 34 Fed Rules Evid Serv 704, 1991 WL 213802, *cert. den*. Yet, even if a taxpayer has legal source funds in a foreign account, his mere filing of an FBAR could incriminate him if he has falsely answered the foreign bank account question on a tax return or failed to report income from a foreign account.

[FN28]. While such a case would present an issue of first impression, the courts generally prohibit the government's use of a defendant's prior assertion of his Fifth Amendment privilege as evidence of guilt. See *Grunewald*, 353 US 391, 77 S Ct 963, 1 L Ed 2d 931, 57-1 USTC ¶9693, 51 AFTR 20, 62 ALR2d 1344; *Monteleone*, 804 F2d 1004, 22 Fed Rules Evid Serv 17, *cert. den.; Vandetti*, 623 F2d 1144, 6 Fed Rules Evid Serv 311; *Long*, 153 F Supp 528, 57-2 USTC ¶9860, 52 AFTR 222, *rev'd on other grounds* 257 F2d 340, 58-2 USTC ¶9621, 1 AFTR 2d 2011. If the defendant takes the stand, some courts have allowed the government to impeach him by using prior assertions of the privilege, but even this is subject to constitutional limitations. See Grunewald, *supra; Savory v. Lane*, 832 F2d 1011.

[FN29]. Similar to the "admittedly incomplete return" (see note 23, *supra*). Smith's lawyer might consider some communication with the Treasury Department short of filing a Fifth Amendment FBAR that might resolve her dilemma. Plainly, however, such a communication could not identify Smith as her client, because that would provide just as much of a testimonial admission as if Smith were to file the form. Thus, such an approach would necessity entail describing her advice to an unspecified client not to file the FBAR. Even if adopted in good faith, such a strategy carries serious risks for Smith's counsel, because she would be admitting that she counseled a client to disregard a statutory filing requirement.

Moreover, the courts have rejected the Fifth Amendment privilege in an analogous context as a basis for a lawyer's refusal to identify a client on required forms. *Sindel*, 53 F3d 874, 63 USLW 2719, 95-1 USTC ¶50237, 75 AFTR 2d 95-1894, 1995 WL 244536; *Blackman*, 72 F3d 1418, 64 USLW 2449, 96 CDOS 18, 96 Daily Journal DAR 20, 96-1 USTC ¶50018, 43 Fed Rules Evid Serv 693, 77 AFTR 2d 96-313, 1995 WL 764254, *cert. den*. The government has imposed serious civil penalties in at least one case on a lawyer who failed to disclose client-identifying information on a required form. *Lefcourt*, 125 F3d 79, 97-2 USTC ¶50648, 80 AFTR 2d 97-6523, 152 ALR Fed 741, 1997 WL 560050, *cert. den*.

JOURNAL OF ACCOUNTANCY

FBAR Resources

UPDATED AUGUST 7, 2009

TD F 90-22.1, *Report of Foreign Bank and Financial Accounts* (FBAR), must be filed by U.S. persons having a financial interest in or signature authority or other authority over any financial account in a foreign country if the aggregate value of these accounts exceeds $10,000 at any time during the calendar year.

June 30 is the deadline for filing the current year FBAR.

The following is a collection of *JofA* news, analysis and feature articles and AICPA and IRS resources dealing with the newly revised FBAR.

NEWS

IRS Extends FBAR Filing Date for 2008 Filings

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Aug. 7, 2009

The IRS announced Friday in Notice 2009-62 that it is extending for certain taxpayers the due date for filing calendar year 2008 Form TD F 90-22.1, *Report of Foreign Bank and Financial Accounts* (FBAR). Because the Treasury Department is still working out various FBAR filing issues, it has decided to give certain taxpayers until June 30, 2010, to file FBARs for 2008 and earlier calendar years.

IRS Releases Streamlined Offshore Voluntary Disclosure Form

July 31, 2009

On July 29, the IRS posted to its Web site a three-page “optional format” short form for taxpayers to use when disclosing applying for the Voluntary Disclosure Program.

New Voluntary Compliance FAQs

June 25, 2009

On June 24, the IRS released new voluntary compliance FAQs, including instructions for taxpayers who only recently learned of their FBAR filing obligation and guidance on delinquent information returns.

Reminder: Foreign Bank Account Report (FBAR) Forms Must Be Received by the IRS by June 30

June 6, 2009

FBAR forms must be received (not just mailed) by June 30; however, the IRS has let non-U.S. taxpayers off the hook for now by reverting to the old definition of “U.S. person.”

FBAR Penalties Reduced for Six Months

April 22, 2009

The IRS created a framework for voluntary disclosure requests containing offshore issues, such as previously undisclosed foreign financial accounts and entities. The policy will remain in place for six months until Sept. 23, 2009.

ARTICLES

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

June 10, 2009

The revised version of the FBAR form surprised many practitioners. This article discusses the new reporting requirements and new traps for the uninitiated.

FBAR Voluntary Disclosure Questions Answered

June 11, 2009

The IRS has answered 51 “frequently asked questions” (FAQs) about its voluntary disclosure and settlement option for previously unreported offshore financial accounts and entities and income from them. The six-month window for making disclosures under the program ends Sept. 23.

RESOURCES

AICPA-ABA Teleconference on Aug. 20 on FBAR Issues

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Aug. 10, 2009

The AICPA's Tax Section and PFP Section are cosponsoring with the ABA Section of International Law a 90-minute teleconference on Aug. 20 at 11 a.m. on FBAR reporting and the IRS Offshore Income Voluntary Disclosure Program.

AICPA/ABA Teleconference on FBAR Issues

June 25, 2009

On Friday, June 12, the AICPA Tax Section and PFP Section cosponsored with the ABA a teleconference on FBAR reporting. The teleconference featured a panel of IRS FBAR experts. Listen to the audio here (95 minutes).

Chart of Information Needed From Clients

June 24, 2009

A handy document for gathering from clients the information needed to file FBAR, produced by the AICPA's FBAR Task Force. (Opens in Microsoft Word.)

FBAR Reporting Requirements - Issues to Consider

June 24, 2009

This report from Eisner LLP outlines FBAR reporting requirements. (Opens as a PDF.)

IRS Voluntary Compliance Questions

June 8, 2009

The information below includes questions that IRS Criminal Investigation special agents have asked some taxpayers participating in the IRS Offshore Voluntary Compliance program. Practitioners might want to document the facts as fully as possible in a detailed summary when submitting under the program.

GUIDANCE

FBAR Procedural

Announcement 2009-51, temporarily reverting to old definition of “United States person”
New TD F 90-22.1 FBAR and instructions
IRS reminder of June 30 FBAR deadlines
IRS information on FBAR reporting
FBAR FAQs
Publication 4261, Do You Have a Foreign Financial Account?
IRS's Beth Elfrey discusses FBAR changes
IRS's Beth Elfrey discusses new FBAR
IRS OPR information on professional responsibility and FBAR
IRS headliner on FBAR reporting by persons with only signature authority
IRS Appeals Coordinated issue information
FBAR definition of “in and doing business in” the United States
FBAR workbook and penalty chart
IRS memo on FBAR job aid and counsel review of penalty cases
Internal Revenue Manual sections on FBAR law and penalties
Internal Revenue Manual FBAR examination procedures

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BSA Compliance Examiners memo on money transmitter FBAR requirements
IRS FBAR requirements webpage

Voluntary Compliance Initiative

Rev. Proc. 2003-11 on Offshore Voluntary Compliance Initiative

Other Procedural

Bank Secrecy Act information
Bank Secrecy Act requirements
IRS Criminal Investigation 2009 business plan
The life and times of a Currency Transaction Report
Civil penalties under Title 31
Currency reporting and money laundering statistics

Voluntary disclosure

IRS voluntary disclosure main webpage
FAQs on voluntary disclosure (updated June 24, 2009)
IRS memo authorizing application of penalty framework to voluntary disclosure requests
IRS memo on routing voluntary disclosure requests
Internal Revenue Manual sections on voluntary disclosure
IRS voluntary disclosure contact information
Offshore voluntary disclosures form - optional format

Offshore income

Commissioner Shulman's statement on offshore income
IRS memo on proper development of offshore examination cases
Income from abroad is taxable

[NOTE]

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Part III — Administrative, Procedural, and Miscellaneous

FBAR Filing Requirements — Extended Filing Date for U.S. Persons Having Signature Authority Over, But No Financial Interest In, a Foreign Financial Account, and for U.S. Persons with Financial Interest In, or Signature Authority Over, Foreign Commingled Funds: Request for Public Comments on FBAR Filing Requirements

Notice 2009-62

I. Background and Purpose

The Report of Foreign Bank and Financial Accounts, Form TD F 90-22.1 (hereinafter referred to as "FBAR"), provides necessary information for certain governmental agencies. Information on the FBAR may be used in criminal, tax, or reg-

ulatory investigations or proceedings, or in the conduct of intelligence or counterintelligence activities, including analysis, to protect against international terrorism. This governmental need for information is balanced with the administrative concerns presented by the filing of the information by U.S. persons.

In October 2008, the IRS revised the FBAR and the accompanying instructions. On June 5, 2009, the IRS issued Announcement 2009-51, 2009-25 I.R.B. 1105, which stated that the IRS is temporarily suspending the filing requirement of the FBAR for those persons who are not U.S. citizens, residents, or domestic entities. On May 6, 2009 and June 24, 2009, the IRS posted questions and answers (Q&As-9 and -43, respectively) on its public website (www.irs.gov) that provide relief to certain persons who only recently learned of their obligation to file an FBAR by setting forth conditions and procedures for filing Form TD F 90-22.1 by September 23, 2009. More information concerning this relief is available at http://www.irs.gov/newsroom/article/0,,id=210027,00.html. This Notice provides additional administrative relief for (i) persons with no financial interest in a foreign financial account but with signature or other authority over the foreign financial account (hereinafter referred to as "signature authority"), and (ii) persons with a financial interest in, or signature authority over, a foreign financial account in which the assets are held in a commingled fund (hereinafter referred to as "foreign commingled funds"). The Department of the Treasury intends to issue regulations clarifying the FBAR filing requirements pertaining to those persons with respect to these foreign financial accounts, and solicits comments related to these FBAR filing requirements in this Notice.

II. Extended Filing Date for Specified Persons

A. Current FBAR Instructions

The current instructions to the FBAR provide, with certain exceptions, that U.S. persons that have signature authority over, but no financial interest in, a foreign financial account are required to file an FBAR. These persons must report the account on an FBAR even if the foreign financial account is reported on an FBAR filed by the owner of the account (or other person that has a financial interest in the account).

The current instructions to the FBAR also provide that a foreign financial account that must be reported on an FBAR includes any bank, securities, securities derivatives, or other financial instruments account. The FBAR instructions further provide that those accounts "generally also encompass any accounts in which the assets are held in a commingled fund and the account owner holds an equity interest in the fund (including mutual funds)."

The current instructions to the FBAR also provide that Form TD F 90-22.1 with respect to a given calendar year must be filed with the Department of the Treasury on or before June 30 of the succeeding year. Thus, except as provided in the prior relief granted by the IRS on its public website and the relief granted in this Notice, FBARs with respect to the 2008 calendar year should have been filed on or before June 30, 2009.

B. Extended Date for Filing an FBAR

In light of the additional time needed for the Department of the Treasury to address issues pertaining to FBAR filing requirements and the need to provide administrative relief for (i) persons with signature authority over, but no financial interest in, a foreign financial account, and (ii) persons with a financial interest in, or signature authority over, a foreign commingled fund, this Notice provides that those persons have until June 30, 2010, to file an FBAR for the 2008 and earlier calendar years with respect to these foreign financial accounts. Thus, eligible persons that avail themselves of the administrative relief provided in this Notice may need to file FBARs for the 2008, 2009 and earlier calendar years on or before June 30, 2010, to the extent provided in future guidance.

The FBAR filing extension provided by this Notice applies to FBARs with respect to 2008 and earlier calendar years. For (i) persons with signature authority over, but no financial interest in, a foreign financial account, and (ii) persons with a financial interest in, or signature authority over, a foreign commingled fund, the FBAR filing extension provided

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in this Notice supplements the filing extension to September 23, 2009, previously provided by the IRS on its public website.

III. Request for Public Comments

The Department of the Treasury is interested in receiving comments on the following issues affecting a person's FBAR filing obligation.

The Department of the Treasury requests comments regarding when a person with signature authority over, but no financial interest in, a foreign financial account should be relieved of filing an FBAR for the account. For example, comments are requested regarding whether relief from filing would be appropriate if a person with a financial interest in the account has filed an FBAR.

The Department of the Treasury requests comments discussing in what circumstances the exception from FBAR filing currently available for officers and employees of banks and certain publicly-traded domestic companies might be expanded to apply to all officers and employees with only signature authority over, and no financial interest in, an employer's foreign financial account, including circumstances in which an individual has been advised that an FBAR has been filed with respect to a foreign financial account for which that person has signature authority. The Department of the Treasury also requests comments discussing how the bank and publicly-traded company exception (including the requirement of notification that an FBAR was filed by a U.S. person with a financial interest in the account) might apply to officers and employees with only signature authority over accounts owned by clients of their employer.

The Department of the Treasury requests comments concerning when an interest in a foreign entity (e.g., a corporation, partnership, trust, or estate) should be subject to FBAR reporting. For example, comments are requested regarding the possibility of applying the principles of sections 1297 and 1298(b) of the Internal Revenue Code to determine when an interest in a foreign entity should be subject to FBAR reporting. Comments are also requested regarding whether the passive asset and passive income thresholds of 50 percent and 75 percent, respectively, are appropriate and whether the tests should apply conjunctively.

The Department of the Treasury also requests comments on whether a U.S. person should be relieved from an FBAR filing requirement with respect to a foreign commingled fund in other circumstances, such as when filing would be duplicative of other reporting.

Interested persons should submit comments and suggestions with respect to the guidance on FBAR reporting in this Notice by October 6, 2009, to:

Internal Revenue Service Attn: CC:PA:LPD:PR (Notice 2009-62) Room 5203 P.O. Box 7604 Ben Franklin Station Washington, D.C. 20044

or hand deliver comments Monday through Friday between the hours of 8 a.m. and 4 p.m. to:

Courier's Desk Internal Revenue Service Attn: CC:PA:LPD:PR (Notice 2009-62) 1111 Constitution Avenue, N.W. Washington, D.C. 20224

A copy of those comments should also be sent to:

Financial Crimes Enforcement Network Department of the Treasury P.O. Box 39 Vienna, VA 22183

Alternatively, the public may submit comments electronically via e-mail to the following address: Notice.Comments@irscounsel.treas.gov with a copy to regcomments@fincen.gov. Respondents should include "Notice 2009-62" in the subject line of any comment submitted.

All comments submitted by the public will be made available for public inspection and copying in their entirety.

IV. Effective Date

This Notice applies to FBARs (Form TD F 90-22.1) with respect to calendar year 2008 and prior calendar years.

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V. Contact Information

For further information regarding the relief relating to signature authority, contact Terra-Lynn Zentara at (202) 283-7659 (not a toll-free call). For further information regarding foreign commingled funds, contact Joseph Henderson at (202) 622-3446 (not a toll-free call).

U.S. Code collection

TITLE 18 > PART I > CHAPTER 46 > § 981

§ 981. Civil forfeiture

(a)

(1) The following property is subject to forfeiture to the United States:

(A) Any property, real or personal, involved in a transaction or attempted transaction in violation of section 1956, 1957 or 1960 of this title, or any property traceable to such property.

(B) Any property, real or personal, within the jurisdiction of the United States, constituting, derived from, or traceable to, any proceeds obtained directly or indirectly from an offense against a foreign nation, or any property used to facilitate such an offense, if the offense—

(i) involves trafficking in nuclear, chemical, biological, or radiological weapons technology or material, or the manufacture, importation, sale, or distribution of a controlled substance (as that term is defined for purposes of the Controlled Substances Act), or any other conduct described in section 1956 (c)(7)(B);

(ii) would be punishable within the jurisdiction of the foreign nation by death or imprisonment for a term exceeding 1 year; and

(iii) would be punishable under the laws of the United States by imprisonment for a term exceeding 1 year, if the act or activity constituting the offense had occurred within the jurisdiction of the United States.

(C) Any property, real or personal, which constitutes or is derived from proceeds traceable to a violation of section 215, 471, 472, 473, 474, 476, 477, 478, 479, 480, 481, 485, 486, 487, 488, 501, 502, 510, 542, 545, 656, 657, 842, 844, 1005, 1006, 1007, 1014, 1028, 1029, 1030, 1032, or 1344 of this title or any offense constituting "specified unlawful activity" (as defined in section 1956 (c)(7) of this title), or a conspiracy to commit such offense.

(D) Any property, real or personal, which represents or is traceable to the gross receipts obtained, directly or indirectly, from a violation of—

(i) section 666 (a)(1) (relating to Federal program fraud);

(ii) section 1001 (relating to fraud and false statements);

(iii) section 1031 (relating to major fraud against the United States);

(iv) section 1032 (relating to concealment of assets from conservator or receiver of insured financial institution);

(v) section 1341 (relating to mall fraud); or

(vi) section 1343 (relating to wire fraud),

if such violation relates to the sale of assets acquired or held by the Resolution Trust Corporation, the Federal Deposit Insurance Corporation, as conservator or receiver for a financial institution, or any other conservator for a financial institution appointed by the Office of the Comptroller of the Currency or the Office of Thrift Supervision or the National Credit Union Administration, as conservator or liquidating agent for a financial institution.

(E) With respect to an offense listed in subsection (a)(1)(D) committed for the purpose of executing or attempting to execute any scheme or artifice to defraud, or for obtaining money or property by means of false or fraudulent statements, pretenses, representations or promises, the gross receipts of such an offense shall include all property, real or personal, tangible or intangible, which thereby is obtained, directly or indirectly.

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(F) Any property, real or personal, which represents or is traceable to the gross proceeds obtained, directly or indirectly, from a violation of—

(i) section 511 (altering or removing motor vehicle identification numbers);

(ii) section 553 (importing or exporting stolen motor vehicles);

(iii) section 2119 (armed robbery of automobiles);

(iv) section 2312 (transporting stolen motor vehicles in interstate commerce); or

(v) section 2313 (possessing or selling a stolen motor vehicle that has moved in interstate commerce).

(G) All assets, foreign or domestic—

(i) of any individual, entity, or organization engaged in planning or perpetrating any any [FN1] Federal crime of terrorism (as defined in section 2332b (g)(5)) against the United States, citizens or residents of the United. States, or their property, and all assets, foreign or domestic, affording any person a source of influence over any such entity or organization;

(ii) acquired or maintained by any person with the intent and for the purpose of supporting, planning, conducting, or concealing any Federal crime of terrorism (as defined in section 2332b (g)(5) [FN2] against the United States, citizens or residents of the United States, or their property;

(iii) derived from, involved in, or used or intended to be used to commit any Federal crime of terrorism (as defined in section 2332b (g)(5)) against the United States, citizens or residents of the United States, or their property; or

(iv) of any individual, entity, or organization engaged in planning or perpetrating any act of international terrorism (as defined in section 2331) against any international organization (as defined in section 209 of the State Department Basic Authorities Act of 1956 (22 U.S.C. 4309 (b)) or against any foreign Government. [FN3] Where the property sought for forfeiture is located beyond the territorial boundaries of the United States, an act in furtherance of such planning or perpetration must have occurred within the jurisdiction of the United States.

(H) Any property, real or personal, involved in a violation or attempted violation, or which constitutes or is derived from proceeds traceable to a violation, of section 2339C of this title.

(2) For purposes of paragraph (1), the term "proceeds" is defined as follows:

(A) In cases involving illegal goods, illegal services, unlawful activities, and telemarketing and health care fraud schemes, the term "proceeds" means property of any kind obtained directly or indirectly, as the result of the commission of the offense giving rise to forfeiture, and any property traceable thereto, and is not limited to the net gain or profit realized from the offense.

(B) In cases involving lawful goods or lawful services that are sold or provided in an illegal manner, the term "proceeds" means the amount of money acquired through the illegal transactions resulting in the forfeiture, less the direct costs incurred in providing the goods or services. The claimant shall have the burden of proof with respect to the issue of direct costs. The direct costs shall not include any part of the overhead expenses of the entity providing the goods or services, or any part of the income taxes paid by the entity.

(C) In cases involving fraud in the process of obtaining a loan or extension of credit, the court shall allow the claimant a deduction from the forfeiture to the extent that the loan was repaid, or the debt was satisfied, without any financial loss to the victim.

(b)

(1) Except as provided in section 985, any property subject to forfeiture to the United States under subsection (a) may be seized by the Attorney General and, in the case of property involved in a violation investigated by the Secretary of the Treasury or the United States Postal Service, the property may also be seized by the Secretary of the Treasury or the Postal Service, respectively.

(2) Seizures pursuant to this section shall be made pursuant to a warrant obtained in the same manner as provided for a search warrant under the Federal Rules of Criminal Procedure, except that a seizure may be made without a warrant

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if—

(A) a complaint for forfeiture has been filed in the United States district court and the court issued an arrest warrant in rem pursuant to the Supplemental Rules for Certain Admiralty and Maritime Claims;

(B) there is probable cause to believe that the property is subject to forfeiture and—

(i) the seizure is made pursuant to a lawful arrest or search; or

(ii) another exception to the Fourth Amendment warrant requirement would apply; or

(C) the property was lawfully seized by a State or local law enforcement agency and transferred to a Federal agency.

(3) Notwithstanding the provisions of rule 41(a) of the Federal Rules of Criminal Procedure, a seizure warrant may be issued pursuant to this subsection by a judicial officer in any district in which a forfeiture action against the property may be filed under section 1355 (b) of title 28, and may be executed in any district in which the property is found, or transmitted to the central authority of any foreign state for service in accordance with any treaty or other international agreement. Any motion for the return of property seized under this section shall be filed in the district court in which the seizure warrant was issued or in the district court for the district in which the property was seized.

(4)

(A) If any person is arrested or charged in a foreign country in connection with an offense that would give rise to the forfeiture of property in the United States under this section or under the Controlled Substances Act, the Attorney General may apply to any Federal judge or magistrate judge in the district in which the property is located for an ex parte order restraining the property subject to forfeiture for not more than 30 days, except that the time may be extended for good cause shown at a hearing conducted in the manner provided in rule 43(e) of the Federal Rules of Civil Procedure.

(B) The application for the restraining order shall set forth the nature and circumstances of the foreign charges and the basis for belief that the person arrested or charged has property in the United States that would be subject to forfeiture, and shall contain a statement that the restraining order is needed to preserve the availability of property for such time as is necessary to receive evidence from the foreign country or elsewhere in support of probable cause for the seizure of the property under this subsection.

(c) Property taken or detained under this section shall not be repleviable, but shall be deemed to be in the custody of the Attorney General, the Secretary of the Treasury, or the Postal Service, as the case may be, subject only to the orders and decrees of the court or the official having jurisdiction thereof. Whenever property is seized under this subsection, the Attorney General, the Secretary of the Treasury, or the Postal Service, as the case may be, may—

(1) place the property under seal;

(2) remove the property to a place designated by him; or

(3) require that the General Services Administration take custody of the property and remove it, if practicable, to an appropriate location for disposition in accordance with law.

(d) For purposes of this section, the provisions of the customs laws relating to the seizure, summary and judicial forfeiture, condemnation of property for violation of the customs laws, the disposition of such property or the proceeds from the sale of such property under this section, the remission or mitigation of such forfeitures, and the compromise of claims (19 U.S.C. 1602 et seq.), Insofar as they are applicable and not inconsistent with the provisions of this section, shall apply to seizures and forfeitures incurred, or alleged to have been incurred, under this section, except that such duties as are imposed upon the customs officer or any other person with respect to the seizure and forfeiture of property under the customs laws shall be performed with respect to seizures and forfeitures of property under this section by such officers, agents, or other persons as may be authorized or designated for that purpose by the Attorney General, the Secretary of the Treasury, or the Postal Service, as the case may be. The Attorney General shall have sole responsibility for disposing of petitions for remission or mitigation with respect to property involved in a judicial forfeiture proceeding.

(e) Notwithstanding any other provision of the law, except section 3 of the Anti Drug Abuse Act of 1986, the Attorney

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General, the Secretary of the Treasury, or the Postal Service, as the case may be, is authorized to retain property forfeited pursuant to this section, or to transfer such property on such terms and conditions as he may determine—

(1) to any other Federal agency;

(2) to any State or local law enforcement agency which participated directly in any of the acts which led to the seizure or forfeiture of the property;

(3) In the case of property referred to in subsection (a)(1)(C), to any Federal financial institution regulatory agency—

(A) to reimburse the agency for payments to claimants or creditors of the institution; and

(B) to reimburse the insurance fund of the agency for losses suffered by the fund as a result of the receivership or liquidation;

(4) in the case of property referred to in subsection (a)(1)(C), upon the order of the appropriate Federal financial institution regulatory agency, to the financial institution as restitution, with the value of the property so transferred to be set off against any amount later recovered by the financial institution as compensatory damages in any State or Federal proceeding;

(5) in the case of property referred to in subsection (a)(1)(C), to any Federal financial institution regulatory agency, to the extent of the agency's contribution of resources to, or expenses involved in, the seizure and forfeiture, and the investigation leading directly to the seizure and forfeiture, of such property;

(6) as restoration to any victim of the offense giving rise to the forfeiture, including, in the case of a money laundering offense, any offense constituting the underlying specified unlawful activity; or

(7) In [FN3] the case of property referred to in subsection (a)(1)(D), to the Resolution Trust Corporation, the Federal Deposit Insurance Corporation, or any other Federal financial institution regulatory agency (as defined in section 8(e)(7)(D) of the Federal Deposit Insurance Act).

The Attorney General, the Secretary of the Treasury, or the Postal Service, as the case may be, shall ensure the equitable transfer pursuant to paragraph (2) of any forfeited property to the appropriate State or local law enforcement agency so as to reflect generally the contribution of any such agency participating directly in any of the acts which led to the seizure or forfeiture of such property. A decision by the Attorney General, the Secretary of the Treasury, or the Postal Service pursuant to paragraph (2) shall not be subject to review. The United States shall not be liable in any action arising out of the use of any property the custody of which was transferred pursuant to this section to any non-Federal agency. The Attorney General, the Secretary of the Treasury, or the Postal Service may order the discontinuance of any forfeiture proceedings under this section in favor of the institution of forfeiture proceedings by State or local authorities under an appropriate State or local statute. After the filing of a complaint for forfeiture under this section, the Attorney General may seek dismissal of the complaint in favor of forfeiture proceedings under State or local law. Whenever forfeiture proceedings are discontinued by the United States in favor of State or local proceedings, the United States may transfer custody and possession of the seized property to the appropriate State or local official immediately upon the initiation of the proper actions by such officials. Whenever forfeiture proceedings are discontinued by the United States in favor of State or local proceedings, notice shall be sent to all known interested parties advising them of the discontinuance or dismissal. The United States shall not be liable in any action arising out of the seizure, detention, and transfer of seized property to State or local officials. The United States shall not be liable in any action arising out of a transfer under paragraph (3), (4), or (5) of this subsection.

(f) All right, title, and interest in property described in subsection (a) of this section shall vest in the United States upon commission of the act giving rise to forfeiture under this section.

(g)

(1) Upon the motion of the United States, the court shall stay the civil forfeiture proceeding if the court determines that civil discovery will adversely affect the ability of the Government to conduct a related criminal investigation or the prosecution of a related criminal case.

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(2) Upon the motion of a claimant, the court shall stay the civil forfeiture proceeding with respect to that claimant if the court determines that—

(A) the claimant is the subject of a related criminal investigation or case;

(B) the claimant has standing to assert a claim in the civil forfeiture proceeding; and

(C) continuation of the forfeiture proceeding will burden the right of the claimant against self-incrimination in the related investigation or case.

(3) With respect to the impact of civil discovery described in paragraphs (1) and (2), the court may determine that a stay is unnecessary if a protective order limiting discovery would protect the interest of one party without unfairly limiting the ability of the opposing party to pursue the civil case. In no case, however, shall the court impose a protective order as an alternative to a stay if the effect of such protective order would be to allow one party to pursue discovery while the other party is substantially unable to do so.

(4) In this subsection, the terms "related criminal case" and "related criminal investigation" mean an actual prosecution or investigation in progress at the time at which the request for the stay, or any subsequent motion to lift the stay is made. In determining whether a criminal case or investigation is "related" to a civil forfeiture proceeding, the court shall consider the degree of similarity between the parties, witnesses, facts, and circumstances involved in the two proceedings, without requiring an identity with respect to any one or more factors.

(5) In requesting a stay under paragraph (1), the Government may, in appropriate cases, submit evidence ex parte in order to avoid disclosing any matter that may adversely affect an ongoing criminal investigation or pending criminal trial.

(6) Whenever a civil forfeiture proceeding is stayed pursuant to this subsection, the court shall enter any order necessary to preserve the value of the property or to protect the rights of lienholders or other persons with an interest in the property while the stay is in effect.

(7) A determination by the court that the claimant has standing to request a stay pursuant to paragraph (2) shall apply only to this subsection and shall not preclude the Government from objecting to the standing of the claimant by dispositive motion or at the time of trial.

(h) In addition to the venue provided for in section 1395 of title 28 or any other provision of law, in the case of property of a defendant charged with a violation that is the basis for forfeiture of the property under this section, a proceeding for forfeiture under this section may be brought in the judicial district in which the defendant owning such property is found or in the judicial district in which the criminal prosecution is brought.

(i)

(1) Whenever property is civilly or criminally forfeited under this chapter, the Attorney General or the Secretary of the Treasury, as the case may be, may transfer the forfeited personal property or the proceeds of the sale of any forfeited personal or real property to any foreign country which participated directly or indirectly in the seizure or forfeiture of the property, if such a transfer—

(A) has been agreed to by the Secretary of State;

(B) is authorized in an international agreement between the United States and the foreign country; and

(C) is made to a country which, if applicable, has been certified under section 481 (h) [FN4] of the Foreign Assistance Act of 1961.

A decision by the Attorney General or the Secretary of the Treasury pursuant to this paragraph shall not be subject to review. The foreign country shall, in the event of a transfer of property or proceeds of sale of property under this subsection, bear all expenses incurred by the United States in the seizure, maintenance, inventory, storage, forfeiture, and disposition of the property, and all transfer costs. The payment of all such expenses, and the transfer of assets pursuant to this paragraph, shall be upon such terms and conditions as the Attorney General or the Secretary of the Treasury may, in his discretion, set.

(2) The provisions of this section shall not be construed as limiting or superseding any other authority of the United

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States to provide assistance to a foreign country in obtaining property related to a crime committed in the foreign country, including property which is sought as evidence of a crime committed in the foreign country.

(3) A certified order or judgment of forfeiture by a court of competent jurisdiction of a foreign country concerning property which is the subject of forfeiture under this section and was determined by such court to be the type of property described in subsection (a) (1)(B) of this section, and any certified recordings or transcripts of testimony taken in a foreign judicial proceeding concerning such order or judgment of forfeiture, shall be admissible in evidence in a proceeding brought pursuant to this section. Such certified order or judgment of forfeiture, when admitted into evidence, shall constitute probable cause that the property forfeited by such order or judgment of forfeiture is subject to forfeiture under this section and creates a rebuttable presumption of the forfeitability of such property under this section.

(4) A certified order or judgment of conviction by a court of competent jurisdiction of a foreign country concerning an unlawful drug activity which gives rise to forfeiture under this section and any certified recordings or transcripts of testimony taken in a foreign judicial proceeding concerning such order or judgment of conviction shall be admissible in evidence in a proceeding brought pursuant to this section. Such certified order or judgment of conviction, when admitted into evidence, creates a rebuttable presumption that the unlawful drug activity giving rise to forfeiture under this section has occurred.

(5) The provisions of paragraphs (3) and (4) of this subsection shall not be construed as limiting the admissibility of any evidence otherwise admissible, nor shall they limit the ability of the United States to establish probable cause that property is subject to forfeiture by any evidence otherwise admissible.

(j) For purposes of this section—

(1) the term "Attorney General" means the Attorney General or his delegate; and

(2) the term "Secretary of the Treasury" means the Secretary of the Treasury or his delegate.

(k) Interbank Accounts.—

(1) In general.—

(A) In general.— For the purpose of a forfeiture under this section or under the Controlled Substances Act (21 U.S.C. 801 et seq.), if funds are deposited into an account at a foreign financial institution (as defined in section 984 (c)(2)(A) of this title), and that foreign financial institution (as defined in section 984 (c)(2)(A) of this title) has an interbank account in the United States with a covered financial institution (as defined in section 5318 (j)(1) of title 31), the funds shall be deemed to have been deposited into the interbank account in the United States, and any restraining order, seizure warrant, or arrest warrant in rem regarding the funds may be served on the covered financial institution, and funds in the interbank account, up to the value of the funds deposited into the account at the foreign financial institution (as defined in section 984 (c)(2)(A) of this title), may be restrained, seized, or arrested.

(B) Authority to suspend.— The Attorney General, in consultation with the Secretary of the Treasury, may suspend or terminate a forfeiture under this section if the Attorney General determines that a conflict of law exists between the laws of the jurisdiction in which the foreign financial institution (as defined in section 984 (c)(2)(A) of this title) is located and the laws of the United States with respect to liabilities arising from the restraint, seizure, or arrest of such funds, and that such suspension or termination would be in the interest of justice and would not harm the national interests of the United States.

(2) No requirement for government to trace funds.— If a forfeiture action is brought against funds that are restrained, seized, or arrested under paragraph (1), it shall not be necessary for the Government to establish that the funds are directly traceable to the funds that were deposited into the foreign financial institution (as defined in section 984 (c)(2)(A) of this title), nor shall it be necessary for the Government to rely on the application of section 984.

(3) Claims brought by owner of the funds.— If a forfeiture action is instituted against funds restrained, seized, or arrested under paragraph (1), the owner of the funds deposited into the account at the foreign financial institution (as defined in section 984 (c)(2)(A) of this title) may contest the forfeiture by filing a claim under section 983.

(4) Definitions.— For purposes of this subsection, the following definitions shall apply:

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(A) Interbank account.— The term “interbank account” has the same meaning as in section 984 (c)(2)(B).
(B) Owner.—
(i) In general.— Except as provided in clause (11), the term “owner”—
(I) means the person who was the owner, as that term is defined in section 983(d)(6), of the funds that were deposited into the foreign financial institution (as defined in section 984 (c)(2)(A) of this title) at the time such funds were deposited; and
(II) does not include either the foreign financial institution (as defined in section 984 (c)(2)(A) of this title) or any financial institution acting as an intermediary in the transfer of the funds into the interbank account.
(ii) Exception.— The foreign financial institution (as defined in section 984 (c)(2)(A) of this title) may be considered the “owner” of the funds (and no other person shall qualify as the owner of such funds) only if—
(I) the basis for the forfeiture action is wrongdoing committed by the foreign financial institution (as defined in section 984 (c)(2)(A) of this title); or
(II) the foreign financial institution (as defined in section 984 (c)(2)(A) of this title) establishes, by a preponderance of the evidence, that prior to the restraint, seizure, or arrest of the funds, the foreign financial institution (as defined in section 984 (c)(2)(A) of this title) had discharged all or part of its obligation to the prior owner of the funds, in which case the foreign financial institution (as defined in section 984 (c) (2)(A) of this title) shall be deemed the owner of the funds to the extent of such discharged obligation.

[FN1]. So in original.

[FN2]. So in original. A second closing parenthesis probably should appear

[FN3]. So in original. Probably should not be capitalized.

[FN4]. See References in Text below.

U.S. Code collection

TITLE 18 > PART I > CHAPTER 95 > § 1956

§ 1956. Laundering of monetary instruments

(a)
(1) Whoever, knowing that the property involved in a financial transaction represents the proceeds of some form of unlawful activity, conducts or attempts to conduct such a financial transaction which in fact involves the proceeds of specified unlawful activity—
(A)
(i) with the intent to promote the carrying on of specified unlawful activity; or
(ii) with intent to engage in conduct constituting a violation of section 7201 or 7206 of the Internal Revenue Code of 1986; or
(B) knowing that the transaction is designed in whole or in part—
(i) to conceal or disguise the nature, the location, the source, the ownership, or the control of the proceeds of specified unlawful activity; or
(ii) to avoid a transaction reporting requirement under State or Federal law,
shall be sentenced to a fine of not more than $500,000 or twice the value of the property involved in the transaction, whichever is greater, or imprisonment for not more than twenty years, or both. For purposes of this paragraph, a financial transaction shall be considered to be one involving the proceeds of specified unlawful activity if it is part of

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a set of parallel or dependent transactions, any one of which involves the proceeds of specified unlawful activity, and all of which are part of a single plan or arrangement.

(2) Whoever transports, transmits, or transfers, or attempts to transport, transmit, or transfer a monetary instrument or funds from a place in the United States to or through a place outside the United States or to a place in the United States from or through a place outside the United States—

(A) with the intent to promote the carrying on of specified unlawful activity; or

(B) knowing that the monetary instrument or funds involved in the transportation, transmission, or transfer represent the proceeds of some form of unlawful activity and knowing that such transportation, transmission, or transfer is designed in whole or in part—

(i) to conceal or disguise the nature, the location, the source, the ownership, or the control of the proceeds of specified unlawful activity; or

(ii) to avoid a transaction reporting requirement under State or Federal law,

shall be sentenced to a fine of not more than $500,000 or twice the value of the monetary instrument or funds involved in the transportation, transmission, or transfer, whichever is greater, or imprisonment for not more than twenty years, or both. For the purpose of the offense described in subparagraph (B), the defendant's knowledge may be established by proof that a law enforcement officer represented the matter specified in subparagraph (B) as true, and the defendant's subsequent statements or actions indicate that the defendant believed such representations to be true.

(3) Whoever, with the intent—

(A) to promote the carrying on of specified unlawful activity;

(B) to conceal or disguise the nature, location, source, ownership, or control of property believed to be the proceeds of specified unlawful activity; or

(C) to avoid a transaction reporting requirement under State or Federal law,

conducts or attempts to conduct a financial transaction involving property represented to be the proceeds of specified unlawful activity, or property used to conduct or facilitate specified unlawful activity, shall be fined under this title or imprisoned for not more than 20 years, or both. For purposes of this paragraph and paragraph (2), the term "represented" means any representation made by a law enforcement officer or by another person at the direction of, or with the approval of, a Federal official authorized to investigate or prosecute violations of this section.

(b) Penalties.—

(1) In general.— Whoever conducts or attempts to conduct a transaction described in subsection (a)(1) or (a)(3), or section 1957, or a transportation, transmission, or transfer described in subsection (a)(2), is liable to the United States for a civil penalty of not more than the greater of—

(A) the value of the property, funds, or monetary instruments involved in the transaction; or

(B) $10,000.

(2) Jurisdiction over foreign persons.— For purposes of adjudicating an action filed or enforcing a penalty ordered under this section, the district courts shall have jurisdiction over any foreign person, including any financial institution authorized under the laws of a foreign country, against whom the action is brought, if service of process upon the foreign person is made under the Federal Rules of Civil Procedure or the laws of the country in which the foreign person is found, and—

(A) the foreign person commits an offense under subsection (a) involving a financial transaction that occurs in whole or in part in the United States;

(B) the foreign person converts, to his or her own use, property in which the United States has an ownership interest by virtue of the entry of an order of forfeiture by a court of the United States; or

(C) the foreign person is a financial institution that maintains a bank account at a financial institution in the United States.

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(3) Court authority over assets.— A court may issue a pretrial restraining order or take any other action necessary to ensure that any bank account or other property held by the defendant in the United States is available to satisfy a judgment under this section.

(4) Federal receiver.—

(A) In general.— A court may appoint a Federal Receiver, in accordance, with subparagraph (B) of this paragraph, to collect, marshal, and take custody, control, and possession of all assets of the defendant, wherever located, to satisfy a civil judgment under this subsection, a forfeiture judgment under section 981 or 982, or a criminal sentence under section 1957 or subsection (a) of this section, including an order of restitution to any victim of a specified unlawful activity.

(B) Appointment and authority.— A Federal Receiver described in subparagraph (A)—

(i) may be appointed upon application of a Federal prosecutor or a Federal or State regulator, by the court having jurisdiction over the defendant in the case;

(ii) shall be an officer of the court, and the powers of the Federal Receiver shall include the powers set out in section 754 of title 28, United States Code; and

(iii) shall have standing equivalent to that of a Federal prosecutor for the purpose of submitting requests to obtain information regarding the assets of the defendant—

(I) from the Financial Crimes Enforcement Network of the Department of the Treasury; or

(II) from a foreign country pursuant to a mutual legal assistance treaty, multilateral agreement, or other arrangement for international law enforcement assistance, provided that such requests are in accordance with the policies and procedures of the Attorney General.

(c) As used in this section—

(1) the term “knowing that the property involved in a financial transaction represents the proceeds of some form of unlawful activity” means that the person knew the property involved in the transaction represented proceeds from some form, though not necessarily which form, of activity that constitutes a felony under State, Federal, or foreign law, regardless of whether or not such activity is specified in paragraph (7);

(2) the term “conducts” includes initiating, concluding, or participating in initiating, or concluding a transaction;

(3) the term “transaction” includes a purchase, sale, loan, pledge, gift, transfer, delivery, or other disposition, and with respect to a financial institution includes a deposit, withdrawal, transfer between accounts, exchange of currency, loan, extension of credit, purchase or sale of any stock, bond, certificate of deposit, or other monetary instrument, use of a safe deposit box, or any other payment, transfer, or delivery by, through, or to a financial institution, by whatever means effected;

(4) the term “financial transaction” means

(A) a transaction which in any way or degree affects interstate or foreign commerce

(i) involving the movement of funds by wire or other means or

(ii) involving one or more monetary instruments, or

(iii) involving the transfer of title to any real property, vehicle, vessel, or aircraft, or

(B) a transaction involving the use of a financial institution which is engaged in, or the activities of which affect, interstate or foreign commerce in any way or degree;

(5) the term “monetary instruments” means

(i) coin or currency of the United States or of any other country, travelers' checks, personal checks, bank checks, and money orders, or

(ii) investment securities or negotiable instruments, in bearer form or otherwise in such form that title thereto passes upon delivery;

(6) the term “financial institution” includes—

(A) any financial institution, as defined in section 5312 (a)(2) of title 31, United States Code, or the regulations

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promulgated thereunder; and

(B) any foreign bank, as defined in section 1 of the International Banking Act of 1978 (12 U.S.C. 3101);

(7) the term "specified unlawful activity" means—

(A) any act or activity constituting an offense listed in section 1961 (1) of this title except an act which is indictable under subchapter II of chapter 53 of title 31;

(B) with respect to a financial transaction occurring in whole or in part in the United States, an offense against a foreign nation involving—

(i) the manufacture, importation, sale, or distribution of a controlled substance (as such term is defined for the purposes of the Controlled Substances Act);

(ii) murder, kidnapping, robbery, extortion, destruction of property by means of explosive or fire, or a crime of violence (as defined in section 16);

(iii) fraud, or any scheme or attempt to defraud, by or against a foreign bank (as defined in paragraph 7 of section 1(b) of the International Banking Act of 1978)); [FN1]

(iv) bribery of a public official, or the misappropriation, theft, or embezzlement of public funds by or for the benefit of a public official;

(v) smuggling or export control violations involving—

(I) an item controlled on the United States Munitions List established under section 38 of the Arms Export Control Act (22 U.S.C. 2778); or

(II) an item controlled under regulations under the Export Administration Regulations (15 C.F.R. Parts 730-774);

(vi) an offense with respect to which the United States would be obligated by a multilateral treaty, either to extradite the alleged offender or to submit the case for prosecution, if the offender were found within the territory of the United States; or

(vii) trafficking in persons, selling or buying of children, sexual exploitation of children, or transporting, recruiting or harboring a person, including a child, for commercial sex acts;

(C) any act or acts constituting a continuing criminal enterprise, as that term is defined in section 408 of the Controlled Substances Act (21 U.S.C. 848);

(D) an offense under section 32 (relating to the destruction of aircraft), section 37 (relating to violence at international airports), section 115 (relating to influencing, impeding, or retaliating against a Federal official by threatening or injuring a family member), section 152 (relating to concealment of assets; false oaths and claims; bribery), section 175c (relating to the variola virus), section 215 (relating to commissions or gifts for procuring loans), section 351 (relating to congressional or Cabinet officer assassination), any of sections 500 through 503 (relating to certain counterfeiting offenses), section 513 (relating to securities of States and private entities), section 541 (relating to goods falsely classified), section 542 (relating to entry of goods by means of false statements), section 545 (relating to smuggling goods into the United States), section 549 (relating to removing goods from Customs custody), section 554 (relating to smuggling goods from the United States), section 641 (relating to public money, property, or records), section 656 (relating to theft, embezzlement, or misapplication by bank officer or employee), section 657 (relating to lending, credit, and insurance institutions), section 658 (relating to property mortgaged or pledged to farm credit agencies), section 666 (relating to theft or bribery concerning programs receiving Federal funds), section 793, 794, or 798 (relating to espionage), section 831 (relating to prohibited transactions involving nuclear materials), section 844 (f) or (1) (relating to destruction by explosives or fire of Government property or property affecting interstate or foreign commerce), section 875 (relating to interstate communications), section 922 (l) (relating to the unlawful importation of firearms), section 924 (n) (relating to firearms trafficking), section 956 (relating to conspiracy to kill, kidnap, maim, or injure certain property in a foreign country), section 1005 (relating to fraudulent bank entries), 1006 [FN2] (relating to fraudulent Federal credit institution entries), 1007 [FN2] (relating to Federal Depos-

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it Insurance transactions), 1014 [FN2] (relating to fraudulent loan or credit applications), section 1030 (relating to computer fraud and abuse), 1032 [FN2] (relating to concealment of assets from conservator, receiver, or liquidating agent of financial institution), section 1111 (relating to murder), section 1114 (relating to murder of United States law enforcement officials), section 1116 (relating to murder of foreign officials, official guests, or internationally protected persons), section 1201 (relating to kidnaping), section 1203 (relating to hostage taking), section 1361 (relating to willful injury of Government property), section 1363 (relating to destruction of property within the special maritime and territorial jurisdiction), section 1708 (theft from the mail), section 1751 (relating to Presidential assassination), section 2113 or 2114 (relating to bank and postal robbery and theft), section 2280 (relating to violence against maritime navigation), section 2281 (relating to violence against maritime fixed platforms), section 2319 (relating to copyright infringement), section 2320 (relating to trafficking in counterfeit goods and services), section 2332 (relating to terrorist acts abroad against United States nationals), section 2332a (relating to use of weapons of mass destruction), section 2332b (relating to international terrorist acts transcending national boundaries), section 2332g (relating to missile systems designed to destroy aircraft), section 2332h (relating to radiological dispersal devices), section 2339A or 2339B (relating to providing material support to terrorists), section 2339C (relating to financing of terrorism), or section 2339D (relating to receiving military-type training from a foreign terrorist organization) of this title, section 46502 of title 49, United States Code, a felony violation of the Chemical Diversion and Trafficking Act of 1988 (relating to precursor and essential chemicals), section 590 of the Tariff Act of 1930 (19 U.S.C. 1590) (relating to aviation smuggling), section 422 of the Controlled Substances Act (relating to transportation of drug paraphernalia), section 38 (c) (relating to criminal violations) of the Arms Export Control Act, section 11 (relating to violations) of the Export Administration Act of 1979, section 206 (relating to penalties) of the International Emergency Economic Powers Act, section 16 (relating to offenses and punishment) of the Trading with the Enemy Act, any felony violation of section 15 of the Food Stamp Act of 1977 (relating to food stamp fraud) involving a quantity of coupons having a value of not less than $5,000, any violation of section 543(a) (1) of the Housing Act of 1949 (relating to equity skimming), any felony violation of the Foreign Agents Registration Act of 1938, any felony violation of the Foreign Corrupt Practices Act, or section 92 of the Atomic Energy Act of 1954 (42 U.S.C. 2122) (relating to prohibitions governing atomic weapons) [FN3] environmental crimes

(E) a felony violation of the Federal Water Pollution Control Act (33 U.S.C. 1251 et seq.), the Ocean Dumping Act (33 U.S.C. 1401 et seq.), the Act to Prevent Pollution from Ships (33 U.S.C. 1901 et seq.), the Safe Drinking Water Act (42 U.S.C. 300f et seq.), or the Resources Conservation and Recovery Act (42 U.S.C. 6901 et seq.); or

(F) any act or activity constituting an offense involving a Federal health care offense;

(8) the term “State” includes a State of the United States, the District of Columbia, and any commonwealth, territory, or possession of the United States.

(d) Nothing in this section shall supersede any provision of Federal, State, or other law imposing criminal penalties or affording civil remedies in addition to those provided for in this section.

(e) Violations of this section may be investigated by such components of the Department of Justice as the Attorney General may direct, and by such components of the Department of the Treasury as the Secretary of the Treasury may direct, as appropriate, and, with respect to offenses over which the Department of Homeland Security has jurisdiction, by such components of the Department of Homeland Security as the Secretary of Homeland Security may direct, and, with respect to offenses over which the United States Postal Service has jurisdiction, by the Postal Service. Such authority of the Secretary of the Treasury, the Secretary of Homeland Security, and the Postal Service shall be exercised in accordance with an agreement which shall be entered into by the Secretary of the Treasury, the Secretary of Homeland Security, the Postal Service, and the Attorney General. Violations of this section involving offenses described in paragraph (c)(7)(E) may be investigated by such components of the Department of Justice as the Attorney General may direct, and the National Enforcement Investigations Center of the Environmental Protection Agency.

(f) There is extraterritorial jurisdiction over the conduct prohibited by this section if—

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(1) the conduct is by a United States citizen or, in the case of a non-United States citizen, the conduct occurs in part in the United States; and

(2) the transaction or series of related transactions involves funds or monetary instruments of a value exceeding $10,000.

(g) Notice of Conviction of Financial Institutions.— If any financial institution or any officer, director, or employee of any financial institution has been found guilty of an offense under this section, section 1957 or 1960 of this title, or section 5322 or 5324 of title 31, the Attorney General shall provide written notice of such fact to the appropriate regulatory agency for the financial institution.

(h) Any person who conspires to commit any offense defined in this section or section 1957 shall be subject to the same penalties as those prescribed for the offense the commission of which was the object of the conspiracy.

(i) Venue.—

(1) Except as provided in paragraph (2), a prosecution for an offense under this section or section 1957 may be brought in—

(A) any district in which the financial or monetary transaction is conducted; or

(B) any district where a prosecution for the underlying specified unlawful activity could be brought, if the defendant participated in the transfer of the proceeds of the specified unlawful activity from that district to the district where the financial or monetary transaction is conducted.

(2) A prosecution for an attempt or conspiracy offense under this section or section 1957 may be brought in the district where venue would lie for the completed offense under paragraph (1), or in any other district where an act in furtherance of the attempt or conspiracy took place.

(3) For purposes of this section, a transfer of funds from 1 place to another, by wire or any other means, shall constitute a single, continuing transaction. Any person who conducts (as that term is defined in subsection (c)(2)) any portion of the transaction may be charged in any district in which the transaction takes place.

[FN1]. So in original. The second closing parenthesis probably should not appear.

[FN2]. So in original. Probably should be preceded by “section”.

[FN3]. So in original. Probably should be followed by a semicolon.

U.S. Code collection

TITLE 18 > PART I > CHAPTER 95 > § 1957

§ 1957. Engaging in monetary transactions in property derived from specified unlawful activity

(a) Whoever, in any of the circumstances set forth in subsection (d), knowingly engages or attempts to engage in a monetary transaction in criminally derived property of a value greater than $10,000 and is derived from specified unlawful activity, shall be punished as provided in subsection (b).

(b)

(1) Except as provided in paragraph (2), the punishment for an offense under this section is a fine under title 18, United States Code, or Imprisonment for not more than ten years or both.

(2) The court may impose an alternate fine to that imposable under paragraph (1) of not more than twice the amount of the criminally derived property involved in the transaction.

(c) In a prosecution for an offense under this section, the Government is not required to prove the defendant knew that the offense from which the criminally derived property was derived was specified unlawful activity.

(d) The circumstances referred to in subsection (a) are—

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(1) that the offense under this section takes place in the United States or in the special maritime and territorial jurisdiction of the United States; or

(2) that the offense under this section takes place outside the United States and such special jurisdiction, but the defendant is a United States person (as defined in section 3077 of this title, but excluding the class described in paragraph (2)(D) of such section).

(e) Violations of this section may be investigated by such components of the Department of Justice as the Attorney General may direct, and by such components of the Department of the Treasury as the Secretary of the Treasury may direct, as appropriate, and, with respect to offenses over which the Department of Homeland Security has jurisdiction, by such components of the Department of Homeland Security as the Secretary of Homeland Security may direct, and, with respect to offenses over which the United States Postal Service has jurisdiction, by the Postal Service. Such authority of the Secretary of the Treasury, the Secretary of Homeland Security, and the Postal Service shall be exercised in accordance with an agreement which shall be entered into by the Secretary of the Treasury, the Secretary of Homeland Security, the Postal Service, and the Attorney General.

(f) As used in this section—

(1) the term "monetary transaction" means the deposit, withdrawal, transfer, or exchange, in or affecting interstate or foreign commerce, of funds or a monetary instrument (as defined in section 1956 (c)(5) of this title) by, through, or to a financial institution (as defined in section 1956 of this title), including any transaction that would be a financial transaction under section 1956 (c)(4)(B) of this title, but such term does not include any transaction necessary to preserve a person's right to representation as guaranteed by the sixth amendment to the Constitution;

(2) the term "criminally derived property" means any property constituting, or derived from, proceeds obtained from a criminal offense; and

(3) the term "specified unlawful activity" has the meaning given that term in section 1956 of this title.

U.S. Code collection

TITLE 18 > PART I > CHAPTER 46 > § 982

§ 982. Criminal forfeiture

(a)

(1) The court, in imposing sentence on a person convicted of an offense in violation of section 1956, 1957, or 1960 of this title, shall order that the person forfeit to the United States any property, real or personal, involved in such offense, or any property traceable to such property.

(2) The court, in imposing sentence on a person convicted of a violation of, or a conspiracy to violate—

(A) section 215, 656, 657, 1005, 1006, 1007, 1014, 1341, 1343, or 1344 of this title, affecting a financial institution, or

(B) section 471, 472, 473, 474, 476, 477, 478, 479, 480, 481, 485, 486, 487, 488, 501, 502, 510, 542, 545, 842, 844, 1028, 1029, or 1030 of this title,

shall order that the person forfeit to the United States any property constituting, or derived from, proceeds the person obtained directly or indirectly, as the result of such violation.

(3) The court, in imposing a sentence on a person convicted of an offense under—

(A) section 666 (a)(1) (relating to Federal program fraud);

(B) section 1001 (relating to fraud and false statements);

(C) section 1031 (relating to major fraud against the United States);

(D) section 1032 (relating to concealment of assets from conservator, receiver, or liquidating agent of insured financial institution);

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(E) section 1341 (relating to mail fraud); or

(F) section 1343 (relating to wire fraud),

Involving the sale of assets acquired or held by the Resolution Trust Corporation, the Federal Deposit Insurance Corporation, as conservator or receiver for a financial institution or any other conservator for a financial institution appointed by the Office of the Comptroller of the Currency or the Office of Thrift Supervision, or the National Credit Union Administration, as conservator or liquidating agent for a financial institution, shall order that the person forfeit to the United States any property, real or personal, which represents or is traceable to the gross receipts obtained, directly or indirectly, as a result of such violation.

(4) With respect to an offense listed in subsection (a)(3) committed for the purpose of executing or attempting to execute any scheme or artifice to defraud, or for obtaining money or property by means of false or fraudulent statements, pretenses, representations, or promises, the gross receipts of such an offense shall include any property, real or personal, tangible or intangible, which is obtained, directly or indirectly, as a result of such offense.

(5) The court, in imposing sentence on a person convicted of a violation or conspiracy to violate—

(A) section 511 (altering or removing motor vehicle identification numbers);

(B) section 553 (importing or exporting stolen motor vehicles);

(C) section 2119 (armed robbery of automobiles);

(D) section 2312 (transporting stolen motor vehicles in interstate commerce); or

(E) section 2313 (possessing or selling a stolen motor vehicle that has moved in interstate commerce);

shall order that the person forfeit to the United States any property, real or personal, which represents or is traceable to the gross proceeds obtained, directly or indirectly, as a result of such violation.

(6)

(A) The court, in imposing sentence on a person convicted of a violation of, or conspiracy to violate, section 274(a), 274A(a)(1), or 274A(a)(2) of the Immigration and Nationality Act or section 555, 1425, 1426, 1427, 1541, 1542, 1543, 1544, or 1546 of this title, or a violation of, or conspiracy to violate, section 1028 of this title if committed in connection with passport or visa issuance or use, shall order that the person forfeit to the United States, regardless of any provision of State law—

(I) any conveyance, including any vessel, vehicle, or aircraft used in the commission of the offense of which the person is convicted; and

(II) any property real or personal—

(I) that constitutes, or is derived from or is traceable to the proceeds obtained directly or indirectly from the commission of the offense of which the person is convicted; or

(II) that is used to facilitate, or is intended to be used to facilitate, the commission of the offense of which the person is convicted.

(B) The court, in imposing sentence on a person described in subparagraph (A), shall order that the person forfeit to the United States all property described in that subparagraph.

(7) The court, in imposing sentence on a person convicted of a Federal health care offense, shall order the person to forfeit property, real or personal, that constitutes or is derived, directly or indirectly, from gross proceeds traceable to the commission of the offense.

(8) The court, in sentencing a defendant convicted of an offense under section 1028, 1029, 1341, 1342, 1343, or 1344, or of a conspiracy to commit such an offense, if the offense involves telemarketing (as that term is defined in section 2325), shall order that the defendant forfeit to the United States any real or personal property—

(A) used or intended to be used to commit, to facilitate, or to promote the commission of such offense; and

(B) constituting, derived from, or traceable to the gross proceeds that the defendant obtained directly or indirectly as a result of the offense.

(b)

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(1) The forfeiture of property under this section, including any seizure and disposition of the property and any related judicial or administrative proceeding, shall be governed by the provisions of section 413 (other than subsection (d) of that section) of the Comprehensive Drug Abuse Prevention and Control Act of 1970 (21 U.S.C. 853).

(2) The substitution of assets provisions of subsection 413(p) shall not be used to order a defendant to forfeit assets in place of the actual property laundered where such defendant acted merely as an intermediary who handled but did not retain the property in the course of the money laundering offense unless the defendant, in committing the offense or offenses giving rise to the forfeiture, conducted three or more separate transactions involving a total of $100,000 or more in any twelve month period.

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APRIL 29, 2009 WEDNESDAY

DEPARTMENT: News, Commentary, and Analysis; News Stories

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HEADLINE: #4 2009 TNT 80-4 FRAUD ENFORCEMENT BILL COMBATING TAX EVASION PASSES SENATE. (Release Date: APRIL 28, 2009) (Doc 2009-9552)

ABSTRACT: A bill that would apply the international money laundering statute to tax evasion as part of a larger effort to help federal investigators fight financial crimes passed the Senate in a 92-4 vote on April 28.

SUMMARY:

Published by Tax Analysts(R)

A bill that would apply the international money laundering statute to tax evasion as part of a larger effort to help federal investigators fight financial crimes passed the Senate in a 92-4 vote on April 28.

The Fraud Enforcement and Recovery Act of 2009 (S. 386) -- originally cosponsored by Senate Judiciary Committee Chair Patrick J. Leahy, D-Vt., and Finance Committee ranking minority member Chuck Grassley, R-Iowa -- also sets aside additional funds for the next two years for financial fraud investigations, with the Justice Department's Tax Division receiving $ 5 million a year.

Lawmakers also agreed to several amendments during the bill's debate, including one offered by Sen. Byron L. Dorgan, D-N.D., that would create a Senate select committee to investigate the circumstances behind the economic crisis. The Senate also approved an amendment by Sen. Johnny Isakson, R-Ga., that would create a financial markets commission to look at several areas related to the economic downturn, including the tax treatment of financial products and investments.

AUTHOR: Shreve, Meg

Tax Analysts

GEOGRAPHIC: United States

REFERENCES:

Subject Area:

Compliance;

Tax havens

TEXT:

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Release Date: APRIL 28, 2009

Published by Tax Analysts(R)

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This is "a good bill touching many other facets of going after fraud, waste, and abuse," Grassley told reporters during a press conference.

Both Leahy and Grassley called on the House to move quickly on the bill. The House Judiciary Committee on April 28 approved a modified version of the Fight Fraud Act of 2009 (H.R. 1748). That bill would also set aside $ 5 million for the Justice Department's Tax Division. (For the text of the substitute amendment to H.R. 1748, see Doc 2009-9575.)

Leahy told reporters President Obama would sign the legislation. The Obama administration offered its strong support for the bill in an April 20 statement of administration policy, saying the measure would give the Justice Department "significant new criminal and civil tools and resources that would assist in holding accountable those who have committed financial fraud." (For the SAP, see Doc 2009-8911 or 2009 TNT 74-26.)

The bill is not without its detractors. In a March 18 letter to the Treasury Department, Justice Department, Senate Finance Committee, and House Ways and Means Committee, 36 tax practitioners voiced their objections to the bill, saying it could have negative effects on repatriation efforts and international commerce. (For previous coverage, see Doc 2009-6330 or 2009 TNT 53-2. For the letter, see Doc 2009-6041 or 2009 TNT 51-35.)

Daily Tax Report: All Issues > 2009 > May > 05/19/2009 > Federal Tax & Accounting > Tax Evasion: International Tax Evasion Provision Struck From Fraud Enforcement Bill

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International Tax Evasion Provision Struck From Fraud Enforcement Bill

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A provision targeting international tax evasion has been definitively struck from a mortgage and financial fraud enforcement bill (S. 386) up for a May 18 House vote.

The Senate amended the bill May 14 but returned it to the House without adding back the provision that would have criminalized the use of tax havens to avoid U.S. income tax.

The Senate's original version, which passed April 28, included the provision (80 DTR G-2, 4/29/09). It was removed when the House adopted a substitute amendment May 6, an atypical move on a bill scheduled for consideration under suspension of the rules (86 DTR G-4, 5/7/09).

An aide to Sen. Charles Grassley (Iowa), the ranking Republican on the Finance Committee and a co-sponsor of S. 386, told BNA May 18 that the provision represents a long-standing goal for Grassley.

Grassley will “continue to push it in his larger money laundering reform package and at every available opportunity,” the aide said.

By Christine Grimaldi

Daily Tax Report: All Issues > 2009 > March > 03/20/2009 > Federal Tax & Accounting > Tax Evasion: Practitioners Want Provision Criminalizing International Tax Fraud Stripped From FERA

52 DTR G-7

Related Terms

Topics:
Tax Evasion
Tax Fraud
Tax Legislation
Tax Policy

Tax Evasion **Practitioners Want Provision Criminalizing International Tax Fraud Stripped From FERA**

Legislation (S. 386) that would target criminal tax evasion as part of preventing various financial frauds should be stripped of a provision criminalizing international tax fraud “as a new and separate money laundering offense,” according to a March 18 letter signed by a number of tax practitioners.

The letter called the provision in the Fraud Enforcement and Recovery Act of 2009 (FERA) “ancillary and unnecessary to the overall salutary purpose of the bill,” and said it requires further consideration.

“We strongly support our system of taxation and tax administration by the IRS. To achieve our goal of Increasing voluntary compliance, the administration of our tax system must sufficiently encourage taxpayers to come forward voluntarily,” the letter said. “We believe that the expansion of IRS power into the international money laundering area is unwarranted and unnecessary given that agency's current level of authority,” it said.

The letter said the provision in S. 386 raises a number of concerns because:

- It will likely discourage voluntary repatriation of funds transmitted outside the U.S. for the purpose of complying with the federal tax laws.
- It may make attorneys and other professional advisers subject to criminal prosecution.
- There is a need to preserve due process considerations governing seizures and forfeitures in tax cases.
- It may cause tax offenses to be prosecuted under the International Money Laundering Statute rather than under the Internal Revenue Code.
- It could have a chilling effect on U.S. commerce and the United States' ability to obtain much-needed cooperation from other nations in tax enforcement.

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"Everybody is burdened with the requirements to deal with this extensively complex [tax] system," Bryan C. Skarlatos who penned the letter on behalf of the tax practitioners told BNA March 19. "So an additional level of sensitivity should be brought to criminalizing any tax-related act."

Skarlatos is a partner with the New York-based firm Kostelanetz & Fink LLP and chairman of the Civil and Criminal Tax Penalties Committee for the American Bar Association Section of Taxation. In addition to Skarlatos, 35 other practitioners signed the letter.

The letter praised the overall legislation, which is intended to prevent mortgage and other types of financial fraud and includes a crackdown on criminal tax evasion.

Congressional, Administration Leaders Solicited

The practitioners sent the letter to officials at the Internal Revenue Service and the Treasury and Justice departments. It also was addressed to congressional tax-writing committee chairmen and ranking members in both chambers, and to leaders and other Democratic members on the senate Judiciary Committee, which has jurisdiction over the legislation.

Among the addressees were Senate Judiciary Committee Chairman Patrick Leahy (D-Vt.) and Sen. Charles Grassley (R-Iowa), the ranking member on the Finance Committee and a Judiciary member, who joined together in introducing the legislation Feb. 5.

The Judiciary Committee cleared S. 386 by voice vote March 5 (42 DTR G-1, 3/6/09). In a March 12 letter, Leahy and Grassley urged Senate Majority Leader Harry Reid (D-Nev.) and Minority Leader Mitch McConnell (R-Ky.) to schedule a floor vote on the bill "without delay." "We hope to consider the bill next week," Reid's office said in an e-mail.

By Christine Grimaldi

Texts of the letter signed by the tax practitioners and the Leahy/Grassley letter are in TaxCore.

Daily Tax Report: All Issues > 2009 > March > 03/20/2009 > TaxCore® Congressional Documents > Correspondence > Letter to Congressional Leaders, Administration Officials on Tax Fraud Provisions in 2009 Fraud Enforcement and Recovery Act (S. 386)

Related Terms

Topics:
Tax Evasion

Letter to Congressional Leaders, Administration Officials on Tax Fraud Provisions in 2009 Fraud Enforcement and Recovery Act (S. 386)

March 18, 2009
Honorable Patrick Leahy
433 Russell Senate Office Building
United States Senate
Washington D.C. 20510
Honorable Edward E. Kaufman
G11 Dirksen Senate Office Building
United States Senate
Washington D.C. 20510
Honorable Max Baucus
511 Hart Senate Office Bldg

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Washington, D.C. 20510
Honorable Dave Camp
341 Cannon Building
Washington, DC 20515
Honorable Timothy F. Geithner
Secretary of the Treasurer
1500 Pennsylvania Avenue, N.W.
Washington D.C. 20220
Honorable Charles Grassley
135 Hart Senate Office Building
United States Senate
Washington D.C. 20510
Honorable Charles E. Schumer
313 Hart Senate Office Building
United State Senate
Washington D.C. 20510
Honorable Charles B. Rangel
2354 Rayburn House Office Bldg,
Washington, D.C. 20515
Honorable Eric H. Holder, Jr.
United States Attorney General
950 Pennsylvania Avenue, N.W.
Washington D.C. 20530
Honorable Douglas Shulman
Room 5203
PO Box 7604
Ben Franklin Station
Washington D.C. 20044

Re: Fraud Enforcement and Recovery Act of 2009 (S. 386)

Dear Sirs:

The undersigned, a group of concerned practitioners, many of whom are members of the American Bar Association Sections of Taxation, International Law, and Criminal Justice, State Bar Associations, and alumni of the Department of Justice, write to express their concerns with the provision contained in the Fraud Enforcement and Recovery Act of 2009, S. 386 ("FERA"), which criminalizes international tax fraud as a new and separate money laundering offense. We believe that subsection 2(g) of FERA has been placed inappropriately in this bill and should be removed for the reasons set forth below.

Overall, this is an excellent bill. FERA deals with mortgage fraud, securities fraud, financial institution fraud, and other frauds relating to federal assistance and relief programs. The proposed funding for the various federal agencies to enforce the legislation and to pursue high level white collar criminals is long overdue. As our federal government tries to correct the current economic downturn through economic stimulus, there will be many opportunities for individuals to commit economic crimes. We see this bill as an appropriate step to control fraud.

Our concern, indeed our objection, is to subsection 2(g) of FERA (hereinafter "FERA §2(g)"), which would make the International Money Laundering statute of 18 U.S.C. §1956(a)(2)(A) apply to tax evasion Subsection 2(g) is ancillary

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and unnecessary to the overall salutary purpose of the bill, and should be removed from FERA to allow for more study and consideration.

From a policy standpoint, it should be noted that the Anti-Money Laundering Act of 1986 did not include tax evasion as a separate offense within the money laundering statute, nor was it included within the definition of a "specific unlawful activity" in section (a)(7) of Title 18 U.S.C. §1956. The reason for this omission was a concern that turning every garden variety tax offense into a money laundering offense would eviscerate the criminal provisions of the federal tax code. In 1988, with little legislative history, the Treasury Department persuaded Congress to add 18 U.S.C. §1956(a)(1)(A)(ii), a domestic money laundering offense where the intent was to engage in conduct constituting a violation of §§7201 or 7206 of the Internal Revenue Code of 1986 (the "Internal Revenue Code").

Expanding the criminal enforcement power of the Internal Revenue Service (the "IRS") into the international money laundering area should be carefully considered, given the power of the IRS over our tax laws generally. The signers have some very serious concerns about the potentially damaging consequences of the passage of FERA §2(g), including the following:

• FERA §2(g) may discourage the future voluntary repatriation of funds transmitted or held outside of the U.S.

• FERA §2(g) could make advising a client who has conducted an international financial transaction with funds derived from an alleged U.S. tax offense a "prohibited transaction," and could expose attorneys, accountants, and other professionals to liability for criminal money laundering offenses.

• The forfeiture provision in FERA §2(g) raises significant due process concerns as it would allow the government to apply, *ex parte*, for seizure orders, shifting the burden to taxpayers to unfreeze seized monies.

• FERA §2(g) may cause U.S. Attorneys to use the International Money Laundering statute (18 U.S.C. §1956), rather than the specifically designated statutes set forth under the Internal Revenue Code (*i.e.*, 26 U.S.C. §§7201 and 7206) to prosecute tax crimes.

• FERA §2(g) could have a "chilling effect" on U.S. commerce and may interfere with the U.S.'s ability to obtain much-needed cooperation from other nations in the tax enforcement area.

Each of these concerns is discussed in move detail below.

1. FERA §2(g) Will Likely Discourage Voluntary Repatriation of Funds Transmitted Outside the U.S. for the Purpose of Complying with the Federal Tax Laws

The proposed amendments will have the unwanted effect of discouraging taxpayers from repatriating funds held in previously unreported foreign accounts, Given the abuses of foreign banks such as United Bank of Switzerland ("UBS"), which acted in concert with U.S. taxpayers to conceal income and assets from the U.S. government, this provision is particularly ill-advised at this time. At the same time that the Commissioner of the IRS is properly encouraging taxpayers to voluntarily disclose previously unreported foreign accounts through its voluntary disclosure program (provided for in internal Revenue Manual ("IRM") §9.5.11.9), and repatriate Rinds held offshore, FERA §2(g) will criminalize the transmission of those funds into the U.S. Under current law, a taxpayer who transmits funds outside of the U.S. with the intent to commit tax evasion in violation of 26 U.S.C. §7201 or tax fraud in violation of 26 U.S.C. §7206, is already subject to various significant criminal and civil penalties set forth in the Internal Revenue Code. [FN1] These penalties are more than adequate. FERA §2 (g) would not enhance enforcement of the Internal Revenue Code, but instead would discourage disclosure and repatriation.

As the government and public have become acutely aware while the UBS drama unfolds, off-shore funds are easily hidden from the IRS in unreported foreign accounts. Even when the IRS is aware of such accounts, the funds in them are very difficult to seize, if they are not outside of the government's reach altogether. Although the U.S. is party to several treaties that provide for assistance in seizure of assets, these treaties do not cover all of the countries where such funds may be located. As a result, there may be situations in which the IRS will not be able to obtain funds that were transmit-

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ted abroad without the taxpayer's voluntary compliance, FERA §2(g) will discourage voluntary repatriation, and may even create an incentive for a taxpayer to ensure that offshore funds remain hidden from and unreachable by the IRS. Our voluntary compliance system of tax administration must encourage, rather than discourage, such disclosure and repatriation actions by U.S. taxpayers.

2. FERA §2(g) May Make Attorneys and Other Professional Advisors Subject to Criminal Prosecution

FERA §2(g) may adversely impact the ability of attorneys and other professionals to advise clients regarding international financial transactions involving proceeds derived from a violation of 26 U.S.C. §§7201 or 7206 to the extent that the statute is interpreted as providing for criminal prosecution for aiding and abetting money laundering under 18 U.S.C. §2, or conspiracy to commit money laundering under 18 U.S.C. §371 for giving that advice. For example, if a taxpayer requests an attorney's advice regarding funds in a foreign account that were previously transmitted from the U.S. with an intent to commit tax fraud or tax evasion, by advising that the client repatriate the funds to the U.S., under one possible reading of FERA §2(g), the attorney may be subject to criminal liability. Moreover, an attorney might unwittingly run afoul of FERA §2(g) by failing to perform sufficient due diligence on clients who have funds in foreign accounts to determine whether those funds are proceeds derived from a violation of 26 U.S.C. §§7201 or 7206.

Under FERA §2(g), practitioners may either represent taxpayers who have committed tax fraud for tax evasion and risk criminal prosecution, or decline to advise such taxpayers. It is likely that most practitioners will choose the latter thus making it more difficult and less likely for taxpayers to voluntarily become compliant with federal tax laws after counseling with an attorney. Taxpayer representatives must not be exposed to prosecution, simply for advising their clients of a manner of complying with U.S. law.

3. The Need to Preserve Due Process Considerations Governing Seizures and Forfeitures in Tax Cases

The amendments proposed under FERA §2(g) will upset the equilibrium of due process safeguards that govern the use by federal tax authorities of their already strong seizure and forfeiture powers in relation to tax controversies. The criminal forfeiture provision in FERA §2(g) would allow for the seizure of funds upon application of the government, without the meaningful due process protections now afforded to the taxpayer. FERA §2(g) would allow the government, *ex parte*, to apply for seizure orders, and under current forfeiture case law, would shift to the taxpayer the burden of unfreezing seized monies. The effect of this subsection would greatly expand the IRS' ability to characterize any international monetary transaction as a money laundering offense, without the checks and balances found within the Internal Revenue Code.

Under current law, the IRS (through the Treasury Department) possesses, under 26 U.S.C. §7321, the power to seize assets that may be forfeitable pursuant to may provision of the Internal Revenue Code. The tax statutes that the IRS generally invokes for these purposes are 26 U.S.C. §7301—targeting property intended to be sold, removed, concealed, or deposited to defraud the U.S. of tax or to avoid payment of tax—and, with greater frequency, 26 U.S.C. §7302, with respect to property used or Intended to be used in violation of the Internal Revenue laws. For example, the IRS may put 26 U.S.C. §7321 to use against tangible property—such as storage facilities and trucks— involved in alleged violations of the motor fuels excise tax law.

In exercising the powers granted to it under the Internal Revenue Code to effectuate tax related seizures and forfeitures, the IRS follows a detailed protocol of checks and oversight. For example, as IRM §9.7.13.4.1 makes clear, “[IRS] Area Counsel must be involved in all Title 26 forfeitures at the pre-seizure stage of the potential action.” An equally strong and intricate system of safeguards applies with equal vigor, under 26 U.S.C. §§6330 through 6344, to the IRS' exercise of its powers to administratively lien and levy taxpayer property.

In addition, the IRS currently may invoke the civil seizure and forfeiture powers contained in 18 U.S.C. §981 (a so-called “Title 18 seizure”), under the premise that use of the U.S. Postal Service or of the means of electronic transmission

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to file a fraudulent tax return may constitute mail, wire, or bank fraud, thus giving rise to the kind of "specified unlawful activities" ("SUAs") that form a predicate act under 18 U.S.C. §981(a)(1). However, as is spelled out in IRM §9.7.13.4.4, it is the "general practice" of the IRS not to engage in a Title 18 seizure during the course of a tax or tax-related case except in "egregious circumstances," such as a refund fraud investigation in which IRS civil collection methods cannot adequately protect the assets subject to forfeiture or a seizure/forfeiture under Title 26 is not applicable.

Even for "egregious" tax cases in which the IRS may seek to effectuate a Title 18 seizure, the IRM prescribes multiple levels of oversight and approval—from an IRS Special Agent in Charge (SAC) to Area Counsel to the IRS Director of Field Operations, with approval sought from the Tax Division of the Department of Justice. Furthermore, an IRS SAC requesting approval for a Title 18 seizure must affirmatively explain why "IRS collection methods cannot adequately protect the assets" and why the "Title 26 seizure/forfeiture provisions are inapplicable."

If the amendments proposed under FERA §2(g) are enacted, then these procedures and safeguards can be bypassed in any potential federal prosecution in which there is an allegation that monies or instruments were "transported, transmitted, or transferred," with some intent to engage in conduct in violation of 26 U.S.C. §§7201 or 7206. In short, individual offices of the U.S. Attorney will be empowered to use the International Money Laundering statute to prosecute allegations of tax evasion—even without any indicia of fraud—independent of any predicate SUA or property representing the proceeds of any SUA. The granting of such unfettered powers to prosecutors, no matter how well-intentioned or wisely employed, would irrevocably upset the carefully-constructed balance of checks and oversights by which seizures and forfeitures in tax and tax-related cases are currently conducted.

4. FERA §2(g) May Cause Tax Offenses to Be Prosecuted under the International Money Laundering Statute rather than under the Internal Revenue Code

FERA §2(g) may encourage U.S. Attorneys to use the International Money Laundering statute (18 U.S.C. §1956), rather than the specifically designated statutes set forth under the Internal Revenue Code (*i.e.*, 26 U.S.C. §§7202 and 7206) to prosecute alleged tax crimes. The legal elements required for a criminal conviction are different in a tax fraud case than a money laundering case. Prosecution under the international Money Laundering statute carries a much greater penalty (a twenty-year penalty as opposed to the five-year penalty for tax fraud), and is not subject to the rigors of proof required in a tax fraud case with a potential penalty of a five-year felony. Serious policy questions exist as to whether any international monetary transaction connected with tax fraud should be subject to such an overwhelmingly harsh penalty. There is also a concern as to whether such a weapon would be used fairly. Money laundering offenses often have been used inappropriately to extract pleas to the underlying offense in order to avoid the money laundering penalty.

5. FERA §2(g) Could Have a Chilling Effect on U.S. Commerce and the U.S.' Ability to Obtain Cooperation from Other Nations in Tax Enforcement

In its testimony on February 11, 2009 before the U.S. Senate Committee on the Judiciary with regard to FERA, the Department of Justice (the "DOJ") stated that "the offshore movement of funds for the purpose of evading income taxes can *contribute* to the *development* of offshore [banking] centers, and businesses operated by international criminal organizations, that facilitate the laundering of proceeds of drug trafficking and other serious offenses." [FN2] (*Emphasis added*.) In substance, the proposed enactment of FERA see 2(g) would, according to the DOJ, seek to preempt, through the threat of potential criminal prosecution, the flow of U.S. funds to financial institutions in certain parts of the developing world in order to prevent these incipient financial centers from developing the kind of sophisticated capabilities—which U.S.-based institutions have long-since attained—that *might* eventually be employed by money launderers or other criminals.

Such interference by U.S. law enforcement agencies with the otherwise legitimate economic development of sovereign nations, occurring wholly outside of recognized diplomatic channels, is not only shortsighted but may well chill interna-

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tional and U.S. commerce. Moreover, there are millions of international monetary transactions in and out of the U.S. on a daily basis. There is a serious question as to whether FERA §2(g)'s proposed expansion of the law enforcement power of the IRS to ferret out illicit transactions connected with tax fraud will have a negative impact on international commerce. The answer is unknown, but it is likely that commerce would be adversely affected, and, at a minimum, more thought should be given to whether this is sound financial policy.

Moreover, such proposed assertion of extraterritorial jurisdiction to preempt the normally applicable laws of sovereigns hosting investment may well trigger similar laws by foreign sovereigns. Since the balance of foreign investment is at least as great into the U.S. as it is out of the U.S. the law has the potential to diminish foreign investment in the U.S. and dampen international financial flows generally.

Before the U.S. takes such aggressive extraterritorial preemptive action, it should first try to broaden international cooperation. For instance, the Clinton administration proposed regulations which would broaden the countries with which the U.S. exchanges information on interest from bank account deposits paid to residents of various countries. The regulations were never promulgated, but on March 4, 2009, the Chair of the Senate Permanent Subcommittee on Investigations proposed making the regulations final. We endorse his suggestion. At present, the U.S. regularly shares such information only with Canada. Broadening bilateral cooperation and regular data sharing will result in better enforcement than unilateral extraterritorial enforcement and does not risk jeopardizing access to global capital markets, especially our own.

Finally, the Treasury Inspector General for Tax Administration (“TIGTA”) has recommended increased outreach and cooperation by the U.S. with our treaty partners and other governments in order to facilitate the exchange of information and assist in law enforcement. [FN3] FERA §2(g) may undercut the very efforts at cooperation and engagement that the TIGTA has described as being essential for closing the burgeoning international tax gap. As such, this proposed amendment should be excised from what is an otherwise thoughtful and necessary bill.

Instead of enacting FERA §2(g) at this time, we recommend that the U.S. work through organizations, such as the Organization for Economic and Cooperative Development, which is working on projects related to the taxation of high-net worth individuals, as well as the International Monetary Fund and the United Nations. Working with these organizations will give any standards adopted more legitimacy since these organizations have universal membership. Only after the U.S. has truly tried to expand its bilateral and multilateral cooperation should it consider other measures.

***

In conclusion, we believe that subsection 2(g) of the proposed Fraud Enforcement and Recovery Act of 2009 is inappropriately placed in the legislation and should be removed. We strongly support our system of taxation and tax administration by the IRS. To achieve our goal of increasing voluntary compliance, the administration of our tax system must sufficiently encourage taxpayers to come forward voluntarily. We believe that the expansion of IRS power into the international money laundering area is unwarranted and unnecessary given that agency's current level of authority. This portion of the S. 386 could benefit from more study, public comment, and consideration.

Sincerely yours,

/s/

Bryan C. Skarlatos
Chair, Civil and Criminal Tax Penalties
Committee, Section of Taxation,
American Bar Association
Kostelanetz & Fink, LLP
7 World Trade Center
New York, New York 10007

Signatories

Stuart E. Abrams
Frankel & Abrams

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New York, New York
Former Chair, Civil and Criminal Tax Penalties Committee Section of Taxation, American Bar Association
Former Chief, Major Crimes Unit, Office of the U.S. Attorney, Southern District of New York
Former Associate Independent Counsel (Iran-Contra)
James G. Atkins, MBA, CPA/ABV/CFF, CVA, CFE
Lake Mary, Florida
David F. Axelrod
Columbus, Ohio
Former Chair, Civil and Criminal Tax Penalties Committee Section of Taxation, American Bar Association
Former Chair, Young Lawyers Division, American Bar Association
Former Assistant U.S. Attorney, Southern District of Florida
Former Trial Attorney (Criminal), Tax Division, Department of Justice
Charles W. Blau
Meadows, Collier, Reed, Cousins, & Blau, LLP
Dallas, Texas
Former Associate Deputy Attorney General, Department of Justice
Megan L. Brackney
Kostelanetz & Fink, LLP
New York, New York
Chair-Elect, Individual Income Tax Committee
Subcommittee Chair, Important Developments (Criminal)
Civil and Criminal Tax Penalties Committee Section of Taxation, American Bar Association
Former Assistant U.S. Attorney, Southern District of New York
James A. Bruton, III
Williams & Connolly LLP
Washington, D.C.
Former Acting Assistant Attorney General, Tax Division, Department of Justice
Former Deputy Assistant Attorney General (Criminal), Tax Division, Department of Justice
Larry A. Campagna
Chamberlain, Hrdlicka, White, Williams & Martin
Houston, Texas
Vice Chair Elect, Civil and Criminal Tax Penalties Committee
Former Chair, Employment Tax Committee Section of Taxation, American Bar Association
Caroline D. Ciraolo
Rosenberg/Martin/Greenberg, LLP
Baltimore, Maryland
Chair, Taxation Section, Maryland State Bar Association
Former Subcommittee Chair, Important Developments (Criminal)
Civil and Criminal Tax Penalties Committee Section of Taxation, American Bar Association
Cella R. Clark
Law Offices of Celia R. Clark, PLLC
New York, NY
Member, Section of Taxation, American Bar Association
John G. DeLancett
Goldenrod, Florida

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Former Chair, Tax Section, Orange County Bar Association
Scott Dickenson
Lathrop & Gage LLP
St. Louis, Missouri
Diana L. Erbsen
DLA Piper US LLP
New York, New York
Vice-Chair, Standards of Tax Practice Committee Section of Taxation, American Bar Association
Gerald A. Feffer
Williams & Connolly, LLP
Washington, D.C.
Former Deputy Assistant Attorney General (Criminal), Tax Division, Department of Justice
Former Assistant Chief, Criminal Division, United States Attorney's Office Southern District of New York
Former Chair, Civil and Criminal Tax Penalties Committee Section of Taxation, American Bar Association
Robert S. Fink
Kostelanetz & Fink, LLP
New York, New York
Former Chair, Civil and Criminal Tax Penalties Committee Section of Taxation, American Bar Association
Miriam L. Fisher
Morgan, Lewis & Bockius LLP
Washington, D.C.
Council Director and Former Chair, Civil and Criminal Tax Penalties Committee Section of Taxation, American Bar Association
Former Co-Chair, Tax Section, D.C. Bar Association
Former Special Assistant to the Assistant Attorney General, Tax Division, Department of Justice
R. Lawrence Heinkel
R. Lawrence Heinkel, P.L.
St. Petersburg, Florida
Member, The Florida Bar
Member, American Bar Association
Matt Jacober
Lathrop & Gage, LLP
St. Louis, Missouri
Paula M. Junghans
Zuckerman Spaeder, LLP
Washington, D.C.
Former Acting Assistant Attorney General, Tax Division, Department of Justice
Former Deputy Assistant Attorney General (Criminal), Tax Division, Department of Justice
Former Chair, Civil and Criminal Tax Penalties Committee Section of Taxation, American Bar Association
Kathryn Keneally
New York, New York
Former Chair, Civil and Criminal Tax Penalties Committee
Former Chair, Standards of Tax Practice Committee Section of Taxation, American Bar Association
Edward Krauland
Steptoe & Johnson, LLP

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Washington, D.C.
Edward James Leyden
Hollrah Leyden LLC
Washington, D.C.
Chair, Employment Tax Committee Section of Taxation, American Bar Association
Robert E. McKenzie
ARNSTEIN & LEHR LLP
Chicago, Illinois
Chair, Pro Bono Committee
Former Vice-Chair, Professional Services Committee Section of Taxation, American Bar Association
Scott D. Michel
Caplin & Drysdale
Washington, D.C.
Chair, Standards of Tax Practice Committee
Former Chair, Civil and Criminal Tax Penalties Committee Section of Taxation, American Bar Association
Kevin E. Packman
Holland & Knight
Miami, Florida
Member, Civil and Criminal Tax Penalties Committee and Administrative Committee Section of Taxation, American Bar Association
Dennis L. Perez
Hochman, Salkin, Rettig, Toscher & Perez, P.C.
Beverly Hills, California
Former Member, Executive Committee Taxation Section, State Bar of California
Member, Section of Taxation, American Bar Association
Ellis L. Reemer
DLA Piper US LLP
New York, New York
Former Senior Trial Attorney, IRS Office of Chief Counsel
Former Co-Chair, Compliance, Practice and Procedure Committee Tax Section, New York State Bar Association
Former Member, Executive Committee Tax Section, New York State Bar Association
Charles P. Rettig
Hochman, Salkin, Rettig, Toscher & Perez, P.C.
Beverly Hills, California
Former Chair, Taxation Section, State Bar of California
Chair-Elect, Civil & Criminal Tax Penalties Committee Section of Taxation, American Bar Association
Edward M. Robbins, Jr.
Hochman, Salkin, Rettig, Toscher & Perez, P.C.
Beverly Hills, California
Former Chief, Tax Division, Office of the U.S. Attorney, Central District of California
William S. Rose, Jr.
McNair Law Firm, P.A.
Hilton Head Island, South Carolina
Former Assistant Attorney General, Tax Division, Department of Justice
Stephen A. Saltzburg

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Professor of Law
George Washington University Law School
Frances D. Sheehy
Coconut Creek, Florida
Chair Elect, Tax Section, Florida Bar Association
Chair, Bankruptcy and Workout Committee Section of Taxation, American Bar Association
Bryan C. Skarlatos
Kostelanetz & Fink, LLP
New York, New York
Chair, Civil and Criminal Tax Penalties Committee Section of Taxation, American Bar Association
Co-Chair, Compliance, Practice and Procedure Committee Tax Section, New York State Bar Association
William W. Taylor
Zuckerman Spaeder, LLP
Washington, D.C.
Former Chair, Criminal Justice Section, American Bar Association
Steven Toscher
Hochman, Salkin, Rettig, Toscher & Perez, P.C.
Beverly Hills, California
Former Chair, Taxation Section, Los Angeles County Bar Association Member, Section of Taxation, American Bar Association
John J. Washburn
Nashua, New Hampshire
Chairman, Taxation Section, New Hampshire State Bar Association
Bruce Zagaris
Berliner Corcoran & Rowe L.L.P.
Washington, D.C.
Subcommittee Chair, International Enforcement, Civil and Criminal Tax Penalties Committee Section of Taxation, American Bar Association Former Chair, International Criminal Law Committee Former Member, Section Council Criminal Justice Section, American Bar Association
Former Chair, International Criminal Law Committee
Former Chair, International Tax Committee Section of International Law, American Bar Association

[FN1]. FERA §2(g) only requires an intent to violate 26 U.S.C. §§7201 or 7206 at the time of transmission. As a result, a taxpayer can violate proposed 18 U.S.C. §1956(a)(2)(A) without actually having committed a tax law violation.

[FN2]. *See* Statement of Rita Glavin, Acting Attorney General, Criminal Division, U.S. Department of Justice, "The Need for Increased Fraud Enforcement in the Wake of the Economic Downturn" (Feb. 11, 2009).

[FN3]. *See* Report of Treasury Inspect or General for Tax Administration "A Combination of Legislative Actions and Increased IRS Capability and Capacity Are Required to Reduce the Mutli-Billion Dollar U.S. International Tax Gap," (Jan. 27, 2009).

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Subchapter C Forfeitures §§7301-7328
Part II PROVISIONS COMMON TO FORFEITURES §§7321-7328
§7321 Authority to seize property subject to forfeiture.

Internal Revenue Code

§ 7321 Authority to seize property subject to forfeiture.

Any property subject to forfeiture to the United States under any provision of this title may be seized by the Secretary.

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Subchapter C Forfeitures §§7301-7328
Part I PROPERTY SUBJECT TO FORFEITURE §§7301-7304
§7301 Property subject to tax.

Internal Revenue Code

§ 7301 Property subject to tax.

(a) Taxable articles.

Any property on which, or for or in respect whereof, any tax is imposed by this title which shall be found in the possession or custody or within the control of any person, for the purpose of being sold or removed by him in fraud of the internal revenue laws, or with design to avoid payment of such tax, or which is removed, deposited, or concealed, with intent to defraud the United States of such tax or any part thereof, may be seized, and shall be forfeited to the United States.

(b) Raw materials.

All property found in the possession of any person intending to manufacture the same into property of a kind subject to tax for the purpose of selling such taxable property in fraud of the internal revenue laws, or with design to evade the payment of such tax, may also be seized, and shall be forfeited to the United States.

(c) Equipment.

All property whatsoever, in the place or building, or any yard or enclosure, where the property described in subsection (a) or (b) is found, or which is intended to be used in the making of property described in subsection (a), with intent to defraud the United States of tax or any part thereof, on the property described in subsection (a) may also be seized, and shall be forfeited to the United States.

(d) Packages.

All property used as a container for, or which shall have contained, property described in subsection (a) or (b) may also be seized, and shall be forfeited to the United States.

(e) Conveyances.

Any property (including aircraft, vehicles, vessels, or draft animals) used to transport or for the deposit or concealment of property described in subsection (a) or (b), or any property used to transport or for the deposit or concealment of property which is intended to be used in the making or packaging of property described in subsection (a), may also

be seized, and shall be forfeited to the United States.

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§7302 Property used in violation of internal revenue laws.

Internal Revenue Code

§ 7302 Property used in violation of internal revenue laws.

It shall be unlawful to have or possess any property intended for use in violating the provisions of the internal revenue laws, or regulations prescribed under such laws, or which has been so used, and no property rights shall exist in any such property. A search warrant may issue as provided in chapter 205 of title 18 of the United States Code and the Federal Rules of Criminal Procedure for the seizure of such property. Nothing in this section shall in any manner limit or affect any criminal or forfeiture provision of the internal revenue laws, or of any other law. The seizure and forfeiture of any property under the provisions of this section and the disposition of such property subsequent to seizure and forfeiture, or the disposition of the proceeds from the sale of such property, shall be in accordance with existing laws or those hereafter in existence relating to seizures, forfeitures, and disposition of property or proceeds, for violation of the internal revenue laws.

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Indictment in 'United States v. Greenstein'

W.D. Wash.

No. CR08-0296RSM

June 4, 2009

UNITED STATES DISTRICT COURT WESTERN DISTRICT OF WASHINGTON AT SEATTLE UNITED STATES OF AMERICA, Plaintiff, v. JEFFREY I. GREENSTEIN, CHARLES H. WILK, and MATTHEW G. KRANE, Defendants.

No. CR08-0296RSM

SUPERSEDING INDICTMENT

08-CR-00296-INDI

THE GRAND JURY CHARGES THAT:

COUNT 1

(Conspiracy to Defraud IRS)

1. Beginning at a time unknown, but no later than in or about June 1999, and continuing until in or about August 2006, at Seattle, Washington, within the Western District of Washington and elsewhere, JEFFREY I. GREENSTEIN and CHARLES H. WILK, and others known and unknown, did knowingly conspire, combine, confederate and agree to defraud the United States and an agency thereof, to wit, the Internal Revenue Service (hereinafter, "IRS") of the United States Department of Treasury, for the purpose of impeding, impairing, defeating and obstructing the lawful governmental functions of the IRS in the ascertainment, evaluation, assessment, and collection of incomes taxes, interest, and penalties.

I. INTRODUCTION

A. ***Defendants and, Other Relevant Parties*****.**

At all times relevant to this Superseding Indictment:

2. Quellos Group, L.L.C. (hereinafter "Quellos"), formerly known as Quadra Capital Management, L.P., was an investment management services firm founded in or about 1994 and headquartered in Seattle, Washington.

3. Defendant JEFFREY I. GREENSTEIN was a founder and Chief Executive Officer of Quellos. JEFFREY I. GREENSTEIN has a bachelors degree in finance and extensive experience dealing in complex securities and derivative markets. Prior to founding Quellos, JEFFREY I. GREENSTEIN was a General Partner of another registered investment advisory firm that provided alternative investment strategies through the use of derivatives and hedging transactions. Previous to that, JEFFREY I. GREENSTEIN had been affiliated with a national investment advisory firm, marketing derivative securities to institutional clients.

4. Beginning in or about 1996, JEFFREY I. GREENSTEIN gained knowledge and experience in tax shelters through work with certain national accounting firms on tax shelter strategies to include, among others, FLIP (Foreign Leveraged Investment Program), OPIS (Offshore Portfolio Investment Strategy), and CDS (Contingent Deferred Swaps). JEFFREY I. GREENSTEIN, with others at Quellos, assisted national accounting firms by designing aspects of FLIP and OPIS, and provided execution services in connection with approximately 150 individual FLIP and OPIS transactions. JEFFREY I. GREENSTEIN, with others at Quellos, also promoted and provided execution services for a number of CDS transactions. Through JEFFREY I. GREENSTEIN's work on the various tax shelters, Quellos earned tens of millions of dollars in fees. Through JEFFREY I. GREENSTEIN's involvement in FLIP and OPIS alone, Quellos earned between $25 million and $50 million in fees. In addition, JEFFREY I. GREENSTEIN gained further knowledge about tax shelters by personally participating in a FLIP shelter for himself.

5. Quellos Customs Strategies, LLC (hereinafter "QCS"), was formed in or about March 1999 as a wholly owned subsidiary of Quellos. QCS was formed with the goal of providing customized services to high net-worth individuals and families, including designing and implementing customized tax shelter strategies to minimize or defer payment of taxes. Through QCS, JEFFREY I. GREENSTEIN sought to capture a part of the lucrative tax shelter market from the national accounting firms for themselves. JEFFREY I. GREENSTEIN also sought to use these tax shelter strategies as a means to attract wealthy clients to the firm who could then be persuaded to invest their assets with Quellos, thereby expanding

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Quellos's investment business. One such tax shelter strategy developed and implemented by QCS was a strategy that came to be known as “POINT” (Portfolio Optimized Investment Transaction).

6. Defendant CHARLES H. WILK, a lawyer with a Masters Degree in tax law, joined Quellos in or about June 1999 as a principal. As part of his duties, CHARLES H. WILK directed QCS's tax shelter business. Prior to joining Quellos, CHARLES H. WILK was a senior manager with a national accounting firm, whose duties included providing tax shelter strategies for the accounting firm's wealthy clients. Previous to his position at the accounting firm, CHARLES H. WILK was an associate in the tax department of a national law firm.

7. European American Investment Holdings NV was incorporated in or about June 1999 in the Netherlands Antilles. European American Investment Holdings NV was a holding company under which a group of companies known as European American Investment Group (hereinafter “Euram”) was organized. Euram was formed by American and European investors, in part, to acquire an Austrian bank, which came to be known as European American Investment Bank AG.

8. In or about 1999, principals from Quellos, including JEFFREY I. GREENSTEIN, became shareholders in Euram and stood to profit from Euram's business.

9. Of the other Euram companies, two United Kingdom-based subsidiaries, European American Corporate Services Limited and European American Advisors Limited, focused on advising and providing structured financial products for high net worth individuals. The key members of the management of Euram included:

a. C.D., Euram's Chief Executive Officer;

b. J.S., Euram's Head of Tax and Structured Products; and

c. R.P., Euram's Head of Risk Management and Alternative Investments.

10. Beginning in or about late 1999 and continuing through in or about 2002, C.D., J.S., and R.P. of Euram assisted Quellos by providing execution services, such as drafting transactional documents and finding and appropriating offshore shell companies, in furtherance of tax shelter strategies developed by QCS. Euram earned large fees for its participation in the tax shelter transactions developed and marketed by QCS, generally 1% of the tax loss desired by the taxpayer client.

11. Beginning in or about 1999 and continuing through in or about 2000, Partner L.S. of Law Firm C.S. & M. LLP provided legal advice to JEFFREY I. GREENSTEIN and CHARLES H. WILK with respect to the development and implementation of POINT, and issued legal opinion letters to at least four clients who entered into POINT tax shelter transactions.

12. In 2001 and 2002, Law Firm B.C. LLP provided legal opinion letters to at least two clients who entered into POINT tax shelter transactions.

B. *The POINT Tax Shelter*.

13. Beginning in or about 1999 and continuing through in or about 2001, JEFFREY I. GREENSTEIN and CHARLES H. WILK designed, marketed and implemented the tax shelter strategy known as POINT. In or about 2000 and 2001, six POINT tax shelters were executed on behalf of five wealthy individuals:

a. In 2000, Client M.Z. executed a POINT tax shelter transaction with Quellos. Client M.Z.'s POINT tax shelter transaction was known as “Torens.”

b. In 2000, Client R.J. executed a POINT tax shelter transaction with Quellos. Client R.J.'s POINT tax shelter transaction was known as “Reka.”

c. In 2000, Client B.J. executed a POINT tax shelter transaction with Quellos. Client B.J.'s POINT tax shelter transaction was known as “Burgundy.”

d. In 2000 and then in 2001, Client M.S. executed two POINT tax shelter transactions with Quellos. Client M.S.'s POINT tax shelter transactions were known respectively as “Platinum” and “Cobalt.”

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e. In 2001, Client H.S. executed a POINT tax shelter transaction with Quellos. Client H.S.'s POINT tax shelter transaction was known as "Titanium."

14. The total amount of fees paid by the clients to participate in POINT was approximately $86 million. The clients who participated in the POINT tax shelter collectively sought to shelter approximately $2 billion in capital gains and avoid payment of more than $400 million in federal taxes.

15. The objective of POINT was to offset capital gains and defer and reduce taxes on those gains. In furtherance of this tax saving objective, JEFFREY I. GREENSTEIN and CHARLES H. WILK, with the assistance of C.D., J.S., and R.P. of Euram, designed a series of transactions and executed those transactions on behalf of their clients in order to obtain the desired tax benefits. While each of the six POINT transactions varied somewhat in actual implementation, they typically included the following steps:

a. During late 1999 and continuing through 2000, an "offshore investment fund" purportedly purchased shares of stock in well known, publicly-traded technology companies. The fund then formed a number of offshore partnership entities and contributed portions of its portfolio of stock to such partnerships. These partnership entities were known generically as "Special Purpose Vehicles" or "SPVs."

b. The fund then purportedly caused each SPV to issue "Covered Warrants" against their respective baskets of stocks. The Covered Warrants operated like a long-dated call, meaning that an outside investor could purchase the Warrant for a premium in return for the right in five years to purchase the stocks in the SPV at a set price. In this case, each Covered Warrant was purportedly placed with a "bank" or some other financial institution that purportedly paid millions in premiums to the SPVs for the Warrants. The institution then was purportedly responsible for further marketing the Warrant to others.

c. Once the Warrants were issued, a U.S. taxpayer acquired from the offshore fund the partnership interests in an SPV. At the time the client acquired his or her partnership, the technology stocks that the fund had purportedly contributed to the partnership had fallen in value and, therefore, the partnership had built-in, unrealized losses.

d. After the client acquired the partnership, he or she contributed to the partnership his or her own assets. These assets, typically other stock that the client desired to sell, had unrealized gains.

e. Shortly after the client contributed his or her own assets, within a matter of two or three months, all or most of the assets within the partnership were sold, including the purported shares of technology stock with the built-in loss. The sale of the pre-existing portfolio also purportedly triggered a cancellation of the "Covered Warrant" under terms that ultimately resulted in no economic impact on the partnership or the client who acquired the partnership. The client then offset the gains from his or her contributed assets with the alleged losses stemming from the pre-existing portfolio.

f. Subsequently, the client was able to draw out of the partnership, tax free, the proceeds up to the client's basis in the partnership, or continue to maintain the proceeds within the partnership tax free, and invest it further.

C. *IRS Treatment of Tax Shelters*.

16. During all times relevant to this Superseding Indictment, JEFFREY I. GREENSTEIN and CHARLES H. WILK knew and understood that tax shelters that the IRS concluded were designed, marketed and implemented solely for the purpose of providing clients with a way to defer or reduce tax, would be challenged by the IRS. In that event, the IRS would seek to collect the unpaid taxes plus interest, and might also seek to impose substantial penalties upon the clients.

17. During all times relevant to this Superseding Indictment, JEFFREY I. GREENSTEIN and CHARLES H. WILK knew and understood that in order for a tax shelter strategy to survive challenge by the IRS, taxpayers were generally required to demonstrate the following:

a. First, the individual transactions that comprised the shelter possessed real economic substance and were not sham transactions;

b. Second, the transactions that comprised the shelter were not pre-arranged and orchestrated solely for the purpose of

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obtaining a tax benefit; and

c. Third, the various parties involved in the transactions had a bona fide business purpose for engaging in the transactions, i.e., that the client and others had a reasonable profit motive to take part in the transaction other than for tax savings.

18. During all times relevant to this Superseding Indictment, JEFFREY I. GREENSTEIN and CHARLES H. WILK also knew and understood in the event that the IRS disallowed a benefit obtained as a result of a tax shelter, the IRS could impose substantial penalties ranging from 20% to 40% of the underpayment attributable to the shelter, unless the claimed tax benefit was supported by an independent legal opinion, reasonably relied upon by the taxpayer in good faith. Therefore, JEFFREY I. GREENSTEIN and CHARLES H. WILK knew and understood that in order to induce clients to participate in a shelter, and to shield the clients from possible penalties, they had to obtain legal opinion letters from reputable law firms concluding that a shelter will at least “more likely than not” survive IRS challenge.

II. OBJECT OF THE CONSPIRACY

19. It was a part of and an object of the conspiracy that JEFFREY I. GREENSTEIN and CHARLES H. WILK, together with others known and unknown, to unlawfully and knowingly defraud and attempt to defraud the IRS by impeding, impairing, defeating and obstructing the lawful governmental functions of the IRS in the ascertainment, evaluation, assessment, and collection of income taxes, interest, and penalties by designing, marketing, implementing, and defending and aiding in the defense before the IRS of a fraudulent tax shelter known as POINT.

III. MANNER AND MEANS OF THE CONSPIRACY

20. It was a part of the conspiracy that JEFFREY I. GREENSTEIN and CHARLES H. WILK designed and developed the POINT tax shelter to consist of a preordained series of sham transactions, executed in precise steps in accordance with the directions of JEFFREY I. GREENSTEIN and CHARLES H. WILK, for the sole purpose of providing a means for wealthy individuals to reduce and/or defer the payment of taxes on capital gains income.

21. It was further a part of the conspiracy that JEFFREY I. GREENSTEIN and CHARLES H. WILK implemented the POINT tax shelter in a manner that minimized costs to Quellos and maximized their profits. Specifically, JEFFREY I. GREENSTEIN and CHARLES H. WILK knew and understood that the procurement of sufficient amounts of actual stocks to generate the losses for the POINT clients would cost more than they or others involved in the implementation of the shelter were able or willing to pay. Furthermore, JEFFREY I. GREENSTEIN and CHARLES H. WILK were unsuccessful in locating any bona fide, independent third-party who had real assets with sufficient built-in losses willing to participate in the POINT transaction. Therefore, JEFFREY I. GREENSTEIN and CHARLES H. WILK caused the creation of a fictional “offshore investment fund” with a fictional portfolio of stocks that had been obtained through a series of sham paper transactions in which no stocks and no money ever exchanged hands.

22. It was further a part of the conspiracy that JEFFREY I. GREENSTEIN and CHARLES H. WILK knew at the time they designed, marketed and implemented the POINT tax shelters that the various clients who participated in the shelter would likely be audited by the IRS. Therefore, JEFFREY I. GREENSTEIN and CHARLES H. WILK drafted and disseminated, and caused to be drafted and disseminated, marketing material, transactional documents, and legal opinions designed to conceal from the IRS the facts that first, each aspect of the POINT tax shelter, including the actions of the “offshore investment fund” was wholly conceived, orchestrated, and directed by JEFFREY I. GREENSTEIN and CHARLES H. WILK for the purpose of implementing a tax shelter, and second, that the purported stocks that generated the off-setting losses for POINT clients were, in truth and fact, non-existent.

A. *Fraudulent POINT Marketing Materials*.

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23. It was further a part of the conspiracy that in order to conceal and attempt to conceal from the IRS the true nature of the POINT tax shelter, JEFFREY I. GREENSTEIN and CHARLES H. WILK drafted and disseminated and caused to be drafted and disseminated to POINT clients and their advisors, false, fraudulent and misleading descriptions of the POINT transaction in a marketing document entitled "POINT Strategy," knowing and expecting that such clients and their advisors would rely upon the document to claim false and fraudulent tax benefits as well as in defense of any audit before the IRS. The POINT Strategy document purportedly set forth the genesis and business rationale for the POINT transaction. According to the document, the POINT Strategy was an investment opportunity independently fashioned by offshore parties to replicate a popular European investment vehicle, and only fortuitously discovered by Quellos. The document described this supposed investment opportunity as follows:

a. A certain unnamed "offshore investment fund" desired to profit from replicating a European financial product sold by large European financial institutions known as "Covered Warrants," "BLOCS," or "HYPOS."

b. In order to replicate this product, the fund formed a partnership entity known generically as an SPV ("Special Purpose Vehicle"). Once the SPV was formed, the fund contributed certain publicly traded "stocks" it purportedly owned to the SPV. The fund then caused the SPV to issue a "Covered Warrant" on the stocks in the SPV. The terms of the Covered Warrant gave the acquirer of the Warrant the right to purchase the SPV's stocks in five years at a set price in return for a large premium. According to the POINT Strategy document, a "bank" agreed to subscribe to the Covered Warrant and paid millions in premiums to the SPV with the intention of marketing the Warrant to other investors.

c. Once the SPV was formed, funded and the Covered Warrant placed with the bank, the fund, with the assistance of the bank, sought to sell the entirety of the SPV interests to potential investors with the goal of profiting from the sale. According to the POINT Strategy document, Quellos only became involved in marketing this opportunity because the bank, which had a pre-existing relationship with Quellos, approached Quellos to assist them in marketing the SPV units to U.S. investors.

24. It was further a part of the conspiracy that JEFFREY I. GREENSTEIN and CHARLES H. WILK knew, in truth and fact, that contrary to what was stated in the POINT Strategy document, the "offshore investment fund" was not an independent investment fund who formed and marketed the SPV interests with the desire to replicate a popular European investment vehicle, but rather, a shell corporation whose actions were wholly controlled by JEFFREY I. GREENSTEIN, CHARLES H. WILK and their Euram associates for the sole purpose of implementing a tax shelter.

25. It was further a part of the conspiracy that JEFFREY I. GREENSTEIN and CHARLES H. WILK knew, in truth and fact, that contrary to what was stated in the POINT Strategy document, the "offshore investment fund" owned no stocks to contribute to the SPVs.

26. It was further a part of the conspiracy that JEFFREY I. GREENSTEIN and CHARLES H. WILK knew, in truth and fact, that contrary to what was stated in the POINT Strategy document, the "Covered Warrant" was a sham paper transaction, that no "bank" subscribed to any Warrant, that no premiums were ever paid for the Warrant by any such bank, and that there was never any intent by any bank to market the Warrant.

27. It was further a part of the conspiracy that JEFFREY I. GREENSTEIN and CHARLES H. WILK knew, in truth and fact, that contrary to what was stated in the POINT Strategy document, Quellos was not fortuitously introduced by the bank to the POINT Strategy and asked to assist in marketing the product to U.S. investors but, rather, JEFFREY I. GREENSTEIN and CHARLES H. WILK conceived, designed and orchestrated the entire POINT strategy, including the actions of the purported "offshore investment fund," and intended from the beginning to market the strategy to U.S. taxpayers as a tax shelter.

B. ***Fraudulent POINT Transaction Documents*.**

28. It was further a part of the conspiracy that in order to conceal and attempt to conceal the true nature of the POINT tax shelter from the IRS, JEFFREY I. GREENSTEIN and CHARLES H. WILK drafted and executed and caused to be

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drafted and executed false, fraudulent and misleading contracts and agreements to document the various steps in the POINT transaction, knowing and expecting that clients who participated in POINT would rely upon such documents to claim a false and fraudulent tax benefit as well as in defense of any audit by the IRS.

29. It was further a part of the conspiracy that JEFFREY I. GREENSTEIN and CHARLES H. WILK represented and caused to be represented to clients and others that an Isle of Man entity known as Barnville Ltd. (hereinafter “Barnville”) was the “offshore investment fund” that created the SPVs and contributed the loss generating stocks.

30. It was further a part of the conspiracy that JEFFREY I. GREENSTEIN and CHARLES H. WILK caused to be drafted and executed a series of false, fraudulent, and misleading “Purchase Agreements” dated December 28, 1999, January 3, 2000, January 10, 2000, February 28, 2000, and June 6, 2000, through which Barnville purportedly purchased more than $9 billion worth of stocks in a number of publicly traded technology companies from another Isle of Man entity known as Jackstones Ltd. (hereinafter “Jackstones”).

31. It was further a part of the conspiracy that JEFFREY I. GREENSTEIN and CHARLES H. WILK knew, in truth and fact, that the Purchase Agreements were false, fraudulent and misleading in that Jackstones possessed no stocks to sell and Barnville had no means to pay for any such stocks.

32. It was further a part of the conspiracy that JEFFREY I. GREENSTEIN and CHARLES H. WILK, in order to conceal the fact that Barnville never acquired any stocks from Jackstones on the dates subscribed to in the various Purchase Agreements, and that the purchases were a sham, caused to be drafted and executed a “Securities Lending Agreement” between Barnville and Jackstones. According to the terms of the Securities Lending Agreement, Barnville, on each day it purchased stocks from Jackstones, immediately loaned the same stocks back to Jackstones in return for “cash” collateral purportedly equal to the purchase price. JEFFREY I. GREENSTEIN and CHARLES H. WILK knew and understood that this lending arrangement would be used to provide an explanation to the clients and their advisors, who, in turn, would provide the explanation to the IRS, as to the reason for the apparent lack of delivery or transfer of any stocks and cash between brokerage accounts of Barnville and Jackstones at the time of the purported purchase and, therefore, conceal the fact that Barnville never owned any stocks in the first place.

33. It was further a part of the conspiracy that JEFFREY I. GREENSTEIN and CHARLES H. WILK, in 2000 and 2001, drafted and executed and caused to be drafted and executed false, fraudulent and misleading “Subscription Agreements” to the Global Call Warrants that were purportedly issued by each of the SPVs associated with the POINT clients. According to the “Subscription Agreement,” a company known as EA Investment Services Limited subscribed to the Global Call Warrants and in return paid a “Subscription Price” to the SPVs. The purported Subscription Price, in each instance, amounted to millions of U.S. dollars, and, according to the Subscription Agreement, the payments were credited to an account at EA Investment Services Limited for the benefit of each SPV. JEFFREY I. GREENSTEIN and CHARLES H. WILK knew, in truth and fact, that no subscription payments were ever made or going to be made, that EA Investments Limited had neither the intention nor the ability to make any such payments, and that the “Subscription Agreements” were shams, implemented solely to provide a fraudulent business purpose for the transaction.

C. *False, Fraudulent and Misleading Information Given to Legal Opinion Writers*.

34. It was further a part of the conspiracy that JEFFREY I. GREENSTEIN and CHARLES H. WILK knew and understood that in order to induce clients to participate in POINT, they would need to provide an opinion from respected law firms concluding that the shelter would at least “more likely than not” survive a challenge from the IRS.

35. It was further a part of the conspiracy that JEFFREY I. GREENSTEIN and CHARLES H. WILK knew and understood that in the event of an audit, these legal opinions would likely be produced to the IRS in defense of the audit and to avoid possible penalties.

36. It was further a part of the conspiracy that JEFFREY I. GREENSTEIN and CHARLES H. WILK secured the participation of Law Firm C.S. & M. LLP and Law Firm B.C. LLP to opine on the various POINT transactions implemented

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by the five clients. Law Firm C.S. & M. LLP opined on the first four POINT transactions executed by Quellos in 2000; specifically, Law Firm C.S. & M. LLP opined on the POINT transactions known as Torens, Reka, Burgundy, and Platinum. Law Firm B.C. LLP opined on the last two POINT transactions executed by Quellos in 2001; specifically, Law Firm B.C. LLP opined on POINT transactions known as Titanium and Cobalt. Each opinion concluded that the POINT transaction would "more likely than not" survive a challenge from the IRS.

37. It was further a part of the conspiracy that in order to conceal and attempt to conceal the true nature of the tax shelter from the opinion writers and, ultimately, the IRS, JEFFREY I. GREENSTEIN and CHARLES H. WILK knowingly and willfully made and caused to be made false, fraudulent and misleading representations to Law Firm C.S. & M. LLP and Law Firm B.C. LLP about the POINT transaction, knowing that Law Firm C.S. & M. LLP and Law Firm B.C. LLP would rely upon their representations in order to understand the POINT transactions and to render their "more likely than not" opinions. These false, fraudulent and misleading representations included the following:

a. JEFFREY I. GREENSTEIN and CHARLES H. WILK falsely, fraudulently and misleadingly represented and caused to be represented that the source of the losses utilized by the clients in the POINT transactions was derived from "stocks" in well-known publicly traded companies that had been purchased by a "non-U.S. investment fund" or "foreign investment fund," and contributed to the various SPVs.

b. JEFFREY I. GREENSTEIN and CHARLES H. WILK falsely, fraudulently and misleadingly represented and caused to be represented that Barnville was the independent "non-U.S. investment fund" or "foreign investment fund" that formed the SPVs, and that Barnville formed the SPVs independent of any pre-conceived plan to utilize the SPVs for a tax shelter; specifically, that Barnville formed the SPVs in order to profit from the issuance and sale of the "Covered Warrants."

38. It was further a part of the conspiracy that JEFFREY I. GREENSTEIN and CHARLES H. WILK provided and caused to be provided to Law Firm C.S. & M. LLP and Law Firm B.C. LLP the same false, fraudulent, and misleading POINT Strategy document that they had provided to their clients, knowing that the document was false, fraudulent and misleading and knowing and expecting that the firms would rely upon the document to understand the POINT transaction and to render their opinions.

39. It was further a part of the conspiracy that JEFFREY I. GREENSTEIN and CHARLES H. WILK provided and caused to be provided to Law Firm C.S. & M. LLP and Law Firm B.C. LLP the same false, fraudulent, and misleading transactional documents, including the Purchase Agreements and the Securities Lending Agreement between Barnville and Jackstones, and the Subscription Agreements for the Covered Warrants that they had provided to their clients, knowing that the transactional documents were false, fraudulent and misleading, and knowing and expecting that the firms would rely upon such documents to understand the POINT transaction and to render their opinions.

40. It was further a part of the conspiracy that JEFFREY I. GREENSTEIN and CHARLES H. WILK provided and caused to be provided to Law Firms C.S. & M. LLP and B.C. LLP, false, fraudulent and misleading documents regarding the fees paid by the Clients to implement the POINT tax shelter strategy, in order to hide the actual amount of fees they paid and, thereby, make it falsely appear that the Clients had a reasonable potential of earning a profit from the POINT tax shelter strategy aside from the tax benefits.

41. It was further a part of the conspiracy that Law Firm C.S. & M. LLP and Law Finn B.C. LLP provided JEFFREY I. GREENSTEIN and CHARLES H. WILK with drafts of their opinion letters, and relied upon JEFFREY I. GREENSTEIN and CHARLES H. WILK to provide corrections and edits to the factual descriptions of the POINT transactions in the opinion letters.

42. It was further a part of the conspiracy that as a result of their reliance upon JEFFREY I. GREENSTEIN's and CHARLES H. WILK's representations regarding the POINT transactions, Law Firm C.S. & M. LLP and Law Firm B.C. LLP issued opinion letters that included false, fraudulent, and misleading descriptions of the POINT transactions.

43. It was further a part of the conspiracy that JEFFREY I. GREENSTEIN and CHARLES H. WILK provided the false, fraudulent, and misleading opinion letters issued by Law Firm C.S. & M. LLP to clients and prospective clients in

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order to induce them to participate in the transaction, knowing that the opinion letters were false, fraudulent, and misleading.

D. ***Kickbacks Paid to Matthew G. Krane, the Personal Attorney of Client H.S.***

44. It was further a part of the conspiracy that in 2001, CHARLES H. WILK met Matthew G. Krane, a tax attorney and advisor to Client H.S. CHARLES H. WILK learned from Matthew G. Krane that Client H.S. anticipated having more than $1 billion in capital gains in 2001.

45. It was further a part of the conspiracy that in 2001, JEFFREY I. GREENSTEIN, CHARLES H. WILK and Matthew G. Krane agreed to kickback to Matthew G. Krane a portion of the fees Quellos obtained from Client H.S.

46. It was further a part of the conspiracy that in 2001, JEFFREY I. GREENSTEIN, CHARLES H. WILK and Matthew G. Krane did not disclose to Client H.S. the kickback arrangement. Instead, beginning in or about March 2001 and continuing through in or about October 2001, JEFFREY I. GREENSTEIN, CHARLES H. WILK and Matthew G. Krane drafted and executed and caused to be drafted and executed a series of false, fraudulent, and misleading fee agreements between Client H.S. and Quellos, wherein Client H.S. was led to believe that he would pay a specific Quellos entity identified in the agreements as “Quellos Financial Advisors LLC” or “QFA,” approximately $46 million for work in connection with the POINT transaction, whereas, in truth and fact, JEFFREY I. GREENSTEIN and CHARLES H. WILK, knew that they would divert a majority of those fees to Matthew G. Krane, Client H.S's own attorney.

47. It was further a part of the conspiracy that in or about October 2001, CHARLES H. WILK introduced Matthew G. Krane to J.S. and R.P. of Euram, and requested that J.S. and R.P. assist Matthew G. Krane in setting up an offshore entity and an offshore account for Matthew G. Krane.

48. It was further a part of the conspiracy that in or about October 2001, Matthew G. Krane, with the assistance of a Swiss associate, B.H., appropriated an existing offshore shell entity and changed its name to “QFS Consulting Ltd.”

49. It was further a part of the conspiracy that in or about October 2001, Matthew G. Krane, with the assistance of a Swiss associate, B.H., opened a bank account at European American Investment Bank A.G. in Vienna, Austria in the name of QFS Consulting Ltd.

50. It was further a part of the conspiracy that in or about October 2001, JEFFREY I. GREENSTEIN and CHARLES H. WILK agreed that the kickback payments for Matthew G. Krane would be paid not to Matthew G. Krane directly, but to QFS Consulting Ltd.

51. It was further a part of the conspiracy that JEFFREY I. GREENSTEIN, CHARLES H. WILK, and Matthew G. Krane knew and intended that the name of the foreign entity and foreign account controlled by Matthew G. Krane, “QFS Consulting Ltd.”, appeared very similar to a number of Quellos entities that were commonly known by acronyms starting with the letter “Q,” including but not limited to “QFA” (Quellos Financial Advisors, LLC), “QCS,” (Quellos Customs Strategies, LLC), “QBS,” (Quellos Brokerage Services, LLC), “QCM,” (Quellos Capital Management, LP), “QFV,” (Quellos Financial Ventures, LP), and “QCI” (Quellos Capital International). JEFFREY I. GREENSTEIN, CHARLES H. WILK, and Matthew G. Krane knew and intended that by using the name “QFS,” parties who were unaware of the kickback arrangement, including bank representatives overseeing the flow of funds, other advisors of Client H.S., and Client H.S. himself, would be mislead into believing that fees that were in truth diverted to Matthew G. Krane was paid to a Quellos entity consistent with the fee agreements signed by Client H.S.

52. It was further a part of the conspiracy that on or about October 24, 2001, CHARLES H. WILK instructed a bank to wire approximately $28 million into the “QFS” account in Vienna, Austria, knowing that the money was derived from fees Client H.S. believed he was paying Quellos.

53. It was further a part of the conspiracy that on or about October 25, 2001, CHARLES H. WILK instructed R.P. to wire approximately $8 million into the “QFS” account in Vienna, Austria, knowing that the money was derived from fees Client H.S. believed he was paying Euram.

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54. It was further a part of the conspiracy that in or about November 2001, after the funds had already been transferred, JEFFREY I. GREENSTEIN, CHARLES H. WILK, and Matthew G. Krane executed and caused to be executed a false, fraudulent, and misleading fee sharing agreement between Quellos and “QFS Consulting Ltd.” The agreement specified that Quellos would pay approximately $28 million to QFS Consulting for “certain advisory and consulting services,” which “did not constitute the provision of legal advice.”

55. It was further a part of the conspiracy that JEFFREY I. GREENSTEIN, CHARLES H. WILK, and Matthew G. Krane did not execute any written agreements to document or otherwise account for the additional $8 million that was wired to QFS on or about October 25, 2001.

56. It was further a part of the conspiracy that in 2001 and 2002, CHARLES H. WILK knowingly and willfully provided and caused to be provided false, fraudulent and misleading information to Law Firm B.C. LLP about the fees paid by Client H.S. in connection with the Titanium transaction, including providing false, fraudulent and misleading fee calculation documents that excluded large portions of fees paid to Quellos as well as the amounts paid to Matthew G. Krane.

E. *False and Fraudulent Tax Returns*.

57. It was further a part of the conspiracy that JEFFREY I. GREENSTEIN and CHARLES H. WILK caused Clients M.Z., R.J., B.J., M.S., and H.S. to file false and fraudulent income tax returns, specifically Form 1040s, claiming capital losses from the sale of the stocks within their respective SPVs which, in truth and fact, JEFFREY I. GREENSTEIN and CHARLES H. WILK knew did not exist.

58. It was further a part of the conspiracy that the following Quellos clients claimed the following false and fraudulent capital losses on their Form 1040s as a result of their participation in the POINT transactions:

Taxpayer	**Tax Year**	**Approx. Date of Filing**	**Approx. amount of Fraudulent Capital Loss**
Client M.Z.	2000	1/12/02	$122 million
Client R.J.	2000	12/27/01	$133 million
Client B.J.	2000	12/26/01	$178 million
Client M.S.	2000	4/15/01	$159 million
Client H.S.	2001	10/15/02	$730 million
Client M.S.	2001	10/16/02	$59 million

F. *False, Fraudulent, and Misleading Representations in Anticipation of and During POINT Clients' IRS Audits*

59. It was further a part of the conspiracy that sometime between 2003 and 2006, CHARLES H. WILK and JEFFREY I. GREENSTEIN knew that Clients M.Z., R.J., B.J., M.S., and H.S. were under or anticipated to be under IRS audit as a result of their participation in the POINT tax shelter strategy.

60. It was further a part of the conspiracy that CHARLES H. WILK, beginning in 2003 and continuing through 2005, when asked by the clients and clients' representatives for assistance responding to IRS inquires or anticipated IRS inquiries about the POINT transaction, provided and caused to be provided to such clients the same false, fraudulent, and misleading documents that purportedly described and documented the POINT transaction, including the “POINT Strategy” document and underlying transactional documents, such as the stock Purchase Agreements between Barnville and Jackstones, the Securities Lending Agreement between Barnville and Jackstones, and the Warrant Subscription Agreements purportedly executed by the SPVs.

61. It was a further part of the conspiracy that CHARLES H. WILK, beginning in 2003 and continuing through 2005,

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when asked by clients and clients' representatives for assistance in responding to the IRS inquires or anticipated IRS inquiries about the POINT transaction, knowingly and willfully made and caused to be made false, fraudulent, and misleading statements to clients' representatives, including the following:

a. In or about March 2003, CHARLES H. WILK falsely, fraudulently and misleadingly represented and caused to be represented to attorneys for Clients R.J. and B.J. that the source of the capital losses derived through the POINT transactions were shares of stock in a number of publicly traded companies that Barnville had contributed to the SPVs.

b. In or about March 2003, CHARLES H. WILK falsely, fraudulently and misleadingly represented and caused to be represented to attorneys for Clients R.J. and B.J. that Barnville formed the SPVs and contributed the securities to those SPVs for an independent business purpose, i.e. to issue “Covered Warrants” for which the SPVs received tens of millions of dollars in premiums.

c. In or about June 2004, CHARLES H. WILK falsely, fraudulently, and misleadingly represented and caused to be represented to the attorneys for Clients R.J. and B.J. that the only reason Quellos was unable to provide independent documentary evidence of the existence of stocks that were purportedly purchased by Barnville from Jackstones, such as brokerage statements or confirmations, was because Quellos did not have access to the internal records of Barnville and Jackstones, whereas, CHARLES H. WILK knew, in truth and fact, that the real reason Quellos could not provide such records was that no such stocks ever existed.

d. In or about October 2004, in response to demands by attorneys for Clients R.J. and B.J. that Quellos provide a written explanation of the transaction between Barnville and Jackstones to provide to the IRS, CHARLES H. WILK provided a false, fraudulent, and misleading written document in which he stated that Euram introduced Quellos to Barnville who happened to be holding a “stock portfolio”, and that Barnville contributed the “Stock” to the SPVs.

e. On or about November 15, 2004, in response to demands by Clients R.J. and B.J. to JEFFREY I. GREENSTEIN for a detailed step-by-step explanation of the transaction between Barnville and Jackstones, CHARLES H. WILK provided the clients with a false, fraudulent, and misleading letter in which he stated, among other things, that “....[Quellos was] not party to the original transactions (Purchase Agreements and Securities Lending Agreements) between Barnville and Jackstones, and therefore, this part of our step-by-step explanation is based on documentation we have reviewed”, whereas, CHARLES H. WILK knew, in truth and fact, that he and JEFFREY I. GREENSTEIN were involved in the original transactions between Barnville and Jackstones. CHARLES H. WILK knew that he and JEFFREY I. GREENSTEIN devised the sham sale and loan-back arrangement between Barnville and Jackstones, that JEFFREY I. GREENSTEIN, himself selected the very stocks that were to be used for the sham transactions, and CHARLES H. WILK and JEFFREY I. GREENSTEIN directed C.D., J.S. and R.P. to appropriate the companies and execute the transactions.

f. On November 15, 2004, CHARLES H. WILK further wrote in the letter to Clients R.J. and B.J. that “[t]he Purchase Agreements between Jackstones (as seller) and Barnville (as purchaser) reflect that Jackstones sold to Barnville the right to beneficial ownership of shares....” whereas CHARLES H. WILK knew, in truth and fact, that the Purchase Agreements falsely stated that actual shares were purchased, and that Barnville engaged in neither a transaction for the “right to beneficial ownership of shares” nor an actual stock purchase since the entire transaction with Jackstones was a sham.

g. In or about January 2005, CHARLES H. WILK, falsely, fraudulently, and misleadingly represented to attorneys for Client H.S. that Barnville was a “fund” that held a stock portfolio and that this fund was “discovered” by Euram, giving the false, fraudulent and misleading impression that Barnville held actual stock and that its stock portfolio pre-existed Quellos's involvement with the company, whereas CHARLES H. WILK knew, in truth and fact, that Barnville held no stock, and that JEFFREY I. GREENSTEIN and CHARLES H. WILK, together with Euram, appropriated Barnville and directed it to enter into sham Stock purchase agreements for the sole purpose of utilizing it in the POINT tax shelter strategy.

62. It was a further part of the conspiracy that beginning in or about April 2003 and continuing in or about October 2005, representatives of Clients M.Z., R.J., B.J., M.S., and H.S. responded to various IRS Information Document Requests (also known as “IDRs”) which sought explanations and documents relating to their respective POINT transactions

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by forwarding to the IRS the same false, fraudulent and misleading documents that had earlier been provided or caused to be provided by CHARLES H. WILK to such clients, including the “POINT Strategy” document and/or underlying transactional documents, such as the stock Purchase Agreements between Barnville and Jackstones, the Securities Lending Agreement between Barnville and Jackstones, and the Warrant Subscription Agreements purportedly entered into by the various SPVs.

G. *False, Fraudulent and Misleading Testimony During Senate Investigation*

63. It was further a part of the conspiracy that by 2006, the IRS had expanded a “promoter” examination of Quellos to include Quellos' role in the POINT transactions.

64. It was further a part of the conspiracy that in or about August 2006, JEFFREY I. GREENSTEIN, in an effort to continue to hide and conceal the true nature of the POINT tax shelter transactions from the IRS and others, knowingly and willfully gave the following false, fraudulent, and misleading testimony before the United States Senate Permanent Subcommittee on Investigations (hereinafter “PSI”) that was conducting an investigation into, among other things, the POINT transactions:

a. JEFFREY I. GREENSTEIN testified that the circular stock purchase and lending agreement entered into between Barnville and Jackstones through which the portfolio of loss stocks were generated was “not dissimilar to swaps or contract for differences or single stock futures,” in an effort to mislead the PSI and others into believing that Barnville and Jackstones engaged in legitimate derivative trades, whereas JEFFREY I. GREENSTEIN knew, in truth and fact, that the Barnville/Jackstones purchase and loan-back arrangement was a sham, paper transaction.

b. JEFFREY I. GREENSTEIN testified that the purported derivative nature of these transactions between Barnville and Jackstones was, to his understanding, disclosed in detail to clients and the clients' advisors, whereas JEFFREY I. GREENSTEIN knew, in truth and fact, that the clients and the clients advisors were never so informed, that none of the descriptions of the POINT transactions provided to the clients and clients advisors described the POINT transaction as such, that none of the transactional documents provided to the clients and the clients' advisors described the transactions between Barnville and Jackstones as such, that none of the opinion letters issued by Law Firm C.S. & M. LLP and Law Firm B.C. LLP described the Barnville and Jackstones transaction as such, and, to the contrary, all representations and materials provided to the clients and client representatives were designed and contrived to mislead them into believing that what Barnville purchased and contributed to the SPVs were actual stock.

c. JEFFREY I. GREENSTEIN testified that the Covered Warrants issued through each of the SPVs provided a potential for profit for the clients who participated in POINT, whereas JEFFREY I. GREENSTEIN knew, in truth and fact, that the Covered Warrants were sham transactions, and that no real premiums were paid or were ever going to be paid, and that the Covered Warrants never provided any profit potential to the clients who participated in POINT because each transaction was designed to be unwound and completed before the Clients could ever profit from such Covered Warrants.

IV. OVERT ACTS

65. In furtherance of the conspiracy and to effect the illegal objects thereof, JEFFREY I. GREENSTEIN and CHARLES H. WILK, and their co-conspirators, known and unknown, committed or caused to be committed the following overt acts, among others, in the Western District of Washington and elsewhere:

a. Beginning in or about August 4, 1999, and continuing through on or about August 11, 1999, JEFFREY I. GREENSTEIN and CHARLES H. WILK together drafted and edited the “POINT Strategy” document.

b. On or about August 30, 1999, CHARLES H. WILK sent an email to Partner L.S. at Law Firm C.S. & M. LLP, attaching the “POINT Strategy” document, which, according to CHARLES H. WILK, described the POINT transaction in its “most basic facts.”

c. On or about January 7, 2000, CHARLES H. WILK, with the knowledge and consent of JEFFREY I. GREENSTEIN,

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forwarded to Partner L.S. at Law Firm C.S. & M. LLP a document that purportedly described how the offshore fund originally obtained its stocks.

d. On or about January 14, 2000, JEFFREY I. GREENSTEIN sent an email to C.D., attaching a list of stocks that JEFFREY I. GREENSTEIN selected to generate the fake capital losses for the POINT transactions.

e. On or about January 19, 2000, JEFFREY I. GREENSTEIN sent an email to Partner L.S. of Law Firm C.S. & M. LLP, forwarding a schematic that purportedly explained the POINT transaction in diagram form. The schematic described the transaction as involving the transfer of "stock" from one entity to another entity.

f. On or about January 20, 2000, JEFFREY I. GREENSTEIN sent an email to an associate at Law Firm C.S. & M. LLP, who was assisting Partner L.S., attaching calculations purportedly demonstrating the potential profits and losses that could be incurred by a POINT investor from the Covered Warrants.

g. On or about January 24, 2000, JEFFREY I. GREENSTEIN and CHARLES H. WILK received by facsimile from Partner L.S. of Law Firm C.S. & M. LLP, a draft of Law Firm C.S. & M. LLP's opinion letter regarding the POINT transaction.

h. On or about February 2, 2000, JEFFREY I. GREENSTEIN, CHARLES H. WILK, C.D., and J.S. of Euram conducted a telephone conference call to discuss the POINT transaction, including, among other things, how Euram had "set up" the companies to be used to generate the sham portfolio; how the parties could increase the size of the sham portfolio to accommodate additional tax shelter clients; how Partner L.S. had not been fully informed as to the manner in which the sham portfolio was created; and the fact that the legal opinion issued by Partner L.S. regarding POINT could be viewed by the IRS as having been "predicated on a fact that [was] not true," specifically, regarding whether the SPVs owned any shares in stock.

i. On or about February 16, 2000, M.P., an individual in Britain, at the direction of C.D. and J.S., who were, in turn, following the instructions of JEFFREY I. GREENSTEIN and CHARLES H. WILK, met with the Isle of Man corporate administrators of Barnville and Jackstones. During the meeting, M.P. explained the following, which he learned from J.S. and C.D.:

1. Barnville and Jackstones were both beneficially owned by one individual, L.B., and that individuals at Quellos and Euram, with the permission of L.B., sought to appropriate Barnville and Jackstones for the purpose of executing a tax shelter strategy;

2. Barnville and Jackstones were being asked, in furtherance of this tax shelter strategy, to enter into a "virtual share transaction" in which Barnville buys a portfolio of non-existent stocks from Jackstones and Jackstones borrows those same shares from Barnville, resulting in no actual exchange of shares or exchange of money;

3. M.P. acknowledged to the administrators of Barnville and Jackstones that over time, as a result of this transaction, one party would have a large debt owed to the other on the books, but that in the end, because the two entities were beneficially owned by the same person, the companies could eventually be merged and any debts eliminated from the books;

4. M.P. stated that L.B. would benefit from allowing the entities to be utilized in this manner through the large fees that Euram was expecting to earn as a result of assisting in executing this transaction because L.B. was a shareholder in Euram; and

5. M.P. agreed that for assisting in the POINT strategy, the corporate administrators for each of the companies would receive a flat fee of £5000 in addition to normal costs and disbursements.

j. On or about February 29, 2000, JEFFREY I. GREENSTEIN emailed J.S. and C.D. another selection of stocks to be added to the sham portfolio being created between the two offshore companies for use in the POINT transactions.

k. On or about March 13, 2000, C.D. emailed JEFFREY I. GREENSTEIN that he was greatly disturbed by a meeting he had with an advisor for Client Rd. during which it was made clear to C.D. that this advisor had no idea how the loss stocks were generated, and C.D. demanded a formal letter from Quellos assuring Euram that they had fully informed POINT clients and their advisors of the manner in which the loss stocks were "created."

l. On or about March 13, 2000, JEFFREY I. GREENSTEIN responded to C.D. in an email stating that the advisor C.D.

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had met with had no involvement in advising Client R.J. in the POINT transaction, and that he was confident that Partner L.S. had fully advised the Client.

m. On or about March 29, 2000, CHARLES H. WILK and JEFFREY I. GREENSTEIN received from J.S. proposed transactional documents for the POINT transaction, including the sham stock Purchase Agreements and the Securities Lending Agreement to be executed between Barnville and Jackstones.

o. On or about April 4, 2000, J.S. emailed CHARLES H. WILK and asked whether the tax shelter clients and their advisors had been fully informed as to the true nature of the sham stock portfolio between Barnville and Jackstones as promised. CHARLES H. WILK responded that per the advice of Partner L.S., the clients should not be informed about the nature of how the shares were created and how they were contributed into the SPVs.

p. On or about April 5, 2000, J.S., in response to requests by the corporate administrator for Jackstones for written assurances from Quellos confirming that the POINT clients and their advisors were fully informed of the nature of the share trading transaction between the two offshore companies, stated that they were not able to provide any such written assurances. J.S. further explained that no such written assurances could be provided because Quellos was sensitive about "having anything in writing which suggests that the investment strategy contemplated for the client is completely preordained and exists only for the possibility of achieving a U.S. tax advantage."

q. In or about April 2000, CHARLES H. WILK edited and caused to be edited transactional documents for the POINT transaction, including the stock Purchase Agreement and the Securities Lending Agreement between Barnville and Jackstones.

r. On or about the following dates, JEFFREY I. GREENSTEIN and CHARLES H. WILK initiated and then unwound the following POINT transactions in order to generate the fake losses for the POINT clients:

Approx. Date Initiated	**Approx, Date Unwound**	**Client**	**Name of Transaction**
April 28, 2000	May 19, 2000	M.Z.	Torens
May 5, 2000	June 5, 2000	R.J.	Reka
May 10, 2000	June 5, 2000	B.J.	Burgundy
Nov. 29, 2000	Dec. 18, 2000	M.S.	Platinum
Sept. 24, 2001	Nov. 18, 2001	H.S.	Titanium
Nov 7, 2001	Dec. 10, 2001	M.S.	Cobalt

s. On or about the following dates, JEFFREY I. GREENSTEIN and CHARLES H. WILK caused Law Firm C.S. & M. LLP and Law Firm B.C. LLP to issue false, fraudulent and misleading opinion letters to each of the POINT Clients as follows:

Approx. Date	**Law Firm**	**Transaction**
Aug. 29, 2000	Law Firm C. S.& M LLP	Reka
Sept. 6, 2000	Law Firm C. S.& M LLP	Burgundy
Sept. 6, 2000	Law Firm C. S.& M LLP	Torens
Dec. 22, 2000	Law Firm C. S.& M LLP	Platinum
Dec. 14, 2001	Law Firm B.C. LLP	Cobalt
Oct. 14, 2002	Law Firm B.C. LLP	Titanium

t. Beginning on or about September 9, 2001, and continuing through September 20, 2001, CHARLES H. WILK informed J.S. through a series of emails and telephone conversations that in order for Euram to be paid for work on Client

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H.S.'s POINT transaction, they must enter into an advisory services agreement with Client H.S. despite the fact that Euram provided no advisory services to Client H.S.

u. On or about September 20, 2001, Matthew G. Krane and CHARLES H. WILK drafted an advisory agreement between Euram and Client H.S., backdated to appear to have been effectuated on May 1, 2001, wherein Client H.S. purportedly agreed to pay Euram fees for advising Client H.S. on European aspects of Client H.S.'s business holdings and forwarded the agreement to J.S. for signature.

v. In or about October 2001, CHARLES H. WILK and Matthew G. Krane telephoned J.S. seeking assistance in setting up a non-U.S, corporation and bank account for Matthew G. Krane.

w. On or about October 24, 2001, CHARLES H. WILK and Matthew G. Krane caused to be drafted and signed a final fee agreement between Quellos and Client H.S. in which Client H.S. agreed to pay a specific Quellos entity more than $46 million in fees for their work on Client H.S.'s transaction.

x. On or about October 24, 2001, CHARLES H. WILK by email directed a bank representative to divert approximately $28 million of Client H.S.'s $46 million in fees that had previously been instructed to go to Quellos to, instead, be deposited into an account in the name of “QFS”.

y. On or about October 24, 2001 and October 26, 2001, CHARLES H. WILK, with the knowledge of JEFFREY I. GREENSTEIN, directed J.S. and R.P. in emails to wire transfer approximately $8 million in additional fees collected from Client H.S. to an account in the name of “QFS”.

z. On or about November 5, 2001, JEFFREY I. GREENSTEIN signed on behalf of Quellos a fee splitting agreement, back-dated to October 25, 2001, in which Quellos agreed to pay “QFS Consultants Ltd.” approximately $28 million for services it rendered as an “independent advisor” in connection with Client H.S.'s transaction.

aa. On or about October 26, 2004, CHARLES H. WILK, in response to requests from the audit attorneys for Clients R.J. and B.J. for a written explanation of the POINT transaction, emailed a document in which CHARLES H. WILK explained that Euram introduced Quellos to Barnville, and that Barnville had in its possession a portfolio of stock that was ultimately contributed to the SPVs for use by the clients.

bb. On or about November 15, 2004, CHARLES H. WILK, in response to further requests by Clients R.J. and B.J. to JEFFREY I. GREENSTEIN for a written description and explanation of the POINT transaction, sent by facsimile a letter stating that Quellos was not a party to the original transaction between Barnville and Jackstones, but from an examination of the documents it appeared that Barnville obtained “rights to an underlying portfolio of stock.”

cc. On or about June 7, 2004, during a meeting with representatives of Client H.S. who were handling an audit of Client H.S., CHARLES H. WILK represented and caused to be represented that he had discovered Barnville during a trip to London and was told that it held losses in stocks that it could not use.

dd. On or about October 21, 2004, CHARLES H. WILK caused to be sent by email the “POINT Strategy” document purporting to describe the POINT transaction to the representatives of Client H.S. who were responding to an audit of the POINT transaction by state taxing authorities and who were also anticipating an audit by the IRS.

ee. On or about January 24 and 25, 2005, CHARLES H. WILK met with representatives of Client H.S. and represented that Euram found Barnville and Jackstones; that CHARLES H. WILK gave instructions to Euram to find loss stocks and did not think it would be so easy to find the loss stocks. CHARLES H. WILK further stated that while he had no additional information regarding the existence of the stocks, perhaps Client H.S.'s representatives could write a letter to Barnville and Jackstones asking for documentation. CHARLES H. WILK additionally stated that he did not know what advice Euram gave to Client H.S. to earn its fees and that he had simply referred Matthew G. Krane to Euram and they entered into a separate engagement. CHARLES H. WILK also represented that Euram got two fees.

ff. On or about August 1, 2006, JEFFREY I. GREENSTEIN testified under oath before the Permanent Subcommittee on Investigations of the Committee on Governmental Affairs United States Senate regarding POINT. JEFFREY I. GREENSTEIN testified that it appeared to him that Jackstones and Barnville engaged in a transaction “not dissimilar to swaps or contract for differences or single stock futures”, that the Covered Warrants provided clients with a potential for

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profit, and that it was his understanding that the clients and their advisors were made fully aware of the nature of the POINT transaction.

66. In furtherance of the conspiracy, and to accomplish one or more of its objects, one or more of the conspirators committed or caused to be committed the overt acts described in Counts 2-14 of this Superseding Indictment.

All in violation of Title 18, United States Code, Section 371.

COUNTS 2-9

(Tax Evasion)

67. The allegations set forth in paragraphs 1-65 of this Superseding Indictment are incorporated and re-alleged as if fully set forth herein.

68. From in or about June 1999 through at least about October 2005, in the Western District of Washington and elsewhere, JEFFREY I. GREENSTEIN and CHARLES H. WILK, unlawfully, willfully and knowingly did attempt to evade and defeat and aid and abet in the attempt to evade and defeat a substantial part of the income tax due and owing by the POINT tax shelter clients set forth below to the United States of America for the calendar years set forth below, by committing and causing to be committed the following affirmative acts, among others:

a. preparing and executing and causing to be prepared and executed false and fraudulent documents to deceive the IRS, including promotional documents purporting to describe the POINT transaction, transactional documents, and opinion letters;

b. creating and causing to be created entities to be used in executing the POINT tax shelter transaction;

c. preparing and filing, and causing to be prepared and filed, false and fraudulent tax returns; and

d. taking various steps to attempt to defeat the audit of the POINT tax shelter clients by causing clients' representatives to provide false, fraudulent and misleading information and documents to the IRS, purporting to describe and document their respective POINT transactions, including, but not limited to, the “POINT Strategy” document and/or underlying transactional documents, such as the stock Purchase Agreements between Barnville and Jackstones, Securities Lending Agreements between Barnville and Jackstones, and the Warrant Subscription Agreements purportedly entered into by the various SPVs.

Count	Client	Tax Returns	Approx. Amount of Fraudulent Tax Savings	Approx. Date of Filing
2	Client M.Z.	2000 Form 1040	$24 million	1/12/02
3	Client R.J.	2000 Form 1040	$18 million	12/27/01
4	Client R.J.	2003 Form 1040	$3 million	10/18/04
5	Client R.J.	2004 Form 1040	$2 million	10/18/05
6	Client B.J.	2000 Form 1040	$36 million	12/26/01
7	Client M.S.	2000 Form 1040	$32 million	4/15/01
8	Client H.S.	2001 Form 1040	$276 million	10/15/02
9	Client M.S.	2001 Form 1040	$11 million	10/16/02

All in violation of Title 26, United States Code, Section 7201 and Title 18, United States Code, Section 2.

COUNTS 10-14

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(Counseling False Tax Filings)

69. The allegations set forth in paragraphs 1-65 of this Superseding Indictment are incorporated and re-alleged as if fully set forth herein.

70. On or about the dates hereinafter set forth, in the Western District of Washington, and elsewhere, JEFFREY I. GREENSTEIN and CHARLES H. WILK, did willfully aid and assist in, and procure, counsel, and advise the preparation and presentation to the Internal Revenue Service, of U.S. Returns of Partnership Income, Forms 1065, for the partnership entities and calendar years hereinafter specified. The returns were false and fraudulent as to material matters, in that they represented and caused to be represented that the partnership entities were entitled under the provisions of the Internal Revenue laws to report the following capital losses in mounts hereinafter specified, whereas, as JEFFREY I. GREENSTEIN and CHARLES H. WILK then and there knew, the partnership entities were not entitled to report the capital losses in such amounts.

Count	Partnership	Tax Year	Approx. Date of Filing	Approx. amount of Fraudulent Capital Loss
10	Torens Limited	2000	10/24/01	$137 million
11	Reka Limited	2000	10/15/01	$137 million
12	Burgundy Limited	2000	10/15/01	$158 million
13	Titanium Trading Partners LLP	2001	10/15/02	$614 million
14	Cobalt Trading Partners LLP	2001	6/17/02	$54 million

All in violation of Title 26, United States Code, Section 7206(2).

COUNTS 15-17

(Wire Fraud)

71. Beginning at a time unknown, but no later than in or about June 1999 and continuing until in or about January 2005, in Seattle, Washington, within the Western District of Washington, and elsewhere, JEFFREY I. GREENSTEIN and CHARLES H. WILK, together with others known and unknown, did knowingly devise and intended to devise, and aided and abetted in devising, a scheme and artifice to defraud, and to obtain money and property by means of materially false and fraudulent pretenses, representations, and promises, and concealment of material facts, knowing that they were false and fraudulent when made, and transmitting and causing to be transmitted certain wire communications in interstate commerce for the purpose of executing the scheme.

I. INTRODUCTION.

72. The allegations set forth in paragraphs 2-18 of this Superseding Indictment are incorporated and re-alleged as if fully set forth herein.

II. ESSENCE OF THE SCHEME AND ARTIFICE TO DEFRAUD.

73. The essence of the scheme and artifice to defraud was for JEFFREY I. GREENSTEIN and CHARLES H. WILK to design, market and execute a fraudulent tax shelter known as POINT on behalf of wealthy individuals through which

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they could and did earn millions of dollars in fees, as well as retain the wealthy clients as investors in Quellos' various investment funds through which the company earned additional revenue. The scheme and artifice to defraud proceeded in two phases:

a. First, in order to induce clients to participate in the fraudulent tax shelter, JEFFERY I. GREENSTEIN and CHARLES H. WILK provided and caused to be provided false, fraudulent and misleading marketing documents, transactional documents, and false, fraudulent and misleading legal opinion letters from national law firms all of which described the transaction as involving the purchase of partnerships that owned low value/high basis “stocks,” whereas, JEFFREY I. GREENSTEIN and CHARLES H. WILK knew, in truth and fact, that the transactions did not involve any such stocks.

b. Second, JEFFREY I. GREENSTEIN and CHARLES H. WILK were aware that clients who executed the POINT tax shelter strategy would likely be subject to IRS audit. As such, JEFFREY I. GREENSTEIN and CHARLES H. WILK, in furtherance of the continuing scheme and artifice to defraud, provided and caused to be provided false, fraudulent and misleading representations and explanations about the POINT transactions to the clients in response to their requests for assistance with audits and anticipated audits in order to prevent detection of the scheme and artifice, and to prevent the loss of such clients as investors.

74. As a result of their scheme and artifice to defraud, a total of five individuals—Clients M.Z., R.J., B.J., M.S., and H.S.—paid approximately $86 million in fees to participate in POINT. Moreover, these clients also collectively invested tens of millions of dollars in various Quellos investment vehicles, earning Quellos substantial sums in additional fees.

III. MANNER AND MEANS OF THE SCHEME AND ARTIFICE TO DEFRAUD.

75. The manner and means of the scheme and artifice to defraud are set forth in paragraphs 20-65 of this Superseding Indictment, which are incorporated and re-alleged as if fully set forth herein.

IV. EXECUTION OF THE SCHEME AND ARTIFICE TO DEFRAUD.

76. On or about the dates set forth below, at Seattle, Washington, within the Western District of Washington, and elsewhere, having devised the above-described scheme and artifice to defraud, JEFFREY I. GREENSTEIN and CHARLES H. WILK, for the purpose of executing this scheme and artifice to defraud, did knowingly cause to be transmitted by wire communication in interstate or foreign commerce writings, signals, picture, and sounds, each transmission of which constitutes a separate count of this Superseding Indictment.

Count	Date	Sender	Recipient	Wire Transmission
15	10/21/04	Employee of Quellos	Attorney for Client H.S.	Email sent from Seattle, Washington to Los Angeles, California attaching the ‘POINT Strategy’ document, which falsely, fraudulently and misleadingly described the POINT transaction as involving the acquisition by the taxpayer of high/basis low value ‘stock’ that had been contributed to a partnership by an ‘offshore investment fund.’
16	10/26/04	CHARLES H. WILK	Attorney for Clients R.J. and B.J.	Email sent from Seattle, Washington to New York, New York

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				attaching a document entitled 'Barnville,' which falsely stated that Barnville contributed 'stock' to the SPV acquired by the clients.
17	11/15/04	CHARLES H. WILK	Clients R.J. and B.J.	Faxed letter sent from Washington D.C. to New York, New York in which CHARLES H. WILK falsely suggests that Quellos was not involved in the original transaction between Barnville and Jackstones; that the documents appear to indicate that Jackstones sold to Barnville 'the fight to beneficial ownership of shares....'

All in violation of Title 18, United States Code, Sections 1343 and 2.

COUNT 18

(Conspiracy to Launder Monetary Instruments)

77. Beginning at a time unknown, but no later than in or about March 2001, and continuing through in or about January 2008, at Seattle, Washington, within the Western District of Washington, and elsewhere, MATTHEW G. KRANE, JEFFREY I. GREENSTEIN, and CHARLES H. WILK, together with others known and unknown to the Grand Jury, did knowingly combine, conspire, and agree with each other to commit offenses against the United States in violation of Title 18, United States Code, Section 1956, to wit, to knowingly conduct and attempt to conduct a financial transaction affecting interstate and foreign commerce, which involved the proceeds of a specified unlawful activity, that is Deprivation of Honest Services Wire Fraud, in violation of Title 18, United States Code, Sections 1343 and 1346, knowing that the transactions were designed in whole or in part to conceal and disguise the nature, location, source, ownership, and control of the proceeds of specified unlawful activity, and that while conducting and attempting to conduct such financial transactions, knew that the property involved in the financial transactions represented the proceeds of some form of unlawful activity, in violation of Title 18, United States Code, Section 1956(a)(1)(B)(i).

I. INTRODUCTION.

At various times relevant to this Superseding Indictment:

78. The allegations set forth in paragraphs 2-18 of this Superseding Indictment are incorporated and re-alleged as if fully set forth herein.

79. Defendant MATTHEW G. KRANE was an attorney, licensed in the State of California. MATTHEW G. KRANE was a sole practitioner who specialized in the area of tax.

80. Client H.S. was a Los Angeles based business man. Beginning approximately in 1990 or 1991, MATTHEW G. KRANE was engaged by Client H.S. to provide tax advice and tax planning services to Client H.S. and Client H.S.'s business.

81. B.H. is a resident of Switzerland and a business associate of MATTHEW G. KRANE.

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II. THE ESSENCE OF THE SPECIFIED UNLAWFUL ACTIVITY: DEPRIVATION OF HONEST SERVICES WIRE FRAUD.

82. Attorneys practicing law in California owe both a fiduciary duty to their clients and a duty of loyalty to act in their clients' best interests, both financially and otherwise, and to comply with the California Rules of Professional Conduct.

83. Rule 3-310 of the California Rules of Professional Conduct requires that members of the California Bar “shall not accept or continue representation of a client without providing written disclosure to the client where...the member has or had a legal, business, financial, or professional interest in the subject matter of the representation.”

84. The essence of the Specified Unlawful Activity is that beginning in or about January 2001 and continuing through in or about December 2002, MATTHEW G. KRANE, knowingly and willfully devised and intended to devise a scheme and artifice to defraud, to obtain money and property by means of materially false and fraudulent pretenses, representations, promises, and omissions, and to deprive Client H.S. of his intangible right to honest services as his attorney.

85. It was part of the scheme and artifice to defraud that in late 2000, Client H.S. engaged MATTHEW G. KRANE to find a means to minimize anticipated capital gains taxes stemming from a sale of certain of Client H.S.'s assets.

86. It was a further part of the scheme and artifice to defraud that sometime in early 2001, MATTHEW G. KRANE introduced Client H.S. to Quellos and CHARLES H. WILK who, according to MATTHEW G. KRANE, had devised a financial transaction through which Client H.S. could shelter his capital gains.

87. It was a further part of the scheme and artifice to defraud that MATTHEW G. KRANE represented to Client H.S. that he would need to pay approximately $46 million in fees to Quellos for their work in implementing the transaction. MATTHEW G. KRANE represented that the fees were reasonable because the transaction would save Client H.S. substantially more in taxes than it cost.

88. It was a further part of the scheme and artifice to defraud that Client H.S., relying upon the advice and representations of MATTHEW G. KRANE that the transaction was legitimate and that the fees and costs were reasonable, agreed to enter into the tax shelter transaction with Quellos.

89. It was a further part of the scheme and artifice to defraud that, contrary to what MATTHEW G. KRANE represented to Client H.S. about the fee arrangements, MATTHEW G. KRANE, JEFFREY I. GREENSTEIN, and CHARLES H. WILK had entered into a separate agreement whereby JEFFREY I. GREENSTEIN and CHARLES H. WILK promised to kickback to MATTHEW G. KRANE more than half of the fees that Client H.S. agreed to pay Quellos.

90. It was a further part of the scheme and artifice to defraud that MATTHEW G. KRANE, contrary to his duties as Client H.S.'s attorney, never disclosed to Client H.S. the kickback arrangement he had entered into with JEFFREY I. GREENSTEIN and CHARLES H. WILK.

91. It was a further part of the scheme and artifice to defraud that MATTHEW G. KRANE knew about and participated with CHARLES H. WILK and others in creating false and misleading documents to hide from the Internal Revenue Service and others the true amount of fees and costs paid by Client H.S. to take part in the tax shelter transaction.

92. It was a further part of the scheme and artifice to defraud that in or about October and November 2001, when Client H.S.'s tax shelter transaction was completed, CHARLES H. WILK, in Seattle, Washington, in fulfillment of the kickback arrangement with MATTHEW G. KRANE, caused, by means of international wire transfers, the following payments totaling approximately $36 million:

a. On or about October 31, 2001, the transfer of approximately $28 million from HSBC Bank in New York, New York, to European American Investment Bank AG in Vienna, Austria, for the benefit of an account in the name of QFS Consultants, Ltd;

b. On or about October 25, 2001, the transfer of approximately $7.5 million from HSBC Bank in New York, New York, to European American Investment Bank AG in Vienna, Austria, which amount was further transferred on or about November 1, 2001, to another account in European American Investment Bank AG in Vienna, Austria for the benefit of an account in the name of QFS Consultants, Ltd.

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c. On or about November 7, 2001, the transfer of approximately $600,000 from HSBC Bank in New York, New York, to European American Investment Bank AG in Vienna, Austria, for the benefit of an account in the name of QFS Consultants, Ltd.

C. ***Manner and Means of the Conspiracy to Launder Monetary Instruments*****.**

93. The manner and means by which MATTHEW G. KRANE, JEFFREY I. GREENSTEIN, CHARLES H. WILK, and their coconspirators sought to accomplish the object of the conspiracy included, among other things, the following:

94. In or about October 2001, CHARLES H. WILK, who was working in Seattle, Washington, introduced MATTHEW G. KRANE to J.S. and R.P. in London, England, and requested that J.S. and R.P. assist MATTHEW G. KRANE in establishing an offshore company and an offshore bank account to hold MATTHEW G. KRANE's share of fees generated from Client H.S.'s tax shelter transaction.

95. In or about October 2001, MATTHEW G. KRANE and B.H. agreed that in return for a payment of $1 million, B.H. would act on behalf of MATTHEW G. KRANE as the sole beneficial owner of the offshore company to be set up through the assistance of J.S. and R.P.B.H. further agreed with MATTHEW G. KRANE that he would manage an offshore account in the name of this offshore company on MATTHEW G. KRANE's behalf.

96. In or about October 2001, B.H., through the assistance of R.P. and others, utilized a corporate administrator based in Gibraltar to obtain the use of a shell company known as Eldred Ltd., incorporated in the British Virgin Islands.

97. On or about October 24, 2001, at the behest of MATTHEW G. KR.ANE, B.H. instructed the corporate administrator of Eldred Ltd. to change the name of the company to QFS Consultants Ltd. QFS was similar to acronyms used by various subsidiaries of Quellos. MATTHEW G. KRANE chose the name QFS so that documents regarding fees that were, in truth, being paid to MATTHEW G. KRANE in fulfillment of the kickback arrangement with JEFFREY I. GREENSTEIN and CHARLES H. WILK, would fraudulently appear to others as if they were being paid to Quellos.

98. On or about October 24, 2001, at the behest of MATTHEW G. KRANE, B.H. opened a bank account in Vienna, Austria, at European American Investment Bank AG in the name of QFS.

99. On or about October 31, 2001, at the behest of MATTHEW G. KRANE, CHARLES H. WILK, from Seattle, Washington, emailed instructions to HSBC, a bank in New York, to transfer approximately $28 million from the fees generated from Client H.S.'s tax shelter transaction to the QFS account at European American Investment Bank AG in Vienna, Austria.

100. On or about October 25, 2001, approximately $28 million in proceeds from the above described scheme and artifice to defraud as set forth in paragraphs 82 through 92, was transferred via wire from an HSBC account in New York, New York, to an account in the name of QFS at European American Investment Bank AG in Vienna, Austria.

101. On or about October 25, 2001, at the behest of MATTHEW G. KRANE and consistent with the undisclosed fee sharing agreement as described in above paragraphs 82 through 92, CHARLES H. WILK, with the knowledge and consent of JEFFREY I. GREENSTEIN, emailed from Seattle, Washington, instructions to Euram, to transfer approximately $8 million in additional fees generated from Client H.S.'s tax shelter transaction that had been held in the name of Euram to the QFS account at European American Investment Bank AG in Vienna, Austria.

102. On or about November 1, 2001, in accordance with the instructions from CHARLES H. WILK, Euram caused approximately $7.5 million in proceeds from the above described scheme and artifice to defraud as set forth in paragraphs 82 through 92, to be transferred from an account in the name of Euram at European American Investment Bank AG in Vienna, Austria, to the account in the name of QFS at European American Bank AG in Vienna, Austria.

103. On or about November 7, 2001, in accordance with the instructions from CHARLES H. WILK, Euram caused approximately $600,000 in proceeds from the above described scheme and artifice to defraud as set forth in paragraphs 82 through 92, to be transferred from an account at HSBC in New York, New York, to the account in the name of QFS at European American Investment Bank AG in Vienna, Austria.

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104. In or about October 2001, in response to due diligence demands by the QFS corporate administrators for explanations as to the source of the $36 million in funds held by QFS, MATTHEW G. KRANE, CHARLES H. WILK and JEFFREY I. GREENSTEIN agreed to execute a written agreement wherein it was made to falsely appear that QFS, and not MATTHEW G. KRANE, obtained the money as a result of a fee-sharing agreement with Quellos for “non-legal” advisory services that QFS provided in connection with Client H.S.'s tax shelter transaction.

105. In or about October 2001, MATTHEW G. KRANE instructed B.H. to find someone wholly unrelated to Client H.S. and MATTHEW KRANE to sign the written fee-sharing agreement on behalf of QFS. B.H. agreed to do so, and caused an acquaintance in London, with no connections to Client H.S., MATTHEW KRANE, or QFS, to sign the agreement on behalf of QFS.

106. On or about November 5, 2001, B.H. faxed from Switzerland the written fee-sharing agreement between QFS and Quellos to Seattle, Washington, for execution of the agreement by Quellos.

107. On or about November 5, 2001, JEFFREY I. GREENSTEIN, in Seattle, Washington, executed the fee sharing agreement on behalf of Quellos, and CHARLES H. WILK caused the agreement to be faxed back to B.H. in Switzerland. B.H. then submitted the executed agreement to the QFS corporate administrators in fulfillment of their due diligence request.

108. By January 2002, the QFS corporate administrators continued to be dissatisfied with the explanation for the source of the $36 million held by QFS. In or about January 2002, in response to the corporate administrator's continued due diligence requests, MATTHEW G. KRANE and B.H. submitted and caused to be submitted a false document that falsely explained that the source of the QFS funds were fees from complex work done by B.H. in connection with the sale of Client H.S.'s assets. In truth, B.H. had done no work in connection with the sale of Client H.S.'s assets.

109. In or about January 2002, MATTHEW G. KRANE caused to be incorporated in the State of Delaware a new corporation known as Goldfiuegel Partnerschaft, LLC (hereinafter “Goldfluegel”).

110. In or about July 2002, MATTHEW G. KRANE caused to be opened a new bank account at European American Investment Bank AG in Vienna, Austria in the name of Goldfluegel.

111. On or about July 31, 2002, MATTHEW G. KRANE and B.H. instructed European American Investment Bank AG to transfer approximately $35 million in proceeds from the above described scheme and artifice to defraud held in the European American Investment Bank AG's QFS account to the new account in the name of Goldfluegel. MATTHEW G. KRANE and B.H. agreed that the remaining approximately $1 million in proceeds in the QFS account was for B.H.'s use in fulfillment of MATTHEW G. KRANE's agreement to pay B.H. for his involvement with QFS.

112. On or about the dates listed below, MATTHEW KRANE caused the following wire transfers from the European American Investment Bank AG's account in Vienna, Austria, in the name of Goldfleugel, to an account in the name of MATTHEW G. KRANE at Charles Schwab & Company, Inc. in San Francisco, California. These monetary transactions involved proceeds from the above described scheme and artifice. In an effort to disguise the purpose, source, and nature of these monetary transactions, MATTHEW G. KRANE caused each of the wired funds to be accompanied with a false notation that those amounts wore being paid to MATTHEW G. KRANE for “legal fees.”

Date of Wire Transfer	**Amount of Wire Transfer**
November 18, 2004	$86,259.77
February 23, 2005	$76,277.23
December 30, 2005	$124,939.52
April 12, 2006	$137,288.68
September 5, 2006	$198,814.07
February 8, 2007	$164,426.22
June 11, 2007	$192,049.93

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September 21, 2007	$65,587.06

All in violation of Title 18, United States Code, Section 1956(h).

ALLEGATION OF FORFEITURE

113. The allegations contained in Count 18 of this Superseding Indictment are hereby realleged and incorporated herein by reference for the purpose of alleging forfeiture to the United States pursuant to Title 18, United States code, section 982(a)(1)(A).

114. As a result of the money laundering offense, in violation of Title 18, United States Code, Section 1956(h) as alleged in Count 1 above, the defendant MATTHEW G. KRANE, shall forfeit to the United States the sum of $36 million as property involved in or traceable to the above-described money laundering violations.

115. If any of the forfeitable property, as a result of any act or omission of the Defendants

a. cannot be located upon the exercise of due diligence;

b. has been transferred or sold to, or deposited with, a third party;

c. has been placed beyond the jurisdiction of the Court;

d. has been substantially diminished in value; or

e. has been commingled with other property which cannot be subdivided without difficulty;

the United States of America shall be entitled to forfeiture of substitute property pursuant to Title 21, United States Code, Section 853(p), as incorporated by Title 18, United States Code, Section 982(b)(1) and Title 28, United States Code, Section 2461(c), including but not limited to the following:

The residence located at:
1451 Kings Road
Los Angeles, California 90069.

All pursuant to Title 18, United States Code, Sections 982(a)(1).

A TRUE BILL:

DATED: 6/04/2009

Signature of Foreperson redacted pursuant to the policy of the Judicial Conference of the United States.

FOREPERSON

/s/ JEFFREY C. SULLIVAN
United States Attorney

/s/ MARK BARTLETT
First Assistant United States Attorney

/s/ KATHERYN KIM FRIERSON
Assistant United States Attorney

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S.D. N.Y. No. 09 Cr. 213 (DC) June 26, 2009

UNITED STATES DISTRICT COURT SOUTHERN DISTRICT OF NEW YORK UNITED STATES OF AMERICA

v.

BERNARD L. MADOFF, Defendant.

PRELIMINARY ORDER OF FORFEITURE (FINAL AS TO THE DEFENDANT)

09 Cr. 213 (DC)

WHEREAS, Information 09 Cr. 213 (DC) ("Information"), filed March 10, 2009, charged BERNARD L. MADOFF, the defendant ("MADOFF" or the "defendant"), in eleven counts in connection with a scheme to defraud clients of Bernard L. Madoff Investment Securities ("BLMIS"), from at least as early as the 1980s through on or about December 11, 2008, by soliciting billions of dollars of funds under false pretenses, failing to invest investors' funds as promised, and misappropriating and converting investors' funds to MADOFF's own benefit and the benefit of others without the knowledge or authorization of the investors;

WHEREAS, the Information also contains two forfeiture allegations, the first of which concerns the offenses charged in Counts One, Three, Four, and Eleven of the Information, which constitute "specified unlawful activity" as that term is defined in 18 U.S.C. §1956(c)(7) (the "SUA Offenses"), and which seeks criminal forfeiture, pursuant to 18 U.S.C. §981 (a)(1)(C) and 28 U.S.C. §2461, of all property, real or personal, which constitutes or is derived from proceeds traceable to the commission of the SUA Offenses, and all property traceable to such property, and substitute assets, pursuant to 21 U.S.C. §853(p) (the "First Forfeiture Allegation");

WHEREAS, the second forfeiture allegation, concerning the money laundering offenses charged in Counts Five through Seven of the Information (the "Money Laundering Offenses"), seeks criminal forfeiture, pursuant to 18 U.S.C. §982(a) (1), of all property, real and personal, involved in the Money Laundering Offenses, and all property traceable to such property, and substitute assets, pursuant to 21 U.S.C. §853(p) (the "Second Forfeiture Allegation");

WHEREAS, the Government filed a notice pursuant to *United States v. Pimentel*, 932 F.2d 1029, 1034 (2d Cir. 1991), advising the defendant of its intent to seek criminal forfeiture (i) as alleged in the First Forfeiture Allegation, of all property constituting or derived from proceeds traceable to the commission of the SUA Offenses, including a money judgment in the amount of $170,000,000,000, representing the amount of proceeds traceable to the commission of the SUA Offenses, all property constituting or derived from proceeds traceable to the commission of the said offenses, all property traceable to such property, and substitute assets; (ii) as alleged in the Second Forfeiture Allegation, all property involved in the Money Laundering Offenses, including a money judgment in the amount of $799,000,000, representing the property involved in the Money Laundering Offenses, all property involved in the said offenses, all property traceable to such property, and substitute assets;

WHEREAS, on March 12, 2009, MADOFF pleaded guilty to all eleven counts in the Information;

WHEREAS, on or about March 16 and 17, 2009, the Office of the United States Attorney for the Southern District of New York (the "Office") filed notices that the property subject to forfeiture includes all right, title and interest of the defendant in certain property identified in the notices;

WHEREAS, the Court will sentence the defendant on June 29, 2009;

WHEREAS, the Government and the defendant stipulate that, if the Government were to apply for an order of criminal forfeiture to be imposed as part of the defendant's sentence, and the Court were to hold a hearing on the Government's claims for forfeiture:

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(i) the Government could prove by a preponderance of the evidence that the defendant is liable for a personal money judgment in the amount of $170,000,000,000, a sum of money representing the amount of property constituting or derived from proceeds traceable to the commission of the SUA Offenses charged in Counts One, Three, Four, and Eleven of the Information, and property traceable to such property, as alleged in the First Forfeiture Allegation; and

(ii) the Government could prove by a preponderance of the evidence that the defendant is further liable for a personal money judgment in the amount of $799,000,000, a sum of money representing the property involved in the Money Laundering Offenses charged in Counts Five through Seven of the Information, and property traceable to such property, as alleged in the Second Forfeiture Allegation;

WHEREAS, the Government represents that:

(i) subject to the provisions of paragraph (iii) below, the Government could prove by a preponderance of the evidence that any and all property and other interests belonging to, owed to or controlled in whole or in part by the defendant, and all property traceable to such property, has the requisite nexus to the SUA Offenses charged in Counts One, Three, Four, and Eleven of the Information and/or the Money Laundering Offenses charged in Counts Five through Seven of the Information, and is therefore forfeitable to the United States of America as property constituting or derived from proceeds traceable to the commission of the SUA Offenses charged in Counts One, Three, Four, and Eleven of the Information, and/or as property involved in the Money Laundering Offenses charged in Counts Five through Seven of the Information;

(ii) subject to the provisions of paragraph (iii) below, the Government could prove by a preponderance of the evidence that the property subject to forfeiture includes, but is not limited to, all right, title and interest of the defendant in the property listed in Exhibit A to this Order (the "Specific Property");

(iii) based on the readily provable facts available at the present time, the evidence at a hearing on the forfeitability of a portion of the approximately $14,500,000 combined equity in two assets listed in Exhibit A, to wit, all those shares of capital stock in 133 East 64th Street Corporation attributable to, and the proprietary lease for, Apartment 11A/12, 133 East 64th Street, New York, New York, which are held in the name of RUTH MADOFF and valued at approximately $7,500,000, and the real property known as 216 Old Montauk Highway, Montauk, New York, held in the name of BERNARD L. MADOFF and RUTH MADOFF as tenants by the entireties and valued at approximately $7,000,000 (collectively, the "New York Real Property"), would not establish the requisite nexus to either the SUA Offenses charged in Counts One, Three, Four, and Eleven of the Information or the Money Laundering Offenses charged in Counts Five through Seven of the Information;

WHEREAS, the defendant stipulates that the property subject to forfeiture as proceeds of the SUA Offenses and/or as property involved in the Money Laundering Offenses includes any and all property and other interests belonging to, owed to or controlled in whole or in part by the defendant, and all property traceable to such property, including, but not limited to, the Specific Property; provided, however, that the defendant does not concede that the Government could prove that the portion of the approximately $14,500,000 combined equity in the New York Real Property described in the preceding paragraph, and any and all personal property or other interests belonging to, owed to or controlled in whole or in part by the defendant (including, but not limited to, the Specific Property) that was purchased in or before 1985, and all property traceable to such property, is forfeitable to the United States of America as property constituting or derived from proceeds traceable to the commission of the SUA Offenses charged in Counts One, Three, Four, and Eleven of the Information, and/or as property involved in the Money Laundering Offenses charged in Counts Five through Seven of the Information;

WHEREAS, the Government and the defendant stipulate that any and all right, title and interest of the defendant in any and all personal property or other interests belonging to, owed to or controlled in whole or in part by the defendant, including, but not limited to, the Specific Property, that was purchased in or before 1985, and all property traceable to such property, and the portion of the approximately $14,500,000 combined equity in the New York Real Property (collectively, the "Substitute Assets") is nonetheless forfeitable to the United States as a substitute asset of the defendant, pursuant to 21 U.S.C. §853(p) and 18 U.S.C. §982(b);

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WHEREAS, the defendant consents to the terms of this Order and its entry against him;

WHEREAS, the Government intends to distribute, as soon as practicable, the net proceeds from the sale or other disposition of the property forfeited in this case to victims of the offenses described herein consistent with applicable Department of Justice regulations;

NOW, THEREFORE, IT IS ORDERED, ADJUDGED AND DECREED THAT:

1. Pursuant to 18 U.S.C. §981(a)(1)(C) and 28 U.S.C. §2461, and Rule 32.2(b)(1) of the Federal Rules of Criminal Procedure, and based on the foregoing, the Court finds by a preponderance of the evidence that the defendant BERNARD L. MADOFF is liable for a personal money judgment in the amount of $170,000,000,000, a sum of money representing the amount of proceeds obtained as a result of the SUA Offenses charged in Counts One, Three, Four, and Eleven of the Information.

2. Pursuant to 18 U.S.C. §981(a)(1)(A) and Rule 32.2(b)(1) of the Federal Rules of Criminal Procedure, and based on the foregoing, the Court finds by a preponderance of the evidence that the defendant BERNARD L. MADOFF is further liable for a personal money judgment in the amount of $799,000,000, as a sum of money representing the property involved in the Money Laundering Offenses charged in Counts Five through Seven of the Information.

3. Pursuant to 18 U.S.C. §981(a)(1)(A) and (a)(1)(C) and 28 U.S.C. §2461, and Rule 32.2(b)(1) of the Federal Rules of Criminal Procedure, and based on the foregoing, except as provided in paragraph 5 below, any and all property and other interests belonging to, owed to or controlled in whole or in part by the defendant, and all property traceable to such property, including, but not limited to, the Specific Property, has the requisite nexus to the SUA Offenses charged in Counts One, Three, Four, and Eleven of the Information and/or the Money Laundering Offenses charged in Counts Five through Seven of the Information, and is therefore forfeitable and is hereby forfeited to the United States of America as property constituting or derived from proceeds traceable to the commission of the SUA Offenses charged in Counts One, Three, Four, and Eleven of the Information, and/or as property involved in the Money Laundering Offenses charged in Counts Five through Seven of the Information.

4. All of the defendant's right, title and interest in the Specific Property, except as provided in paragraph 5 below, is hereby forfeited to the United States for disposition in accordance with law, subject to the provisions of 21 U.S.C. §853 (n)(1) and 18 U.S.C. §982(b)(1), and shall be applied to the Money Judgments imposed upon the defendant, as set forth in paragraphs 1 and 2, above, in partial satisfaction thereof.

5. Any and all interest of the defendant in the Substitute Assets is hereby forfeited to the United States pursuant to 21 U.S.C. §853(p) and 18 U.S.C. §982(b), and shall be applied to the Money Judgments to be entered against the defendant in partial satisfaction thereof.

6. The United States is hereby authorized to take possession of the Specific Property and the Substitute Assets (hereinafter collectively referred to as the "Subject Property") and to hold such property in its secure custody and control.

7. Pursuant to Rule G(4)(a) of the Supplemental Rules for Certain Admiralty and Maritime Claims and Asset Forfeiture Actions, the United States is permitted to publish forfeiture notices on the government internet site, www.forfeiture.gov. This site incorporates the forfeiture notices that have been traditionally published in newspapers. The United States forthwith shall publish the internet ad for at least thirty (30) consecutive days. Any person, other than the defendant, claiming interest in the Subject Property must file a Petition within sixty (60) days from the first day of publication of the Notice on this official government internet web site, or no later than thirty-five (35) days from the mailing of actual notice, whichever is earlier, pursuant to Rule G(5) of the Supplemental Rules for Admiralty or Maritime Claims and Asset Forfeiture Actions.

8. The published notice of forfeiture shall state that the petition (i) shall be for a hearing to adjudicate the validity of the petitioner's alleged interest in the Subject Property, (ii) shall be signed by the petitioner under penalty of perjury, and (iii) shall set forth the nature and extent of the petitioner's right, title or interest in the Subject Property, the time and circumstances of the petitioner's acquisition of the right, title and interest in the Subject Property, any additional facts supporting the petitioner's claim, and the relief sought, pursuant to 21 U.S.C. §853(n).

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9. The United States may also, to the extent practicable, provide direct written notice to any person known to have an alleged interest in the Subject Property, as a substitute for published notice as to those persons so notified.

10. Upon adjudication of all third-party interests, this Court will enter a final order of forfeiture pursuant to 21 U.S.C. §853(n) and 18 U.S.C. §982(b)(1), in which all interests will be addressed.

11. Pursuant to Rule 32.2(b)(3) of the Federal Rules of Criminal Procedure, this Order of Forfeiture shall be final against the defendant BERNARD L. MADOFF, shall be made part of the sentence of the defendant BERNARD L. MADOFF, and shall be included in the judgment of conviction therewith.

12. Pursuant to Rule 32.2(b)(3) of the Federal Rules of Criminal Procedure, upon entry of this Preliminary Order of Forfeiture the Office is authorized to conduct any discovery needed to identify, locate or dispose of property subject to forfeiture, including depositions, interrogatories, requests for production of documents and subpoenas, pursuant to Rule 45 of the Federal Rules of Civil Procedure.

13. If any of the Subject Property, as a result of any act or omission of the defendant, (a) cannot be located upon the exercise of due diligence; (b) has been transferred or sold to, or deposited with, a third party; (c) has been placed beyond the jurisdiction of the court; (d) has been substantially diminished in value; or (e) has been commingled with other property which cannot be divided without difficulty, any other property of the defendant up to the value of said property listed above as being subject to forfeiture is forfeitable as substitute property pursuant to 21 U.S.C. §853(p) and 18 U.S.C. §982(b).

14. As the defendant has stipulated and the Court has found that the property subject to forfeiture as proceeds of the SUA Offenses and/or as property involved in the Money Laundering Offenses includes any and all property and other interests belonging to, owed to or controlled in whole or in part by the defendant, and all property traceable to such property (excluding the Substitute Assets.), (i) this order of forfeiture entered against the defendant encompasses not only the Specific Property but also any and all property and other interests in which the defendant has or will acquire an interest (excluding the Substitute Assets), regardless of whether such property and other interests are extant or known to the Government or the defendant at the time of the entry of this Preliminary Order of Forfeiture or the final order of forfeiture to be entered against the defendant; and (ii) the defendant is hereby barred from challenging, or assisting a third party in challenging, the forfeiture of any such property at any time in any manner or forum.

15. In executing upon this order of forfeiture, the Government may use all remedies available to it pursuant to 21 U.S.C. §853 and 18 U.S.C. §982 and any other applicable federal law. If no such federal law exists, the Government may use all remedies available to it pursuant to the laws of New York State.

16. The Court retains jurisdiction to take additional action, enter further orders, and amend this and any future orders as necessary to implement and enforce this Order.

17. The Clerk of the Court shall forward four certified copies of this order to Assistant U.S. Attorney Barbara A. Ward, One St. Andrews Plaza, New York, New York, 10007.

SO ORDERED.

Dated: New York, New York

June 26, 2009

/s/

DENNY CHIN

United States District Judge

EXHIBIT A

1. All shares of capital stock in 133 East 64th Street Corporation (a cooperative housing corporation), attributable to, and the proprietary lease for, Apartment 11A/12 in the building located at 133 East 64th Street, New York, New York, 10021, which may be held in the name of Ruth Madoff and/or Bernard L. Madoff (valued at approximately $7,500,000),

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together with its appurtenances, improvements and fixtures and all valuable, insured or salable personal property contained therein, including, but not limited to:

a. All furniture, clocks, lamps, lighting fixtures and wall sconces, including those with an insured replacement value of approximately $1,754,811;

b. All musical instruments, including one Steinway piano with an insured replacement value of approximately $39,000;

c. All floor and window coverings, including those with an insurance replacement value of approximately $382,000;

d. All tableware and serving pieces, including that silverware and plate with an insurance replacement value of approximately $41,580, and that chinaware and glassware with an insured replacement value of approximately $16,910;

e. All paintings, prints, professional photographs, sculpture, and other artwork, including but not limited to that fine art with an insurance replacement value of approximately $1,634,100;

f. All linens and bedding, including but not limited to those with an insured replacement value of approximately $18,000;

g. All decorative objects, including but not limited to those with an insured replacement value of approximately $160,870;

i. All electronics and appliances;

2. All that lot or parcel of land, together with its buildings, appurtenances, improvements, fixtures, attachments and easements known as 216 Old Montauk Highway, Montauk, New York, 11954, held in the name of BERNARDL. MADOFF and Ruth Madoff as tenants by the entireties (valued at approximately $7,000,000), and all insured and salable personal property contained therein;

3. All that lot or parcel of land, together with its buildings, appurtenances, improvements, fixtures, attachments and easements known as 410 North Lake Way, Palm Beach, Florida, 33480, held in the name of Ruth Madoff (valued at approximately $7,450,000), and all insured and salable personal property contained therein, including, but not limited to:

a. All furniture, including but not limited to that with an insured replacement value of approximately $1,175,100;

b. All floor and wall coverings, including but not limited to those with an insurance replacement value of approximately $107,510;

c. All tableware and serving pieces, including but not limited to that silverware and metals with an insurance replacement value of approximately $8,505, and that chinaware and glassware with an insured replacement value of approximately $16,664;

d. All paintings, prints, professional photographs, sculpture, and other artwork, including but not limited to those with an insurance replacement value of approximately $858,150;

e. All decorative objects, including that having an insured replacement value of approximately $248,158;

g. All electronics and appliances;

4. $1,480,636.69 on deposit in the U.S. Marshals Service Seized Asset Fund, representing the net proceeds from the sale of all that lot or parcel of land, together with its buildings, appurtenances, improvements, fixtures, attachments and easements known as Chateau des Pins Villa 2, 279 Chemin de la Garoupe, Cap d' Antibes, France, 06600; and all insured and salable personal property contained therein;

5. One Leopard 23M Sport Yacht known as *Bull*, Hull No. 27, HIN IT ARNA 2327 K 202, approximately 23 meters long, 5.35 meters wide and 1.5 meters draft, and registered in the name of Yacht Bull Corp., George Town, Grand Cayman, Cayman Islands;

6. Any and all interest held in the name of Yacht Bull Corp., George Town, Grand Cayman, Cayman Islands, in Mooring Number 25, Port Gallice, Pointe du Crouton, Boulevard Baudoin, 06160, Juan-les-Pins, Cap d'Antibes, France;

7. One 2003 CH Marine Shelter Island Runabout Known as *Sitting Bull*, Hull Identification Number CQI38032F303, approximately 38 feet in length, and all electronics, equipment, appliances, and fixtures and all valuable, insured or salable personal property contained thereon;

8. One 1969 Rybovich Custom Motor Yacht Known as *Bull*, Hull Identification Number 522159, approximately 55

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feet in length, and all electronics, equipment, appliances, and fixtures and all valuable, insured or salable personal property contained thereon;

9. One Pathfinder Open Motorboat Known as *Little Bull*, Hull Identification Number MVIPH016C000, approximately 24 feet in length, and all electronics, equipment, appliances, and fixtures and all valuable, insured or salable personal property contained thereon;

10. One 2003 EZLO Trailer, Vehicle Identification Number IZEDAE5G03A003546, Florida License Number J521CF;

11. One 1999 Mercedes Benz CLK Class, vehicle identification number WDBLK65G9XT012137, Florida registration number K556WB, and all electronics, equipment, fixtures and valuable, insured or salable personal property contained therein;

12. One 2004 Volkswagen Touareg, vehicle identification number WVGEM77L34D077975, New York registration number CYC6394, and all electronics, equipment, fixtures and valuable, insured or salable personal property contained therein;

13. One 2001 Mercedes Benz E Class, vehicle identification number WDBJH82J71X043517, New York registration number BAR8009, and all electronics, equipment, fixtures and valuable, insured or salable personal property contained therein;

14. One 2006 Dark Grey Peugeot 206, with vehicle identification number VF32JNFUB47457280 (approximately $6,900);

15. All funds on deposit in any and all accounts at Wachovia Bank, N.A., held in the name of Ruth Madoff, and any accounts to which said funds have been transferred, and all funds traceable thereto, including but not limited to:

a. At least approximately $13,310,450 on deposit in account no. 1010219632245, f/k/a No. 1010146337325;

b. At least approximately $153,680 on deposit in account no. 1010192443920;

c. At least approximately $34,720 on deposit in account no. 1010219633516;

d. At least approximately $1,150 on deposit in account no. 1010219632779;

16. Any and all interest in COHMAD Securities Corporation, 885 Third Avenue, New York, New York, 10022, held in the name of Bernard Madoff, and all property traceable thereto; and

17. Any and all securities, funds and other property on deposit in Account No. 126-01070 in the name of Ruth Madoff at CCHMAD Securities Corp., 885 Third Avenue, New York, New York, 10022, including but not limited to, municipal bonds valued at approximately $46,665,673, and all property traceable thereto;

18. The contents of any and all safe deposit boxes held in the name or for the benefit of Bernard Madoff and/or Ruth Madoff, including, but not limited to, those held at Bank of New York Mellon, 706 Madison Avenue, New York, New York, 10021; and Box No. 151 at Wachovia Bank, N.A., Biltmore Galleria Financial Center, 285 Sunrise Avenue, Palm Beach, Florida, 33480;

19. Any and all ownership interest held in the name of Ruth Madoff and/or Bernard Madoff in the assets of any and all corporations, partnerships or other entities, and/or their subsidiaries, affiliates and joint ventures, including, but not limited to, the following:

a. Sterling Equity Partners;

b. Sterling American Property III LP;

c. Sterling American Property IV LP;

d. Sterling American Property V LP;

e. Sterling Acquisitions LLC;

f. Sterling/Carl Marks Capital;

g. Realty Associates Madoff II;

h. Hoboken Radiology LLC;

i. Delivery Concepts LLC;

j. The Clarke's Group LLC;

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k. PJ Clarke's on the Hudson LLC;
l. FINARF Germantown LLC;
m. Delta Ventures (Israel) and/or Delta Fund 1 LP;
n. Viager II LLC;
o. Laguardia Corporate Center Associates, LLC;
p. EB et al.;
q. W.D.I. LLC;
r. 4th & Forty, LLC;
s. DWD Associates, LLC;
t. Duhl & Mayer et al.;
u. Madoff La Brea LLC;
v. EZ Petshop.com, Inc. d/b/a PetCareRx, Inc.;
w. Bank Madoff;

20. Any and all loans or promissory notes in favor of Bernard L. Madoff and/or Ruth Madoff, as lender(s) and/or assignee (s), including but not limited to the following:

a. A May 24, 1999 unsecured promissory note for $1,000,080, executed by Allan Gary Klesch in favor of Bernard L. Madoff;

b. A March 25, 2000 promissory note for $1,100,000, executed by Mark Madoff in favor of Ruth Madoff, due March 31, 2001 ("given as a substitution in part of a Note dated December 4, 1994, in the principal sum of $1,000,000");

c. An October 31, 2000 demand promissory note for $5,491,525.35, executed by Peter B. Madoff as Manager of Madoff Technologies, L.L.C. in favor of Bernard L. Madoff;

d. A March 6, 2003 loan or other transfer of funds from Bernard L. Madoff in the amount of $1,500,000 to David Kugel,

e. A November 25, 2003 unsecured promissory note for $6,800,000, executed by Andrew Madoff in favor of Ruth Madoff, due November 30, 2007;

f. A March 1, 2004 unsecured promissory note for $3,200,000, executed by Mark Madoff in favor of Ruth Madoff, due February 29, 2008;

g. A July 8, 2004 demand promissory note for $2,000,500, executed by Peter B. Madoff as Manager of Madoff Family Fund LLC in favor of Bernard L. Madoff;

h. The balance due on a September 7, 2004 loan in the principal amount of approximately $1,000,000 to Steven Raven;

i. A May 1, 2005 demand promissory note for $1,000,000, executed by Peter B. Madoff as Manager of Madoff Family Fund LLC in favor of Bernard L. Madoff;

j. A June 17, 2005 unsecured promissory note for $6,000,000, executed by Mark Madoff in favor of Ruth Madoff, due May 31, 2010;

k. A December 31, 2005 unsecured promissory note for $5,000,000 (Restatement of Loan Agreement dated December 31, 2001, which in turn memorializes and modifies an unsecured Loan Agreement dated December 28, 1998, for $5,000,000), executed by Andrew Madoff in favor of Bernard L. Madoff, due December 31, 2010;

l. A December 31, 2005 unsecured promissory note for $5,000,000 (Restatement of Loan Agreement dated December 31, 2001, which in turn memorializes and modifies an unsecured Loan Agreement dated, December 28, 1998, for $5,000,000), executed by Mark Madoff in favor of Bernard L. Madoff, due December 31, 2010;

m. A December 31, 2005 unsecured promissory note for $2,500,000 executed by Peter B. Madoff in favor of Bernard L. Madoff, due December 31, 2010 (restating a loan agreement dated December 31, 2001);

n. An August 31, 2007 unsecured loan from Bernard L. Madoff for $1,000,000 to David Kugel at 6% interest;

o. A December 12, 2007 unsecured promissory note for $9,000,000, executed by Peter Madoff in favor of Bernard L. Madoff, due December 31, 2012 at 4.13% interest, and all property traceable thereto, including a 50% interest in BDG

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Yaphank, LLC and a 50% interest in BDG Leroy, LLC, held in the name of Peter Madoff and/or Essex Realty Development, LLC;

p. An April 24, 2008 unsecured loan from Bernard L. Madoff for $132,000 to Seth Hochman;

q. A June 16, 2008 unsecured promissory note for $6,500,000 executed by Mark Madoff and Stephanie Madoff in favor of Bernard L. Madoff, due June 30, 2013;

r. A May 8, 2008 loan or other transfer of funds in the amount of $2,800,000 from Bernard L. Madoff to Marion Madoff;

s. A June 27, 2008 loan or other transfer of funds in the amount of $720,000 from Bernard L. Madoff to Eric Lipkin;

t. A September 21, 2008 unsecured promissory note for $250,000, executed by Andrew Madoff in favor of Bernard L. Madoff, due August 31, 2012;

u. An October 6, 2008 unsecured promissory note for $4,300,000, executed by Andrew Madoff in favor of Bernard L. Madoff, due September 30, 2012; and

v. The balance due on a loan made by Bernard L. Madoff in or after 2005 in the principal amount of approximately $300,000 to Steven Raven;

21. Any and all jewelry owned or held in the name of Ruth Madoff, including that with an insurance replacement value of approximately $2,624,340;

22. Approximately 35 sets of watches and cuffiinks owned by Bernard Madoff;

23. One black dyed and sheared women's mink coat purchased from the J. Mendel salon at Bergdorf Goodman on or about November 16, 2003, appraised at $12,500;

24. One Russian sable fur three-quarter length coat, appraised at $36,000;

25. All salable apparel, accessories, footwear, leather goods, and luggage not otherwise identified herein;

26. All salable furniture, art, musical instruments, silverware and plate, chinaware, glassware, bedding, linens, decorative objects, electronics, appliances and other personal property not otherwise identified herein;

27. Any and all Social Security payments made to Bernard L. Madoff;

28. Any and all tax refunds paid to Bernard L. Madoff and/or Ruth Madoff attributable to assets and liabilities incurred through calendar year 2008;

29. Any and all income, including but not limited to investment income or dividends, paid to Bernard L. Madoff and/or Ruth Madoff;

30. The contents of Account No. 120-0202690 in the name of Bernard L. Madoff and Ruth Madoff at Bank of New York Mellon (approximately $22,000);

31. Travelers Life & Annuity life insurance policy no. 3596139, Bernard Madoff, Insured (cash surrender value approximately $50,000);

32. Travelers Life & Annuity life insurance policy no. 3732336, Bernard Madoff, Insured;

33. Phoenix Life Insurance Company policy no. 1,778,899, Bernard Madoff, Insured;

34. Any and all interest in any and all accounts at financial institutions held in the name of Bernard Madoff and/or Ruth Madoff, and all property traceable thereto, including, but not limited to, any and all accounts held at:

a. Lehman Brothers and/or the successor(s) thereto;

b. Morgan Stanley;

c. Bear Stearns and/or the successor(s) thereto; and

d. Fidelity.

Superseding Indictment in ‘United States v. Daugerdas'

S.D.N.Y.

No. S1 09 Cr. 581 (WHP)

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June 23, 2009

UNITED STATES DISTRICT COURT SOUTHERN DISTRICT OF NEW YORK UNITED STATES OF AMERICA

-v-

PAUL M. DAUGERDAS, ERWIN MAYER, DONNA GUERIN, DENIS FIELD, ROBERT GREISMAN, RAYMOND CRAIG BRUBAKER, and DAVID PARSE, Defendants. INDICTMENT

S1 09 Cr. 581 (WHP)

COUNT ONE

(Conspiracy—All Defendants)

The Grand Jury charges:

I. PERTINENT INDIVIDUALS AND ENTITIES

A. The Jenkens & Gilchrist Defendants and Co-Conspirator

1. Through on or about August 31, 1994, defendant PAUL M. DAUGERDAS, a lawyer and Certified Public Accountant ("CPA"), was a long-time tax partner at the accounting firm of Arthur Andersen LLP, in Chicago, Illinois. From in or about November 1994 until late December 1998, DAUGERDAS was a tax partner and head of the tax department at the Chicago law firm of Altheimer & Gray ("A&G"). On or about December 29, 1998, DAUGERDAS resigned from A&G and, commencing on or about January 1, 1999, became the managing shareholder of the newly-formed Chicago office of Jenkens & Gilchrist, PC ("J&G"), a law firm headquartered in Dallas, Texas. DAUGERDAS served as the Chicago office's managing shareholder and head of the Chicago tax practice at J&G until in or about April 2004. At both A&G and J&G, DAUGERDAS's tax practice centered around the design, marketing, and implementation of tax shelters.

2. At all times relevant to this Indictment, defendant ERWIN MAYER was a lawyer and an accountant, and defendant DONNA GUERIN was a lawyer and a CPA. From at least 1994 through late December 1998, MAYER and GUERIN were tax partners in A&G's Chicago office. In late December 1998, MAYER and GUERIN moved to the Chicago office of J&G as shareholders with defendant PAUL DAUGERDAS and other A&G lawyers. From at least 1994 (Title 26, United States Code, Section 7201.)

FORFEITURE ALLEGATION

117. As the result of committing the conspiracy offense in violation of Title 18, United States Code, Section 371, alleged in Count One of this Indictment, PAUL DAUGERDAS, ERWIN MAYER, DONNA GUERIN, DENIS FIELD, ROBERT GREISMAN, CRAIG BRUBAKER, and DAVID PARSE, the defendants, shall forfeit to the United States, pursuant to 18 U.S.C. §981(a)(1)(C) and 28 U.S.C. §2461, all property, real and personal, that constitutes or is derived from proceeds traceable to the commission of the offense, including but not limited to the following:

a. At least $180,000,000 in United States currency, in that such sum in aggregate is property representing the amount of proceeds obtained as a result of the conspiracy to commit the wire fraud offense contained in Count One, for which the defendants are jointly and severally liable;

I. PAUL DAUGERDAS

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b. All that lot or parcel of land, together with its buildings, appurtenances, improvements, fixtures, attachments and easements, located at 619 Cedar Point Drive, Williams Bay, Wisconsin 53191, more particularly described as a single-family home owned by PAUL M. DAUGERDAS and/or family members, either directly or indirectly;

c. All United States currency, funds, or other monetary instruments on deposit in account number 5300022551 in the name of PAUL M. DAUGERDAS at JP Morgan Chase;

d. All United States currency, funds, or other monetary instruments on deposit in account number 020-31659-2 in the name of Forest Investors LLC at Goldman Sachs & Co.:

e. All United States currency, funds, or other monetary instruments on deposit in account number 020-50725-7 in the name of Michael Paul Daugerdas at Goldman Sachs & Co.;

f. All United States currency, funds, or other monetary instruments on deposit in account number 03-375152 in the name of PMD Investments LLC at Fidelity;

g. All United States currency, funds, or other monetary instruments on deposit in account number 03-315540 in the name of Eleanor Daugerdas at Fidelity;

h. All United States currency, funds, or other monetary instruments on deposit in account number Z46-623261 in the name of Eleanor Spina Daugerdas Trust U/A 05/23/85 at Fidelity;

i. All United States currency, funds, or other monetary instruments on deposit in account number 766-9355530 in the name of PAUL M. DAUGERDAS at TD Ameritrade;

j. All United States currency, funds, or other monetary instruments on deposit in account number 06-78C3Z in the name of PMD Investments LLC at Morgan Stanley;

k. All United States currency, funds, or other monetary instruments on deposit in account number 5XR 122063 in the name of PMD Investments LLC at Deutsche Bank;

l. All United States currency, funds, or other monetary instruments on deposit in account number 3960-1400001511 in the name of PAUL M. DAUGERDAS liar the benefit of Nicole K. Daugerdas at Putnam Fiduciary Trust;

m. All United States currency, funds, or other monetary instruments on deposit in account number 3960-0488483198 in the name of PAUL M. DAUGERDAS for the benefit of Daniel W. Daugerdas at Putnam Fiduciary Trust;

n. All United States currency, funds, or other monetary instruments on deposit in account number 3968-0357819711 in the name of PAUL M. DAUGERDAS for the benefit of Michael P. Daugerdas at Putnam Fiduciary Trust;

o. All United States currency, funds, or other monetary instruments on deposit in account number 3973-0357661803 in the name of PAUL M. DAUGERDAS for the benefit of Alexander P. Jeffrey at Putnam Fiduciary Trust;

p. All United States currency, funds, or other monetary instruments on deposit in account number 3975-0357804838 in the name of PAUL M. DAUGERDAS for the benefit of Eleanor M. Daugerdas at Putnam Fiduciary Trust;

q. All United States currency, funds, or other monetary instruments on deposit in account number 3975-0357820510 in the name of PAUL M. DAUGERDAS for the benefit of Courtney M. Daugerdas at Putnam Fiduciary Trust;

r. All United States currency, funds, or other monetary instruments on deposit in account number 3976-0357817116 in the name of PAUL M. DAUGERDAS for the benefit of Megan A. Jeffrey at Putnam Fiduciary Trust;

s. All United States currency, funds, or other monetary instruments on deposit in account number 7232735006 in the name of PAUL M. DAUGERDAS at Fifth Third Bank; and

t. All right, title, and interest in Credit Suisse Catalytic Investors LP Fund held in the name of PAUL M. DAUGERDAS/Treasurex Financial;

II. ERWIN MAYER

u. All that lot or parcel of land, together with its buildings, appurtenances, improvements, fixtures, attachments and easements, located at 340 White Oak Lane, Winnetka, Illinois 60093, more particularly described as a single-family home owned by ERWIN MAYER and/or family members, either directly or indirectly; and

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v. A sum of at least $5,000,000 in securities, notes, United States currency, funds, or other monetary instruments, on deposit at Goldman Sachs & Co., in account numbers 020-68232-4, 020-27889-1, 020-27888-3, 020-27-887-5, 020-49539-6, 020-68233-2, and 020-30032-3, all held in the name of Maxoscar Investments LLC.

Substitute Asset Provision

118. If any of the above-described forfeitable property, as a result of any act or omission of the defendants:

(1) cannot be located upon the exercise of due diligence;

(2) has been transferred or sold to, or deposited with, a third person;

(3) has been placed beyond the jurisdiction of the Court;

(4) has been substantially diminished in value; or

(5) has been commingled with other property which cannot be subdivided without difficulty;

it is the intent of the United States, pursuant to 21 U.S.C. §853(p), to seek forfeiture of any other property of said defendants up to the value of the above forfeitable property.

(Title 18, United States Code, Section 981, and Title 28, United States Code, Section 2461.) /s/ FOREPERSON /s/ LEV L. DASSIN Acting United States Attorney Form No. USA-33s-274 (Ed. 9-25-58) UNITED STATES DISTRICT COURT SOUTHERN DISTRICT OF NEW YORK UNITED STATES OF AMERICA -v- PAUL M. DAUGERDAS, ERWIN MAYER, DONNA GUERIN, DENIS FIELD, ROBERT GREISMAN, RAYMOND CRAIG BRUBAKER, and DAVID PARSE, Defendants. INDICTMENT S1 09 Cr. 581 (WHP) (Title 18, U.S.C. §§371 and 2, Title 26, U.S.C. §§7201 and 7212(a)) LEV L. DASSIN Acting United States Attorney. A TRUE BILL /s/ Foreperson

6-4.210 Tax-Related Mail, Wire, or Bank Fraud, RICO, or Money Laundering Charges

The Tax Division must approve any and all criminal charges that a United States Attorney intends to bring against a defendant in connection with conduct arising under the internal revenue laws, regardless of which criminal statute(s) the United States Attorney proposes to use in charging the defendant. *See* USAM 6-4.200; 28 C.F.R. § 0.70. Thus, a United States Attorney must obtain Tax Division approval *before* bringing mail, wire or bank fraud charges, either alone or as the predicate to RICO or money laundering charges, if the conduct arises under the internal revenue laws. Conduct arising under the internal revenue laws includes a defendant's submission of a document or information to the IRS. A United States Attorney also must obtain Tax Division approval to bring charges based on state tax violations if the case involves parallel federal tax violations. *See* Tax Division Directive No. 128 (October 29, 2004), Tax Resource Manual 14.

A. Mail, Wire or Bank Fraud Charges. The Tax Division may approve mail, wire or bank fraud charges in tax- related cases involving schemes to defraud the Government or other persons if there was a large fraud loss or a substantial pattern of conduct and there is a significant benefit to bringing the charges instead of or in addition to Title 26 violations. *See generally* USAM 9-43.100. Absent unusual circumstances, however, the Tax Division will not approve mail or wire fraud charges if a case involves only one person's tax liability or when all submissions to the IRS were truthful.

Examples of situations where, with Tax Division approval, a United States Attorney may appropriately use mail, wire or bank fraud charges in a tax case include:

1) when a target has filed multiple fraudulent returns seeking tax refunds, using fictitious names, or using the names of real taxpayers without their knowledge, appropriate charges may include mail fraud (18 U.S.C. § 1341) or wire fraud (18 U.S.C. §1343);

2) when a target has promoted a fraudulent tax scheme, appropriate charges may include mail fraud (18 U.S.C. § 1341) or wire fraud (18 U.S.C. §1343);

3) when a target has induced a financial institution to approve refund anticipation loans on the basis of the fraudulent information submitted to the IRS, appropriate charges may include bank fraud charges (18 U.S.C. § 1344).

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The Government may derive significant benefits at different stages of the litigation by using mail, wire or bank fraud charges. First, at the charging stage, the charges may support the Government's effort to forfeit the proceeds of the fraud scheme or may enable the Government to describe the entire scheme in the indictment. Second, at trial, the charges may support the Government's presentation of all relevant evidence of the scheme or permit flexibility in the Government's choice of witnesses. And third, at sentencing, the charges may support the Government's efforts to obtain full restitution. *See* USAM 9-27.320(B)(3) ("If the evidence is available, it is proper to consider the tactical advantages of bringing certain charges.").

B. Racketeering and Money Laundering Charges Based on Tax Offenses. The Tax Division will not authorize the use of mail, wire or bank fraud charges to convert routine tax prosecutions into RICO or money laundering cases, but will authorize prosecution of tax-related RICO and money laundering offenses when unusual circumstances warrant such a prosecution. A United States Attorney who wishes to bring a RICO charge (18 U.S.C. § 1962) in any criminal matter arising under the internal revenue laws, must first obtain the authorization of the Tax Division and the Criminal Division's Organized Crime and Racketeering Section. *See* USAM 9-110.101. This requirement also applies to RICO cases where the predicate act is a state tax violation and there is a parallel federal violation. A United States Attorney who wishes to bring a money laundering charge (18 U.S.C. § 1956) based on conduct arising under the internal revenue laws, must first obtain the authorization of the Tax Division and, if necessary, the Criminal Division's Asset Forfeiture and Money Laundering Section. *See* USAM 9-105.300.

[updated September 2007] [cited in USAM 6-2,000]

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14. Tax Division Directive No. 128 (supersedes Directive No. 99) Charging Mail Fraud, Wire Fraud or Bank Fraud Alone or as Predicate Offenses in Cases Involving Tax Administration

Tax Division approval is required for any criminal charge if the conduct at issue arises under the internal revenue laws, regardless of the criminal statute(s) used to charge the defendant. Tax Division authorization is required before charging mail fraud, wire fraud or bank fraud alone or as the predicate to a RICO or money laundering charge for any conduct arising under the internal revenue laws, including any charge based on the submission of a document or information to the IRS. Tax Division approval also is required for any charge based on a state tax violation if the case involves parallel federal tax violations.

The Tax Division may approve mail fraud, wire fraud or bank fraud charges in tax-related cases involving schemes to defraud the government or other persons if there was a large fraud loss or a substantial pattern of conduct and there is a significant benefit to bringing the charges instead of or in addition to Title 26 violations. *See generally* United States Attorneys' Manual (U.S.A.M.) §9-43.100. Absent unusual circumstances, however, the Tax Division will not approve mail or wire fraud charges in cases involving only one person's tax liability, or when all submissions to the IRS were truthful.

Fraud charges should be considered if there is a significant benefit at the charging stage (*e.g.*, supporting forfeiture of the proceeds of a fraud scheme; allowing the government to describe the entire scheme in the indictment); at trial (*e.g.*, ensuring that the court will admit all relevant evidence of the scheme; permitting flexibility in choosing witnesses); or at sentencing (*e.g.*, ensuring that the court can order full restitution). *See id.* §9-27.320(B)(3) ("If the evidence is available, it is proper to consider the tactical advantages of bringing certain charges.").

For example, mail fraud (18 U.S.C. §1341) or wire fraud (18 U.S.C. §1343) charges may be appropriate if the target filed multiple fraudulent returns seeking tax refunds using fictitious names, or using the names of real taxpayers without their knowledge. Fraud charges also may be considered if the target promoted a fraudulent tax scheme.

Bank fraud charges (18 U.S.C. §1344) can be appropriate in the case of a tax fraud scheme that victimized a financial institution. Example: the defendant filed false claims for tax refund and induced a financial institution to approve refund anticipation loans on the basis of the fraudulent information submitted to the IRS.

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Racketeering and Money Laundering Charges Based on Tax Offenses

The Tax Division will not authorize the use of mail, wire or bank fraud charges to convert routine tax prosecutions into RICO or money laundering cases. The Tax Division will authorize prosecution of tax- related RICO and money laundering offenses, however, when unusual circumstances warrant it.

A United States Attorney who wishes to charge a RICO violation (18 U.S.C. §1962) in any criminal matter arising under the internal revenue laws— including a predicate act based on a state tax violation, in the case of a parallel federal tax violation—must obtain the authorization of the Tax Division and the Criminal Division's Organized Crime and Racketeering Section. U.S.A.M. §9-110.101.

A United States Attorney who wishes to bring a money laundering charge (18 U.S.C. §1956) based on conduct arising under the internal revenue laws must obtain the authorization of the Tax Division and, if necessary, the Criminal Division's Asset Forfeiture and Money Laundering Section. U.S.A.M. §9-105.300.

Date: October 29, 2004 ____________________
Eileen J. O'Connor
Assistant Attorney General
[Added September 2007] [cited in USAM 6-4.210]

U.S. DEPARTMENT OF JUSTICE TAX DIVISION CRIMINAL TAX MANUAL

2008

Nathan J. Hochman Assistant Attorney General Tax Division

John A. Marrella Deputy Assistant Attorney General (Criminal) Tax Division

Editor-in-Chief: Alan Hechtkopf Chief Criminal Appeals & Tax Enforcement Policy Section Tax Division

Managing Editor: Gregory V. Davis Trial Attorney Criminal Appeals & Tax Enforcement Policy Section Tax Division

Contributors

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7.00 *STATUTE OF LIMITATIONS*

7.01 *GENERALLY*

7.01[1] *Statutory Provisions*

This section gives a general overview of statute of limitations issues in criminal tax cases. For a more detailed discussion of a specific offense, reference should be made to the applicable chapter in this Manual.

Section 6531 of Title 26 controls the statute of limitations periods for most criminal tax offenses. This statute provides:

> No person shall be prosecuted, tried, or punished for any of the various offenses arising under the internal revenue laws unless the indictment is found or the information instituted within 3 years next after the commission of the offense, except that the period of limitations shall be 6 years --
>
> (1) for offenses involving the defrauding or attempting to defraud the United States or any agency thereof, whether by conspiracy or not, and in any manner;
>
> (2) for the offense of willfully attempting in any manner to evade or defeat any tax or the payment thereof;
>
> (3) for the offense of willfully aiding or assisting in, or procuring, counseling, or advising, the preparation or presentation under, or in connection with any matter arising under, the internal revenue laws, of a false or fraudulent return, affidavit, claim, or document (whether or not such falsity or fraud is with the knowledge or consent of the person authorized or required to present such return, affidavit, claim, or document);
>
> (4) for the offense of willfully failing to pay any tax, or make any return (other than a return required under authority of part III of subchapter A of chapter 61) at the time or times required by law or regulations;
>
> (5) for offenses described in sections 7206(1) and 7207 (relating to false statements and fraudulent documents);
>
> (6) for the offense described in section 7212(a) (relating to intimidation of officers and employees of the United States);
>
> (7) for offenses described in section 7214(a) committed by officers and employees of the United States; and
>
> (8) for offenses arising under section 371 of Title 18 of the United States Code, where the object of the conspiracy is to attempt in any manner to evade or defeat any tax or the payment thereof.

26 U.S.C. § 6531.

Thus, under Section 6531, the general rule is that a three-year statute of limitations exists for Title 26 offenses. However, a six-year period applies to certain excepted offenses. Section 6531 switches back and forth between enumerating the exception by specific Code reference and by a description of the offense. For example, 26 U.S.C. §§ 7206(1), 7207, 7212(a) and 7214(a) and 18 U.S.C. § 371 (conspiracy to evade taxes) are all specifically designated by Section 6531 as falling within the six-year exception. By contrast, willful failure to file an income tax return and willful failure to pay a tax, criminalized by 26 U.S.C. § 7203, are each designated as subject to the six-year exception solely by description of the offense.

Generally, the statute of limitations begins to run when an offense is completed. ***Toussie v. United States***, 397 U.S. 112, 115 (1970). Prosecutors should be aware that not all tax offenses are completed upon the filing of a tax return. For

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example, in a multiple-year tax evasion case where the affirmative acts of evasion include the subsequent filing of a single false amended return intended to evade all years' taxes, each crime is completed at the time the amended return was filed, not when the tax liabilities arose at the time each of the false original returns was filed. ***United States v. Thompson***, 518 F.3d 832, 856-57 (10th Cir. 2008), *petition for cert. filed*, 76 U.S.L.W. 3655 (U.S. Jun 9, 2008) (No. 07-1539); *see also* ***United States v. Goodyear***, 649 F.2d 226, 228 (4th Cir. 1981) (in evasion case in which the affirmative act of evasion is a subsequent false statement to IRS agents, crime is complete at time of false statement, not when false return is filed). Consequently, careful examination of the various elements is required to determine when a specific tax offense is completed.

7.01[2] ***Limitations Periods for Common Tax Offenses***

Description of Offense	***Code Section***	***Statute of Limitations***	***Code Section***
Tax Evasion	26 U.S.C. § 7201	6 years	26 U.S.C. § 6531(2)
Failure to Collect, Account For or Pay Over	26 U.S.C. § 7202	6 years[1]	26 U.S.C. § 6531(4)
Failure to Pay Tax	26 U.S.C. § 7203	6 years	26 U.S.C. § 6531(4)
Failure to File a Return	26 U.S.C. § 7203	6 years[2]	26 U.S.C. § 6531(4)
Failure to Keep Records	26 U.S.C. § 7203	3 years	26 U.S.C. § 6531
Failure to Supply Information	26 U.S.C. § 7203	3 years	26 U.S.C. § 6531
Supplying False Withholding Exemption Certificate	26 U.S.C. § 7205	3 years	26 U.S.C. § 6531
Filing a False Tax Return	26 U.S.C. § 7206(1)	6 years	26 U.S.C. § 6531(5)
Aid or Assist in Preparation or Presentation of False Tax Return	26 U.S.C. § 7206(2)	6 years	26 U.S.C. § 6531(3)
Deliver or Disclose False Document	26 U.S.C. § 7207	6 years	26 U.S.C. § 6531(5)
Attempt to Interfere With Administration of Internal Revenue Laws	26 U.S.C. § 7212(a)	6 years[3]	26 U.S.C. § 6531(6)
Conspiracy to Commit Tax Evasion	18 U.S.C. § 371	6 years	26 U.S.C. § 6531(8)
Conspiracy to Defraud the Internal Revenue Service	18 U.S.C. § 371	6 years	26 U.S.C. § 6531(1)
False Claim for Refund	18 U.S.C. § 286/287	6 years[4]	26 U.S.C. § 6531(1)
False Statement	18 U.S.C. § 1001	5 years	18 U.S.C. § 3282

7.02 ***TRIGGERING OF STATUTE OF LIMITATIONS***

7.02[1] ***Filing a False Tax Return***

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7.02[1][a] ***General Rule***

The general rule is that the statute of limitations for the filing of a false tax return starts on the day the return is filed. ***United States v. Habig***, 390 U.S. 222, 223 (1968); ***United States v. Kelly***, 864 F.2d 569, 574 (7th Cir. 1989). However, if the return is filed early (*i.e*., before the statutory due date), the statute of limitations does not start to run until the statutory due date. 26 U.S.C. § 6513(c) (1); ***Habig***, 390 U.S. at 225; ***United States v. Marrinson***, 832 F.2d 1465, 1475-76 (7th Cir. 1987). For example, if a tax return that is due to be filed on April 15, 2009, is filed early on February 26, 2009, the statute of limitations on the return would not begin to run until April 15, 2009.

Conversely, if a return is filed late (*i.e*., after the statutory due date), the statute of limitations begins running the day the return is filed. ***Habig***, 390 U.S. at 223-25; ***United States v. Anderson***, 319 F.3d 1218, 1220-21 (10th Cir. 2003). Thus, if a return that was due on April 15, 2008, was filed late on June 1, 2008, the statute of limitations began to run on June 1, 2008.

In cases where an extension of time to file at a later date has been obtained, the statute of limitations begins to run from the date the return is filed, regardless of whether it was filed before or after the extension date. ***Habig***, 390 U.S. at 225-27. Thus, where a return was initially due on April 16, 2007, and the taxpayer was granted an extension to October 16, 2007, and actually filed on October 1, 2007, the statute of limitations started to run on October 1, 2007. Similarly, if the extension was to October 16, 2007, and the return was filed November 1, 2007, the statute of limitations began to run on November 1, 2007.

The statutory due date for filing a return depends upon the type of tax and the return involved. Section 6072 of Title 26 sets out the statutory due dates for the filing of various tax returns. Individual income tax returns made on a calendar year basis are due on April 15th of the following year. 26 U.S.C. § 6072(a). Individual returns made on a fiscal year basis are due on the fifteenth day of the fourth month of the following fiscal year. 26 U.S.C. § 6072(a). Corporate returns made on a calendar year basis are due on March 15th of the following year. 26 U.S.C. § 6072 (b). Corporate returns made on a fiscal basis are due on the fifteenth day of the third month of the following fiscal year. 26 U.S.C. § 6072(b). Other types of returns may have unusual rules applicable only to the particular type of return.

7.02[1][b] ***Definition of Timely Filed***

A tax return is generally considered timely filed if it is received by the IRS on or before the due date of the return. Typically, when a return is received on or before the statutory due date, it is not date stamped by the IRS upon receipt. However, in cases in which a return is filed after the statutory due date, the return is date stamped on the date it is received by the Service Center. This date then becomes the date of filing for statute of limitation purposes.

Prosecutors should be aware of the timely mailed/timely filed exception to the general rule. Section 7502 of Title 26 deems the date of mailing by the taxpayer (as opposed to the date of receipt by the IRS) to be the date of filing if (1) the return is sent by U.S. Mail and contains a U.S. postmark that is dated on or before the statutory due date, (2) the return is deposited in the mail addressed to the appropriate IRS office with postage prepaid, and (3) the return is delivered to the IRS after the date it was due. 26 U.S.C. § 7502(a). [FN5]

In these circumstances, the return may be date stamped after the statutory due date and still be deemed timely filed under Section 7502. Typically, the IRS will retain the envelope in which the return was mailed only if the return was filed after the due date.

7.02[2] ***Failing to File a Tax Return***

Generally, the statute of limitations does not begin to run until the crime is complete. ***Toussie v. United States***, 397 U.S. 112, 115 (1970). In cases in which the defendant has failed to file a tax return, the statute of limitations begins to run when the return is due. ***United States v. Phillips***, 843 F.2d 438, 443 (11th Cir. 1988). For example, if a defendant did

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not file a tax return that was due to be filed on April 15, 2008, the statute of limitations on the return began to run on that date.

If a defendant has obtained a valid extension of time to file a tax return, there is no duty to file until the extension date. ***Phillips***, 843 F.2d at 442-43. Thus, if a defendant obtained an extension to file from April 16, 2007, to October 16, 2007, and failed to file on or before the extended due date, the statute of limitations began to run on October 16, 2007. The extension date applies only if the extension is valid. An invalid, untimely application for automatic extension does not extend the statute of limitations beyond the statutory due date. *See* ***Phillips***, 843 F.2d at 443.

Section 6081 of Title 26 governs extensions. The regulations promulgated under Section 6081 detail the application procedures and lengths of extensions for various types of returns. Treas. Reg. (26 C.F.R.) § 1.6081-1, *et seq.* The regulations provide for an automatic extension of time for filing individual income tax returns that varies in length depending upon the tax year involved. For individual returns filed before January 1, 2006, the regulations provided for a four-month automatic extension. Treas. Reg. § 1.6081-4(a)(1) (1983), *superseded by* Temp. Treas. Reg. § 1.6081-4T(a) (2005). For individual returns filed on or after January 1, 2006, the regulations provide for a six-month automatic extension for the filing of personal income tax returns. Temp. Treas. Reg. § 1.6081-4T(a) (2005), *superseded by* Treas. Reg. § 1.6081-4(a) (2008). Prosecutors should be aware that an automatic extension of time does not operate to extend the time for the payment of any tax due on the return. Treas. Reg. § 1.6081-4(c) (2008); Treas. Reg. § 1.6081-4(b) (1983). Thus, an extension request is valid only when accompanied by payment of the taxpayer's estimated tax liability. Treas. Reg. § 1.6081-4(a)(4) (as amended in 2008).

7.02[3] ***Tax Evasion***

In order to commit tax evasion, the defendant must commit some affirmative act to evade a tax. While this act most often is the filing of a false tax return, it may also be "any conduct, the likely effect of which would be to mislead or conceal." ***Spies v. United States***, 317 U.S. 492, 499 (1943).

The general rule is that the statute of limitations for tax evasion begins to run on the date the last affirmative act took place or the statutory due date of the return, whichever is later. ***United States v. Carlson***, 235 F.3d 466, 470 (9th Cir. 2000); ***United States v. Hunerlach***, 197 F.3d 1059, 1065 (11th Cir. 1999); ***United States v. Wilson***, 118 F.3d 228, 236 (4th Cir. 1997); ***United States v. Dandy***, 998 F.2d 1344, 1356 (6th Cir. 1993); ***United States v. Payne***, 978 F.2d 1177, 1179 (10th Cir. 1992); ***United States v. DiPetto***, 936 F.2d 96, 98 (2d Cir. 1991). Thus, in a case in which the affirmative act of evasion is the filing of a false tax return, the statute of limitations begins to run on the date the return is filed or the statutory due date, whichever is later. In a case where a false return is filed and there is an affirmative act of evasion occurring after the filing date, the statute of limitations starts to run on the date the last affirmative act took place or the statutory due date, whichever is later. ***United States v. Thompson***, 518 F.3d 832, 856-57 & n.13 (10th Cir. 2008), *petition for cert. filed*, 76 U.S.L.W. 3655 (U.S. Jun 9, 2008) (No. 07-1539); ***United States v. Hunerlach***, 197 F.3d 1059, 1065 (11th Cir. 1999); ***United States v. Dandy***, 998 F.2d at 1355; ***United States v. Ferris***, 807 F.2d 269, 271 (1st Cir. 1986); ***United States v. Trownsell***, 367 F.2d 815, 816 (7th Cir. 1966). For example, if a false 2000 tax return was timely filed on April 16, 2001, and, on September 15, 2002, the defendant engaged in further affirmative acts of evasion (*e.g.*, lying to IRS agents) regarding his 2000 taxes, the statute of limitations began to run on September 15, 2002.

Further, in cases in which no return is filed and some other act constitutes the affirmative act of evasion, the statute of limitations begins to run on the date the last affirmative act took place or the statutory due date of the return, whichever is later. *See* ***Carlson***, 235 F.3d at 470; ***Payne***, 978 F.2d at 1179 & n.2; ***United States v. Winfield***, 960 F.2d 970, 973-74 (11th Cir. 1992); ***DiPetto***, 936 F.2d at 98. For example, if a 2000 tax return that was due to be filed on April 16, 2001, was not filed by the defendant, and, on June 6, 2000, the defendant had committed an act of evasion (*e.g.*, filing a false Form W-4 exemption certificate) relating to his 2000 taxes, the statute of limitations started to run on April 16, 2001. Conversely, if a 2000 tax return that was due to be filed on April 16, 2001, was not filed by the defendant and, on

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December 1, 2003, the defendant committed an act of evasion (*e.g*., lying to agents of the IRS) relating to her 2000 taxes, the statute of limitations started to run on December 1, 2003.

7.02[4] ***Conspiracy***

The statute of limitations for a conspiracy to evade taxes, under the offense clause of Section 371, is six years. Similarly, the statute of limitations for a ***Klein*** conspiracy, under the defraud clause of Section 371, is six years. Both of these offenses are controlled by 26 U.S.C. § 6531. Occasionally, a defendant charged with a tax conspiracy under Section 371 will argue that the five-year statute of limitations generally applicable to Title 18 offenses [FN6] should apply to Section 371. The courts have routinely rejected this position and affirmed the application of the six-year limitations period to tax conspiracies. *See* ***United States v. Aracri***, 968 F.2d 1512, 1517 (2d Cir. 1992); ***United States v. Waldman***, 941 F.2d 1544, 1548 (11th Cir. 1991); ***United States v. Pinto***, 838 F.2d 426, 435 (10th Cir. 1988); ***United States v. White***, 671 F.2d 1126, 1133-34 (8th Cir. 1982); ***United States v. Brunetti***, 615 F.2d 899, 901-02 (10th Cir. 1980); ***United States v. Fruehauf Corp***., 577 F.2d 1038, 1070 (6th Cir. 1978); ***United States v. Lowder***, 492 F.2d 953, 955-56 (4th Cir. 1974).

The statute of limitations in a conspiracy begins to run from the date of the last overt act proved. ***Grunewald v. United States***, 353 U.S. 391, 397 (1957). The government is not required to prove,, however, that each member of a conspiracy committed an overt act within the statute of limitations. ***Hyde v. United States***, 225 U.S. 347, 369-70 (1912); *see also* ***United States v. Read***, 658 F.2d 1225, 1234 (7th Cir. 1981) (interpreting the ***Hyde*** decision). Once the government shows that a member joined the conspiracy, his continued participation in the conspiracy is presumed until the object of the conspiracy has been achieved. *See, e.g.,* ***United States v. Schorovsky***, 202 F.3d 727, 729 (5th Cir. 2000); ***United States v. Barsanti***, 943 F.2d 428, 437 (4th Cir. 1991); ***United States v. Juodakis***, 834 F.2d 1099, 1103-04 (1st Cir.1987); ***United States v. Finestone***, 816 F.2d 583, 589 (11th Cir. 1987); ***United States v. Krasn***, 614 F.2d 1229, 1236 (9th Cir. 1980); ***United States v. Panebianco***, 543 F.2d 447, 453 (2d Cir. 1976). [FN7]

However, a showing of withdrawal before the limitations period (*i.e*., more than 6 years prior to the indictment, where the limitations period is 6 years) is a complete defense to conspiracy. ***Read***, 658 F.2d at 1233. The defendant carries the burden of going forward to establish this affirmative defense. ***United States v. Lash***, 937 F.2d 1077, 1083 (6th Cir. 1991) ; ***Juodakis***, 834 F.2d at 1102-03; ***Finestone***, 816 F.2d at 589; ***Krasn***, 614 F.2d at 1236; ***United States v. Boyd***, 610 F.2d 521, 528 (8th Cir. 1979); ***United States v. Parnell***, 581 F.2d 1374, 1384 (10th Cir. 1978); ***United States v. Borelli***, 336 F.2d 376, 385 (2d Cir. 1964). The government, however, retains the burden of persuasion. ***United States v. West***, 877 F.2d 281, 289 (4th Cir. 1989) (government retains burden of persuasion); ***United States v. Jannoti***, 729 F.2d 213, 221 (3d Cir. 1984) (initial burden on defense, then shifted to government); ***Read***, 658 F.2d at 1236 (burden of production on defendant; burden of persuasion remains on government to negate withdrawal defense); ***Manual of Model Criminal Jury Instructions for the Ninth Circuit***, Instruction No. 8.19 (2003) (following ***Read***).

The courts have held that mere cessation of activity is insufficient to prove withdrawal. Rather, some sort of affirmative action to defeat the object of the conspiracy is required. *See, e.g.,* ***Lash***, 937 F.2d at 1083; ***Juodakis***, 834 F.2d at 1102; ***Finestone***, 816 F.2d at 589; ***United States v. Gonzalez***, 797 F.2d 915, 917 (10th Cir. 1986); ***Krasn***, 614 F.2d at 1236.

7.03 ***TOLLING PROVISION: FUGITIVE OR OUTSIDE U.S.***

Section 6531 of Title 26 contains its own tolling provision. The statute provides:

> The time during which the person committing any of the various offenses arising under the internal revenue laws is outside the United States or is a fugitive from justice within the meaning of section 3290 of Title 18 of the United States Code, shall not be taken as any part of the time limited by law for the commencement of such proceedings.

26 U.S.C. § 6531. Thus, the statute of limitations in Title 26 cases can be tolled if the defendant is outside the United States or is a fugitive.

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"Outside the United States" and "fugitive from justice" are interpreted in the disjunctive. Mere absence from the United States without any intent to become a fugitive is sufficient to toll the statute of limitations. *See* ***United States v. Marchant***, 774 F.2d 888, 892 (8th Cir. 1985). In ***Marchant***, for example, the Eighth Circuit held that defendant's eleven-day health and pleasure trip to Switzerland tolled the statute of limitations under 26 U.S.C. § 6531. According to the court, persons are "outside the United States," as that term is used in Section 6531, whenever they cannot be served with criminal process within the jurisdiction of the United States under Rule 4(d)(2) of the Federal Rules of Criminal Procedure. ***Marchant***, 774 F.2d at 892.

The "fugitive from justice" clause in Section 6531 refers to 18 U.S.C. § 3290, which provides: "No statute of limitations shall extend to any person fleeing from justice." The circuits are split as to the intent required under this statute. The majority rule, as adopted by the First, Second, Fifth, Sixth, Seventh, Ninth, and Tenth Circuits is that intent to avoid arrest or prosecution must be proved before section 3290 applies. ***Brouse v. United States***, 68 F.2d 294, 296 (1st Cir. 1933); ***Jhirad v. Ferrandina***, 486 F.2d 442, 444-45 (2d Cir. 1973); ***Donnell v. United States***, 229 F.2d 560, 563-65 (5th Cir. 1956); ***United States v. Greever***, 134 F.3d 777, 780-81 (6th Cir. 1998); ***United States v. Marshall***, 856 F.2d 896, 897-900 (7th Cir. 1988); ***United States v. Wazney***, 529 F.2d 1287, 1289 (9th Cir. 1976); ***Ross v. United States Marshal***, 168 F.3d 1190, 1194 (10th Cir. 1999). By contrast, two circuits, the District of Columbia Circuit and the Eighth Circuit, have held that mere absence from the jurisdiction, regardless of intent, is sufficient to toll the statute of limitations. *See* ***McGowen v. United States***, 105 F.2d 791, 792 (D.C. Cir. 1939); ***In Re Assarsson***, 687 F.2d 1157, 1162 (8th Cir. 1982).

7.04 *COMPLAINT TO EXTEND STATUTE OF LIMITATIONS*

Section 6531 of Title 26 also contains a mechanism for extending the statute of limitations period. The statute provides:

> Where a complaint is instituted before a commissioner of the United States within the period above limited, the time shall be extended until the date which is 9 months after the date of the making of the complaint before the commissioner of the United States.

26 U.S.C. § 6531. Thus, the government may file a complaint within the limitations period and effectively extend the statute period nine months.

However, Section 6531 "was not meant to grant the Government greater time in which to make its case." ***Jaben v. United States***, 381 U.S. 214, 219 (1965). Rather, Section 6531 "was intended to deal with the situation in which the Government has its case made within the normal limitation period but cannot obtain an indictment because of the grand jury schedule." ***Jaben***, 381 U.S. at 219-20; *cf.* ***United States v. O'Neal***, 834 F.2d 862, 865 (9th Cir. 1987) (investigation and case preparation need not cease upon filing of complaint; whether government improperly invoked extension is tested by sufficiency of the complaint at the preliminary hearing). For there to be a valid complaint triggering the extension of the limitations period under Section 6531, the complaint must allege sufficient facts to support a probable cause finding that a tax crime has been committed by the defendant. ***Jaben***, 381 U.S. at 220. Further, to take advantage of the extension under Section 6531, the government must fully comply with the complaint process and afford the defendant a preliminary hearing. ***Jaben***, 381 U.S. at 220.

As a practical matter, a complaint should only be filed for the year in which the statute of limitations would otherwise expire. This procedure will not preclude development before the grand jury of counts for subsequent years as to which the statute has not expired. Prosecutors should be aware, however, that the filing of a complaint may trigger the Speedy Trial Act as to the charge that is the subject of the complaint and, as a practical matter, may shorten the time within which the government may act on the remaining tax years under investigation. *See* 18 U.S.C. § 3161(b).

7.05 *SUSPENSION OF STATUTE: SUMMONS ENFORCEMENT*

Section 7609(e)(1) of Title 26 provides for the suspension of the statute of limitations in certain types of summons en-

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forcement proceedings. This statute provides:

> If any person takes any action as provided in subsection (b) and such person is the person with respect to whose liability the summons is issued (or is the agent, nominee, or other person acting under the direction or control of such person), then the running of any period of limitations . . . under section 6531 (relating to criminal prosecutions) with respect to such person shall be suspended for the period during which a proceeding, and appeals therein, with respect to the enforcement of such summons is pending. [FN8]

26 U.S.C. § 7609(e)(1).

It is beyond the scope of this Manual to treat in detail the nuances of summons enforcement proceedings. Any reliance on the suspension issue in this area requires a thorough analysis of Section 7609, and particular care must be taken in measuring and documenting any period for which the statute of limitations is suspended.

7.06 ***SUSPENSION OF STATUTE: OFFICIAL REQUEST FOR FOREIGN EVIDENCE***

Criminal tax prosecutions increasingly involve the use of evidence obtained from foreign sources. Section 3292 of Title 18 provides for the suspension of the statute of limitations to permit the United States to obtain foreign evidence. This statute provides:

> (a)(1) Upon application of the United States, filed before return of an indictment, indicating that evidence of an offense is in a foreign country, the district court before which a grand jury is impaneled to investigate the offense shall suspend the running of the statute of limitations for the offense if the court finds by a preponderance of the evidence that an official request has been made for such evidence and it reasonably appears, or reasonably appeared at the time the request was made, that such evidence is, or was, in such foreign country.
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> . . . .
>
> (b) Except as provided in subsection (c) of this section, a period of suspension under this section shall begin on the date on which the official request is made and end on the date on which the foreign court or authority takes final action on the request.
>
> (c) The total of all periods of suspension under this section with respect to an offense--
>
> (1) shall not exceed three years; and
>
> (2) shall not extend a period within which a criminal case must be initiated for more than six months if all foreign authorities take final action before such period would expire without regard to this section.

18 U.S.C. § 3292.

Letters rogatory, requests under a treaty or convention, or any other request made by a court or law enforcement authority of the United States will qualify as an “official request.” 18 U.S.C. § 3292(d). The statute does not require that the “request expressly list by citation the alleged statutory violations in order for a foreign evidence request to pass muster under 18 U.S.C. § 3292.” ***United States v. Neill***, 952 F.Supp. 831, 832 (D.D.C. 1996).

The Eleventh Circuit has held that, in an application for an order suspending the running of the statute of limitations, the government “must provide something with evidentiary value -- that is, testimony, documents, proffers, and other submissions bearing some indicia of reliability -- tending to prove it is reasonably likely that evidence” of an offense is in the foreign country. ***United States v. Trainor***, 376 F.3d 1325, 1332-33 (11th Cir. 2004). In ***Trainor***, the court held that the government's submission of only its application and a request, by the Criminal Division Office of International Affairs, for foreign evidence, which were not sworn or verified, was inadequate to satisfy the government's burden of showing by a preponderance of the evidence that “it reasonably appears, or reasonably appeared at the time the request was made, that such evidence is, or was, in such foreign country.” ***Id.*** at 1333. The court stated that the government may satisfy that burden by including a sworn or verified application containing the necessary factual information, testimony by government officials, affidavits, declarations, exhibits, or other materials of evidentiary value, including even hearsay testimony. ***Id.*** at 1333.

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While the maximum period for which the statute of limitations may be suspended for an offense is three years, the period begins to run when the government requests evidence from a foreign government. "[T]he starting point for tolling the limitations period is the official request for evidence, not the date the § 3292 motion is made or granted." ***United States v. Bischel***, 61 F.3d 1429, 1434 (9th Cir. 1995).

Likewise, the period ends when the foreign court or authority takes final action on the request. "'[F]inal action' for purposes of § 3292 means a dispositive response by the foreign sovereign to both the request for records and for a certificate of authenticity of those records." ***United States v. Bischel***, 61 F.3d at 1434. The prosecutor's satisfaction with the evidence provided is not determinative of whether there has been a final action. "However, when the foreign government believes it has completed its engagement and communicates that belief to our government, that foreign government has taken a 'final action' for the purposes of § 3292(b)." ***United States v. Meador***, 138 F.3d 986, 992 (5th Cir. 1998). Such a communication from a foreign government does not preclude further inquiry by the United States. "If dissatisfied with a dispositive response from a foreign authority, the prosecutor need only file another request and seek a further suspension of the limitations period, subject to the ultimate three-year limitation on the suspension period." ***United States v. Meador***, 138 F.3d at 993 (footnote omitted).

All requests for foreign evidence in criminal tax investigations should be coordinated with the Criminal Appeals & Tax Enforcement Policy Section, Tax Division, and the Office of International Affairs, Criminal Division. For further information on foreign evidence gathering in criminal tax cases, see Chapter 41.00 of this Manual.

[FN1]. The limitations period for Section 7202 offenses has been the subject of recent litigation. It is the view of the Tax Division that the six-year statute of limitations provided for in Section 6531(4) is applicable to prosecutions under Section 7202. Reference should be made to the discussion of this issue in the chapter dealing with Section 7202. *See* Chapter 9.00, *infra*.

[FN2]. As provided by Section 6531(4), the six-year rule for failure to file a return does not apply to returns that are required to be filed under part III of subchapter A of chapter 61. Part III covers information returns required to be filed under 26 U.S.C. §§ 6031-6060, and includes, for example, partnership returns, returns of exempt organizations, subchapter S returns, and returns relating to cash received in a trade or business (Form 8300). The rules in this area are rather complicated, as there is a further exception that makes the applicable limitations period for failure to file a subchapter S return six years, rather than the three-year period generally applicable for failures to file information returns. *See* 26 U.S.C. § 6037(a). Reference should be made to these specific Code provisions for a more detailed discussion of applicable limitations periods.

[FN3]. Section 7212(a) refers to two types of offenses: (1) impeding employees of the United States acting in an official capacity; and (2) impeding the administration of the Internal Revenue laws. The Tax Division takes the position that a six-year limitations period applies to offenses under both prongs of Section 7212(a), pursuant to 26 U.S.C. § 6531(6). Reference should be made to the discussion of this issue in the chapter dealing with Section 7212(a). *See* Chapter 17.00, *infra*.

[FN4]. The Tax Division is not aware of any cases in which the statute of limitations applicable to false claim for refund cases arising under the internal revenue laws has been litigated. The Tax Division takes the position that a six-year limitations period applies to such offenses under 18 U.S.C. §§ 286, 287 pursuant to 26 U.S.C. § 6531(1). Reference should be made to the discussion of this issue in the chapter dealing with 18 U.S.C. §§ 286, 287. *See* Chapter 22.00, *infra*

[FN5]. Returns sent by designated private delivery services are treated as having been sent by U.S. mail for purposes of the timely mailed/timely filed exception to the general rule. 26 U.S.C. § 7502(f)(1). "Designated delivery service" is defined under Section 7502(f)(2).

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[FN6]. *See* 18 U.S.C. § 3282(a): "Except as otherwise expressly provided by law, no person shall be prosecuted, tried, or punished for any offense . . . unless the indictment is found or the information is instituted within five years next after such offense shall have been committed."

[FN7]. Although the government technically is not required to prove that each member of the conspiracy committed an overt act within the statute period, in practice, the prosecutor should critically review each conspirator whose membership in the conspiracy predates the limitations period and be prepared to rebut a withdrawal defense coupled with a statute of limitations defense.

[FN8]. Subsection (b) of 26 U.S.C. § 7609 permits certain persons to intervene in proceedings with respect to enforcement of summonses and to initiate proceedings to quash summonses.

Statute of Limitations Primer: Tax and Related Title 18 Prosecutions

Author: Harris, Steven M.

Introduction

All tax and related Title 18 criminal offenses investigated by IRS special agents have a statute of limitations. [FN1] However, the determination of the applicable limitations period is not usually just a straightforward counting of days, months, or years.

General Considerations

The statute of limitations is an affirmative defense. It is waived if not timely asserted. [FN2] A conviction will be affirmed when a defendant knowingly waives a viable statute of limitations defense. [FN3]

The principal issues that arise when a statute of limitations defense is raised are: what is the applicable statute of limitations period; when did the limitations period begin to run; and has there been a tolling event or an extension provision affecting the normal expiration of the applicable limitations period.

The usual federal criminal statute of limitations for noncapital offenses is five years. [FN4] The statute of limitations for an offense prosecuted under most code offense provisions and related conspiracies is determined under section 6531. That provision sets forth the general rule of a three-year limitations period. However, as discussed in more detail below, the general rule is consumed by a list of exceptions that lengthen the limitations periods to six years for most tax crimes.

It is hornbook law that the statute of limitations on a criminal prosecution begins to run only on occurrence of all of the essential elements of the offense -- that is, when the crime is said to be "complete." [FN5] In determining whether the statute of limitations has expired, the day of the commission of the offense is normally excluded; the day of the return of the indictment or filing of an information is included.

A tax return filed early is deemed filed on the initial statutory due date prescribed by the code. [FN6] A return that is filed beyond the due date generally triggers the statute of limitations period on the date the return is filed, [FN7] that is, the date the IRS receives the return. That date is usually fixed by the official receipt date stamped on the return. [FN8] A return that has an extended due date triggers the limitations period whenever filed after the original statutory due date, regardless of whether it was filed before or after the extended due date. [FN9]

A crime that is said to be "continuing" might have an indefinite limitations period. With the exception of conspiracy, the notion that a crime is a continuing offense is disfavored. [FN10] Nevertheless, under certain circumstances, ordinary tax violations have been held to assume continuing offense status. In one case, a course of evasion of payment of assessed taxes continuing over many years was charged in a single count. The district court rejected a statute of limitations argument and determined the indictment properly charged a continuing course of conduct that included the evasion of

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payment for taxes more than six years old. [FN11] In another case, the government argued that the limitations period for an evasion prosecution was extended annually by the defendant's failure to correct documents that contained a false Social Security number, resulting in a tax deficiency in later years. Although the opinion upheld the indictment as timely, the court did not rule on the continuing offense issue. [FN12]

Tolling and Extension

The statute of limitations is tolled upon the timely filing of an information or indictment. [FN13] Section 6531 tolls the running of the statute of limitations while the defendant is "outside the United States" or a "fugitive from justice". [FN14] Mere absence from the United States invokes the code tolling provision, because neither the intention for the absence from the United States nor its duration are pertinent. [FN15] No criminal statute of limitations runs on a Title 18 offense while one is "fleeing from justice." [FN16]

Another code provision, section 7609(e), suspends the limitations period for criminal prosecution when a "third-party recordkeeper" summons is not complied with or when there is a related summons proceeding instituted. [FN17]

A district judge may enter an order suspending the statute of limitations in certain situations when a formal request for foreign evidence is outstanding. [FN18]

Tax Misdemeanors

Except for certain information returns, the statute of limitations to prosecute the willful failure to timely file a return under section 7203 is six years. [FN19] The general three-year period applies to misdemeanor failure to file any information return required under sections 6031-6060. Included are the information returns required to be filed by partnerships, exempt organizations, certain trusts, certain foreign corporations, trade or business payers (Form W-2 and Form 1099 series), pension plans, and for mortgage foreclosures. Also included is Form 8300, which is required for certain cash receipts. [FN20]

A failure-to-file offense is complete -- and the statute begins to run -- when the failure becomes willful. Ordinarily, that would be the day after the due date of a tax return, but it can be later if there is sufficient proof the failure did not become willful until later. [FN21] The determination of the date when a failure-to-file offense became willful is factual, and is therefore a question to be determined by the jury. [FN22] When a valid extension of time to file has been obtained, [FN23] failure to file does not become willful until the day after the extended due date. [FN24]

The offense of willful failure to pay charged under section 7203 has a six-year limitations period. [FN25] In those cases, the concepts are similar; the running of the limitations period commences the day after the failure to pay becomes willful. [FN26]

Lesser known misdemeanors of omission enumerated by section 7203 (the failure to keep records and the failure to supply information) are not subject to an exception contained in section 6531. Those offenses are subject to a three-year statute of limitations. The misdemeanor offenses set forth in sections 7204 and 7205, which regard withholding statements, are also subject to a three-year limitations period.

Section 7207, which provides for the misdemeanor punishment of a false or fraudulent document, is subject to a six-year limitations period. [FN27] That limitations period will ordinarily begin to run on the date the document is presented. For example, if a taxpayer submitted a false or fraudulent document during an examination in 2004 to support a deduction claimed on his timely filed 2001 tax return, although the statute of limitations on prosecution of the false tax return or evasion offense expires in the year 2008, the limitations period on the section 7207 false presentment offense does not expire until 2010.

Tax Felonies

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Tax felonies normally implicate a six-year limitations period. That includes tax evasion (section 7201); filing a false return or other document (section 7206(1)); the aiding and assisting thereof (section 7206(2)); and the intangible misconduct provision (section 7212(a)), which is somewhat analogous to an obstruction offense. The statute of limitations to prosecute both the evasion of assessment and evasion of payment under section 7201 is six years. [FN28]

When the sole affirmative act of tax evasion charged is the filing of a false return, the general filing date rules apply to compute the limitations period. However, in other cases, the limitations period for an evasion offense runs on the commission of the last affirmative act of evasion, so evasion cases can be brought long after six years from the anniversary date of the filing of the offending tax return. [FN29] Therefore, if any affirmative act is committed after a return is filed, the six-year period may run from the time of the commission of the affirmative act. [FN30] In a failure-to-file case in which affirmative acts result in a Spies evasion charge, the limitations period commences to run from the due date of the return or the last affirmative act of evasion, whichever is later. [FN31]

The statute of limitations to prosecute the filing of false tax returns, statements, affidavits, or other documents is six years. [FN32] For an original return, the statute of limitations commences on the later of the due date or date of filing, whichever is earlier. For a delinquent return or an amended return filed after the due date, the limitations period commences when the return is filed with the IRS. [FN33]

Under section 7206(2), the statute of limitations to prosecute one who assists in the preparation or presentation of a false return or other document is six years. [FN34] There is no case that provides a clear-cut answer to the question of when the statute of limitations commences to run under section 7206(2). Because a violation of that provision can be charged in different ways, all of the possible issues have not received critical examination. In one case, a section 7206(2) violation was held to occur every time a taxpayer relied on the advice of the defendant, a tax shelter promoter, to file false returns, even though more than six years had elapsed since he provided the initial advice to claim false deductions. [FN35] Depending on how an indictment charges an aiding and assisting offense and what view is followed (whether or not the actual filing of a return or other document is an element of the offense [FN36]), the statute of limitations may not commence until a false return or other document is actually filed. If filing is not deemed an element of a particular section 7206(2) offense -- for example, when an indictment only charges counseling or advising the preparation of a false return or document, or when the false return or document is provided to an intermediary who is required by law to file it -- the crime would appear to be complete when the defendant provided the prohibited aid or assistance, and the six-year period would run from that date, regardless of filing or the due date. [FN37] If a defendant is charged with the actual preparation of a false tax return, it might be argued that the statute of limitations runs from the last date prescribed for filing the return, regardless of when the preparation occurred and whether or not the return was ever filed. [FN38]

Offenses under section 7202 regarding employment tax withholding have been held to be subject to the six-year limitations period. [FN39] The offenses described in section 7212(a), including the omnibus obstruction-type clause regarding the due administration of the IRS, is subject to a six-year limitations period. [FN40] The limitations period commences upon the occurrence of the last corrupt act. [FN41]

Tax-Related Title 18 Offenses

The principal nontax offenses [FN42] investigated by IRS special agents (other than conspiracy and money-laundering), including false statements (18 U.S.C. section 1001), false claims (18 U.S.C. section 287), and aiding and abetting (18 U.S.C. section 2), are subject to the customary five-year statute of limitations. [FN43]

The limitations period to prosecute a false statement under 18 U.S.C. section 1001 ordinarily begins to run when the false oral or written statement is made. One decision holds that a false statement that is mailed begins the limitations period when mailed, not when received, based on the rationale that neither the receipt nor reliance by the agency are elements of the offense. [FN44] Generally, each false statement is a separate crime against which a separate limitations period is applied. [FN45] An indictment charging a false oral statement made within the limitations period that serves to con-

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firm a similar false written statement made outside the limitations period is not subject to a statute of limitations defense. [FN46]

The period of limitations to prosecute a false claim under 18 U.S.C. section 287 normally begins to run when the false claim is presented. For income tax returns and other documents that claim a false refund from the IRS, that will ordinarily be when the return or other document is filed. [FN47]

The ordinary statute of limitations for prosecution of criminal conspiracies under 18 U.S.C. section 371 is five years. [FN48] The statute of limitations period on a conspiracy commences from the date of the last overt act undertaken in furtherance of the main criminal objectives. [FN49]

A conspiracy under the offense clause of 18 U.S.C. section 371 is not necessarily subject to the same limitations period as the underlying offense. Conspiracy is not the commission of the crime which it contemplates, nor does a conspiracy violate or arise under the statute whose violation is the object of the conspiracy. [FN50] Thus, a conspiracy to commit a substantive tax offense ordinarily has a five-year limitations period regardless of whether the underlying offense carries a three- or six-year statute of limitations. Under section 6531, however, there is a six-year limitations period applicable when a conspiracy charges "the defrauding or attempting to defraud the United States or any agency thereof" or attempts "in any manner to evade or defeat any tax or the payment thereof." [FN51] It is unclear whether a five- or six-year statute applies to a conspiracy to violate section 7206(2). [FN52]

The exact language used in an indictment to express the objects of a conspiracy must be carefully scrutinized to determine the applicable limitations period. When a single-count conspiracy charges conduct subject to both five- and six-year periods of limitations, dual jury instructions and special verdict forms are appropriate. [FN53]

Title 18 Obstruction and Perjury Offenses

IRS special agents encounter obstruction and perjury offenses during both administrative and grand jury investigations. They have authority to investigate and recommend prosecution in those cases when there are tax-related offenses that can or are to be charged. Obstruction and perjury offenses have a five-year limitations period. The principal obstruction offenses are 18 U.S.C. sections 1503 (typically misconduct during a grand jury investigation or trial), 1505 (agency proceeding obstruction), 1510 (obstruction of a criminal investigation), and 1512 (witness tampering and related offenses). In due course, IRS special agents will have cases involving Sarbanes-Oxley offenses (18 U.S.C. section 1519), punishing the destruction and alteration of records. Perjury prosecution is recommended by IRS special agents under 18 U.S.C. sections 1621 and 1623, and usually relates to testimony before a grand jury or in a tax trial.

Obstruction and perjury offenses rarely raise limitations questions. They are not historical crimes being investigated years after completion and are ordinarily prosecuted rather quickly after occurrence and discovery, usually during an investigation of principal tax and related offenses.

Conclusion

The statute of limitations on criminal prosecution can provide a complete and perfect defense, albeit technical. Tax and related charges are often involved and complex. Determination of the applicable limitations period is often not merely counting elapsed time.

[FN1]. Special agents routinely determine and note in their investigative files the expiration date(s) of each offense being considered. Although the application of the Sentencing Guidelines makes it immaterial to a sentence whether one or more charges become time-barred, consideration of the statute of limitations and resolution of any issues are part of the case review processes of both IRS Criminal Investigation (CI) division and the Tax Division of the Department of Justice.

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[FN2]. See United States v. Arky, 938 F.2d 579 (5th Cir. 1991); United States v. Karlin, 785 F.2d 90 (3d Cir. 1986).

[FN3]. In United States v. Akmakjian, 647 F.2d 12 (9th Cir. 1981), the defendant was not allowed to withdraw a guilty plea to an admittedly time-barred count, because he expressly waived a statute of limitations defense motion that was pending at the time of his guilty plea.

[FN4]. 18 U.S.C. section 3282(a).

[FN5]. See United States v. Irvine, 98 U.S. 450 (1879); Toussie v. United States, 397 U.S. 112 (1970).

[FN6]. United States v. Habig, 390 U.S. 222 (1968); section 6513(a).

[FN7]. Habig, 390 U.S. 222.

[FN8]. See United States v. Robinson, 811 F.Supp. 1174 (S.D. Miss. 1993); United States v. Stella, 745 F.Supp. 195 (S.D.N.Y. 1990).

[FN9]. Habig, 390 U.S. 222.

[FN10]. Toussie, 397 U.S. 112; Irvine, 98 U.S. 450. See also, e.g., United States v. Knoll, 16 F.3d 1313 (2d Cir. 1994).

[FN11]. Shorter v. United States, 608 F.Supp. 871 (D.D.C. 1985), aff'd, 809 F.2d 54 (D.C. Cir. 1987).

[FN12]. United States v. Payne, 978 F.2d 1177 (10th Cir. 1992).

[FN13]. See, e.g., United States v. Schmick, 904 F.2d 936 (5th Cir. 1990); United States v. Saussy, 802 F.2d 849 (6th Cir. 1986). When a timely indictment or information is dismissed after the limitations period has expired for a reason other than one that bars a later prosecution, a new indictment or information may be brought within six calendar months. 18 U.S.C. section 3288. Similarly, if a timely brought indictment or information is dismissed when the limitations period will expire within six calendar months, a new indictment or information can be brought within six calendar months. 18 U.S.C. section 3289. See, e.g., United States v. Serubo, 502 F.Supp. 299 (E.D. Pa. 1980). A time-barred indictment dismissed under a plea agreement can be reinstated if a guilty plea is vacated. See 18 U.S.C. section 3296.

[FN14]. A fugitive from justice is defined under 18 U.S.C. section 3290.

[FN15]. See United States v. Marchant, 774 F.2d 888 (8th Cir. 1985) (while on an 11-day vacation to Switzerland, the defendant could not be served criminal process); United States v. Myerson, 368 F.2d 393 (2d Cir. 1966) (115 days total absence during the statute of limitations period for various purposes without indicia of flight).

[FN16]. 18 U.S.C. section 3290. It remains unresolved whether mere absence from the jurisdiction is sufficient to invoke that tolling provision, or whether intended flight in the face of pending charges is required.

[FN17]. See, e.g., United States v. Orlowski, 808 F.2d 1283 (8th Cir. 1986).

[FN18]. 18 U.S.C. section 3292. See, e.g., United States v. Torres, 318 F.3d 1058 (11th Cir. 2003).

[FN19]. Section 6531(4) refers to a failure to "make a return at the time or times required by law or regulation." The failure to file a foreign financial account form, TDF 90.22-1, a felony, is not technically a tax offense. See 31 U.S.C. section 5322(a). The offense has a five-year statute of limitations under 18 U.S.C. section 3282(a).

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[FN20]. The offense is, however, a felony, because the potential term of imprisonment is five years, not one year. See section 7203 (last sentence).

[FN21]. The government's evidentiary burden to prove willfulness other than immediately on passage of the due date will likely be difficult. See United States v. Goldstein, 502 F.2d 526 (3d Cir. 1974).

[FN22]. United States v. Hook, 781 F.2d 1166 (6th Cir. 1986).

[FN23]. See section 6081. Extensions are invalid or can be invalidated retroactively when they are filed untimely, not accompanied by proper payment of estimated liability when required, or in the case of an extension that is not automatic and subject to discretion, when the reason provided for requesting the extension is false. See, e.g., Phillips v. United States, 843 F.2d 438 (11th Cir. 1988); Crocker v. Comm'r, 92 TC 899 (1989); Rev. Rul. 79-113, 1979-1 C.B. 389.

[FN24]. Phillips, 843 F.2d 438. See also United States v. Pandilidis, 524 F.2d 644 (6th Cir. 1975). Compare United States v. Calhoun, 566 F.2d 969 (5th Cir. 1978) (nonfiling after claimed application of automatic extension for residing or traveling outside the United States results in lookback to April 15), and Galuska v. Comm'r, 98 T.C. 661 (1992) (filing extensions have no effect on the civil refund limitations period).

[FN25]. Section 6531(4).

[FN26]. United States v. Sams, 865 F.2d 713 (6th Cir. 1988) (jury could have inferred from the defendant's attachment to the return indicating a willingness to make payment arrangements that willfulness was lacking until that date or later); United States v. Andros, 484 F.2d 531 (9th Cir. 1973) (limitations period can commence at a date later then when taxes are assessed or payment demanded).

[FN27]. Section 6531(5).

[FN28]. Section 6531(2).

[FN29]. See, e.g., United States v. Beacon Brass Co., 344 U.S. 43 (1952) (post-filing false statements to officials); United States v. Goodyear, 649 F.2d 226 (4th Cir. 1981) (false statements made after filing of false return).

[FN30]. That date can be much later than the return due date or actual filing date. See, e.g., United States v. Dandy, 998 F.2d 1344 (6th Cir. 1993) (December 1990 indictment for 1982 and 1983 evasion was timely more than six years from delinquent return filings when evasive acts occurred through November 1985); United States v. Winfeld, 906 F.2d 970 (11th Cir. 1992) (indictment in 1988 was timely on January 31, 1979, for fiscal year-end false return filed December 5, 1980, when false statement was made to agents in 1984); United States v. DeTar, 832 F.2d 1110 (9th Cir. 1987) (timely indictment in October 1985 charging evasion of payment of 1977 and 1978 taxes); United States v. Ferris, 807 F.2d 269 (1st Cir. 1986) (1985 indictment for evasion in 1976 and 1977 held timely when 1979 and 1985 statements to agents were made to conceal prior evasion); United States v. Trownsell, 367 F.2d 815 (7th Cir. 1966) (1964 indictment charging 1961 affirmative act made to conceal evasion of 1946-1953 taxes held timely). Accord, United States v. Payne, 978 F.2d 1177 (10th Cir. 1992) (discussing cases and focusing on the date a tax deficiency is incurred when affirmative acts occur earlier).

[FN31]. See, e.g., United States v. DiPetto, 936 F.2d 96 (2d Cir. 1991) (when earlier filing and maintaining of false withholding document, Form W-4, is the affirmative act charged, limitations period runs from later due date of unfiled income tax return).

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[FN32]. Section 6531(5).

[FN33]. United States v. Samara, 643 F.2d 701 (10th Cir. 1981).

[FN34]. Section 6531(3).

[FN35]. United States v. Kelley, 864 F.2d 569 (7th Cir. 1989).

[FN36]. See United States v. Dahlstrom, 713 F.2d 1423 (9th Cir. 1983).

[FN37]. See United States Cutler, 948 F.2d 691 (10th Cir. 1991). A similar argument was rejected in Imholte v. United States, 226 F2d 585 (8th Cir. 1955).

[FN38]. See Hull v. United States, 356 F.2d 919 (5th Cir. 1966). In United States v. Bursten, 395 F.2d 976 (5th Cir. 1968), the Fifth Circuit stated it deemed Hull overruled by Habig.

[FN39]. United States v. Mussachia, 900 F.2d 493 (2d. Cir. 1990); United States v. Porth, 426 F.2d 519 (10th Cir. 1970).

[FN40]. Section 6531(6). See United States v. Kassouf, 144 F.3d 952, Doc 98-16265, 98 TNT 100-81 (6th Cir. 1998); United States v. Kelly, 147 F.3d 172 (2d. Cir. 1998); United States v. Wilson, 118 F.3d 328, Doc 97-20500, 97 TNT 135-14 (4th Cir. 1997).

[FN41]. See United States v. Workinger, 90 F.3d 1409, Doc 96-21347, 96 TNT 147-64 (9th Cir. 1996).

[FN42]. For a listing including others, see IRM Part 9, Exhibit 9.1.3-2 (Aug. 11, 2003).

[FN43]. 18 U.S.C. section 3282(a). The government may argue that under section 6531(1), the limitations period for an 18 U.S.C. section 287 offense is six years. That argument would appear to be correct for 18 U.S.C. section 286, which criminalizes conspiracies relating to fraudulent claims, but not section 287, because neither the intent to defraud nor an attempt to evade are elements of a section 287 offense.

[FN44]. United States v. Smith, 740 F.2d 734 (9th Cir. 1984).

[FN45]. See, e.g., United States v. Jordan, 890 F.2d 247 (10th Cir. 1989); United States v. Warnick, 815 F.2d 1341 (10th Cir. 1987). Repeated false statements given in response to identical questions can result in a defendant being convicted for only one such false statement. United States v. Olsowy, 836 F.2d 439 (9th Cir. 1987). When those multiple false statements are made, the government need only indict and prove one false statement made within the five-year limitations period.

[FN46]. United States v. Roshko, 969 F.2d 9 (2d Cir. 1992).

[FN47]. It is unclear whether the code filing provisions (for example, section 6513(a)) are applicable to a Title 18 false claim prosecution.

[FN48]. 18 U.S.C. section 3282(a).

[FN49]. Grunewald v. United States, 353 U.S. 391 (1957). See also United States v. Fletcher, 928 F.2d 495 (2d Cir. 1991).

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[FN50]. See Braverman v. United States, 317 U.S. 49 (1942).

[FN51]. Sections 6531(1), 6531(8). See, e.g., United States v. Aracri, 968 F.2d 1512 (2d Cir. 1992); United States v. Vogt, 910 F.2d 1184 (4th Cir. 1990); United States v. Brunetti, 615 F.2d 899 (10th Cir. 1980); United States v. Waldman, 941 F.2d 1544 (11th Cir. 1991), United States v. Lowder, 492 F.2d 953 (4th Cir. 1974); United States v. Ingredient Technology Corp., 698 F.2d 88 (2d Cir. 1983).

[FN52]. United States v. Fruehauf, 577 F.2d 1038 (6th Cir. 1978).

[FN53]. See United States v. The Southland Corporation, 760 F.2d 1366 (2d Cir. 1985) (18 U.S.C. section 371 count with dual objects: to violate the Travel Act and to defraud the United States by impeding the function of the Service).

[NOTE]

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Assessment and Collection of U.S. Taxes From Non-U.S. Taxpayers

Jeffrey Rubinger **Holland** & Knight, LLP

Statute of Limitations, in General

• Section 6501(a) provides the general rule that "the amount of any tax imposed by this title shall be assessed within 3 years after the return was filed."

• If the IRS fails to assess the tax within three years, it is not only prohibited from collecting the tax administratively by lien and levy, it is also barred from instituting a court proceeding for the collection of the tax after the three-year period on assessment expires.

• The critical act that starts the statute of limitations on assessment is the filing of a "return," which for this purpose means "the return required to be filed by the taxpayer (and does not include a return of any person from whom the taxpayer has received an item of income, gain, loss, deduction, or credit)."

• There are several important exceptions to the general three-year statute of limitations.

— For one, the statute of limitations will be extended indefinitely if a taxpayer files a false return, engages in a willful attempt to evade tax, or files no return at all.

— Another exception exists when a donor fails to report a gift, the value of which is required to be reported on a gift tax return, in which case the IRS may assess gift tax at any time, unless the donor has disclosed the item on a return or in a document attached to the return.

• A further exception was added recently by the American Jobs Creation Act of 2004.

• Under new Section 6501(c)(10), the statute of limitations on assessment regarding a "listed transaction" that a taxpayer fails to disclose will not expire before one year after the earlier of (i) the date on which the secretary is furnished the information required under Section 6011, or (ii) the date that a material advisor meets the requirements of Section 6112 regarding a request by the secretary under Section 6112 relating to the undisclosed listed transaction.

• Section 6707A(c)(2) defines a listed transaction as a reportable transaction that is the same as, or substantially similar to, a transaction identified by the secretary as a tax avoidance transaction for purposes of Section 6011.

• Section 6501(e)(1) and (2) also provide two very important provisions that extend the general three-year statute of limitations on assessment to six years in certain situations.

— Section 6501(e)(1) extends the statute of limitations on the assessment of income tax to six years if the taxpayer omits from gross income an amount "properly included therein" that is in excess of 25 percent of the amount of gross income stated in the return.

— Similarly, Section 6501(e)(2) extends the statute of limitations on assessment of estate or gift tax to six years if the taxpayer omits from the gross estate or from the total amount of the gifts made during the period amounts in excess of 25 percent of the gross amount stated in the return.

— Neither of those provisions apply, however, if the particular item that is omitted is disclosed in a manner adequate to apprise the secretary of the nature and amount of such item.

What Constitutes a Return for Section 6501 Purposes?

• The critical act that starts the running of the statute of limitations for purposes of Section 6501 is the filing of a "return."

• Neither the code nor the regulations define what constitutes a return for that purpose.

• The Tax Court, however, has stated that a return, within the meaning of Section 6501(a), is filed when the return (i) purports to be a return; (ii) evinces an honest and reasonable attempt to satisfy the requirements of the tax; (iii) contains sufficient information to calculate the taxpayer's tax liability; and (iv) is executed by the taxpayer under penalties of perjury.

• Therefore, the form or document need not state any amount due as tax or calculate any tax, provided that it contains all the data from which the tax could be computed and assessed.

Does the Filing of Form 1042-S Constitute Filing of Return?

• Regarding non-U.S. taxpayers, one of the issues that arises is whether the filing of IRS Forms 1042 and 1042-S constitute the filing of a return for purposes of commencing the limitation on assessment against a non-U.S. taxpayer under Section 6501(a).

• In general, Forms 1042 and 1042-S are required to be filed whenever payments of U.S.-source FDAP income are made to non-U.S. taxpayers, regardless of whether those payments are exempt from U.S. withholding tax under a treaty or code exception (e.g., portfolio interest).

• The person responsible for filing the Forms 1042 and 1042-S is the withholding agent (that is, the person required to withhold the tax), rather than the non-U.S. person itself.

Taxation of Non-U.S. Persons, In General

• In general, non-U.S. taxpayers are subject to U.S. federal income tax on two categories of income:

— (i) certain passive types of U.S.-source income (for example, interest, dividends, rents, annuities, and other types of "fixed or determinable annual or periodical income," collectively known as FDAP),

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• FDAP income is subject to a 30 percent withholding tax that is imposed on a foreign person's gross income (subject to reduction or elimination by an applicable income tax treaty) and

— (ii) income that is effectively connected to a U.S. trade or business (ECI).

• ECI is subject to tax on a net basis at the graduated tax rates generally applicable to U.S. persons.

ICI Pension Fund

• In ICI Pension Fund v. Commissioner, 112 T.C. 83 (1999), the issue was whether the IRS was prohibited from assessing deficiencies against a non-U.S. pension fund more than three years after Forms 1042 and 1042-S were filed for U.S.-source payments made to that fund.

• ICI was a pension fund that had its principal office in London. For the tax periods at issue, ICI neither was engaged in a U.S. trade or business nor did it have any income that was effectively connected with a U.S. trade or business or that was attributable to a permanent establishment in the United States.

• During the 1991 and 1992 tax years, ICI received dividends on stock of U.S. corporations, resulting in U.S. federal income tax withholding of more than $ 1.5 million each year. The withholding agent timely filed Forms 1042 and 1042-S with the IRS on which it reported and withheld the proper amount of tax.

• In 1992 and 1993, ICI submitted Forms 990-T to the IRS, claiming a refund of the taxes withheld in 1991 and 1992 on the grounds that it was a tax-exempt entity under Section 501(c)(5). The IRS issued the refunds for both years.

• Later, however, the IRS determined deficiencies against ICI for 1991 and 1992. Although ICI conceded it was not a tax-exempt organization, it argued that the IRS was prohibited from assessing tax against it for those years.

• Specifically, ICI argued that the assessment for 1991 was time barred because the IRS issued the deficiency notice more than three years after the withholding agent filed the Form 1042 for that year.

• The Tax Court rejected that argument, reasoning that ICI was the “taxpayer” for purposes of Section 6501(a), but that the withholding agent's Form 1042 was not ICI's “return.”

• In fact, the court stated that the Form 1042 did not even constitute a return for purposes of Section 6501 because it did not set forth sufficient information to allow the IRS to determine ICI's liability, and because it wasn't signed by ICI or its trustee under penalties of perjury.

• As a result, the Tax Court held that the IRS was not time barred from assessing taxes against ICI for the years at issue.

• The ICI decision is interesting because non-U.S. taxpayers generally are not required to file U.S. federal income tax returns to the extent that their U.S. federal income tax liability is fully satisfied by way of withholding.

• Originally, when ICI received the dividend payments, the withholding agent withheld the proper amount of tax and therefore ICI was not required to file a U.S. federal income tax return.

• However, because ICI requested and received a refund of the taxes that were withheld, ICI was no longer subject to the general rule that non-U.S. taxpayers are not required to file U.S. federal income tax returns when their taxes are fully satisfied by way of withholding.

• It was that fact that caused ICI to be subject to the unlimited statute of limitations under Section 6501(c)(3) and allowed the IRS to assess taxes against ICI, rather than against the withholding agent, which is usually the case regarding U.S.-source payments of FDAP income.

Treatment of Protective Returns

• Another issue that commonly arises regarding the statute of limitations on assessment of taxes against non-U.S. taxpayers is whether a “protective return” constitutes a valid return for purposes of the period of limitations on assessment under Section 6501(a).

• That issue arises because, unlike a typical tax return filed by a non-U.S. taxpayer engaged in a U.S. trade or business,

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a protective return generally does not contain information on cost of goods sold and deductible expenses that is necessary to compute the taxpayer's effectively connected taxable income.

• Non-U.S. taxpayers whose U.S. activities give rise to income effectively connected to a U.S. trade or business (for example, ECI) are subject to U.S. federal income on that income on a net basis at the graduated tax rates generally applicable to U.S. persons.

• Unlike FDAP income, which is subject to a 30 percent withholding tax on a gross basis, non-U.S. taxpayers are allowed to deduct expenses that are allocable to ECI.

• A foreign taxpayer, however, is entitled to the benefit of deductions and credits only if it timely files, "in the manner prescribed in subtitle F, a true and accurate return of its taxable income which is effectively connected" with the conduct of a trade or business in the United States.

• If a foreign taxpayer determines that its activities do not give rise to gross income that is ECI, it may nevertheless file a return on a timely basis and thereby protect its right to receive the benefit of the deductions and credits attributable to that gross income if it is later determined that the original determination was incorrect.

• If such a protective return is filed, the foreign taxpayer is not required to report any gross income as effectively connected or any deductions or credits, but it should attach a statement indicating that the return is being filed to protect the corporation's right to deductions and credits.

• In FSA 3809 (June 11, 1996), the primary issue was whether a protective return filed by a Canadian corporation that sold goods in the United States constituted a return and therefore began the three-year statute of limitations.

• The IRS ruled that it did, stating that if the protective return did not constitute a return for purposes of Section 6501(a), it would, in effect, "make compliance with section 1.882-4(a)(3)(iv) a trap for the unwary, so that following the explicit requirements set forth in that regulation . . . would cause a taxpayer to fail to comply with another provision of the Code."

• According to the IRS, that would not only subject the taxpayer to an unlimited period of limitations for assessment, but could also cause the taxpayer to be subject to penalties under Section 6651 for failure to file a return.

• Based on those factors, the IRS ruled that it did "not believe that a successful argument can be made that protective returns that satisfy the requirements of section 1.882-4(a)(3)(iv) . . . are not returns for purposes of starting the Section 6501(a) period of limitations."

When Will the Three-Year Statute of Limitations be Extended?

• Section 6501(e)(1) provides that if a taxpayer omits more than 25 percent of its gross income from an income tax return, the IRS has six years from the filing of that return to assess tax or to begin a proceeding in court to collect the tax without assessment.

• When attempting to apply the six-year statute of limitations, the IRS must prove by a preponderance of the evidence that the rule applies.

• For purposes of that rule, however, items that are omitted from a taxpayer's return will not be taken into account if the corresponding amount is disclosed in the return, or in a statement attached to the return, in a manner adequate to apprise the IRS of the nature and amount of the item.

• In the context of U.S.-source payments of FDAP income to non-U.S. taxpayers, the question has arisen whether the special six-year period of limitation for assessment applies when a withholding agent omits from the form 1042 items of gross income paid to nonresident aliens and those omissions exceed 25 percent of the amount shown on the Form 1042.

• In Northern Indiana Public Service Co. v. Commissioner, (1993), the taxpayer was a U.S. corporation that wholly owned a foreign subsidiary in the Netherlands Antilles. The foreign subsidiary made interest payments attributable to Euronote obligations issued to non-U.S. taxpayers.

• The IRS determined that the foreign subsidiary was inadequately capitalized and therefore treated the U.S. corporate

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parent as making the interest payments. As a result, the IRS held that the U.S. corporate parent was liable for the 30 percent withholding tax under Section 1441 for the tax years 1982 through 1985.

• While the taxpayer filed Forms 1042 and 1042-S for the years at issue on which it reported amounts paid to non-U.S. taxpayers, the taxpayer failed to include the interest payments that were attributable to the bondholders of the Euronotes.

• The taxpayer conceded that the amount of those interest payments was in excess of 25 percent of the amount of "gross income paid" that was stated on the Form 1042, but argued that the IRS was prohibited in 1989 from assessing tax attributable to the 1982 interest payments because the general three-year statute of limitations on assessment had expired.

• The IRS contended that the six-year statute of limitations on assessment was applicable and, therefore, it had the authority to assess those taxes. More specifically, the taxpayer as the withholding agent argued that the six-year period for assessment of tax under Section 6501(e) did not apply to its Form 1042, because the Form 1042 "is a tax return designed to report . . . withholding tax liability on amounts paid to foreign persons" rather than gross income, and Section 6501(e) pertains only to gross income received by a taxpayer.

• The Tax Court rejected that argument, holding that Section 6501(e) applies to Form 1042 because that section states that it applies "in the case of any tax imposed by subtitle A," which includes Sections 1441 and 1442. The Tax Court also noted that Reg. Section 301.6501(e)-1(a)(1)(i) refer to "a return of a tax imposed by subtitle A," which includes Form 1042.

• Accordingly, the court in Northern Indiana applied the six-year statute of limitations to assess taxes against the withholding agent despite the fact that the taxes were borne economically by the non-U.S. taxpayers, who either reported the full amount of gross income on a timely filed U.S. tax return or were not required to file a U.S tax return because their tax liability was fully satisfied by way of withholding.

• Query whether the result would have been the same if the payments the withholding agent omitted were not even gross income to the non-U.S. taxpayers, in the first instance.

• That issue arose in 1997 FSA Lexis 205 (June 26, 1997).

• In that FSA, a German corporation owned a percentage of the stock of a U.S. corporate subsidiary. The U.S. sub transferred its interest in certain European subsidiaries to the German shareholder and simultaneously declared a dividend in the amount of the aggregate value of the interests transferred.

• At the time of the distribution, the U.S. sub had no current or accumulated earnings and profits. Also, the "dividend" that was paid did not exceed the German shareholder's basis in the U.S. sub's stock. Accordingly, the distribution constituted a nontaxable return of capital.

• The U.S. subsidiary timely filed for the year at issue a Form 1042 reporting payments to foreign persons but failed to report the distribution to the German shareholder. The normal three-year statute of limitations on assessment for that return had expired.

• Subsequently, a Form 872 was executed to extend the statute of limitations to six years. The taxpayer argued that the distribution was not income, because it was not a dividend (that is, the taxpayer had no earnings and profits) and therefore there was no income item to withhold on and to report on Form 1042. As a result, the taxpayer contended that there was no 25 percent omission of gross income from the Form 1042 that would cause the six-year statute of limitations on assessment to apply.

• The IRS contended that the concerns behind Section 6501(e) are similar to the concerns behind Reg. Section .1141-3(b): Corporate distributions are treated as if they are taxable dividends subject to withholding and reporting on Form 1042 because otherwise the IRS would be specially disadvantaged in detecting the payment, determining its taxability, and collecting any tax that might be due. Therefore, the IRS ruled that the six-year statute of limitations on assessment applied.

• That ruling demonstrates the IRS's broad interpretation as to what constitutes an omission from gross income for purposes of Section 6501(e) and appears to be the wrong result.

• It is difficult to imagine a court agreeing that an omission of gross income includes a payment that does not even con-

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stitute "gross income" under the code.

• The IRS seemed to acknowledge that fact when it stated that "Sections 881 and 1442 impose tax on gross income, and Section 6501(e) also relates to omissions of gross income. Because the distribution . . . was not in fact gross income, there are litigating hazards with respect to this issue."

• The IRS also indicated that it is "questionable" whether any penalties would apply in the situation because, if the taxes were assessed and paid now, the shareholder would be entitled to a refund.

• A more complicated issue has arisen whether the unlimited statute of limitations under Section 6501(c)(3) will apply for issuing a notice of deficiency to a U.S. subsidiary that fails to withhold tax and timely file a Form 1042, if the withholding tax liability arises from a Section 482 adjustment to the subsidiary's income, the tax on which cannot be assessed or collected because of the expiration of the statute of limitations under Section 6501(a).

• In 1997 FSA Lexis 518, a federal income tax examination of a U.S. subsidiary's Form 1120 resulted in an allocation of income to that subsidiary from its Japanese parent under Section 482. That income allocation caused an increase in the subsidiary's earnings and profits and resulted in a "conforming" Section 482 adjustment that was treated as a dividend by the subsidiary to the parent.

• The IRS's position was that this dividend was subject to withholding tax and, because no Forms 1042 were filed by the subsidiary for the years at issue, the unlimited statute of limitations on assessment applied for those years. The IRS stated, however, that the subsidiary did not have sufficient earnings and profits to cause the distribution to be characterized as a dividend to the parent without the Section 482 adjustment, and the IRS was prohibited from assessing the income tax on the income resulting from the Section 482 adjustment to the subsidiary because of the expiration of the three-year statute of limitations.

• The issue was whether the statute of limitations for issuing a notice of deficiency relating to the subsidiary's withholding tax liability on its Forms 1042 remained open, despite the fact that assessment and collection of the taxpayer's income tax liability on its Forms 1120 were barred by the statute of limitations. Somewhat surprisingly, the IRS ruled that the statute of limitations concerning the withholding tax liabilities did remain open.

• The IRS based its determination on the premise that the income tax liability of a recipient of income is separate and distinct from the liability of a withholding agent. That analysis is consistent with the Tax Court's holding in S.K. Liquidating Co. v. Commissioner, 64 T.C. 713, where the court held that "the two statutory notices of deficiency (one with respect to the withholding agent and the other with respect to the non-U.S. payee) . . . are based on two separate returns, the returns cover different taxable periods, and the asserted liabilities originate from taxes enacted for different purposes."

• Nevertheless, the IRS's analysis appears to contradict the Interstate Fire Insurance Co. decision. In circumstances different from those at issue in the FSA, the Sixth Circuit held "as a general rule the use and application of Section 482 does not result in an enforceable tax consequence until there has been a reallocation resulting in a reassessment of taxes."

• In the FSA, it would not have been possible for the IRS to assess taxes on the subsidiary's income resulting from the Section 482 adjustment because the statute of limitations on assessment against the subsidiary was time barred. In light of that factor and the possibility of litigation, the IRS recommended that the field agent "continue to coordinate with the National Office."

Can the Taxes be Collected Once Assessed?

• Although many of the cases and rulings discussed above generously interpret the statute of limitations on assessment provisions in favor of the IRS, as a practical matter it may not always be possible for the IRS to collect the taxes even if they are assessed.

• Once an assessment has been made against a taxpayer, the IRS is required to give the taxpayer notice of the assessed amount and demand payment within 60 days.

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• If the taxpayer fails to pay the assessed amount after notice and demand for payment, the federal tax lien arises under Section 6321. That federal tax lien attaches to property wherever situated, including foreign-situs property.

• The code, however, does not provide the IRS with express statutory authority to take administrative collection action against foreign-situs property.

• The IRS's best opportunity to collect U.S. taxes from a non-U.S. taxpayer would be under a collection assistance provision contained in a U.S. tax treaty.

• In general, there are two types of collection assistance provisions in U.S. tax treaties:

— (i) "narrower purpose provisions" and

— (ii) "broader purpose provisions."

• The majority of the income tax treaties concluded with the United States contain the narrower purpose clause, which are basically designed to ensure that the tax treaty benefits are enjoyed only by those entitled to them, and therefore function primarily as anti-abuse provisions.

• The typical narrower purpose collection assistance provision reads as follows:

(1) Each of the Contracting States shall endeavor to collect on the behalf of the other Contracting State such amounts as may be necessary to ensure that relief granted by the present Convention from taxation imposed by such other Contracting State does not inure to the benefit of persons not entitled thereto.

(2) This paragraph shall not impose upon either of the Contracting States the obligation to carry out administrative measures that would be contrary to its sovereignty, security or public policy.

• The second category of collection assistance provision (the broader purpose provision) found in U.S. tax treaties serves a much different function than the narrower purpose one as it obligates the contracting states to lend assistance and support to each other in collecting taxes to which the treaty applies, without regard to the limited anti-abuse purpose.

• Only five U.S. income tax treaties contain such a provision

— Denmark, France, Canada, the Netherlands, and Sweden. Similarly,

• Only five U.S. estate and/or gift tax treaties contain similar provisions

— Finland, France, Greece, Italy, and South Africa.

• The typical broader purpose provision provides, in relevant part, that:

(1) The Contracting States undertake to lend assistance and support to each other in the collection of the taxes to which this Convention applies (together with interest, costs, and additions to the taxes and fines not being of a penal character) in cases where the taxes are definitively due according to the laws of the State making the application.

(2) Revenue claims of each of the Contracting States which have been finally determined will be accepted for enforcement by the State to which application is made and collected in that State in accordance with the laws applicable to the enforcement and collection of its own taxes.

(3) If the revenue claim has not been finally determined, the State to which application is made will take such measures of conservancy (including measures with respect to transfer of property of nonresident aliens) as are authorized by its laws for the enforcement of its own taxes.

• There is only one domestic case dealing with collection assistance provisions in a U.S. income tax treaty.

• In Miller v. United States, 955 F. Supp. 795 (N.D. Ohio 1996), the U.S. District Court upheld an IRS treaty collection request to the Dutch government, which resulted in the seizure of the taxpayer's assets held in a bank safe deposit box in the Netherlands.

• Despite that decision, because of the relatively few treaties that contain broader purpose collection assistance provisions and the lack of favorable case law supporting the IRS in its extraterritorial enforcement and collection efforts, the IRS may be facing an uphill battle when it comes to actually collecting U.S. taxes that have been assessed against non-U.S. taxpayers.

IRS Strategic Plan

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STRATEGY 1: Expand the use of alternative taxpayer treatments, including soft notices and other non-audit contacts
STRATEGY 2: Review and enhance current notice regimen
STRATEGY 3: Provide and expand incentives for taxpayers to conduct independent external audits
STRATEGY 4: Increase self-correction opportunities for taxpayers

OBJECTIVE 3: Meet the challenges of international tax administration

Recognizing the tax administration challenges presented by the explosive growth in cross-border transactions, the IRS joined with its counterparts in the United Kingdom, Australia, Canada and Japan to establish the Joint International Tax Shelter Information Centre (JITSIC). More recently, China has joined as an observer. This effort co-locates highly technical personnel from all countries to conduct bilateral exchanges of information on potentially abusive tax shelter transactions. An example of this group's success was the detection of an abusive scheme that improperly generated a foreign tax credit by large multinational corporations. It is highly unlikely that these transactions would have been uncovered and understood without JITSIC.

Taxpayers with international activities — including individuals, businesses, and tax-exempt organizations — are growing in number and variety. With businesses that have multiple domestic and global-tiered entities, for example, it is often difficult for a taxing authority to determine the full scope and resulting impact of any particular transaction. Different jurisdictions impose varying legal requirements on multinational enterprises, leading to complex business structures. In addition, the percentage of Americans' income originating from foreign sources doubled between 2001 and 2006.

The IRS must invest to meet the challenges of international tax administration. We will train employees to identify and understand issues in a complex and cross-border international environment. Even basic issues, such as the correct reporting of income, might require our employees to understand returns prepared under the International Financial Reporting Standards. We will continue to develop deep expertise on specific international enforcement topics, such as how to treat transfer pricing, and will support our people with the systems and processes needed to analyze data related to international enforcement efforts.

The IRS will also continue to work with other nations to coordinate and cooperate on enforcement issues. We will increase the effectiveness of tax treaties with partner nations and international organizations and participate in cooperative efforts to identify tax issues.

We will carefully study the risks associated with international financial activities and identify priorities for increased enforcement resources. We will explore innovative enforcement strategies that keep pace with the realities of a globalized tax environment, including convening issue management teams and conducting strong, issue-based risk assessments to target the areas of most significant risk.

STRATEGY 1: Expand employee knowledge and awareness of international tax issues
STRATEGY 2: Develop deep expertise and capabilities in key international issue areas
STRATEGY 3: Enhance coordination with treaty partners and international organizations
STRATEGY 4: Aggressively target areas of significant risk

OBJECTIVE 4: Allocate compliance resources using a data-driven approach to target existing and emerging high-risk areas

It is essential that the IRS continue to direct resources toward enforcement activities that have the greatest overall impact on compliance. The IRS has already made significant advancements in efficient enforcement of the law. In 2007, we collected $12.60 for every dollar spent on enforcement.

By enhancing our case-selection processes, the IRS will focus its enforcement tools on activities that pose the highest risk of noncompliance. We will make extensive use of our research capabilities to inform our efforts. The IRS will sustain its focus on taxpayer populations where complexity creates opportunities for noncompliance, such as flow-through

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entities, high-income individuals and corporations. We will also continue to investigate those who create and promote tax schemes to ensure that we aggressively address and deter noncompliance.

False claims for tax refunds continue to be a significant risk for fraud. We will focus resources on criminal investigations involving existing and emerging high-risk areas, developing the necessary personnel and technological resources to identify, investigate, prosecute, and publicize the convictions of taxpayers participating in this criminal activity.

STRATEGY 1: Identify high-risk transactions and taxpayers by revising and enhancing case selection procedures

STRATEGY 2: Continue focus on corporations, high-income individuals, business income, and flow-through entities

STRATEGY 3: Identify and pursue promoters of tax schemes

STRATEGY 4: Improve filing compliance by implementing a comprehensive non-filer program

STRATEGY 5: Increase focus on criminal investigations of existing and emerging high-risk areas

Large corporate taxpayers are required to report separately certain financial transactions to the IRS — more than 100,000 transactions every year. The IRS uses this data to focus its resources on areas of highest risk and to detect issues sooner in the audit process.

OBJECTIVE 5: Continue focused oversight of the tax-exempt sector

The 489 non-profit hospitals covered by a recent IRS study represent approximately $88 billion in annual revenues, and a similar amount of total assets. The study provides valuable insights into how they provide community benefit and meet the standards required under the law.

More than $15 trillion in assets are currently controlled by tax-exempt organizations or held in tax-exempt retirement programs and financial instruments. The massive size of this sector requires us to provide more careful oversight and advisory support than ever before.

Tax-exempt and government entities often find it difficult to navigate the complicated, specialized and changing tax rules that apply to them. The IRS will provide guidance and information to help tax-exempt and government entities understand their responsibilities and comply with the law. We will also discourage those who abuse tax-exempt status by actively seeking them out and addressing wrongdoing, making it clear that violations carry a high risk of meaningful punishment.

Certain segments of the tax-exempt sector, such as hospitals and universities, are especially large, complex and growing. For example, university endowments grew by 17 percent to $411 billion in 2007, with the largest nearing $35 billion. Due to their size and complexity, and consequent risk to the tax base, the IRS will continue to monitor compliance and enforce the rules applicable to universities, hospitals and other major segments of the tax-exempt community.

STRATEGY 1: Provide outreach and guidance to ensure widespread adherence to the requirements for tax-exempt status

STRATEGY 2: Proactively address misuse of tax-exempt organizations and/or tax-exempt status

STRATEGY 3: Maintain focus on universities, hospitals and other major segments of the tax-exempt community

OBJECTIVE 6: Ensure that all tax practitioners, tax preparers, and other third parties in the tax system adhere to professional standards and follow the law

With preparers numbering approximately 1 million, their actions have an enormous impact on our ability to administer the tax laws effectively.

As we focus on providing service to tax preparers, we will also expect cooperation from them. The IRS will implement a coordinated, servicewide plan to ensure a consistent and appropriate approach to preparer noncompliance.

When preparers fail to follow the law, they not only contribute to the tax gap, they erode public confidence in the tax system and create serious consequences for the taxpayers they represent. For those preparers and practitioners who engage in misconduct and illegal activity, the IRS will apply the most effective penalties available. We will expand our

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analytical capabilities to identify and prioritize areas of noncompliance and abuse associated with third parties. Using these new capabilities, we will design specific outreach and enforcement efforts.

STRATEGY 1: Develop and implement a coordinated preparer plan across the IRS and the preparer community

STRATEGY 2: Administer a fair, diligent, and effective system of sanctions and penalties for those who fail to follow the law

STRATEGY 3: Leverage research to identify fraudulent return preparers and other areas of abuse and noncompliance by return preparers

To ensure compliance by paid return preparers and in an effort to protect clients, the IRS monitors and conducts due diligence audits on preparers who file questionable returns.

INSTRUCTIONS FOR THESE REQUESTS-READ CAREFULLY

1. The term “document(s)” is used in the broadest sense and includes all attachments. Document(s) include any written, typed, photo static, recorded, or otherwise visually reproduced communications or presentations, whether comprised of letters, words, numbers, pictures, sounds, symbols, or any combination thereof. Document(s) refers to all written, printed, typed, graphically, visually or aurally reproduced material of any kind, or other means of preserving thought or expression, and all tangible things from which information can be processed or transcribed. Further, “documents” include, but are not limited to:

a. Items designated as internal, confidential, “not to be disclosed” or private;

b. All electronic mail (e-mail), whether on an electronic disk and/or any other system or device which saves e-mails, attachments, links; and

c. Videotapes, audiotapes, CDs, cassettes, DVDs, films, flash drives (memory sticks, etc.), microfilm, computer files, computer discs, computer programs and other electronic media.

2. If a document has been prepared in several copies, or additional copies have been made, and the copies are not identical (or, by reason of subsequent modification or notation, are no longer identical), each nonidentical copy is a separate “document.”

3. The taxpayer has “possession, custody, or control” if the taxpayer has actual or constructive possession of the document and/or can access the document upon inquiry and/or through a legal right to obtain the document.

4. All responsive documents in the taxpayer's possession, custody, or control should be provided, as well as all docuements, in the possession, custody or control of the taxpayer's agents, employees, and/or representatives, including, but not limited to, responsive documents in the possession, custody, or control of taxpayers' lawyer(s), accountant(s), banker(s), advisor(s), and/or trust advisor(s).

5. If any responsive document was, but is no longer, in the taxpayer's possession, custody or control, state what disposition was made of it, the reason for such disposition and who has possession or control of the document.

6. The term “taxpayer” means the individual under audit. The term “taxpayer” also means all foreign or domestic entities or structures over which the individual taxpayer exercises control including, but not limited to, corporations, partnerships, associations, limited liability companies, trusts, estates, foundations, escrows, charitable foundations, banks, and nominees.

7. A taxpayer can “exercise control” by acting directly or indirectly. Indirect control includes, but is not limited to, the use of nominees, agents, powers of attorney, protectors, advisors, trusts, letter of wishes, by-laws, letters of direction, or any device whatsoever.

8. The taxpayer has “signature or other authority” over an account if the taxpayer can control the disposition of money or other property in the account by delivery of a document containing the taxpayer's signature-either alone or with the signature of other person(s) and/or with code word(s) and/or code name(s)-to the bank or other person with whom the account is maintained, or if the taxpayer can exercise comparable authority over the account by direct or indirect commu-

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nication with the bank or other person with whom the account is maintained, either orally or by some other means.

9. If the taxpayer claims a "privilege" for any document responsive to any request, or any part of such document, specify:

a. name and title of the author;

b. date appearing on such document or, if undated, the date or approximate dates such document was created;

c. name and title of each addressee and of each recipients of the document and/or copies thereof;

d. subject matter of the document;

e. name and address of each person having present possession, custody, or control of such document and/or copies thereof;

f. privilege or protection claimed; and

g. number of the request(s) to which the production of the document would otherwise be responsible.

TAX RETURNS

1. Copies of all Tax Returns and Information Return Forms filed:

a. Form 1040, U.S. Income Tax return for Individuals including all schedules and attached informational returns for the years(s) 2001, 2002, 2003, 2004 and 2006.

b. Form 1099 received by the taxpayer for the year 2005.

c. Form 1099 issued by the taxpayer for the year 2005.

d. Form 1041, U. S. Income Tax return for Estates and Trusts, including all schedules and attached returns for which the taxpayer was the administrator, executor, fiduciary, trustee, grantor, or a beneficiary for years 2000, 2001, 2002, 2003, 2004, and 2005.

e. Form 3520A, Annual Information Return of Foreign Trust with a U. S. Owner for years 2000, 2001, 2003, 2004, and 2005 for which the taxpayer is or is treated as an owner

f. Form 3520, Annual Return to Report Transactions with Foreign Trusts and Receipt of Certain Foreign Gifts for years 2000, 2001, 2002, 2003, 2004, 2005 and 2006 for which the taxpayer is or is treated as an owner.

g. TD F90-22.1, Report of Foreign Bank and Financial Accounts for years 2000, 2001, 2002, 2003, 2004 and 2005.

h. All amended tax returns and informational returns.

BANK RECORDS

2. For each domestic bank account, in any name, over which the taxpayer had signature or other authority and/or over which the taxpayer exercised control, during the year 2005 produce all documents in the taxpayer's possession, custody, control including, but not limited to:

a. account applications (regardless of date)

b. monthly or periodic statements

c. wire transfer authorizations and confirmations

d. deposit slips and deposited items

e. credit and debit memos and advices

f. passbooks

g. safe deposit box rental agreements (regardless of date)

h. safe deposit box visitation ledgers

i. documents verifying the origin of all funds used to open the accounts or deposited to these accounts (regardless of date)

3. From the date of inception for each foreign bank account(s), i.e. opening the account(s), provide all period statements, under any name, over which the taxpayer had signature or other authority or over which the taxpayer exercised

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control.

a. account applications (regardless of date)

b. monthly or periodic statements

c. wire transfer authorizations and confirmations

d. deposit slips and deposited items

e. credit and debit memos and advices

f. passbooks

g. memorandum files maintained by the bank or other financial institution or any of their officers or employees, reflecting communications between the bank and the taxpayer or others acting on the taxpayer's behalf, and documenting actions taken pursuant to directions received from the taxpayer or on the taxpayer's behalf; and reflecting any thoughts or decisions of the bank or its employees or officers regarding the account

h. documents verifying the origin of all funds used to open the accounts or deposited to these accounts (regardless of date)

4. From the date of inception for each foreign bank account, i.e. opening the account(s), under any name, over which the taxpayer had signature or other authority and/or over which the taxpayer exercised control, produce the Know Your Customer Account information given to the bank and/or financial institution by the taxpayer and/or on the taxpayer's behalf including, but not limited to, all account set up documents (regardless of the year), such as signature cards, opening deposit slips, passport copies, certificates of beneficial ownership, letters of reference, certificates of clean funds and/or other source of funds documentation.

5. For each domestic Certificate of Deposit, Time Deposit, or equivalent account at a bank or financial institution, over which the taxpayer had signature authority or other authority or over which the taxpayer exercised control at any time during the year 2005 produce statements of certificate of deposit, records reflecting the purchase of the certificate, earnings, and records reflecting redemption or other disposition of the certificate. In addition, provide documents verifying the origin of all funds used to open these accounts or deposited to these accounts at any time.

6. From the date of inception, i.e. opening the account(s), for any foreign Certificate of Deposit, Time Deposit, or equivalent account at a bank or financial institution, over which the taxpayer had signature authority or other authority or over which the taxpayer exercised controll at any time, produce statements of certificate of deposit, records reflecting the purchase of the certificate, earnings, and records reflecting redemption or other disposition of the certificate. In addition, provide documents verifying the origin of all funds used to open these accounts or deposited or deposited to these accounts at any time.

7. For all transfers of funds between all bank accounts, financial accounts, and other accounts referred to in Requests “2”, “3”, “4”, “5” and “6” above, over which the taxpayer had signature or other authority, or over which the taxpayer exercised control, provide the following:

a. list of transfers

b. documents showing the source of the funds transferred (e.g., copy of check-back and front, wire transfer authorizations, bank statement, source of cash deposit)

c. documents showing the deposit of the funds transferred (e.g., bank statement)

8. All documents relating to domestic credit, debit, ATM or charge accounts over which the taxpayer had signature or other authority or over which the taxpayer exercised control for the year 2005 including, but not limited to:

a. card applications (regardless of date)

b. monthly or periodic charge statements

9. From the date of inception, i.e. opening the account(s), for each foreign credit, debit, ATM or charge account, all documents relating to foreign over which the taxpayer had signature or other authority or over which the taxpayer exercised control, including, but are not limited to:

a. card applications (regardless of date)

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b. agreements (regardless of date)
c. monthly or periodic charge statements

BROKERAGE OR SECURITIES ACCOUNTS

10. For each domestic brokerage or securities account, in any name, over which the taxpayer had signature, dealer or other authority or which the taxpayer controlled, either directly or through nominees, agents, powers of attorney, letters of direction, or any device whatsoever, during the year 2005 produce all documents in the taxpayer's possession, custody or control or to which the taxpayer had right of access for the period January 1, 2005 through December 31, 2005 including but not limited to:
a. account application (regardless of date)
b. signature cards (regardless of date)
c. monthly or periodic account statements
d. annual account summaries
e. wire transfer authorizations and confirmations
11. From the date of inception, i.e. opening the account(s), for each foreign brokerage/securities account(s), in any name, over which the taxpayer had signature, dealer or other authority or which the taxpayer controlled, either directly or through nominees, agents, powers of attorney, letters of direction, or any device whatsoever, produce all documents in the taxpayer's possession, custody or control or to which the taxpayer had the right of access, including but not limited to:
f. account application (regardless of date)
g. signature cards (regardless of date)
h. monthly or periodic account statements
i. annual account summaries
j. wire transfer authorizations and confirmations

OWNERSHIP

12. For each entity or structure--foreign or domestic-- in which the taxpayer exercised control and/or held an ownership interest, legal interest, fiduciary interest, and/or beneficial interest from the date of creation/inception of such entity(ies), provide all documents relating to each entity, including but not limited to:
a. organizational documents, deeds of incorporation, by-laws, registrations (regardless of date)
b. ownership documents including those reflecting the taxpayer's percentage of legal ownership, percentage of beneficial ownership, and all changes in ownership (regardless of date)
c. operational and business documents
d. financial statements
13. For each entity or structure identified in Request “12” above, provide all documents distributed, sent, and/or transmitted by or to any legal, fiduciary and/or beneficial owners to and from professionals (e.g., attorneys, accountants, bankers, trust advisors, etc.) including, but not limited to, contracts, agreements, advisories, schedules, letters, memoranda, notes, and instructions.
14. For each entity or structure identified in Request “12” above, provide the name, address and telephone number of the person(s) controlling the assets of the entity or structure from the date of inception/creation.
15. All written contracts, agreements, letters, memoranda, notes, statements, and all other documents of the years 2000, 2001, 2002, 2003, 2004 and 2005 pertaining to the assignment and transfer of ownership interest in the rights to use of real, personal or intangible property by or for the taxpayer or the taxpayer's benefit.
16. All powers of attorney giving the taxpayer authority to act on behalf of any person or entity, foreign or domestic,

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during the years 2000, 2001, 2002, 2003, 2004 and 2005.

17. All powers of attorney executed by the taxpayer giving another the authority to act on the taxpayer's behalf or on behalf of any person or entity, whether foreign or domestic over which the taxpayer exercises control, during the years 2000, 2001, 2002, 2003, 2004 and 2005.

18. All certificates of beneficial ownership, stock certificates, including bearer shares, or other similar evidences of ownership interests owned by the taxpayer at any time, from the date of creation/inception with respect to any foreign trust, corporation, foundation, international business company, or similar entity.

NON-TAXABLE SOURCES OF INCOME

19. All records pertaining to any non-taxable sources of income, including, but not limited to, child support, proceeds of loans, gifts, inheritances, insurance settlements, tax refunds, and tax-exempt interest the taxpayer received for years 2005 and 2006.

LOANS

20. For each loan, whether commercial or private, made or obtained by the taxpayer or on the taxpayer's behalf during the year 2005 or which was in existence during the year 2005 provide all documents evidencing the term and performance of the transaction, including, but not limited to:

a. loan applications (regardless of date)
b. loan agreements and contracts (regardless of date)
c. loan amortization schedules (regardless of date)
d. promissory notes
e. grant deeds, deeds of trust, mortgages, or other security
f. documents showing disbursement of the loan proceeds (e.g., wire transfer authorization)
g. records of receipt of principal and interest
h. records of payment of principal and interest

PROFESSIONALS

21. Provide the name, address, telephone number of each private banker, broker, trust advisor, investment or other financial advisor, advisor on privacy matters, lawyer and accountant from whom the taxpayer received advice or services during the years 2000, 2001, 2002, 2003, 2004 and 2005.

22. All business cards for attorneys, paralegals, consultants, accountants, and/or other professionals in the taxpayer's possession and/or within the taxpayer's control during years 2000, 2001, 2002, 2003, 2004 and 2005.

23. All records relating to any payments in the years 2000, 2001, 2002, 2003, 2004 and 2005 by or for the benefit of the taxpayer or any nonpublically traded domestic entity, in which the taxpayer held a direct or indirect ownership or beneficial interest or over which the taxpayer exercised control, either directly or through a nominee, agent, power of attorney, letter of direction, letter of wishes, or any device whatsoever, for:

a. management fees
b. consulting fees
c. legal fees

24. From the date of inception/creation, all records relating to any payments by or for the benefit of the taxpayer or any nonpublically traded foreign entity, in which the taxpayer held a direct or indirect ownership or benefical interest or over which the taxpayer exercised control, either directly or through a nominee, agent, power of attorney, letter of direction, letter of wishes, or any device whatsoever, for:

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a. management fees
b. consulting fees
c. legal fees

TRAVEL

25. All of the taxpayer's original U.S. passports, both current and expired.
26. All of the taxpayer's original foreign passports, both current and expired.
27. All records of foreign travel during the years 2000, 2001, 2002, 2003, 2004 and 2005, including, but not limited to, commercial transportation, private leasing, and vehicles/aircraft/boats owned by the taxpayer.

OTHER

28. Copy of divorce decree/settlement, including all schedules and attachments.

Foreign Accounts/Entities Information

Part I: Do you have any legal or beneficial interest in, or direct or indirect signature, management, or other authority over foreign bank accounts or brokerage accounts or mutual funds in the following countries, between 1997 and the present?

If yes, please describe the type of account and name of account holder.

Bank Secrecy Jurisdiction Countries	Geographical Location			
Andorra	Europe	yes	no	____________________
Anguilla	Caribbean	yes	no	____________________
Antigua and Barbuda	Caribbean	yes	no	____________________
Aruba	Caribbean	yes	no	____________________
Austria	Europe	yes	no	____________________
Bahamas	Caribbean	yes	no	____________________
Bahrain	Arabian Sea	yes	no	____________________
Barbados	Caribbean	yes	no	____________________
Belize	Caribbean/Central America	yes	no	____________________
British Virgin Islands	Caribbean	yes	no	____________________
Cook Islands	Pacific Ocean	yes	no	____________________
Gibraltar	Europe	yes	no	____________________
Grenada	Caribbean	yes	no	____________________
Guernsey/Sark/Alderney	Europe	yes	no	____________________
Isle of Man	Europe	yes	no	____________________

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Jersey	Europe	yes	no	____________________
Liberia	Horn of Africa	yes	no	____________________
Liechtenstein	Europe	yes	no	____________________
Montserrat	Caribbean	yes	no	____________________
Nauru	Pacific Ocean	yes	no	____________________
Netherlands Antilles	Caribbean	yes	no	____________________
Nevis	Caribbean	yes	no	____________________
Niue	Pacific Ocean	yes	no	____________________
Panama	Caribbean/Central America	yes	no	____________________
Samoa	Pacific Ocean	yes	no	____________________
St. Lucia	Caribbean	yes	no	____________________
St. Vincent and the Grenadines	Caribbean	yes	no	____________________
Switzerland	Europe	yes	no	____________________
The Commonwealth of Dominica	Caribbean	yes	no	____________________
The Principality of Monaco	Europe	yes	no	____________________
The Republic of the Maldives	Indian Ocean	yes	no	____________________
The Republic of the Marshall Islands	Pacific Ocean	yes	no	____________________
The Republic of the Seychelles	Indian Ocean	yes	no	____________________
The Republic of Vanuatu	Pacific Ocean	yes	no	____________________
Tonga	Pacific Ocean	yes	no	____________________
Turks & Caicos	Caribbean	yes	no	____________________
US Virgin Islands	Caribbean	yes	no	____________________

Part II: Do you have any legal or beneficial interest in, or direct or indirect signature, management, or other authority over foreign bank accounts or brokerage accounts or mutual funds in other foreign countries, between 1997 and the present?

yes_____ no_____

If yes, please list the countries in which you have foreign bank accounts or brokerage accounts or mutual funds, and describe the type of accounts:

____________________ ____________________

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____________________	____________________
____________________	____________________
____________________	____________________

Part III: Did you have any legal or beneficial interest in, or direct or indirect signature, management, investment or other authority over any foreign entities, trusts, corporations, partnerships, foundations in the following countries, between 1997 and the present?

If yes, please describe the type of entity, name of the entity, and relationship to the entity.

Bank Secrecy Jurisdiction Countries	Geographical Location			
Andorra	Europe	yes	no	____________________
Anguilla	Caribbean	yes	no	____________________
Antigua and Barbuda	Caribbean	yes	no	____________________
Aruba	Caribbean	yes	no	____________________
Bahamas	Caribbean	yes	no	____________________
Bahrain	Arabian Sea	yes	no	____________________
Barbados	Caribbean	yes	no	____________________
Belize	Caribbean/Central America	yes	no	____________________
British Virgin Islands	Caribbean	yes	no	____________________
Cook Islands	Pacific Ocean	yes	no	____________________
Gibraltar	Europe	yes	no	____________________
Grenada	Caribbean	yes	no	____________________
Guernsey/ Sark/Alderney	Europe	yes	no	____________________
Isle of Man	Europe	yes	no	____________________
Jersey	Europe	yes	no	____________________
Liberia	Horn of Africa	yes	no	____________________
Liechtenstein	Europe	yes	no	____________________
Montserrat	Caribbean	yes	no	____________________
Nauru	Pacific Ocean	yes	no	____________________
Netherlands Antilles	Caribbean	yes	no	____________________
Nevis	Caribbean	yes	no	____________________
Niue	Pacific Ocean	yes	no	____________________
Panama	Caribbean/Central America	yes	no	____________________
Samoa	Pacific Ocean	yes	no	____________________

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St. Lucia	Caribbean	yes	no	____________________
St. Vincent and the Grenadines	Caribbean	yes	no	____________________
Switzerland	Europe	yes	no	____________________
The Commonwealth of Dominica	Caribbean	yes	no	____________________
The Principality of Monaco	Europe	yes	no	____________________
The Republic of the Maldives	Indian Ocean	yes	no	____________________
The Republic of the Marshall Islands	Pacific Ocean	yes	no	____________________
The Republic of the Seychelles	Indian Ocean	yes	no	____________________
The Republic of Vanuatu	Pacific Ocean	yes	no	____________________
Tonga	Pacific Ocean	yes	no	____________________
Turks & Caicos	Caribbean	yes	no	____________________
US Virgin Islands	Caribbean	yes	no	____________________

Part IV: Did you have any legal or beneficial interest in, or direct or indirect signature, management, investment or other authority over any foreign entities, trusts, corporations, partnerships, foundations in other foreign countries, between 1997 and the present?

yes_____ no_____

If yes, please describe the type of entity name of the entity, and your relationship to the entity.

Part V: Certification/Declaration

I have read and completed the foregoing statements consisting or 3 pages, each of which I have signed. Under the penalties of perjury, I declare that I have examined this statement and to the best of my knowledge and belief, it is true, correct and complete.

____________________	____________________	____________________
TPH Signature	TPH Name	Date
____________________	____________________	____________________
TPW Signature	TPW Name	Date

Analysis & Update on Offshore Bank Investigations

Internal Revenue Service

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Form 4564

Liechtenstein

INSTRUCTIONS FOR THESE REQUESTS-READ CAREFULLY

1. The term “documents)” is used in the broadest sense and includes all attachments. Documents) include any written, typed, photo static, recorded, or otherwise visually reproduced communications or presentations, whether comprised of letters, words, numbers, pictures, sounds, symbols, or any combination thereof. Documents) refers to all written, printed, typed, graphically, visually or aurally reproduced material of any kind, or other means of preserving thought or expression, and all tangible things from which information can be processed or transcribed. Further, “documents” include, but are not limited to:

a. Items designated as internal, confidential, “not to be disclosed” or private;

b. All electronic mail (e-mail), whether on an electronic disk and/or any other system or device which saves e-mails, attachments, links; and

c. Videotapes, audiotapes, CDs, cassettes, DVDs, films, flash drives (memory sticks, etc.), microfilm, computer files, computer discs, computer programs and other electronic media.

2. If a document has been prepared in several copies, or additional copies have been made, and the copies are not identical (or, by reason of subsequent modification or notation, are no longer identical), each non-identical copy is a separate “document.”

3. The taxpayer has “possession, custody, or control” if the taxpayer has actual or constructive possession of the document and/or can access the document upon inquiry and/or through a legal right to obtain the document.

4. All responsive documents in the taxpayer's possession, custody, or control should be provided, as well as all documents, in the possession, custody or control of the taxpayer's agents, employees, and/or representatives, including, but not limited to, responsive documents in the possession, custody, or control of taxpayers' lawyers), accountants), bankers), advisors), and/or trust advisor(s).

5. If any responsive document was, but is no longer, in the taxpayer's possession, custody or control, state what disposition was made of it, the reason for such disposition and who has possession or control of the document.

6. The term “taxpayer” means the individual under audit. The term “taxpayer” also means all foreign or domestic entities or structures over which the individual taxpayer exercises control including, but not limited to, corporations, partnerships, associations, limited liability companies, trusts, estates, foundations, escrows, charitable foundations, banks, and nominees.

7. A taxpayer can “exercise control” by acting directly or indirectly. Indirect control includes, but is not limited to, the use of nominees, agents, powers of attorney, protectors, advisors, trusts, letter of wishes, by-laws, letters of direction, or any device whatsoever.

8. The taxpayer has “signature or other authority” over an account if the taxpayer can control the disposition of money or other property in the account by delivery of a document containing the taxpayer's signature-either alone or with the signature of other persons) and/or with code word(s) and/or code name(s)-to the bank or other person with whom the account is maintained, or if the taxpayer can exercise comparable authority over the account by direct or indirect communication with the bank or other person with whom the account is maintained, either orally or by some other means.

9. If the taxpayer claims a “privilege” for any document responsive to any request, or any part of such document, specify:

a. name and title of the author;

b. date appearing on such document or, if undated, the date or approximate dates such document was created;

c. name and title of each addressee and of each recipients of the document and/or copies thereof;

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d. subject matter of the document;

e. name and address of each person having present possession, custody, or control of such document and/or copies thereof;

f. privilege or protection claimed; and

g. number of the requests) to which the production of the document would otherwise be responsible.

TAX RETURNS (Cont.)

1. Copies of all Tax Returns and Information Return Forms filed:

a. Form 1040, U.S. Income Tax return for Individuals including all schedules and attached informational returns for the years(s) 2001, 2002,2003, 2004 and 2006.

b. Form 1099 received by the taxpayer for the year 2005.

c. Form 1099 issued by the taxpayer for the year 2005.

d. Form 1041, U. S. Income Tax return for Estates and Trusts, including all schedules and attached returns for which the taxpayer was the administrator, executor, fiduciary, trustee, grantor, or a beneficiary for years 2000, 2001, 2002, 2003, 2004, and 2005.

e. Form 3520A, Annual Information Return of Foreign Trust with a U. S. Owner for years 2000, 2001, 2003, 2004, and 2005 for which the taxpayer is or is treated as an owner.

f. Form 3520, Annual Return to Report Transactions with Foreign Trusts and Receipt of Certain Foreign Gifts for years 2000, 2001, 2002,2003,2004, 2005 and 2006 for which the taxpayer is or is treated as an owner.

g. TD F90-22.1, Report of Foreign Bank and Financial Accounts for years 2000, 2001,2002, 2003, 2004 and 2005. h. All amended tax returns and informational returns.

h. All amended tax returns and informational returns.

BANK RECORDS

2. For each **domestic bank account**, in any name, over which the taxpayer had signature or other authority and/or over which the taxpayer exercised control, during the year 2005 produce all documents in the taxpayer's possession, custody, control including, but not limited to:

a. account applications (regardless of date)

b. monthly or periodic statements

c. wire transfer authorizations and confirmations

d. deposit slips and deposited items

e. credit and debit memos and advices

f. passbooks

g. safe deposit box rental agreements (regardless of date)

h. safe deposit box visitation ledgers

i. documents verifying the origin of all funds used to open the accounts or deposited to these accounts (regardless of date)

3. From the date of inception for each **foreign bank accounts**), i.e. opening the accounts), provide all period statements, under any name, over which the taxpayer had signature or other authority or over which the taxpayer exercised control.

a. account applications (regardless of date)

b. monthly or periodic statements

c. wire transfer authorizations and confirmations

d. deposit slips and deposited items

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e. credit and debit memos and advices

f. passbooks

g. memorandum files maintained by the bank or other financial institution or any of their officers or employees, reflecting communications between the bank and the taxpayer or others acting on the taxpayer's behalf, and documenting actions taken pursuant to directions received from the taxpayer or on the taxpayer's behalf; and reflecting any thoughts or decisions of the bank or its employees or officers regarding the account

h. documents verifying the origin of all funds used to open the accounts or deposited to these accounts (regardless of date)

4. From the date of inception for each **foreign bank account**, i.e. opening the accounts), under any name, over which the taxpayer had signature or other authority and/or over which the taxpayer exercised control, produce the Know Your Customer Account information given to the bank and/or financial institution by the taxpayer and/or on the taxpayer's behalf including, but not limited to, all account set up documents (regardless of the year), such as signature cards, opening deposit slips, passport copies, certificates of beneficial ownership, letters of reference, certificates of clean funds and/or other source of funds documentation.

5. For each **domestic Certificate of Deposit, Time Deposit, or equivalent account at a bank** or financial institution, over which the taxpayer had signature authority or other authority or over which the taxpayer exercised control at any time during the year 2005 produce statements of certificate of deposit, records reflecting the purchase of the certificate, earnings, and records reflecting redemption or other disposition of the certificate. In addition, provide documents verifying the origin of all funds used to open these accounts or deposited to these accounts at any time.

6. From the date of inception, i.e. opening the accounts), for any foreign Certificate of Deposit, Time Deposit, or equivalent account at a bank or financial institution, over which the taxpayer had signature authority or other authority or over which the taxpayer exercised control) at any time, produce statements of certificate of deposit, records reflecting the purchase of the certificate, earnings, and records reflecting redemption or other disposition of the certificate. In addition, provide documents verifying the origin of all funds used to open these accounts or deposited or deposited to these accounts at any time.

7. For **all transfers of funds between all bank accounts**, financial accounts, and other accounts referred to in Requests “2”, “3”, “4”, “5” and “6” above, over which the taxpayer had signature or other authority, or over which me taxpayer exercised control, provide the following:

a. list of transfers

b. documents showing the source of the funds transferred (e.g., copy of check-back and front, wire transfer authorizations, bank statement, source of cash deposit)

c. documents showing the deposit of the funds transferred (e.g., bank statement)

8. All documents relating to **domestic credit, debit, ATM or charge accounts** over which the taxpayer had signature or other authority or over which the taxpayer exercised control for the year 2005 including, but not limited to:

a. card applications (regardless of date)

b. monthly or periodic charge statements

9. From the date of inception, i.e. opening the account(s), for **each foreign credit, debit, ATM or charge account**, all documents relating to foreign over which the taxpayer had signature or other authority or over which the taxpayer exercised control, including, but are not limited to:

a. card applications (regardless of date)

b. agreements (regardless of date)

c. monthly or periodic charge statements

BROKERAGE OR SECURITIES ACCOUNTS

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10. For each **domestic brokerage or securities account**, in any name, over which the taxpayer had signature, dealer or other authority or which the taxpayer controlled, either directly or through nominees, agents, powers of attorney, letters of direction, or any device whatsoever, during the year 2005 produce all documents in the taxpayer's possession, custody or control or to which the taxpayer had right of access for the period January 1, 2005 through December 31, 2005 including but not limited to:

a. account application (regardless of date)

b. signature cards (regardless of date)

c. monthly or periodic account statements

d. annual account summaries

e. wire transfer authorizations and confirmations

11. From the date of inception, i.e. opening the accounts), for each foreign brokerage/securities accounts), in any name, over which the taxpayer had signature, dealer or other authority or which the taxpayer controlled, either directly or through nominees, agents, powers of attorney, letters of direction, or any device whatsoever, produce all documents in the taxpayer's possession, custody or control or to which the taxpayer had the right of access, including but not limited to:

a. account application (regardless of date)

b. signature cards (regardless of date)

c. monthly or periodic account statements

d. annual account summaries

e. wire transfer authorizations and confirmations

OWNERSHIP

12. For each entity or structure-foreign or domestic- in which the taxpayer exercised control and/or held an ownership interest, legal interest, fiduciary interest, and/or beneficial interest from the date of creation/inception of such entity(ies), provide all documents relating to each entity, including but not limited to:

a. organizational documents, deeds of incorporation, by-laws, registrations (regardless of date)

b. ownership documents including those reflecting the taxpayer's percentage of legal ownership, percentage of beneficial ownership, and all changes in ownership (regardless of date)

c. operational and business documents

d. financial statements

13. For each entity or structure identified in Request “12” above, provide all documents distributed, sent, and/or transmitted by or to any legal, fiduciary and/or beneficial owners to and from professionals (e.g., attorneys, accountants, bankers, trust advisors, etc.) including, but not limited to, contracts, agreements, advisories, schedules, letters, memoranda, notes, and instructions.

14. For each entity or structure identified in Request “12” above, provide die name, address and telephone number of the person(s) controlling the assets of the entity or structure from the date of inception/creation.

15. All written contracts, agreements, letters, memoranda, notes, statements, and all other documents of the years 2000, 2001, 2002, 2003, 2004 and 2005 pertaining to the assignment and transfer of ownership interest in the rights to use of real, personal or intangible property by or for the taxpayer or the taxpayer's benefit.

16. All powers of attorney giving the taxpayer authority to act on behalf of any person or entity, foreign or domestic, during the years 2000, 2001, 2002, 2003,2004 and 2005.

17. All powers of attorney executed by the taxpayer giving another the authority to act on the taxpayer's behalf or on behalf of any person or entity, whether foreign or domestic over which the taxpayer exercises control, during the years 2000,2001, 2002, 2003, 2004 and 2005.

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18. All certificates of beneficial ownership, stock certificates, including bearer shares, or other similar evidences of ownership interests owned by the taxpayer at any time, **from the date of creation/inception with respect to any foreign trust, corporation, foundation, international business company, or similar entity.**

Non-Taxable Sources of Income

19. All records pertaining to any non-taxable sources of income, including, but not limited to, child support, proceeds of loans, gifts, inheritances, insurance settlements, tax refunds, and tax-exempt interest the taxpayer received for years 2005 and 2006.

LOANS

20. For each loan, whether commercial or private, made or obtained by the taxpayer or on the taxpayer's behalf during the year 2005 or which was in existence during the year 2005 provide all documents evidencing the term and performance of the transaction, including, but not limited to:

a. loan applications (regardless of date)
b. loan agreements and contracts (regardless of date)
c. loan amortization schedules (regardless of date)
d. promissory notes
e. grant deeds, deeds of trust, mortgages, or other security
f. documents showing disbursement of the loan proceeds (e.g., wire transfer authorization)
g. records of receipt of principal and interest
h. records of payment of principal and interest

PROFESSIONALS

21. Provide the name, address, telephone number of each private banker, broker, trust advisor, investment or other financial advisor, advisor on privacy matters, lawyer and accountant from whom the taxpayer received advice or services during the years 2000, 2001, 2002, 2003, 2004 and 2005.

22. All business cards for attorneys, paralegals, consultants, accountants, and/or other professionals, in the taxpayer's possession and/or within the taxpayer's control during years 2000, 2001, 2002, 2003, 2004 and 2005.

23. All records relating to any payments in the years 2000,2001,2002,2003,2004 and 2005 by or for the benefit of the taxpayer or any nonpublically traded domestic entity, in which the taxpayer held a direct or indirect ownership or beneficial interest or over which the taxpayer exercised control, either directly or through a nominee, agent, power of attorney, letter of direction, letter of wishes, or any device whatsoever, for:

a. management fees
b. consulting fees
c. legal fees

24. From the date of inception/creation, all records relating to any payments by or for the benefit of the taxpayer or any nonpublically traded **foreign entity,** in which the taxpayer held a direct or indirect ownership or beneficial interest or over which the taxpayer exercised control, either directly or through a nominee, agent, power of attorney, letter of direction, letter of wishes, or any device whatsoever, for:

a. management fees
b. consulting fees
c. legal fees

TRAVEL

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25. All of the taxpayer's original U.S. passports, both current and expired.
26. All of the taxpayer's original foreign passports, both current and expired.
27. All records of foreign travel during the years 2000, 2001, 2002, 2003, 2004 and 2005, including, but not limited to, commercial transportation, private leasing, and vehicles/aircraft/boats owned by the taxpayer.

OTHER

28. Copy of divorce decree/settlement, including all schedules and attachments.

Foreign Accounts/Entities Information

Part I: Do you have **any legal or beneficial interest in, or direct or indirect signature, management, or other authority over foreign bank accounts or brokerage accounts or mutual funds** in the following countries, between 1997 and the present? If yes, please describe the type of account and name of account holder.

Client Interview Liechtenstein Foundation

Foreign Accounts/Entities Information

Bank Secrecy Jurisdiction Countries	Geographical Location
Andorra	Europe
Anguilla	Caribbean
Antigua and Barbuda	Caribbean
Aruba	Caribbean
Austria	Europe
Bahamas	Caribbean
Bahrain	Arabian Sea
Barbados	Caribbean
Belize	Caribbean/Central America
British Virgin Islands	Caribbean
Cook Islands	Pacific Ocean
Gibraltar	Europe
Grenada	Caribbean
Guernsey/Sark/Aldemey	Europe
Isle of Man	Europe
Jersey	Europe
Liberia	Horn of Africa
Liechtenstein	Europe
Montserrat	Caribbean
Nauru	Pacific Ocean
Netherlands Antilles	Caribbean
Nevis	Caribbean

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Niue	Pacific Ocean
Panama	Caribbean/Central America
Samoa	Pacific Ocean
St. Lucia	Caribbean
St. Vincent and the Grenadines	Caribbean
Switzerland	Europe
The Commonwealth of Dominica	Caribbean
The Principality of Monaco	Europe
The Republic of the Maldives	Indian Ocean
The Republic of the Marshall Islands	Pacific Ocean
The Republic of the Seychelles	Indian Ocean
The Republic of Vanuatu	Pacific Ocean
Tonga	Pacific Ocean
Turks & Caicos	Caribbean
US Virgin Islands	Caribbean

Part II: Do you have any legal or beneficial interest in, or direct or indirect signature, management, or other authority over foreign bank accounts or brokerage accounts or mutual funds in other foreign countries, between 1997 and the present?

Yes ________ no ________

If yes, please list the countries in which you have foreign bank accounts or brokerage accounts or mutual funds, and describe the type of accounts:

____________________ ____________________

____________________ ____________________

Part III: Did you have any legal or beneficial interest in, or direct or indirect signature, management, investment or other authority over any foreign entities, trusts, corporations, partnerships, foundations in the following countries, between 1997 and the present? If yes, please describe the type of entity, name of the entity, and relationship to the entity.

	Bank Secrecy Jurisdiction Countries	Geoaraphical Location
•	Andorra	Europe
•	Anguilla	Caribbean
•	Antigua and Barbuda	Caribbean
•	Aruba	Caribbean
•	Bahamas	Caribbean
•	Bahrain	Arabian Sea
•	Barbados	Caribbean
•	Belize	Caribbean/Central America

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•	British Virgin Islands	Caribbean
•	Cook Islands	Pacific Ocean
•	. Glbraltar	Europe
•	Grenada	Caribbean
•	Guemsey/Sark/Aldemey	Europe
•	Isle of Man	Europe
•	. Jersey	Europe
•	Liberia	Horn of Africa
•	Liechtenstein	Europe
•	Montserrat	Caribbean
•	Nauru	Pacific Ocean
•	Netherlands Antilles	Caribbean
•	Nevis	Caribbean
•	Niue	Pacific Ocean
•	• Panama	Caribbean/Central America
•	Samoa	Pacific Ocean
•	St Lucia	Caribbean
•	St. Vincent and the Grenadines	Caribbean
•	Switzerland	Europe
•	The Commonwealth of Dominica	Caribbean
•	The Principality of Monaco	Europe
•	The Republic of the Maldives	Indian Ocean
•	The Republic of the Marshall Islands	Pacific Ocean
•	The Republic of the Seychelles	Indian Ocean
•	The Republic of Vanuatu	Pacific Ocean
•	Tonga	Pacific Ocean
•	Turks & Caicos	Caribbean
•	US Virgin Islands	Caribbean

Part IV: Did you have any legal or beneficial interest in, or direct or indirect signature, management, investment or other authority over any foreign entities, trusts, corporations, partnerships, foundations in other foreign countries, between 1997 and the present?

Yes ________ no ________

If yes, please describe the type of entity, name of the entity, and your relationship to the entity.

____________________ ____________________

____________________ ____________________

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___________________ ___________________

Part V: Certification/Declaration

I have read and completed the foregoing statements consisting of 3 pages, each of which I have signed. Under the penalties of perjury, I declare that I have examined this statement and to the best of my knowledge and belief, it is true, correct and complete.

___________________	___________________	___________________
TPH Signature	TPH Name	Date
___________________	___________________	___________________
TPW Signature	TPW Name	Date

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Real Estate
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MARSHALL R. PASTERNACK and **ANDREW** H. **WEINSTEIN**, Attorneys, Miami [FNa1]

HOW TO CONTROL THE INTEREST AND BASIS PROBLEMS CREATED BY THE NEW TYPES OF MORTGAGES

Mortgages involving adjustments to interest or principal as well as those calling for a sharing of the increase of the property's value all present tax considerations that may differ from a fixed-rate mortgage. This article analyzes the tax effects of the various types of mortgages currently in use.

Due to the volatility of interest rates during the past decade, lenders and borrowers have become increasingly creative. Some of the creations, such as the variable rate mortgage, have reflected a desire to remain flexible in the face of uncertain economic conditions. Other designs, such as the shared appreciation mortgage, reflect the lender's desire to benefit from (and the borrower's willingness to share) the increase in value of the property for which the loan is made.

The variations to the traditional fixed-rate mortgage may be classified into three main categories: (1) those involving principal adjustments, (2) those involving interest rate adjustments, and (3) those involving the ability of the lender to share in the increase in value of the subject property. In analyzing the tax consequences of mortgages in each of these categories, there are two general considerations that must be taken into account, as indicated in the box on p. 285.

Principal adjustment mortgages

The least troublesome of the recent mortgage variations, from a tax standpoint, is the principal adjustment mortgage. Mortgages that provide for principal adjustments at periodic dates include those generally referred to as equity adjustment mortgages, growing equity mortgages, and price level adjusted mortgages.

Equity adjustment mortgages. Under an equity adjustment mortgage, the loan agreement provides for automatic additional loans each year, based on a specified percentage of the equity accumulation over the prior year. Such mortgages should have no effect on the purchaser's basis in the property purchased with the proceeds of the original loan. [FN1] Interest on the original as well as the increased mortgage amount should be deductible in full in accordance with the borrower's method of accounting.

Growing equity mortgages. A growing equity mortgage, under which the mortgage payments are increased over time, reflecting increased principal payments, should have no adverse tax consequences to the borrower. Basis in the property will be unaffected, and the interest payments will be deductible in full in accordance with the borrower's method of accounting.

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Price level adjusted mortgages. More troublesome is the price level adjusted mortgage (PLAM) in which the outstanding principal balance is periodically adjusted by a percentage change in a selected price index. At the time of the original acquisition, the principal amount of the mortgage, as well as the other consideration given by the purchaser, will be included in the buyer's basis. Under a PLAM, however, the principal amount will be subject to change. Two alternatives are possible with respect to such adjustments. If the mortgage is a purchase money mortgage, an argument can be made that the adjustment reflects a change in the purchase price of the property. If such is the case, the borrower should be entitled to allocate such increase to the various assets to which the mortgage relates. Depreciation deductions should be available with respect to the portion of the basis increase allocable to depreciable property.

A question arises, however, as to whether the borrower would also be entitled to the investment tax credit and whether a decrease in the principal amount would trigger depreciation and investment tax credit recapture. In *Panhandle Eastern Pipeline Co.* [FN1a] the Court of Claims distinguished between adjusted basis under Section 1011 and cost basis under Section 1012 in holding that no recapture of investment credit is required as a result of a basis reduction following an election under Section 108 (regarding income from discharge of indebtedness). If changes in the principal amount of a purchase money PLAM affect adjustments to cost basis, it is not clear whether they are retroactive adjustments to cost basis for investment tax credit purposes, or merely prospective adjustments to basis for purposes of determining gain or loss.

If the mortgage is not of the purchase money variety, the tax treatment associated with the changing principal amount is not clear. Unlike an equity adjustment mortgage, the borrower receives no additional cash when the principal amount of a PLAM increases. Whether this increase is chargeable to the capital account or represents additional interest remains an open question. In any event, any additional interest charged as the result of the increased principal should be deductible in full in accordance with the borrower's method of accounting.

Interest rate adjustments

Variable-rate mortgages. Mortgages involving interest rate adjustments have become increasingly popular over the past few years. The most popular forms of such mortgages are the variable, or adjustable, rate mortgages, which are long-term mortgages which provide for interest rate adjustments throughout the term of the loan. These mortgages should provide no tax surprises-the interest payments should be fully deductible in the year paid or incurred in accordance with the borrower's method of accounting. No changes are made to the taxpayer's basis in his property as a result of such mortgages.

Buy-down mortgages. A second form of mortgage involving interest rate adjustments is the buy-down mortgage, which is made with a base rate less than the current market rate. The tradeoff for the lower rate is that the borrower must prepay some of the interest at closing. Under Section 461(g), a taxpayer using the cash method of accounting must capitalize the increased interest payment and amortize it over the period to which it relates. One well-known exception to this rule is in the case of "points." Points paid in connection with the purchase or improvement of a principal residence are deductible in the year in which paid, under specified conditions, so long as the amount charged is not in excess of the amount generally charged in the area in which the loan is made. Taxpayers will seek to argue that the increased interest payment made at closing represents "points." If the document specifies the purpose of the payment, the Service is likely to succeed in requiring the taxpayer to capitalize the cost under Section 461(g). The accrual-basis taxpayer may deduct the interest (whether or not prepaid) only in the period in which the use of the money occurs. The result to each is effectively the same.

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Graduated payment mortgages. A graduated payment mortgage is one in which lower mortgage payments are made in the early years of the loan because a portion of the interest is deferred to the latter part of the amortization period. A taxpayer using the accrual method of accounting could under Reg. 1.461-1(a)(2), prior to the Deficit Reduction Act of 1984, deduct an expense in the taxable year in which “all the events have occurred which determine the fact of the liability and the amount thereof can be determined with reasonable accuracy.” However, under the 1984 Act, interest incurred by accrual method taxpayers with respect to debts incurred in transactions occurring after June 8, 1984 will be deductible only on a “constant interest” basis. [FN2] The constant interest terminology is the adaptation of the 1984 Act's “economic performance” standard in the case of interest.

Interest on obligations issued on or prior to 6/8/84 is not subject to the statutory prohibition against non-economic accruals of interest. Thus, the language of a particular graduated payment mortgage issued prior to that date may determine the deductibility, for an accrual basis taxpayer, of the deferred portion of the interest. On the other hand, a taxpayer using the cash method of accounting will be entitled to deduct the deferred portion when it is paid. [FN3]

Participating mortgages

There are two primary forms loans may take when the lender seeks to benefit from the increase in value of the property subject to the mortgage. The first is the shared-appreciation mortgage (SAM) in which the lender contracts to receive a percentage of the appreciation in value of the mortgaged property in exchange for providing a below market interest rate. An equity-participation mortgage (EPM) is one in which the lender can share in a portion of the entire equity of the mortgaged property, including the down payment. The shared-appreciation mortgage, and variations on its theme, are more prevalent and will be examined in depth.

Equity-participation mortgages. The reason for limiting the discussion of EPMs is the inherent uncertainties associated with them. It is unclear with an EPM whether the relationship between the “borrower” and the “lender” creates a joint tenancy, tenancy-in-common, joint venture or partnership. Many borrowers who may consider entering into such a loan agreement will not want to be treated as having ***284** entered a partnership for tax purposes. As such, they will want to avoid the use of EPMs. Thus, despite the fact that an EPM conceivably could generate capital gain income on the final “equity” payment (if dealer status can be avoided), this article will not address any further tax considerations of an EPM.

Shared-appreciation mortgages. The primary tax issue with respect to a SAM is the deductibility of the contingent interest payment, representing the lender's share of the appreciation in the property. As stated in the accompanying box, the Supreme Court has defined interest as “compensation for the use or forbearance of money.” Furthermore, the Service has ruled that the method of computation does not control a payment's characterization as interest, so long as the amount in question is an ascertainable sum contracted for the use of borrowed money. [FN4] Thus, if a bona fide debtor-creditor relationship is established, the contingent interest portion of a SAM should be deductible in full when paid. The Service has so ruled in a residential context.

In *Rev. Rul.* 83-51, [FN5] a cash basis taxpayer received a residential SAM from a financial institution. A fixed interest rate of 12% was provided (the market rate was 18%) and contingent interest equal to 40% of the appreciation in value of the property over the term of the SAM was payable upon the SAM termination date. The SAM termination date was the earliest of the date of (1) prepayment of the outstanding balance, (2) transfer of ownership of the residence, or (3) ten years from the date of the SAM loan. Other essential terms of the SAM

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included (1) a statement that the mortgagor and mortgagee intended that the SAM create no more than a debtor-creditor relationship, (2) the mortgagor was solely responsible for the obligations to pay real estate taxes, insurance, and other charges relating to ownership of the property, (3) the mortgagor had the right to sell, transfer, or otherwise deal with the property without the consent of the mortgagee, and (4) the mortgagee was not liable for any decrease in the value of the property.

In all three of the factual situations presented in the Ruling, the Service, after noting that the amount of contingent interest was an ascertainable sum, concluded that the appreciation element constituted "interest" under Section 163. Thus, the taxpayer was allowed a deduction for the full amount of the contingent interest in the year of payment.

The Service indicated that its conclusions were limited to the facts set forth in the Ruling and concluded as follows:

"Accordingly, such conclusions should not be considered to apply to SAM agreements, particularly in situations in which the loan proceeds are used for commercial or business activities, in which the lender acquires greater rights with respect to the borrower or the mortgaged property than are described in the facts section of this ruling; in which the parties evidence an intention to create a relationship other than that of debtor and creditor; or if other circumstances indicate that the SAM loan represents in substance an equity interest in the mortgaged property. In addition, the ruling should not be considered to apply where the borrower under the SAM is a corporation."

Where the funds are being used "for commercial or business activities," the Ruling will apply only if the lender's rights with respect to the property are no greater than those described in the Ruling. Thus, if the shared-appreciation concept is being considered in such a context, particular attention must be focused on the facts set out in the Ruling.

Further, no court has addressed the tax consequences of a shared-appreciation mortgage. The only reported case with facts similar to those contained in the Ruling produced a surprising result. In *Farley Realty Corp.,* [FN6] the lender advanced $70,000 to the borrower for ten years in exchange for 15% interest for two years, 13% interest for eight years and the right to 50% of the appreciation in the value of the property. The court held that the right to share in the appreciation in the value of the property represented an "equity interest in the property" which was separable from the right to interest on the indebtedness. Thus, the corporate borrower could not deduct the payment which represented the appreciation in value. Although not addressed by the court, the lender in *Farley* would appear, at first blush, to be entitled to capital gain treatment on the appreciation payment. This treatment would seem to be very desirable to the lender. Planning the transaction to fit within this holding, however, gives rise to a different set of considerations.

If the lender is viewed as having an equity interest in the venture, it will be necessary to characterize ***285** the nature of that interest. The most logical classification of that interest seems to be that it is held by the lender as a joint venturer or partner. If this is the result obtained under a *Farley* -type analysis, would the same result occur when using a SAM? Two strong arguments can be made that the answer is no.

First, the facts of *Farley* are materially different than those present in a SAM context. In that case, the agreement did not provide for a fixed date at which the relationship was to be terminated. The court was able to rely on this fact as supporting the lack of a debtor-creditor relationship. This objection can be overcome by placing a termination date provision in the SAM agreement. A further factor relied on by the court was the fact that the

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lender could initiate proceedings that would result in a sale of the property to third parties. Such a situation could be avoided in a SAM agreement.

The second argument relates to the concept of a "partnership." Under Reg. 301.7701-3(a), a partnership includes "a syndicate, group, pool, joint venture, or other unincorporated organization through or by means of which any business, financial operation, or venture is carried on, and which is not a corporation or a trust or estate within the meaning of the Internal Revenue Code of 1954."

The same provision indicates that the term "partnership" is broader in scope than the common law meaning given to such term. It is clear that the determination of whether an entity is a "partnership" for tax purposes is determined under the concepts espoused by the Internal Revenue Code. However, "local law governs in determining whether the legal relationships which have been established in the formation of an organization" are such that the Code standards are met. [FN7] Therefore, state statutory provisions with respect to partnerships have some relevance. Additionally, if there is no intention on the part of the parties that a partnership be formed, such intention will be helpful (although not determinative) in supporting the desired result. Although the lack of such an intent is not controlling, it should go a long way toward supporting the desired debtor-creditor result.

One other point that should be considered is the ***286** possibility that the contingent interest payment will be disallowed as usurious. Again, relevant statutory provisions must be considered.

The *Farley* case has been widely criticized, with one commentator's opinion representative of others: "the case should be narrowly construed and limited to its own admittedly 'complicated' facts." [FN8] The authors believe that a SAM can be drafted which will be distinguishable from the agreement drafted in *Farley*. The primary drafting consideration will be to establish a debtor-creditor relationship. The importance of a fixed SAM termination date in the agreement is critical.

A carefully drafted SAM should consider, at a minimum, the following clauses:

1. A statement that the parties intend to create a debtor-creditor relationship, and do not intend to create a partnership for state law or Federal income tax purposes.
2. A fixed rate of interest should be provided, which will be payable in all events, but which will be below the current market rate.
3. The borrower should agree to pay "contingent interest" in an amount equal to a stated percentage of the appreciation in the value of the property between the date of purchase and the "termination date" of the SAM.
4. The SAM "termination date" should be the earliest of the following:
   A. Transfer of ownership by the borrower.
   B. Prepayment of outstanding balance by borrower.
   C. A stated period from the original date of the SAM.
5. The principal payments should be due and payable in all events.
6. The SAM should be secured by a lien on the subject property.
7. The SAM should not be subordinated to other mortgages.

Taxpayers seeking the advance blessings of the Service with respect to a particular SAM arrangement must be aware of the Service's position that no advance rulings will be issued where the SAM proceeds "are used for commercial or business activities or where used to finance a personal residence if the facts are not similar to those described in Rev. Rul. 83-51. . . ." [FN9]

Summary

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The fundamental tax considerations with respect to any mortgage, be they traditional fixed-rate mortgages, principal adjustment mortgages, interest-rate adjustment mortgages or shared-appreciation mortgages are those of tax basis (as limited by fair market value of the property mortgaged) and deductibility of interest payments.

Principal adjustment mortgages, including equity adjustment and growing equity mortgages, should not affect tax basis or the deductibility of interest. Although the tax treatment associated with price level adjusted mortgages is not clear, it is arguable that basis is increased by the amount of the principal adjustment, in at least a purchase-money price level adjusted mortgage.

Interest-rate-adjustment mortgages, consisting of variable-rate mortgages and graduated payment mortgages, yield predictable tax results. Basis is a constant, and interest payments are deductible in the case of variable-rate mortgages whether of the adjustable interest rate variety or of the buy-down variety. The limitation in the case of the latter is the statutory requirement for capitalization of the interest prepaid at closing (exclusive of actual points) by the cash-basis borrower. In the case of the graduated-payment mortgage, the accrual-basis taxpayer looks to the language of the instrument to determine when interest is deductible, and the cash-basis taxpayer deducts interest when actually paid. As above noted, basis remains a constant.

Participating mortgages, consisting of equity-participation mortgages and shared-appreciation mortgages, require careful consideration of the tax consequences. EPMs are not clearly categorized as debtor-creditor relationships and are not treated in this article. SAMs raise the difficult issue of deductibility of the contingent interest payment but generally should produce the desired result if drafted to include (1) a debtor-creditor relationship rather than a partnership; (2) a fixed (albeit below market) rate of interest that is payable in all events; (3) a contingent interest payment equal to a stated percentage of appreciation in value; (4) a fixed termination date; (5) a definite obligation to pay principal in all events; (6) a lien on the property; and (7) a non-subordination provision.

In a sense, the creative mortgage permits both debtor and creditor to “borrow of Peter to pay Paul,” a new approach to an old and time-tested theorem, to be shared and appreciated by all concerned in the financing arrangement.

[FNa1]. *MARSHALL R. PASTERNACK is associated with the law firm of Greenberg, Traurig, Askew, Hoffman, Lipoff, Rosen & Quentel, P.A., Miami, Florida. He is a member of the Massachusetts Bar and is awaiting admission to the Florida Bar. He is also a CPA and a member of the ABA.* ***ANDREW*** *M.* ***WEINSTEIN*** *is a partner in the law firm of* ***Holland*** *& Knight, Miami, Florida. He is chairman of the ABA Tax Section's Subcommittee on Liens, Levies and Limitations. He is also a member of the Florida Bar Association Tax Section's Executive Council.*

[FN1] See *Woodsam Associates, Inc.,* 198 F.2d 357, 52-2 USTC ¶9396, 42 AFTR 505 (CA-2, 1952).

[FN1a] 654 F.2d 35, 81-2 USTC ¶9496, 48 AFTR2d 81-5261 (Ct. Cls., 1981).

[FN2] See Helfand and MacNeil, *New economic performance test will defer many deductions of accrual-basis taxpayers,* 13 TL 110 (Sep/Oct 1984).

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[FN3] *Rev. Rul.* 77-135, 1977-1 CB 133.

[FN4] *Rev. Rul.* 76-413, 1976-2 CB 214.

[FN5] *Rev. Rul.* 83-51, 1983-1 CB 48.

[FN6] 279 F.2d 701, 60-2 USTC ¶9525, 5 AFTR2d 1646 (CA-2, 1960), *aff'g,* TCM 1959-93.

[FN7] Reg. 301.7701-1(c).

[FN8] Friend, "Shared Appreciation Mortgages," 34 *Hastings Law Journal* 331, 388 (1982).

[FN9] *Rev. Rul.* 83-31, 1983-1 CB 722.

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Estate Planning
Volume 12, Number 2
March, 1985

Trusts
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Andrew Weinstein, Attorney, Miami, and Harold Bucholtz, Attorney, D.C. [FNa]

DESPITE RESTRICTIONS, FOREIGN TRUSTS CAN BE EFFECTIVE TAX PLANNING DEVICES

Although the Provisions of Section 679 Severely Limit the Use of Foreign Trusts in Tax Planning, in Some Situations They May Be Used to Accumulate Income Tax Free and the So-Called “Cash-Flow” Trust Can Be Beneficial in Other Instances. the Authors Analyze the Restrictions On, as Well as the Benefits Of, Their Use.

Section 679 is intended to discourage U.S. taxpayers from establishing foreign trusts to accumulate income free from U.S. tax. [FN1] It accomplishes this by, in certain circumstances, treating a U.S. person who transfers property to a foreign trust as the owner of all or part of the property held by the trust and therefore taxable on the income attributable to that property. If more than one person makes transfers, the ownership of the trust's assets will be treated as divided among those persons. Thus, Section 679(a)(1) adapts the grantor trust concepts of Subchapter J.

Because of the section's complexity, this article is limited to two very basic, but extremely difficult interpretive problems it raises: (1) in determining the portion of which the transferor is considered the owner, what is meant in Section 679(a)(1) by the phrase “the portion of such trust attributable . . .” to property transferred by a U.S. person, and (2) what test is used to determine whether the transferor is a U.S. person. Depending upon how those two questions are answered, foreign trusts may continue to provide significant planning opportunities for some taxpayers.

Although Section 679 was enacted almost nine years ago, the Service is still yet to issue even Proposed Regulations clarifying that section. Further, the IRS has not yet issued a single published or private ruling interpreting Section 679.

The statutory language

The language of Section 679 is deceptively straightforward. The general rule of Section 679(a)(1) simply states: “A United States person who directly or indirectly transfers property to a foreign trust (other than a trust described in section 404(a)(4) or 404A(a)(4)) shall be treated as the owner for his taxable year of the portion of such trust attributable to such property if for such year there is a United States beneficiary of any portion of such trust.”

By itself, Section 679(a)(1) would apply to any direct or indirect transfer. Section 679(a)(2), however, describes two types of transfers that are excepted from the general rule. Section 679(a)(2)(A) excepts transfers made because of the death of the transferor. That exception allows a U.S. taxpayer to establish a testamentary foreign trust for the benefit of U.S. persons without concern about Section 679(a)(1).

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The exception provided by Section 679(a)(2)(B) is far more important during the taxpayer's life. The thrust of this exception is that a U.S. person may engage in transactions with a foreign trust without concern about Section 679 if (1) the transactions are truly on an arm's-length basis and lack any gratuitous element and (2) he or she is willing to either immediately recognize the gain realized on the sale or exchange or to report it on the installment basis. This exception is of great importance in determining whether a portion of a trust is “attributable to” gratuitously transferred property. Unfortunately, there is great uncertainty generally as to the breadth of the exception.

As already mentioned, the various other requirements for the applicability of Section 679(a)(1) may also present difficult interpretative problems. For example, Section 679(a)(1) applies only with respect to a foreign trust. Difficulties arise with classifying a trust as foreign or domestic.

Section 679 also applies only to trusts having one ***95** or more U.S. beneficiaries. Section 679(c) specifies that a trust is treated as having a U.S. beneficiary if any part of its income or corpus may be paid or accumulated for the benefit of a “U.S. person.” Section 679(c)(2) provides rules for attributing to U.S. persons amounts paid to foreign corporations, partnerships, trusts, or estates. Those rules, together with the need to classify a beneficiary as foreign or domestic, provide additional complexity.

The applicability of Section 679 is further limited to transfers by U.S. persons. Section 679(a) applies to direct or indirect transfers by such persons. The legislative history to Section 679(a) provides considerable discussion of what constitutes an indirect transfer. For example, a transfer by a foreign corporation in which a U.S. person owns a majority of the stock may be regarded as an indirect transfer to a foreign trust by the U.S. person. [FN2] Under some circumstances, a loan to a trust or a guarantee of a loan may be considered an indirect transfer. [FN3] Thus, Section 679 may apply to transactions with a trust to which it might not appear to apply on first reading of the statutory language. As a result, any transaction with a foreign trust must be carefully analyzed to consider the possible effects of Section 679.

Meaning of “attributable to”

As mentioned, one of the most basic yet difficult interpretive problems posed by this area is what is meant in Section 679(a)(1) by the phrase, “portion of such trust attributable to . . . [the transferred] property.” On first reading, one might simply regard the portion of a trust attributable to a particular item of transferred property as being the portion of the trust that the value of that item represents of the value of the total trust assets. Unfortunately, that simple construction of “attributable to” ignores that a nonbusiness trust may acquire and accumulate funds in several ways, not merely by receipt of lifetime or testamentary gratuitous contributions. For example, such a trust may earn income on the property gratuitously contributed, or it may realize gains on the sale or exchange of such property. The IRS is likely to regard income so earned and gains so realized as also “attributable to” the earlier-transferred property.

The basic purpose of Section 679 is to prevent the use of a foreign trust to accumulate income tax-free for the benefit of one or more U.S. beneficiaries in a manner that cannot be accomplished with a domestic trust. [FN4] Were a U.S. transferor not taxable both on the income earned on its original contribution and upon income earned on undistributed past income derived from that contribution, the transferor could still use a foreign trust to accumulate income tax free. Income on past income would compound tax free. Because this would not be the case with a domestic trust, the IRS is likely to treat the transferor as the owner of both the contributed property and the undistributed income derived therefrom. This would require broadly interpreting “attributable to” to in-

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clude past years' income.

The "sale" exception. The IRS is also likely to treat any gain realized on a sale or exchange of contributed property as attributable to the property originally transferred. Were the original transferor not treated as the owner of the gain realized, a U.S. transferor could avoid Section 679 in some instances. For example, the transferor could transfer property that it expects to appreciate prior to the appreciation taking place. The trust could then sell the property after the property has increased in value. Income on the portion of the trust attributable to the gain could then be accumulated tax free.

An argument can be made that the gain should not be treated as owned by the original transferor because the sale of the originally transferred property would be a transaction to which Section 679(a)(2)(B) would apply, *i.e.,* an arm's-length sale in which the gain is both realized and fully recognized. Applying Section 679(a)(2)(B) very literally, not only would the gain not be treated as owned by the original transferor but the taint would also be removed from the portion of the trust previously subject to Section 679(a)(1). Not just the gain but all of the sale proceeds would be received in a transaction to which Section 679(a)(2)(B) applied.

The difficulty with this position is that Section 679(a)(1) would be rendered a virtual nullity. It could be avoided by a foreign trust's merely replacing one property with another of equal value. The IRS is highly unlikely to accept such a construction of Section 679(a)(2)(B). Rather, the IRS is likely to argue that the purpose of Section 679(a)(2)(B) is simply to prevent Section 679(a)(1) from applying to ***96** the third party to whom the foreign trust may later sell the gratuitously transferred property at arm's-length terms.

Under the likely IRS analysis, a sole transferor to a Section 679 trust would continue to be treated as the owner of the entire trust, despite the trust engaging in any number of arm's-length sales or exchanges to which Section 679(a)(2)(B) applied. If the size of the trust's property holdings are increased by additional gratuitous contributions, by earning income on existing trust property, or by realizing a previously unrealized gain on existing trust property, the transferor would continue to be treated as the owner of the entire trust (unless, of course, the additional contributions were from someone else). Because any Section 679(a)(2)(B) transactions must involve an exchange of properties of equal value, such transactions could not increase the trust's holdings. In a Section 679(a)(2)(B) transaction, existing trust assets are simply replaced with other assets of equal value and, for the reasons explained above, the replacement assets would have the same status as the assets they replaced: they would be treated as owned by the original transferor (regardless of whether the trust realized a gain on the transaction).

Loans to foreign trust

Although the "attributable to" language may be quite broad, there remains a further method of increasing a foreign trust's holdings to which Section 679(a)(1) may not apply-through arm's-length borrowing. The borrowing could be in the form of purchase money mortgages or simply a straight-forward loan from a third party, the proceeds of which are reinvested for what is hoped to be a higher return. The latter, simpler situation may be illustrated as follows.

Example. Transferor T gratuitously contributes $100 to foreign trust FT. All requirements for the application of Section 679(a)(1) are satisfied. Subsequently, FT borrows $50 from unrelated party P on arm's-length terms. Interest is payable annually on the $50 loan at the fair market rate of 10% and principal is repayable over ten years. FT offers $50 of its existing $100 trust corpus as collateral. FT invests the $50 loan proceeds with expectation of receiving a 20% annual return. FT expects to satisfy most, if not all, of the annual debt service on the

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loan from that return.

A strong argument can be made that the loan transaction qualifies for the Section 679(a)(2)(B) “sale exception” so that Section 679(a)(1) does not apply to P but, at the same time, the loan proceeds are not “attributable to” any of the existing trust assets and, therefore, should not be treated as owned by T. A distinction between this situation and the situations described earlier is clear. In each of the earlier situations, the proceeds of the Section 679(a)(2)(B) transaction simply replaced existing trust properties. There was no increase in the value of the trust's properties; at most, there was a realization of a previously unrealized gain. In this example, however, the gross value of the trust's assets does increase, from $100 to $150. The $50 in loan proceeds does not simply replace $50 of the prior trust assets.

There are at least three theories under which the loan proceeds could be treated as “attributable to” T's original contribution despite not being simply a replacement thereof. Each has significant weaknesses, however. The first theory would be that the loan proceeds are “attributable to” T's contribution because trust property derived from that contribution serves as the loan's collateral. Some support for this view may be found in the legislative history to Section 679, which provides: “If a foreign trust borrows money or other property the repayment of which is guaranteed by a U.S. person, the U.S. person may be treated as having transferred to the trust the property to which the guarantee applies. For this purpose, a guarantee may consist of any understanding, formal or informal, by which payment of an obligation is assured.” [FN5]

Under that language, if T had guaranteed the loan or provided the collateral for it from his personal property, rather than trust property being offered, T would likely be treated as the owner of the loan proceeds or any property purchased therewith.

The quoted language does not directly apply, however, to a situation in which only trust property is offered as collateral. It would, therefore, not apply to the situation in the example unless it is also asserted that, pursuant to Section 679(a)(1), T is regarded as continuing to own the $100 he contributed to FT for purposes of determining the source of the collateral. The effects of applying Section 679(a)(1) should be limited to those prescribed by Section 671. Under Section 671, the income and deductions of a grantor trust are attributed to the grantor; the trust is not otherwise disregarded. [FN6]

This first collateral theory would also be problematical in a situation in which more than one person has made gratuitous transfers to the trust. For instance, if the $100 had been jointly contributed by T and his wife, W, should the $50 collateral for the loan be attributable all to T's $50 contribution, all to W's $50 contribution, or to $25 from each?

The second theory under which the loan proceeds might be treated as owned by T would be premised on challenging FT's expectation that debt service ***97** would be wholly satisfied from income earned on the loan proceeds (or, if necessary, by repaying the proceeds themselves). In other words, if either income earned on the original $100 or some portion of the $100 itself must be used to service the loan, are the loan proceeds “attributable to” those trust funds to the extent those funds are used, and is T the owner of the loan proceeds to that extent?

This theory would appear to be very difficult to apply in practice since it would require very strict tracing. It is difficult to imagine how it could be applied in a situation in which there were several transferors to the trust. The only alternative to tracing, however, would be an initial determination, based on facts available at the time the loan was made, that the loan proceeds cannot be invested at a return at least equal to the interest charged on the loan (since, theoretically at least, if the proceeds can be invested at a return of at least that rate, resort to other

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trust funds will be unnecessary). Such a determination could not reasonably be made in most cases, however, because funds will generally only be borrowed (whether by a foreign trust or anyone else) if there is a reasonable expectation that a profit may be made from doing so.

The third theory under which T might be treated as taxable on the loan proceeds would not involve an interpretation of "attributable to." The legislative history to Section 679, in a somewhat confusing discussion of the significance of loans to a foreign trust, states: "For purposes of determining the portion of a trust over which the U.S. grantor is treated as owner, loans to the trust by the grantor or by any other person shall be disregarded." [FN7]

That statement is accompanied by the following footnote: "For example, if a U.S. person transfers $10 to a foreign trust having U.S. beneficiaries, and also lends $90 to that trust, he may be treated as the owner of trust income attributable to $100. For this purpose, if a U.S. person makes a deposit in a bank (or a contribution to another entity) and that deposit (or contribution) is followed (or preceded) by a loan of a similar amount to a foreign trust, the U.S. person may be considered to have made the loan directly to the trust." [FN8]

This language appears to allow the IRS to treat all of the loan proceeds from P as owned by T if T induced the loan in some manner. If such was the case or, changing the facts, if T made the loan directly to FT, the quoted language would appear broad enough to allow T to be treated as the owner even if the loan is made on strictly arm's-length terms.

Such a reading of the legislative history is too broad, however, for two reasons. First, the language is that the U.S. person "may" be treated as the owner and that the loan "may" be treated as a transfer of corpus. The use of "may" implies that the loan proceeds should be treated as subject to Section 679(a)(1) only in appropriate cases, *e.g.,* where the loan was at other than arm's-length terms and, therefore, really an indirect transfer to the trust.

Second, construing the language to apply to arm's-length loans would be inconsistent with Section 679(a)(2)(B), which specifically excepts arm's-length installment sales from Section 679(a)(1). Obviously, an installment sale produces a loan from the seller to the purchaser. If the terms of the sale are arm's-length, under Section 679(a)(2)(B), the seller should not be treated as owning the property sold to the trust as a result of the installment sale, even though it has loaned the trust most of the purchase price. This should be the case whether the seller is a third party or a transferor/ owner. Otherwise, a sale by joint owners could produce bizarre results if one of the joint owners is a transferor/owner and the other is not. In such a case, the installment sale would be treated as a Section 679(a)(1) transfer as to one joint owner but not the other, despite the terms of the transaction being identical as to each owner.

Possible tax advantage

If amounts borrowed on an arm's length basis are not "attributable to" property gratuitously transferred by a U.S. transferor, foreign trusts may still be used to accumulate income tax-free, despite Section 679. This may be illustrated by the following examples, contrasting arm's-length sales to a foreign trust and to a domestic trust, in each of which the U.S. seller would take back a purchase-money mortgage from the trust. In each case, the seller would report his or her gain on the sale on the installment basis, bringing the transaction within the Section 679(a)(2)(B) exception.

***98** *Example.* Transferor T sells property having a fair market value of $9 million to foreign trust FT in return for a 30-year note under which FT must pay $300,000 a year plus interest at 10% (which was 110% of the Fed-

eral long-term rate specified under Section 1274(d) prevailing at the time of the sale). Assume that FT is established in Country X, which imposes no tax on FT's income. Distributions from FT are wholly within the trustee's discretion.

In year 1, FT sells the property at its $9 million value, invests the proceeds, and earns 15% on its investments-$1.35 million. FT's income from its investments is neither U.S.-sourced nor effectively connected with a U.S. business. As a result, FT pays no tax whatsoever on the $1.35 million in income. FT also makes no distributions during year 1. FT does, however, pay $300,000 in principal and approximately $900,000 in interest to T at the end of the year. FT holds property at the end of year 1 with a total value of $9.15 million (

$9 million + $1.35 million - $300,000 - $900,000), a net increase of $150,000.

Example. The facts are the same as in the preceding example, except that T transfers the property to domestic trust DT. Further, assume a fixed 50% tax rate.

In year 1, DT sells the property at its $9 million value, invests the proceeds, and earns 15% on its investment-$1.35 million. DT makes no distributions during year 1. DT pays $300,000 in principal and approximately $900,000 in interest to T at the end of the year. DT has taxable income of $450,000 ($1.35 million in income less a $900,000 interest deduction) and pays a tax of $225,000. DT holds property at the end of year 1 with a total value of $8,925,000 (

$900,000 + $1,350,000 - $300,000 - $900,000 - $225,000), a net decrease of $75,000.

A foreign trust arrangement of the type described in the example above might be very attractive to an older individual desiring a fixed source of income for the remainder of his or her life. Such an arrangement appears to be a suitable replacement for the foreign-trust/private-annuity arrangements that proliferated prior to the enactment of Section 679. Under present law, an installment sale arrangement of the type described is preferable to a private annuity because, for the reasons stated earlier, the Section 679(a)(2)(B) exception should apply to an installment sale arrangement. Indeed, an IRS Special Counsel for International Taxation has apparently conceded the existence of the just-described opportunity to accumulate income tax-free by employing an installment sale arrangement. He has also questioned whether the Section 679(a)(2)(B) exception should be amended to prevent that opportunity. [FN9] The opportunity to accomplish the same end with a private annuity probably no longer exists because the Section 679(a)(2)(B) exception would be unlikely to apply to a private annuity arrangement, no matter how structured. [FN10]

One caution should be offered regarding an installment sale to a foreign trust. In planning such a sale, the Section 668 interest charge on accumulation distributions should not be ignored. Because Section 679(a)(1) will not apply to the income earned on the property sold to the foreign trust, Section 668 should apply to that income when it is eventually distributed. The cost to the beneficiaries of that 6% simple interest charge must be weighed against the ability of the trust to earn income on a compounded basis tax free.

Status as a U.S. person

As already stated, Section 679 only applies to transfers to a foreign trust by a U.S. person. What is less than clear, however, is how a transferor's status as a U.S. person is determined. Is a transferor's status determined only once-at the time of the transfer-or is it determined on a year-by-year basis?

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The legislative history contains no express discussion of this question. This is in great contrast to the detailed rules in the statute itself and the lengthy discussion in the legislative history, clearly establishing that whether a trust has a U.S. beneficiary is determined year-to-year. [FN11] This suggests perhaps that a simple, straightforward, one-time test was intended as to transferors, and so little explanation was necessary.

The issue of when a transferor's status as a U.S. person is determined may arise in a number of contexts. For example, a nonresident alien may establish a foreign trust for the benefit of U.S. persons and later emigrate to the U.S. Does such a trust escape the applicability of Section 679 because the transferor was not a U.S. person at the time of the transfer? Alternatively, a resident alien might establish a foreign trust for the benefit of U.S. persons and subsequently return to his or her country of origin. Does the foreign trust remain "tainted" by Section 679 even after the transferor's emigration from the U.S. because the transferor was a U.S. person at the time of the transfer? Further, similarly to a resident alien ceasing to be a resident, a U.S. citizen might establish a foreign trust and later expatriate. This last situation would of course also raise questions under Sections 877 and 2107 (dealing with expatriation to avoid tax).

A number of commentators have discussed the issue of when the transferor's status as a U.S. person is determined, as that issue is posed by the factual ***99** situation involving a nonresident alien who emigrates to the U.S. They have generally concluded that Section 679 would not apply to the trust because the transferor was not a U.S. person at the time of the transfer. [FN12] Among those who have accepted that interpretation of Section 679(a)(1) is the IRS Special Counsel for International Taxation referred to earlier. [FN13] This would suggest, of course, that the determination of the transferor's status as a U.S. person is not done on a year-by-year basis.

Cash-flow trusts

If a transferor's status is determined only once, an opportunity exists for taxpayers to use Section 679 to their advantage. Knowledgeable tax planners have previously realized that the grantor trust rules of Subchapter J are a double-edged sword. As a result, "defective" insurance trusts and cash-flow trusts have been created which are intentionally subject to one or more of the grantor trust rules. An additional planning tool of that type would be the intentionally defective Section 679 cash-flow trust.

Such a trust might be used by a resident alien who intends to return to his or her home country, or by a U.S. citizen who intends to expatriate. Property that would initially generate little or no income could be transferred to a foreign trust while the individual is a resident alien or a U.S. citizen. By the time the individual has ceased residing in the U.S. or has renounced his or her U.S. citizenship, the property could be generating substantial income. Under this arrangement, the transferor would be subject to little U.S. tax while he or she was a U.S. resident or citizen because there was little income. Further, to the extent the transferor was subject to tax while remaining a U.S. citizen or resident, he or she would only be subject to the ordinary tax on the trust's income. The transferor would not be subject to the Section 668 interest charge. The legislative history to Section 668 makes it quite clear that the interest charge is not applicable to trusts subject to Section 679. [FN14]

The joint effect of Section 679(a)(1) and Section 671 is that the transferor would continue to be treated as the owner of the trust's assets and as the recipient of the trust's income even after he or she had ceased residing in the U.S. or had renounced his or her U.S. citizenship. As a nonresident alien, however, the transferor would be subject to U.S. tax on the trust's more substantial income in the later years only to the extent the income was either U.S.-sourced or "effectively connected" to a U.S. trade or business. Thus, if the trust is initially funded with non-U.S. investments or if non-U.S. investments are substituted for earlier-held U.S. properties, the trans-

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feror will have no U.S. tax liability in the later years. Further still, because the trust is ignored for U.S. tax purposes, any distributions made by the trust to its U.S. beneficiaries will not be treated as such for U.S. tax purposes and, therefore, will not be taxable to them. [FN15] Thus, such a Section 679 trust would function much like other “defective” foreign cash-flow trusts.

Conclusion

Section 679 was a largely successful effort to limit the usefulness of foreign trusts as tax-planning tools. It does not appear, however, to have wholly eliminated the usefulness of such trusts. Rather, at least one significant benefit appears to remain available if the foreign trust is carefully used: the ability to accumulate income tax free in trusts funded through arm's-length loans. Further, Section 679 may itself have unintentionally provided a new tax planning tool, the Section 679 cash-flow trust.

[FNa] ***ANDREW** H. **WEINSTEIN** is a partner with the law firm of* **Holland** *& Knight in Miami, Florida. He is the Chairman of the ABA Tax Section's Subcommittee on Liens, Levies and Limitations, and of the Committee on Civil Tax Procedure of the Florida Bar. He also frequently writes for professional tax publications. HAROLD R. BUCHOLTZ is a partner in the Washington, D.C., office of the same firm. His articles have appeared in* The Journal of Taxation *and* Estate Planning.

[FN1] H. Rep't No. 94-658, 94th Cong., 1st Sess., 1976-3 (Vol. 2) CB 899; S. Rep't No. 94-938, 94th Cong., 2d Sess., 1976-3 (Vol. 3) CB 254; Joint Committee on Taxation, *General Explanation of the Tax Reform Act of 1976,* 1976-3 (Vol. 2) CB 231.

[FN2] H. Rep't No. 94-658, *supra,* at 901; S. Rep't No. 94-938, *supra,* at 257; *General Explanation, supra,* at 233.

[FN3] H. Rep't No. 94-658, *supra* note 1, at 901; S. Rep't No. 94-938, *supra* note 1, at 257; *General Explanation, supra* note 1, at 221.

[FN4] H. Rep't No. 94-658, *supra* note 1, at 899; S. Rep't No. 94-938, *supra* note 1, at 254; *General Explanation, supra* note 1, at 231.

[FN5] H. Rep't No. 94-658, *supra* note 1, at 901; S. Rep't No. 94-938, *supra* note 1, at 257; *General Explanation, supra* note 1, at 233.

[FN6] See *Rothstein,* 735 F.2d 704, 84-1 USTC ¶ 9505, 54 AFTR2d 84-5072 (CA-2, 1984).

[FN7] H. Rep't No. 94-658, *supra* note 1, at 901; S. Rep't No. 94-938, *supra* note 1, at 256.

[FN8] *Id.*

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[FN9] Gordon, *Tax Havens and Their Use by United States Taxpayers-An Overview* (Rep't by Special Counsel for Int'l Tax'n, 1/12/81), at 103, 106.

[FN10] H. Rep't No. 94-658, *supra* note 1, at 902; S. Rep't No. 94-938, *supra* note 1, at 257; *General Explanation, supra* note 1, at 234.

[FN11] H. Rep't No. 94-658, *supra* note 1, at 902; S. Rep't No. 94-938, *supra* note 1, at 258; *General Explanation, supra* note 1, at 234.

[FN12] See Duncan, "Use of Foreign Trusts by Non-Resident Aliens," 9 *Int'l Tax J.* 113 (December, 1982); Zaritsky, *Foreign Trusts,* 427 T.M. at A-10.

[FN13] Gordon, *supra* note 9.

[FN14] H. Rep't No. 94-658, *supra* note 1, at 903; S. Rep't No. 94-938, *supra* note 1, at 259; *General Explanation, supra* note 1, at 235.

[FN15] See *Rev. Rul.* 69-70, 1969-1 CB 182.

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