

July 11, 2011

FBAR (Foreign Bank Account Reports) Amnesty Program Allows Taxpayers to Avoid Criminal and Severe Civil Penalties

In February 2011 the Internal Revenue Service announced a second voluntary disclosure initiative to allow taxpayers with undisclosed offshore bank, securities and other financial accounts to comply with US income tax and other offshore account reporting rules for prior years and avoid criminal penalties with reduced civil penalties. In addition to other persons, these rules apply to citizens and U.S. resident aliens (e.g., U.S. resident aliens that have maintained accounts in their home country).

Taxpayers that do not voluntarily comply with the reporting and disclosure rules may be subject to severe penalties. The failure to report income from and ownership of or signatory authority over offshore accounts potentially exposes the taxpayer to criminal penalties. There are numerous civil penalties that can apply for the failure each year to report income from and the existence of offshore accounts, for example:

- A penalty of 20% accuracy related penalty on the underpayment of tax on previously unreported income;
- A penalty in the amount of 50% of the balance of the offshore account at the time of the violation; and
- In lieu of the 50% penalty, a penalty of \$10,000 for non-willful violations.

The civil penalties may potentially be reduced based on a showing of reasonable cause. The civil penalties are assessed in addition to the requirement to pay the tax and interest due with respect to the previously unreported income.

The first voluntary disclosure initiative was announced in 2009 with an extended deadline of October 15, 2009. An extended deadline of November 1, 2011 for the 2009 program applies to taxpayers, for tax years 2009 and prior, with signature authority over but no financial interest in an offshore account.

The deadline for the 2011 Offshore Voluntary Disclosure Initiative (2011 OVDI) is August 31, 2011 and applies to the 2010 and prior tax years. The reporting rules relating to foreign financial accounts apply broadly to individuals and entities including individuals who are taxed as US residents because they have passed the physical presence test or are green card holders and individuals who are officers of domestic corporations that have foreign financial accounts.

The 2011 OVDI provides some options to taxpayers for relief from penalties for the 2010 tax year and all prior tax years, as follows:

- Relief from criminal penalties;
- A reduction of the 50% penalty to a one-time penalty of 25% and to 12.5% (for taxpayers with offshore accounts having a balance of \$75,000 or less); and
- A reduction of the 50% penalty to a one-time penalty of 5% for certain taxpayers, for example, with “inherited” or “gifted” accounts.

In June 2011 the Internal Revenue Service issued an updated list of answers to FAQs and guidance for an “Opt Out” procedure from the civil settlement structure in connection with the 2011 OVDI. The Opt Out feature (not offered with the 2009 initiative) provides an opportunity for taxpayers to participate in 2011 OVDI to avoid criminal penalties and incur reduced civil penalties for non-willful violations and reasonable cause exceptions such as when the taxpayer may also have available foreign tax credits to reduce or eliminate US tax liabilities and related income tax penalties.

US citizens and residents are generally taxable on their worldwide income. Income from offshore bank, securities and other financial accounts of US citizens and residents is subject to US income tax. If the income is also taxable in offshore jurisdictions, foreign tax credits may reduce a taxpayer’s US tax exposure.

In addition to reporting income from offshore accounts, U.S. citizens and resident aliens are subject to separate reporting requirements concerning their signature authority over and financial interest in offshore accounts (generally with an aggregate balance of \$10,000 or more). As noted above, the reporting rules can potentially apply to individuals, unincorporated entities (e.g., trusts, LLCs, and partnerships), corporations, and officers and employees of US entities who are directly or indirectly connected to an interest in or signatory authority over offshore accounts.

The 2010 HIRE Act created additional reporting requirements for taxpayers with offshore accounts applicable generally for tax years beginning after March 18, 2010. The answers to the FAQs specifically discourage so called “quiet” disclosures by filing amended returns and paying any related tax and interest and encourage taxpayers to come forward under the 2011 OVDI. The HIRE Act additional reporting requirements and the availability of 2011 OVDI provide taxpayers an opportunity to resolve issues with respect to prior tax years.

The deadline for voluntary disclosure under the 2011 OVDI is August 31, 2011. We can assist you in navigating the rules and requirements of a voluntary disclosure whether the matter involves a small undisclosed account left in the home country or assets moved offshore with the misunderstanding that the assets are beyond the jurisdiction of the U.S. taxing authority.

If you have any questions regarding this topic, please contact your Butzel Long attorney or the author of this Client Alert.

Terry O. Lang
248.258.4462
lang@butzel.com

Copyright 2011, Butzel Long, a professional corporation
Any reproduction without permission of the author is prohibited.

The above news is only intended to highlight some of the important issues. This e-mail has been prepared by Butzel Long for information only and is not legal advice. This information is not intended to create, and receipt of it does not constitute, a client-lawyer relationship. Readers should not act upon this information without seeking professional counsel. This electronic newsletter and the information it contains may be considered attorney advertising in some states. If you feel you have received this information in error, or no longer wish to receive this service, please follow the instructions at the bottom of this message.

Attorney Advertising Notice - The contents of this e-mail may contain attorney advertising under the laws of various states. Prior results do not guarantee a similar outcome.

For previous e-news or to learn more about our law firm and its services, please visit our website at: www.butzel.com