



Mobility Matters

Non-Willful FBAR Violation and Compliance Through Various IRS Programs

December 2022 | by Yoori Sohn, KPMG LLP (U.S.), Washington National Tax Practice, Washington, DC (a member firm of KPMG International)



On November 2, 2022, the Supreme Court of the United States heard oral arguments with respect to a contentious appeals court split over whether the definition of the term “violation” under the Bank Secrecy Act (the “BSA”) means “per-form” or “per-account” for purposes of the requirement to file a Report of Foreign Bank and Financial Accounts, FinCEN Form 114 (the “FBAR”).

The Court did not appear to lean one way or the other as justices probed and challenged both sides of the argument regarding the statutory interpretation of the BSA. The court is expected to issue its decision before the end of June 2023.

The question presented to the Supreme Court is whether the term “violation” under the BSA means the failure to file an annual FBAR, without regard to the number of unreported foreign accounts, or whether each unreported account is considered a separate violation.¹

Taxpayers with delinquent FBARs should be aware that there are several IRS compliance programs that can bring taxpayers into compliance and should not wait for the Supreme Court’s final decision to come into compliance.

Background

The BSA was enacted to combat money laundering for purposes of criminal enterprise, terrorism, tax evasion, and other unlawful activity. The BSA authorized the Department of the Treasury to collect information from U.S. persons who have financial interest² in, or signature authority³ over, financial accounts⁴ maintained with foreign financial institutions.⁵

The corresponding regulations require filing a single annual report, the FBAR, for anyone with an aggregate balance over \$10,000 at any time during the calendar year in foreign financial accounts.⁶ There is a \$10,000 maximum civil penalty (adjusted for inflation)⁷ for any non-willful violation of I.R.C. section 5314.⁸ No penalty is imposed if all income from the account has been reported and there was reasonable cause for failing to file the FBAR.⁹

In addition to the non-willful penalty, the BSA authorizes penalties for willful violations. The maximum civil penalty for a willful violation is

the greater of \$100,000 (adjusted for inflation)¹⁰ or 50 percent of the maximum account balance during the year.¹¹

The statute of limitations for the FBAR for assessment of penalties is six years from the due date of the form.¹³ This means that taxpayers with delinquent FBARs only have to file the last six years of delinquent FBARs.

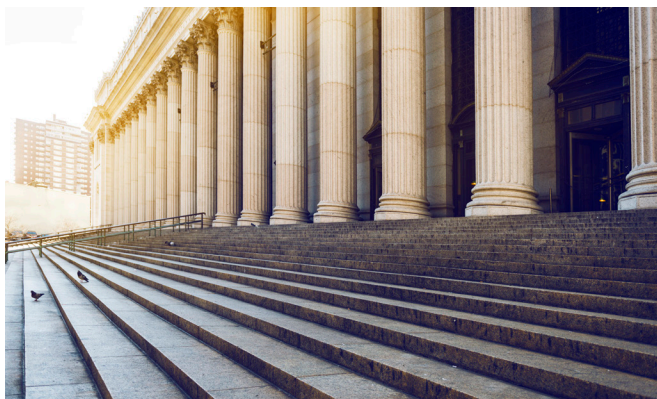
The screenshot shows the top portion of the FinCEN Form 114 website. At the top, it says "Report of Foreign Bank and Financial Accounts". Below this is a navigation bar with links for Home, File Information, Separate Joint Account, No Financial Interest, Consolidated Report, and Signature Information. The main content area features the FinCEN logo, the title "Report of Foreign Bank and Financial Accounts", and the version number "1.0". It also includes the FinCEN Form 114 OMB No. 1506-0009 and a note about the filing deadline coinciding with the current IRS tax season filing deadline for annual tax returns. Under the heading "Filing Instructions", there are four numbered steps: 1. Complete the FBAR, 2. Sign the completed FBAR, 3. Submit the signed FBAR, and 4. Retain a copy of your submission.

The Split between the Fifth Circuit and Ninth Circuit

In March 2021, the Ninth Circuit held that the Internal Revenue Service (IRS) could impose the maximum penalty amount of \$10,000 per-form rather than per-account.¹³ Just a few months later, in November 2021, the Fifth Circuit expressly rejected this interpretation and held that the term “violation” means the failure to report a qualifying account; thus, the maximum penalty applies on a per-account basis.¹⁴

The current circuit split produces inconsistent and dissimilar penalty assessments for similarly situated taxpayers depending on their residence. With the exception of taxpayers who reside within the jurisdiction of the Ninth Circuit, the IRS could assess the maximum FBAR penalty on a per-account basis for taxpayers who failed to timely file a proper FBAR and whose failure to do so is considered non-willful.

For example, on the facts of the *Bittner* case, if the government’s interpretation is correct that the penalty applies on a per-account basis, the taxpayer would be liable to pay a total of \$2,720,000 for more than 25 unreported accounts during the period from 2007 through 2011. By contrast, if the taxpayer’s per-form argument is correct, the taxpayer would be liable for a penalty of just \$50,000, which is a penalty assessment of \$10,000 for each year’s delinquent FBAR from 2007 through 2011. As demonstrated by the example, non-willful violations could result in a large or more modest penalty assessment depending on the final ruling of the Supreme Court.



Delinquent FBARs

There are several available options for taxpayers to come into compliance with their FBAR filing requirements.

Taxpayers with delinquent FBARs may choose to use the delinquent FBAR submission procedures or the streamlined filing compliance procedures depending on the individual’s situation. As the current issue before the Supreme Court shows, the failure to file an FBAR, or a late filing, may subject

taxpayers to civil or criminal penalties. However, if taxpayers can show reasonable cause for delinquent FBARs, the IRS may waive FBAR-related penalties if it finds that the taxpayer exercised ordinary business care and prudence to fulfill his or her reporting obligations but was unable to comply.¹⁵

Relief from Penalties

No penalty is assessed for a non-willful violation if the violation was due to “reasonable cause” and the amount of the transaction or the balance in the account at the time of the transaction was properly reported.¹⁶ Reasonable cause is not defined in the statute and case law requires that the taxpayer exercised ordinary business care and prudence, considering all pertinent facts and circumstances on a case-by-case basis.¹⁷ The burden is on the taxpayer to provide evidence in support of reasonable cause for penalty relief.¹⁸

When determining reasonable cause, the IRS will consider all relevant facts, having regard to the taxpayer’s experience, knowledge, education, sophistication, and the extent of the taxpayer’s effort to comply with the requirements.¹⁹ For example, an IRS examiner would look to the taxpayer’s reason for noncompliance, compliance history, the length of time between the event cited as a reason for the noncompliance and subsequent compliance to determine whether a taxpayer exercised ordinary business care and prudence.²⁰ The determination whether the exception applies is a fact-intensive inquiry.



Delinquent FBAR Submission Procedures

The delinquent FBAR submission procedures program is for taxpayers who are not under civil or criminal exam and have reported all income related to unreported accounts. Taxpayers who have not been contacted by the IRS about late FBARs and are not under civil or criminal investigation by the IRS should file delinquent FBARs in accordance with the FBAR Instructions.²¹

The IRS will not impose a penalty if income from the foreign financial accounts reported on the delinquent FBARs was properly reported on U.S. tax returns and all taxes were paid.²² Delinquent FBARs should indicate a reason for the late filing by using the drop-down menu and selecting “Other” as the reason, allowing the taxpayer to include a statement with the filing. A separate statement should be included with each delinquent FBAR and the statement should indicate the reasons as to why the taxpayer qualifies for penalty-free treatment.

If the above criteria under the IRS’s current policy are met (i.e., all income reported, all taxes paid, not under IRS exam, IRS correspondence has not been received regarding missing FBARs), the included statement should affirmatively state that these facts have been satisfied, thus qualifying the filer for penalty relief. Taxpayers filing an amended FBAR do not need to include a statement and an amended FBAR is not likely to result in a penalty.

Streamlined Filing Compliance Procedures

The streamlined filing compliance procedures are available to both U.S. individual taxpayers residing within (Streamlined Domestic Offshore Procedures) and outside (Streamlined Foreign Offshore Procedures) the United States.

Taxpayers can participate in these procedures if:

1. they are able to certify that conduct was not willful;
2. the IRS has not initiated a civil examination of taxpayer’s returns for any taxable year; and
3. they have a valid Taxpayer Identification Number.²³



In addition to meeting the general eligibility requirements above, taxpayers participating in either the Streamlined Foreign Offshore Procedures or Streamlined Domestic Offshore Procedures must meet the specific eligibility requirements for respective streamlined procedures.

U.S. taxpayers seeking to use the Streamlined Foreign Offshore Procedures must:

1. meet the applicable non-residency requirement described below (for joint return filers, both spouses must meet the applicable non-residency requirement described below); and
2. have failed to report the income from a foreign financial asset and pay tax as required by U.S. law, and may have failed to file an FBAR with respect to a foreign financial account, and such failures resulted from non-willful conduct.²⁴

Individual taxpayers²⁵ meet the applicable non-residency requirement if, in any one or more of the most recent three years for which the U.S. tax return due date (or properly applied for extended due date) have passed, the individual did not have a U.S. abode, and the individual was physically outside the United States for at least 330 full days.²⁶

An eligible taxpayer who uses these Streamlined Foreign Offshore Procedures and complies with all of the instructions will not be subject to any offshore penalties.²⁷

For individual taxpayers seeking to use the Streamlined Domestic Offshore Procedures, they must:

1. fail to meet the applicable non-residency requirement described in the “Eligibility for the Streamlined Offshore Procedures” (for joint return filers, one or both of the spouses must fail to meet the applicable non-residency requirement described in the “Eligibility for the Streamlined Offshore Procedures”);
2. have previously filed a required U.S. tax return for each of the most recent three years for which the U.S. tax return due date (or properly applied for extended due date) has passed;
3. have failed to report gross income from a foreign financial asset and pay tax as required by U.S. law, and may have failed to file an FBAR and/or one or more international information returns (e.g., Forms 3520, 3520-A, 5471, 5472, 8938, 926, and 8621) with respect to the foreign financial asset, and such failures resulted from non-willful conduct.²⁸



IRS Criminal Investigation Voluntary Disclosure Practice

Taxpayers who are unable to certify that the failure to report income, pay tax, and file required informational returns was non-willful, and therefore do not qualify for streamlined procedures, should consider consulting with their legal or professional adviser regarding participation in the IRS's Criminal Investigation Voluntary Disclosure Practice to avoid criminal liability and substantial penalties.

Conclusion

As illustrated by the delinquent FBAR filing procedures as well as the streamlined procedures, there are many ways for noncompliant taxpayers to comply with the FBAR filing requirements and reduce or avoid penalties. For taxpayers eligible for these favorable programs, the Supreme Court's decision in the *Bittner* case should not affect them.

Thus, for taxpayers who reported income and paid taxes related to their foreign financial accounts, and unintentionally failed to file required FBARs, relief may be found simply by filing their delinquent FBARs under one of the IRS's generous programs. These taxpayers need not wait for a favorable ruling from the Supreme Court in the *Bittner* case.

But these programs exist at the discretion of the IRS, so taxpayers who discover reporting failures should take prompt corrective action while the opportunity for favorable relief is available.

If all of the above requirements are met and the eligible taxpayer complies with all of the instructions provided under the streamlined procedures, the taxpayer will be subject only to a five-percent miscellaneous offshore penalty²⁹ and will not be subject to accuracy-related penalties, information return penalties, or FBAR penalties.³⁰

Footnotes:

1. See *United States v. Bittner*, 19 F.4th 734 (5th Cir. 2021), cert. granted, 142 S. Ct. 2833 (2022).
2. Generally, a person has a financial interest in a financial account if the person is the owner of record, holder of legal title; acts as an agent, nominee, attorney, or in some other capacity on behalf of a U.S. person with respect to the account; has a more-than-50-percent ownership interest (held directly or indirectly) in a corporation, partnership, or other entity, is the grantor of a trust, or has a more than 50-percent beneficial interest in a trust (based on the trust assets or current income). See 31 C.F.R. § 1010.350(e).
3. Signature or other authority means the authority of an individual (alone or in conjunction with another) to control the disposition of money, funds or other assets held in a financial account by direct communication (whether in writing or otherwise) to the person with whom the financial account is maintained. 31 C.F.R. § 1010.350(f)(1).
4. The definition of "financial accounts" includes bank accounts, securities account, insurance/annuity with cash value, mutual funds, and any other accounts maintained in a foreign financial institution. 31 C.F.R. § 1010.350(c).
5. See 31 U.S.C. § 5311, et seq.
6. 31 C.F.R. §§ 1010.350(a), 1010.306(c).
7. For 2022 FBAR violations, the non-willful penalty is \$14,489.
8. See 31 U.S.C. § 5321(a)(5)(A); 31 C.F.R. § 1010.821. The maximum value of an account is a reasonable estimate of the greatest value of currency and non-monetary assets in the account during the calendar year.
9. See 31 U.S.C. § 5321(a)(5)(B).
10. For 2022 FBAR violations, the willful penalty is \$144,886.
11. See 31 U.S.C. § 5321(a)(5)(C).
12. See 31 U.S.C. § 5321(b)(1).

13. See *United States v. Boyd*, 991 F.3d 1077 (9th Cir. 2021) (holding that only one penalty may be imposed per-form when an untimely but accurate FBAR is filed).
14. See *United States v. Bittner*, 19 F.4th 734 (5th Cir. 2021), cert. granted, 142 S. Ct. 2833 (2022) (a holding that rejected the reasonable cause argument and upheld a penalty amount of \$2.72 million for failing to file for over 25 foreign financial accounts for five years). The Fifth Circuit rejected the reasonable cause argument because the taxpayer failed to exercise ordinary business care and prudence. See *id.* at 742.
15. See 31 U.S.C. § 5321(a)(5)(B)(ii); IRM 4.26.16.5.2.1 (06-24-2021); IRS LB&I Reasonable Cause and Good Faith (Mar. 18, 2021).
16. See 31 U.S.C. § 5321(a)(5)(B)(ii).
17. See *Bittner*, 19 F.4th at 741–742; I.R.M. 20.1.1.3.2.2 (Feb. 22, 2008).
18. See *United States v. Boyle*, 469 U.S. 241, 245 (1985).
19. See IRS LB&I Reasonable Cause and Good Faith (Mar. 18, 2021).
20. See IRM 20.1.1.3.2.2.
21. See “IRS Delinquent FBAR Submission Procedures”; “BSA Electronic Filing Requirements For Report of Foreign Bank and Financial Accounts” (Form TD F 90-22.1) (<https://www.fincen.gov/>) at: <https://www.fincen.gov/sites/default/files/shared/FBAR%20Line%20Item%20Filing%20Instructions.pdf>. (Last visited Nov. 2, 2022).
22. See “IRS Delinquent FBAR Submission Procedures.”
23. See <https://www.irs.gov/individuals/international-taxpayers/streamlined-filing-compliance-procedures> (last visited Nov. 2, 2022).
24. See <https://www.irs.gov/individuals/international-taxpayers/us-taxpayers-residing-outside-the-united-states> (last visited Nov. 2, 2022). Non-willful conduct is conduct that is due to negligence, inadvertence, or mistake or conduct that is the result of a good faith misunderstanding of the requirements of the law.
25. The term “individual taxpayers” includes U.S. citizens or lawful permanent residents, or estates of U.S. citizens or lawful permanent residents. See *id.*
26. *Id.*
27. Offshore penalties refer to failure-to-file and failure-to-pay penalties, accuracy-related penalties, information return penalties, or FBAR penalties. See *id.*
28. See <https://www.irs.gov/individuals/international-taxpayers/u-s-taxpayers-residing-in-the-united-states> (last visited Nov. 2, 2022).
29. The Title 26 miscellaneous offshore penalty is equal to 5 percent of the highest aggregate balance/value of the taxpayer’s foreign financial assets that are subject to the miscellaneous offshore penalty during the years in the covered tax return period and the covered FBAR period.
30. See <https://www.irs.gov/individuals/international-taxpayers/u-s-taxpayers-residing-in-the-united-states> (last visited Nov. 2, 2022).

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