Offshore Update: *USA v. Kaufman* and How Not to FUBAR Your FBARs

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About Green & Sklarz LLC and Jeff Sklarz

Green & Sklarz LLC is a business law boutique headquartered in New Haven, CT.

Jeff represents business and individuals around the country in matters involving bankruptcy, civil and criminal tax litigation, and business litigation.

Jeff is a Fellow of the American College of Tax Counsel (ACTC), and has been included in the 2021 Edition of *The Best Lawyers in America*© for Bankruptcy and Creditor Debtor Rights / Insolvency and Reorganization Law.

He received his J.D. from the University of Connecticut School of Law, and received his LL.M from Boston University School of Law.

About Marcus Neiman Rashbaum & Pieneiro LLP and Jeff Neiman

Jeff regularly defends individuals and corporations in white collar criminal litigation, matters involving tax controversies, government regulatory enforcement matters, internal investigations, compliance counseling, and complex civil litigation. Jeff has tried more than a dozen white collar matters in federal court.

Prior to being a Founding Member of Marcus Neiman & Rashbaum LLP, Jeff had his own law firm that focused on white collar and tax controversy matters. Jeff is an alum of the United States Department of Justice (DOJ) Attorney General's Honors Program. He began his career working for the DOJ. He then served as an Assistant United States Attorney for the Southern District of Florida, where he received national recognition for handling complex, high profile matters including the ground-breaking and historic prosecution of Switzerland's largest bank, UBS AG, for aiding American citizens to commit tax fraud. Jeff was awarded the Attorney General's John Marshall Award for Outstanding Legal Achievement and the Internal Revenue Service Commissioner's Award, the highest recognition a prosecutor can receive.

Jeff graduated with honors from the University of Florida and also graduated from law school at the University of Florida where he was a member of Order of the Coif. Jeff currently serves as an adjunct professor at Florida Atlantic University, where he teaches Criminal Procedure and Tax Fraud in their graduate accounting executive program. Jeff also is a frequent lecturer, panelist, and contributor at national conferences on topics including offshore tax evasion, tax fraud, Ponzi schemes and trial practice.

Agenda

- Foreign account reporting generally
- *USA v. Kaufman*
- Questions

FBARs Generally

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Foreign Account Reporting Generally

- Established by Bank Secrecy Act (BSA), 31 U.S.C. 5311, *et seq.* establishes various rules for reporting foreign income, among other things.
- Any "United States person" who has an *interest in* or *signature authority over* foreign financial accounts with an *aggregate value* of more than $10,000 must file a *Foreign Bank and Financial Accounts Report* (FBAR)
- Not an IRS form, it's a FinCEN form – Form 114
- The term "United States Person" means: a citizen, resident, corporation, partnership, LLC, trust, or estate.
- Applies to most financial accounts not just bank accounts.

Foreign Account Reporting Generally

Exceptions to requirement to file:

- You are a notice party on an account (neither financial interest nor signature party)
- The account is owned by a governmental entity
- The account is owned by an international financial institution
- The account is maintained on an overseas military based banking facility
- The account is held in an IRA or other retirement plan
- The account is held as part of a trust of which you're a beneficiary *but only if* a U.S. person files an FBAR reporting these accounts.

Foreign Account Reporting Generally

Financial Interest of U.S. Person:

- Holds legal title to account, regardless of whether for the benefit of another person (i.e. a trustee)
- A corporation that owns directly or indirectly (a) more than 50% of stock of company that owns a foreign account or (b) more than 50% of the voting power of the stock
- A partnership that owns directly or indirectly (a) holds an interest in 50% or more of the partnership's profits or (b) more than 50% of the ownership interest
- A trust which has a greater than 50% beneficial interest in the assets of the foreign account in any year. *Note,* remainder interests don't count.
- The owner of record or holder of legal title is an entity in which owns directly or indirectly more than 50% of the voting power, total value of equity interest or assets, or interest in profits
- Signature authority, alone or with another person

Foreign Account Reporting Generally

Additional Rules

- Each U.S. Person must report
- Typically, the spouse of a U.S. Person required to file an FBAR doesn't have to separately file an FBAR
- FBAR is due April 15th and must be electronically filed

Foreign Account Reporting Generally

Information You Need to Complete FBAR

- Name on each account
- 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.

Required for each account

Foreign Account Reporting Generally

Penalties for Failure to File

- Non-Willful Violation: $10,000. 31 USC 5321(a)(5)(A) and (B)(i).
- Willful: Up to the greater of $100,000 or 50% of the average amount in the account at the time of the violation

FBAR penalties are not assessed taxes. Thus, the government must bring a lawsuit to enforce an FBAR penalty

Foreign Account Reporting Generally

IRM 4.26.16.6.4.1 (11-06-2015) - Penalty for Nonwillful Violations - Calculation

1. After May 12, 2015, in most cases, examiners will recommend one penalty per open year, regardless of the number of unreported foreign accounts. The penalty for each year is limited to $10,000. Examiners should still use the mitigation guidelines and their discretion in each case to determine whether a lesser penalty amount is appropriate.
2. For multiple years with nonwillful violations, examiners may determine that asserting nonwillful penalties for each year is not warranted. In those cases, examiners, with the group manager's approval after consultation with an Operating Division FBAR Coordinator, may assert a single penalty, not to exceed $10,000, for one year only.
3. For other cases, the facts and circumstances (considering the conduct of the person required to file and the aggregate balance of the unreported foreign financial accounts) may indicate that asserting a separate nonwillful penalty for each unreported foreign financial account, and for each year, is warranted. In those cases, examiners, with the group manager's approval after consultation with an Operating Division FBAR Coordinator, may assert a separate penalty for each account and for each year. The examiner's workpapers must support such a penalty determination and document the group manager's approval.
4. In no event will the total amount of the penalties for nonwillful violations exceed 50 percent of the highest aggregate balance of all unreported foreign financial accounts for the years under examination.

Foreign Account Reporting Generally

IRM 4.26.16.6.5.3 (11-06-2015) -Penalty for Willful FBAR Violations - Calculation

1. For violations occurring after October 22, 2004, a penalty for a willful FBAR violation 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 USC 5321(a)(5)(C). For cases involving willful violations over multiple years, examiners may recommend a penalty for each year for which the FBAR violation was willful.
2. After May 12, 2015, in most cases, the total penalty amount for all years under examination will be limited to 50 percent of the highest aggregate balance of all unreported foreign financial accounts during the years under examination. In such cases, the penalty for each year will be determined by allocating the total penalty amount to all years for which the FBAR violations were willful based upon the ratio of the highest aggregate balance for each year to the total of the highest aggregate balances for all years combined, subject to the maximum penalty limitation in 31 USC 5321(a)(5)(C) for each year. **Note:** Examiners should still use the mitigation guidelines and their discretion in each case to determine whether a lesser penalty amount is appropriate
3. Examiners may recommend a penalty that is higher or lower than 50 percent of the highest aggregate account balance of all unreported foreign financial accounts based on the facts and circumstances. In no event will the total penalty amount exceed 100 percent of the highest aggregate balance of all unreported foreign financial accounts during the years under examination. The examiner's workpapers must support all willful penalty determinations and document the group manager's approval.
4. If an account is co-owned by more than one person, a penalty determination must be made separately for each co-owner. The penalty against each co-owner will be based on his or her percentage of ownership of the highest balance in the account. If the examiner cannot determine each owner's percentage of ownership, the highest balance will be divided equally among each of the co-owners.

USA v. Kaufman

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The Facts and Background

- Kaufman lived in Israel since 1979.
- From 2008-2010, Kaufman was a U.S. Person for FBAR reporting purposes and maintained several accounts in Israel.
- Kaufman failed to file FBARs for those years.
- The IRS assessed a non-willful FBAR penalty of $42,249 for 2008, $42,287 for 2009, and $59,708 for 2010.
- Kaufman took the position that he was not liable as he properly relied on professionals regarding his tax reporting ***but*** even if he was, the maximum penalty is $30,000, or $10,000 maximum penalty per year.

Arguments: Reasonable Cause

- No dispute about the failure to file.
- Kaufman had "reasonable cause" for the failure to file:
  - "If the taxpayer exercised ordinary business care and prudence and was nevertheless unable to file the return within the prescribed time, then the delay is due to a reasonable cause." 26 C.F.R. § 301.6651-1(c)(1)
  - While a taxpayer may reasonably rely on the advice of an accountant or attorney on a matter of tax law, "that reliance cannot function as a substitute for compliance with an unambiguous statute... The failure to make a timely filing of a tax return is not excused by the taxpayer's reliance on an agent, and such reliance is not 'reasonable cause' for a late filing under § 6651(a)(1)." *United States v. Boyle*, 469 U.S. 241 (1985).
- Kaufman did not tell his CPA about foreign accounts.
- "There is no dispute that Kaufman knew that he had an interest in or signatory authority over multiple financial accounts in Israel. Yet, Kaufman failed to undertake any efforts to ascertain his reporting obligations in the United States for these accounts prior to September of 2011." *Kaufman* at 11.

Arguments: $10,000 per Year Maximum Penalty

- Government argued for a penalty of $10,000 per account.
- Kaufman argued for $10,000 per year maximum.
- Two courts have ruled on this issue, with contradictory results:
  - *USA v. Bittner*, 469 F. Supp. 3d 709 (E.D. Tex. 2020) (per year), *appeal docketed No. 20-40597, (5th Cir. Sept. 11, 2020)*
  - *USA v. v. Boyd*, 2019 WL 1976472 (C.D. Cal. Apr. 23, 2019) (per account), *appeal argued*, No. 19-55585 (9th Cir. Sept. 1, 2020)
- Court undertook a rigorous statutory analysis with reference to the willful penalty provisions
- Determined that the statute says $10,000/year, based on clear wording of statute, which excluded the "balance [of the account] as a benchmark for" assessing the penalty that is done for willful penalties.

Takeaways

- Two cases are on appeal and *Kaufman* is likely to be appealed.
- Circuit splits could result.
- Reasonable cause is a hard argument to make, particularly where the accountant asks for the information and it isn't supplied

Questions?