

On 5/6/09, the IRS posted FBAR: FAQ #12

Under FAQ #12, the IRS projected a \$1M deposit on account in a foreign bank, interest income (\$50,000 per year) for 6 years, total income \$300,000. Based on IRS projections, the \$300,000 unreported income (undisclosed foreign bank account) may result in up to \$2,306,000 due the IRS for:

1. Tax
2. Accuracy Related Penalty
3. FBAR Penalty
4. Compounded Interest
5. Plus Additional Penalties (e.g. failure to pay penalty) and Criminal Prosecution

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.)

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 x 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 x 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.

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