FBARs for the Immigration Bar

By Jo Anne C. Adlerstein

Introduction

In recent years, immigration practitioners have increasingly been required to deal with complex corporate and tax issues. We have examined voluminous corporate annual reports, SEC filings and audited financial statements to demonstrate L-1 relationships, analyzed federal income tax returns of U.S. employers to establish ability to pay the prevailing wage, documented affidavits of support for I-130 petitioners, and reviewed clients' Forms W-2 in connection with H-1B/Labor Condition Application compliance audits. Now there is one more financial form that demands our attention: the FBAR.

The Report of Foreign Bank and Financial Accounts (FBAR), TDF 90-22.1, is not a tax return. It is an information report that must be filed annually by every "U.S. person" who is an owner, joint owner, or signator of a financial or bank account outside the U.S. which has a balance in excess of $10,000 in the prior year. Unlike income tax returns, FBARs are not due by April 15 and are not filed with the Internal Revenue Service (IRS). FBARs are due by June 30 and filed with the U.S. Department of the Treasury in Detroit, Michigan.

While there have not yet been IRS alerts on the relevance of FBARs for foreign nationals or AILA seminars on the subject, FBAR compliance can be a ticking time-bomb for affluent visa holders and NAFTA foreign nationals. This article provides an introduction to the FBAR – its history, definitions, requirements, non-filing penalties, and suggestions for counseling nonimmigrant visa (NIV), lawful permanent resident (LPR) and naturalization clients.

History of the FBAR

The gangster Al Capone made his illicit fortune smuggling and bootlegging liquor in the Prohibition years. However, he was ultimately convicted of tax evasion. From that time on, law enforcement has followed the money trail of organized criminals and drug dealers in an attempt to deter crime. The FBAR was developed as a mechanism to detect and deter money laundering as part of the Bank Secrecy Act of 1970 ("BSA") (31 USC §5314 and 31 CFR §§103.24, 103.27). The BSA, in pertinent part, requires financial institutions in the United States to report currency transactions involving $10,000 or more and to report suspicious activity that might suggest criminal conduct such as money laundering and tax evasion.

After 9/11 and the enactment of the U.S. Patriot Act in 2001, the U.S. Financial Crimes Enforcement Network (FinCen) and IRS stepped up investigation of alleged money laundering by terrorist organizations.

Since 1970, the U.S. Government has had the authority to use the BSA to deter money laundering, terrorist financing, and tax evasion by seeking information about foreign bank accounts and transfers and to prosecute those who failed to file FBARs. In 2003, Congress gave the IRS responsibility for imposing penalties on failure to file FBARs, and IRS conducted its first Offshore Voluntary Compliance Initiative. Still, it took until 2008 for the FBAR to catch the attention of the general public. That year, the battle between the U.S. Department of Justice (DOJ) with Union Bank of Switzerland (UBS) over the identity of U.S. citizens with secret numbered Swiss accounts became public. In February 2009, UBS entered into an agreement with the DOJ whereby UBS admitted to helping U.S. taxpayers hide accounts from the IRS, and UBS agreed to provide the U.S. Government with the identities and account information for U.S. customers of UBS with cross-border business. IRS has now moved on to other banks.

In 2009, the IRS again tried to increase FBAR filing and deter tax evasion with a Voluntary Disclosure Program (VDP) for taxpayers with unreported income from offshore accounts. By October 15, 2009, almost 15,000 taxpayers filed VDP applications for reduced penalties for under-reporting of income and non-filing of FBARs. Soon after, criminal prosecutions of UBS account holders began in earnest. In April 2010, the U.S. Attorney's Office for the Southern District of New York filed charges against seven UBS account holders including charges of willful failure to file FBARs and filing false FBARs. These cases continue to garner media coverage.

Signs of an even greater Government crackdown on hidden foreign accounts are increasing. It is reported that a whistleblower from another Swiss bank turned over account information to the DOJ on U.S customers who were hiding income from IRS. On December 9, 2010 the Commissioner of IRS confirmed that IRS is "data mining" the information it received from 2009 VDP applicants. Taxpayers who successfully completed the VDP and entered into closing agreements with IRS are now being

contacted by the IRS Criminal Investigation Division (CID) so they can be questioned about their contacts with the offshore banks they disclosed. On February 8, 2011 launched its 2011 Offshore Voluntary Disclosure Initiative (2011 OVDI). Because so many individuals are now under investigation as a result of IRS data mining, the first step in the 2011 OVDI is to contact CID to confirm that the applicant is not under audit or investigation. Only then can the application be made.

In late September 2010, FinCen released controversial proposed regulations which would require financial institutions to report cross-border electronic transmittals of fund (CBETF)and to annually file a list of the taxpayer identification numbers of account holders who transmitted or received a CBETF. It is beyond the scope of this article to discuss the impact of the 2010 Foreign Account Tax Compliance Act (FATCA) which would require all kinds of disclosures from foreign banks and U.S. taxpayers. In this environment, the immigration practitioner must learn about FBARs in order to alert and better represent clients who are potentially required to file FBARs.

Who Must File an FBAR?

FBARs must be filed by "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." TDF 90-22.1. Over the past year, there has been increased scrutiny over who is a "United States person." In Announcement 2010-16, IRS stated that it considers a "U.S. person" to include a citizen or resident of the United States, a domestic partnership, a domestic corporation, and a domestic estate or trust.

One of the confusing legal concepts immigration practitioners must often explain to their clients is that a "resident" of the U.S. is defined differently under federal immigration and tax laws. Under the Immigration and Nationality Act (INA), an LPR is a person who has "been lawfully accorded the privilege of residing permanently in the United States as an immigrant in accordance with the immigration laws…" INA 101(a) (20) Under the Internal Revenue Code (IRC), a foreign national is a resident for tax purposes if s/he meets one of two tests: the "green card" test or the "substantial presence" test. Under the first test, any individual who holds a "green card", or otherwise has been accorded at any time during the calendar year LPR status under immigration law, is a resident for tax purposes. IRC 7701(b)(1)(A). Under the second test, a foreign national who has been "substantially present" in the United States is a "resident" for tax purposes. The tax code defines "substantial presence" as: "an individual who has been physically present in the United States at least 31 days during the current year, **and** 183 days during the 3 year period that includes the current year and the 2 years immediately before." IRC 7701(b)(3). This means foreign nationals working in the U.S. in a myriad of NIV statuses may be considered "residents" for federal income tax purposes including individuals on TN, E, H, L, O, P and R visas.

It could be worse. The FBAR statute, 31 USC §5314 actually includes "a person in, and doing business in, the United States" in the enumeration of who must file an FBAR. Announcement 2010-16 has temporarily excluded persons and entities who are neither citizens nor residents but are "doing business in the United States" from those required to file FBARs. The expansion of enforcement to persons merely "doing business" would have vast repercussions for the immigration bar. It could arguably mean a foreign national doing business in the United States pursuant to the Visa Waiver program or a B-1 visa could be required to file FBARs.

Accounts Requiring FBARs

One or more qualifying foreign accounts with an aggregate value greater than $10,000 in a calendar year must be reported by "U.S. persons." These accounts include bank accounts—saving, checking, certificate of deposit, insurance policies with a cash surrender value, securities accounts, certain pension funds, and mutual funds. IRS is clear that individual stock certificates, art collections, jewelry and real property are not accounts. The IRS Workbook explains that the location of the account, not the nationality of the institution at which it is held, determines whether an account is foreign and must be reported. Thus, an account at a New York branch of a European-based bank need not be reported on an FBAR, but an account at a European branch of a New York-based bank must be reported on an FBAR. It is important to note that Form 1040 Schedule B instructions explain that if a "U.S. person" owned more than 50% of the stock in any corporation that owns one or more foreign bank accounts, the "U.S. person" must report it on an FBAR.

Civil Penalties for Non-Filing of FBARs

In 2004, Congress increased the civil penalty for failing to file an FBAR to $10,000 if the non-filing was not willful, and if willful, the greater of $100,000 or 50% of the account balance (31 USC §5321(a)(5)) If a U.S. taxpayer has timely reported all income,

including income derived from the foreign account, it is unlikely that the maximum FBAR penalty will be imposed and possible that no FBAR penalty will be imposed. However, non-reporting of income exposes taxpayers to civil accuracy related penalties, interest, fraud penalties and criminal prosecution.

The $10,000 penalty is generally not imposed if the violation was due to reasonable cause and the balance in the account is properly reported on an FBAR. Great discretion is given to IRS examiners in evaluating mitigating circumstances. Even the gargantuan 50% penalty is a ceiling, not a mandated amount.

Criminal Prosecution Relating to FBARs

One of the 2010 indictments brought by the U.S. Attorney for the Southern District of New York describes in detail how an LPR can run afoul of the FBAR laws. (*U.S. v. Sternfeld*, 10 Crim. 328 (MGC)) According to the allegations, the defendant, a citizen of Israel and LPR of the United States, opened a UBS account in the name of a Hong Kong shell corporation and from 2004 to 2008 transferred hundreds of thousands of dollars from his UBS account to a bank account in the Czech Republic and to another Swiss bank (which, unlike UBS, did not have a U.S. presence). He also transferred money from his UBS account to make a down payment on a Florida condominium, and right after the U.S. criminal investigation of UBS was reported by the press, he closed his UBS account.

The first count of the indictment charges the defendant with conspiring with UBS and others to defraud the United States and the IRS by impeding, impairing, defeating and obstructing the lawful governmental functions of the IRS in ascertaining, computing, assessing and collecting income taxes. Conspiracy to defraud the U.S. (18 U.S.C. 371) carries a maximum sentence of five years in jail and a $250,000 fine. The second count charges the defendant with filing a false tax return (26 USC §7206(1). in two regards – the failure to report interest, dividends and other income from his UBS account and failing to disclose that he had an interest in or authority over foreign bank accounts on Form 1040, Schedule B . Filing a false tax return carries a maximum sentence of three years in jail, a $250,000 fine and costs of prosecution. The remaining counts charge willful failure to file FBARs for five years in violation of 31 USC §5314 and 5322(a) and 31 CFR §§103.24, 103.27 and 103.59(b). Each of these counts carries a maximum sentence of five years in jail and a $250,000 fine.

Another criminal statute that could have been charged was income tax evasion in violation of 26 USC §7201.

The immigration consequences of conviction of any of these charges to a foreign national client could be severe as they may constitute aggravated felonies (INA 101(a)(43)(M)) and crimes of moral turpitude (INA 212a)(2)).

However, the lawyer who encounters a client who has failed to file an FBAR does not have to tell him to pack his toothbrush for jail. Remediation is encouraged. Late-filed FBARs, amended tax returns, and in serious cases, voluntary disclosure through 2011 OVDI, can avert hefty penalties and prosecution in the majority of cases. However, 2011 OVDI is not the answer for every client. If all offshore income has been timely reported on U.S. tax returns, mere late filing of FBARs may suffice.

FBARs and the NIV Client

So far neither FinCen nor the IRS has publicly targeted non-immigrants who have failed to file FBARs. The latest version of the *U.S. Tax Guide for Aliens* (IRS Publication 519, 2009) makes no mention of FBARs.

Foreign nationals who will work in non-immigrant visa status in the United States generally consult with an accountant annually to determine if they will be required to file federal income tax returns. Initially and typically they will file as non-residents on Form 1040-NR (U.S. Nonresident Alien Income Tax Return) or Form 1040-NR-EZ (U.S. Income Tax Return for Certain Nonresident Aliens With No Dependents). Neither of these forms inquires about ownership of foreign bank accounts.

However, at such time foreign nationals become "residents" as defined by tax law, they are be required to file U.S. resident tax return forms. Form 1040, Schedule B includes the following questions:

> **7 a** At any time during 2009, 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 instructions on back for exceptions and filing requirements for Form TD F 90-22.1 . . ..
>
> **b** If "Yes," enter the name of the foreign country >_____.

The form instructs the filer to review instructions for filing requirements for FBARs and exceptions relating to same.

An LPR or a non-immigrant who must file a resident income tax return might choose to file the simpler Form 104EZ if he or she has no dependents. Surprisingly, Form 1040EZ does not inquire about foreign financial accounts, and its instructions make no mention of FBAR filing requirements. Thus, an NIV may know nothing of the FBAR requirements unless his or her tax-preparer raises the concern.

Not all accountants are aware of these issues. For example: A Canadian citizen is in the U.S. under TD status. Her husband is on a TN visa. They hired an accountant to prepare their 2009 U.S. tax return. Because they had both been in the United States for more than 183 days in 2009, they met the "substantial presence" test and the accountant correctly advised them to file Form 1040 as U.S. "residents." The clients were concerned that their "resident" tax returns might violate their NIV visa status under NAFTA. We advised them that filing tax returns as a "resident" does not violate NIV status. The accountant neglected to ask the couple about any financial accounts in Canada. The clients have now filed an FBAR and retained a new accountant for preparation of an amended Form 1040.

FBARs and the LPR Client

When NIV clients apply for LPR status, they must be found eligible. The Application to Adjust Status to Permanent Resident on Form I-485 asks at Part 3 C1 if the applicant has "ever knowingly committed any crime of moral turpitude … for which you have not been arrested?" A willful failure to acknowledge at Schedule B of Form 1040 that the applicant has a foreign bank account and the willful failure to file an FBAR could be construed to constitute a crime of moral turpitude and, thus, could jeopardize the applicant's eligibility for LPR status. Thus, before filing Form I-485, immigration practitioners should ask whether the applicant has had foreign bank or financial accounts since entering the United States. If the answer is in the affirmative, tax returns must be reviewed, and if necessary, amended to reflect the accounts. If the accounts exceed the FBAR threshold of $10,000, FBARs should be late filed.

After clients obtain LPR status and, if applicable, seek a Reentry Permit because they need to live outside the United States for a period of time, immigration practitioners should advise their clients of the need to file federal and state income tax returns annually as "U.S. residents." Moreover, if the client maintains certain foreign bank and/or financial accounts, the client should consult with his or her accountant or tax attorney to determine if he or she is required to file an FBAR.

FBARs and the Naturalization Client

Immigration practitioners should consider the relevance of FBARs to LPR clients applying for citizenship. While Form N-400 does not yet mention FBARs, it has two questions which should raise FBAR concerns:

> Part 10A (General Questions) Question 4: "Since becoming a lawful permanent resident have you ever failed to file a required federal, state or local tax return?"
>
> Part 10D (Good Moral Character) Question 15: "Have you **ever** committed a crime or offense for which you were **not arrested**?"

The FBAR is not a "tax return"; it is an information return or report. Unless and until Question 4 is revised, FBARs are not covered by Question 4. However, the *willful* failure to file an FBAR when required to do so could be considered "a crime or offense." Thus, if the LPR client was required to file one or more FBARs and has not done so, the client should be referred to a tax attorney to evaluate how to file the FBARs and whether a voluntary disclosure is necessary.

Recently an immigration practitioner reported that a New Jersey client had been denied naturalization because while the client had timely filed tax returns and had entered into a payment plan with IRS, he had failed to make the agreed-upon monthly payments to IRS. While the question raised by the naturalization examiner was not related to FBARs, it shows that examiners are increasingly aware of tax issues and they may inquire further into a person's IRS records. Potentially, failure to file an FBAR, like failure to honor an IRS payment plan, may affect one's ability to establish good moral character for naturalization purposes.

FBARs and the Affidavit of Support

Immigration practitioners routinely submit their clients' individual federal tax returns to U.S. Citizenship and Immigration Services (USCIS) or to U.S. Consulates in support of Forms I-864, I-864A,or I-864EZ to show that the beneficiary will not become a public charge. A sponsoring family member who is a U.S. citizen or LPR may have a bank or financial account in the country from which the foreign national is emigrating. At this time, it is unlikely that a USCIS adjudicator in a spousal adjustment of status case will ask the petitioning spouse about FBARs or foreign bank and financial accounts. However, with the tax return in the adjudicator's file, and depending upon the foreign nationality of the applicant, it is an area of questioning that could arise in the future.

Thus, the immigration practitioner should counsel the petitioning spouse to verify with his or her accountant or tax attorney whether FBAR filing was or is necessary.

Protecting Your Client

Your NIV and immigrant clients may be required to file FBARs and may be asked about FBARs at immigration interviews. It is therefore incumbent upon the immigration practitioner to alert both her immigrant and NIV clients of the "substantial presence" test and, thus, not only the necessity of filing federal income tax returns, but also the possibility that FBARs may need to be filed if foreign accounts or foreign corporate ownership meet the regulatory requirements. In the event that the client has not filed required tax returns or FBARs, a referral should be made to a certified public accountant or tax attorney, depending on the circumstances.

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