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Treaty Case Training - Session 3 Offshore Information Return Penalties

Please call into our Conference Call
@ 1-866-606-4717

Access Code 3024120

**You will NOT need your Headsets for
this session**

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Treaty Case Training - Session 3 Offshore Information Return Penalties

Today's Session

- Combination of CENTRA & a Conference call
- If you have a question, please click on the button that looks like a raised hand



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Handouts & Technical Problems

If you have a technical problem with
CENTRA, or
you need copies of the handouts for
today's presentation,
please email

Larry.G.Akins@IRS.GOV

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Treaty Case Training

○ Today's Session

- Combination of CENTRA with a Conference Call
- Please mute your phone line
- *6 to mute & *7 to un-mute
- Do NOT put your phone on "hold"
- If you have a question, please click on the button that looks like a raised hand



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Instructors

- Larry Akins, SBSE Program Manager, St. Louis, MO
- Dana Duckworth, LB&I Technical Advisor, Wichita, KS
- Frank Bucci, LB&I Technical Advisor, Philadelphia, PA
- Dave Breen, SBSE Senior Counsel Attorney, Philadelphia, PA

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Objectives

1. Explain FBAR law and procedures for processing an FBAR penalty case file
2. Explain penalties applicable to Offshore Information returns
 - Form 5471
 - Form 8865
 - Form 3520/3520-A
3. Review of some Treaty Case Issues

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Treaty Case Training

FBAR
Treasury Form 90-22.1
**Report of Foreign Bank and
Financial Accounts**

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Report of Foreign Bank Accounts & Financial Accounts

Background

- Bank Secrecy Act (BSA) enacted in 1970
- Codified primarily in Title 31
- Responsibility delegated to the Financial Crimes Enforcement Network (FinCEN)
- Since April, 2003, the IRS has FBAR examination and enforcement authority under a delegation from FinCEN

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Report of Foreign Bank Accounts & Financial Accounts

Background

- o The Report of Foreign Bank and Financial Accounts, TD F 90-22.1, (FBAR), is required when a U.S. Person has a financial interest in or signature authority over one or more foreign financial accounts with an aggregate value greater than \$10,000

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Report of Foreign Bank Accounts & Financial Accounts

- o IRM 4.26.16 FBAR Law & Penalty Criteria (Rev 7.1.08)
- o IRM 4.26.17 Procedures for IRS Examinations (Rev 5.2.08)
- o CBRS Database - records of FBAR filings (check for both TPH & TPW) from the Detroit Computing Center (DCC)

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FBAR Filing Basics

Four Elements of FBAR Filing

- "United State Persons" must file if
- They have a financial interest or signature authority over
- A foreign financial account(s), and
- The aggregate value of the account(s) exceed \$10,000 at any time during the calendar year

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Factors Required for the filing of an FBAR

There must be:

A United States person

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Factors Required for the filing of an FBAR

United States Person for purposes of the
FBAR filing requirement is:

- A U.S. citizen (no matter where they
reside)
- A U.S. resident – IRC § 7701(b)
- A U.S. entity- any entity created or
organized in U.S. or under U.S. law
(partnership, corporation, limited
liability company, estate or trust)

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Factors Required for the filing of an FBAR

There must be:

A financial interest or
signature authority

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Factors Required for the filing of an FBAR

Financial Interest

- U.S. person has legal title to or is owner of record on an account even if the account is for the benefit of others including non-United States persons.
- If an account is maintained in the name of two persons jointly, or if several persons each own a partial interest in an account, each of those United States persons have a financial interest in that account.

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Factors Required for the filing of an FBAR

When the owner of record or holder of legal title on the account is:

- (1) a person acting as an agent, nominee, attorney, or in some other capacity on behalf of the U.S. person;
- (2) a corporation in which the United States person owns directly or indirectly more than 50 percent of the total value of shares of stock;
- (3) a partnership in which the United States person owns an interest in more than 50 percent of the profits (distributive share of income); or
- (4) a trust in which the United States person either has a present beneficial interest in more than 50 percent of the assets or from which such person receives more than 50 percent of the current income.

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Factors Required for the filing of an FBAR

Signature Authority

- Individual(s) can control disposition of account assets (can be in conjunction with another)
- By direct communication (oral or written)
- Signature Authority is not:
 - Supervisory approvals
 - Attributed to entities

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Factors Required for the filing of an FBAR

There must be:

A Foreign Financial Account

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Factors Required for the filing of an FBAR

Foreign

- Outside the "United States," which is:
 - States
 - D.C.
 - Territories and Possessions
 - Indian lands
- Physical location of the accounts governs

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Factors Required for the filing of an FBAR

Financial

- Both monetary and non-monetary assets
- Bank, brokerage, and investment accounts; insurance and annuity policy cash values; and mutual funds are specifically included
- Generally no real and personal property

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Factors Required for the filing of an FBAR

Account

- Relationship with financial institution or person acting as a financial institution
- Not assets directly held

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Factors Required for the filing of an FBAR

Aggregate Value Exceeds \$10,000

- Aggregate accounts with financial interest and those with signature authority
- Aggregate accounts owned directly and those owned indirectly
- Do not use family attribution of Title 26

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Factors Required for the filing of an FBAR

Reportable Accounts

- Bank accounts (checking, savings, CDs)
- Securities or brokerage accounts
- Other financial accounts
 - Other deposit accounts
 - Cash value of insurance or annuities
 - Commodity futures or option accounts
 - Mutual funds or similar pooled funds

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Factors Required for the filing of an FBAR

- The maximum value of an account is the largest amount of currency and non-monetary assets that appear on any quarterly or more frequent account statement issued for the applicable year.
- If periodic account statements are not so issued, the maximum account asset value is the largest amount of currency and non-monetary assets in the account at any time during the year.

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Factors Required for the filing of an FBAR

Note:

- It is not the final balance showing on the statement; it is the highest amount appearing on the statement - This amount may appear in the middle of the period.
- If U.S. person had a financial interest in more than one account, each account is to be valued separately. The maximum value of each account is determined and then all are added together to determine if the aggregate value exceeds \$10,000 (U.S.).

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Factors Required for the filing of an FBAR

Reportable Account Exceptions

- U.S. military banking facility
- Account of U.S. governmental entities
- International financial institutions
- Correspondent accounts
- Held in an IRA (if owner or beneficiary)
- Held in a tax-qualified retirement plan (if participant or beneficiary)
- Consolidated filing

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Factors Required for the filing of an FBAR

Custodial Accounts

- “Omnibus” foreign accounts held by U.S. banks or other financial institutions to hold investments of multiple persons
- If U.S. person can only access account through U.S. entity and cannot directly access the foreign account, no FBAR reporting is required

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Factors Required for the filing of an FBAR

Valuing Accounts for FBAR

- Each account valued separately at its highest value
- Periodic statements may be relied upon
- Value in local currency is converted to U.S. dollars at December 31st rate
- Aggregate all accounts
- Do not double-count for determining threshold

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Factors Required for the filing of an FBAR

Signature Authority Exceptions

- Officer or employee (no financial interest) of:
 - Bank examined by U.S. federal regulators
 - SEC or CFTC registered institutions
 - Authorized Service Provider (SEC registered)
 - U.S. listed entity (foreign or domestic)
 - A U.S. subsidiary of a U.S. listed entity
 - Entity registered under 12(g) of SEC

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Factors Required for the filing of an FBAR

Trust Beneficiary Exceptions

- Trust beneficiary does not need to file if trust, trustee or agent is a U.S. person and filed an FBAR disclosing the trust's foreign financial accounts
- Reportable beneficial interest does not include remainder interest
- Discretionary beneficial filing not required based on discretionary status

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Factors Required for the filing of an FBAR

Special Filing Rules

Spousal Filing

- Spouses allowed to file one combined FBAR if:
 - Second (non-filing) spouse has only joint accounts with first (filing) spouse
 - All joint accounts reported on single FBAR
 - Both spouses sign in item 44

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Factors Required for the filing of an FBAR

FBAR Record Keeping Requirements

- Account records must be maintained for five years
- Exception: officers or employees who file an FBAR because of signature authority over the foreign financial account of their employers are not expected to personally maintain the records of these foreign financial account

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FBAR Administrative Guidance

2010 Guidance

- Announcement 2010-16
 - Use 2000 definition of U.S. Person for 2009 & prior
- Notice 2010-23
 - Hedge funds and private equity funds excepted
 - Signature authority filing delayed until 2011 & Check Sch. B box "NO" for 2009

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FBAR Administrative Guidance

2011 Guidance

- Notice 2011-31
 - If filed before March 28, 2011, may reference then-existing guidance or no regulations and instructions
 - If filed after March 27, 2011, should refer to final regulations and revised instructions
- TD F 90-22.1, 3/2011 Revision

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FBAR Case Procedures



"FBAR Cases to Close"

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Report of Foreign Bank & Financial Accounts

Resources

- IRM 4.26.16 FBAR Law & Penalty Criteria (Rev 7.1.08)
- IRM 4.26.17 Procedures for IRS Examinations (Rev 5.5.08)
- FBAR Leadsheet - RGS

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Schedule B

Part III Foreign Accounts and Trusts

You must complete this part if you (a) had over \$1,500 of taxable interest or ordinary dividends; (b) had a foreign account; or (c) received a distribution from, or were a grantor of, or a transferor to, a foreign trust.

Yes No

7a At any time during 2010, 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

(See instructions on back.)

b If "Yes," enter the name of the foreign country ▶

8 During 2010, did you receive a distribution from, or were you the grantor of, or transferor to, a foreign trust? If "Yes," you may have to file Form 3520. See instructions on back

For Paperwork Reduction Act Notice, see your tax return instructions.

Cat. No. 17146N

Schedule B (Form 1040A or 1040) 2010

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Today

- Schedule B audit
- RA asks proudly if the taxpayer has any control or signature authority over a foreign bank account—hoping for a YES answer
- RA now knows BSA, FinCEN, DCC, FBAR, RSM, FMD, FMS, Code 545, 6 year statute, and a bunch of new letters to TP, L3709 & 3800 and forms TD F 90-22.1, 13448 and 13449

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Related Statute Memorandum (RSM)

- IRM 4.26.17.2 No interview or document request without approved RSM
- RSM is **Form 13535** (Rev. 10-04)
- Forward RSM thru group manager to TM
 - FBAR case file and brief memo describing facts should accompany RSM
- Separate RSM for EACH person (MFJ)
- TM will sign the RSM and return case file to examiner (TM makes determination)

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TM Determination Negative

- TM determines that the failure of the taxpayer to report or record the foreign financial account....*was not in furtherance of the tp's effort to conceal or underreport income*
- FBAR case is terminated
- Include RSM in Title 26 case file

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TM Determination Positive

- TM determines that apparent violations in FBAR case are in furtherance of apparent violations of Title 26 case
- Title 26 evidence can be used in FBAR case
- FBAR case continues.....
- And the *exam* begins

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FBAR Case Procedures

- Fax RSM to:
IRS-Detroit Computing Center
FAX (313) 234-2278
- DCC will enter RSM information on the FBAR database (No AIMS/ERCS)
- Original RSM and Fax transmittal are retained in the case file
- No AIMS/ERCS for FBAR case

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Examiner Procedures (cont'd)

- FBAR case file will include original RSM
- RA will download [Form 13526](#) FBAR Monitoring Document (FMD)
- FMD is to be updated as necessary and a copy forwarded to DCC for update
- FMD is eventually forwarded to DCC when case is closed from group (same address as RSM at DCC)

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FBAR Case File

- Activity Record-time charged to Activity Code 545
- RSM
- FBAR workpapers
- Brief summary memorandum explaining FBAR violation(s) if any
- Original delinquent FBAR(s) must be date stamped and annotated in red "Secured by Examination" @ top

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FBAR Case File (cont'd)

- Copy of delinquent FBAR(s) kept in case file
- Original delinquent FBAR(s) are mailed to:
 - IRS
 - CTR Operations
 - Edit & Error Resolution Mailroom
 - PO Box 32621
 - Detroit, MI 48232

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No FBAR Violation

- Complete summary memo and update FMD
- Close FBAR case to group manager
- Forward case to DCC on Form 3210
 - IRS
 - PO Box 33113
 - Detroit MI 48232-0113
- DCC will update FBAR database and maintain follow-up FBAR exam if needed

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FBAR Warning Letter

- No willful violation or negligence penalty
- Issue [Letter 3800](#) and copy to Filer
- Retain Copy of letter 3800 for case file
- Filer will return delinquent or corrected FBAR(s) if any and a copy of warning letter
- "Secured by Exam" on top of FBAR and include original and copy in case file

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FBAR Warning Letter (cont'd)

- Complete summary memo and FMD
- Close case to group manager
- Forward case to DCC on Form 3210
IRS-DCC
PO Box 33113,
Detroit MI 48232-0113
- DCC will update FBAR database and maintain follow-up FBAR exam if needed

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FBAR Penalty Asserted

- FBAR Penalties **must** be reviewed by SBSE Counsel prior to issuance to TP
- Counsel will render legal advice within 45 days
- Counsel will prepare written review
- Review will assist Appeals if case appealed
- Counsel may NOT recommend penalty

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FBAR Penalty

- Counsel written approval received
- Examiner issues
 - [Letter 3709](#) (30-day letter)
 - [Form 13449](#) (Agreement to Assess)
 - [Notice 1330](#) (Payments by check)
- TP has choice in 30-day letter
 - Agree & sign F 13449 or file protest

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TP Agrees to Assessment

Case file will include

- Delinquent FBAR(s) (original & copy)
- Signed & dated Form 13449
- Separate payment (if also Title 26 assessment) to US Treasury with FBAR account number and year on check
- Summary memo, workpapers, FMD

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Closed - Agreed Case

- Close case to group manager
- Forward case to DCC on Form 3210
IRS
PO Box 33113
Detroit, MI. 48232-0113
- DCC will update FBAR database and maintain follow-up FBAR exam if needed

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DCC Procedures Agreed Case

- Update FBAR database from FMD
- Determine FBAR follow-up examination
- Enter information on CBRS
- Complete [Form 13448](#) (internal use only)
- Issue Letter 3708 requesting payment (if necessary)
- Forward for collection to Federal Management System (FMS)

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Payment with Form 13449

- Copy the check (retain copy in case file)
- Copy Form 13449 and paper clip to check
- Forward by certified mail Form 3210 with the check and copy of 13449 to IRS
PO Box 33115 **NOTE:** Different PO Box
Detroit, MI. 48232-0115
- DCC will record and process payment

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TP Does Not Agree to Assessment

- Examiner wait 45 days to see if taxpayer will appeal as provided Letter 3709
- TP files complete protest
- Appeals requires 180 days on SOL
- Copy Title 26 information for FBAR file
- Forward case as provided previously to group manager
- Manager will forward FMD to DCC
- Manager will forward case to appeals (UIL 9999.99-01 Appeals Coordinated Issue Program)

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TP Failure to Respond to L 3709

- Examiner must wait 45 days
- Case closed to group manager
- Forward case to DCC on Form 3210
IRS
PO Box 33113
Detroit, MI. 48232-0113
- Penalty will be assessed and collection initiated as described for agreed case procedures

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FBAR Particulars

- SOL 31 USC 5321(b)(1)
 - 6 years from date of violation
 - date of violation is due date for FBAR (June 30th of following year)
 - special extension of SOL
 - 872 under Title 26 does not extend SOL for FBAR
- POA Form 2848 for Title 31 case acceptable after RSM determination

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FBAR Particulars (cont'd)

- Filed FBARs are entered on the CBRS database by the Detroit Computing Center

- IRP has limited FBAR data fields
 - Financial Institution & Country
 - Maximum Value in Account
 - Account Type

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FBAR Penalty

- 2004 American Jobs Creation Act raised the penalty ceiling for willful FBAR violations
- 31 USC 5321 amended
- New FBAR penalty mitigation guidelines were issued for post 10/22/04 violations

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FBAR Penalty Mitigating Factors

- The statutory penalty provides a ceiling on the FBAR Penalty
- The actual amount of the penalty is left to the discretion of the examiner
- the Service has adopted mitigation guidelines to promote consistency in exercising this discretion
- Examiners should apply these guidelines to calculate the penalty on each separate, unreported account

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FBAR Penalty Mitigating Factors (post 10/22/04)

- The examiner must make a determination with the written approval of the group manager
- To qualify for mitigation, 4 criteria must be met:
 1. No fraud penalty is assessed for year in question
 2. TP cooperated during examination
 3. No illegal source income
 4. TP has no history of criminal tax or BSA conviction for preceding 10 years and no FBAR assessments

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Degree of Fault by Your Taxpayer

The degree of fault is key in determining the applicable FBAR penalty.

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Degree of Fault by Your Taxpayer

Generally, there are two types of failures that apply to individuals:

1. Willful Violation
2. Non-Willful Violation

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Degree of Fault by Your Taxpayer

1. Willful Violation - A voluntary, intentional violation of a known legal duty

- Knowledge
- Intent

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Degree of Fault by Your Taxpayer

Documents to support Willfulness include:

- Evidence showing income related to the offshore funds wasn't reported
- Signed Form 1040 with Sch. B showing no acknowledgement of a foreign account.
- Statements of the Foreign Account
- Previously filed FBARs or FBARs with certain foreign accounts not claimed
- Interview notes with the TP/POA and/or Preparer about the foreign account

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Degree of Fault by Your Taxpayer

- 2. Non-willful Violation** - Generally the establishment of this penalty will turn on negligence and the taxpayer's knowledge of the FBAR filing requirements.

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FBAR Mitigation Penalties Post October 24, 2004

Non-Willful Penalty (Negligence)

- **Level I** Max Value \$50,000 in A/C
Penalty \$500/violation NTE \$5,000
- **Level II** Max Value \$250,000 in A/C
Penalty \$5,000/violation NTE 10% max
- **Level III** Value over \$250,000 in A/C
Penalty \$10,000/violation

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FBAR Mitigation Penalties Post October 24, 2004

Willfulness Penalty

- **Level I** Max Value \$50,000 in A/C
Penalty - Greater of \$1,000/violation
or 5% of maximum balance
- **Level II** Max Value \$250,000 in A/C
Penalty - Greater of \$5,000/violation
or 10% maximum balance

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FBAR Mitigation Penalties Post October 24, 2004

Willfulness Penalty

- **Level III** Max Value \$1,000,000
Penalty – Greater of 10% of maximum balance or 50% of closing balance
- **Level IV** Max Value Greater \$1,000,000
Penalty - Greater of \$100,000 or 50% of closing balance

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FBAR Mitigation Penalties Example 1

Facts – Non-Willful Mitigation Rules Apply

2 Accounts: Account #1 = \$15,000
Account #2 = \$5,000

Penalty Computation:

Level 1 Penalty = Aggregate Balance Less than
\$50,000, Penalty \$500 per account

Total FBAR Penalty = \$500 @ 2 =
\$1,000

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FBAR Mitigation Penalties Example 2

Facts – Non-Willful Mitigation Rules Apply

2 Accounts: Account #1 = \$150,000
Account #2 = \$3,000

Penalty Computation

Level 2 Penalty = Lessor of \$5,000 or 10% of maximum balance in account

Penalty = Account #1 = \$5,000
Account #2 = \$300 (10% x \$3,000)
Total FBAR Penalty = \$5,300

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FBAR Mitigation Penalties Example 3

Facts – Willful Mitigation Rules Apply

2 Accounts: Account #1 = \$35,000
Account #2 = \$3,000

Penalty Computation

Level 1 Penalty = Greater of \$1,000 or 5% of maximum balance in account

Penalty = Account #1 = \$1,750 (5% of \$35,000)
Account #2 = \$1,000
Total FBAR Penalty = \$2,750

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FBAR Mitigation Penalties Example 4

Facts – Willful Mitigation Rules Apply

1 Account: Account Balance 1,500,000

Penalty Computation

Level 4 Penalty = Greater of \$100,000 or
50% of closing balance in account

Total FBAR Penalty = \$750,000

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FBAR Summary

- Provides some leverage in offshore examinations
- RA should now know BSA, FinCEN, DCC, FBAR, RSM, FMD, FMS, Code 545, 6-year statute, and a bunch of new letters to TP L3709, 3800 and forms TD F 90-22.1, 13448 and 13449
- Remember that TM has responsibility for FBAR determination
- Additional help always available

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FBAR Help

- 31 USC § 5314
- 31 CFR Chapter X
- IRM 4.26.16 & 4.26.17
- Treaty Case SME
- Counsel Attorney

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Break

Please take a 10 minute break and be
back by

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Information Return Penalties



"Information Return Issues to Resolve"

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Objective

- To provide an overview of the information returns that may be required in certain offshore situations
- To provide the revenue agent with some of the tools necessary to ensure that applicable penalties are properly assessed

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TYPICAL ABUSIVE OFFSHORE STRUCTURE

What was filed

F1040

Individual – U S Person

F1065

LC/LLP

K-1

F1041

Domestic Trust
(Income-Distributions=Zero Profit)

K-1

F1040NR

Foreign Trust

International Business Corp
(IBC)

Bank Accts
& credit/debit cards

What should have been filed

F3520 – By U. S. persons who formed or funded (owner) or received a distribution (beneficiary) from a foreign trust.

F3520A – Annual return for foreign trust with U. S. owners.

F5471 - By U.S. owners of a CFC

TD 90-22.1 (FBAR)

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Purpose

- US Taxpayers are required to report their world-wide income
- International information returns provide information that the IRS has no other method of securing
- Returns are required for entities or events that the taxpayer "controls"

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Common Offshore Information Returns

- Forms 3520 & 3520-A Foreign Trust Information Returns
- Forms 5471 & 5472 Relationships with Foreign Corporations
- Form 8865 Relationships with Foreign Partnerships
- Form 926 Transfer of Property to a Foreign Corporation

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Form 3520

- U.S. person creates or transfers assets to a foreign trust
- U.S. person receives a distribution from a foreign trust
- Form 3520, *Annual Return to Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts*

IRC § 6048(a) and (c)

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Form 3520

- U.S. person receives a gift or bequest from a foreign person or entity
- Form 3520, *Annual Return to Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts*

IRC § 6039F

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IRC § 6677 Penalty

- If any return is not timely filed or
- Does not include all required information or
- Includes incorrect information
- The person required to file is subject to a penalty of 35% of the gross reportable amount (beginning in 2010, penalty is > of \$10,000 or 35% of gross reportable amount)
- If FTF continues penalty increases to \$10,000 for each 30-day period

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IRC § 6039F(c) Penalty

- US Person receives a gift or bequest from a foreign person or estate
- The person required to file is subject to a penalty of 5% (per month) of the gift (max 25%)
 - Plus tax consequences of gift determined by IRC § 6039F(c)(1)(A)

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Form 3520-A

- U.S. person treated as the “owner” of any portion of a foreign trust
- Form 3520-A, *Annual Information Return of Foreign Trust with a U.S. Owner*

IRC § 6048(b)

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IRC § 6677(b) Penalty

- If any return is not timely filed, or
- does not include all required information, or
- includes incorrect information;
- the person required to file is subject to a penalty of 5% of the gross reportable amount (beginning in 2010, penalty is > of \$10,000 or 5% of gross reportable amount)
- If FTF continues penalty increases to \$10,000 for each 30-day period

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Filing Verification

- Form 3520 is processed to BMF as MFT 68 under the TIN of the U.S. person who is responsible for filing the return
- Form 3520-A is processed to BMF as MFT 42 under the TIN of the foreign trust

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Form 5471

- U.S. person owns 10% of a foreign corporation (CFC)
- [Form 5471](#), *Information Return of U.S. Persons With Respect to Certain Foreign Corporations*

IRC § 6035, 6038, and 6046

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IRC § 6038(b) Penalty

- If any return is not timely filed, or
- does not include all required information, or
- includes incorrect information

- the person required to file is subject to a penalty of \$10,000 for each period

- If FTF continues penalty increases to \$10,000 for each 30-day period

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Form 5471 Penalty

- Reasonable Cause – Decision Tree
 - 21 page document to assist in the consistent response in assessment and abatement of the FTF Form 5471 penalty
- 5471 Leadsheet
- FTF Pattern Letter Exhibit 20.1.9-6

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Form 5472

- U.S. corporation is 25% or more “Foreign-owned.”
- Form 5472, Information Return of a 25% Foreign-Owned U.S. Corporation or a Foreign Corporation Engaged in a U.S. Trade or Business

IRC §§ 6038A and 6038C

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IRC § 6038A(d) Penalty

- If corporation fails to furnish any information or
- Fails to maintain required records
- Corp shall pay penalty of \$10,000 for each taxable year
- If FTF continues there is additional penalty of \$10,000 for each 30-day period
- FTF Pattern Letter IRM Exhibit 20.1.9-9

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Form 8865

- U.S. person owns 10% of a foreign partnership
- *Form 8865, Return of U.S. Persons With Respect to Certain Foreign Partnerships*

IRC §§ 6038, 6038B, and 6046A

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Form 8865 Penalty Depends on Filer

- IRC § 6038-US person who controlled foreign partnership-penalty \$10,000/yr
- IRC § 6038B-US person who contributed property to foreign partnership-penalty equal to 10% of FMV of property contribution (Sch O)
- IRC § 6046A-US person acquires, disposes or changes interest (10% or more)
 - penalty \$10,000/yr(Sch P)
- FTF Pattern Letter IRM Exhibit 20.1.9-7

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Form 926

- U.S. person transfers assets to a foreign corporation
- Form 926, Return by a U.S. Transferor of Property to a Foreign Corporation

IRC § 6038B

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IRC §6038B(c) Penalty

- If US person fails to furnish information timely, such person shall pay a penalty equal to 10% of the FMV of the property at the time of the exchange
- The penalty shall not exceed \$100,000 unless the failure was due to intentional disregard
- FTF Pattern letter IRM Exhibit 20.1.9-11

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Penalty Procedures Overview

- IRM 20.1.9 (Rev 4.22.11)
- LMSB International Penalty [website](#)
- Managerial Approval & International Exam referral (per area) (IRM 20.1.9.2(9))
- Penalties have reasonable cause exceptions
- Assessable Penalties – No agreement form

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Penalty Assessment

These penalties are assessed without regard to deficiency procedures, so...

Taxpayer's signature is NOT required

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Penalty Assessment

- Begin your Penalty assessment case by sending the appropriate Penalty Notice letter
- Notice letters should be addressed to the U.S. person responsible for filing the information return
- A notice letter is sent via Certified Mail and has specific language which gives the taxpayer:
 - 90 days to file the required returns or additional penalties will be assessed
 - The additional penalties are \$10,000 per month per return as limited by the maximum penalty
- Does not apply to F926 / F3520 foreign gifts

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Form 3520 & 3520-A Penalty/Notice Letters

- Letter 3804 – Opening notice letter
- Letter 3943 – Closing acceptance letter
- Letter 3944 – Closing no response letter
- Letter 3946 – Closing reasonable cause rejection letter

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Form 5471, 5472, 8865 & 926 Pattern Letters

- IRM 20.1.9 Exhibit 13
- Pattern Letters for F to F appropriate forms and schedules.

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Penalty Assessment

The assessment of these penalties requires the use of two forms...

Form 8278, Computation and Assessment of Miscellaneous Penalties

Form 886A, Explanation of Items

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Penalty Assessment

- IRM 20.1.9.2.1
- A separate penalty case (P-9) file is required for each year and each IRC section
- Form 5344, 870, 4549 or 4549-A is NOT used for a penalty case file
- Penalties are assessed to MFT 13 for entities and MFT 55 for individuals
- On Form 3198, indicate the PRN and penalty amount (per Form 8278)

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Penalty Assessment

- Prepare Form 5345 - the penalty case should be controlled on ERCS (there are no AIMS Controls)
 - Name & Address of the U.S. person (single individual or entity) responsible for filing the return
 - Activity Code 506 (the secretary will input the activity code and MFT P9 and SC 99 will be generated by ERCS)
 - Tracking Code - this is the only way to gather information that your penalty case is related to a project

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Penalty Assessment

- The case will appear on your 4502 with the name and TIN of the U.S. Person, MFT P9 and the tax year
- Charge time to this case as you would any other case
- If you have the related income tax case, post the time spent on the penalty determination to the penalty case

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Penalty Assessment

Power Of Attorney

- A separate Power of Attorney is needed for the penalty case file
- Power of Attorney should state "Miscellaneous Penalty under IRC § XXX"
- A Power of Attorney for the income tax case does not cover the penalty case

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Penalty Assessment

Reasonable Cause

- Requests for reasonable cause must be received in writing and under penalty of perjury
- Document your determination for allowance or disallowance of reasonable cause

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Reasonable Cause for FTF?

Ignorance of filing requirement:

- TPs may tell you they were unaware of the duty to file, so have reasonable cause.
- To have reasonable cause, the taxpayer must inquire of a tax professional, disclose all the relevant facts, and rely on the advice given.

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Penalty Assessment

- Appeal Rights
 - Penalties are not covered by Deficiency procedures of IRC § 6212
 - No 30 or 90 day letter
- Appeals currently provides a prepayment appeal process for all International Penalties
 - IRM Exhibit 20.1.9-17 has procedures and appropriate pattern letter

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Penalty Assessment

- Penalties are assessed on Form 8278 and Form 886-A with an explanation of items
- A separate 8278 for each tax year and IRC section for which a penalty assessment is made
- Penalties are assessed with a TC 240 with a penalty reference number for the specific penalty
- Appeal rights are included on the assessment notice

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Penalty Case File

- Form 3198 attached to the outside of the case file
- Inside the case file on the right side of the file (in order from top down):
 - Form 3645 - Computation of Penalty
 - Form 8278 - Assessment of Miscellaneous Penalty (for any penalty)
 - Contact Sheet
 - Statement of Reasonable Cause and determination
 - Copy of delinquent forms
 - Copy of Pattern Letters
 - Work papers / Correspondence
 - Transcript of MFT 13 or 55 (BMF or IMF)

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Penalty Assessment

- SBSE
Internal Revenue Service
201 West Rivercenter Blvd.
Covington, KY. 41011
Attn: Centralized Case Processing
Mail Stop 9413-G
- LMSB
IRS - Centralized Case Processing
Scowcroft Bldg
Mail Stop 4030
1973 North Rulon White Blvd
Ogden, UT 84404

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Information Returns Penalties

Summary

1. Information Returns are a way for IRS to identify transactions with offshore entities
2. Enforcement of these penalties is necessary for compliance
3. Reasonable cause applies to many of the penalties
4. Penalty assessment requires a separate case file

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Treaty Case Issues



"Treaty Case Issues to Resolve"

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Treaty Case Issues

1. Examination
2. Exam Procedures (including RSM)
3. Statutes
4. Technical Issues
5. Release of Bank Provided Data
6. SharePoint Treaty site

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Treaty Case Issues

Examination

- Pre-examination analysis (scope and depth, prep)
- Risk assessment (other accounts and/or offshore transactions)
- Strategy (communication, records request, timing of requested information, et al)
- Initial contact and IDR
- Initial Interview
- Information gathering phase
- Analysis phase
- Closing phase

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Treaty Case Issues

Examination Procedures

Applicable Guidance

- IRM, including
- Right's Notification
- Dual Notices
- Summons
- Innocent Spouse Provisions
- Etc.

Remember

- RSM must precede any request for and/or questions regarding the FBAR

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Treaty Case Issues

Statutes

- 2008 controlled/assigned, generally
- Records included for earlier periods
- Consider, develop and utilize exceptions to the 3-year statute within IRC § 6501(a)
- YY Alpha Code (IRM 25.6.23-3)
- Remember, FBAR statute is separate and unique

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Treaty Case Issues

Statutes

Exceptions to IRC § 6501(a);

- IRC § 6501(e): 25% omission, 6-yr statute
- IRC § 6501(c)(1)-(3): No return, false return, fraudulent return, no statute
- IRC § 6501(c)(8): FTF certain foreign transfers, statute open until provided plus 3 years (limited)
- FATCA: \$5000 unreported from a foreign account (generally), six year statute. Effective date (3/18/10) of statute governs applicability
 - See Centra 1 for additional details

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Treaty Case Issues

Technical Issues

- Income – Interest, Dividend and Capital Transactions.
- Fees – Miscellaneous Itemized Deduction
- Additions to the Account - pre v post tax
- Passive Foreign Income Company (PFIC)
- Foreign Tax Credit
- CFC – Subpart F Income
- Foreign Trusts and Other Related Entities
- Withholding
- Income Tax Penalties
- Foreign Information Returns (FBAR, Trusts, etc)
- Penalties – Foreign Information Returns
- Other

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Treaty Case Issues

Release of Bank Provided Data

- Source – treaty
- Content – contact log, decisions, communication, agreements, statements, etc
- Guidance – IRM 11.3.25.2(8); request in writing and to be coordinated with the Deputy Commissioner (Int'l) in advance of release.
- FOIA – Disclosure will coordinate with EOI and the Field Group. All responses will come from that office (IRM 11.3.13.7.8)
- Any update – SME calls

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Treaty Case Issues

SharePoint

- OVDI SharePoint Site --
<http://wsep.ds.irsnet.gov/sites/co/dcse/sbse/specialty/io/liechtenstein/UBS/default.aspx>
- Program related source of information
- Awareness

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Treaty Case CENTRA Training

Questions?

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Treaty Case CENTRA Training

This concludes the planned training

As unique issues present themselves,
resources are available. Start with
your GM and SME

As events occur, topics warranting
further communication will be
identified and share

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Treaty Case CENTRA Training

Thank you for your active
participation

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