

U.S. Tax Compliance

Not filing U.S. tax forms serious for Americans in Canada

By **Veronika Chang**

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(May 10, 2019, 8:24 AM EDT) -- It's been nine years since the *Foreign Account Tax Compliance Act (FATCA)* was passed in the United States, and almost five since the U.S. and Canada entered into an intergovernmental agreement to share tax-related information. Americans who live in Canada should know now that they are required to file a U.S. tax return and other information returns annually.

The most common information return a U.S. citizen or permanent resident must file annually is the FBAR — Report of Foreign Bank and Financial Accounts. Under the U.S. *Bank Secrecy Act*, which fights money laundering, American citizens and residents must file an FBAR. They must do so if they: a) own or have signature authority over one or more financial accounts outside of the U.S., and b) if the aggregate value of all their foreign financial accounts exceeds US\$10,000 at any time during the

year.

The FBAR is an annual report and must be filed electronically through the Financial Crimes Enforcement Network by Oct. 15. The due date is actually April 15 following the calendar year being reported, but there is an automatic six-month extension.

The FBAR is not a complicated form. You simply provide the identifying information of your financial accounts, along with the maximum value of the accounts during the year. Unlike other U.S. information returns (such as Form 8621 with which you report your Canadian mutual funds), there is no complex math formula required. However, this simple form does carry a big penalty.

Currently, a "non-willful violation" carries a maximum penalty of US\$12,921 (\$10,000 adjusted for inflation), while a "willful violation" is much more. For FBAR purposes willful violation is an intentional violation of a known legal duty and carries a penalty of US\$129,210 (\$100,000 adjusted for inflation), or 50 per cent of the total amount in the foreign accounts, whichever is greater. If the violation rises to the level of criminal violation, penalties can be up to US\$250,000 and/or up to five years of imprisonment.

The FBAR penalty is harsh when compared to the Canadian equivalent, which is Form T1135 — Foreign Income Verification Statement. With Form 1135, failure to file carries a minimum penalty of \$100 and \$25 per day to a maximum of \$2,500. For failure to file knowingly, or under circumstances amounting to gross negligence, the penalty increases to \$500 per month up to a maximum of \$12,000, less other penalties already levied. Additional penalties may be assessed, but Canadian penalties are bearable compared to the FBAR penalty.

And the FBAR penalties may get worse. So far, FBAR penalties have been applied on an annual basis. So, if you missed five years of FBAR, your potential FBAR penalties would have been \$50,000 (ignoring the inflation adjustment). But in April 2019, two court cases in California changed the math. In these cases, U.S. District Court ruled that FBAR penalties are to be applied on a per-account basis. Thus, if you have five foreign accounts, then your potential FBAR penalty exposure is now increased to \$50,000 per year *times* the number of years you missed filing those FBARS.

In both these cases, a U.S. citizen had foreign bank accounts with collective balances in excess of

\$10,000. Both taxpayers participated in the IRS Offshore Voluntary Disclosure Program, but one taxpayer was removed from the program for undisclosed reasons and the other decided to opt out entirely. The IRS then assessed FBAR penalties of \$10,000 for each of the foreign accounts that the taxpayers owned and failed to disclose on the FBAR.

In both cases, the court upheld the IRS position that the \$10,000 FBAR penalty applies to *each* non-willful violation, and a single, undisclosed, foreign financial account equals an FBAR violation. In one of the cases, the judgment entered for the IRS was a default judgment (for some reason the defendant chose not to defend), so the court did not discuss the merits of the case. But the outcome for both cases was the same. No matter how you look at it, this was a huge win for the government.

The long-standing belief of tax professionals is that the FBAR penalty cannot exceed \$10,000, regardless of the number of foreign bank accounts which should have been reported on the FBAR. But this is no longer true. The above two cases were decided in the U.S. District Courts, so there is a possibility that another equal or higher court may decide differently. Until then, however, the exposure for the potential FBAR penalty is significant.

Moral of the story? Americans who are not up to date on their FBAR filing requirements should file them as soon as possible. In September 2018, the IRS closed the Offshore Voluntary Disclosure Program, but you may be able to participate in another IRS program to resolve FBAR non-compliance and keep those penalties to a minimum. But you should still file.

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