



## US TAX ALERT

**US TAX ALERT** is a commentary on topics of current interest – usually topics relating to recent changes in tax law, new IRS administrative practices or current interpretations arising from tax cases. *Professional advice should be obtained before acting on any of this information.* ed.08/11

### AMERICANS LIVING IN CANADA NOT FILING FBAR RETURNS IS A SERIOUS MATTER

The US Annual Report of Foreign Bank and Financial Accounts (FBAR returns) is reported on form TDF 90-22.1. It must be filed by United States *persons* which includes individuals who are US citizens, green card holders or US residents and may include others. The information reported on the form is recorded on the database of the United States Financial Crime Enforcement Network to counteract terrorism, money laundering and tax avoidance. ***Filing is required by a US person who has a financial interest in or signature authority over foreign (non US) financial accounts.***

The reporting in this memo is more extensive than normal given the many intricate provisions of the legislation and the very serious penalties for failure to file or complete correctly. Consequently, much of the instructions for the FBAR return are reported verbatim.

#### Requirement to File

*If the aggregate of the maximum account values exceeds \$10,000, an FBAR must be filed. An FBAR is not required to be filed if the person did not have \$10,000 of aggregate value in foreign financial accounts at any time during the calendar year.*

*For United States persons with a financial interest in or signature authority over fewer than 25 accounts that are unable to determine if the aggregate maximum account values of the accounts exceeded \$10,000 at any time during the calendar year.....enter “value unknown” in Item 15.*

#### Penalties

The FBAR return is due June 30 each year and no filing extension is allowed. The penalties for non – wilful violation are up to US \$10,000 and for wilful violation the greater of \$10,000 or 50% of the balance in the accounts at the time of the offence. Criminal penalties can also be assessed. The penalties section of the FBAR instructions reads in part as follows:

*A person who is required to file an FBAR and fails to properly file may be subject to a civil penalty not to exceed \$10,000. **If there is reasonable cause for the failure and the balance in the account is properly reported, no penalty will be imposed.***

For those who have not filed FBAR returns for past years 1) an explanation for the delinquent returns such as the taxpayer had no knowledge of the FBAR reporting requirement (if that is the case) and 2) all income from these financial accounts was reported on tax returns will probably avoid penalties.

## Voluntary Disclosure

The bottom line is that US tax authorities will eventually find you out if you have not been filing US returns. It is far better to voluntarily disclose now and avoid or minimize fines and penalties. The closer we get to 2013 (when Canadian financial institutions must start reporting tax information to the IRS) the higher the stakes get so put your house in order now.

The United States has had a few US amnesty programs available recently – the most recent expiring on August 31, 2011. They are primarily designed for individuals intentionally committing tax evasion. On the other hand, individuals who have not been complying with US tax laws because of ignorance or neglect have usually been able to file past due returns as a voluntary disclosure. This generally results in no penalties providing the disclosure is truthful, timely and complete. Six years of returns is the standard disclosure period for tax returns but the current amnesty requires eight years of FBAR returns. We have helped several taxpayers with their filings and none have been penalized.

## Determining Maximum Account Values

The instructions to the TDF 90-22.1 form are very helpful in this regard.

*The maximum value of an account is a reasonable approximation of the greatest value of currency or non monetary assets in the account during the calendar year. Periodic account statements may be relied on to determine the maximum value of the account, provided that the statements fairly reflect the maximum account value during the calendar year. If the filer had a financial interest in more than one account, each account must be valued separately.*

*In the case of non-United States currency, convert the maximum account value for each account into United States dollars.*

## US Person, Joint Accounts and Spouses

The instructions for the FBAR return indicate that the following persons must file:

*A United States person that has a financial interest in or signature authority over foreign financial accounts must file an FBAR if the aggregate value of the foreign financial accounts exceeds \$10,000 at any time during the calendar year.*

A United States person is defined as follows:

*United States citizens; United states residents; entities, including but not limited to, corporations, partnerships, or limited liability companies created or organized in the United States or under the laws of the United States; and trusts or estates formed under the laws of the United States.*

If a US Citizen living in Canada and married to a Canadian and is a joint owner of their spouse's investments and/or bank accounts, they must report these account interests– even if they don't have enough income to file a US personal tax return. With respect to spouses, the FBAR instructions state the following:

*The spouse of an individual who files an FBAR is not required to file a separate FBAR if the following conditions are met: 1) all the financial accounts that the non-filing spouse is required to report are jointly owned with the filing spouse; 2) the filing spouse reports the jointly owned accounts on a timely filed FBAR; and 3) both spouses sign the FBAR. Otherwise, both spouses are required to file separate FBARs, and each spouse must report the entire value of the jointly owned accounts.*

## Financial Accounts in a Foreign Country

The meaning of a *financial account* in a foreign country includes all accounts in geographical areas outside the United States. The definition of an *account* is as follows:

*A financial account includes, but is not limited to, a securities, brokerage, savings, demand, checking, deposit, time deposit, or other account maintained with a financial institution (or other person performing the services of a financial institution). A financial account also includes a commodity futures or options account, and insurance policy with a cash value (such as a whole life insurance policy), and annuity policy with a cash value, and shares in a mutual fund or similar pooled fund (i.e., a fund that is available to the general public with a regular net asset value determination and regular redemptions).*

*A Foreign financial account is a financial account located outside of the United States. For example, an account maintained with a branch of a United States bank that is physically located outside of the United States is a foreign financial account. An account maintained with a branch of a foreign bank that is physically located in the United States is not a foreign financial account.*

A financial account would include RRSP's, RESP's, RRIF's, RDSPs, TFSA's and insurance policies with a cash surrender value (to be reported by the policy holder not the beneficiary).

## Financial Interest or Signature Authority over an Account

What is so frightening about this legislation is how far it reaches. It not only covers ownership and joint ownership of accounts but also includes accounts where you simply have signing authority (say you are treasurer of a local charity, hold a power of attorney or are an executor of an estate).

The instructions to the FBAR return indicate that a United States person has a financial interest in a foreign financial account when certain conditions exist:

*United States person has a financial interest in a foreign financial account for which:*

- 1. The United States person is the owner of record or holder of legal title, regardless of whether the account is maintained for the benefit of the United States person or for the benefit of another person; or*
- 2. The owner of record or holder of legal titles is one of the following:*
  - a. An agent, nominee, attorney, or a person acting in some other capacity on behalf of the United States person with respect to the account;*
  - b. The corporation in which the United States person owns directly or indirectly (i) more than 50 percent of the total value of shares of stock or (ii) more than 50 percent of the voting power of all shares of stock;*
  - c. A partnership in which the United States person owns directly or indirectly: (i) and interest in more than 50 percent of the partnerships' profits (e.g., distributive share of partnership income taking into account any special allocation agreement) or (ii) an interest in more than 50 percent of the partnership capital;*
  - d. A trust of which the United States person: (i) is the trust grantor and (ii) has an ownership interest in the trust for United States federal tax purposes;*
  - e. A trust in which the United States person has a greater than 50 percent present beneficial interest in the assets or income of the trust for the calendar year; or*
  - f. Any other entity in which the United States person owns directly or indirectly more than 50 percent of the voting power, total value of equity interest or assets, or interest in profits.*

You have a signature authority over an account if you meet the following test:

*Signature authority is the authority of an individual (alone or in conjunction with another individual) to control the disposition of assets held in a foreign financial account by direct communication (whether in writing or otherwise) to the bank or other financial institution that maintains the financial account.*

It is obvious that any account for which you are acting as a trustee or hold a power of attorney would be included.

## Filing Deadline

Filing deadline details are as follows:

*The FBAR is an annual report and must be received by the Department of the Treasury on or before June 30<sup>th</sup> of the year following the calendar year being reported.*

*The FBAR may be hand delivered to any local office of the Internal Revenue Service for forwarding to the department of the treasury, Detroit, MI. The FBAR may also be delivered to the Internal Revenue Service's tax attaches located in United States embassies and consulates for forwarding to the Department of the Treasury. **The FBAR is not considered filed until it is received by the Department of the Treasury in Detroit, MI.***

***There is no extension of time available for filing and FBAR. Extensions of time to file federal tax returns do not extend the time for filing and FBAR.** If a delinquent FBAR is filed, attach a statement explaining the reason for the late filing as noted above.*

## Record Keeping

*Persons required to file an FBAR must retain records that contain the name in which each account is maintained, the number or other designation of the account, the name and address of the foreign financial institution that maintains the account, the type of account, and the maximum account value of each account during the reporting period. The records must be retained for a period of 5 years from June 30<sup>th</sup> of the year following the calendar year reported and must be available for inspection as provided by law. **Retaining a copy of the filed FBAR can help to satisfy the record keeping requirements.***

## Information to Report on FBAR Return

Until 2008 you simply had to report the maximum value of accounts within a range. Starting in 2009 you have to report the actual maximum value. The following information is required for *each* account:

- ◆ Maximum value in the year
- ◆ Type of account (bank, securities, other)
- ◆ Name of financial institution
- ◆ Account number
- ◆ Mailing address of institution

## Reporting Categories

The FBAR return has a series of schedules requiring details of each account in each of the following categories:

- ◆ Part II – Accounts owned separately
- ◆ Part III – Accounts owned jointly
- ◆ Part IV – Accounts where the filer has signature or other authorization but no financial interest
- ◆ Part V –Accounts where filer is filing a consolidated report.

In most cases only Parts II, III and perhaps IV will apply.

### Summing Up

US vigilance has been stepped up substantially at US borders by the IRS, by US Immigration and by Homeland Security. The IRS and CRA also exchange information. Your Canadian passport shows your place of birth and that may get you an invite at the border for a little chat in a small room with steel chairs and no pictures on the wall – not a pleasant experience – especially if your US filings are delinquent.

The onerous penalties should be compelling to make US *persons* file the FBAR return. Penalties apply if the return is not filed either for non-wilful or wilful reasons. Many US individuals living in Canada treat far too lightly the fact that they are not filing their US 1040 personal income tax returns or the FBAR return. Actually, US citizens in Canada have to file a number of returns with the IRS whether or not they have taxable income. Carelessness about not filing the FBAR return could be a very serious and costly oversight.

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