

When Noncompliance With FATCA Is More Than a Civil Tax Matter

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In this article, Brown examines the government's use of 18 U.S.C. section 371 to charge related criminal violations under the Foreign Account Tax Compliance Act.

Following on the heels of the Justice Department's expanded use of the federal statutory reporting obligations that require some U.S. persons to disclose their offshore bank accounts by filing annual reports of foreign bank and financial accounts, the government has a new foreign bank account reporting tool at its disposal. That reporting tool is the Foreign Account Tax Compliance Act. FATCA is part of the Internal Revenue Code, unlike the FBAR obligations, which are found under Title 31¹ as part of the Bank Secrecy Act.²

Although Congress did not provide for separate criminal penalties for a violation of FATCA, that has not presented an insurmountable obstacle to criminal prosecution of violations of FATCA. To the contrary, by all indications, FATCA, like the FBAR, looks like a tool the government intends to use not only in its civil enforcement of offshore tax compliance, but also in prosecuting those who intentionally violate those laws.

FATCA Civil Reporting Obligations

FATCA, enacted under the Hiring Incentives to Restore Employment (HIRE) Act of 2010,³ created a new withholding regime designed to expand reporting on foreign accounts owned by some U.S. persons as well as disclosure of U.S. owners of some foreign entities. FATCA also requires individuals and specific domestic entities to report ownership of financial accounts, foreign interests, foreign stocks and securities, contracts held for investment, and financial instruments with non-U.S. issuers or counterparties.

FATCA contains information reporting requirements both for U.S. persons and for foreign financial institutions.

The reporting requirements for those defined as a U.S. person are triggered by any interest in a "specified foreign financial asset" if the value of the assets exceeds \$50,000, unless the persons or entities are not required to file an income tax return for the year at issue.⁴ A specified foreign financial asset includes: assets held in a trust and where the individual is the owner of the trust under sections 671 through 679; assets held by disregarded entities owned by the individual or specific domestic entities, stock or securities issued by a non-U.S. person; financial instruments or contracts held for investment with a non-U.S. issuer or counterparty; and any interest in a foreign entity. The U.S. person must file Form 8938, "Statement of Foreign Financial Assets," which requires that any distributions, income, or gross proceeds attributable to holding or disposing of the asset be reported by the individual on an income tax return. Assets must

¹ 31 U.S.C. sections 5311 and 5322; and 31 C.F.R. section 1010.350(b).

² Sections 1471-1474.

³ P.L. 111-147.

⁴ Section 6038D.

be reported even if no income or distributions are made during the tax year. The civil penalty for failure to file Form 8938 is \$10,000, subject to a reasonable cause exception. The \$10,000 penalty applies if Form 8938 is not filed within 90 days after the IRS mails notice of the failure to file the form. There is an additional \$10,000 penalty imposed for each 30-day period the failure continues, up to a maximum penalty of \$50,000. There is no statute of limitations if the Form 8938 has not been filed.

The FATCA requirements for foreign financial institutions are slightly different. FATCA imposes a withholding requirement on an FFI⁵ that holds accounts for U.S. account holders. The withholding agents⁶ for the FFI must deduct and withhold 30 percent of the withholdable payments⁷ for the FFI's U.S. account holders⁸ unless it agrees to apply verification and due diligence procedures to identify U.S. account holders and annually report to Treasury information including names, addresses, taxpayer identification numbers, account numbers, and account balances or values, and continue withholding 30 percent tax on any payments for uncooperative account holders or nonparticipant FFIs. Also, under its broad regulatory authority, the IRS can exclude some FFIs from entering agreements or withholding.⁹

Criminalizing FATCA Violations

While Congress did not expressly set forth criminal penalties for violations of FATCA, there is no bar to the government's use of 18 U.S.C. section 371, given the appropriate evidence, to charge a FATCA-related conspiracy. That is exactly what the government has done, and notably did so within 60 days after the FATCA withholding obligations became effective.

⁵ An FFI is any financial institution that is a foreign entity, but excludes any financial institution organized under the laws of any U.S. possession. Section 1471(d)(4).

⁶ A withholding agent includes any person in whatever capacity having control, receipt, custody, disposal, or payment of any withholdable payment. Section 1473(4).

⁷ Withholdable payments are any payments of interest, dividends, rents, salaries, wages or other fixed or determinable annual periodic gains or income from sources within the United States. Section 1473(1)(A).

⁸ Sections 1471(a) and 1472(a).

⁹ Section 1471(b)(1).

On September 9, 2014, Robert Bandfield was charged, along with five other individuals and six corporations, in three interrelated schemes.¹⁰ The indictment alleged a conspiracy to aid U.S. clients in circumventing the IRS's reporting requirements under FATCA.

On July 31, 2015, a superseding indictment was returned by the grand jury adding two more defendants, including Gregg R. Mulholland, a client of Bandfield's.¹¹ The superseding indictment alleged that the defendants enabled U.S. clients to evade reporting requirements to the IRS by concealing the proceeds generated by the manipulated stock transactions through the shell companies and their nominees. The superseding indictment revealed the government's use of undercover agents and wiretaps to record numerous conversations involving the defendants in its investigation. According to the allegations surrounding a recorded conversation with an undercover agent, Bandfield bragged about their strategy to enable clients to specifically evade FATCA's requirements, describing it as a "slick" structure designed to counter President Obama's new laws — a reference to FATCA.¹²

In May 2016 Bandfield pleaded guilty to money laundering conspiracy regarding his role as the architect of the offshore fraud haven scheme. Mulholland pleaded guilty to money laundering conspiracy for his role as the orchestrator of more than 40 pump-and-dump schemes.¹³ While neither defendant was convicted of the FATCA conspiracy, Bandfield received a sentence of six years and Mulholland received a sentence of 12 years in prison for their criminal conduct. Presented to the court were facts about the defendants' schemes to circumvent the

¹⁰ FBI, "Six Corporate Executives and Six Corporate Entities Indicted for Orchestrating a \$500 Million Offshore Asset Protection, Securities Fraud, and Money Laundering Scheme" (Sept. 9, 2014).

¹¹ *United States v. Banfield*, 1:14-cr-00476-ILG (E.D.N.Y. 2015) (superseding indictment).

¹² *Id.*

¹³ United States Attorney's Office, Eastern District of New York, "Architect of Offshore Fraud Haven and Orchestrator of More Than 40 Pump and Dump Schemes Sentenced to 6 and 12 Years in Prison, Respectively, for Executing a \$250 Million Money Laundering Scheme" (Feb. 6, 2017).

payment of capital gains taxes and the IRS's reporting requirements under FATCA.¹⁴

Following the successful prosecution of Bandfield, on September 11 the Justice Department announced the first conviction under FATCA.¹⁵ This conviction came through a plea agreement entered into between Adrian Baron, who is a citizen of the United Kingdom and a former executive of Loyal Bank Ltd., which has offices in Budapest, Hungary, and St. Vincent and the Grenadines.

Based on information set forth in a superseding indictment,¹⁶ Baron conspired with an undercover federal agent, identified as a U.S. citizen, in opening foreign bank accounts in a manner intended to disguise the true owner of the accounts, with a stated goal of circumventing the obligations to report those accounts to the IRS under FATCA. In furtherance of that conspiracy, Baron was alleged to have aided in opening nominee bank accounts at Loyal Bank and in providing the undercover agent with debit cards that were linked to the accounts to enable the undercover agent's use of about \$95,000, which was deposited in the newly created foreign nominee bank accounts. According to the superseding indictment, Baron fully understood that a U.S. citizen was the true beneficial owner of the foreign accounts he had helped set up. Baron was also alleged to have been fully aware that this U.S. account holder's goal was to open and maintain the foreign accounts in a way that circumvented FATCA reporting requirements. At no time did either Baron or Loyal Bank request or collect FATCA information from the U.S. account holder.

Baron's agreement to conspire and his acts in furtherance of the conspiracy, almost all of which appear to have been recorded during the undercover sting operation, led to him pleading guilty to conspiring to defraud the United States in violation of 18 U.S.C. section 371, based on his intended failure to comply with FATCA.¹⁷

Conclusion

In addition to the government's use of 18 U.S.C. section 371 to charge FATCA-related criminal violations in those cases, we can expect to see the government pursue criminal FATCA violations under the IRC. Such changes may include intentional violations involving a U.S. account holder's filing of a false Form 8938 as an affirmative act under section 7201 — a felony — or the willful failure to file Form 8938 under section 7203 — a misdemeanor. In light of a recent announcement by the IRS Criminal Investigation division that it is hiring an additional 250 special agents — a more than 10 percent increase in investigative manpower — we can definitely expect to see more criminal FATCA prosecutions. ■

¹⁴ *Id.*

¹⁵ United States Attorney's Office, Eastern District of New York, "Former Executive of Loyal Bank Ltd Pleads Guilty to Conspiring to Defraud the United States by Failing to Comply With Foreign Account Tax Compliance Act (FATCA)" (Sept. 1, 2018).

¹⁶ *United States v. Kyriacou*, 1:18-cr-00102-KAM (E.D.N.Y. 2018).

¹⁷ *Id.*