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Storing Gold Offshore: What Your Clients Need To Know

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The federal government has recently increased its efforts to curb nondisclosure of offshore assets and underreported income by U.S. taxpayers. The Foreign Account Tax Compliance Act (FATCA), enacted in 2010 as part of the Hiring Incentives to Restore Employment Act (HIRE), imposes new reporting requirements on U.S. taxpayers and foreign financial institutions to identify U.S. persons who have invested in non-U.S. financial accounts or non-U.S. entities.

Tax compliance has risen to the top of federal law-enforcement agendas, and with widely publicized alerts from the Internal Revenue Service (IRS), claims of ignorance of the law are likely to fall on deaf ears. However, not all foreign assets owned by U.S. taxpayers are required to be disclosed to the IRS. This article provides guidance on tax compliance for U.S. taxpayers who store gold abroad — an increasingly attractive investment given an uncertain global economy and the sharp decline in currency values.

Prior to the enactment of FATCA, the primary method for U.S. taxpayers to report foreign financial assets was by checking a box on Form 1040, Schedule B and completing Form TD F 90-22.1, Report of Foreign Bank and Financial Accounts (FBAR). The FBAR, with an annual June 30th filing deadline, requires U.S. persons to disclose each foreign financial account for which they have signature authority or a financial interest, if the aggregate value of the foreign financial accounts exceeds $10,000 at any time during the year in question. In addition, if those foreign financial assets are owned by foreign entities such as corporations, U.S. persons who are officers, directors, or shareholders may also be required to file forms and schedules with the IRS (e.g., Form 5471 is used to satisfy the reporting requirements of IRC Sections 6038 and 6046 and the related regulations).

According to the Treasury Regulation 31 C.F.R. § 1010.350, a "financial account" includes securities, brokerage, savings, demand, checking, deposit, time-deposit or other accounts *maintained* with a person engaged in banking. On Feb. 24, the regulations expanded the term "other financial accounts" to clarify that it includes commodities, futures or options accounts, insurance policies with cash value, and mutual funds or similar pooled funds that issue shares available to the general public and that have a regular net asset value determination and regular redemptions. Financial accounts also include an account with a person that is in the business of accepting deposits as a financial agency or a person who acts as a broker or dealer for futures or option transactions in any commodity or is subject to the rules of a commodity exchange or association. The regulations define a foreign financial account as a financial account located outside the U.S.

The Treasury Regulations do not specify whether a U.S. person must report gold on an FBAR where it is stored abroad in a safe-deposit box at a foreign financial institution. An IRS-published list of frequently asked questions (FAQs) includes whether an FBAR is required for accounts maintained with financial institutions located in a foreign country if the accounts hold noncash assets, such as gold. The IRS responds affirmatively, stating that an account with a financial institution that is located in a foreign country is a financial account for FBAR purposes, whether the account holds cash or nonmonetary assets. See http://www.irs.gov/businesses/small/article/0,,id=210249,00.html (last accessed Aug. 28, 2011).

This FAQ answer, however, assumes that the asset is being maintained in a financial account with a foreign financial institution. What is not addressed is

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whether a safe-deposit box (or something comparable) stored at a foreign financial institution qualifies as a "financial account" for FBAR purposes. If an offshore asset is not being maintained in a financial account, a U.S. person would not be required to disclose the existence of those assets even if the aggregate value exceeds $10,000.

The question is whether an FBAR is required to be filed when a U.S. taxpayer stores gold in a safe-deposit box at a foreign financial institution. The answer depends upon whether a safe-deposit box qualifies as a financial account maintained by a foreign financial institution under the Treasury Regulations. This analysis begins with determining whether a safe-deposit box is a "financial account." The regulations do not specify whether a safe-deposit box is a financial account. The regulations state, however, that a financial account must be maintained by the foreign financial institution. 31 C.F.R. § 1010.350. Therefore, even if a safe-deposit box qualifies as a financial account, to trigger a reporting requirement, it must be maintained by the foreign financial institution. This necessitates an examination of the relationship between the owner of the safe-deposit box and the foreign financial institution.

If the safe-deposit box is maintained by a foreign financial institution, the institution must be able to exercise control over the contents of the box, such as having the authority to access and make deposits and/or withdrawals. In a case where unrestricted access is granted by the owner to the foreign financial institution, it would indicate that the safe-deposit box is a financial account and an FBAR is required if the gold exceeds the reporting threshold. This analysis is consistent with the IRS' position expressed at a teleconference sponsored by the ABA Section of International Law's Committee on International Taxation, albeit prior to the revised Treasury Regulations. "Foreign Bank Account Reports: Getting it Straight before the June 30 Deadline!" teleconference June 12, 2009, http://www.ruchelaw.com/pdfs/ FBAR%20Insights.pdf.

On the other hand, where the owner maintains exclusive control over the safe-deposit box and does not give the foreign financial institution access, it appears that reporting gold on an FBAR stored in a safe-deposit box is not required regardless of its value. *Id*. This relationship between the owner and the financial institution, which is analogous to a bailment contract under the common law, is distinguishable from maintaining a financial account with a person engaged in banking or in the business of accepting deposits as a financial agency. Likewise, if gold is stored in a private vault overseas, the vault itself and the company operating the vault would likely not be deemed a financial account *maintained* with a person engaged in banking or in the business of accepting deposits as a financial agency. 31 CFR 1010.350. Therefore, in either of these instances where the owner has exclusive access to the gold being stored, it would not appear that he/she would be required to file an FBAR.

Under FATCA, similar to the FBAR filing requirements, U.S. persons holding "specified foreign financial assets" outside the U.S. must report those assets to the IRS. A "specified foreign financial asset" is defined to include any financial account *maintained* by a foreign financial institution. A "financial account" defined by IRC Section 1471(d)(2) includes any depository or custodial account *maintained* by a financial institution. Thus, the definition of a financial account under FATCA is similar to the Treasury Regulations for FBAR filing requirements.

Form 8938, Statement of Specified Foreign Financial Assets, requires additional disclosures. A draft version of this form has been released by the IRS, with a draft version of the instructions released shortly thereafter. Finalized versions of the form and its instructions have yet to be issued. IRC Section 6038D requires the disclosure of foreign assets other than foreign financial accounts. Summary of Key FATCA Provisions, http://www.irs.gov/businesses/corporations/article/0,,id=236664,00.html (last accessed Aug. 28, 2011). Notice 2011-55 provides that the IRS suspended the IRC Section 6038D reporting requirements until it releases a final Form 8938. After the final Form 8938 is released, individuals for whom the filing of that form was suspended for a tax year will have to attach the form for the suspended tax year to their next income-tax return required to be filed with the IRS.

Reporting requirements under FATCA are imposed only upon holding qualifying assets with an aggregated value exceeding $50,000. IRC Section 6038D. The HIRE Act's reporting requirement must be fulfilled in addition to the current FBAR reporting requirements, and U.S. taxpayers risk penalties for failure to comply.

Although FATCA creates new compliance obligations for U.S. taxpayers, does it require U.S. taxpayers to report gold stored in an offshore safe-deposit box where the owner has exclusive access? As with the FBAR filing requirements, under FATCA (with the limited exceptions discussed above) a reportable financial accounts is an account *maintained* with a foreign financial institution. Similar to the FBAR requirements, assets stored in a safe-deposit box in a foreign financial institution, which does not exercise control nor has access to the contents, does not appear to meet the requirements of a financial account under FATCA. It should be noted, however, that even if gold is not required to be reported on an FBAR or Form 8938, if it is owned by a corporation, partnership or trust, there may be other information returns required by the IRS. Noncompliance for failing to file information returns related to a foreign corporation, partnership or trust carries its own penalties, which may be equally or more severe than failing to comply with the FBAR or Form 8938 requirements.

In an effort to give U.S. taxpayers an opportunity to remedy past delinquencies related to prior nondisclosure of offshore assets and undeclared income, the IRS has offered two amnesty programs during the past two-and-a-half years. (FAQs Regarding 2011 Offshore Voluntary Disclosure Initiative (OVDI), http://www.irs.gov/businesses/international/article/0,,id=235699,00.html, last visited July 12, 2011.) While the most recent amnesty program, the 2011 OVDI, expired on Sept. 9, there are still options for taxpayers who desire to come clean before the IRS detects noncompliance and imposes criminal or civil penalties. ■