Form 8938 and Foreign Financial Assets: A Comprehensive Analysis of the Reporting Rules after IRS Issues Final Regulations

By Hale E. Sheppard

Introduction

The U.S. government has been outraged for years about widespread international tax noncompliance, and it has recently taken major steps to address the problem. One such step was the enactment of the Foreign Account Tax Compliance Act (FATCA).[1] This legislation established various tax provisions, including Code Sec. 6038D, which requires certain U.S. individual taxpayers to report data to the IRS about their foreign financial assets by filing an annual Form 8938 (*Statement of Specified Foreign Financial Assets*).

Compliance with the Form 8938 filing requirement is critical for taxpayers because violations trigger new information-reporting penalties, increased sanctions for tax understatements, extended periods for IRS enforcement, potential criminal charges and a costly fight with the U.S. government on three fronts simultaneously. Even though Code Sec. 6038D was enacted back in 2010, the biggest challenge remains an absence of clear, consolidated direction from the IRS about the complex rules associated with Form 8938. The guidance available at this time is a hodgepodge, mainly comprised of temporary regulations issued in 2011 ("Temporary Regulations"), final regulations promulgated in December 2014 ("Final Regulations"), numerous versions of the Instructions for Form 8938 and information periodically placed on the IRS's website. Unfortunately, not all the pertinent data can be found in one place, and that which is accessible is highly technical. This obligates beleaguered taxpayers to search multiple sources, many of them obscure and/or fleeting, in an effort to determine whether they are required to file Form 8938.

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Cognizant of this muddled state of affairs, this article aims to be a "one-stop shop" for taxpayers, a *comprehensive* source of all data available at this time with respect to Form 8938.[2]

Analysis of Foreign Financial Asset Reporting

General Rule and Overview

The general rule in Code Sec. 6038D(a) looks innocuous, but it is loaded with defined terms, conditions and nuances. This tax provision contains the following mandate:

> Any individual who, during any taxable year, holds any interest in a specified foreign financial asset shall attach to such person's return of tax imposed by subtitle A for such taxable year the information described in subsection (c) with respect to each such asset if the aggregate value of all such assets exceeds $50,000 (or such higher dollar amount as the Secretary may prescribe).

That statutory language is daunting, even for seasoned tax professionals. When faced with such density and complexity, it helps to separate the language into manageable pieces. Below is a breakdown of rules under Code Sec. 6038D, which might serve as a checklist for those conducting their own Form 8938 evaluation.

- any specified individual ("SI")
- who holds an interest
- during any portion of a tax year
- in a specified foreign financial asset ("SFFA")
- must attach to his timely Form 1040 or Form 1040NR
- a complete and accurate Form 8938
- if the aggregate value of all SFFAs
- exceeds the applicable filing threshold

Who Must File a Form 8938?

General Rule

According to the Final Regulations, the following categories of individuals are considered SIs: (i) U.S. citizens, (ii) individuals who are not U.S. citizens but who are U.S. residents for any portion of the relevant year, (iii) nonresident aliens who affirmatively elect under Code Sec. 6013(g) or Code Sec. 6013(h) to be treated as U.S. residents for federal tax purposes, (iv) nonresident aliens who are *bona fide* residents of Puerto Rico, and (v) nonresident aliens who are *bona fide* residents of a so-called "Section 931 Possession," which, at this point, means American Samoa.[3]

Special Rules for Dual-Residents

Background

Dual-residents are individuals who meet the test to be considered a "resident" for tax purposes of both the United States and a foreign country. Tax treaties between the United States and foreign countries normally contain "tie-breaker provisions," which assist in determining in which of the two countries the individual will be deemed a "tax resident" in a particular year. The tax residency of an individual affects many things, including which country has the right to tax what, which country can demand that an individual file information returns about "foreign" assets and other matters, *etc*.

Original Position by IRS

The IRS initially took the position that U.S. residency status for any part of the year, no matter how small and/or nonexclusive, suffices to trigger the Form 8938 filing requirement. In this regard, the preamble to the Temporary Regulations explained that "[a] resident alien who elects to be taxed as a resident of a foreign country pursuant to a U.S. income tax treaty's residency tie-breaker rules is [an SI] for purposes of Section 6038D."[4] The initial version of the Instructions for Form 8938 echoed that sentiment, giving the following warning to individuals with multiples residences: "If you qualify as a resident alien, you are [an SI] even if you elect to be taxed as a resident of a foreign country under the provisions of a U.S. income tax treaty. If you have to file Form 8938, attach it to your Form 1040NR."[5]

New Position by IRS

The IRS received comments in response to the Temporary Regulations, including at least one suggesting that dual-residents who file a Form 8833 (*Treaty-Based Return Position*) claiming foreign residency under the "tie-breaker" rules should not be considered an SI for purposes of Form 8938.[6] Surprisingly, the IRS accepted this recommendation and reversed course regarding the rules affecting dual-residents. The IRS explained its capitulation in the preamble to the Final Regulations, as follows:

> The Treasury Department and the IRS have concluded that reporting under Section 6038D is closely associated with the determination of an individual's income tax liability. Because the taxpayer's filing of a Form 8833 with his or her Form 1040NR (or other appropriate form) will permit the IRS to identify individuals in this category and take follow-up enforcement actions when considered appropriate, reporting of Form 8938 . . . is *not* essential to effective

IRS tax enforcement efforts relating to this category of U.S. residents.[7]

The Final Regulations contain new rules expressly relieving dual-residents from filing Forms 8938 in various circumstances.[8]

No Tax Return Requirement Means No Form 8938 Requirement

Description of General Rule

Generally, an SI who is not required to file an annual tax return with the IRS for the relevant year is not required to file a Form 8938 either.[9] The Instructions for Form 8938 enlarges this idea, indicating that if an SI has no tax return filing duty, then has no Form 8938 filing duty, even if the value of the SFFAs exceeds the applicable reporting threshold.[10] This exception could affect various taxpayers, such as those whose gross income is below certain levels.[11] It could also impact those living in Puerto Rico and American Samoa, as explained by the preamble to the Temporary Regulations:

> In general, bona fide residents of the U.S. Virgin Islands and U.S. territories to which Section 935 applies (currently, Guam and the Northern Mariana Islands) *are not required* to file a federal income tax return provided they correctly report and pay tax on their worldwide income to their U.S. territory taxing authority. Bona fide residents of Puerto Rico or a Section 931 possession (currently, American Samoa) generally *are required* to file a federal income tax return with the Internal Revenue Service *only if* they have income from sources without the relevant U.S. territory, because Sections 931(a) and 933 generally exclude from gross income any income derived from sources within the relevant U.S. territory. Section 6038D and these regulations generally require only bona fide residents of Puerto Rico or a Section 931 possession that are required to file a federal income tax return with the Internal Revenue Service to file a Form 8938 with the Internal Revenue Service.[12]

Rejection by IRS of Public Comments

The IRS received two main suggestions about this issue in response to the Temporary Regulations, and the rejection thereof provides clarity on the IRS's stance. First, one commentator asked to the IRS to exempt from the Form 8938 filing duty those SIs with no U.S. income tax liability during a particular year. The IRS underscored the general rule that SIs who have no duty to file a Form 1040 or Form 1040NR are not required to file a separate Form 8938, but stood firm on the notion that the data on Form 8938 is an important component of the overall tax return package, even if no U.S. tax liability is shown.[13]

Second, another commentator requested that certain individuals who are working in the United States temporarily under nonimmigrant visas (such as H, L or E visas) be exempted from the Form 8938 filing requirement. In denying this proposal, the IRS noted that (i) Code Sec. 6038D is designed to provide the IRS data about SFFAs of all individual taxpayers in order to assist in the fair and uniform enforcement of U.S tax laws, (ii) excluding certain categories of U.S. residents (including those who are considered U.S. residents solely because of their "substantial presence" in the United States) from the Form 8938 filing requirement when all U.S. residents are subject to taxation on worldwide income would be contrary to the purpose of Code Sec. 6038D, and (iii) "[i]ndividuals in the United States under non-immigrant visas often stay in the United States for years, making it difficult to justify treating them more favorably than other U.S. residents."[14]

What Period of Time Does each Form 8938 Cover?

The requirement to file a Form 8938 currently applies *only* to individuals, and they are calendar-year taxpayers by default, starting each tax period on January 1 and ending on December 31.[15] Thus, when an individual meets the definition of SI for the entire year, the reporting period generates no uncertainty. Things get more complicated, though, when an individual is considered an SI for only part of a year, which could occur when an individual is arriving in or departing from the United States, when an individual dies mid-year, *etc*.

The Final Regulations explain that the reporting period covered by Form 8938 is the SI's tax year (*i.e.*, January 1 to December 31), except in cases where the individual is an SI for less than a full year. In such partial-year situations, the reporting period is shortened to the portion of the calendar year that the individual actually meets the definition of SI.[16] The Instructions for Form 8938 contain three examples that elucidate these partial-year scenarios:

- John is a U.S. citizen and a calendar-year taxpayer who was alive the entire year. The Form 8938 reporting period begins January 1 and ends December 31.
- Agnes was a single, calendar-year taxpayer, who was a U.S. citizen, and who died on March 6. The Form 8938 reporting period begins January 1 and ends March 6.
- George, a calendar-year taxpayer, is not a U.S. citizen or married. George arrived in the United States on

February 1 and became a U.S. resident for tax purposes that year because of his "substantial presence" in the United States. The Form 8938 reporting period begins on George's residency starting date, February 1, and ends December 31.[17]

When Does an Individual "Hold an Interest" in an SFFA?

General Rules

Holding an interest in an asset means different things in different contexts. For instance, when dealing with FBARs, an individual has a "direct financial interest" in a foreign account when he is the owner of record or holds legal title, regardless of whether the account is maintained for his own benefit or for the benefit of others.[18] The individual has an "indirect financial interest" for FBAR purposes where the accountholder is (i) a person acting as an agent, nominee, attorney, *etc*. for the individual; (ii) a corporation in which the individual owns, directly or indirectly, more than 50 percent of the shares; (iii) a partnership in which the individual owns, directly or indirectly, 50 percent or more of the profits or capital interests; (iv) any other entity (other than certain trusts) in which the individual owns, directly or indirectly, more than 50 percent of the profits interests, capital interests, voting power, or assets; (v) a grantor trust where the individual is the grantor; or (vi) a trust in which the individual has a present beneficial interest in more than 50 percent of the assets or from which the individual receives more than 50 percent of the current income.[19]

The definition of "holding an interest" varies significantly for purposes of Form 8938, and this has caused some confusion among taxpayers and practitioners accustomed to the FBAR standards. Generally, an SI has an interest in a SFFA if any income, gains, losses, deductions, credits, gross proceeds or distributions attributable to the holding or disposition of the SFFA are (or should be) reported, included or otherwise reflected on the SI's annual tax return.[20] The regulations clarify that an SI has an interest in the SFFA *even if* no income, gains, losses, deductions, credits, gross proceeds or distributions are attributable to the holding or disposition of the SFFA for the year in question.[21] Stated differently, an SI must file a Form 8938 despite the fact that none of the SFFAs that must be reported affect his U.S. tax liability for the year.[22]

Special Rules in Five Situations

There are five special rules about "holding an interest" in the context of Form 8938.

No Entity Attribution

An SI is *not* treated as having an interest in an SFFA that is held by a corporation, partnership, trust or estate solely as a result of the SI's status as a shareholder, partner or beneficiary of such entity.[23] In other words, there is no entity-attribution here, no ascribing an interest in an SFFA to an SI simply because the SI has an ownership interest in the entity that actually holds SFFAs. This nonattribution rule is distinct from the FBAR standards, which, as explained above, generally demand reporting of foreign financial accounts that an individual is deemed to hold, either directly or through others.

Disregarded Entities Holding SFFAs

An SI who owns a "disregarded entity" is treated as having an interest in any SFFA that is held by such entity.[24] As the Instructions for Form 8938 succinctly put it, "[i]f you are the owner of a disregarded entity, you have an interest in any [SFFAs] owned by the disregarded entity."[25]

A number of commentators requested clarification about the preceding rule in response to the Temporary Regulations, and the IRS accommodated in the preamble to the Final Regulations by stating as follows: "a specified person that owns a foreign or domestic entity that is a disregarded entity is treated as having an interest in any [SFFAs] held by the disregarded entity. As a result, a specified person that owns a disregarded entity (whether domestic or foreign) that, in turn, owns [SFFAs] must include the value of those assets in determining whether the specified person meets the reporting thresholds … and, if so, must report such assets on Form 8938."[26]

Grantor Trusts Holding SFFAs

Similar to the treatment afforded owners of disregarded entities, an SI who is the owner (full or partial) of a grantor trust generally is considered to hold an interest in any SFFA that is actually held by such trust.[27]

SFFAs Held by Children

An SI who makes the so-called "kiddie tax" election under Code Sec. 1(g)(7) to include certain passive income of his child in his own gross income for U.S. income tax purposes is considered to "hold an interest" in any SFFA held by such child.[28] The Instructions for Form 8938 state this rule clearly, warning that "[i]f you file Form 8804 (Parent's Election to Report Child's Interest and Dividends) with your income tax return [then] you have an interest in any [SFFA] held by the child."[29]

Certain Nonvested SFFAs

After issuing the Temporary Regulations in late 2011, the IRS received requests for clarification about whether

an SI is considered to "hold an interest" in property transferred to the SI in connection with performance of personal services during any period that the SI's interest in the property has not yet vested.[30] The Final Regulations create two rules in this regard. First, an SI who receives property for the performance of personal services is first considered to "hold an interest" in the property for purposes of Code Sec. 6038D on the first date that the property is substantially vested, within the meaning of Reg. §1.83-3(b).[31] Second, in the case of property with respect to which an SI makes an election under Code Sec. 83(b) to be taxed immediately at present value on the entire amount that will eventually vest, the SI is deemed to "hold an interest" on the date of transfer of the property.[32]

What Types of Assets Constitute SFFAs?

For purposes of Code Sec. 6038D, the term SFFA includes two major categories: (i) foreign financial accounts maintained at a foreign financial institution[33]; and (ii) other foreign financial assets, which are held for investment purposes.[34] The details and unexpected twists associated with each category are examined below.

Foreign Financial Accounts

Foreign Financial Accounts

The concept of "financial account" for purposes of Form 8938 is complicated for several reasons and will inevitably trigger confusion for taxpayers and tax advisors alike.

The definition contained in the first place many taxpayers look (*i.e.*, the Instructions for Form 8938) is an oversimplification that could lead to unintentional omissions by taxpayers. They simply state that a "financial account" is a depository account, a custodial account or any equity or debt interest held in a foreign financial institution (other than an interest that is regularly traded on an established securities market).[35] This is a deceptively simple and misleading description of a dense, technical term.

Moreover, the definition of "financial account" is not even found in Code Sec. 6038D; rather, it is located elsewhere in the Code, in the international tax withholding provision, Code Sec. 1471, and its ultra-dense regulations.[36]

After a significant amount of cross-referencing, head-scratching and consternation, one slowly begins to understand the items that will and will not fall within the definition of "financial account" for purposes of Form 8938. Below is the current list, to the extent that it can be compiled from various sources.

Items Considered "Financial Accounts"

- Depository accounts are considered "financial accounts" for purposes of Form 8938. In this context, the term "depository accounts" generally encompasses (i) commercial accounts; (ii) savings accounts; (iii) time-deposit accounts; (iv) thrift accounts; (v) accounts evidenced by a certificate of deposit, thrift certificate, investment certificate, passbook, certificate of indebtedness, or any other instrument for placing money in the custody of an entity engaged in a banking or similar business for which the entity is obligated to give credit, regardless of whether such instrument is interest-bearing or non-interest-bearing; and (vi) any amount held by an insurance company under a guaranteed investment contract or similar agreement to pay or credit interest.[37]
- Custodial accounts are deemed to be "financial accounts" for purposes of Form 8938. Here, the term "custodial accounts" generally means an arrangement for holding for the benefit of another person a financial instrument, contract or investment, such as shares of corporate stock, promissory notes, bonds, debentures, other evidences of debt, currency or commodity transactions, credit default swaps, swaps based on a nonfinancial index, notional principal contracts, insurance policies, annuity contracts and any options or other derivative instruments.[38]
- Equity or debt interests in a foreign financial institution, other than interests regularly traded on established securities markets, generally are categorized as "financial accounts."[39]
- The term "financial account" also includes "cash-value insurance contracts" and certain types of annuity contracts issued or maintained by an insurance company, a holding company for an insurance company or certain foreign financial institutions.[40] Commentators to the Temporary Regulations requested clarifications about the reporting of life insurance policies with cash-surrender values on Form 8938, but the IRS declined to elaborate on grounds that the international withholding regulations under Code Sec. 1471 "already provide clear rules" on this topic.[41]
- Tax-favored foreign retirement accounts, foreign pension accounts and foreign nonretirement savings accounts meeting certain criteria are treated as "financial accounts" for purposes of Form 8938. This issue is complicated by the fact that some of the items expressly *excluded* from the definition of "financial account" in the regulations are reversed later in the very same regulations. For example, the regulations under Code Sec. 1471 state that tax-favored foreign retirement

accounts, pension accounts and nonretirement savings accounts meeting certain criteria generally are *not* considered "financial accounts" and thus would not be reportable on Form 8938.[42] However, later in the same opaque regulations under Code Sec. 1471, the IRS back tracks, stating that the pertinent exclusions "shall not apply for purposes of determining whether an account or other arrangement is a financial account for purposes of Section 6038D."[43]

- Tax-favored foreign retirement accounts, foreign pension accounts and foreign nonretirement savings accounts that have already been excluded from the definition of "financial account" pursuant to an intergovernmental agreement ("IGA") between the United States and a foreign country to implement FATCA will be considered "financial accounts" for purposes of Form 8938. In other words, while certain foreign governments and financial institutions are not required to provide data to the IRS pursuant to FATCA about certain retirement-type accounts, SIs holding an interest in such accounts will not benefit from such an accommodation. Arriving at this conclusion is challenging. It requires one to first consult the Final Regulations under Code Sec. 6038D, then analyze by cross-reference the numerous filing exceptions located in the international withholding regulations under Code Sec. 1471, and, ultimately, check again the Final Regulations under Code Sec. 6038D for the exceptions-to-the-filing-exceptions.[44] The IRS has indicated that it intends to rectify this circular reasoning and the resulting confusion by amending the regulations under Code Sec. 1471 to add a "coordination rule" expressly stating that the retirement-type accounts excluded from the definition of "financial account" for purposes of the IGAs will be included in the definition of "financial accounts" for purposes of Code Sec. 6038D and Form 8938.[45]

Items Not Considered "Financial Accounts"

- Certain term life insurance contracts are not considered "financial accounts."[46]
- Accounts held by an estate of an individual will not be considered "financial accounts" if the documentation for such accounts includes a copy of the deceased's will or death certificate.[47]
- Certain escrow accounts escape the definition of "financial account."[48]
- Non-investment-linked, nontransferable, immediate life annuity contracts that monetizes certain types of retirement or pension accounts will not be classified as "financial accounts."[49]
- Accounts or products that are excluded from the definition of "financial account" under an IGA (other than certain tax-favored foreign retirement accounts, foreign pension accounts and foreign nonretirement savings accounts) will not be considered "financial accounts."[50]
- Accounts held with "U.S. payors" are not deemed to be "financial accounts."[51] The Final Regulations broadly define the term "U.S. payor" as a "U.S. person," which includes a foreign branch of the U.S. person, a foreign office of the U.S. person and a U.S. branch of certain foreign banks and foreign insurance companies.[52] Examples of financial accounts that are exempt from reporting on Form 8938 because they are held with "U.S. payors" include U.S. mutual funds, U.S. individual retirement accounts, Code Sec. 401(k) retirement accounts, qualified U.S. retirement plan and brokerage/investment accounts maintained by U.S. financial institutions.[53]
- Accounts whose holdings are subject to the mark-to-market rules under Code Sec. 475 are not considered "foreign accounts" for purposes of Form 8938.[54]

Foreign Financial Institution

A "foreign financial institution" generally means a non-U.S. entity that (i) accepts deposits in the ordinary course of a banking or similar business; (ii) holds financial assets for the account of others as a substantial portion of its business; or (iii) is engaged primarily in the business of investing, reinvesting or trading securities, partnership interests, commodities or any interest in such securities, partnership interests or commodities.[55]

SFFAs Other Than Foreign Financial Accounts

Items That Are Considered Other SFFAs

SFFAs also include certain other assets that do meet the broad definition of "financial account" for purposes of Form 8938 and that are held for investment purposes. Among these assets are (i) stocks or securities issued by a non-U.S. person, (ii) financial instruments or contracts held for investment purposes whose issuer or counterparty is a non-U.S. person, and (iii) any interest in a foreign entity.[56] The IRS recognized in the preamble to the Temporary Regulations that creating such expansive categories could lead to redundancies:

> These three categories [of other SFFAs] are broad and overlap in certain cases such that an asset not held in a financial account may be within more than one of the statutory categories … For example, stock issued by a

foreign corporation is stock that is issued by a person other than an U.S. person, and is also an interest in a foreign entity.[57]

The Final Regulations enlarge and clarify the categories, identifying the following items as SFFAs: (i) stock issued by a foreign corporation; (ii) a capital interest or profits interest in a foreign partnership; (iii) a note, bond, debenture or other form of debt issued by a foreign person; (iv) an interest in a foreign trust; (v) an interest swap, currency swap, basis swap, interest rate cap, interest rate floor, commodity swap, equity swap, equity index swap, credit default swap or similar agreement with a foreign counterparty; and (vi) any option or other derivative instrument with respect to any of the items listed as examples or with respect to any currency or commodity that is entered into with a foreign counterparty or issuer.[58]

Items That Are Not Considered Other SFFAs

The IRS guidance *excludes* two types of foreign assets from classification as SFFAs.

Interests in Foreign Social Security and Social Insurance

Various sources state that an interest in a social security, social insurance or other similar program of a foreign government is not an SFFA.[59] Commentators to the Temporary Regulations requested that the IRS incorporate this exclusion into the Final Regulations, but the IRS declined because, from its perspective, this issue has already been adequately addressed in the preamble to the Temporary Regulations, the Instructions for Form 8938, the comparison chart posted on the IRS's website showing similarities and differences between Form 8938 and the FBAR and by the fact that interests in foreign social security or social insurance were not specifically listed as "other SFFAs" in the Final Regulations.[60]

Certain Interests in Foreign Trusts or Foreign Estates

The Final Regulations provide that an interest in a foreign trust or a foreign estate is not an SFFA, *unless* the SI either knows or has reason to know of the existence of the interest based on readily accessible information.[61] Receipt of a distribution from the foreign trust or foreign estate constitutes actual knowledge of its existence for purposes of Code Sec. 6038D; that is, an SI who receives cash or other property from a foreign trust or estate during a given year is prohibited from later denying its existence when it comes to reporting it on Form 8938.[62]

Commentators to the Temporary Regulations were concerned that the "reason-to-know" standard would result in compliance challenges for SIs who are aware of their interest in foreign trust or estate, but who have not received a distribution from the trust or estate, and who do not know the value of the interest. The commentators suggested that SIs should not be required to report the interest in the foreign trust or estate for any year in which the SI did not receive an actual distribution. [63] The IRS rejected this recommendation in issuing its Final Regulations because the issue has "already been addressed comprehensively," and the existing rules "achieve a reasonable an appropriate balance between the government's tax administration interests and the beneficiary's compliance burdens."[64] In support of its position, the IRS points to the simplified valuation rules applicable this to scenario, which allow SIs to place a value of $0 on the SFFA in years that they do not receive distributions and do not know the value of the interest based on readily accessible information.[65]

What Does "Held for Investment Purposes" Mean? General Trade-or-Business Test

As mentioned above, assets are only considered SFFAs (and thus reportable on Form 8938) if they are "held for investment purposes" and meet certain other criteria.[66] What does this phrase mean for purposes of Code Sec. 6038D?

The Final Regulations indicate that an asset is "held for investment purposes" if it is *not* used in, or held for use in, the conduct of a trade of business.[67] For purposes of Form 8938, an asset is used in, or held for use in, the conduct of a trade or business (and thus not "held for investment purposes") if the asset is (i) held for the principal purpose of promoting the present conduct of a trade or business; (ii) acquired and held in the ordinary course of a trade or business, such as an account or note receivable arising from the trade or business; or (iii) otherwise held in a "direct relationship" to the trade or business.[68]

In analyzing the "direct relationship" criterion described above, the Final Regulations indicate that the IRS will give principal consideration to whether the asset is needed in the trade or business; that is, is the asset held to meet the present needs of the trade or business (such as its operating expenses) and not its anticipated future needs.[69] The Final Regulations clarify that an asset is *not* currently needed in the trade or business (and thus is "held for investment purposes") if it is held to allow future diversification into a new trade or business, future plant replacement or future business contingencies.[70] The Final Regulations also feature a presumption that an asset is held in direct relationship to conducting a trade or business if (i) the asset was acquired with funds generated by the trade or business of the taxpayer or an affiliated group, (ii) the income from the asset is retained or reinvested in the trade or business,

and (iii) personnel who are actively involved in the conduct of the trade or business exercise significant management and control over the investment of such asset.[71]

Clarification about Ownership of Foreign Stock

The Final Regulations state that stock is "never" considered an asset used or held for use in a trade or business for purposes of Code Sec. 6038D.[72] The Instructions to Form 8938 second this interpretation, stating that "[s]tock is not considered used or held for us in the conduct of a trade or business."[73]

Rejection by IRS of Bright-Line Test

Several commentators to the Temporary Regulations asked the IRS to develop a "bright-line" test (instead of the general trade-or-business test that currently exists) to determine whether an asset is an SFFA required to be reported on Form 8938.[74] The IRS rejected this request in issuing the Final Regulations because the trade-or-business test "strikes an appropriate balance under Section 6038D by focusing on whether the asset is held for investment," the proper characterization of a foreign asset is an "inherently factual determination that is not susceptible to a bright line test," and the Final Regulations contain "reasonable rules that will yield appropriate reporting results in a wide variety of fact patterns involving the taxpayer's trade or business."[75]

Items That Might Be Considered SFFAs

Commentators to the Temporary Regulations asked the IRS to expand its list of items that are specifically excluded from the definition of "other SFFA." The IRS rebuffed these requests. The following review of the relevant items and the IRS's rationale for not automatically excluding them from SFFA status provides valuable insight.

Certain Hedging Transactions

The IRS declined to exclude certain hedging transactions described in Code Sec. 1221(a)(7) from the definition of SFFA because "taxpayers engaging in hedging transactions should determine whether such transactions are [SFFAs] by applying the same general test applied by other taxpayers," *i.e.*, the standard trade-or-business test described above.[76]

Employment Contracts

The IRS was unwilling to exclude employment contracts from the definition of SFFA because the type of property covered by an employment contract could vary widely depending on the industry and location of the taxpayer and because the standard trade-or-business test "should apply broadly to a wide range of financial assets in order to achieve uniform reporting results with aggregate [SFFAs] of similar value."[77]

Publicly Traded Stock

The IRS discarded the idea that stock of a foreign corporation that is traded on a public stock exchange (located in the United States or elsewhere) should escape classification as an SFFA.[78]

Virtual Currency

The IRS is reserving judgment at this time regarding whether "virtual currency," like Bitcoin, should be considered an SFFA for purposes of Code Sec. 6038 and "welcomes comments on this topic."[79]

Examples and Clarifications on All Types of SFFAs

The IRS is convinced that it has already done an adequate job of defining the concept of "SFFA" for purposes of Form 8938 and has no immediate plans of expanding efforts in this area. The IRS's position is set forth in the preamble to the Final Regulations:

> A number of comments [to the Temporary Regulations] requested *examples* of the types of financial assets that are *not* required to be reported under Section 6038D. The Treasury Department and the IRS have not provided these examples in the final rule because the 2011 temporary regulations, as well as the relevant portions of the regulations under chapters 4 and 61, already include detailed rules to support taxpayer determinations as to whether an asset is [an SFFA] that must be reported.[80]

While the IRS is unwilling at this time to issue regulations listing specific examples of items that are not considered SFFAs, it has provided clarity in two ways. First, the IRS posted to its website a chart explaining and comparing the key issues for Forms 8938 and FBARs. A copy of this chart can be found as Exhibit 1 to this article. Second, the IRS issued "Basic Questions and Answers on Form 8938." The IRS initially placed these on its website in February 2012 (with the issuance of the Temporary Regulations) and later revised them in December 2014 (with the issuance of the Final Regulations). This "basic" guidance from the IRS, subject to change in the future, is set forth below.

- *What are the specified foreign financial assets that I need to report on Form 8938?* If you are required to file Form 8938, you must report your financial

accounts maintained by a foreign financial institution. Examples of financial accounts include: savings, deposit, checking and brokerage accounts held with a bank or broker-dealer. And, to the extent held for investment and not held in a financial account, you must report stock or securities issued by someone who is not a U.S. person, any other interest in a foreign entity and any financial instrument or contract held for investment with an issuer or counterparty that is not a U.S. person. Examples of these assets that must be reported if not held in an account include: stock or securities issued by a foreign corporation; a note, bond or debenture issued by a foreign person; an interest rate swap, currency swap, basis swap, interest rate cap, interest rate floor, commodity swap, equity swap, equity index swap, credit default swap or similar agreement with a foreign counterparty; an option or other derivative instrument with respect to any of

EXHIBIT 1 – IRS'S COMPARISON CHART OF FORM 8938 AND FBAR REQUIREMENTS AND ISSUES, AVAILABLE ON WWW.IRS.GOV, CURRENT AS OF FEBRUARY 2, 2015.

	Form 8938, Statement of Specified Foreign Financial Assets	Form TD F 90-22.1, Report of Foreign Bank and Financial Accounts (FBAR)
Who Must File?	Specified individuals, which include U.S citizens, resident aliens, and certain non-resident aliens that have an interest in specified foreign financial assets and meet the reporting threshold	U.S. persons, which include U.S. citizens, resident aliens, trusts, estates, and domestic entities that have an interest in foreign financial accounts and meet the reporting threshold
Does the United States include U.S. territories?	No	Yes, resident aliens of U.S territories and U.S. territory entities are subject to FBAR reporting
Reporting Threshold (Total Value of Assets)	$50,000 on the last day of the tax year or $75,000 at any time during the tax year (higher threshold amounts apply to married individuals filing jointly and individuals living abroad)	$10,000 at any time during the calendar year
When do you have an interest in an account or asset?	If any income, gains, losses, deductions, credits, gross proceeds, or distributions from holding or disposing of the account or asset are or would be required to be reported, included, or otherwise reflected on your income tax return	Financial interest: you are the owner of record or holder of legal title; the owner of record or holder of legal title is your agent or representative; you have a sufficient interest in the entity that is the owner of record or holder of legal title. Signature authority: you have authority to control the disposition of the assets in the account by direct communication with the financial institution maintaining the account. See instructions for further details.
What is Reported?	Maximum value of specified foreign financial assets, which include financial accounts with foreign financial institutions and certain other foreign non-account investment assets	Maximum value of financial accounts maintained by a financial institution physically located in a foreign country
How are maximum account or asset values determined and reported?	Fair market value in U.S. dollars in accord with the Form 8938 instructions for each account and asset reported Convert to U.S. dollars using the end of the taxable year exchange rate and report in U.S. dollars.	Use periodic account statements to determine the maximum value in the currency of the account. Convert to U.S. dollars using the end of the calendar year exchange rate and report in U.S. dollars.
When Due?	By due date, including extension, if any, for income tax return	Received by June 30 (no extensions of time granted)
Where to File?	File with income tax return pursuant to instructions for filing the return	File electronically through FinCENs BSA E-Filing System. The FBAR is not filed with a federal tax return.
Penalties	Up to $10,000 for failure to disclose and an additional $10,000 for each 30 days of non-filing after IRS notice of a failure to disclose, for a potential maximum penalty of $60,000; criminal penalties may also apply	If non-willful, up to $10,000; if willful, up to the greater of $100,000 or 50 percent of account balances; criminal penalties may also apply

EXHIBIT 1 – IRS'S COMPARISON CHART OF FORM 8938 AND FBAR REQUIREMENTS AND ISSUES, AVAILABLE ON WWW.IRS.GOV, CURRENT AS OF FEBRUARY 2, 2015.		
	Form 8938, Statement of Specified Foreign Financial Assets	**Form TD F 90-22.1, Report of Foreign Bank and Financial Accounts (FBAR)**
Types of Foreign Assets and Whether They are Reportable		
Financial (deposit and custodial) accounts held at foreign financial institutions	Yes	Yes
Financial account held at a foreign branch of a U.S. financial institution	No	Yes
Financial account held at a U.S. branch of a foreign financial institution	No	No
Foreign financial account for which you have signature authority	No, unless you otherwise have an interest in the account as described above	Yes, subject to exceptions
Foreign stock or securities held in a financial account at a foreign financial institution	The account itself is subject to reporting, but the contents of the account do not have to be separately reported	The account itself is subject to reporting, but the contents of the account do not have to be separately reported
Foreign stock or securities not held in a financial account	Yes	No
Foreign partnership interests	Yes	No
Indirect interests in foreign financial assets through an entity	No	Yes, if sufficient ownership or beneficial interest (i.e., a greater than 50 percent interest) in the entity. See instructions for further detail.
Foreign mutual funds	Yes	Yes
Domestic mutual fund investing in foreign stocks and securities	No	No
Foreign accounts and foreign non-account investment assets held by foreign or domestic grantor trust for which you are the grantor	Yes, as to both foreign accounts and foreign non-account investment assets	Yes, as to foreign accounts
Foreign-issued life insurance or annuity contract with a cash-value	Yes	Yes
Foreign hedge funds and foreign private equity funds	Yes	No
Foreign real estate held directly	No	No
Foreign real estate held through a foreign entity	No, but the foreign entity itself is a specified foreign financial asset and its maximum value includes the value of the real estate	No
Foreign currency held directly	No	No
Precious Metals held directly	No	No
Personal property, held directly, such as art, antiques, jewelry, cars and other collectibles	No	No
'Social Security'- type program benefits provided by a foreign government	No	No

these examples or with respect to any currency or commodity that is entered into with a foreign counterparty or issuer; a partnership interest in a foreign partnership; an interest in a foreign retirement plan or deferred-compensation plan; an interest in a foreign estate; and any interest in a foreign-issued insurance contract or annuity with a cash-surrender value. The examples listed above do not comprise an exclusive list of assets required to be reported.[81]

- *Does foreign real estate need to be reported on Form 8938?* Foreign real estate is not a specified foreign asset required to be reported on Form 8938. For example, a personal residence or a rental property does not have to be reported. If the real estate is held through a foreign entity, such as a corporation, partnership, trust or estate, then the interest in the entity is a specified foreign financial asset that is reported on Form 8938 if the total value of all your specified foreign financial assets is greater than the reporting threshold that applies to you. The value of the real estate held by the entity is taken into account in determining the value of the interest in the entity to be reported on Form 8938, but the real estate itself is not separately reported on Form 8938.[82]
- *I directly hold foreign currency (that is, the currency isn't in a financial account). Do I need to report this on Form 8938?* Foreign currency is not a specified foreign financial asset and is not reportable on Form 8938.[83]
- *I am a beneficiary of a foreign estate. Do I need to report my interest in a foreign estate on Form 8938?* Generally, an interest in a foreign estate is a specified foreign financial asset that is reportable on Form 8938 if the total value of all of your specified foreign financial assets is greater than the reporting threshold that applies to you.[84]
- *I acquired or inherited foreign stock or securities, such as bonds. Do I need to report these on Form 8938?* Foreign stock or securities, if you hold them outside of a financial account, must be reported on Form 8938, provided the value of your specified foreign financial assets is greater than the reporting threshold that applies to you. If you hold foreign stock or securities inside of a financial account, you do not report the stock or securities on Form 8938.[85]
- *I directly hold shares of a U.S. mutual fund that owns foreign stocks and securities. Do I need to report the shares of the U.S. mutual fund or the stocks and securities held by the mutual fund on Form 8938?* If you directly hold shares of a U.S. mutual fund you do not need to report the mutual funds or the holdings of the mutual fund.[86]
- *I have a financial account maintained by a U.S. financial institution that holds foreign stocks and securities. Do I need to report the financial account or its holdings?* You do not need to report a financial account maintained by a U.S. financial institution or its holdings. Examples of financial accounts maintained by U.S. financial institutions include U.S. mutual fund accounts, IRAs (traditional or Roth), 401(k) retirement plans, qualified U.S. retirement plans and brokerage accounts maintained by U.S. financial institutions.[87]
- *I have a financial account maintained by a foreign financial institution that holds investment assets. Do I need to report the financial account if all or any of the investment assets in the account are stock, securities or mutual funds issued by a U.S. person?* If you have a financial account maintained by a foreign financial institution and the value of your specified foreign financial assets is greater than the reporting threshold that applies to you, you need to report the account on Form 8938. A foreign account is a specified foreign financial asset even if its contents include, in whole or in part, investment assets issued by a U.S. person.[88]
- *I have a financial account with a U.S. branch of a foreign financial institution. Do I need to report this account on Form 8938?* A financial account, such as a depository, custodial or retirement account, at a U.S. branch of a foreign financial institution is an exception to the general rule that a financial account maintained by a foreign financial institution is a specified foreign financial asset. A financial account maintained by a U.S. branch or U.S. affiliate of a foreign financial institution does not have to be reported on Form 8938, and any specified foreign financial assets in that account also do not have to be reported.[89]
- *I own foreign stocks through a foreign branch of a U.S.-based financial institution. Do I need to report these on Form 8938?* If a financial account, such as a depository, custodial or retirement account, is held through a foreign branch or foreign affiliate of a U.S.-based financial institution, the foreign account is not a specified foreign financial asset and is not required to be reported on Form 8938.[90]
- *I have an interest in a foreign pension or deferred-compensation plan. Do I need to report it on Form 8938?* If you have an interest in a foreign pension or deferred-compensation plan, you have to report this interest on Form 8938 if the value of your specified foreign financial assets is greater than the reporting threshold that applies to you.[91]
- *I am a U.S. taxpayer and have earned a right to foreign social security. Do I need to report this on Form 8938?* Payments or rights to receive the foreign equivalent

or social security, social insurance benefits or another similar program of a foreign government are not specified foreign financial assets and are not reportable.[92]

- *If I have to file Form 8938, am I required to report all of my specified foreign financial assets regardless of whether the assets have a* de miminis *maximum value during the tax year?* If you meet the applicable reporting threshold, you must report all of your specified foreign financial assets, including the specified foreign financial assets that have a *de minimis* maximum value during the tax year. For exceptions to reporting, see Exceptions to Reporting on page 6 of the instructions for Form 8938.[93]
- *I directly hold tangible assets for investment, such as art, antiques, jewelry, cars and other collectibles, in a foreign country. Do I need to report these assets on Form 8938?* No. Directly held tangible assets, such as art, antiques, jewelry, cars and other collectibles, are not specified foreign financial assets.[94]
- *I directly hold precious metals for investment, such as gold, in a foreign country. Do I need to report these assets on Form 8938?* No. Directly held precious metals, such as gold, are not specified foreign financial assets. Note, however, that gold certificates issued by a foreign person may be a specified foreign financial asset that you would have to report on Form 8938 if the total value of all your specified foreign financial assets is greater than the reporting threshold that applies to you.[95]

When and How Does an SI File Form 8938?

General Rules

If an SI is required to file a Form 8938, then he must attach it to his "annual return" for the relevant year.[98] The Final Regulations clarify that, in the case of an SI, the "annual return" means the federal income tax return, such as Form 1040 (*U.S. Individual Income Tax Return*) or Form 1040NR (*U.S. Nonresident Alien Income Tax Return*).[99]

Answering a question that will be raised by countless taxpayers and return-preparers, the Instructions for Form 8938 indicate that Form 8938 will still be considered timely if it accompanies a Form 1040 or Form 1040NR filed on extension: "Attach Form 8938 to your annual return and file by the due date *(including extensions)* for that return."[100]

Finally, the IRS guidance indicates that a Form 8938 cannot be sent to the IRS separately under any circumstances. The Instructions for Form 8938 feature the following warning: "Caution—Do not send a Form 8938 to the IRS unless it is attached to an annual return or an amended return."[101] Other guidance from the IRS follows suit, explaining to taxpayers that "[i]f you omitted Form 8938 when you filed your income tax return, you should file Form 1040X (Amended U.S. Individual Income Tax Return) with your Form 8938 attached."[102] Thus, logic dictates that an SI who is unable to file a timely Form 1040 or Form 1040NR cannot avoid the penalty associated with Form 8938 by sending to the IRS a timely Form 8938, followed by a delinquent Form 1040 or Form 1040NR attaching a copy of the previously-filed Form 8938.[103]

Special Filing Rules for Married Taxpayers

Married Taxpayers Filing Joint Tax Returns

Special rules apply in the case of married individuals. According to the Final Regulations, married SIs who file *joint* Forms 1040 must include only one Form 8938 reporting all the SFFAs in which either spouse has an interest.[104] In this situation, each SFFA, even if jointly owned by the spouses, is reported on the Form 8938 "only once."[105]

Married Taxpayers Filing Separate Tax Returns

The filing requirements vary when married SIs file separately. The Final Regulations state that a married SI who files a *separate* Form 1040 must include a *separate* Form 8938 reporting all the SFFAs in which the married SI has an interest, including assets jointly held with his or her spouse.[106] The Final Regulations go on to clarify that, if both spouses are SIs, then each one must report on his or her own Form 8938 the entire value of each SFFA that the spouses jointly own.[107]

Coordination with Special Valuation Rules for Married Taxpayers

Married couples present two unique issues in the context of Code Sec. 6038D, namely, the special filing rules described immediately above and the special valuation rules analyzed later in this article. It is critical to review both issues when making determinations about married persons with respect to their obligations related to Form 8938.

What Information Must Be Reported on Form 8938?

General Rule

As with most tax statutes, Code Sec. 6038D itself does not identify the form on which taxpayers will be required to report the requisite data; this type of detail is best left to the regulations promulgated after Congress has given

its mandate. Indeed, while Code Sec. 6038D(c) purports to list the "required information," Congress was careful to state that "[t]he Secretary shall prescribe such regulations or other guidance as may be necessary or appropriate to carry out the purposes of this section, including regulations or other guidance which provide appropriate exceptions from the application of this section … ."[108] Based on this authority, the IRS issued the Temporary Regulations in 2011, the Final Regulations in late 2014, the Instructions for Form 8938 and various pages on the IRS website. Together, these items mandate that SIs provide to the IRS information about their interests in nearly all SFFAs.[109]

One commentator to the Temporary Regulations asked the IRS to reduce the amount of data required to be reported on Form 8938. Specifically, the commentator desired to avoid disclosing whether a "financial account" was opened or closed during a given year, the date on which an SFFA (other than a "financial account") was acquired or disposed of during the year and details about income, gain, loss, deductions or credits recognized during the year and where such items are reported on the SI's Form 1040 or Form 1040NR.[110] Predictably, the IRS snubbed this request, explaining that all the information sought by Form 8938 "is necessary for effective tax enforcement actions and is consistent with congressional intent in enacting Section 6038D."[111]

Items Exempted from Reporting on Form 8938

As explained in the preceding paragraph, Code Sec. 6038(h) expressly granted the IRS authority to create certain exemptions from filing Form 8938, and it has exercised this authority.

Exemption for SFFAs Reported to the IRS Elsewhere

General Explanation of Duplication Exemption

One exemption is designed to eliminate duplicative reporting of SFFAs. The Final Regulations state that an SI is not required to report an SFFA on Form 8938, provided that the SI already reports such SFFA on at least one of the following international information returns that was timely filed with the IRS:

- Form 3520 (*Annual Return to Report Transactions with Foreign Trusts and Receipt of Certain Foreign Gifts*)
- Form 3520-A (*Annual Information Return of Foreign Trust With a U.S. Owner*)
- Form 5471 (*Information Return of U.S. Persons with Respect to Certain Foreign Corporations*)
- Form 8621 (*Return by a Shareholder of a Passive Foreign Investment Company of a Qualified Electing Fund*)
- Form 8865 (*Return of U.S. Persons with Respect to Certain Foreign Partnerships*)
- Form 8891 (*U.S. Information Return for Beneficiaries of Certain Canadian Registered Retirement Plans*)
- Any other international information return under the Code that is timely filed with the IRS and identified for this purpose in regulations "or other guidance"[112]

Even though the SI avoids the need to resubmit lots of duplicative information to the IRS thanks to this exemption, all duties are not eliminated. The SI must still identify on Form 8938 the type and number of other information returns that he previously filed with the IRS.[113] For instance, if the SI held a reportable interest in a controlled foreign corporation, then he would file a Form 5471 and, instead of repeating much of the data about the corporation on a separate Form 8938, he would simply check the box on Form 8938 confirming that he had filed a separate Form 5471.

Proposed Changes to Duplication Exemption

Commentators to the Temporary Regulations proposed eliminating Form 8938 altogether and then either (i) creating one consolidated international information return addressing absolutely all issues, or (ii) modifying Schedule B to Form 1040 to permit SIs to check a box there notifying the IRS that it had separately filed other international information returns (such as Forms 3520, 3520-A, 5471, 8865, 8891, *etc.*). The IRS rejected this suggestion, explaining that continuing to use Form 8938 best carries out the purposes of Code Sec. 6038D and indicating that the costs associated with revising existing information returns, IT systems, submissions-processing programs and enforcement programs would be "disproportionate to expected benefits" of jettisoning Form 8938.[114]

Less extreme commentators suggested adding Form 8858 (*Information Return of U.S. Persons with Respect to Foreign Disregarded Entities*) to the list of information returns that would satisfy the reporting requirement of Form 8938. The IRS discarded this idea because the information on Form 8858 regarding SFFAs held by a foreign disregarded entity is not sufficiently detailed to warrant complaints of duplicative reporting on Form 8938.[115]

Another commentator to the Temporary Regulations asked the IRS to add Form 8854 (*Initial and Annual Expatriation Statement*) to the list of international information returns relieved from duplicative reporting. The IRS opposed this idea because, not only is the information collected on Form 8854 not duplicative of that collected on Form 8938, the IRS expects that requiring people who are expatriating from the United States to file both Form 8854 and Form 8938 will "substantially enhance IRS compliance programs" for expatriates.[116]

Exemption for Certain SFFAs in Puerto Rico or American Samoa

As explained at the beginning of this article, various categories of nonresident aliens are considered SIs, namely, nonresident aliens who are *bona fide* residents of Puerto Rico and nonresident aliens who are *bona fide* residents of a so-called Section 931 Possession, *i.e.*, American Samoa.[117] Also, as explained above, *bona fide* residents of Puerto Rico and American Samoa must file Forms 1040 with the IRS if they have income from sources outside their respective territories.[118] Cognizant of these realities, the IRS adopted another exemption.

An SI who is a *bona fide* resident of a U.S. possession and who is required to file a Form 8938 with the IRS is *not* required to report the following SFFAs: (i) a financial account maintained by a financial institution organized under the laws of the U.S. possession of which the SI is a *bona fide* resident; (ii) a financial account maintained by a branch of a financial institution not organized under the laws of the U.S. possession of which the SI is a *bona fide* resident if the branch is subject to the same tax and information reporting requirements applicable to a financial institution organized under the laws of the U.S. possession; (iii) stock or securities issued by an entity organized under the laws of the U.S. possession of which the SI is a *bona fide* resident; (iv) an interest in an entity organized under the laws of the U.S. possession of which the SI is a *bona fide* resident; and (v) a financial instrument or contract held for investment, provided that each issuer or counterparty that is a non-U.S. person is either an entity organized under the laws of the U.S. possession of which the SI is a *bona fide* resident or a *bona fide* resident of the U.S. possession of which the SI is a *bona fide* resident.[119] The IRS warned in the preamble to the Temporary Regulations that these criteria would be strictly enforced, as this exemption is not applicable to assets held by an SI who is not a *bona fide* resident of any U.S. territory or to an SI who is a *bona fide* resident of a U.S. territory other than the one to which the SFFAs are connected.[120]

Exemption for Certain Foreign Grantor Trusts

General Explanation of Exemption

The Final Regulations state that an SI who is an owner of a foreign trust under the grantor trust rules of Code Secs. 671 to 679 is not required to report any SFFAs held by the foreign trust, provided that three conditions are met: (i) the SI reports the trust on a Form 3520 that is timely filed with the IRS; (ii) the foreign trust timely files Form 3520-A with the IRS; and (iii) the SI checks the proper boxes on Form 8938 to confirm the prior filing of Form 3520 and Form 3520-A.[121]

Proposed Changes to Duplication Exemption

Commentators to the Temporary Regulations made various suggestions with respect to foreign trust reporting, including (i) allowing a foreign trustee of a foreign trust with a U.S. owner to satisfy Section 6038D for all trust beneficiaries by filing just one Form 3520-A, and (ii) permitting a foreign trustee of a foreign trust to file one Form 8938 on behalf of all the trust's U.S. beneficiaries.[122] In issuing the Final Regulations, the IRS rejected these suggestions from commentators because "[t]he IRS can best use the information reported on the Form 8938 to enforce tax compliance when it is provided in connection with the filing of an annual return [*i.e.*, Form 1040 or Form 1040NR] by the taxpayer who is the beneficial owner of the interest in the foreign trust."[123]

Exemption for Certain Domestic Grantor Trusts

The final exemption provides that an SI who is treated as an owner of a domestic trust under the grantor trust rules of Code Secs. 671 to 679 does not need to file a Form 8938 to report any SFFA held by the trust if the trust is a domestic liquidating trust created pursuant to a court order issued in a Chapter 7 bankruptcy, a confirmed plan in a Chapter 11 bankruptcy or a domestic widely held fixed investment trust.[124]

How Do You Value an SFFA?

Valuing SFFAs can be deceptively complicated. This is caused, in part, by various rules applicable to different types of SFFAs. These rules are examined below.

General Valuation Principles

The value of an SFFA is normally its fair market value, which can be determined from a "reasonable estimate."[125] The preamble to the Temporary Regulations confirms how lax this standard can be:

> A specified person may determine the fair market value of a specified foreign financial asset based on information publicly available from reliable financial information sources or from other verifiable sources. Even if there is no information from reliable financial information sources regarding the fair market value of a reported asset, the regulations *do not require a specified person to obtain an appraisal by a third party in order to reasonably estimate the asset's fair market value*.[126]

The Instructions for Form 8938 confirm these relaxed valuation rules, stating that "[a]n appraisal by a third party is not necessary to estimate the maximum fair market value during the year."[127]

Commentators to the Temporary Regulations asked to incorporate this nonappraisal rule directly in the Final Regulations, but the IRS declined to do so on grounds that other guidance, described above, "adequately addresses" the issue.[128] Commentators also requested more clarity on the concept of a "reasonable estimate" of the fair market value of an SFFA, to which the IRS indicated that it had already concluded that "the reasonable estimate standard is an appropriately flexible one that will result in helpful information for the IRS with respect to a wide range of assets, while not proving unduly burdensome for taxpayers" and that "valuation is an inherently factual inquiry, and it is not feasible to devise detailed rules that clearly describe outcomes that are appropriate for a broad range of factual situations."[129] The IRS also rejected the request by commentators for a "presumptive standard" to be applied when trying to determine the fair market value of hard-to-value SFFAs, such as illiquid assets like contractual rights and interests in private entities.[130]

Valuation of Foreign Currency

Building on the preceding general rule, the Final Regulations provide specifics for valuing different types of SFFAs. For instance, with respect to valuing foreign currency, they instruct SIs to use the Treasury Department's Bureau of the Fiscal Service foreign currency exchange rate.[131] If no such rate is available, then SIs can utilize another publicly available currency exchange, though the source must be expressly disclosed on Form 8938.[132] In terms of timing, the Final Regulations clarify that SIs should use the applicable foreign currency exchange rate on the last day of the relevant year, even if the SI sold or otherwise disposed of an SFFA before the last day of the year.[133]

Valuation of Foreign Accounts

In the case of foreign accounts, an SI can rely on "periodic account statements provided at least annually" to determine the maximum value, unless the SI knows or has reason to know, based on readily accessible information, that the statements do not reflect a reasonable estimate of the maximum account balance during the year.[134]

Valuation of Other SFFAs

When it comes to SFFAs other than foreign accounts, the Final Regulations provide that an SI may use the value of the asset on the last day of the year in which the SI held an interest, except in situations where the SI has actual or constructive knowledge, based on readily accessible information, that such year-end value does not constitute a reasonable estimate of the maximum value.[135] The Instructions for Form 8938 illustrate this idea with the following example:

> I have publicly traded foreign stock not held in a financial account that has a fair market value as of the last day of the tax year of $100,000, although, based on daily price information that is readily available, the 52-week high trading price for the stock results in a maximum value of the stock during the year of $150,000. If you are required to file Form 8938, the maximum value of the foreign stock to be reported is $150,000, based on readily available information of the stock's maximum value during the tax year.[136]

Valuation of Foreign Trusts

The rules regarding valuation of foreign trusts considered SFFAs are different. If the SI is a beneficiary of a foreign trust, then the maximum value of his interest is the sum of (i) the fair market value, determined on the last day of the relevant year, of all the currency and other property distributed by the trust during the year to the SI as a beneficiary; plus (ii) the fair market value, determined on the last day of the relevant year, of the SI's right as a beneficiary to receive mandatory distributions from the trust.[137]

Valuation of Foreign Estates, Pension Plans and Deferred Compensation Plans

The Final Regulations simplify the valuation process when it comes to interests in foreign estates, foreign pension plans and foreign deferred compensation plans. They say to report the fair market value of the SI's interest in the assets as determined on the last day of the relevant year.[138] If this information is not readily accessible and the SI does not otherwise have it, then the SI is directed to use the year-end fair market value of the currency and other property that was distributed to the SI as a beneficiary or participant during the year.[139] The IRS provided further guidance about these valuations on its webpage called "Basic Questions and Answers on Form 8938," as follows:

> *How do I value my interest in a foreign pension or deferred compensation plan for purposes of reporting this on Form 8938?* In general, the value of your interest in the foreign pension plan or deferred compensation plan is the fair market value of your beneficial interest in the plan on the last day of the year. However, if you do not know or have reason to know based on readily accessible information the fair market value

of your beneficial interest in the pension or deferred compensation plan on the last day of the year, the maximum value is the value of the cash and/or other property distributed to you during the year. This same value is used in determining whether you have met your reporting threshold.

If you do not know or have reason to know based on readily accessible information the fair market value of your beneficial interest in the pension plan or deferred compensation plan on the last day of the year *and* you did not receive any distributions from the plan, the value of your interest in the plan is zero. In this circumstance, you should also use a value of zero for the plan in determining whether you have met your reporting threshold. If you have met the reporting threshold and are required to file Form 8938, you should report the plan and indicate that its maximum is zero.[140]

Commentators to the Temporary Regulations suggested that the value of interests in foreign pension and foreign deferred compensation plans should not be considered to be readily ascertainable if the SI has no current rights to withdraw assets without penalty. The IRS declined this suggestion in issuing the Final Regulations because it would have the effect of having an SI's interest in a foreign pension or deferred compensation plan being valued at $0 if the SI has no right to withdraw, even if the SI regularly receives statements indicating the fair market value of the interest. The IRS finds such result inconsistent with the rationale for requiring the reporting of the maximum value of an SFFA.[141]

Valuation of SFFAs with No Value or a Negative Value

The Final Regulations state that an SFFA is subject to reporting on Form 8938 even if it does not have a positive value.[142] This would not occur, of course, unless the aggregate value of all SFFAs exceeded the applicable threshold.

The Final Regulations further clarify that in situations where the maximum value of an SFFA is less than $0, its value is treated as $0 for purposes of determining the aggregate value of the SFFAs in which the SI has an interest.[143] This guidance prevents taxpayers from using an SFFA with a negative value to offset other SFFAs with positive values.

Valuation of SFFAs Exempt from Reporting on Form 8938

As explained earlier in this article, certain SFFAs are exempt reporting on Form 8938, despite the fact that they meet all the regular criteria for reporting. These unique filing exemptions apply to (i) SFFAs that the SI already reported to the IRS on information returns other than the Form 8938, such as Forms 3520, 3520-A, 5471, 8621, 8865 or 8891; (ii) certain SFFAs held by SIs in Puerto Rico and American Samoa; (iii) certain SFFAs held by a foreign grantor trust properly reported to the IRS; and (iv) SFFAs held by certain types of domestic trusts.

Just because an SFFA is exempt from reporting on Form 8938 does not necessarily mean that it can be disregarded when it comes to valuing SFFAs in order to determine whether an SI surpasses the applicable reporting threshold. The regulations create two distinct valuation-related rules in this regard.

On one hand, the value of any SFFA that is exempt from reporting on Form 8938 because of Reg. §1.6038D-7(a) (*i.e.*, SFFAs that the SI already reported to the IRS on information returns other than the Form 8938, such as Forms 3520, 3520-A, 5471, 8621, 8865 or 8891, and certain SFFAs held by a foreign grantor trust properly reported to the IRS) *is included* for purposes of determining the aggregate value.[144] Thus, just because an SI is not required to report on Form 8938 details about his ownership in a controlled foreign corporation because the SI already disclosed such data on his Form 5471, does not mean that the value of his interest in the controlled foreign corporation (which is an "other SFFA") is ignored by the SI when calculating whether the total value of all SFFAs exceeds the applicable reporting threshold, such that he will be required to file Form 8938.

On the other hand, the value of any SFFA that is exempt from reporting on Form 8938 because of Reg. §1.6038D-7(b) or (c) (*i.e.*, certain SFFAs held by SIs in Puerto Rico and American Samoa and SFFAs held by certain domestic trusts specified in the regulations) *is excluded* when it comes to calculating the aggregate value.[145] For example, if an SI holds an interest in certain domestic grantor trusts, he is not required to include the value of the SFFAs held through the trusts for purposes of measuring the total value of his SFFAs, and he is not obligated to report the SFFAs held through the trusts on Form 8938, even if he must file Form 8938 because the total value of his SFFAs (not counting those held through the domestic grantor trusts) exceeded the applicable reporting threshold.

Valuation of Jointly Owned SFFAs

Unique rules also exist in cases of jointly owned SFFAs.

General Rule

Generally, each SI who is a joint owner of an SFFA (i) must include the entire value of the SFFA (and not just the

value of the SI's partial interest in an SFFA) for purposes of determining whether the aggregate value of the SFFAs exceeds the reporting thresholds, and (ii) must report the entire value of the jointly owned SFFA on Form 8938.[146] As the Instructions for Form 8938 warn, "[i]f you jointly own an asset with someone else, the value that you use to determine the total value of all of your [SFFAs] depends on whether the other owner is your spouse and, if so, whether your spouse is [an SI] and whether you file a joint or separate return."[147]

Special Rules Affecting Married Individuals

Special Married Rule #1

Married SIs who file *joint* Forms 1040 must count only once the value of an SFFA that they jointly own for purposes of calculating whether the aggregate value of all SFFAs in which either spouse holds an interest exceeds the reporting thresholds.[148]

Special Married Rule #2

In a situation where both spouses are SIs, they hold joint SFFAs and they file *separate* Form 1040, then each SI includes one-half of the value of the SFFA in determining whether he or she has an interest in SFFAs whose aggregate value surpasses the reporting thresholds.[149]

Special Married Rule #3

Where only one spouse is an SI, the spouses hold joint SFFAs and the spouses file *separate* Forms 1040, the SI must include the entire value of the SFFA in determining whether he or she has an interest in SFFAs whose aggregate value surpasses the reporting thresholds.[150]

Examples of Special Married Rules

The special valuation rules pertaining to married individuals are illustrated by the following examples crafted by the IRS:

> *Facts*. Two married specified individuals, H and W, jointly own a specified foreign financial asset with a value of $90,000 at all times during the taxable year. H separately has an interest in a specified foreign financial asset with a value of $10,000 at all times during the taxable year. W separately has an interest in a specified foreign financial asset with a value of $1,000 at all times during the taxable year.
>
> *Married SIs Filing Separate Forms 1040*. If H and W file separate annual returns, the aggregate value of the specified foreign financial assets in which H has an interest at the end of the taxable year is $55,000, comprising one-half of the value of the jointly owned asset, $45,000, and the value of H's separately owned specified foreign financial asset, $10,000. The aggregate value of the specified foreign financial assets in which W has an interest at the end of the taxable year is $46,000, comprising one-half of the value of the jointly owned asset, $45,000, and the value of W's separately owned specified foreign financial asset, $1,000. H must file Form 8938 with his annual return for the taxable year because the aggregate value of the specified foreign financial assets in which H has an interest exceeds the applicable reporting threshold ($50,000) set forth in §1.6038D-2(a)(1). H must report the maximum value of the entire jointly owned asset, $90,000, and the maximum value of the separately owned asset, $10,000. See §1.6038D-5(b) regarding the maximum value of a jointly owned specified foreign financial asset to be reported by a specified person, including a married specified individual, that is a joint owner of an asset. The aggregate value of the specified foreign financial assets in which W has an interest, $46,000, does not exceed the applicable reporting threshold forth in §1.6038D-2(a)(1). W is not required to file Form 8938 with her separate annual return.
>
> *Married SIs Filing Joint Forms 1040*. If H and W file a joint annual return, they must file a single Form 8938 with their joint annual return for the taxable year because the aggregate value of all of the specified foreign financial assets in which either H and W have an interest ($90,000 (included only once), $10,000, and $1000, or $101,000) exceeds the applicable reporting threshold ($100,000) set forth in §1.6038D-2(a)(2). The single Form 8938 must report the maximum value of the jointly owned specified foreign financial asset, $90,000, and the maximum value of the specified foreign financial assets separately owned by H and W, $10,000 and $1,000, respectively.[151]

How Large/Valuable Must the SFFAs Be Before a Form 8938 Is Required?

Even if an individual is considered an SI and holds an interest in certain SFFAs during a given year, he is only required to file a Form 8938 if the aggregate value of the SFFAs surpasses certain reporting thresholds. This is easy to say but often hard to determine because the thresholds vary depending on an SI's location, civil status and return-filing status.

Description of Six Reporting Thresholds

1. *Unmarried SI living in the United States*. The SI must attach a Form 8938 to his Form 1040 if the aggregate value of the SFFAs exceeds (i) $50,000 on the last day of the year, or (ii) $75,000 at any time during year.[152]
2. *Unmarried SI living abroad*. An SI who is a "qualified individual" for purposes of Code Sec. 911 during the relevant year must attach a Form 8938 to his or her Form 1040 if the aggregate value of the SFFAs exceeds (i) $200,000 on the last day of the year, or (ii) $300,000 at any time during the year.[153] A "qualified individual" in the context of Code Sec. 911 is either a U.S. citizen who has been a *bona fide* resident of a foreign country or countries for an uninterrupted period that includes an entire calendar year or a U.S. citizen or U.S. resident who is present in a foreign country or countries at least 330 full days during any consecutive 12-month period.[154]
3. *Married SI living in the United States filing separate Form 1040 from his or her spouse*. The married SI must attach a Form 8938 to his separate Form 1040 if the aggregate value of the SFFAs exceeds (i) $50,000 on the last day of the year, or (ii) $75,000 at any time during year.[155]
4. *Married SI living abroad filing separate Form 1040 from his or her spouse*. The married SI who is a "qualified individual" for purposes of Code Sec. 911 during the relevant year must attach a Form 8938 to his or her separate Form 1040 if the aggregate value of the SFFAs exceeds (i) $200,000 on the last day of the year, or (ii) $300,000 at any time during the year.[156]
5. *Married SIs living in the United States and filing joint Forms 1040*. The married SIs must attach a Form 8938 to their joint Form 1040 if the aggregate value of the SFFAs exceeds (i) $100,000 on the last day of the tax year, or (ii) $150,000 at any time during the year.[157]
6. *Married SIs living abroad and filing joint Forms 1040*. The married SI who is a "qualified individual" for purposes of Code Sec. 911 during the relevant year and his or her spouse must attach a Form 8938 to their joint Form 1040 if the aggregate value of the SFFAs held by either spouse exceeds (i) $400,000 on the last day of the year, or (ii) $600,000 at any time during the year.[158]

Suggested Modifications to Reporting Thresholds

Commentators to the Temporary Regulations asked the IRS to raise the reporting thresholds for three different categories of SIs, namely, (i) those receiving assets (such as interests in foreign pension plans) in connection with the performance of personal services, (ii) employees seconded to companies in the United States by foreign employers, and (iii) individuals who do not qualify for the foreign earned income exclusion under Code Sec. 911. The IRS declined to adopt any of these requests in issuing the Final Regulations on various grounds, practical and administrative.[159]

Examples Provided by the IRS

The reporting thresholds, like other aspects of Form 8938, are intricate. In an effort to clarify these issues, the Instructions for Form 8938 contain the following illustrations to help taxpayers decide whether filing is required:

- *I am not married and do not live abroad. The total value of my specified foreign financial assets does not exceed $49,000 during the tax year.* You do not have to file Form 8938. You do not satisfy the reporting threshold of more than $50,000 on the last day of the tax year or more than $75,000 at any time during the year.[160]
- *I am not married and do not live abroad. I sold my only specified foreign financial asset on October 15, when its value was $125,000*. You have to file Form 8938. You satisfy the reporting threshold even though you do not hold any specified foreign assets on the last day of the tax year because you did own specified foreign financial assets of more than $75,000 at any time during the tax year.[161]
- *I am not married and do not live abroad. An unrelated U.S. resident and I jointly own a specified foreign financial asset valued at $60,000***.** You each have to file Form 8938. You each satisfy the reporting threshold of more than $50,000 on the last day of the tax year.[162]
- *I am not married and do not live abroad. I own an entity disregarded for tax purposes, which owns one specified foreign financial asset valued at $30,000. In addition, I own a specified foreign financial asset valued at $25,000.* You have to file Form 8938. You own both the specified foreign financial asset owned by the disregarded entity and the specified foreign financial asset you own directly, for a total value of $55,000. You satisfy the reporting threshold of more than $50,000 on the last day of the tax year.[163]
- *My spouse and I do not live abroad and file a joint income tax return. We jointly own a single specified foreign financial asset valued at $60,000*. You and your spouse do not have to file Form 8938. You do not satisfy the reporting threshold of more than $100,000 on the last day of the tax year or more than $150,000 at any time during the tax year.[164]
- *My spouse and I do not live abroad, file a joint income tax return, and jointly and individually own specified*

foreign financial assets. On the last day of the tax year, my spouse and I jointly own a specified foreign financial asset with a value of $90,000. My spouse has a separate interest in a specified foreign financial asset with a value of $10,000. I have a separate interest in a specified foreign financial asset with a value of $1,000. You and your spouse have to file a combined Form 8938. You and your spouse have an interest in specified foreign financial assets in an amount of $101,000 on the last day of the tax year. This is the entire value of the specified foreign financial asset that you jointly own, $90,000, plus the value of the asset that your spouse separately owns, $10,000, plus the value of the asset that you separately own, $1,000. You and your spouse satisfy the reporting threshold of more than $100,000 on the last day of the tax year.[165]

- *My spouse and I do not live abroad, file separate income tax returns, and jointly own a specified foreign financial asset valued at $60,000 for the entire year.* Neither you nor your spouse has to file Form 8938. You each use one-half of the value of the asset, $30,000, to determine the total value of the specified foreign financial assets that you each own. Neither of you satisfies the reporting threshold of more than $50,000 on the last day of the tax year or more than $75,000 at any time during the year.[166]
- *My spouse and I file separate income tax returns, jointly and individually own specified foreign financial assets, and do not live abroad. On the last day of the tax year, my spouse and I jointly own a specified foreign financial asset with a value of $90,000. My spouse has a separate interest in a specified foreign financial asset with a value of $10,000. I have a separate interest in a specified foreign financial asset with a value of $1,000.* You do not have to file Form 8938, but your spouse does. Your spouse has an interest in specified foreign financial assets in the amount of $55,000 on the last day of the tax years. This is one-half of the value of the asset that you jointly own, $45,000, plus the entire value of the asset that your spouse separately owns, $10,000. You have an interest in specified foreign financial assets in the amount of $46,000 on the last day of the tax year. This is one-half of the value of the asset that you jointly own, $45,000, plus the entire value of the asset that you separately own, $1,000. Your spouse satisfies the reporting threshold of more than $50,000 on the last day of the tax year. You do not satisfy the reporting requirement of more than $50,000 on the last day of the tax year or more than $75,000 at any time during the tax year.[167]
- *My spouse and I are U.S. citizens but live abroad for the entire tax year and file a joint income tax return. The total value of our combined specified foreign financial assets on any day of the tax year is $150,000.* You and your spouse do not have to file Form 8938. You do not satisfy the reporting threshold of more than $400,000 on the last day of the tax year or more than $600,000 at any time during tax year for married individuals who live abroad and file a joint income tax return.[168]
- *My spouse and I live abroad and file separate income tax returns. My spouse is not a specified individual. On the last day of the tax year, my spouse and I jointly own a specified foreign financial asset with a value of $150,000. My spouse has a separate interest in a specified foreign financial asset with a value of $10,000. I have a separate interest in a specified foreign financial asset with a value of $60,000.* You have to file Form 8938, but your spouse, who is not a specified individual, does not. You have an interest in specified foreign financial assets in the amount of $210,000 on the last day of the tax year. This is the entire value of the asset that you jointly own, $150,000, plus the entire value of the asset that you separately own, $60,000. You satisfy the reporting threshold for a married individual living abroad and filing a separate return of more than $200,000 on the last day of the tax year.[169]

Overlap of Form 8938 and the FBAR

As explained above, the IRS relieves taxpayers from filing duplicative data to the IRS by exempting from Form 8938 information about SFFAs that an SI has already supplied to the IRS in other international information returns, such as Forms 3520, 3520-A, 5471, 8865 and 8891. One item conspicuously absent from this list of information returns is the FBAR, and this is intentional. Taxpayers and practitioners have complained about the compliance burden from the outset, and the government has always been cognizant of the issue. The following information demonstrates that the Form 8938 and the FBAR will continue to co-exist for the foreseeable future.

Legislative history to Code Sec. 6038D from early 2010 shows that Congress has been aware of this situation from the beginning: "Although the nature of the information required [on Form 8938] is similar to the information disclosed on an FBAR, it is not identical … Nothing in [Code Sec. 6038D] is intended as a substitute for compliance with the FBAR reporting requirements, which are unchanged by [Code Sec. 6038D]."[170]

Later, in June 2011, when the IRS issued provisional guidance about Code Sec. 6038D in Notice 2011-55,

it confirmed the dual-filing requirement: "Compliance with Sections 6038D … does not relieve a person of the responsibility to file Form TD F 90-22.1, Report of Foreign Bank and Financial Accounts, (FBAR) if the FBAR is otherwise required to be filed."[171]

Likewise, when the IRS first released the official Instructions for Form 8938 in 2011, they contained the following words of caution: "Filing Form 8938 does not relieve you of the requirement to file Form TD F 90-22.1, Report of Foreign Bank and Financial Accounts (FBAR), if you are otherwise required to file Form TD F 90-22.1."[172]

Shortly thereafter, in December 2011, the IRS issued the Temporary Regulations, the preamble to which features explanations and justifications:

> Reporting on Form TD F 90-22.1 is required under Title 31 (31 U.S.C. 5314) for other law enforcement purposes in addition to tax administration. As a consequence, different policy considerations apply to Form 8938 and FBAR reporting. These are reflected in the different categories of persons required to file Form 8938 and the FBAR, the different filing thresholds for Form 8938 and FBAR reporting, and the different assets (and accompanying information) required to be reported on each form. Although certain information may be reported on both Form 8938 and the FBAR, the information required by the forms is not identical in all cases, and reflects the different rules, key definitions (for example, "financial account"), and reporting requirements applicable to Form 8938 and FBAR reporting. These differing policy considerations were recognized during the passage of the HIRE Act and the enactment of section 6038D, and the intention to retain FBAR reporting notwithstanding the enactment of section 6038D was specifically noted in the Technical Explanation [of the HIRE Act by the U.S. Joint Committee on Taxation] … Against this background, reporting on Form 8938 and the FBAR is not duplicative and both forms must be filed, if required.[173]

The objections raised by taxpayers and practitioners grabbed the attention of certain lawmakers, as those heading the Senate Finance Committee and the Senate Judiciary Committee requested that the U.S. Government Accountability Office ("GAO") analyze potential duplicative reporting requirements triggered by Form 8938 and the FBAR.[174] The GAO issued a report in February 2012, concluding that the overlap increases compliance burden and creates confusion.[175]

There have been no surprises concerning this debate recently, with commentators to the Temporary Regulations asking the IRS to excuse SIs from including on Form 8938 any information about foreign accounts that it has already provided on an FBAR, and with the IRS rejecting these requests.[176] For the majority of taxpayers who do not pass their days scouring dense tax regulations, the IRS presented this issue in a straightforward way. It warned the following in the most recent Instructions for Form 8938: "Filing Form 8938 does not relieve you of the requirement to file FinCEN Form 114 (Report of Foreign Bank and Financial Accounts)(FBAR), if you are otherwise required to file the FBAR."[177]

The Importance of Code Sec. 6038D and Form 8938

Taxpayers and practitioners who lack a profound passion for international tax compliance and procedure might be inclined at this point to surrender, throw up their hands with frustration, put down some information about foreign assets on Form 8938 and simply hope for the best. This option, while appealing, likely would trigger some or all of the negative consequences described below.

Penalties for Violating Code Sec. 6038D

General Rule

The most obvious reason why Code Sec. 6038D matters is that noncompliance triggers new civil penalties. Like other penalties in the international arena, this one comes in layers. If the taxpayer fails to file the Form 8938 in a timely manner, then he "shall" pay a penalty of $10,000.[178] The penalty increases if the taxpayer does not rectify the problem quickly after contact from the IRS. In particular, if the taxpayer has not filed a Form 8938 within 90 days after the day on which the IRS sends a notice about the missing return, then, in addition to the initial penalty of $10,000, the taxpayer "shall" pay another penalty of $10,000 for each 30-day period (or portion thereof) during which he fails to file the Form 8938, with a maximum penalty of $50,000.[179]

Penalties for Married SIs

Married individuals who file joint Forms 1040 and neglect to enclose a Form 8938 are penalized just once. In this regard, the Final Regulations clarify that such taxpayers are subject to penalties "as if the married [SIs] are a single [SI]."[180] The Final Regulations note, however, that the penalties on joint taxpayers are joint and several, such that the IRS can take collection actions against either taxpayer.[181]

Presumption of Violation

Code Sec. 6038D(e) and the Final Regulations create a presumption of noncompliance in certain situations. Specifically, if the IRS determines that an SI holds an interest in one or more SFFAs but fails to provide sufficient information to prove the aggregate value of the SFFAs, then the IRS is allowed to presume that the value exceeds the applicable reporting threshold and assert the $10,000 penalty.[182]

Penalty Waiver in Cases of Reasonable Cause

An SI who unintentionally fails to file a timely, accurate Form 8938 can avoid penalties under Code Sec. 6038D if he can demonstrate that the violation was due to reasonable cause and not due to willful neglect.[183] The Final Regulations clarify that the SI bears the burden of making "an affirmative showing of all the facts alleged as reasonable cause."[184] The Final Regulations also emphasize that civil or criminal penalties threatened or imposed by a foreign country against the SI (or any other person) for disclosing the information on the Form 8938 does not constitute reasonable cause.[185]

Comments about Penalty Rules

Commentators made assorted suggestions about the penalty rules in the Temporary Regulations. These included: (i) having the IRS incorporate into the Final Regulations "objective examples" of when a taxpayer would be considered to have "reasonable cause" for not filing a Form 8938; (ii) waiving penalties for Form 8938 violations where all SFFAs were otherwise reported to the IRS on timely Forms 3520, 3520-A, 5471, 8865 or 8621; (iii) adopting a blanket first-time penalty abatement; (iv) halting the $10,000-per-month penalty for continuing violations once the SI furnishes to the IRS proof that he has requested all the data necessary to ultimately complete and file Form 8938; (v) utilizing a range of penalties, commiserate with the severity of the violation, instead of a flat penalty of $10,000; and (vi) establishing that an SI could not be penalized more than once for failing to report an SFFA on multiple international information return, such as a penalty of $10,000 for not reporting a controlled foreign corporation on Form 5471 and another $10,000 for not reporting data about the same corporation on Form 8938.[186] The IRS did not adopt these suggestions in issuing the Final Regulations, indicating that all penalty issues concerning Form 8938, including the existence or absence of "reasonable cause," will be resolved in accordance with the general standards set forth in the IRS's Penalty Handbook, located within the Internal Revenue Manual.[187]

Penalties Doubled for Tax Underpayments Related to Unreported SFFAs

Code Sec. 6038D also matters because, in addition to subjecting violators to specialized penalties under Code Sec. 6038D, transgressions could also lead to other civil penalties.[188] Code Sec. 6662(a) generally provides that if there is a tax underpayment on any return, then the IRS may assert a penalty equal to 20 percent of the amount of such underpayment.[189] Code Sec. 6662(b) lists the items that give rise to tax underpayments susceptible to penalties. FATCA expanded this penalty regime by adding Code Sec. 6662(b)(7), which says that any "undisclosed foreign financial asset understatement" can be grounds for an accuracy-related penalty.

To appreciate this new brand of penalty, one must turn to the other provision introduced by FATCA, Code Sec. 6662(j). This statute does several things. For example, it defines an "undisclosed foreign financial asset understatement" as the portion of a tax understatement for a tax year that is attributable to any transaction involving an "undisclosed foreign financial asset."[190] It also describes the term "undisclosed foreign financial asset" as any asset with respect to which information was required to be reported to the IRS under various tax provisions, including Code Sec. 6038D, but was not reported.[191] Finally, this provision doubles the size of the accuracy-related penalty, providing that, in the case of any tax underpayment due to an "undisclosed foreign financial asset" (such as an SFFA not reported on a Form 8938), the penalty jumps from 20 percent of the underpayment to 40 percent.[192] The legislative history clarifies the applicability of these rules in light of the new Form 8938:

> An understatement is attributable to an undisclosed foreign financial asset if it is attributable to any transaction involving such asset. Thus, a U.S. person who fails to comply with various self-reporting requirements for a foreign financial asset and engages in a transaction with respect to that asset incurs a penalty on any resulting underpayment that is double the otherwise applicable penalty for substantial understatements or negligence. For example, if a taxpayer fails to disclose amounts held in a foreign financial account, any underpayment of tax related to the transaction that gave rise to the income would be subject to the penalty provision, as would any underpayment related to interest, dividends, or other returns accrued on such undisclosed amounts.[193]

The Instructions to Form 8938 contain additional information about the application of the strengthened accuracy-related penalty under Code Sec. 6662, providing examples

of transactions involving undisclosed SFFAs: (i) "You do not report ownership of shares in a foreign corporation on Form 8938 and you received taxable distributions from the company that you did not report on your income tax return"; (ii) "You do not report ownership of shares in a foreign company on Form 8938 and you sold the shares in the company for a gain and did not report the gain on your income tax return"; and (iii) "You do not report a foreign pension on Form 8938 and you received a taxable distribution form the pension plan that you did not report on your income tax return."[194]

Do Not Forget the Criminal Penalties

Code Sec. 6038D is also important because, aside from taking a big bite out of a taxpayer's pocketbook for civil penalties, violations can lead to potential criminal penalties. Lest there be any doubt in this regard, the Final Regulations explain that "[i]n addition to other penalties, failure to comply with the reporting requirements of Section 6038D and the regulations, or any underpayment related to such failure, may result in criminal penalties under Sections 7201, 7203, 7206, *et seq.*, or other provisions of Federal law."[195] Similarly, the Instructions for Form 8938 warn taxpayers that "if you fail to file Form 8938, fail to report an asset, or have an underpayment of tax, you may be subject to criminal penalties."[196]

Extension of the Assessment Period

The importance of Code Sec. 6038D derives from its impact on assessment periods, too. FATCA modified the assessment period rules under Code Sec. 6501 in two major ways: It modified the existing Code Sec. 6501(c)(8) to insert violations of Code Sec. 6038D, and it added a new Code Sec. 6501(e)(1)(A) concerning "substantial omissions" of income from returns. These two modifications are discussed further below.

Unlimited Assessment Period if Form 8938 Not Filed

The general rule is that the IRS has three years from the time a taxpayer files his tax return for the IRS to audit him and propose adjustments.[197] There are various exceptions to the normal three-year rule. One such exception applies to situations where a taxpayer fails to file an information return with the IRS regarding particular foreign entities, transfers or assets.[198] Code Sec. 6501(c)(8), before the enactment of FATCA, stated the following:

> In the case of any information which is required to be reported to the Secretary [under various international tax provisions, but not Section 6038D], the time for assessment of any tax imposed by [the Internal Revenue Code] with respect to any event or period or period to which such information relates shall not expire before the date which is 3 years after the date on which the Secretary is furnished the information required to be reported … .[199]

Congress changed the preceding exception in two major ways with FATCA. The first way is that Congress specifically identified Code Sec. 6038D as one of the relevant international tax provisions. The second way, which was more subtle, is that Congress added the phrase "tax return," such that under Code Sec. 6501(c)(8), the IRS now has additional time to assess taxes and penalties with respect to any "tax return, event, or period" to which the omitted information relates. Thus, if an SI neglects to file a Form 8938 or files an incomplete Form 8938, then the assessment period essentially stays open indefinitely with respect to the *entire tax return*. This expansive notion is supported by legislative history, which contains the following explanation:

> [Code Sec. 6501(c)(8)] also suspends the limitations period for assessment if a taxpayer fails to provide timely information with respect to … the new self-reporting of financial assets. The limitations period will *not* begin to run until the information required … has been furnished to the Secretary. [Code Sec. 6501(c)(8)] also clarifies that the extension is *not* limited to adjustments of income related to the information required to be reported by one of the enumerated sections.[200]

Notably, Code Sec. 6501(c)(8)(B), which was added in 2010 by separate legislation, clarifies that the extended assessment period applies even if the taxpayer's failure to file Form 8938 was unintentional. However, in such instances, the only open issues are those related to the Form 8938 itself, not the entire Form 1040 to which the Form 8938 should have been attached.[201]

In late 2011, the IRS released a Chief Counsel Advisory clarifying and confirming the points above about the extended assessment period.[202] Particularly helpful in such IRS guidance is the following example illustrating how the former version and current version of Code Sec. 6501(c)(8) could apply to a single taxpayer:

> Taxpayer timely filed tax returns for the tax years 2004 through 2009 but failed to properly include a Form 5471 with each return. Under the general limitations period provided in Section 6501(a), only the assessment

periods for the 2008 and 2009 tax years remain open under the general three-year limitations period.

For the 2004 and 2005 tax years, it is assumed that the general three-year assessment period for each year had expired before 3/18/2010, the effective date of the recent amendments to Section 6501(c)(8). Accordingly, based on the [IRS's] prior application of 6501(c)(8), the assessment statute remains open for these tax years *only with respect to any item(s) related to the failure to provide the required information*.

For the 2006 through 2009 tax years, *the assessment limitations period remains open indefinitely with respect to all items on the tax returns for each of these tax years* … However, if the taxpayer can establish that the failure to file the required form was due to reasonable and not willful neglect for any of these tax years, then the limitations period *is only extended with respect to those items related to the failure to furnish the required information*.[203]

Six-Year Assessment Period for Certain Income Omissions

In addition to modifying the existing rules of Code Sec. 6501(c)(8), FATCA also added new Code Sec. 6501(e)(1)(A) about "substantial omissions" of income from returns. The new provision states that if (i) a taxpayer omits from gross income amounts that should have been included, and (ii) such omitted amount exceeds 25 percent of the gross income actually reported on the return, or (iii) such omitted amount is attributable to one or more SFFAs that were required to be reported under Code Sec. 6038D (or that would have been required to be reported if Code Sec. 6038D were applied without regard to the reporting threshold specified in Code Sec. 6038D(a) and without regard to any filing exemptions in Code Sec. 6038(h)) and exceeds $5,000, then the tax may be assessed within six years of the time the relevant Form 1040 was filed.[204] The legislative history provides additional background about this extended assessment period:

> In providing that the applicability of Section 6038D information reporting requirements is to be determined without regard to the statutory or regulatory exceptions, the statute ensures that the longer limitation period [*i.e.*, the six-year assessment period] applies to omissions of income with respect to transactions involving foreign assets owned by individuals. Thus, a regulatory provision that alleviates duplicative reporting obligations by providing that [an information return] that complies with another provision of the Code may satisfy one's obligations under new Section 6038D does not change the nature of the asset subject to reporting. The asset remains one that is subject to the requirements of Section 6038D for purposes of determining whether the exception to the three-year statute of limitation applies.[205]

Fighting the U.S. Government on Three Fronts Simultaneously

Code Sec. 6038D is particularly important because taxpayers violating this provision could find themselves fighting the U.S. government on three fronts simultaneously, engaged in a war of attrition against a rival with limitless resources. A simple example helps clarify this possibility.

Assume that Tommy Taxcheat held two foreign accounts during 2011 with an aggregate balance of approximately $2 million, which generated a total of $200,000 in interest income. Further assume that Tommy Taxcheat did not report the foreign-source income on his 2011 Form 1040, did not disclose the existence of the foreign accounts by checking the "yes" box on Schedule B of the 2011 Form 1040, did not enclose a Form 8938 with his 2011 Form 1040 and did not file a separate FBAR by the deadline of June 30, 2012. After conducting an audit of 2011, the IRS issues the following items to Tommy Taxcheat: (i) a Notice of Deficiency proposing increased taxes on the $200,000 of unreported income, a 40-percent accuracy-related penalty under new Code Sec. 6662(b)(7) and interest charges; (ii) an FBAR 30-day letter (*i.e.*, Letter 3709) and an FBAR Agreement to Assessment and Collection (*i.e.*, Letter 13449) asserting a penalty of $1 million, which constitutes the maximum sanction of 50 percent of the highest aggregate balance of the unreported foreign accounts[206]; and (iii) a Notice Letter (*i.e.*, Letter 4618) and/or Form 8278 (*Assessment and Abatement of Miscellaneous Civil Penalties*) asserting a penalty of $10,000 for failure to file a Form 8938 and warning of increased penalties of up to $50,000 for continued noncompliance.[207] Things could be considerably worse if the IRS decided to bring criminal charges, but we are assuming for purposes of this example that this route was not pursued.

If Tommy Taxcheat disputes all the proposed taxes and penalties, then he will become familiar with three different venues, as well as the costs of fighting in each.

First, Tommy Taxcheat may file a petition with the Tax Court to dispute the taxes and accuracy-related penalty proposed in the Notice of Deficiency.[208] Doing so delays the assessment of such amounts against Tommy Taxcheat until the conclusion of the Tax Court proceeding and any judicial appeal thereof.[209]

Second, because the FBAR penalty derives from Title 31 of the U.S. Code (*i.e.*, Money and Finance) as opposed to Title 26 of the U.S. Code (*i.e.*, the Internal Revenue

Code), it cannot be challenged in Tax Court.[210] Thus, after Tommy Taxcheat exhausts his administrative appeal rights with the IRS, the U.S. government, through the U.S. Department of Justice, will bring a civil collection against Tommy Taxcheat in U.S. district court.[211]

Third, given that penalties for not filing Form 8938 are not related to a tax deficiency, the IRS takes the position that they are not challengeable in Tax Court. Specifically, the IRS's internal guidance states that "[d]eficiency procedures under Subchapter B of Chapter 63 (relating to deficiency procedures for income, estate, gift, and certain excise taxes) do *not* apply to penalties discussed in this section."[212] This guidance is consistent with the Chief Counsel Advice 201226028, which explains that "[t]he Section 6038D penalty is not itself part of a deficiency, so it cannot be subject to deficiency procedures on that ground … [and] the Section 6038D penalty is not calculated on the basis of a tax that is itself subject to deficiency procedures; instead, the penalty is in specific amounts set forth in the statute. As a result, the Section 6038D penalty is assessable by the Service without following deficiency procedures first."

Methods for Resolving Form 8938 Violations

While reading this article, some taxpayers and/or their tax advisors will experience the "oh shoot" moment, *i.e.*, the dreaded instant when they realize that they have failed to fully comply with the Form 8938 filing requirement. The question, after the panic subsides, quickly becomes how does the taxpayer fix the problem?

Individual taxpayers who are approaching the IRS proactively now have the following main options, depending on particular facts of each case: (i) participate in the 2014 Streamline Foreign Offshore Procedure ("SFOP"); (ii) participate in the 2014 Streamline Domestic Offshore Procedure ("SDOP"); (iii) participate in the 2014 Offshore Voluntary Disclosure Program ("OVDP"); (iv) file delinquent FBARs on a penalty-free basis under the 2014 "Delinquent FBAR Submission Procedure"; or (v) file delinquent international information returns other than FBARs (including Forms 8938) on a penalty-free basis under the 2014 "Delinquent International Return Submissions Procedure." The SFOP, SDOP and OVDP are designed for taxpayers who have both income tax problems and information-reporting problems with the IRS, while the "Delinquent FBAR Submissions Procedure" and the "Delinquent International Return Submissions Procedure" only apply to situations where taxpayers solely have information-reporting infractions (*i.e.*, they did not omit foreign income and thus do not owe the IRS back taxes).

A detailed analysis of the eligibility criteria, filing and payment obligations, settlement terms and strategic considerations for each resolution method far exceeds the scope of this article, which is centered on Form 8938. The important thing is that taxpayers appreciate that various options exist, such that they can seek specialized legal and/or accounting assistance to solve any past noncompliance on the most favorable terms possible.

Conclusion

There is no way around it, international tax compliance issues, including challenges associated with Form 8938, are becoming more pervasive and complicated each year. Confronted with the increasing complexity, and frustrated with the lack of clear, consolidated, comprehensive guidance from the IRS, many taxpayers and tax professionals become fatalistic, resigning themselves to merely "doing their best" and hoping to avoid scrutiny by the IRS. This behavior, while entirely understandable, is not the best approach because, as this article demonstrates, running afoul of the Form 8938 filing requirement can spark a long list of serious, negative consequences for taxpayers.

The tax community appreciates the recent issuance of the Final Regulations in December 2014 and eagerly awaits further guidance from the IRS regarding Code Sec. 6038D and Form 8938, preferably in one centralized document. Until then, this article should serve as a comprehensive resource for taxpayers and practitioners coping with significant uncertainty about the reporting of foreign financial assets.

ENDNOTES

1 FATCA is a portion of The Hiring Incentives to Restore Employment Act (P.L. 111-147), enacted on March 18, 2010.

2 This current article supplements an earlier one on the same topic, Hale E. Sheppard, *The New Duty to Report Foreign Financial Assets on Form 8938: Demystifying the Complex Rules and Severe Consequences of Noncompliance*, International Tax J., May–June 2012, at 11.

3 Reg. §1.6038D-1(a)(1) and (2). Interestingly, the Treasury Department takes the complete opposite approach with respect to FBAR requirements for nonresident aliens choosing to be treated as U.S. residents for tax purposes. The preamble to the most recent FBAR regulations states the following: "Commentators also sought clarification about the interaction of elections under Section 6013(g) and (h) of the Internal Revenue Code and the definition of resident. FinCEN wishes to clarify that the determination of whether an individual is a United States resident [for FBAR purposes] should be made without regard to elections under Section 6013(g) or (h) of the Internal Revenue Code." *See* 76 Fed. Reg. 10238 (Feb. 24, 2011).

4 T.D. 9657, IRB 2014-13, 687, Preamble to Temporary Regulations, 76 Fed. Reg. 78555 (Dec.

19, 2011).

[5] Instructions for Form 8938 (November 2011), pg. 2.

[6] Preamble to Final Regulations, 76 Fed. Reg. 73818 (Dec. 12. 2014).

[7] Preamble to Final Regulations, 76 Fed. Reg. 73818 (Dec. 12. 2014). The Treasury Department takes the complete opposite approach with respect to FBAR requirements of dual-resident taxpayers. The preamble to the most recent FBAR regulations states the following: "A legal permanent resident who elects under a tax treaty to be treated as a non-resident for tax purposes must still file the FBAR." 76 Fed. Reg. 10238 (Feb. 24, 2011).

[8] Reg. §1.6038D-2(e)(1), (2), and (3).

[9] Reg. §1.6038D-2(a)(7)(i).

[10] Instructions to Form 8938 (December 2014), pg. 1.

[11] Code Sec. 6012(a).

[12] T.D. 9657, IRB 2014-13, 687, Preamble to Temporary Regulations, 76 Fed. Reg. 78555 (Dec. 19, 2011).

[13] Preamble to Final Regulations, 76 Fed. Reg. 73818 (Dec. 12. 2014).

[14] Preamble to Final Regulations, 76 Fed. Reg. 73818 (Dec. 12. 2014).

[15] Code Sec. 441; Reg. §1.441-1.

[16] Reg. §1.6038D-2(a)(9).

[17] Instructions for Form 8938 (December 2014) pg. 5. These examples have been slightly altered to provide additional clarity.

[18] 31 C.F.R. § 1010.350(e)(1).

[19] 31 C.F.R. § 1010.350(e)(2).

[20] Reg. §1.6038D-2(b)(1).

[21] Reg. §1.6038D-2(b)(1).

[22] Reg. §1.6038D-2(a)(8).

[23] Reg. §1.6038D-2(b)(4)(i).

[24] T.D. 9657, IRB 2014-13, 687, Preamble to Temporary Regulations, 76 Fed. Reg. 78555 (Dec. 19, 2011).

[25] Instructions for Form 8938 (December 2014), pg. 4.

[26] Preamble to Final Regulations, 76 Fed. Reg. 73819 (Dec. 12, 2014).

[27] Reg. §1.6038D-2(b)(4)(ii). This rule does not apply to domestic liquidating trusts under Reg. §301.7701-4(d) created pursuant to a court order issued in a Chapter 7 bankruptcy, a confirmed plan in a Chapter 11 bankruptcy, or a domestic widely held fixed investment trust under Reg. §1.671-5.

[28] Reg. §1.6038D-2(b)(3).

[29] Instructions for Form 8938 (December 2014), pg. 5.

[30] Preamble to Final Regulations, 76 Fed. Reg. 73819 (Dec. 12, 2014).

[31] Reg. §1.6038D-2(b)(2).

[32] Reg. §1.6038D-2(b)(2).

[33] Code Sec. 6038D(b)(1); Reg. §1.6038D-3(a)(1).

[34] Code Sec. 6038D(b)(2); Reg. §1.6038D-3(b)(1).

[35] Instructions for Form 8938 (Rev. December 2014), pg. 4.

[36] Reg. §1.6038D-1(a)(7)

[37] Reg. §1.1471-5(b)(1)(i); Reg. §1.1471-5(b)(3)(i).

[38] Reg. §1.1471-5(b)(1)(ii); Reg. §1.1471-5(b)(3)(ii).

[39] Reg. §1.1471-5(b)(1)(iii); Reg. §1.1471-5(b)(3)(iii)(iv).

[40] Reg. §1.1471-5(b)(1)(iv); Reg. §1.1471-5(b)(3)(vii); Reg. §1.1471-5(b)(2)(v).

[41] Preamble to Final Regulations, 76 Fed. Reg. 73820 (Dec. 12, 2014).

[42] Reg. §1.1471-5(b)(2)(i)(A) and (B).

[43] Reg. §1.1471-5(b)(2)(i)(D); *See also* Reg. §1.6038D-3(a)(7).

[44] The regulations under Code Sec. 1471, which are specifically cross-referenced by the Final Regulations under Code Sec. 6038D, state that an account that is excluded from the definition of "financial account" under an IGA will not be considered a "financial account" for purposes of Form 8938. However, the Final Regulations and the Preamble thereto later make it clear that that the IRS intends to disregard the IGA definitions and exceptions when it comes to obligating SIs to file Forms 8938. *See* Reg. §1.1471-5(b)(2)(vi); Reg. §1.6038D-1(a)(7); Preamble to Final Regulations, 76 Fed. Reg. 73819-73820 (Dec. 12, 2014).

[45] Preamble to Final Regulations, 76 Fed. Reg. 73819-73820 (Dec. 12, 2014).

[46] Reg. §1.1471-5(b)(2)(ii).

[47] Reg. §1.1471-5(b)(2)(iii).

[48] Reg. §1.1471-5(b)(2)(iv).

[49] Reg. §1.1471-5(b)(2)(v).

[50] Reg. §1.1471-5(b)(2)(vi).

[51] Reg. §1.6038D-3(a)(3)(i).

[52] Reg. §1.6038D-3(a)(3)(i); Reg. §1.6049-5(c)(5)(i); T.D. 9657, IRB 2014-13, 687, Preamble to Temporary Regulations, 76 Fed. Reg. 78556 (Dec. 19, 2011); Instructions for Form 8938 (December 2014), pg. 6. The IRS defines "U.S. payor" by directing taxpayers to the regulations under an unrelated tax provision, Section 6049.

[53] Instructions for Form 8938 (Rev. December 2014), pg. 6.

[54] Reg. §1.6038D-3(a)(3)(ii); Reg. §1.6038D-3(b)(2).

[55] Reg. §1.6038D-1(a)(8) and (9); Code Sec. 1471(d)(5); Reg. §1.1471-5(d).

[56] Code Sec. 6038D(b)(2); Reg. §1.6038D-3(b)(1).

[57] T.D. 9657, IRB 2014-13, 687, Preamble to Temporary Regulations, 76 Fed. Reg. 78556 (Dec. 19, 2011).

[58] Reg. §1.6038D-3(d).

[59] T.D. 9657, IRB 2014-13, 687, Preamble to Temporary Regulations, 76 Fed. Reg. 78556 (Dec. 19, 2011); *See also* Instructions for Form 8938 (December 2014), pg.4., which state that "[a] n interest in social security, social insurance, or other similar program of a foreign government is not a specified foreign financial asset."

[60] Preamble to Final Regulations, 76 Fed. Reg. 73821 (Dec. 12, 2014)

[61] Reg. §1.6038D-3(c).

[62] Reg. §1.6038D-3(c).

[63] Preamble to Final Regulations, 76 Fed. Reg. 73821 (Dec. 12, 2014).

[64] Preamble to Final Regulations, 76 Fed. Reg. 73821 (Dec. 12, 2014).

[65] Preamble to Final Regulations, 76 Fed. Reg. 73821 (Dec. 12, 2014).

[66] Codes Sec. 6038D(b)(2); Reg. §1.6038D-3(b)(1).

[67] Reg. §1.6038D-3(b)(3).

[68] Reg. §1.6038D-3(b)(4).

[69] Reg. §1.6038D-3(b)(5)(i).

[70] Reg. §1.6038D-3(b)(5)(i).

[71] Reg. §1.6038D-3(b)(5)(ii).

[72] Reg. §1.6038D-3(b)(5)(i).

[73] Instructions for Form 8938 (December 2014), pg. 4.

[74] Preamble to Final Regulations, 76 Fed. Reg. 73820 (Dec. 12, 2014).

[75] Preamble to Final Regulations, 76 Fed. Reg. 73820 (Dec. 12, 2014).

[76] Preamble to Final Regulations, 76 Fed. Reg. 73821 (Dec. 12, 2014).

[77] Preamble to Final Regulations, 76 Fed. Reg. 73821 (Dec. 12, 2014).

[78] Preamble to Final Regulations, 76 Fed. Reg. 73821 (Dec. 12, 2014).

[79] Preamble to Final Regulations, 76 Fed. Reg. 73821 (Dec. 12, 2014).

[80] Preamble to Final Regulations, 76 Fed. Reg. 73820 (Dec. 12, 2014).

[81] IRS website—Basic Questions and Answers on Form 8938 (current as of Dec. 22, 2014)—FAQ #1; 2014 Worldwide Tax Daily 247-35 (Dec. 22, 2014).

[82] IRS website—Basic Questions and Answers on Form 8938 (current as of Dec. 22, 2014)—FAQ #3; 2014 Worldwide Tax Daily 247-35 (Dec. 22, 2014).

[83] IRS website—Basic Questions and Answers on Form 8938 (current as of Dec. 22, 2014)—FAQ #4; 2014 Worldwide Tax Daily 247-35 (Dec. 22, 2014).

[84] IRS website—Basic Questions and Answers on Form 8938 (current as of Dec. 22, 2014)—FAQ #5; 2014 Worldwide Tax Daily 247-35 (Dec. 22, 2014).

[85] IRS website—Basic Questions and Answers on Form 8938 (current as of Dec. 22, 2014)—FAQ #6; 2014 Worldwide Tax Daily 247-35 (Dec. 22, 2014).

[86] IRS website—Basic Questions and Answers on Form 8938 (current as of Dec. 22, 2014)—FAQ #7; 2014 Worldwide Tax Daily 247-35 (Dec. 22, 2014).

[87] IRS website—Basic Questions and Answers on Form 8938 (current as of Dec. 22, 2014)—FAQ #8; 2014 Worldwide Tax Daily 247-35 (Dec. 22, 2014).

[88] IRS website—Basic Questions and Answers on Form 8938 (current as of Dec. 22, 2014)—FAQ #9; 2014 Worldwide Tax Daily 247-35 (Dec. 22, 2014).

[89] IRS website—Basic Questions and Answers on Form 8938 (current as of Dec. 22, 2014)—FAQ #10; 2014 Worldwide Tax Daily 247-35 (Dec. 22, 2014).

[90] IRS website—Basic Questions and Answers on Form 8938 (current as of Dec. 22, 2014)—FAQ #11; 2014 Worldwide Tax Daily 247-35 (Dec. 22, 2014).

[91] IRS website—Basic Questions and Answers on Form 8938 (current as of Dec. 22, 2014)—FAQ #12; 2014 Worldwide Tax Daily 247-35 (Dec. 22, 2014).

[92] IRS website—Basic Questions and Answers on Form 8938 (current as of Dec. 22, 2014)—

FAQ #14; 2014 Worldwide Tax Daily 247-35 (Dec. 22, 2014).

[93] IRS website—Basic Questions and Answers on Form 8938 (current as of Dec. 22, 2014)—FAQ #15; 2014 Worldwide Tax Daily 247-35 (Dec. 22, 2014).

[94] IRS website—Basic Questions and Answers on Form 8938 (current as of Dec. 22, 2014)—FAQ #19; 2014 Worldwide Tax Daily 247-35 (Dec. 22, 2014).

[95] IRS website—Basic Questions and Answers on Form 8938 (current as of Dec. 22, 2014)—FAQ #20; 2014 Worldwide Tax Daily 247-35 (Dec. 22, 2014).

[96] IRS website—Basic Questions and Answers on Form 8938 (current as of Dec. 22, 2014)—FAQ #21; 2014 Worldwide Tax Daily 247-35 (Dec. 22, 2014).

[97] IRS website—Basic Questions and Answers on Form 8938 (current as of Dec. 22, 2014)—FAQ #22; 2014 Worldwide Tax Daily 247-35 (Dec. 22, 2014).

[98] Code Sec. 6038D(a); Reg. §1.6038D-2(a)(1).

[99] Reg. §1.6038D-1(a)(11); Instructions for Form 8938 (December 2014), pg. 1.

[100] Instructions for Form 8938 (December 2014), pg. 1.

[101] Instructions for Form 8938 (December 2014), pg. 1.

[102] IRS website—Basic Questions and Answers on Form 8938 (current as of Dec. 22, 2014)—FAQ #16; 2014 Worldwide Tax Daily 247-35 (Dec. 22, 2014).

[103] Until the IRS issued new regulations in December 2014 under Code Secs. 6038A and 6038C, taxpayers could use a similar technique to avoid penalties related to Form 5472 (*Information Return of a 25% Foreign-Owned U.S. Corporation or a Foreign Corporation Engaged in a U.S. Trade or Business*).

[104] Reg. §1.6038D-2(d)(1).

[105] Reg. §1.6038D-2(d)(1).

[106] Reg. §1.6038D-2(d)(2).

[107] Reg. §1.6038D-2(d)(2).

[108] Code Sec. 6038(h).

[109] *See* Code Sec. 6038D(c); Reg. §1.6038D-4.

[110] Preamble to Final Regulations, 76 Fed. Reg. 73822 (Dec. 12, 2014).

[111] Preamble to Final Regulations, 76 Fed. Reg. 73822 (Dec. 12, 2014).

[112] Reg. §1.6038D-7(a)(1)(i). The mention of Form 8891 applies only to years beginning after March 18, 2010, and ending on or before December 31, 2013, because of changes to rules regarding Form 8891 and certain Canadian retirement plans recently introduced by Rev. Proc. 2014-55, IRB 2014-44, 753.

[113] T.D. 9657, IRB 2014-13, 687, Preamble to Temporary Regulations, 76 Fed. Reg. 78554 (Dec. 19, 2011); Instructions for Form 8938 (December 2014), pg. 6.

[114] Preamble to Final Regulations, 76 Fed. Reg. 73823 (Dec. 12, 2014).

[115] Preamble to Final Regulations, 76 Fed. Reg. 73823 (Dec. 12, 2014).

[116] Preamble to Final Regulations, 76 Fed. Reg. 73823 (Dec. 12, 2014).

[117] Reg. §1.6038D-1(a)(2).

[118] T.D. 9657, IRB 2014-13, 687, Preamble to Temporary Regulations, 76 Fed. Reg. 78555 (Dec. 19, 2011).

[119] Reg. §1.6038D-7(c).

[120] T.D. 9657, IRB 2014-13, 687, Preamble to Temporary Regulations, 76 Fed. Reg. 78558 (Dec. 19, 2011).

[121] Reg. §1.6038D-7(a)(2).

[122] Preamble to Final Regulations, 76 Fed. Reg. 73823 (Dec. 12, 2014).

[123] Preamble to Final Regulations, 76 Fed. Reg. 73823 (Dec. 12, 2014).

[124] Reg. §1.6038D-7(b).

[125] Reg. §1.6038D-5(b)(1).

[126] T.D. 9657, IRB 2014-13, 687, Preamble to Temporary Regulations, 76 Fed. Reg. 78557 (Dec. 19, 2011).

[127] Instructions to Form 8938 (December 2014), pg. 5.

[128] Preamble to Final Regulations, 76 Fed. Reg. 73822 (Dec. 12, 2014).

[129] Preamble to Final Regulations, 76 Fed. Reg. 73822 (Dec. 12, 2014).

[130] Preamble to Final Regulations, 76 Fed. Reg. 73822 (Dec. 12, 2014).

[131] Reg. §1.6038D-5(c)(1).

[132] Reg. §1.6038D-5(c)(2).

[133] Reg. §1.6038D-5(c)(4).

[134] Reg. §1.6038D-5(d).

[135] Reg. §1.6038D-5(f)(1).

[136] Instructions for Form 8938 (December 2014), pg. 6.

[137] Reg. §1.6038D-5(f)(2)(i).

[138] Reg. §1.6038D-5(f)(3)(i).

[139] Reg. §1.6038D-5(f)(3)(i).

[140] IRS website—Basic Questions and Answers on Form 8938 (current as of Dec. 22, 2014)—FAQ #13; 2014 Worldwide Tax Daily 247-35 (Dec. 22, 2014).

[141] Preamble to Final Regulations, 76 Fed. Reg. 73822 (Dec. 12, 2014).

[142] Reg. §1.6038D-2(a)(5).

[143] Reg. §1.6038D-5(b)(3).

[144] Reg. §1.6038D-2(a)(6).

[145] Reg. §1.6038D-2(a)(7).

[146] Reg. §1.6038D-2(c)(1)(i) and (ii).

[147] Instructions for Form 8938 (December 2014), pg. 3.

[148] Reg. §1.6038D-2(c)(2); Reg. §1.6038D-2(c)(1)(ii).

[149] Reg. §1.6038D-2(c)(3)(i).

[150] Reg. §1.6038D-2(c)(3)(ii).

[151] Reg. §1.6038D-2(f).

[152] Reg. §1.6038D-2(a)(1); Instructions for Form 8938 (December 2014), pg. 2.

[153] Reg. §1.6038D-2(a)(3); Instructions for Form 8938 (December 2014), pg. 2.

[154] Code Sec. 911(d)(1).

[155] Reg. §1.6038D-2(a)(1); Instructions for Form 8938 (December 2014), pg. 2.

[156] Reg. §1.6038D-2(a)(3); Instructions for Form 8938 (December 2014), pg. 2.

[157] Reg. §1.6038D-2(a)(2); Instructions for Form 8938 (December 2014), pg. 2.

[158] Reg. §1.6038D-2(a)(4); Instructions for Form 8938 (December 2014), pg. 2.

[159] Preamble to Final Regulations, 76 Fed. Reg. 73819 (Dec. 12, 2014).

[160] Instructions for Form 8938 (December 2014), pg. 3.

[161] Instructions for Form 8938 (December 2014), pg. 3.

[162] Instructions for Form 8938 ((December 2014), pg. 3.

[163] Instructions for Form 8938 (December 2014), pg. 3.

[164] Instructions for Form 8938 (December 2014), pg. 3.

[165] Instructions for Form 8938 (December 2014), pg. 3.

[166] Instructions for Form 8938 (December 2014), pg. 3.

[167] Instructions for Form 8938 (December 2014), pg. 3.

[168] Instructions for Form 8938 (December 2014), pg. 3.

[169] Instructions for Form 8938 (December 2014), pg. 3.

[170] U.S. Joint Committee on Taxation, Technical Explanation of the Revenue Provisions Contained in Senate Amendment 3310, the "Hiring Incentives to Restore Employment Act," JCX-4-10, Feb. 23, 2010, at 60.

[171] IRS Notice 2011-55, IRB 2011-29, 53.

[172] Instructions for Form 8938 (November 2011), pg. 1.

[173] T.D. 9657, IRB 2014-13, 687, Preamble to Temporary Regulations, 76 Fed. Reg. 78559 (Dec. 19, 2011).

[174] U.S. Government Accountability Office, "Reporting Foreign Accounts to IRS—Extent of Duplication Not Currently Known, but Requirements Can Be Clarified," GAO-12-403 (Feb. 2012), at 1.

[175] U.S. Government Accountability Office, "Reporting Foreign Accounts to IRS—Extent of Duplication Not Currently Known, but Requirements Can Be Clarified," GAO-12-403 (Feb. 2012), at 29.

[176] Preamble to Final Regulations, 76 Fed. Reg. 73823-73824 (Dec. 12. 2014).

[177] Instructions for Form 8938 (December 2014), pg. 1. *See also* IRS website—Basic Questions and Answers on Form 8938 (current as of Dec. 22, 2014)—FAQ #17; 2014 Worldwide Tax Daily 247-35 (Dec. 22, 2014).

[178] Code Sec. 6038D(d)(1); Reg. §1.6038D-8(a).

[179] Code Sec. 6038D(d)(2); Reg. §1.6038D-8(c).

[180] Reg. §1.6038D-8(b).

[181] Reg. §1.6038D-8(b).

[182] Code Sec. 6038D(e); Reg. §1.6038D-8(d).

[183] Code Sec. 6038D(g); Reg. §1.6038D-8(e)(1).

[184] Reg. §1.6038D-8(e)(2).

[185] Code Sec. 6038D(g); Reg. §1.6038D-8(e)(3).

[186] Preamble to Final Regulations, 76 Fed. Reg. 73824 (Dec. 12. 2014); *Florida Bar Tax Section Comments on Proposed Regs on Reporting Foreign Financial Assets*, Tax Notes Today, 42-20 (Feb. 14, 2012); *CPA Group Comments on U.S. Regs for Reporting of Foreign Financial Assets*,

Worldwide Tax Daily, 75-37 (March 19, 2012).

[187] Preamble to Final Regulations, 76 Fed. Reg. 73824 (Dec. 12. 2014).

[188] Reg. §1.6038D-8(f)(1).

[189] Code Sec. 6662(a).

[190] Code Sec. 6662(j)(1).

[191] Code Sec. 6662(j)(2).

[192] Code Sec. 6662(j)(3).

[193] U.S. Joint Committee on Taxation, Technical Explanation of the Revenue Provisions Contained in Senate Amendment 3310, the "Hiring Incentives to Restore Employment Act," JCX-4-10, February 23, 2010, pages 63–64.

[194] Instructions for Form 8938 (December 2014), pg. 7.

[195] Reg. §1.6038D-8(f)(2).

[196] Instructions for Form 8938 (December 2014), pg. 7.

[197] Code Sec. 6501(a).

[198] Code Sec. 6501(c)(8).

[199] Code Sec. 6501(c)(8)(A) as in effect before P.L. 111-147, which was enacted on March 18, 2010.

[200] U.S. Joint Committee on Taxation, Technical Explanation of the Revenue Provisions Contained in Senate Amendment 3310, the "Hiring Incentives to Restore Employment Act," JCX-4-10. Feb. 23, 2010, pg. 66 (emphasis added).

[201] Code Sec. 6501(c)(8)(B).

[202] CCA 201147030 (Nov. 25, 2011).

[203] CCA 201147030 (Nov. 25, 2011) (emphasis added).

[204] Code Sec. 6501(e)(1)(A).

[205] U.S. Joint Committee on Taxation, Technical Explanation of the Revenue Provisions Contained in Senate Amendment 3310, the "Hiring Incentives to Restore Employment Act," JCX-4-10, Feb. 23, 2010, pg. 66; *see also* Instructions to Form 8938 (December 2014), pg. 8.

[206] I.R.M. § 4.26.17.3 (01-01-2007).

[207] I.R.M. § 20.1.9.2 (04-22-2011); I.R.M. § 20.1.9.2.1 (04-22-2011); I.R.M. § 20.1.9. 22 (04-22-2011).

[208] Code Sec. 6213(a).

[209] Code Sec. 6213(a). Tommy Taxcheat could choose instead to pay the tax liability and initiate a refund action in U.S. district court or the Court of Federal Claims, but this option generally is not preferred because of the prepayment requirement.

[210] *See* Hale E. Sheppard, *Two More Blows to Foreign Account Holders: Tax Court Lacks FBAR Jurisdiction and Bankruptcy Offers No Relief from FBAR Penalties*," J. Tax Practice & Procedure, February–March 2009, at 27.

[211] 31 U.S.C. § 5321(b)(2). The government must initiate this lawsuit within two years of assessing the FBAR penalty.

[212] I.R.M. § 20.1.9.2 (04-22-11) (emphasis added); I.R.M. Exhibit 20.1.9-4.