

# FBAR vs. Form 8938

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## Summary

Do we really have to file both the FBAR and Form 8938?! The consequences of noncompliance can be severe. This session breaks down the filing requirements for each, distinguishes between foreign accounts and foreign assets, and reviews the reporting thresholds. You'll learn what you must do to ensure that your clients satisfy their foreign reporting obligations and what to do if they don't.

***The information contained herein is for educational use only and should not be construed as tax, financial, or legal advice. Each individual's situation is unique and may require specialized treatment. It is, therefore, imperative that you consult with tax and legal professionals prior to implementation of any strategies discussed.***

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## I. Introduction

No more “secret” Swiss bank accounts! Credit Suisse (Switzerland’s second largest bank) has announced that it will lift the veil of secrecy shrouding its bank accounts and will turn over previously confidential account information, including client names to the Swiss Federal Tax Administration which may, at its discretion, then share the information with the IRS.<sup>1</sup> Prosecutors have already charged taxpayers or bankers in cases implicating Julius Baer, the third-largest Swiss wealth manager; Zürcher Kantonalbank, the biggest Swiss publicly owned regional bank; and Mizrahi Tefahot Bank Ltd. and Bank Leumi Le-Israel Ltd., two Israeli banks with Swiss units.<sup>2</sup>

Gone are the days of hiding money abroad. Whether by corporate decision to avoid criminal prosecution by cooperating with US tax prosecutors or by multi-national agreement between governments,<sup>3</sup> the time has come for US taxpayers to come clean. To date, more than 43,000 taxpayers have voluntarily disclosed previously hidden offshore accounts and paid over \$6 billion in back taxes, interest and penalties.<sup>4</sup> Those who have not (yet) disclosed foreign accounts and assets face stiff penalties and potential criminal prosecution.



Time is up! Time is *now*...

## II. Reporting Requirements for Foreign Accounts and Assets

### A. Foreign Accounts

Mandated by the Bank Secrecy Act of 1970,<sup>5</sup> a US person must file a report with the US Treasury if, at any time during the calendar year, he had a financial

<sup>1</sup> *Not So Secret Swiss Bank Accounts*, SmartPros, January 3, 2012.

<sup>2</sup> Voreacos and Broom, *Credit Suisse Offers Map to 13 Swiss Banks in U.S. Tax Probe*, Bloomberg Business, May 26, 2014 [available at <http://www.bloomberg.com/news/articles/2014-05-25/credit-suisse-offers-map-to-13-swiss-banks-in-u-s-tax-probes>, last accessed April 21, 2015].

<sup>3</sup> On November 19, 2014, Switzerland became the 52<sup>nd</sup> jurisdiction to sign the Multilateral Competent Authority Agreement, enabling automatic exchange of financial account information in tax matters with other countries beginning in 2018 as per *International Financial Law Prof Blog*, available at [http://lawprofessors.typepad.com/intfinlaw/2014/11/switzerland-takes-important-step-to-boost-international-cooperation-against-tax-evasion.html?utm\\_source=feedburner&utm\\_medium=email&utm\\_campaign=Feed%3A+IntFinLaw+%28International+Financial+Law+Blog%29](http://lawprofessors.typepad.com/intfinlaw/2014/11/switzerland-takes-important-step-to-boost-international-cooperation-against-tax-evasion.html?utm_source=feedburner&utm_medium=email&utm_campaign=Feed%3A+IntFinLaw+%28International+Financial+Law+Blog%29), last accessed April 21, 2014].

<sup>4</sup> From a GAO Report [available at [http://www.gao.gov/modules/ereport/handler.php?l=1&path=/ereport/GAO-14-343SP/data\\_center\\_savings/General\\_government/20\\_Tax\\_Policies\\_and\\_Enforcement#\\_ftn2\\_1](http://www.gao.gov/modules/ereport/handler.php?l=1&path=/ereport/GAO-14-343SP/data_center_savings/General_government/20_Tax_Policies_and_Enforcement#_ftn2_1), last accessed April 21, 2015].

<sup>5</sup> Codified as Title 31 of US Code.

interest in or signatory authority over one or more foreign financial accounts with an aggregate value of \$10,000 or more.

## B. Foreign Assets

In addition to foreign account reporting, certain taxpayers may be required to file supplemental forms. Indeed, some reporting requirements may seem annoyingly duplicative but are nevertheless required based on differing legislative mandates and regulatory oversights. While the **FinCEN 114** must be filed with the US Department of Treasury, **Form 8938 Statement of Specified Foreign Financial Assets** must be submitted to the IRS along with the taxpayer's income tax return.<sup>6</sup>

**NOTE:** If the taxpayer is not required to file an income tax return, he does not have to file **Form 8938**.

## III. Foreign Bank Account Report (FBAR)

### A. FinCEN114<sup>7</sup>

This form has replaced **Form TD F 90-22.1 Report of Foreign Bank and Financial Accounts** (FBAR) effective April 2013. It must be *electronically* filed.

### B. Definitions

1. A US person is defined as a US citizen, a US resident,<sup>8</sup> or any entity created (organized) under US law. The actual tax status of the "person" is disregarded for purposes of foreign account reporting compliance.
2. Signature authority allows an individual to control the disposition of account assets by written or oral communication. Authority may be exercised alone or in conjunction with others. Accounts may have multiple signatories and all will be required to comply with foreign account reporting requirements.

**NOTE:** If the US person cannot directly access the foreign account but must, instead, communicate through a US entity or branch, no FBAR filing is required.

3. Financial interest means that the US person holds title to the account directly, is the beneficial owner of an account held by a third party, or holds title

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<sup>6</sup> IRC § 6038D.

<sup>7</sup> FinCEN = Financial Crimes Enforcement Network.

<sup>8</sup> IRC § 7701(b).



indirectly (e.g. through majority ownership of an entity that holds title to the account).

4. A foreign account is any account held outside of the US (including all 50 states and Washington DC), as well as Puerto Rico, the Northern Mariana Islands and all US territories (including Guam, American Samoa, and the US Virgin Islands). , US territories and possessions, as well as Indian lands). **EXCEPTION:** An account in an institution known as a US “military banking facility” is not considered to be an account in a foreign country, regardless of its geographic location.
5. Financial accounts may include monetary and non-monetary assets (e.g. banks, brokerage accounts, insurance cash values, annuities, mutual funds, online gambling accounts,<sup>9</sup> amongst others). Real and personal property is generally not included.<sup>10</sup>

### C. Rules

#### Valuation

Each account must be valued separately at its highest value as reported to the account holder on periodic statements, regardless of when the valuation was achieved during the calendar year. The value must then be converted to US currency using the applicable exchange rate on December 31<sup>st</sup>.

Once each separate account has been valued and converted, all account values are aggregated to determine whether the foreign account reporting threshold (\$10,000) has been met for the reporting period.

A US taxpayer has a foreign account valued at \$8,000 at Bank A. He closes the account and transfers the entire balance to Foreign Bank B during the year. Although the value of both accounts totals \$16K, the filing threshold was not met at any given time during the year since assets are not double-counted.

A US taxpayer has a foreign account valued at \$8,000 at Bank A and another account valued at \$4,000 at Bank C. He closes the Bank A account and transfers the entire balance to Foreign Bank B during the year. The aggregate value of the accounts at Bank A [later Bank B] and Bank C now exceed the reporting threshold.

<sup>9</sup> *US v Hom*, US District Court, N.D. California, Case No. 3:13-cv-03721 (June 4, 2014).

<sup>10</sup> In response to an inquiry from *Forbes* contributor Kelly Phillips Erb, the IRS issued this statement: “The Financial Crimes Enforcement Network, which issues regulatory guidance pertaining to reports of Foreign Bank and Financial Accounts (FBARs), is not requiring that digital (or virtual) currency accounts be reported on an FBAR at this time but may consider requiring such accounts to be reported in the future.” [*IRS Says Bitcoin Not Reportable on FBAR (For Now)*, June 30, 2014, available at <http://www.forbes.com/sites/kellyphillipserb/2014/06/30/irs-says-bitcoin-not-reportable-on-fbar-for-now/>, last accessed April 21, 2015].



## Joint and Consolidated Reporting

Spouses may file one combined report to report jointly-held accounts. However, separately-held accounts must be reported individually.

Entities of all types may file consolidated reports. Truncated filing is permitted for more than 25 accounts.

### **D. How to File**

The annual reporting cycle is on a calendar year basis (January to December). The deadline for filing **FinCEN 114** is June 30<sup>th</sup> every year. No extension is available.<sup>11</sup>

E-file is now mandatory. Filers have the option to prepare and submit individual reports online at <http://bsaeiling.fincen.treas.gov/NoRegFBARFiler.html> or engage the services of a Bank Secrecy Act (BSA) e-Filer.<sup>12</sup>

Step-by-step instructions are available online to enroll in the BSA e-filing system as a Supervisory User with primary responsibility for the preparation and submission of all BSA filings by authorized users within a professional organization. Users may submit single reports or process multiple reports in batches through third-party software. Acknowledgments of all filings are sent to the user's secure inbox.

**Form 114a Record of Authorization to Electronically File FBARS** must be completed and signed by the client to authorize a registered BSA user to file on the client's behalf. The signed form must be kept on file for 5 years.<sup>13</sup>

Corrections to previously filed reports may be made by opening the saved file, checking the box at the top of the form marked "Amendment", making the necessary corrections on affected lines of the form, entering the current date, saving the changes as a new file, and resubmitting the form electronically.

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<sup>11</sup> The IRS offers taxpayers a practitioners a helpline with a team of specially trained technicians and examiners to answer technical questions:

- (866) 270-0733 for callers within the US (toll-free)
- (313) 234-6146 for callers outside of the US (not toll-free)

<sup>12</sup> Some professional tax preparation packages offer FBAR e-filing which eliminates the need to enroll with the BSA e-Filing System.

<sup>13</sup> 31 CFR 1010.430(d).



## E. Penalties



Unintentional failure to file may result in a maximum fine of \$10,000 per account that was not reported. However, if the government can prove that there was “willful violation” of the filing mandate, the penalty is increased to the greater of \$100,000 or 50% of the account value, along with potential criminal sanctions (maximum \$250,000) and/or up to five years jail time.<sup>14</sup> The “willful” penalty is computed on a *per year* basis for up to six tax years!

To impose the “willful” penalty, the government must prove that failure to file was the result of the taxpayer’s voluntary, conscious and intentional act. The Supreme Court explained that the term willful “consistently has been read by the Courts of Appeals to require both knowledge of the reporting requirement and a specific intent to commit the crime.”<sup>15</sup> The IRS Internal Revenue Manual goes a step further by suggesting that “willfulness may be attributed to a person who has made a conscious effort to avoid learning about the FBAR recordkeeping requirements.”<sup>16</sup>

FBAR failure to file penalties should not be taken lightly: In a recent case,<sup>17</sup> penalties totaling \$3.4 million were assessed against a taxpayer who failed to disclose his Swiss bank account which, at its highest, had a balance of only \$1.7 million. By applying the 50% penalty to each year and aggregating the years in question, the taxpayer faced a total penalty that was more than double his account holdings! (On appeal a jury reduced the penalty to \$2.2 million; the taxpayer eventually settled with the IRS for a mere \$1.8 million.)

**REMINDER:** Taxpayers must also report interest and dividend income received from foreign sources on **Form 1040, Schedule B** and must check the box in Part III, Line 7 as “Yes” if the aggregate value of all foreign accounts was equal to or greater than \$10,000 at any time during the year.

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<sup>14</sup> In certain circumstances – if other laws were violated – the criminal penalty may be increased to \$500,000 and/or 10 years in jail.

<sup>15</sup> *Ratzlaf v United States*, 114 S. Ct. (1994).

<sup>16</sup> Rettig, *Jury Determines 150-Percent FBAR Penalty and US Seeks FBAR Related Forfeiture of \$12 million!*, Journal of Tax Practice and Procedure, June-July 2014.

<sup>17</sup> *United States v. Carl R. Zwerner*, Case # 1:13-cv-22082-CMA (SD Florida, June 11, 2013).

## F. Fixes for Failure to File

### 1. Offshore Voluntary Disclosure Program (OVDP)

The program currently in effect is the fourth incarnation<sup>18</sup> to be offered by the IRS allowing taxpayers who have failed to file requisite foreign account reports to provide full disclosure in exchange for reduced civil penalties and no criminal prosecution.<sup>19</sup>

**NOTE:** Taxpayers already under civil examination or criminal investigation are ineligible for the program.

The penalty imposed under the OVDP is equal to 27.5% of the highest year's aggregate value during the period covered by the voluntary disclosure – the most current 8 years.<sup>20</sup> The penalty amount is fixed and due at the time that the requisite amended returns are filed. IRS examiners have no authority or discretion to negotiate alternate penalty amounts.

#### Process

Step 1: Taxpayers who wish to participate in the program should begin with a pre-clearance request which may be faxed to the IRS Criminal Investigation Lead Development Center at (267) 941-1115. While pre-clearance does not guarantee OVDP acceptance, it helps to streamline the process by providing basic taxpayer information and an executed power of attorney to the tax authority.

Step 2: Thereafter, the taxpayer must submit an Offshore Voluntary Disclosure Letter and attachment to the IRS Voluntary Disclosure Coordinator (1-D04-100) at 2970 Market Street Philadelphia, PA 19104. Criminal Investigations will review the submission and respond within 45 days indicating preliminary acceptance into the program and requesting further documentation and payment of the total amount of tax, interest and penalties within 90 days.

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<sup>18</sup> The 2003 program was offered to taxpayers who used offshore credit, debit and other payment cards. The 2009 program was intended to encourage taxpayers who held Swiss bank accounts to come forward voluntarily before global banking giant UBS was required to disclose the names of roughly 4,450 US clients. In 2011, taxpayers were encouraged to make voluntary disclosures of foreign accounts held in Israel, India, Hong Kong and Asia while the Department of Justice pursued HSBC, a financial services firm headquartered in the UK.

<sup>19</sup> OVDP is available for all foreign reporting, including **Forms 8938, 3520 and 5471**, as well as **FinCEN 114**.

<sup>20</sup> In fact, 27.5% merely represents the base penalty which may be increased to 50% for any foreign financial account that was held at a bank that has been publicly identified as being under investigation or as cooperating with a government investigation.



Step 3: A civil examiner will be assigned to complete the certification of the taxpayer's returns for accuracy, completeness and correctness; a process that is less formal than an audit and does not carry with it all the rights and legal consequences of an examination.

There is no definitive time limit specified for approval or denial of the OVDP request; cases are handled on a first-come, first-served basis.

## 2. The Streamlined Disclosure Program (SDP)



On June 18<sup>th</sup>, 2014,<sup>21</sup> the IRS introduced a new program for resident and non-resident taxpayers whose failure to comply with FBAR filing requirements was not willful. In fact, the SDP requires taxpayers to sign a self-certifying statement under penalty of perjury that “failure to report all income, pay all tax, and submit all required information returns, including FBARs, was due to non-willful conduct [which was the result of] negligence, inadvertence, mistake or conduct that is the result of good faith misunderstanding of the requirements of the law.”

**NOTE:** False certification will expose the taxpayer to civil fraud penalties.

Although the IRS will not impose accuracy-related, information return or FBAR penalties on SDP participants, US taxpayers will nevertheless be subject to a “miscellaneous” penalty equal to 5% of the highest aggregate balance of the taxpayer’s foreign accounts during the most recent six-year period. US taxpayers who lived abroad in any one or more of the most recent three years are exempt from the penalty.

While SDP offers participants the benefit of simplified reporting and reduced penalties, taxpayers should beware that the program is only available to those who acted unintentionally. Regulatory interpretation of willful and fraudulent conduct may differ from the taxpayer’s understanding and lay opinion; expert counsel should be engaged prior to SDP submission.

Taxpayers who are already participating in the OVDP process but have not yet signed a final closing agreement, may request reduced penalty treatment under SDP if they can satisfy (and certify) the non-willfulness standard. Previously, OVDP participants who wished to discontinue the process were forced to “opt-out” of the program in hopes of negotiating more favorable settlement terms.

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<sup>21</sup> IR 2014-73.



### 3. The Delinquent Information Return Program (DIRP)

If a taxpayer properly included all foreign account income on his originally-filed returns and paid the tax for all years but did not file the required foreign bank account reports, he may simply file the omitted returns as soon as possible. The IRS will not impose failure-to-file penalties on delinquent or late-filed reports if the taxpayer has no outstanding tax liabilities and is not being audited.<sup>22</sup>

**BEWARE:** The IRS has taken the position that even a single dollar of unreported income can make a taxpayer ineligible for penalty-free disposition.<sup>23</sup>

### 4. Summary

	No Program	OVDP	SDP	DIRP
Penalty	\$10K/unreported account/year if unintentional; \$100K or 50% of highest balance if willful <i>plus</i> \$250K criminal penalty &/or max 5 years jail	27.5% of highest balance (max 50% if foreign bank under investigation)	5% of highest balance	None if all income was reported; otherwise \$10,000/violation
Penalty Negotiable	Yes	No	No	Yes
Number of past FBARs required to be filed	6	8	6	No guidance given
Possible criminal prosecution	Yes	No, if accepted into program	Yes	Yes



**PRACTITIONER WARNING:** Because the penalties are high and the consequences extreme, practitioners should beware of offering advice outside of their areas of expertise and should instead refer clients with unreported foreign accounts and/or income to a competent tax attorney.

A tax attorney recently circulated an inquiry requesting counsel from fellow attorneys: "I just picked up a case [in which] my client is in the process of being hit with a FBAR penalty in excess of \$4,000,000. [During the] civil audit (most likely sparked by the client's name being turned over in an investigation of UBS) it was discovered that [he] had made a quiet disclosure... The CPA [who] took the client through the quiet disclosure told the IRS that he was unfamiliar with the offshore voluntary disclosure program; [t]his looks like a malpractice case on a silver platter against the CPA."

<sup>22</sup> FAQ 17, Offshore Voluntary Disclosure Program Frequently Asked Questions and Answers [available at <http://www.irs.gov/Individuals/International-Taxpayers/Offshore-Voluntary-Disclosure-Program-Frequently-Asked-Questions-and-Answers>, last accessed April 21, 2015].

<sup>23</sup> Fisher and McManus, *Offshore Voluntary Disclosure: IRS simplifies path back to tax compliance*, NATP TAXPRO Journal, Fall 2014.



## G. The Trouble with the FBAR

Although the FBAR filing requirement has been mandated since 1970 to help combat money laundering and related financial criminal activities, the rule was only sporadically enforced. Then, in 2004, Congress linked the FBAR to its counter-terrorism efforts but failed to adjust the decades-old filing threshold<sup>24</sup> and soon ensnared ordinary and unsuspecting taxpayers in its web.

Often oblivious to a filing requirement that is separate and distinct from income tax reporting, taxpayers with no criminal intent whatsoever who live, work and study abroad are surprised to discover that they have inadvertently overlooked an important filing obligation. For these individuals, “FBAR noncompliance constitutes nothing but a paperwork crime.”<sup>25</sup> On the other hand, those who comply find that they must submit personal information to a federal financial crimes enforcement registry!

## IV. Foreign Asset Reporting

### A. Form 8938, Statement of Specified Foreign Financial Assets

The **Form 8938** filing requirement was enacted in 2010<sup>26</sup> to improve tax compliance by US taxpayers with offshore financial accounts.<sup>27</sup> US citizens, residents, non-residents who elect to file a joint return with a US citizen or resident, and certain non-residents who live in a US territory must file if the total value of specified foreign assets exceeds specified thresholds.

**NOTE:** The filing thresholds are higher for taxpayers who live abroad (referred to as “foreign” taxpayers) than for those who live in the US (“domestic” taxpayers).

### B. Reportable Assets

Specified foreign financial assets include:<sup>28</sup>

- Depository or custodial accounts at foreign financial institutions

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<sup>24</sup> The FBAR threshold has been fixed at a mere \$10,000; far lower than the tax filing threshold for most taxpayers which tops out at more than double that amount for married taxpayers in 2015.

<sup>25</sup> Christians, *Paperwork and Punishment: It's Time to Fix FBAR*, Tax Analysts, October 13, 2014.

<sup>26</sup> Hiring Incentives to Restore Employment Act of 2010 (HIRE).

<sup>27</sup> The Foreign Account Tax Compliance Act (FATCA), enacted as part of HIRE, is intended to apply to “specified entities” as well as individuals. Prop. Reg. § 1.6038D-6 was introduced to establish conditions under which a domestic entity would be required to file **Form 8938**. Yet, IRS Notice 2013-10 has temporarily postponed the implementation of reporting requirements for domestic entities and trusts.

<sup>28</sup> IRC §1471(d).

- Stocks or securities issued by foreign persons
- Foreign pension or deferred compensation plans<sup>29</sup>
- Any other financial instrument or contract held for investment that is issued by or has a counter-party that is not a US person
- Any interest in a foreign entity<sup>30</sup>
- Gold certificates

Assets that do not have to be reported include:

- Foreign real estate (e.g., personal residence or rental property)<sup>31</sup>
- Foreign currency holdings
- Directly held shares of a US mutual fund that owns foreign stocks and securities
- A financial account maintained by a US financial institution that holds foreign stocks and securities, such as IRAs, 401(k) plans, qualified US retirement plans, and brokerage accounts maintained by US financial institutions
- A financial account maintained by a US branch or US affiliate of a foreign financial institution
- A financial account (e.g., depository, custodial or retirement account) held through a foreign branch or foreign affiliate of a US-based financial institution
- Payments or the rights to receive the foreign equivalent of social security, social insurance benefits or another similar program of a foreign government
- Directly held tangible assets, such as art, antiques, jewelry, cars and other collectibles (once these assets are sold, the resulting proceeds become reportable)
- Directly held precious metals, such as gold (but gold certificates issued by a foreign person are reportable)

### C. Filing Thresholds

The filing requirement applies only to US taxpayers, including US citizens and residents as well as certain non-resident aliens. Thus, the reference to “domestic” and “foreign” filers may be misleading. In fact, the terms merely distinguish between those US taxpayers that live in the US and those who live abroad.

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<sup>29</sup> Canadian Registered Retirement Savings Plans, for example, are reportable.

<sup>30</sup> IRC § 6038D(b).

<sup>31</sup> Non-Mexican citizens may not hold title to real property in Mexico within 100 km of international borders and 50 km of the coastline and are instead required to establish a Mexican Land Trust (MLT), also known as a “fideicomiso”. Upon purchase, legal title is transferred to a Mexican bank which acts as fiduciary but otherwise disclaims all responsibility for the property, allowing (forcing) the foreign buyer to pay maintenance, taxes and all expenses associated with his investment. Rev Rul 2013-14 clearly states that an MLT is not a “trust” for income tax purposes; hence, no **Form 8938** filing is required.

## Domestic Taxpayers

An individual taxpayer residing in the US must file **Form 8938** if he has an interest in one or more specified foreign financial assets with an aggregate value of either \$50,000 on December 31<sup>st</sup> or \$75,000 at any time during the year.

Married individuals must file if they exceed the thresholds of \$100,000 and \$150,000, respectively.<sup>32</sup>

## Foreign Taxpayers

If residing abroad,<sup>33</sup> **Form 8938** must be filed if the taxpayer has an interest in one or more specified foreign financial assets with an aggregate value of either \$200,000 on December 31<sup>st</sup> or \$300,000 at any time during the year.



Married individuals must file if they exceed the thresholds of \$400,000 and \$600,000, respectively.<sup>34</sup>

**NOTE:** Currently, only individuals must file **Form 8938**; domestic entities will be required to file when applicable Treasury Regulations are finalized.

## Summary

	Single or MFS	MFJ
Domestic – living in the US	\$50K on 12/31 OR \$75K at any time	\$100K on 12/31 OR \$150K at any time
Foreign – living outside of the US	\$200K on 12/31 OR \$300K at any time	\$400K on 12/31 OR \$600K at any time

To avoid duplicative reporting, foreign financial assets that have been reported on other forms – including **Forms 3520, 5471, 8621, 8865, 8891** – do not also have to be reported on **Form 8938**.<sup>35</sup> If an owner of a Canadian Registered

<sup>32</sup> Reg. § 1.6038D-2T(a)(1), Reg. § 1.6038D-2T(a)(2).

<sup>33</sup> “Foreign” taxpayers must satisfy the Bona Fide Residence (BFR) or Physical Presence (PP) tests (IRC § 911). BFR requires that the taxpayer is a resident of one or more foreign countries for an uninterrupted period that includes an entire tax year. PP requires that the taxpayer is present for at least 330 full days during any 12-month period of time that ends during the current tax year.

<sup>34</sup> The regulations have not clarified filing threshold requirements for joint returns if one spouse resides abroad and the other lives in the US.

<sup>35</sup> **Form 3520** Annual Return to Report Transactions with Foreign Trusts and Receipt of Certain Foreign Gifts, **Form 5471** Information Return of US Persons With Respect, **Form 8621** Information Return by a Shareholder of a Passive Foreign Investment Company or Qualified Electing Fund, **Form 8865** Return of US Persons With Respect to Certain Foreign Partnerships, **Form 8891** US Information Return for Beneficiaries of Certain Canadian Registered Retirement Plans.

Retirement Savings Plan (RRSP) elects to file **Form 8891** to postpone income recognition, he will be exempt from providing account details on **Form 8938** but must nevertheless include RRSP's account value when determining his filing threshold; he will still have to file **FinCEN 114**.<sup>36</sup>

### Valuation

Valuation of assets is based on the highest fair market value during the year, converted into US dollars at the applicable exchange rate on December 31<sup>st</sup>.<sup>37</sup>

## **D. Penalties**

Failure to disclose may result in a maximum fine of \$10,000 plus an additional \$10,000 penalty for each 30-day period after IRS issues its 90-day failure to disclose notification. The maximum penalty equals \$50,000.<sup>38</sup>

**NOTE:** The statute of limitations for an income tax return (**Form 1040**) remains open until three years after an associated **Form 8938** with all reportable assets has been filed – if even just one asset is omitted, the entire return remains at risk! If failure to file **Form 8938** is due to reasonable cause, the open statute will apply only to the item(s) related to the failure.<sup>39</sup>

If a taxpayer fails to report gross income in excess of \$5,000 attributable to reportable assets, the statute of limitations is extended to six years after the return was filed, whether or not the assets were reported on **Form 8938**.<sup>40</sup>

## **E. Relief**

The IRS announced<sup>41</sup> that procedures will go into effect September 1, 2012 to help non-compliant taxpayers resolve their delinquencies. Under the mandate,

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<sup>36</sup> With the issuance of Rev Proc 2014-55, **Form 8891** became obsolete as of December 31, 2014. The IRS has provided for prospective as well as retroactive relief for eligible US citizens and resident aliens by granting them *automatic* tax deferral on income earned in Canadian registered retirement savings plans (RRSPs) and registered retirement income funds (RRIFs). Eligibility requires that these taxpayers must have filed US tax returns for all years in which they held an interest in these accounts and must have included distributions (if taken) on all previously-filed returns.

**NOTE:** The revenue procedure does not modify other US reporting requirements that may apply under the Bank Secrecy Act and IRC § 6038D. Therefore, affected taxpayers must still file FBARs by June 30<sup>th</sup> of each year as well as attach **Form 8938** to their US income tax returns and provide all account details.

<sup>37</sup> Taxpayer may use the Treasury Department Financial Management Service rate (available at <https://www.fms.treas.gov/intn.html>) or any accepted currency converter (Treas. Reg. § 1.6038D-5T(c)).

<sup>38</sup> IRC § 6038D(d).

<sup>39</sup> IRC § 6501(c)(8).

<sup>40</sup> Additionally, a penalty equal to 40% of the resulting under-payment of tax will be assessed [IRC § 6662(b)(7)].



US citizens who live overseas and pose a “low compliance risk”<sup>42</sup> will be required to file all delinquent tax returns for the past three years, as well as delinquent foreign account reports for the past six years. While the returns will be subject to expedited examination, the IRS will not assess penalties or pursue follow-up actions. Taxpayers that present higher compliance risks will be subject to more thorough review and an audit that might well cover more than three years.

**NOTE:** “Taxpayers who are in a situation where they are concerned about the risk of criminal prosecution should be advised that this new procedure does not provide protection from criminal prosecution if the IRS and Department of Justice determine that the taxpayer’s particular circumstances warrant such prosecution.”<sup>43</sup> These taxpayers should consult their legal advisers about the Offshore Voluntary Disclosure Program. However, once a taxpayer makes a submission under the new procedures [detailed in the prior paragraph], OVDP is no longer available. Furthermore, taxpayers who are ineligible to participate in OVDP are also ineligible to participate in the new procedure.

## V. Is all this reporting working?

It is widely acknowledged that “offshore tax evasion is a significant contributor to the tax gap.”<sup>44</sup> A US Senate report estimates that more than \$100 billion of tax revenues are lost each year, giving the IRS plenty of incentive to pursue scofflaws and not-so gently prodding these taxpayers to step forward voluntarily.



And as FATCA becomes the global standard in the universal battle against offshore tax evasion, increasing numbers of foreign governments continue to sign on through intergovernmental agreements (IGAs) which have been developed by the US Treasury facilitating the exchange of tax information between countries.<sup>45</sup> While Americans abroad were initially treated as pariahs and the embodiment of a banker’s record-keeping and reporting nightmare, many foreign regulatory authorities have recognized the power and benefit of international cooperation enabling governments to fill their own coffers with tax revenues that previously eluded detection.

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<sup>41</sup> IR 2012-65 (June 26, 2012).

<sup>42</sup> These taxpayers generally file simple returns and owe less than \$1,500.

<sup>43</sup> Excerpted from *New Help for US Citizens Overseas*, TheTaxBook News, June 28, 2012.

<sup>44</sup> Stack, *Myth vs. FATC: The Truth About Treasury’s Effort to Combat Offshore Tax Evasion*, White & Case Tax Flash, September 20, 2013.

<sup>45</sup> Wood, *Incredibly, 48 Nations Embrace FATCA To Reveal U.S. Depositors*, Forbes, April 7, 2014 [available at <http://www.forbes.com/sites/robertwood/2014/04/07/incredibly-48-nations-embrace-fatca-to-reveal-u-s-depositors/>, last accessed May 29, 2014].



## APPENDIX A

### Comparison of Form 8938 and FinCEN 114 Requirements<sup>46</sup>

	Form 8938	FinCEN 114
<b>Who Must File?</b>	Specified individuals, which include US citizens, resident aliens, and certain non-resident aliens that have an interest in specified foreign financial assets and meet the reporting threshold	US persons, which include US citizens, resident aliens, trusts, estates, and domestic entities that have an interest in foreign financial accounts and meet the reporting threshold
<b>Does the United States include US territories?</b>	No	Yes, resident aliens of US territories and US territory entities are subject to foreign account reporting
<b>Reporting Threshold (Total Value of Assets)</b>	\$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
<b>When do you have an interest in an account or asset?</b>	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.
<b>What is Reported?</b>	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
<b>How are maximum account or asset values determined and reported?</b>	Fair market value in US dollars in accord with the Form 8938 instructions for each account and asset reported  Convert to US dollars using the end of the taxable year exchange rate and report in US dollars.	Use periodic account statements to determine the maximum value in the currency of the account.  Convert to US dollars using the end of the calendar year exchange rate and report in US dollars.
<b>When Due?</b>	By due date, including extension, if any, for income tax return	Received by June 30 (no extensions of time granted)
<b>Where to File?</b>	File with Income tax return pursuant to instructions for filing the return	Must be electronically filed
<b>Penalties</b>	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

<sup>46</sup> Available at <http://www.irs.gov/Businesses/Comparison-of-Form-8938-and-FBAR-Requirements> [last accessed May 28, 2014].





**APPENDIX B**  
**Options Available to Noncompliant Taxpayers<sup>47</sup>**

	OVDP	SDP	DIRP
<b>Who may participate</b>	Individuals, estates, partnerships, corporations and other entities	Individuals and estates	Individuals and estates
<b>Willful failure to report</b>	Eligible	Not eligible	Not eligible
<b>Prior tax returns filed</b>	Not required	Not required	Must have filed
<b>Under IRS audit</b>	Not eligible (even if taxpayer not aware of audit)	Not eligible	Not eligible
<b>Must self-certify non-willfulness</b>	Not required	Required	Required
<b>File amended tax returns with payment</b>	Required	Required	Required
<b>Applicable penalty</b>	27.5% of foreign financial assets (or 50% if bank publicly under investigation), plus standard tax penalties	None	5% of foreign financial assets
<b>Required filings</b>	Original or amended tax returns (8 years), FBARs (8 years) and other miscellaneous forms	Original or amended returns (3 years), FBARs (6 years)	Amended returns (3 years), FBARs (6 years)

<sup>47</sup> Fisher and McManus, *Offshore Voluntary Disclosure: IRS simplifies path back to tax compliance*, NATP TAXPRO Journal, Fall 2014.

