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March 19, 2012

CC:PA:LPD:PR (REG-130302-10)
Room 5205
Internal Revenue Service
P.O. Box 7604
Ben Franklin Station
Washington, DC 20044

By email: regina.johnson@irscounsel.treas.gov

Re: Internal Revenue Bulletin: 2012-8, February 21, 2012, REG-130302-10, Notice of Proposed Rulemaking by Cross-Reference to Temporary Regulations Reporting of Specified Foreign Financial Assets (T.D. 9567)

The New York State Society of Certified Public Accountants, representing more than 28,000 CPAs in public practice, industry, government and education, submits the following comments to you regarding the above captioned notice of proposed rulemaking. The NYSSCPA thanks the Internal Revenue Service for the opportunity to comment.

The NYSSCPA's International Taxation Committee deliberated the provisions and drafted the attached comments. If you would like additional discussion with us, please contact Melissa Gillespie, Chair of the International Taxation Committee, at (212) 880-2620, or Ernest J. Markezin, NYSSCPA staff, at (212) 719-8303.

Sincerely,

NYSSCPA

Richard E. Piluso
President

Attachment

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NEW YORK STATE SOCIETY OF

CERTIFIED PUBLIC ACCOUNTANTS

COMMENTS ON

INTERNAL REVENUE BULLETIN: 2012-8, FEBRUARY 21, 2012, REG-130302-10, NOTICE OF PROPOSED RULEMAKING BY CROSS-REFERENCE TO TEMPORARY REGULATIONS REPORTING OF SPECIFIED FOREIGN FINANCIAL ASSETS (T.D. 9567)

March 19, 2012

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New York State Society of Certified Public Accountants

Comments on

Internal Revenue Bulletin: 2012-8, February 21, 2012, REG-130302-10, Notice of Proposed Rulemaking by Cross-Reference to Temporary Regulations Reporting of Specified Foreign Financial Assets (T.D. 9567)

The New York State Society of Certified Public Accountants respectfully submits its comments to T.D. 9567 with respect to both Proposed Regulations REG-130302-10 and the related Temporary Regulations which pertain to the required reporting of foreign financial assets. According to this Internal Revenue Bulletin, the text of the temporary regulations also serves as the text of the proposed regulations, and, accordingly, we have addressed them both herein.

The Exception to the Definition of Specified Domestic Entities for Certain Domestic Trusts under Prop. Reg. § 1.6038D-6 Should Be Extended to Also Apply Where Such Trusts Are Not Required to File a Form 1041, U.S. Fiduciary Income Tax Return, or Any Information Returns (*§1.6038D-6(d)*)

Under the proposed regulations, domestic entities that are subject to the reporting requirements of section 6038D are designated as "specified domestic entities." These include certain domestic corporations, domestic partnerships, and domestic trusts within the meaning of section 7701(a)(30)(E).

The proposed regulations provide an exception to the definition of "specified domestic entities" for certain domestic trusts where a corporate trustee or bank "[t]imely files (including any applicable extensions) annual returns and information returns on behalf of the trust." (Prop. Reg. § 1.6038D-6(d)(2)(ii)). This exception, however, does not take into account the possibility that a domestic trust may not be required to file a Form 1041, *U.S. Fiduciary Income Tax Return* ("Form 1041"), or any information returns for a particular tax year. The instructions to the 2011 Form 1041 provide that a fiduciary must file Form 1041 for a domestic trust that is subject to tax under IRC Section 641 that has: (1) any taxable income for the tax year, (2) gross income of $600 or more (regardless of taxable income) or (3) a beneficiary who is a nonresident alien. Therefore, a domestic trust is <u>not</u> required to file Form 1041 for any year in which a domestic trust's gross income is less than $600 provided that it does not have any taxable income for that year and does not have a nonresident alien beneficiary.

We believe that it would be fully consistent with the Proposed Regulations' objective to exclude compliant corporate trustees and banks from Form 8938 (Statement of Specified Foreign Financial Assets) reporting in the case of domestic trusts that are not required to file a Form 1041 (and which do not file such return). Accordingly, the regulations should expand the scope of this exception to the definition of "specified domestic entities" to apply as well to domestic trusts for which the corporate trustee or bank is not required to file any annual returns and information returns on behalf of the domestic trust.

Exemption for a De Minimis Number of Days

Form 8938 reports both the specified foreign assets and their related income. Frequently, there can be valid reasons to transfer funds temporarily into a foreign account for a short period of time. Reporting such accounts on the Form 8938 would provide little informational value to Treasury because the income generated on such funds would be minimal.

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In addition, such an account will be reported on the Form TD F 90-22.1 Report of Foreign Bank and Financial Accounts (the "FBAR") due to the significantly lower FBAR reporting threshold of $10,000 for any point in the calendar year as compared to the Form 8938 reporting requirement of $ 50,000.

We therefore propose an exemption for a minimum number of days, such as 15 days, for funds transferred into an account for a short period of time provided that the income generated from such foreign account does not exceed a specified amount such as $1,000.

Penalties

Consideration in the assessment of penalties should be given to the fact that specified persons will often have difficulty in valuing certain assets. If there is an error in their valuation – for example, their valuation brings them below the threshold but it is later determined that their specified foreign financial assets exceeded their individual reporting threshold – the specified individual will be subject to a failure to file penalty of $10,000 unless reasonable cause can be shown.

Reg. §1.6038D-8T(e)(2) provides for an affirmative showing in order to show the failure to disclose is due to reasonable cause and not due to willful neglect, but an affirmative showing still may be difficult to prove when working with valuations. Areas which we foresee this to be particularly problematic are the valuation of trusts (Reg. §1.6038D-5T(f)(2)) and interests in estates, pension plans and deferred compensation arrangements (Reg. §1.6038D-5T(f)(3)) that are each considered to be specified foreign financial assets. Reg. §1.6038D-5T(f)(2)(ii) and Reg. §1.6038D-5T(f)(3)(ii) provide an alternative method for purposes of determining the aggregate value of an interest in such specified foreign financial assets, but in each case, if the true fair market value of the interest is later determined and it is greater than the amounts calculated pursuant to the alternative methods as provided in subparagraph (ii) of each section (thereby triggering a reporting requirement), the failure to file penalty is $10,000.

In light of these concerns, we propose a range of errors related to the various thresholds with a corresponding range in penalty as opposed to a flat $10,000 failure to file penalty. We also propose for the first year of filing (2011) that reasonable cause should generally be presumed to exist to encompass a broad range of errors as it will be difficult the first year to gather all of this information and also to be able to understand what exactly is required in order to accurately report such assets on the Form 8938.

In addition, §1.6038D-8T(c) provides that an additional penalty of $10,000 will be assessed every 30 days for which the failure to reply exceeds 90 days. We propose that in the

case when the specified person is attempting to collect the necessary information in order to accurately report the specified foreign financial assets on the Form 8938, this increased penalty should not be applicable if proof of the requests to obtain this information is submitted to the IRS (correspondence, e-mails, *etc*.)

Reporting an Interest in a Foreign Trust, Foreign Estate, Foreign Pension Plan or Foreign Deferred Compensation Plan

Neither Reg. §1.6038D-5T(f)(2)(i) or Reg. §1.6038D-5T(f)(3)(i) contain a specific provision to report $0 if the filer is unable to otherwise determine the fair market value of their interest and if there were no distributions received by the foreign trust, foreign estate, foreign pension plan or foreign deferred compensation plan. The instructions to Form 8938 under the caption "Valuing interests in foreign estates, foreign pension plans and foreign deferred compensation plans" provide "[i]f you received no distributions during the tax year and do not have reason to know based on readily accessible information the fair market value of your interest as of the last day of the tax year, use a value of zero as the maximum value of the asset." No similar language is provided in the instructions under the caption: "Valuing interests in foreign trusts."

We propose inserting a similar $0 based reporting provision under the caption "Valuing interests in foreign trusts." A discretionary beneficiary of a foreign trust could not determine the value of the right as a beneficiary to receive mandatory distributions as determined under IRC § 7520 because by definition, there are no mandatory distributions. By a strict read of §1.6038D-5T(f)(2)(i) or Reg. §1.6038D-5T(f)(3)(i), by default, (1) if no distributions were received, and (2) if one cannot calculate under IRC §7520, the value of the right to receive the mandatory distributions, there would be $0 reported, and pursuant to (ii) of each section, $0 should be used for determining the aggregate value threshold.

Exchange Rate

§1.6038D-5T(c) provides that the U.S. Treasury Department's Financial Management Service foreign currency exchange rate is to be used, unless there is no available exchange rate for a particular currency. Many financial institutions will provide reporting with both the foreign currency and the $US conversion on the statements.

We propose that if a large, well-known foreign financial institution converts the account balance on their reporting statements, the currency conversion rate reflected in the financial institution's reporting should be allowed in lieu of the additional administrative complexity of requiring the foreign currency to be converted using the U.S. Treasury exchange rate as described in the Regulation.

Clarification is Needed Concerning Disregarded Entities

Reg. 1.6038D-2T(b)(3) should be revised to clarify that a specified person will be treated as having an interest in any specified foreign financial assets held by a disregarded entity, *i.e.*, an entity disregarded as an entity separate from its owner as provided in § 301.7701-2(c)(2)(i).

Clarification Needed for Reporting of Joint Accounts for Joint Account Holders Who Are Not Married

There appears to be an omission in the providing of guidance on how to report joint accounts on the Form 8939 for joint account owners that are not married. See Reg. 1.6038D-2T(c)(1). (This section provides guidance how to determine the aggregate value of jointly owned accounts for: (1) joint account owners and not married, (2) joint account owners who are married and filing jointly and (3) joint account owners who are married and filing separately); and Reg. 1.6038D-2T(c)(2) (provides guidance how to report these accounts on the Form 8938 for (1) joint account owners who are married and filing jointly and (2) joint account owners who are married and filing separately but there is no guidance how to report joint accounts on the Form 8938 for those who are joint account owners and not married).

In addition, Reg. 1.6038D-2T (d) Example- should provide additional examples for joint asset owners who are not married. In this regard, there appears to be an incorrect cross-reference in the example set forth in Reg. 1.6038D-2T(d) Example- (2) to §1.6038D-4T(b). §1.6038D-**5**T contains the valuation guidelines but there are no specific valuation guidelines for jointly held assets by married specific individuals.

Additional Cross-Reference Needed re Financial Accounts in a U.S. Possession

An additional cross-reference should be added concerning financial accounts in a U.S. possession, as described below.

Reg. 1.6038D-3T (a)(2) provides: *Financial account in a U.S. possession. A specified foreign financial asset includes a financial account maintained by a financial institution that is organized under the laws of a U.S. possession;* but:

Reg. 1.6038D-1T (a)(9) defines Foreign financial institution and refers to IRC § 1471(d)(4) which specifically excludes a financial institution which is organized under the laws of any possession of the United States.

There should be a cross reference between the two Temporary Regulations with an emphasis that although Reg. 1.6038D-3T(a)(1) provides that a specified foreign financial asset includes any financial account maintained by a foreign financial institution (which is defined in Reg. 1.6038D-1T(a)(9)), by way of Reg. 1.6038D-3T(a)(2), any financial account held in a U.S. possession will be specifically included in the term "specified foreign financial asset."

Additional Consideration Should Be Given to Accounts Maintained by U.S. Payors

Reg. 1.6038D-3T(a)(3)- *Excepted financial accounts-(i) Accounts maintained by U.S. payors*- sets forth a contrary rule as compared to the reporting requirements of the FBAR, which requires accounts held by foreign financial institutions, regardless of the nationality of the payor, to be reported. Although there are many differences between the FBAR reporting and the Form 8938 reporting, this constitutes a major difference that should be clarified. For this reason, in

addition to the reference to §1.6049-5(c)(5)(i), there should be a description of which accounts are excepted, *i.e.*, "A financial account maintained by a U.S. payor and located outside of the U.S (as defined in §1.6049-5(c)(5)(i)) is not considered a specified foreign financial asset for purposes of section 6038D and the regulations." There should also be the following example.

(a) Example: Taxpayer A has two accounts located outside of the U.S and its territories/possessions, in foreign Country X:

Account A is owned by a bank which is a U.S. payor, US Bank, and Account B is owned by a bank which is a non U.S. payor, Foreign Bank. Both are located in Foreign Country X. Which account(s) are reported on Form 8938? For purposes of reporting specified foreign financial assets for purposes of section 6038D and the regulations, the account held at US Bank located in foreign country X is not reportable on the Form 8938 because it is a bank which is a U.S. payor. The account held at Foreign Bank in foreign country X is reportable on the Form 8938 because it is a bank which is a foreign payor.

Additional Guidance Needed Concerning Other Specified Foreign Financial Assets

Reg. 1.6038D-3T (b)(1) delineates three specific assets which are to be considered "Other specified foreign financial assets." Reg. 1.6038D-3T (d) provides "Examples" of assets other than financial accounts that may be considered other specified foreign financial assets. As listed, (1)-(3)(5) and (6) are examples of the three assets listed in Reg. 1.6038D-3T (b)(1). Accordingly, it would facilitate a greater understanding of these rules if these examples appeared immediately below the specific asset listing

Guidance Needed Concerning Certain Other Assets

Additional guidance is necessary in order to determine what other assets, such as foreign life insurance; foreign annuities; an interest in various pooled investment companies, such as foreign hedge funds, foreign private equity funds and foreign venture capital funds; and an interest in a foreign mutual fund or other similar pooled fund; and/or interests in foreign retirement plans and foreign pension plans, are to be considered "Other specified foreign financial assets" for purposes of Section 6038D and the regulations. Furthermore, additional examples of other assets not held in a foreign financial account should also be included under Reg. 1.6038D-3T (b)(1) "Other specified foreign financial assets."

Similarly, additional guidance is necessary in order to determine what is not considered to be a specified foreign financial asset. The preamble to the temporary regulations provide in Section 2 D (3) "An interest in social security, social insurance, or other similar program of a foreign government" is not considered to be specified foreign financial assets but this specific exemption is not found in the Temporary Regulations themselves. Reg. 1.6038D-3T (b)(2) should be revised as follows and to include the following new section:

Reg. 1.6038D-3T (b)(2) Not considered specified foreign financial assets

(a) Mark-to-market election under section 475; and

(b) An interest in a social security, social insurance, or other similar program of a foreign government.

Consolidating Item

Reg. 1.6038D-3T (a)(3)(i) and (ii) should be moved to Reg. 1.6038D-3T (b) (2) Reg. 1.6038D-3T (d) (4) "interest in a foreign trust" —this should be removed as this is specifically addressed in Reg. 1.6038D-3T(c).

Clarifying Item

Reg. 1.6038D-5T(d) and (f) both provide that "unless the specified person has actual knowledge or reason to know based on readily accessible information that the value does not reflect a reasonable estimate of the maximum value of the asset." Examples should be provided to clarify what is meant by this language. Also, when determining the FMV of other specified foreign financial assets, Reg. 1.6038D-5T(f), please provide guidance as to whether any discounts can be applied for closely held companies such as lack of marketability or lack of control.

Incorrect Cross-References

Reg. 1.6038D-5T(c) refer to "paragraph (d) (2) of this section which does not exist.

The preamble to these Temporary Regulations, Section 4, and Paragraph C provide "the regulations do not require a specified person to obtain an appraisal by a third party in order to reasonable estimate the asset's fair market value." This should also appear in Reg. 1.6038D-5T.

Clarification is Needed Concerning the Elimination of Duplicative Reporting of Assets

The following items relating to the elimination of duplicative reporting of assets need to be clarified.

Reg. 1.6038D-7T(a) Elimination of duplicative reporting of assets- Section (1) provides that the specified person is not required to report a specified foreign financial asset on Form 8938 if the specified person "[r]eports the asset on at least one of the following forms timely filed with the Internal Revenue Service for the taxable year."

Significantly, not all of Forms as listed in (A) through (E) provide for the asset itself to be reported; instead, it may just be the income from the asset itself, *e.g.*, Forms 3520, 8621.

In addition, Reg. 1.6038D-7T(a)(1)(i) should be revised to read: "Reports the asset **or any income** derived from the specified foreign financial asset on at least one of the following forms timely filed with the Internal Revenue Service for the taxable year."

Further, Reg. 1.6038D-7T(a)(1)(i) should specifically include Form 8858 "Information Return of U.S. Persons With Respect To Foreign Disregarded Entities" because the owner of a disregarded entity is treated as having an interest in any specified foreign financial assets held by the disregarded entity. Therefore, if these assets are reported on a timely filed Form 8858, the detail 8938 reporting should be specifically eliminated, as with the listed forms in (A) through (E).

Other Clarifying Revision

Reg. 1.6038D-7T (a)(1)(i)(F) should be revised to read as follows:

> (F) Form 8858, "Information Return of U.S. Persons With Respect To Foreign Disregarded Entities" or
>
> (G) "Any other form… guidance; and" [the current (F) should now be (G)]

Comments to Form 8938

Finally, we propose that Form 8938 itself be revised to add a box at page two, Part IV, for the Form 8891 (which is listed in Reg. §1.6038D-4T (a)(10) and Reg. §1.6038D-7T (E)).