

FATCA – New Filing Requirements for Foreign Assets

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Congress and the IRS have determined that taxpayers need yet an additional form to file in order to report foreign held assets. This latest filing requirement will add to the Form TD F 90-22.1 – *Report of Foreign Bank and Financial Accounts (FBAR)*, Form 8865 – *Return of U.S. Persons With Respect to Certain Foreign Partnerships*, Form 5471 – *Information Return of U.S. Persons With Respect To Certain Foreign Corporations*, and the plethora of other foreign asset reporting requirements. Holding foreign assets has never been more difficult and potential very costly from a tax perspective.

As part of the Hiring Incentives to Restore Employment (HIRE) Act, The Foreign Account Tax Compliance Act (FATCA) was enacted March 18, 2010. The IRS states that “The Foreign Account Tax Compliance Act (FATCA) is an important development in U.S. efforts to improve tax compliance involving foreign financial assets and offshore accounts.” In order to implement the reporting requirements under FATCA the IRS has just recently released the final [Form 8938](#). Although FATCA has been in effect since enactment in 2010, its implementation has been delayed until the final form was published. As such, the 2011 tax return is the first return that will require this form to be attached.

The Form 8938 increases the scope of reportable assets and persons required to report foreign assets. For instance, certain private equity assets held through hedge funds that were exempted under the FBAR rules will now have to be reported on the Form 8938. Section 511 of FATCA creates a new IRC code section, Section 6038D. This code section sets forth the threshold filing requirements. Additionally, the IRS has published [guidance on their website](#) on who will be required to file the Form 8938.

Generally, you must file a Form 8938 if you are a specified individual. A specified individual is defined as:

- A U.S. citizen;
- A resident alien of the United States for any part of the tax year (see Pub. 519 for more information);
- A nonresident alien who makes an election to be treated as resident alien for purposes of filing a joint income tax return; or
- A nonresident alien who is a bona fide resident of American Samoa or Puerto Rico (See Pub. 570 for definition of a bona fide resident) **and**
- Any such person holds an interest in a specified foreign financial asset required to be reported.

A specified foreign financial asset is defined as:

- Any financial account maintained by a foreign financial institution, (with some exceptions)
- Other foreign financial assets held for investment that are not in an account maintained by a US or foreign financial institution, namely:
 - Stock or securities issued by someone other than a U.S. person

- Any interest in a foreign entity, and
- Any financial instrument or contract that has as an issuer or counterparty that is other than a U.S. person.

It should be noted that this will not encompass international equity assets held in a US-based mutual fund or issued through a US broker. Though, it ostensibly would apply to a non-US based mutual fund or foreign broker.

There are filing thresholds such that not everyone that qualifies above will have to file this form. For **unmarried taxpayers living in the US**, the threshold will be if the total value of all specified foreign financial assets is more than \$50,000 on the last day of the tax year or more than \$75,000 at any time during the tax year. For **married taxpayers filing a joint income tax return and living in the US**, the threshold will be if the total value of all specified foreign financial assets is more than \$100,000 on the last day of the tax year or more than \$150,000 at any time during the tax year. For **married taxpayers filing separate income tax returns and living in the US**, the threshold will be if total value of all specified foreign financial assets is more than \$50,000 on the last day of the tax year or more than \$75,000 at any time during the tax year.

There are special rules if you are a US taxpayer living abroad. These rules need to be reviewed carefully as they set forth a different standard of residency than found elsewhere in the IRC and regulations. Under the FATCA rules, a person is a taxpayer living abroad if:

- You are a U.S. citizen whose tax home is in a foreign country and you are either a bona fide resident of a foreign country or countries for an uninterrupted period that includes the entire tax year, or
- You are a US citizen or resident, who during a period of 12 consecutive months ending in the tax year is physically present in a foreign country or countries at least 330 days.

Note the second definition for US citizens living abroad and not qualifying under the first definition – you will have a requirement to file if you are present in the US for more than 35 days (or 36 this year). For US citizens living abroad, this could catch a few persons unexpectedly.

The thresholds are also different for a taxpayer living abroad with a filing requirement. The IRS states that you will be required to report if:

- You are filing a return other than a joint return **and** the total value of your specified foreign assets is more than \$200,000 on the last day of the tax year or more than \$300,000 at any time during the year; or
- You are filing a joint return **and** the value of your specified foreign asset is more than \$400,000 on the last day of the tax year or more than \$600,000 at any time during the year.

FATCA also added, as would be expected, draconian penalties similar to the FBAR penalties. IRC § 6662 allows the IRS to impose a 20% penalty on a substantial understatement of income tax for negligence and other non-fraudulent behavior. FATCA amended this section and added a potential penalty of 40% for any underpayment attributable to financial assets required to be disclosed pursuant to IRC § 6038D. Additionally, there is a stiff failure to file penalty of \$10,000.00 for failing



to file by the required filing date for the tax return. After being notified of the failure to file, the taxpayer will be fined an additional \$10,000.00 for each 30 day period during which they fail to file the return (capped at \$50,000.00).

Additionally, FATCA has extended the statute of limitations with respect to returns which contained errors in the filing of the Form 8938. Generally, if all the tax is paid and a Form 8938 filed timely, the statute of limitations will remain at the usual 3 year period. However, if a Form 8938 is not filed, the statute of limitations will not start to run on any income attributable to assets which should have been reported on the form. Even after filing the Form 8938 and paying the tax due, the statute of limitations which respect to the form and the tax liability attributable thereto will be extended to 6 years if the amount of under-reporting of income from the reportable foreign assets was greater than \$5,000.00.

This tax season it is imperative to alert your tax professional if you have foreign held assets. Even if you consider them exempt from reporting, it best to let your tax preparer know about those assets. The penalties for improper reporting are quite severe and therefore foreign assets warrant increased attention.

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