

# NEW U.S. REPORTING FOR SPECIFIED FOREIGN FINANCIAL ASSETS

*Federal/International Tax Alert*  
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As tax filing season approaches, U.S. citizens and residents owning certain specified foreign financial assets (SFFAs) are reminded that they may have a new Internal Revenue Service (IRS) tax filing obligation, Form 8938 (Statement of Specified Foreign Financial Assets), beginning with their 2011 tax returns. By now, most U.S. taxpayers with foreign bank accounts are familiar with the Report of Foreign Bank and Financial Accounts (FBAR) on Form TD F 90.22-1, which is required annually if the aggregate value of such accounts exceeds \$10,000 during the tax year. Now, in addition to the FBAR, certain U.S. individuals are required to file Form 8938 with their U.S. tax return to report certain detailed information about their SFFAs as required by Section 6038D of the Internal Revenue Code.

## Specified Foreign Financial Assets

In addition to the types of non-U.S. financial accounts that are also reported on the FBAR, the term SFFA is broadly defined to include foreign financial assets held for investment that are not in an account—namely stock or securities of non-U.S. issuers, any interest in a non-U.S. entity, and any financial interest or contract that has as a non-U.S. issuer or counterparty. In general, an individual is not deemed to own an interest in an SFFA held by a corporation, partnership, trust, or estate solely because of an individual's status as a shareholder, partner, or beneficiary, but if an individual is considered an owner of all or a part of a trust under the grantor trust rules, he or she is considered to have an interest in any SFFA held by that part of the trust. Similarly, an individual with an interest in a disregarded entity is considered to own any SFFAs owned by that entity.

## Individuals Required to File in 2011; Domestic Entities Beginning in 2012?

For 2011, only specified individuals are required to file Form 8938: U.S. citizens, resident aliens of the United States for any part of the tax year (even if electing to be a nonresident under treaty residency tie-breaker rules), nonresident aliens who elect to be treated as a resident alien for purposes of filing a joint U.S. tax return, and certain residents of U.S. possessions. Proposed regulations have been issued that

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would require Form 8938 reporting by certain U.S. entities for taxable years beginning after December 31, 2011. However, if a person is not required to file a U.S. income tax return for the year, Form 8938 is also not required.

### Filing Thresholds

The Form 8938 reporting thresholds are more generous than the FBAR threshold and take into account a taxpayer's filing status and residency. For taxpayers living in the United States and filing a return other than a joint return, Form 8938 reporting is required if the total value of the SFFAs for the year is \$50,000 on the last day of the tax year or \$75,000 any time during the tax year. For taxpayers living in the United States and filing jointly, these thresholds increase to \$100,000 and \$150,000, respectively. For taxpayers living abroad and filing a return other than a joint return, the thresholds are \$200,000 and \$300,000, respectively. For taxpayers living abroad and filing a joint tax return, the thresholds are \$400,000 and \$600,000, respectively.

To qualify as living abroad for purposes of the higher filing thresholds, an individual's tax home must be in a foreign country and he or she must meet a presence-abroad test, which are the same as the qualifications for the "foreign-earned income" exclusion.

### Duplicative Reporting

If an individual would be required to file Form 8938 and has a SFFA that is reported on other U.S. information returns (e.g., Forms 3520, 3520-A, 5471, 8865, or 8891), the asset need not be reported on Form 8938, but the value is included in determining whether the threshold for filing is met, and Part IV of Form 8938 must be completed to disclose which and how many other information returns report the SFFAs. Note that the FBAR is not one of the forms that is treated as duplicative reporting; if a foreign financial account is required to be reported on the FBAR and Form 8938, it must be reported on both.

### Information Disclosed

The information required to be disclosed on Form 8938 depends on the particular type of asset, but generally includes basic identification of the account/asset; the name and address of the financial institution or of the issuer or counterparty of stock, securities, or financial instruments; the maximum value of the account/asset during the year; whether the account/asset was acquired or disposed of during the year; the amount of income, gain, or loss recognized during the year and the schedule, form, or return on which it is reported to the IRS; and the currency exchange rate used. In addition, with respect to interests in foreign entities, Form 8938 asks whether the entity is a passive foreign investment company.

## Consequences of Noncompliance

The consequences of not complying with the new Form 8938 reporting requirements can be harsh. The penalty for failing to file Form 8938 or to accurately report SFFAs is a minimum fine of \$10,000. If the taxpayer does not file a correct and complete Form 8938 within 90 days after IRS notice, the penalty is increased by \$10,000 for each 30-day period of noncompliance, up to a \$50,000 maximum. Reasonable cause may be asserted to avoid the penalty, but only if the taxpayer affirmatively shows the facts that support a reasonable cause claim. A foreign law restriction, whether civil or criminal, on disclosing the information required to be reported is not reasonable cause.

In addition, if a taxpayer underpays his or her U.S. tax as a result of a transaction involving an undisclosed foreign financial asset, the accuracy-related penalty is increased from 20 percent to 40 percent. If a taxpayer fails to file Form 8938 or fails to report an SFFA, the statute of limitations for all or part of the taxpayer's U.S. return for the tax year remains open until three years after a complete and accurate Form 8938 is filed. Moreover, if a taxpayer omits from gross income more than \$5,000 and the omission relates to a SFFA, the statute of limitations is six years from the date the return is filed.

New Form 8938 is just one of many tax and information returns that U.S. taxpayers with non-U.S. assets and accounts are required to file each year with the IRS, and it represents the IRS's latest efforts to collect as much information as possible about such assets from U.S. taxpayers. Given the significant penalties associated with Form 8938 reporting, the breadth of the information to be reported, and the issues many U.S. taxpayers have faced with respect to FBAR noncompliance, U.S. taxpayers should carefully review new Form 8938 and the regulations issued under Section 6038D to determine whether they are required to file Form 8938 with their U.S. tax returns beginning with the 2011 tax year.