

# SMITH CARMICHAEL ASSOCIÉS

Re: HIRE Act: Foreign Account Tax Compliance Requirements

In 2010, Congress passed the Hiring Incentives to Restore Employment (HIRE) Act. A section of the HIRE Act, called the Foreign Account Tax Compliance Act (FATCA), imposes additional reporting requirements on certain taxpayers holding specified foreign financial assets. Just before year-end 2011, the IRS released Form 8938, Statement of Specified Foreign Financial Assets, which taxpayers will use to report specified foreign financial assets if they are required to do so by FATCA. This letter describes the reporting requirements under FATCA and Form 8938.

Form 8938 reporting under FACTA applies for “specified foreign financial assets” in which the taxpayer has an interest in tax years starting after March 18, 2010. For most individual taxpayers, the IRS has explained that this means they will start filing Form 8938 with their 2011 income tax return.

FATCA reporting applies to individuals. The IRS has explained in regulations that a specified individual for purposes of FATCA is a person owning specified foreign financial assets and the value of the specified foreign financial assets is more than the applicable reporting threshold. At this time, a person includes any specified individual, or, to the extent provided in future IRS regulations or other guidance, a specified domestic entity. More guidance about specified domestic entities is being prepared by the IRS.

Who must report?

Determining who must report under FATCA as a specified individual requires answering a number of questions. First, a specified individual is:

A U.S. citizen

A resident alien of the U.S. for any part of the tax year

A nonresident alien who makes an election to be treated as resident alien for purposes of filing a joint income tax return

A nonresident alien who is a bona fide resident of American Samoa or Puerto Rico

Second, a specified individual also has an interest in a specified foreign financial asset that is required to be reported.

A specified foreign financial asset is:

Any financial account maintained by a foreign financial institution, except as indicated above

Other foreign financial assets held for investment that are not in an account maintained by a US or foreign financial institution, such as 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.

Third, the aggregate value of the taxpayer’s specified foreign financial assets is more than the reporting thresholds that applies to the taxpayer.

Unmarried taxpayers living in the U.S.: The total value of the taxpayer's 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

Married taxpayers filing a joint income tax return and living in the U.S.: The total value of the couple's 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

Married taxpayers filing separate income tax returns and living in the U.S.: The total value of the taxpayer's 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.

Taxpayers living abroad. An individual is a taxpayer living abroad if (1) the individual is a U.S. citizen whose tax home is in a foreign country and the individual is either a bona fide resident of a foreign country or countries for an uninterrupted period that includes the entire tax year; or the individual is 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.

Example. Tyler and Amanda reside in California and file a joint federal income tax return. Tyler and Amanda jointly own a specified foreign financial asset valued at \$60,000. The IRS explained that Tyler and Amanda do not need to file Form 8938, Statement of Specified Foreign Financial Assets, because they do not satisfy the reporting threshold of more than \$100,000 on the last day of the tax year or \$200,000 on any day of the tax year.

There are some exceptions to reporting under FATCA. Please contact our office for more information about these exceptions.

#### Information to be reported

The required information varies depending on the type of specified foreign financial asset. Therefore, taxpayers with an interest in:

Foreign bank accounts must provide the name and address of the financial institution where the account is maintained, and the account number;

Foreign-issued stocks and securities must provide the name and address of the issuer, and all pertinent information that allows the class or issue of such stock or security to be identified; and

Foreign instruments, contracts, or entities must provide the names and addresses of all foreign issuers and counterparties, the maximum value of the asset during the tax year, and all pertinent information required to identify the foreign asset.

FATCA also requires a withholding agent to deduct and withhold a tax equal to 30 percent on any withholdable payment made to a foreign financial institution if the foreign financial institution does not meet certain requirements. There are exceptions and special rules in situations where there is an agreement in effect between the financial institution and the Secretary of the Treasury.

A withholding agent includes any person, in whatever capacity, having the control, receipt, custody, disposal, or payment of any payment of interest (including OID), dividends, rents, salaries, wages,

premiums, annuities, compensations, remunerations, emoluments, and other fixed or determinable annual or periodic gains, profits, and income from sources within the U.S..

#### Penalties

The penalty for failing to disclose the required information in a timely manner is \$10,000. If the failure to disclose continues for more than 90 days after the IRS notifies the taxpayer of a failure to report, the taxpayer must pay an additional \$10,000 for each 30-day period (or fraction thereof) during which such failure continues after the expiration of the 90-day period. The maximum penalty is \$50,000. However, no penalty is imposed if the failure to disclose is due to reasonable cause, and not due to willful neglect. The IRS has cautioned that the fact that a foreign jurisdiction would impose a civil or criminal penalty on the taxpayer if the taxpayer discloses the required information is not reasonable cause. In addition, penalties for underpayment and fraud may apply as well as criminal penalties.

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