

Foreign Tax Issues For US Citizens

By:

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Summary

Whether here or overseas, US taxpayers face a myriad of issues and must contend with countless special forms. This course will help the practitioner assist his American clients as they live, travel and work abroad. Topics will include foreign earned income and foreign housing, the foreign tax credit, information for military personnel, inter-agency cooperation, and tax avoidance schemes.

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

“Unlike most other nations, the United States operates under a world-wide tax system”¹ which means that US citizens and resident aliens will owe taxes to the US, even if their foreign source income is also subject to taxation abroad. To mitigate tax liabilities resulting from double taxation, US taxpayers may avail themselves of an exclusion for foreign earned income and/or a foreign tax credit for duplicative taxes paid to another government.²

Often, US tax liabilities can be significantly reduced or eliminated altogether. Depending on applicable regulations in the host country, US citizens may or may not be liable for taxes abroad; the focus of this manual, however, is on US tax law only.

II. US Citizens Living Abroad³

US citizens and resident aliens living abroad have the same filing requirements as those living in the US. All amounts of income and expenses must be reported in US dollars on the tax return. The prevailing exchange rate at the time the income was received or the expenses paid should be used.⁴

Extensions

If the taxpayer is living outside of the US on the due date of his return (April 15th), he will receive an automatic two-month extension (until June 15th) to file and must attach a statement of explanation to his return when filing. The taxpayer will receive an automatic six-month extension (until October 15th) if he files **Form 4868**.⁵ He may choose to file **Form 4868** as late as June 15th, but will then still only receive an extension until October 15th.

Withholdings

US employers must withhold US income tax from wages paid to US citizens living abroad, unless the employer is required by law to withhold foreign income tax. If the taxpayer expects to be eligible for the Foreign Earned Income or Foreign Housing

¹ Stancil, *Saving Taxes on Foreign Earned Income*, NATP TAXPRO Journal Summer 2013 [available at <http://www.natptax.com/Publications/TaxPro%20Library/summer2013TaxesForeignEarnedIncome.pdf>, last accessed May 27, 2014].

² **TIP:** Sometimes it is more beneficial to claim a credit rather than an exclusion if the tax rate in the foreign country is higher than that to which the taxpayer is subject in the US or if the taxpayer is ineligible to claim the exclusion. However, the exclusion has the obvious benefit of removing income from the tax equation as well as reducing AGI for purposes of computing Schedule A and other limitations. A taxpayer’s choice to use the credit or the exclusion is binding in the year first made and all future years unless revoked by attaching a statement to **Form 1040**. Once revoked, the election cannot again be changed for 5 years without IRS consent.

³ See *IRS Publication 54—Tax Guide for US Citizens and Resident Aliens Abroad* for additional information.

⁴ Many online currency converters are available; for example, www.oanda.com/currency/converter/.

⁵ In the alternative, **Form 2350** may be filed if a taxpayer expects to file **Form 2555** and needs the time to meet either the Bona Fide Residence or the Physical Presence tests to qualify for the Foreign Earned Income and/or the Foreign Housing exclusions or deduction.

exclusions, he may use **Form 673 Statement for Claiming Exemption From Withholding on Foreign Earned Income Eligible for the Exclusion (Provided by Section 911)**, exempting the employer from US withholding requirements.

III. **Military Personnel**

Includes all uniformed members serving in the Army, Navy, Air Force, and Coast Guard.⁶

The following items of income are includable as taxable income:

- Active and reserve duty pay
- Special pay, including hostile fire and special duty
- Re-enlistment bonuses, leave and other payments

The following items are excludable:

- Combat zone pay as designated by Presidential Order
- Living, death, family, moving and travel allowances
- In-kind military benefits, including medical and dental care

Extensions

Military personnel are entitled to an automatic two-month filing extension if serving outside of the US. Those on duty in a combat zone receive an additional grace period of 180 days. **NOTE:** Those taken hostage receive automatic extensions until the 15th day of the third month after their eventual release.

If a member of the US Armed Forces dies while on active duty in a combat zone, his entire income tax liability is forgiven for the year of death and one preceding year.

IV. **Available Exclusions and Deductions**

To qualify for foreign earned income exclusions and deductions, the taxpayer must:

- have foreign earned income
- be either a US citizen or resident alien who resides in a foreign country for at least one full tax year from January 1st through December 31st (Bona Fide Residence Test)⁷ or is physically present in the foreign country for at least 330 days⁸ during any consecutive 12-month period (Physical Presence Test)⁹ AND

⁶ See *IRS Publication 3—Armed Forces Tax Guide*.

⁷ **NOTE:** The Bona Fide Residence test is not satisfied automatically once a taxpayer has resided in the foreign country for a full tax year. In fact, if a taxpayer has made a statement to foreign authorities that he is not a resident of the host country and he has been granted an exemption from local income taxation, he will be unable to satisfy the Bona Fide Residence Test required for the Foreign Earned Income Exclusion.

⁸ Only full days spent in the foreign country count; thus, travel days and dates of arrival and departure are not included in the count. **NOTE:** The taxpayer is not required to be employed when counting days but may be retired or on vacation as long as he does not return to the US for more than 35 days in any 12-month period.

⁹ If the taxpayer satisfies the Physical Presence Test in a period that spans two tax years, he may claim a pro-rated portion of the exemption in each year. Example: Craig moved abroad on August 2, 2013 and will satisfy the 330-

- have a tax home in a foreign country (with no abode in the US)

A “tax home” may be (a) the taxpayer’s main place of business or employment, or (b) the place where he is permanently or indefinitely engaged to work, and (c) may depend on whether the work is temporary (less than one year) or indefinite. Example: An itinerant’s tax home is wherever he works.

A “foreign country” is defined as any territory under the sovereignty of a government other than that of the United States and does not include US possession such as Guam, American Samoa, US Virgin Islands or Puerto Rico.¹⁰ Based on this definition, the 7th Circuit Court of Appeals upheld IRS denial of a taxpayer’s claim for the Foreign Earned Income Exclusion. Arnett, a US citizen, attempted to exclude wage income of \$48,894 earned while working at McMurdo Station in Ross Island, Antarctica. However, Antarctica has been deemed to be a sovereign-less region based on the Antarctic Treaty of 1961 that provided that the continent was to be used for peaceful and scientific purposes and that all questions of sovereignty would be put into abeyance.¹¹

Amanda is a US citizen who lives and works abroad. She has lived in Germany for 14 months—from September 1, 2009 through October 31, 2010. However, she is unable to meet the Bona Fide Residence Test since she has not been in Germany for a full *calendar year*. Instead, she is able to pass the Physical Presence Test.

Nick is employed on an offshore oil rig in the territorial waters of Scotland and works a 28-day on/28-day off schedule. He returns to his family residence in the US during his off periods. He is considered to have an abode in the US and does not satisfy the tax home test in the foreign country. He cannot claim the exclusions.

Bob is a marketing executive with a US company which transferred him to London for a minimum of 18 months. Before he left, Bob distributed business cards showing his new business and home addresses in London. He kept ownership of his US house, but rented it to another family after moving his family, furniture and pets to London. He and his wife obtained British driving licenses, opened local bank accounts and joined a neighborhood civic association. Bob’s abode is in London—he satisfies the tax home test in the foreign country.

The time limits for the Bona Fide Residence or Physical Presence tests may be waived if the taxpayer is forced to leave the foreign country due to war or civil unrest as determined annually by Internal Revenue Bulletin.¹²

day requisite time limit by June 29, 2014 if he does not return to the US in the interim. Once he satisfies the test and files his 2013 return, he may claim an exclusion equal to \$40,110 [= 150/365 days X \$97,600].

¹⁰ Treas. Reg. 1.911-2(h).

¹¹ *Arnett v. Comm.*, 2007-1 USTC 50,162; 7th circ. 06-1934.

¹² For example, the IRS has just announced that residency requirements may be waived for Haiti (on or after January 13, 2010) and Cote d’Ivoire (on or after December 19, 2010). *Federal Tax Alert*, May 2011, 10. In 2011, the following countries were eligible for waiver: Egypt (on or after February 1, 2011), Libya (February 21), Syria

TIP: If a taxpayer is unable to satisfy the Bona Fide Residence or Physical Presence tests by the due date of his return but expects to meet the requisite time limits to claim the Foreign Earned Income Exclusion, he may submit **Form 2350 Application for Extension of Time to File US Income Tax Return** to Department of the Treasury – Internal Revenue Service Austin, TX 73301-0045.

Generally, an extension will be granted until 30 days after the date on which the taxpayer satisfies the time limit under the tests.¹³ This form may be filed only once for each move overseas; once the taxpayer meets either time test and remains abroad continuously, he must file **Form 4868** to request an extension for any future year. As with all extensions, a **Form 2350** extension merely extends the time for filing but not payment – a taxpayer, who believes he will owe tax, should submit a payment with his extension application on or before April 15th.

Once the Physical Presence Test has been satisfied, the taxpayer may check to see if he can amend a prior-year return on which he did not claim the income exclusion because he had not yet been in-country for the requisite 330 days.

If the taxpayer resides in a foreign country in violation of US law,¹⁴ neither of the tests can be met and thus, the taxpayer is not eligible for the exclusions.

Foreign Earned Income must be paid for personal services performed and includes wages, salaries, commissions, bonuses, professional fees, tips and self-employment income. It does not include:

- The value of meals and lodging
- Pension or annuity payments
- Social Security or Medicare benefits
- US government salaries paid to civilian or military personnel
- Income for services performed in international waters or in specific combat zones
- Investment or passive income
- Gambling winnings
- Alimony

(April 25), and Yemen (May 25). In 2012, waivers were granted for Central African Republic (December 28), Sudan (September 15), and Tunisia (September 15). In 2013, waivers were granted for Egypt (July 3), Lebanon, (September 5), Pakistan (August 9) and Yemen (August 6).

¹³ An extension may be granted up to 90 days after the end of the year following the year you moved to the foreign country, if moving expenses are required to be allocated.

NOTE: An extension of time to file (but not pay) an income tax return also extends the time to file **Form 709 Gift and Generation-skipping Transfer Tax Return**.

¹⁴ Cuba is still the only country to which travel restrictions have been continuously applied. However, IRS Notice 2006-84 provides that civilian individuals who are performing services at the US Naval Base in Guantanamo Bay Cuba are eligible for Foreign Earned Income and/or the Foreign Housing exclusions, provided that they otherwise meet all of the usual eligibility criteria.

The source of the income is determined by the location of the payee, not by the nationality or locale of the payer.

Lastly, it should be noted that the exclusion may only be claimed by filing a tax return. Thus, **Form 1040** must be prepared whether or not that taxpayer expects to have a tax liability.

A. Foreign Earned Income Exclusion

The maximum exclusion for 2014 is the lesser of \$99,200/year or the amount of the foreign earned income less any foreign housing exclusion claimed. If both spouses work in a foreign country and meet the qualifications for the exclusion, up to \$198,400 of foreign earned income can be excluded in 2014. The excludable limit is adjusted annually for cost-of-living.¹⁵

NOTE: Although excluded, foreign earned income may still be subject to Social Security taxes under some circumstances.

The election to claim the exclusion can be made on a timely filed return or a late-filed return within one year after the original due date.

If the exclusion is claimed, the taxpayer may not take the Foreign Tax Credit for taxes paid on the excluded income and is ineligible to claim the Earned Income Credit.

B. Foreign Housing Exclusion

Amounts received for employer-provided housing (less a government-calculated base amount) are eligible for the exclusion.

The base amount is calculated as follows:

- 16% of the amount (computed on a daily basis) of the Foreign Earned Income Exclusion for the calendar year in which the tax year begins
 $\$99,200 \times 16\% = \$15,872$ divided by 365 days = \$43.48/day

Multiplied by

- The number of days of the tax year within the applicable period of foreign residence (bona fide residence test) or presence (physical presence test) for that tax year

The allowable Housing Exclusion is limited to 30% of the Income Exclusion [$\$99,200 \times 30\% = \$29,760$ divided by 365 days = \$81.53/day]. Thus, only housing costs in excess of \$43.48/day and less than \$81.53/day are excludable – resulting in a maximum exclusion of \$13,888 in 2014.

¹⁵ The maximum exclusion amounts in prior years were: \$76,000 (2000), \$78,000 (2001), \$80,000 (2002 – 2005), \$82,400 (2006), \$85,700 (2007), \$87,600 (2008), \$91,400 (2009), \$91,500 (2010), \$92,900 (2011), \$95,100 (2012), and \$97,600 (2013).

NOTE: Certain high-cost locales¹⁶ are eligible for additional exclusion amounts.¹⁷

Unless self-employed, all earnings are considered employer-provided, making the entire housing amount eligible for exclusion. To clarify, housing costs incurred by employed individuals are eligible for exclusion whether paid by the employer or by the employee, since it is presumed that employees use employer-provided funds (i.e., wages) to pay for these expenses. Do not be confused or dissuaded from claiming the exclusion due to the bureaucracy's poor choice of wording – "employer-provided housing" includes all employee housing.

Housing expenses include rent, repairs, utilities, real and personal property insurance, occupancy taxes, furniture rental, and residential parking. Expenses not eligible for the exclusion are deductible mortgage interest and property taxes, cost of purchasing a property, cost of domestic labor, leasehold and homeowner's improvements, and depreciation.

Tom was a bona fide resident of and had his tax home in Ghana from August 17, 2007 through the end of the year, while his wife Jane began her residency one month later on September 15th. Tom paid \$10,000 for housing expenses; \$7,500 of this amount was incurred from September 15th through the end of the year. Jane paid \$3,000 for housing expenses.

Although Tom and Jane will file jointly, they can choose to let either Tom or Jane claim the housing exclusion in hopes of maximizing the allowable tax benefit:

- If Tom claims the housing exclusion, the couple's combined housing exclusion would be \$7,890 (= \$13,000 less the government-calculated base amount of \$5,110).
- If Jane instead claims the housing exclusion, their allowable exclusion would be \$6,480 (= \$10,500 expenses less the government-calculated base amount of \$4,020).

On **Form 2555**, the housing exclusion must be elected before the foreign earned income exclusion because, as the IRS explains on its website:¹⁸

The foreign earned income exclusion is limited to the actual foreign earned income minus the foreign housing exclusion. Therefore, to exclude a foreign housing amount, the qualifying individual must first

¹⁶ Listed in the Instructions for **Form 2555**.

¹⁷ Notice 2006-87, I.R.B. 2006-43, October 6, 2006. For example, the limitation on Housing Expenses for 2014 in Hong Kong is \$114,300. High costs areas for 2014 are listed in IRS Notice 2014-29 [available at <http://www.irs.gov/pub/irs-drop/n-14-29.pdf>, last accessed May 26, 2014].

¹⁸ <http://www.irs.gov/Businesses/Foreign-Earned-Income-Exclusion-1> [last accessed May 26, 2014].

figure the foreign housing exclusion before determining the amount for the foreign earned income exclusion.

This is often interpreted this to mean that the housing amount must be deducted from total foreign earned income to arrive at the excludable amount for income exclusion purposes; thus, the combined total exclusion could not exceed the annual threshold amount. Indeed, while foreign housing expenses may not exceed total foreign earned income for the taxable year, a taxpayer may nevertheless elect to claim the Foreign Housing Exclusion in addition to the Foreign Earned Income Exclusion, resulting in a combined exclusion that exceeds the annual threshold.

In 2012, Joe's foreign earned income exceeded the annual limitation of \$150,000. Joe was eligible to claim the Foreign Earned Income Exclusion (up to \$95,100) as well as the Foreign Housing Exclusion for costs totaling \$37,480. Joe's total 2012 exclusions equaled [$\$132,580 = \$95,100$ plus $\$37,480$].

Returning now to **Form 2555**, look at Page 3: There you will find Housing Exclusion is calculated first on Line 36; the Income Exclusion is calculated next on Line 42; and the total allowable exclusion is calculated on Line 43 by combining Lines 36 and 42.

NOTE: Although amounts excluded under the income and housing exclusion are not taxed, they are nevertheless added back when computing regular and alternative minimum tax liabilities; thereby bumping taxable income into higher marginal tax brackets.

Taxpayer has \$80,000 of foreign earned income eligible for the exclusion plus \$20,000 of other non-excluded income which will be taxed at the marginal rate applicable to \$100,000 (not \$20,000).

C. Foreign Housing Deduction

This deduction is *available only to the self-employed* and is limited to foreign earned income less any foreign earned income and/or housing exclusions claimed. Disallowed deductions in excess of the limitation may be carried over for one year only.

The deduction is calculated in the same manner as the housing exclusion but claimed on the front page of the taxpayer's **Form 1040** as an adjustment to gross income.¹⁹ Thus, the deduction offers the taxpayer the possibility that he may actually exclude more from his taxable income than might otherwise be allowed by the foreign income and housing exclusions alone.

¹⁹ Enter amount from **Form 2555**, Part IX, Line 50 on **Form 1040**, Line 36 with the notation "Form 2555". Add this amount to all other adjustments claimed on Line 36 and subtract from gross income to arrive at Adjusted Gross Income (AGI).

In 2012, Felipe's total foreign earned income was \$130,000, of which half was from self-employment and half from services as an employee. Therefore, half of his total housing amount of \$12,000 is considered to have been provided by his employer, allowing Felipe to claim \$6,000 as a housing exclusion. The remainder is eligible for the housing deduction. However, because Felipe has exceeded the limitation (\$95,100 in 2012) he must carry the \$6,000 deduction forward and hope that he can claim the deduction in 2013.

D. Forms to File

- **Form 2555 Foreign Earned Income** must be attached to the tax return
- **Form 2555-EZ** may be used if foreign earned income is less than the maximum exclusion amount, the taxpayer is not self-employed, and the taxpayer does not claim the housing exclusion or deduction

E. Do the Exclusions Work?

The foreign income and housing exclusions have been available to US taxpayer living and working abroad since 1926; ostensibly, to encourage parity and make it more affordable for employers abroad to hire US citizens rather than local residents. A recent review by the Government Accountability Office (GAO) discovered that 445,000 taxpayers claimed the Foreign Earned Income Exclusion in 2011, roughly 0.3% of all individual returns filed. About 17% of taxpayers who claimed the income exclusion, also claimed the housing exclusion. More than half of the filers reported working for foreign employers. By claiming the allowable exclusions, 88% of US taxpayers filing from overseas were exempt from US taxation [many were also not subject to taxation in the countries of their foreign residence].

The GAO was asked to evaluate the efficacy of modifying or eliminating the available exclusions and found that ""in terms of good tax policy, there is room for debate regarding how potential revisions to the current tax expenditure may affect choices about where to work and who to hire. It may have positive and negative effects on both the efficient allocation of labor resources, but the magnitude of these effects is unknown, making it unclear whether the tax expenditure provides any net economic benefits."²⁰ However, the GAO suggested that "targeted tax relief" for extreme cost of living areas may be justified.

V. Foreign Tax Credit

A taxpayer may elect to claim either a credit (using **Form 1116 Foreign Tax Credit**)²¹ or a deduction (using **Schedule A Itemized Deductions**) for income taxes paid to foreign

²⁰ Godfrey, *Review Of Tax Exemption For American Expats Inconclusive*, Tax-News, Global Tax News [available at http://www.tax-news.com/news/Review_Of_Tax_Exemption_For_American_Expats_Inconclusive_64766.html, last accessed May 26, 2014].

²¹ Certain taxpayers may claim the credit without filing **Form 1116** by entering the amount of the credit on **Form 1040**, Line 47 if all of the following apply:

governments. This election applies to all foreign income taxes uniformly for any given tax year but can be amended within 10 years from the due date of the return.

Credits and deductions are disallowed for foreign income taxes paid on earnings excluded under the Foreign Earned Income or Foreign Housing exclusions, as well as foreign taxes:

- attributable to countries not recognized by the US government;
- excludable from US taxation based on international treaties;
- that would be refundable if the taxpayer filed a claim;
- of US persons controlling foreign corporations or partnerships;
- in connection with certain oil and gas transactions as well as mineral rights;
- on dividends from stock that has been held less than 16 days; and
- that are deductible only as Itemized Deductions (e.g. property and value-added taxes)

The tax credit or deduction is limited to the amount of US tax that would be attributable to the foreign income had it been taxed by the US, but cannot exceed the actual foreign tax paid.

A US citizen taxpayer was eligible to exclude his foreign earned income and did exclude \$70,000 wages earned in India where he paid foreign income tax of \$10,000. He also received dividends from India in the amount of \$2,000 and paid a foreign income tax of \$600 thereon. He can use the \$600 tax payment for his foreign tax credit because the dividends relating to it were subject to US tax, but cannot claim a credit against the income tax of \$10,000 since it was paid on US-excluded income.

Income tax rates in Germany may be as high as 60% but because the tax rate on the same income in the US is only 25%, that taxpayer may not claim a credit for the excess tax. However, he may carry the unused credit forward to future years.

-
- All foreign source income is “passive category income” derived from interest and dividends which have been reported on Forms 1099 or Schedule K-1;
 - The shares of stock generating dividend income have been held for at least 16 days;
 - **Form 4563 Exclusion of Income for Bona Fide Residents of American Samoa** is not filed;
 - Total foreign tax liability is under \$300 (\$600 if filing jointly); and
 - All foreign taxes were legally owed, not eligible for a refund, and paid to a country that is recognized by the US and does not support terrorism.

Tax Computation

To compute the maximum allowable credit:

$$\frac{\text{Foreign Source Taxable Income}}{\text{Worldwide Taxable Income}} \times \text{US Income Tax before Credit}$$

If the other country has a higher tax rate than the US there will be unused credits which may be carried back 1 year and forward 10 years; they expire if unused. If the other country has a lower tax rate than the US, the taxpayer will be required to pay the difference.²²

Several items to note when computing the Foreign Tax Credit:

- Foreign source income must be adjusted for foreign capital gains that are eligible for reduced rates, including long-term, collectible, un-recaptured §1250 and §1231 gains.
- Interest expense must be apportioned between US and foreign source income.
- Charitable contributions are not apportioned against foreign source income.

Deduction versus Credit

Taxpayers may choose to claim a credit for foreign taxes paid by filing **Form 1116** or a deduction by filing **Schedule A**. The election may be changed annually but once elected, it applies to *all* foreign taxes paid or accrued during that tax year. While a credit generally yields a larger tax benefit, it may sometimes be better to claim a deduction, particularly if the taxpayer has incurred foreign taxes ineligible for the credit. On the other hand, a credit may be advantageous if the taxpayer's itemized deductions are less than the Standard Deduction or he plans to carry his unused tax credit into other tax years.

VI. Miscellaneous Provisions

A. Charitable Contributions

Generally, contributions to *foreign* charitable and religious organizations cannot be deducted. However, contributions to US charities which forward funds to foreign entities are allowable, as long as the US organization controls the use of the funds.

NOTE: Treaty provisions allow for deductions made to certain Canadian, Israeli, and Mexican organizations.

B. Moving Expenses²³

US citizens and residents may deduct the cost of moving household goods and personal effects (including in-transit or foreign-move storage expenses) and

²² Adams, *The Foreign Tax Credit Explained* [available at <http://americansabroad.org/files/3913/3589/8026/foreigntaxcreditadams.pdf>, last accessed May 27, 2014].

²³ Use **Form 3903 Moving Expenses**.

travel expenses (including lodging but not meals) for one trip by the taxpayer and each member of the household. If the time and distance tests are satisfied, the deduction will be taken above-the-line on **Form 1040**, Line 26.

Distance Test

The distance between the taxpayer's new job location and former house must be at least 50 miles more than the distance between the old job location and former house.

Time Test

The taxpayer must work as a full-time employee at the new location for at least 39 weeks in the 12-month period following the move. Self-employed individuals must work full-time for at least 39 weeks during the first 12 months and a total of at least 78 weeks during the first 24 months after arriving at the new job location. The time test is waived in the event of involuntary separation from the new job and for members of the Armed Forces on active duty who move because of a permanent change of station.

NRAs may only deduct the cost of *inbound* moves to the US, subject to the time and distance restrictions listed above.

VII. Taxpayer Concerns

A. Inter-agency Information Sharing

Although the IRS and Social Security Administration (SSA) routinely exchange information reported on **Forms W-2**, neither agency shares any detailed information with the USCIS which is generally prohibited by IRC § 6013.²⁴

The Department of Homeland Security maintains the Verification Information System (VIS), a nationally accessible database that includes limited citizenship, immigration, and employment status information. VIS enables the implementation of two programs: Systematic Alien Verification for Entitlements (SAVE) and E-Verify. SAVE is used to verify citizenship and immigration status of individuals applying for government benefits; while E-Verify is a free and voluntary program for any US employer wishing to verify the identity and employment authorization status of newly hired employees based, in part, on data provided by the SSA.

²⁴ “In July 2004, we reported that data sharing between IRS and the United States Citizenship and Immigration Services (USCIS) has the potential to improve tax compliance as well as immigration eligibility decisions (GAO-04-972T)... Data sharing can help improve (1) tax compliance if businesses applying to sponsor immigrant workers are required to meet tax filing and payment requirements, and (2) the accuracy and timeliness of USCIS's immigration eligibility decisions if it obtained tax data from IRS to help ensure business sponsors meet eligibility criteria... [However,] no legislative changes have been made. On 9/15/09, USCIS said they have abandoned any work on the recommended pilot project, due to many management concerns, including public relations issues.” *Taxpayer Information: Options Exist to Enable Data Sharing Between IRS and USCIS but Each Presents Challenges*, GAO-06-100 October 11, 2005, available at <http://www.gao.gov/products/GAO-06-100> [last accessed May 27, 2014].

Undocumented (Illegal) Resident Aliens

Whether US residents have proper immigration status or not is irrelevant for tax purposes. These individuals are required to file income tax returns and report income in the same manner as US citizens and legal residents. Since illegal aliens are ineligible for SSNs, they must file **Form W-7 Application for IRS Individual Taxpayer Identification Number** to obtain an ITIN for tax filing purposes only—the ITIN does not provide work authorization or eligibility for Social Security benefits. **NOTE:** ITIN filers are also ineligible to claim the Earned Income Credit.

A practitioner preparing tax returns for an undocumented worker who has provided an improper or incorrect Social Security Number (SSN) to his employer should do the following:

1. List the properly issued ITIN at the top of the tax return and
2. Enter the incorrect SSN along with the remaining W-2 information

Despite the resulting mis-match between ITIN and SSN, the return can now be electronically filed.

B. Tax Avoidance Schemes

1. Expatriation Tax (a.k.a. Exit Tax)

US citizens who have renounced their citizenship and long-term US residents who have ended their residency may be subject to this tax for up to 10 years after the date of expatriation, if the principal purpose for their actions was tax avoidance.²⁵

Green Card holders may inadvertently forfeit their immigration status if working abroad and claiming the Foreign Earned Income Exclusion. By qualifying for the exclusion under the Physical Presence Test, which mandates that the taxpayer is away from the US for at least 330 days during any 12-month period, the individual may instead violate immigration laws which require him to be physically present *in* the US.

Citizenship is deemed relinquished if nationality is renounced before a US consular officer, a signed statement has been submitted to the State

²⁵ In recent times, it has been reported that Eduardo Saverin, the billionaire co-founder of Facebook, Inc. has renounced his citizenship prior to the company's initial public offering in the hopes of reducing his US tax bill and become a resident of Singapore which does not have a capital gains tax. While his holdings will be treated as sold on the date of expatriation and subject to the exit tax, the anticipated future appreciation of his holdings in the company will escape further US taxation. (Kucera, *Facebook Co-Founder Saverin Gives Up U.S. Citizenship Before IPO* as reported by Yahoo! Finance, May 11, 2012). US Senators Schumer (D) and Casey (D) promptly introduced a new bill intending to re-impose taxes on expatriates even after they flee the US and take up residence abroad. (Solomon, *On Eve of Facebook IPO, Eduardo Saverin Fires Back at Critics Over Accusations of Tax-Dodging* as reported by Forbes, May 19, 2012).



Department, the State Department issues a Certificate of Loss of Nationality, or a US court cancels a naturalized citizen's status.²⁶

The IRS will presume that avoidance was the primary purpose if:

- the taxpayer's average annual net income for the previous five years was in excess of \$155,000 in 2013, or
- the taxpayer's net worth is in excess of \$2 million, or
- the taxpayer is unable to certify that he has been in compliance with US tax laws for the preceding five years

Under certain circumstances, taxpayers may request an IRS ruling within one year from the date of expatriation to avoid the tax.

Exempt Individuals

- US citizens who relinquish their citizenship before age 18½ and were not residents for more than ten previous years
- Dual citizens if they are became citizens of the US and another country at birth AND have no substantial contact with the US, which means that they were never a US resident, never held a US passport, and were not present in the US for more than 30 days during any 10 calendar years prior to expatriation.

The tax is assessed on all US-source income and gains without the benefit of any otherwise applicable tax treaty rates.²⁷ All global assets are treated as sold on the day prior to expatriation at fair market value; resulting gains are taxed to the extent that they exceed \$668,000 in 2013 (indexed for inflation each year). **NOTE:** Expatriation becomes effective only after all notification and tax satisfaction certificates have been properly filed with the IRS and the Departments of State or Homeland Security.

Form 8854 Initial and Annual Expatriation Information Statement must be filed with a US consular office or federal court at the time of expatriation and may also be required to be filed annually thereafter. Failure to file may carry a penalty equal to the greater of 5% of the expatriation tax or \$10,000. Expatriates subject to the expatriation tax must also file **Form 1040NR** for each of the next 10 years after expatriation reporting US-sourced income only.

NOTE: Only US citizens and resident aliens are eligible for the Foreign Income Exclusion—since the expatriate has given up his citizenship, he is no longer entitled to this exclusion.

²⁶ IRC § 877A.

²⁷ IRC § 877.

Changing residency for state purposes may be equally challenging. California, for example, requires that a taxpayer must abandon his California domicile as well as physically move out of state with an intent to remain permanently or indefinitely in the new location, although intent alone is not sufficient.²⁸ Each taxpayer's situation will be evaluated based on facts and circumstances, including sale of the California residence; change of job; the establishment of business and social ties in the new state; even discontinuation of similar ties in California.

2. Foreign Cash

Each individual who receives or distributes any non-US currency or other monetary instrument, whether shipped, mailed or physically transported, in excess of \$10,000 at one time must file **Customs Form 4790 Report of International Transportation of Currency or Monetary Instruments**. Monetary instruments include foreign coins and currency, money orders, traveler's checks, securities and negotiable instruments in bearer form. Funds transferred through normal banking procedures are exempt. This form is due within 15 days after taking receipt of the transfer²⁹ and must be filed with the Commissioner of Customs – Currency Transportation Reports Washington, D.C. 20229.

VIII. Reporting Requirements for Foreign Accounts and Assets

A. Foreign Accounts³⁰

A US person must *electronically* file **FinCEN 114 Foreign Bank Account Report**³¹ if, at any time during the calendar year, he had a financial interest in or signatory authority over one or more foreign financial accounts with an aggregate value of \$10,000 or more.³²

²⁸ *Homer E. Noble v. Franchise Tax Board*, 118 Cal. App. 4th 560 (2004).

²⁹ Civil and criminal penalties for not filing **Form 4790** may apply and the transferred funds may be subject to forfeiture or seizure.

³⁰ 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. (*Not So Secret Swiss Bank Accounts*, SmartPros, January 3, 2012).

³¹ This form has replaced **Form TD F 90-22.1 Report of Foreign Bank and Financial Accounts** (FBAR) effective April 2013. FinCEN = Financial Crimes Enforcement Network.

³² Mandated by the Bank Secrecy Act of 1970 (codified as Title 31 of US Code).

Definitions

1. A US person is defined as a US citizen, a US resident,³³ 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 means that the individual can 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 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 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, Washington DC, US territories and possessions, as well as Indian lands). **Exceptions:** Military banking facilities and accounts located in Guam, Puerto Rico and US Virgin Islands.
5. Financial accounts may include monetary and non-monetary assets (e.g. banks, brokerage accounts, insurance cash values, annuities, and mutual funds, amongst others). Real and personal property is generally not included.

Each account must be valued separately at its highest value (any time during the calendar year) as reported to the account holder on periodic statements. The values must then be converted to US currency using the applicable exchange rate on December 31st. Only then are the converted values aggregated to determine whether the foreign account reporting threshold (\$10,000) has been met.

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.

³³ IRC § 7701(b).

Special Rules

1. Spouses may file a combined report to report joint accounts. All separate accounts must be reported individually.
2. Truncated filing is permitted for more than 25 accounts.
3. Consolidated filing is allowed for all types of entities.

Filing Deadline

The annual reporting cycle is on a calendar year basis (January to December). The deadline for filing **FinCEN 114** is June 30th every year. No extension is available.³⁴

Electronic Filing

E-file is now mandatory. Filers have the option to prepare and submit individual reports online at <http://bsaefiling.fincen.treas.gov/NoRegFBARFiler.html> or engage the services of a Bank Secrecy Act (BSA) e-File. 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 the 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.³⁵

Amendments and Corrections

Corrections to previously filed reports are 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.

Penalties

- \$10,000 maximum fine for failure to file
- Greater of \$100,000 or 50% of the account value, if willful violation
- Potential criminal sanctions & jail time

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.

³⁴ 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)

³⁵ 31 CFR 1010.430(d).

Offshore Voluntary Disclosure Program

The OVDP currently in effect is the fourth incarnation³⁶ 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.³⁷ 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. Certain taxpayers in limited situations may be eligible for a reduced penalty of only 5%³⁸ or 12.5%.³⁹ **NOTE:** IRS examiners have no authority or discretion to negotiate alternative penalty amounts under OVDP.

It is suggested that taxpayers who wish to participate in the program 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. 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. 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.

Quiet Disclosure

Taxpayers who choose to "quietly" file amended income tax returns to report previously omitted income from offshore accounts and pay the resulting tax,

³⁶ 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.

³⁷ OVDP is available for all foreign reporting, including **Forms 8938, 3520 and 5471**, as well as **FinCEN 114**.

³⁸ The taxpayer must be a foreign resident and meet all the following conditions for all covered years: (1) taxpayer resides in a foreign country; (2) taxpayer has made a good faith showing that he has timely complied with all tax reporting and payment requirements in the country of residency; and (3) taxpayer has \$10,000 or less of US source income each year.

³⁹ The taxpayer's highest aggregate account balance in each of the covered years covered must be than \$75,000.

penalties and interest, are eligible to participate in the 2012 OVDP program. Those who do not participate run the risk of eventual audit, full assessment of penalties, and referral to the Department of Justice for criminal prosecution for all applicable years.

NOTE: 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 should simply e-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.⁴⁰



WARNING: Because the penalties are high and the consequences extreme, tax 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."

B. Foreign Assets

In addition to foreign account reporting, certain taxpayers may be required to file additional 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.⁴¹ If the taxpayer is not required to file an income tax return, he does not have to file **Form 8938**.

The **Form 8938** filing requirement was enacted in 2010⁴² to improve tax compliance by US taxpayers with offshore financial accounts.⁴³ US citizens,

⁴⁰ 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 May 28, 2014].

⁴¹ IRC § 6038D.

⁴² Hiring Incentives to Restore Employment Act of 2010 (HIRE).

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).

Specified foreign financial assets include:⁴⁴

- Depository or custodial accounts at foreign financial institutions
- Stocks or securities issued by foreign persons
- Foreign pension or deferred compensation plans⁴⁵
- Any other financial instrument or contract held for investment that is issued by or has a counterparty that is not a US person
- Any interest in a foreign entity⁴⁶
- Gold certificates

Assets that do not have to be reported include:

- Foreign real estate (e.g., personal residence or rental property)
- 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)

⁴³ 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**. For now, IRS Notice 2013-10 has postponed the implementation of reporting requirements for domestic entities and trusts.

⁴⁴ IRC §1471(d).

⁴⁵ Canadian Registered Retirement Savings Plans, for example, are reportable.

⁴⁶ IRC § 6038D(b).

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**.⁴⁷ **NOTE:** If an owner of a Canadian Registered 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**.

Filing Thresholds

1. 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 31st 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.⁴⁸

2. Foreign Taxpayers

If residing abroad,⁴⁹ **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 31st 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.⁵⁰

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

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 31st.⁵¹

Penalties

- \$10,000 maximum fine for failure to disclose
- Plus \$10,000 additional penalty for each 30-day period after IRS issues its 90-day failure to disclose notification

⁴⁷ **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.

⁴⁸ Reg. § 1.6038D-2T(a)(1), Reg. § 1.6038D-2T(a)(2).

⁴⁹ “Foreign” taxpayers must satisfy the Bona Fide Residence or Physical Presence tests (IRC § 911).

⁵⁰ The regulations have not clarified filing threshold requirements for joint returns if one spouse resides abroad and the other lives in the US.

⁵¹ Taxpayer may use the Treasury Department Financial Management Service rate (available at <https://www.fms.treas.gov/intn.html>) or any accepted currency converter.

- Maximum penalty equals \$50,000⁵²

NOTE: The statute of limitations for a tax return 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 the form is due to reasonable cause, the open statute will apply only to the item(s) related to the failure.⁵³

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**.⁵⁴

Relief

The IRS announced⁵⁵ that procedures will go into effect September 1, 2012 to help non-compliant taxpayers resolve their delinquencies. Under the mandate, US citizens who live overseas and pose a “low compliance risk”⁵⁶ 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.”⁵⁷ These taxpayers should consult their legal advisers about the Offshore Voluntary Disclosure Program (OVDP) announced on January 9, 2012.

NOTE: Once a taxpayer makes a submission under the new procedures [see above], OVDP is no longer available. Furthermore, taxpayers who are ineligible to participate in OVDP are also ineligible to participate in the new procedure.

C. Form 3520 Annual Return to Report Transactions with Foreign Trusts and Receipt of Certain Foreign Gifts – US persons who receive \$100,000 or more in gifts and bequests from foreigners in a year must report those amounts on Form 3520 by April 15th of the following year. Additionally, US persons who

⁵² IRC § 6038D(d).

⁵³ IRC § 6501(c)(8).

⁵⁴ Additionally, a penalty equal to 40% of the resulting under-payment of tax will be assessed [IRC § 6662(b)(7)].

⁵⁵ IR 2012-65 (June 26, 2012).

⁵⁶ These taxpayers generally file simple returns and owe less than \$1,500.

⁵⁷ Excerpted from *New Help for US Citizens Overseas*, TheTaxBook News, June 28, 2012.

receive distributions from foreign trusts must also use this form.⁵⁸ Gifts and bequests are not taxable, but distributions from trusts are generally taxed as income. Taxpayers who receive a large inheritance (\$100,000+) will need to file this form with the return. **NOTE:** An extension to file income taxes does not apply to filing this form.

Other Forms

- **FinCEN Form 104 Currency Transaction Report**⁵⁹ – Any currency transaction or series of transactions over \$10,000 must be reported by a US financial institution that receives the foreign funds.
- **FinCEN Form 105** – Any person who physically brings, sends or receives \$10,000 or more into the US must complete and file this form with the Commissioner of Customs or the Customs Officer when entering the US.

D. Is all this reporting working?

It is widely acknowledged that “offshore tax evasion is a significant contributor to the tax gap.”⁶⁰ A US Senate report estimates that more than \$100 billion of tax revenues are lost each year but US Deputy Attorney General James Cole has testified that as many as 43,000 taxpayers have disclosed their previously hidden accounts since 2009, allowing the IRS to collect more than \$6 billion in back taxes and penalties.⁶¹ While that is but a drop in the bucket, it provides an indication that the IRS has the willingness and ability to pursue scofflaws, prodding them to step forward voluntarily. More will likely do so following Swiss banking giant’s Credit Suisse recent plea agreement, settling for a “mere” \$2.6 billion penalty in exchange for disclosure of client names.

As FATCA becomes the global standard in the perennial combat against offshore tax evasion, increasing numbers of foreign governments are signing on through intergovernmental agreements (IGAs) developed by the US Treasury facilitating the exchange of tax information between countries. Currently 48 countries have IGAs with the US.⁶²

⁵⁸ Rev Rul 2013-14 states that a Mexican Land Trust (“fideicomiso”) – necessitated by the fact that non-Mexican citizens may not individually hold title to property in Mexico – is not a trust for income tax purposes as long as the trust owns only the subject property and the Mexican bank is not engaged in any activity other than merely holding title. **NOTE:** An MLT exempt from **Form 3520** reporting is also exempt from **Form 8938** reporting.

⁵⁹ BSA e-filing of the FinCEN has been available since September 19, 2012 in lieu of paper filing of **Form 8300 Report of Cash Payments Over \$10,000 Received in a Trade or Business**, although electronic filing is not (yet) mandatory.

⁶⁰ Stack, *Myth vs. FATC: The Truth About Treasury’s Effort to Combat Offshore Tax Evasion*, White & Case Tax Flash, September 20, 2013.

⁶¹ Schoenberg and Voreacos, *Credit Suisse Hearing Likely to Drive New Taxpayer Confessions*, AccountingToday, February 27, 2014.

⁶² 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 Requirements⁶³

	Form 8938	FinCEN 114
Who Must File?	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
Does the United States include US territories?	No	Yes, resident aliens of US territories and US territory entities are subject to foreign account reporting
Reporting Threshold (Total Value of Assets)	\$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
When do you have an interest in an account or asset?	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.
What is Reported?	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
How are maximum account or asset values determined and reported?	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.
When Due?	By due date, including extension, if any, for income tax return	Received by June 30 (no extensions of time granted)
Where to File?	File with income tax return pursuant to instructions for filing the return	Must be electronically filed
Penalties	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

⁶³ Available at <http://www.irs.gov/Businesses/Comparison-of-Form-8938-and-FBAR-Requirements> [last accessed May 28, 2014].

APPENDIX B
Types of Foreign Assets and whether they are Reportable⁶⁴

	Form 8938	FinCEN 114
Financial (deposit and custodial) accounts held at foreign financial institutions	Yes	Yes
Financial account held at a foreign branch of a US financial institution	No	Yes
Financial account held at a US branch of a foreign financial institution	No	No
Foreign financial account for which you have signature authority	No, unless you otherwise have an interest in the account as described above	Yes, subject to exceptions
Foreign stock or securities held in a financial account at a foreign financial institution	The account itself is subject to reporting, but the contents of the account do not have to be separately reported	The account itself is subject to reporting, but the contents of the account do not have to be separately reported
Foreign stock or securities not held in a financial account	Yes	No
Foreign partnership interests	Yes	No
Indirect interests in foreign financial assets through an entity	No	Yes, if sufficient ownership or beneficial interest (i.e., a greater than 50 percent interest) in the entity. See instructions for further detail.
Foreign mutual funds	Yes	Yes
Domestic mutual fund investing in foreign stocks and securities	No	No
Foreign accounts and foreign non-account investment assets held by foreign or domestic grantor trust for which you are the grantor	Yes, as to both foreign accounts and foreign non-account investment assets	Yes, as to foreign accounts
Foreign-issued life insurance or annuity contract with a cash-value	Yes	Yes
Foreign hedge funds and foreign private equity funds	Yes	No
Foreign real estate held directly	No	No
Foreign real estate held through a foreign entity	No, but the foreign entity itself is a specified foreign financial asset and its maximum value includes the value of the real estate	No
Foreign currency held directly	No	No
Precious Metals held directly	No	No
Personal property, held directly, such as art, antiques, jewelry, cars and other collectibles	No	No
'Social Security'- type program benefits provided by a foreign government	No	No

⁶⁴ Available at <http://www.irs.gov/Businesses/Comparison-of-Form-8938-and-FBAR-Requirements> [last accessed May 28, 2014].

APPENDIX C Glossary of Terms

Abode	Taxpayer's domestic home where he maintains his family, social and political ties
Bona Fide Residence Test	Taxpayer must be a resident of a foreign country for an entire year to be eligible for the Foreign Earned Income or Foreign Housing exclusions
Domicile	Permanent home to which the taxpayer intends to eventually return
Dual Citizen	An individual regarded as a national by more than one country, with the option to be treated as a citizen by one or both based on treaty provisions
Foreign Earned Income	Amounts paid for personal services performed
Foreign Earned Income Exclsn.	Max exclusion \$85,700/year if US citizen or resident alien lives and works abroad
Foreign Country	Any territory under the sovereignty of a government other than that of the United States
Foreign Housing Deduction	Self-employed individuals may deduct the value of housing if US citizen or resident alien lives and works abroad
Foreign Housing Exclusion	The value of employer-provided housing may be excluded from taxable income if US citizen or resident alien lives and works abroad
Foreign Tax Credit	Available to US citizen or resident alien who has paid foreign income taxes
Housing Expenses	Include rent, repairs, utilities, real and personal property insurance, occupancy taxes, furniture rental, and residential parking
Illegal Alien	An undocumented alien who entered the US without authorization or an alien who once entered legally and then overstayed his welcome
ITIN	Individual Taxpayer Identification Number issued by IRS in lieu of Social Security Number (SSN) or Employer Identification Number (EIN)
Military Personnel	Includes all uniformed members serving in the Army, Navy, Air Force, and Coast Guard
Signature Authority	Individual can control the disposition of account assets
Specified Foreign Fncl. Assets	Include depository or custodial accounts at foreign financial institutions, stocks or securities issued by foreign persons, and any interest in a foreign entity
Tax Home	A taxpayer's place of business or employment
US National	A resident of American Samoa or Northern Mariana Islands who has sworn allegiance to the US
US Person	A US citizen, resident or entity created under US law