

## FILE FORM 8938 WITH FORM 1040 TO REPORT CERTAIN FOREIGN FINANCIAL ASSETS

by Cameron L. Hess

Preparers are going to have to be a lot more inquisitive with their client's 2011-year personal income tax returns and will have to ask about their foreign financial investments.

Starting with the 2011-year Form 1040, clients may now also have to file Form 8938 with their return in order to report certain financial investments. Form 8938 must be filed if their client's total value certain foreign financial investments exceeds \$50,000. (\$100,000 for married individuals; both numbers double for those living overseas.) The foreign investments considered are bank accounts, stock interests, other foreign equity interests and debt investments. These filing requirements apply to "US persons", typically a US citizen or permanent resident of the United States.

In valuing foreign assets (and in reporting values) the IRS provides several rules. First, as to any investment, the measure of "value" includes the entire value of jointly held investments. Second, for interests held in trust, these must be included by the grantor of a grantor trust, or by the beneficiary in other situations. Third, in computing value, limited guidance is provided. Generally, if not known, a reasonable estimate may be used. Special rules apply to non-grantor trust beneficiaries.

While seemingly simple, the Form 8938 aims at complete reporting through four parts. Part I duplicates FBAR reporting somewhat by asking for financial bank account information. Because Form 8938 will not waive the requirement to file a Report of Foreign Bank and Financial Accounts ("FBAR"), due separately to the Treasury by June 30, some taxpayers may want to extend their returns to assure that both returns, if required, are consistent with each other. (A U.S. person must file the FBAR with the Treasury if the he or she has a financial interest in or signature authority over at least one financial account outside the United States if the total value of such exceeds \$10,000 during the year.)

The next part, Part II, requires that there be listed other foreign financial investments, i.e. non-bank account assets. However, if Forms 3520, 3520-A, 5471 8621 or 8865 are required, then in lieu of Part II, there is completed Part IV, which is a "check the box" index forms, and how many of each form were filed.

Part III provides financial income information, disclosing the type of income, the amount, and where the income is actually reported on the tax return.

While not intended to apply to directly held real estate, because of foreign investor laws may require that real estate to be held by an investment entity, clients who hold foreign investment real estate may be required to file Form 8938 in those circumstances.

**Example.** John Moneyworks with his brother Sam Moneyworks (both unmarried) own a vacation condominium in Baja California through a Mexico Corporation. The total value of their joint tenancy certificate share is worth \$75,000. While real estate directly owned is not reportable, because the Moneyworks brothers own investment real estate through a stock equity interest, a Form 8938 probably would be required because the total value of the joint interest exceeds \$50,000.

In summary, this form is obviously intended to assist the IRS in insuring that taxpayers fully report their foreign income, including disclosing to the IRS foreign investment asset holdings. These reporting rules are somewhat complex and our office can assist in advising on Form 8938 reporting.