

**Federal Filing and Reporting Requirements
with Respect to Certain Investments and Accounts**

April 10, 2014

Puerto Rico residents having an interest in, including signing authority for, certain financial assets may be required to file Internal Revenue Service (“IRS”) Form 8938, Statement of Specified Foreign Financial Assets, or FinCEN Form 114, Report of Foreign Bank and Financial Accounts (“FBAR”), or both.

IRS Form 8938

Form 8938 must be filed with the federal income tax return of a “specified individual” to report “specified foreign financial assets”.

Generally, a US citizen or resident alien residing in Puerto Rico will only be considered a “specified individual” if, for the applicable taxable year, the individual (1) is required to file a federal income tax return, **and** (2) meets the following reporting thresholds:

<u>Aggregate value of specified foreign financial assets (“SFFAs”)</u>	<u>Single/Married Filing Separate Return</u>	<u>Married Filing Joint Return</u>
At the close of the taxable year, or	\$50,000	\$100,000
At any time during the taxable year	\$75,000	\$150,000

In general, a SFFA is (1) a “financial account maintained by a foreign financial institution,” or (b) other “foreign financial assets.”

A “financial account” for these purposes means (1) a depository account, (2) a custodial account, or (3) equity or debt interest in a financial institution.

“Other foreign financial assets,” in turn, include assets “held for investment” and classified within three broad categories, to wit: (1) “any stock or security issued by a non-U.S. person”; (2) “any financial instrument or contract that has an issuer or counterparty” that is not a U.S. person; and (3) “any interest in a foreign entity.” The IRS has indicated that the term “other foreign financial assets” includes an “interest in” a foreign retirement plan or deferred compensation plan.

Certain exceptions to the requirement of filing Form 8938 should be noted:

- (1) As previously mentioned, an individual (including one who is a bona fide resident of Puerto Rico) is not required to file Form 8938 for a taxable year if for such taxable year, the individual is not required to file a U.S. federal income tax return.
- (2) An individual is not treated as having an interest in an SFFA if any income, gain, loss, deduction, credit, gross proceeds, or distributions attributable to the holding or disposition thereof is not required to be reported in a U.S. federal income tax return. This would appear to mean that a Puerto Rico resident would not be required to report his/her interest in an SFFA if any income to be derived thereunder would constitute income from sources within Puerto Rico and therefore not reportable in a federal income tax return on account of being excludable from gross income under §933 of the U. S. Internal Revenue Code.
- (3) An individual that is a bona fide resident of Puerto Rico is not required to report:
 - (a) financial accounts maintained in financial institutions organized in Puerto Rico, or the Puerto Rico branch of certain foreign financial institutions;
 - (b) stocks or securities issued by an entity organized under the laws of Puerto Rico;
 - (c) an “interest in an entity” organized in Puerto Rico, or
 - (d) a “financial instrument or contract held for investment” if the issuer or counterparty is organized in or a resident of Puerto Rico.

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In accordance with IRS Circular 230 requirements, you are advised that any discussion of U.S. federal tax issues in this document cannot be used to avoid penalties imposed under the U.S. Internal Revenue Code or to promote, market, or recommend to another party any transaction or matter addressed herein.

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Failure to comply with the Form 8938 requirements entails a \$10,000 penalty unless the failure is due to reasonable cause and not due to willful neglect. The penalty can increase if the IRS notifies a failure and the failure continues for more than 90 days after the mailing of the notice by the IRS. Special statute of limitations rules also apply.

FinCEN Form 114

FinCEN Form 114 is used to report a financial interest in or signature authority held by a “U.S. person” over a “financial account” in a “foreign country.” It must be filed electronically with the Department of the Treasury through FinCEN’s BSA E-Filing System, on or before June 30th of the year immediately following the calendar year being reported. The June 30 filing date may not be extended. A “U.S. person” means (a) a citizen of the United States, (b) a resident of the United States (including Puerto Rico), (c) an entity organized under the laws of the United States or a State.

The term “foreign country” includes all geographical areas located outside the United States. For FBAR purposes, “United States” includes the fifty States, the District of Columbia, all United States territories and possessions (e.g., Puerto Rico, American Samoa, Northern Mariana Islands, Guam, and U.S. Virgin Islands), and the Indian lands as defined in the Indian Gaming Regulatory Act. Thus, no reporting is required with respect to interests in or signature authority over financial accounts in Puerto Rico. However, individuals residing in Puerto Rico and entities organized under the laws of Puerto Rico must file the report if they have a financial interest in or signature authority over financial accounts in a foreign country **and** the aggregate value of the foreign financial accounts exceeds \$10,000 at any time during the calendar year.

A “financial account” includes, among other instruments, a securities, brokerage, savings, demand, checking, deposit, time deposit, or other account maintained with a financial institution (or other person performing the services of a financial institution), an insurance policy with a cash value (such as a whole life insurance policy), an annuity policy with a cash value, and shares in a mutual fund or similar pooled fund (i.e., a fund that is available to the general public with a regular net asset value determination and regular redemptions).

A person that is the owner of record or holder of legal title of a foreign financial account will be treated as having a financial interest therein, whether or not the account is for the benefit of the titleholder or another person. U.S. persons will also be deemed to have a financial interest in foreign financial accounts maintained by their agents or representatives, as well as by entities controlled by said persons and certain trusts.

Signature authority, in turn, means the authority of an individual (alone or in conjunction with another individual) to control the disposition of the assets in a foreign financial account by direct communication with the financial institution maintaining the account. There are exceptions for, among others, officers and employees of certain banks, of SEC-registered investment companies and of publicly-traded entities.

Penalties for failure to comply are up to \$10,000 per violation; if due to willful disregard, the penalty may be up to the greater of \$100,000 or 50 percent of account balances, and criminal penalties may also apply.

Offshore Voluntary Disclosure

The Internal Revenue Service has an Offshore Voluntary Disclosure program which may be considered by persons that have not been complying with these and other reporting requirements. This program offers persons with offshore financial accounts or other foreign assets an opportunity to resolve their tax and information reporting obligations. One of the principal benefits of this program is that it significantly reduces the risk of criminal penalties.



If you have any questions or comments, or would like additional information about this matter, please call any of our tax attorneys:

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