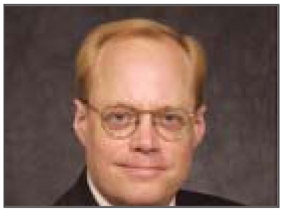

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THE TAX LAWYER

IRS Has Gone Wild Over FATCA, But Watchdog Warns Of Compliance Glitches

FATCA, the Foreign Account Tax Compliance Act, is up and running. If you have foreign accounts or foreign assets, it is an important law that has changed banking and privacy in radical ways. And it has done so worldwide, not just for Americans, but for anyone having even remote American connections. The IRS says it is now swapping taxpayer data reciprocally with other countries. The IRS says the data exchanges are in place and going well. But there are some warning signs.

FATCA was passed in 2010 with staggered effective dates that in most respects did not apply until 2014. And yet, many individual tax returns had to start complying with FATCA in 2011. A key part of the law is compliance by banks and other financial institutions. Non-U.S. banks around the world must reveal American account details or risk big penalties. One big penalty on offshore banks who do not hand over Americans is withholding at 30% on most transactions.

(AP Photo/Kin Cheung)

FATCA requires foreign banks to reveal Americans with accounts over $50,000. Non-compliant institutions are frozen out of U.S. markets, so there is little choice but to comply. But a new report suggests that the IRS may not be as far along in ramping up FATCA as it would like. The Treasury Inspector General did an audit to determine the IRS's progress in implementing FATCA.

The report notes that the IRS has taken steps to provide information to affected stakeholders that explains the FATCA requirements and expectations. However, the report dentified improvements that are required to ensure compliance and to measure performance for foreign financial institutions. If plans are not properly documented, the report says, implementation and performance of compliance activities could experience unnecessary delays.

The report also identified limitations with the processing of paper Forms 8938. Beginning with 2011, taxpayers with specified foreign financial assets that meet a certain dollar threshold had to file Form 8938 with their 1040 or Form 1040-NR. That remains true for each year since 2011. FATCA also requires foreign financial institutions to report to the IRS information about financial accounts held by U.S. taxpayers or held by foreign entities in which U.S. taxpayers hold a substantial ownership interest.

The report says matching up the data will be tough, since:

- Transcribed data are not validated to ensure accuracy.
- Data on Form 8938 continuation statements (used to report additional foreign accounts or other foreign assets) are not transcribed.
- Losses reported by taxpayers cannot be input as negative amounts.

If these issues are not properly addressed, the report warns, any analysis of the potentially inaccurate or incomplete paper Form 8938 data will be compromised. The goal of FATCA is improved compliance in the reporting of offshore income and assets. Thus, the Treasury Inspector General recommended that the IRS:

1. Update the compliance activities in the FATCA Compliance Roadmap for identifying noncompliance by foreign financial institutions;
2. Initiate a periodic quality review process for the processing of paper Forms 8938 to ensure the accuracy of the data being transcribed; and

3. Ensure that the transcription issues identified in this report are addressed in the newest version of the Form 8938 transcription program.

The IRS agreed with the first two recommendations. However, the IRS disagreed with some programming changes related to the third recommendation. Still, the Inspector General's report notes that the accuracy of the data obtained from Forms 8938 is a critical component for the success of the IRS's compliance activities with implementing FATCA. As such, the Treasury Inspector General believes that the IRS should make these programming changes a priority.

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