Foreign Financial Assets and U.S. Tax Reporting

What New U.S. Tax Residents and Americans Abroad Should Know

Moving to the United States changes more than where you live.

It can also change how your bank accounts, investments, retirement plans, businesses, and other financial assets are taxed and reported.

The United States generally taxes its citizens and tax residents on their worldwide income. Once you become subject to the U.S. tax system, income earned outside the United States may have to be reported even if:

- The income remains in a foreign account.
- The money is never transferred to the United States.
- The investment is tax-deferred or tax-exempt in another country.
- The account existed for many years before you moved.
- No U.S. tax form was issued.

Foreign assets can also create reporting obligations that are separate from the calculation of income tax.

Two of the most common are:

- **The Report of Foreign Bank and Financial Accounts**, commonly called the FBAR or FinCEN Form 114.
- **Form 8938, Statement of Specified Foreign Financial Assets**, which is filed with a federal income tax return.

These two reporting systems overlap, but they are not interchangeable. A person may be required to file one, both, or neither, depending on the type and value of the assets involved.

In most situations, reporting a foreign account does not itself create additional tax. The tax generally comes from the income generated by the account, such as interest, dividends, capital gains, pension distributions, or business income.

The reporting forms disclose the existence and value of the foreign assets.

The distinction matters.

A foreign bank account containing previously taxed savings may not generate a significant U.S. income tax liability. Nevertheless, the account may still have to be reported. On the other hand, an investment may generate taxable income even when its value is below a particular information-reporting threshold.

The penalties associated with international information returns can be substantial. This is why foreign financial assets should be reviewed before a person moves to the United States—not after the first U.S. tax return is already due.

This guide explains the major categories of foreign financial assets, how the principal reporting systems work, and which issues deserve attention before U.S. tax residency begins.

1. When Do the U.S. Rules Begin to Apply?

For individuals who are not U.S. citizens, the first step is determining when U.S. tax residency begins.

A person is generally treated as a U.S. tax resident after satisfying one of the following tests:

The Green Card Test

A person is generally a U.S. tax resident if they are a lawful permanent resident of the United States at any time during the calendar year.

However, the residency starting date does not always correspond to the date printed on the green card. For a person who receives lawful permanent resident status while outside the United States, residency generally begins on the first day the person is physically present in the United States after receiving that status.

The Substantial Presence Test

A person may also become a U.S. tax resident based on the number of days physically present in the United States.

The test generally requires:

- At least 31 days of U.S. presence during the current year; and
- A weighted total of at least 183 days over the current year and the two preceding years.

The formula counts:

- All qualifying days in the current year;
- One-third of qualifying days in the previous year; and
- One-sixth of qualifying days in the second preceding year.

Certain days may be excluded, including some days associated with exempt visa categories, medical conditions, or regular commuting from Canada or Mexico.

A person who satisfies the mathematical test may also qualify for a closer-connection exception or claim treaty benefits in certain circumstances. These exceptions are highly fact-specific and often require timely disclosure forms.

Elections That Can Change the Result

A person who would otherwise be a nonresident for part or all of a year may sometimes elect to be treated as a U.S. resident.

Examples include:

- The First-Year Choice.
- An election by a nonresident spouse to be treated as a U.S. resident.
- Certain joint-return elections involving a U.S. citizen or resident spouse.

These elections can simplify filing, but they can also bring additional foreign income and foreign assets into the U.S. tax system.

An election should not be made simply because it allows a joint return. The worldwide-income and international-reporting consequences must be evaluated first.

The IRS treats dual-status taxpayers differently during the resident and nonresident portions of the year. Worldwide income is generally subject to U.S. taxation during the period of U.S. residence, while different sourcing rules apply during the nonresident period.

Why the Starting Date Matters

The tax-residency starting date may affect:

- Which income is included on the U.S. return.
- Whether a foreign asset sale occurs before or after U.S. residency begins.
- Whether foreign dividends, pension distributions, or business income are subject to U.S. taxation.
- Whether foreign information returns are required.
- How a dual-status return is prepared.

The rules for the FBAR and Form 8938 do not always follow exactly the same mechanics as the income tax return.

A person who becomes a U.S. person during the year should not automatically assume that every balance or transaction from the entire year is treated the same way. The reporting period, residency starting date, ownership period, and any elections made must be reviewed together.

Practical Example

Maria is a Canadian citizen who enters the United States on July 1 and becomes a lawful permanent resident.

She owns:

- A Canadian checking account.
- A Canadian investment account.
- An RRSP.
- Shares in a Canadian corporation.

Her first U.S. filing may involve far more than reporting income earned after July 1.

The analysis may also include:

1. FBAR reporting.
2. Form 8938.
3. Retirement-plan treatment.
4. Foreign tax credits.
5. Potential foreign-corporation reporting.
6. Classification of Canadian investment funds.
7. A dual-status return or a possible full-year residency election.

The correct answer cannot be determined merely by looking at her immigration status on December 31.

2. Worldwide Taxation Does Not Mean the United States Owns Your Foreign Savings

One of the most common concerns is that moving to the United States will cause the balance of an existing foreign account to become taxable.

That is generally not how the system works.

The transfer of your own money from one account to another usually does not create taxable income merely because the money is moved into the United States.

For example, transferring $100,000 of previously accumulated savings from a French bank account to a U.S. bank account generally does not create $100,000 of taxable income.

However, several separate questions still have to be addressed:

1. Did the foreign account generate interest?
2. Did investments inside the account generate dividends or capital gains?
3. Was foreign tax withheld?
4. Did the account exceed an FBAR or Form 8938 reporting threshold?
5. Was the money accumulated through an entity, trust, pension plan, or insurance arrangement?
6. Can the original source of the funds be documented?

The balance itself may not be income, but income generated by the assets may be taxable.

The United States generally taxes its citizens and resident aliens on worldwide income, regardless of where the income is earned or where the money is held.

Good records are particularly important when a person transfers substantial funds after moving. Bank statements, purchase records, inheritance documents, property-sale records, and prior tax returns may help demonstrate that a transfer represents existing capital rather than previously unreported income.

3. What Is a Foreign Financial Account?

For FBAR purposes, the location of the financial institution maintaining the account is generally more important than the currency in which the account is denominated.

A foreign financial account may include:

- Checking accounts.
- Savings accounts.
- Time deposits and certificates of deposit.
- Securities and brokerage accounts.
- Certain commodity futures or options accounts.
- Certain foreign retirement accounts.
- Certain foreign pension accounts.
- Cash-value life insurance policies.
- Annuity contracts with cash value.
- Certain pooled investment accounts.

An account is not foreign merely because it holds foreign currency or foreign investments.

For example:

- A euro-denominated account maintained by a bank in New York is generally not a foreign account solely because it holds euros.
- A U.S.-dollar account maintained by a bank in France is generally a foreign account even though the balance is denominated in U.S. dollars.
- An account maintained at a foreign branch of a U.S. bank may be reportable for FBAR purposes.
- An account maintained at a U.S. branch of a foreign bank is generally not treated as a foreign account for FBAR purposes.

> FinCEN requires a U.S. person to file an FBAR when the person has a financial interest in, or signature or other authority over, reportable foreign financial accounts and the aggregate value exceeds $10,000 at any time during the calendar year.

4. Form 8938 Covers More Than Foreign Accounts

Form 8938 is broader in certain respects than the FBAR.

It may cover foreign financial accounts as well as specified foreign financial assets that are not held inside an account.

Depending on the circumstances, specified foreign financial assets may include:

- Stock issued by a foreign corporation.
- An interest in a foreign partnership.
- An interest in certain foreign entities.
- Foreign notes, bonds, and debt instruments.
- Financial contracts with non-U.S. counterparties.
- Certain foreign retirement plans.
- Certain foreign pension rights.
- Foreign-issued cash-value insurance or annuity contracts.

A taxpayer must file Form 8938 only when the total value of the specified foreign financial assets exceeds the applicable threshold. The thresholds depend on filing status and whether the taxpayer is considered to live in the United States or abroad.

Assets Generally Outside These Reporting Categories

The following assets are generally not directly reportable merely because they are located outside the United States:

- Real estate owned directly.
- Physical gold or other precious metals owned directly.
- Artwork and collectibles owned directly.
- Foreign currency held personally as physical cash.
- Personal property such as vehicles, furniture, or jewelry.

However, the answer changes if the asset is held through a foreign company, partnership, trust, investment account, or other entity.

For example:

- A rental apartment owned directly is generally not itself listed on the FBAR or Form 8938.
- A foreign bank account collecting the rent may be reportable.
- Shares of a foreign company that owns the apartment may be reportable.
- The company may create a separate Form 5471, Form 8858, or Form 8865 filing obligation.
- Rental income and a later sale may still have to be reported on the U.S. income tax return.

The ownership structure matters as much as the underlying asset.

5. Foreign Bank Accounts

Foreign checking and savings accounts are usually the easiest category to identify, but the aggregation rule causes frequent errors.

The FBAR Threshold

An FBAR is generally required when the aggregate value of all reportable foreign financial accounts exceeds $10,000 at any time during the calendar year.

The threshold is not applied separately to each account.

Example

You own three foreign accounts with the following maximum values:

- UK current account: $4,200.
- Canadian savings account: $3,800.
- Australian term deposit: $2,500.

The combined maximum values total $10,500. Even though no single account exceeded $10,000, the aggregate amount did. An FBAR may therefore be required, and all reportable accounts are generally included.

The FBAR threshold is an annual reporting threshold, not an exemption for the first $10,000.

Maximum Account Value

The account owner generally determines the highest value of each account during the year in the account's local currency and converts that amount into U.S. dollars.

For FBAR purposes, FinCEN's instructions generally require the Treasury year-end exchange rate for the relevant calendar year. The taxpayer does not simply select whichever daily exchange rate produces the preferred result.

Exact daily statements are not always available. FinCEN permits reasonable periodic account statements to be used when they reasonably reflect the highest value, but the taxpayer should retain support for the calculation.

Income Reporting

Interest earned by a foreign bank account is generally reportable on the U.S. income tax return even when:

- The interest remains in the account.
- The bank does not issue a Form 1099.
- The amount is exempt from tax in the foreign country.
- The account balance is below the FBAR threshold.

Foreign tax paid on the interest may qualify for a foreign tax credit, subject to the applicable limitations.

COMMON MISTAKE

A frequent mistake is excluding dormant accounts because they produced no income. Income and account reporting are separate matters. A dormant account may still be reportable if the aggregate FBAR or Form 8938 threshold is met.

PLANNING CONSIDERATION

Before moving to the United States, review old accounts and determine which ones still serve a practical purpose. Closing unnecessary accounts may reduce future administrative work. However, moving money between accounts or consolidating accounts does not automatically eliminate an FBAR obligation because the $10,000 threshold applies to the aggregate value of all reportable accounts. The objective should be simplifying the structure—not artificially manipulating balances.

6. Foreign Brokerage and Investment Accounts

A foreign brokerage account may create several layers of U.S. tax work:

8. Reporting the account.
9. Reporting income generated inside the account.
10. Calculating gains and losses in U.S. dollars.
11. Determining the classification of each investment.
12. Evaluating foreign tax credits.
13. Identifying investments subject to special U.S. rules.

The account itself may be reportable on both the FBAR and Form 8938 once the applicable thresholds are met.

Generally, when investments are held inside a reportable financial account, Form 8938 reports the account rather than separately listing every security held inside it. Directly held foreign securities outside an account may require separate reporting.

Foreign Brokers May Not Provide U.S.-Style Tax Information

A foreign broker may provide a statement that is entirely correct under local law but insufficient for a U.S. return.

Common missing information includes:

- Original purchase date.
- Original purchase price.
- Reinvested distributions.
- Corporate actions.
- Return-of-capital adjustments.
- U.S.-dollar cost basis.
- Identification of the specific units sold.

- Foreign tax allocated to particular income categories.

The absence of a Form 1099 does not remove the U.S. reporting obligation.

Currency Conversion

Capital gains are generally measured in U.S. dollars. This can produce a result that appears inconsistent with the gain measured in the local currency.

Example

An investment is purchased for €80,000 when the euro is worth $1.20. The U.S.-dollar basis is approximately $96,000. The investment is later sold for €90,000 when the euro is worth $1.00. The local-currency gain is €10,000, but the U.S.-dollar sale proceeds are approximately $90,000. For U.S. tax purposes, the transaction may produce a $6,000 capital loss even though the investor earned a gain in euros.

This is one reason historical exchange-rate and cost-basis records are important.

PLANNING CONSIDERATION

Before becoming a U.S. tax resident, obtain complete transaction histories, purchase confirmations, records of reinvested dividends, corporate-action statements, documentation of foreign taxes paid, and statements identifying the domicile and legal classification of each fund. Reconstructing ten or twenty years of cost basis after a sale is usually more expensive than gathering the information while the records are still accessible.

7. Foreign Mutual Funds and ETFs

Foreign mutual funds and exchange-traded funds are among the most significant issues for people moving to the United States.

Many non-U.S. pooled investment funds are classified as Passive Foreign Investment Companies, commonly called PFICs.

The name can be misleading. A PFIC does not have to be an aggressive offshore investment or a tax-avoidance vehicle. A normal retail mutual fund purchased through a Canadian, European, British, Australian, or Asian bank may fall within the definition.

Common examples that may require PFIC analysis include:

- Foreign mutual funds.
- Foreign ETFs.
- UCITS funds.
- OEICs.
- Unit trusts.
- Investment funds held inside certain insurance products.
- Certain money-market funds.
- Certain foreign investment companies.

A foreign corporation generally meets the PFIC definition when either:

- At least 75% of its gross income is passive income; or
- At least 50% of its assets produce, or are held to produce, passive income.

The classification is based on U.S. tax law—not on the name used by the financial institution or the regulatory classification in the country where the fund is sold.

Why the Default PFIC Rules Can Be Unfavorable

Under the default Section 1291 regime, certain distributions and gains may be allocated over the investor's entire holding period.

Amounts allocated to prior PFIC years may be subject to:

- Tax calculated using the highest applicable ordinary income tax rate for those years.
- An interest charge.
- Loss of normal long-term capital-gain treatment on the gain.

The calculation can be disproportionately complex relative to the value of the investment.

Qualified Electing Fund Election

A Qualified Electing Fund election may provide more favorable treatment, but the fund generally must supply a PFIC Annual Information Statement containing information required under U.S. tax rules. Many foreign retail funds do not provide this information. Without the required statement, a valid QEF election may not be available.

Mark-to-Market Election

A mark-to-market election may be available for qualifying marketable PFIC stock. Under this method, annual appreciation is generally recognized as ordinary income even when the investment has not been sold. Loss deductions are subject to limitations tied to prior mark-to-market inclusions. The election may simplify future treatment, but it does not necessarily eliminate the consequences of PFIC ownership before the election becomes effective.

Form 8621

Form 8621 may be required for each PFIC in which a U.S. person is a direct or indirect shareholder. However, the statement that every small PFIC holding always requires a separate annual form is too broad. The regulations and instructions provide limited exceptions from certain annual reporting requirements, including an exception based on aggregate PFIC value in some circumstances. Those exceptions may not apply when the taxpayer receives an excess distribution, recognizes gain on a disposition, makes or maintains certain elections, or is otherwise required to complete substantive portions of Form 8621. The exception must be evaluated carefully rather than assumed.

Practical Example

A person living in Belgium owns an Irish-domiciled UCITS ETF tracking a broad U.S. stock index. Economically, the fund may resemble a U.S.-domiciled index ETF. For U.S. tax purposes, the domicile of the fund matters. The Irish fund may be treated as a PFIC even though it invests primarily in U.S. companies. The investment strategy does not control the classification.

PLANNING CONSIDERATION

Foreign funds should be reviewed before U.S. residency begins. Possible strategies may include selling the investment before the U.S. residency starting date, retaining the investment and accepting the reporting consequences, determining whether QEF information is available, evaluating whether a mark-to-market election may be appropriate, replacing the investment with a U.S.-domiciled investment after the move, or coordinating the transaction with foreign capital-gain taxes and available foreign tax credits.

Selling before moving is not automatically the correct answer. The analysis should consider local capital-gain tax, exit-tax rules, transaction costs, market exposure, residency timing, foreign tax credit limitations, whether the investment is held through a pension or insurance arrangement, and whether the person has already become a U.S. person. The important point is to complete the analysis while choices remain available.

A Note About FATCA and International Data Sharing

Foreign financial institutions in participating jurisdictions may report information concerning U.S. account holders under FATCA agreements. The United States also receives and exchanges financial information through tax treaties, intergovernmental agreements, and other information-sharing mechanisms.

However, the United States has not adopted the OECD Common Reporting Standard in the same manner as many other countries. It is therefore inaccurate to say that the IRS automatically receives all foreign account data through both FATCA and CRS.

The practical conclusion remains the same: taxpayers should not assume that a foreign account is invisible merely because it is located outside the United States. Compliance should be based on the applicable law—not on whether the taxpayer believes the government will discover the account.

Key Takeaway

The most expensive international tax problems often begin with ordinary financial products:

- A savings account left open after a move.
- A local mutual fund purchased years earlier.
- A pension that is tax-deferred in one country but treated differently in the United States.
- An investment account with no usable cost-basis records.
- A jointly owned family account.
- A foreign company used to hold personal investments.

The issue is rarely that the client intentionally did something wrong. More often, no one explained that becoming a U.S. tax resident changes the rules.

That is why international tax planning should start before the move.

A tax return can report what already happened. Planning gives you an opportunity to decide what should happen next.

DISCLAIMER

This guide provides general educational information and does not constitute individualized tax, legal, investment, or immigration advice. International reporting depends on the taxpayer's residency, filing status, asset ownership, account structure, elections, treaty position, and other facts. Professional advice should be obtained before acting on any strategy discussed in this guide.

CONTINUING THE GUIDE

The next sections should cover foreign pensions, life insurance, cryptocurrency, joint and signature-authority accounts, foreign business accounts, the full FBAR-versus-Form-8938 comparison, common mistakes, and the pre-move checklist.

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