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FinCEN Issues Final FBAR Regulations for Certain U.S. Persons Holding Foreign Financial Accounts

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The Financial Crimes Enforcement Network (FinCEN) of the U.S. Treasury Department issued final regulations (RIN 1506-AB08) on February 24 regarding the requirements for certain U.S. persons to file Form TD F 90-22.1, Report of Foreign Bank and Financial Accounts (FBAR) (the Final Regulations). These final rules reflect only slight modifications to the proposed rules issued February 23, 2010 (the Proposed Regulations).[1]

I. Background

Generally, any U.S. person or entity that at any time during a calendar year had a financial interest in, or signature or other authority over, financial accounts located in a foreign country with an aggregate value in excess of $10,000 is required to file an FBAR. The filing deadline for FBARs for each year is June 30 of the following year.

On February 26, 2010, the Internal Revenue Service (IRS) issued Notice 2010-23, which provided a delayed filing date for certain FBARs until June 30, 2011, for some persons with only signature authority over foreign financial accounts but no financial interest in such accounts and for persons owning certain commingled funds. The FBARs affected by the delayed filing date are for accounts for 2009 and prior calendar years.

Following the issuance of the Proposed Regulations, FinCEN received 42 filed comment letters which generally sought broader exemptions then set forth in the proposed rules. Very few of these comments resulted in changes to the Proposed Regulations.

II. Highlights of Changes to Proposed Regulations

A. **Reportable Accounts.** The preamble to the Final Regulations (the Preamble) clarifies the meaning of a foreign account for filing purposes. The Preamble notes that "[t]he mere fact that the account may contain holdings or assets of foreign entities does not render the account 'foreign' for purposes of the FBAR." What is important in this instance is where the account is maintained. If the account is maintained in the United States, it will not be considered a foreign account even if it holds

1. See Notice of Proposed Rulemaking (RIN 1506-AB08), 75 Fed. Reg. 8844 (Feb. 26, 2010).

foreign assets. Further, an omnibus account held by a custody bank that holds assets both in the United States and outside the United States is not considered a foreign account unless the client has direct access to its foreign holdings maintained at the foreign institution.

B. **Signature Authority or Other Authority.** The Preamble rejected a number of commenters' requests to completely eliminate the requirements that persons file an FBAR if they have signature or other authority over a foreign account. FinCEN believes that FBARs "filed by individuals with only signature authority are valuable tools in investigations . . . because the signature authority requirement also acts as an independent check on FBAR reporting." Accordingly, the requirement to file FBARs by U.S. persons with signature authority will remain.

As noted above, the IRS guidance provided an extension until June 30, 2011 for reporting of any person with signature authority over, but no financial interest in, a foreign account for the 2010 and prior calendar years. The IRS guidance also provided that these persons were permitted to check "no" on Schedule B of their IRS Forms 1040 for 2009 and earlier for the question regarding whether they have signature authority over a foreign financial account. Such persons are now required to check "yes" on their 2010 Form 1040, Schedule B to this question.

The Final Regulations adjust the definition of persons who fall within the definition of signature authority. The revised test for determining whether an individual has signature or other authority over an account is whether the foreign financial institution will act upon *a direct communication* from that individual (either individually or together with others) regarding the disposition of assets in that account. Therefore, persons who merely participate in the decision to allocate assets or have the ability to instruct or supervise others with signature authority over a reportable account are not included within the definition of signature authority. The Preamble also clarifies that signature and other authority only applies to individuals.

Lastly, the Final Regulations also provide that employees with only signature authority over a foreign financial account but no financial interest are not required to personally maintain the FBAR records of their employer which gave rise to their obligation to file the FBAR for five years, as is required by persons with financial interests in such accounts.

C. **No Exemption for Pension and Welfare Benefit Plans.** FinCEN received a number of comments seeking an exemption from FBAR filings for pension and welfare benefit plans, generally because such plans are already subject to comprehensive regulation and the FBAR requirements would be burdensome and duplicative of existing filing requirements (e.g., Form 5500). The IRS rejected these requests for broader exemptions for such plans because it did not believe their tax-exempt status nor their exemption from other provisions was a sufficient reason to treat such plans differently given FBAR's broader purposes. FinCEN also rejected a request that employee benefit plans of publicly traded corporations be exempted based on the requirements that the assets and liabilities of its employee benefit plans are included on the corporation's SEC filings and retained the requirement that such plans should continue to report their foreign accounts.

D. **Electronic Filing of FBARs.** FinCEN noted that it is in the process of modernizing its IT system and has plans to include the ability to file FBARs electronically.

E. **Valuation.** Commenters requested additional guidance on determining the value of accounts. The Preamble provides that bona fide statements prepared in the ordinary course of business may be relied upon. This should provide persons with FBAR filing responsibilities with some comfort

that a reasonable approach will be taken in determining whether an account has exceeded $10,000 at any time during the calendar year.

F. **Applicability Date.** Although the Final Regulations are not retroactive, persons who delayed their filing under IRS Notice 2010-23 are permitted to rely on the provisions in the Final Regulations for reports due June 30, 2011 for calendar years prior to the 2010 calendar year.

G. **Certain Exemptions From the Proposed Regulations Are Retained and Clarified**

1. **Foreign hedge funds, venture capital funds, or private equity funds.** The Final Regulations currently do not require an FBAR filing with respect to interests in certain foreign hedge funds, venture capital funds, or private equity funds if such funds are not "mutual funds or similar pooled funds," and instead reserve a section within the Final Regulations to cover interests in such entities, if FinCEN later determines it appropriate to do so. Mutual funds and similar pooled funds for this purpose are those that issue shares available to the general public that have regular net asset value determination and regular redemptions. The Preamble stresses that an FBAR is required only where the shares of the entity are offered to the general public. Accordingly, interests in most hedge funds, venture capital funds, and private equity funds are not required to be reported on an FBAR because they are privately offered.

2. **Tax-exempt investors that own offshore "blocker corporations"** that only own privately offered hedge fund interests (unless the tax-exempt investor owns more than 50% of the blocker and the blocker itself has a foreign financial account (e.g., a bank account)) are exempt.

3. **Government pension plans** are exempt.

4. **Pension plan participants and IRA owners** (provided the trustee files an FBAR) are exempt. Under the Proposed Regulations, only plans under Sections 401(a), 403(a), and 403(b) of the Internal Revenue Code (the Code), as well as owners of IRAs and Roth IRAs, were included within the exemption. FinCEN refused to extend this exemption to other types of plans not covered and noted that it would be unlikely that the ownership of participants in such plans would exceed the 50% exception threshold.

5. **Investment advisers and employees of such advisers** that provide advice to entities registered with the U.S. Securities and Exchange Commission (SEC) (such as regulated investment companies, also known as U.S. mutual funds), which might otherwise have been found to have signature or other authority over a foreign financial account are exempt. FinCEN, however, notes that this exemption applies only with respect to the reportable accounts of clients of the advisers that are registered under the Investment Company Act of 1940. FinCEN refused to expand this exception to service providers to mutual funds where such service providers are not registered with the SEC. FinCEN also clarified that the exception provided to officers and employees of financial institutions that are registered with and examined by the SEC and CFTC with respect to accounts owned or maintained by such entities is only available when such entities are registered investment companies.

6. **Discretionary trusts or remainder interests in trusts**. The Preamble provides that FinCEN did not intend for a beneficiary of a discretionary trust to be considered to have a financial interest in a foreign account simply because of his status as a discretionary beneficiary and did not intend to include remainder interests within the scope of the term "present beneficial interests." Clarifying language was added to make these intentions clear.

7. **Anti-avoidance rule.** The Preamble provides that an entity will not be treated as being formed to evade the FBAR requirements if the person creating the entity is making a good-faith effort to comply with the Final Regulations.

8. **Exemption for employees of certain employers including employers that issue ADRs.** FinCEN accepted a comment that provides a filing exemption to the employees of a U.S. or foreign entity that issued a class of equity securities (including American Depository Receipts, or ADRs) registered under section 12(g) of the Securities Exchange Act of 1934 (i.e., those with at least $10 million in assets and 500 or more shareholders). This exemption was not, however, extended to mutual insurance companies with assets of more than $10 million and more than 500 policyholders.

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