

**REMINDER: CERTAIN FOREIGN FINANCIAL ACCOUNT REPORTS FOR 2009  
ARE DUE BY JUNE 30, 2010****Filers Are Subject to Interim Treasury Department Guidance for FBARs****The HIRE Act Adds Separate New Foreign Financial Account Reporting Obligations**

Several recent developments significantly affect U.S. persons with interests in foreign financial accounts. The U.S. Department of Treasury issued several releases in February 2010 modifying the filing requirements for the Report of Foreign Bank and Financial Accounts (“FBAR”) with respect to accounts held in 2009.<sup>1</sup> The U.S. Treasury’s Financial Crimes Enforcement Network (“FinCEN”) has published proposed FBAR regulations and revised instructions for Treasury Form TD F 90-22.1 that are expected to take effect for future years. The Hiring Incentives to Restore Employment Act (the “HIRE Act”), enacted in March 2010, requires U.S. persons with certain foreign financial assets to disclose information regarding those assets on their federal tax returns, effective for tax years beginning after March 18, 2010. Each of these developments is summarized below.

**FBAR REPORTING FOR 2009*****Reporting of Foreign Accounts by Persons and Entities with a Financial Interest in Such Accounts during 2009***

Any person (including an individual, trust, or business entity) subject to the jurisdiction of the United States (a “U.S. person”) and having a financial interest in a foreign financial account is generally required to file an FBAR by June 30 of each year for accounts held during the previous calendar year in which the aggregate value of such accounts was more than \$10,000. U.S. persons are required to file the FBAR with respect to foreign financial accounts, including bank and similar depository institution accounts, securities brokerage accounts, and certain other financial accounts, such as commodity futures and options accounts in which the person or entity has an interest. A person or entity with an ownership or similar interest of more than 50% in a corporation or partnership that holds foreign financial accounts is considered to have a reportable interest in those foreign accounts. If an FBAR filer has a financial interest in 25 or more foreign financial accounts, the filer may file an FBAR that discloses only the number of such accounts and other basic information, but not the maximum account value, type of account, account number, or information about the financial institution where the account is held.

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<sup>1</sup> See Willkie Farr & Gallagher Client Memorandum of March 3, 2010.

### ***Reporting by Individuals with Signature Authority over Foreign Accounts***

Under previous rules, an individual with signature or other authority over—but no financial interest in—a foreign financial account in 2009 would have been required to file an FBAR reporting such authority by June 30, 2010. Such a requirement typically affects employees with signature authority over their employers’ foreign accounts. However, pursuant to Notice 2010-23, the filing deadline for such individuals has been postponed until June 30, 2011. The proposed FinCEN regulations, when finalized, are likely to eliminate the reporting requirement for some of these individuals. However, in the meantime, appropriate records with respect to signature authority should be retained in case they may be needed for future filings. Individuals with signature authority over foreign accounts in which they also have a financial interest are still required to file an FBAR because of their financial interest.

### ***Reporting Obligations for Investors in Foreign “Funds”***

Pursuant to informal IRS staff guidance in 2009, U.S. persons having investments in foreign “commingled funds,” such as offshore hedge funds and private equity funds, in 2008 and prior years were expected to report their interests in these funds as if the funds were foreign accounts. However, the IRS guidance issued in February 2010 suspends this filing requirement as to financial interests in foreign investment funds other than offshore mutual funds. Therefore, U.S. persons with a financial interest in a foreign hedge fund or private equity fund during 2009 do not have to file an FBAR with respect to such interest. U.S. persons with a financial interest in a mutual fund account located offshore are still required to report their interest in such account.

## **THE PROPOSED REGULATIONS**

The proposed FinCEN regulations published in February 2010, if adopted as drafted, would make several significant changes to, and clarify, the FBAR requirement and revise the Form TD F 90-22.1. Some of the key changes include the following. These proposed FinCEN regulations have not yet been finalized.

### ***Who Must Report***

Under the proposed regulations, United States persons who have a financial interest in, or signature or other authority over, a reportable account in a foreign country would be required to file an FBAR for each year in which such relationship exists. “United States persons” would be defined as citizens and residents of the United States and domestic entities, such as corporations, partnerships, trusts and limited liability companies created, organized or formed under the laws of the United States.

Under current interpretations and guidance, there is an exemption from filing the FBAR available for certain employees who have signature authority over—but no financial interest in—their employers’ foreign financial accounts. Such exemption applies only to an individual with signature authority in his or her capacity as an officer or employee of a federally regulated bank or a large, publicly traded corporation. Under the proposed regulations, the exemption would be

extended to officers or employees of certain other financial companies, including securities broker-dealers and investment advisers registered with and examined by the Securities and Exchange Commission and futures commission merchants registered with and examined by the Commodity Futures Trading Commission. In addition, an officer or employee of an “Authorized Service Provider” registered with and examined by the SEC who has signature authority over, but no financial interest in, a foreign financial account owned or maintained by a registered investment company would also be exempt from reporting such authority.<sup>2</sup>

United States persons who are employed in a foreign country and who have signature authority over a foreign financial account that is owned or maintained by the individual’s employer would still need to file FBAR reports under the new draft instructions to Form TD F 90-22.1.

### ***Accounts That Must Be Reported***

Under the proposed regulations, United States persons would be required to report foreign accounts which they have a financial interest in or signature or other authority over. “Signature or other authority” would be defined as “authority of an individual (alone or in conjunction with another) to control the disposition of money, funds or other assets held in a financial account by delivery of instructions (whether communicated in writing or otherwise) directly to the person with whom the financial account is maintained.”

If adopted as currently drafted, FinCEN’s proposed regulations would clarify the reporting requirements with respect to certain types of financial interests. Specifically, they would require United States persons to report their interests in foreign bank accounts, securities accounts, and “other financial accounts,” which are defined to include: accounts with a person in the business of accepting deposits as a financial agency; insurance policies with cash value or annuity policies; accounts with a broker or dealer for futures or options transactions in any commodity on, or subject to the rules of, a commodity exchange or association; and accounts with a “mutual fund or similar pooled fund which issues shares available to the general public that have a regular net asset value determination and regular redemptions.” The proposed regulations do not include offshore hedge funds, private equity funds, or venture capital funds within that definition. When the proposed regulations were released, FinCEN acknowledged that the diverse characteristics and “lack of functional regulation” of these funds make it difficult to define them for FBAR purposes. Therefore, FinCEN “reserved” judgment with respect to FBAR reporting of interests in such funds. The agency also noted that the then-pending legislation (described below) “would apply additional regulation and oversight over the operations of some of these investment companies.”

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<sup>2</sup> An “Authorized Service Provider” is defined as an entity—such as an investment adviser—that is registered with and examined by the SEC and provides services to an investment company registered under the Investment Company Act of 1940. This exception is being proposed to address the fact that a mutual fund’s day-to-day operations are conducted by officers or employees of fund service providers.

The proposed regulations provide that a United States person having a financial interest in, or signature authority over, 25 or more foreign financial accounts need only provide the number of financial accounts and certain other basic information on the FBAR report. Such persons would be required to provide more detailed information about each account if requested by the Secretary of the U.S. Treasury.

The FinCEN proposed regulations also provide for special rules for consolidated reports. An entity that is a United States person and owns directly or indirectly more than a 50% interest in an entity required to file an FBAR report would be permitted to file a consolidated report on behalf of itself and such other entity.

The proposed regulations also provide for special rules for trusts. A financial interest in a foreign financial account would include a financial interest in a foreign account held by certain trusts. Such trusts would include (1) trusts as to which a United States person is the trust settlor and has an ownership interest in the account for federal tax purposes, (2) trusts that were established by a United States person and for which the United States person has appointed a trust protector that is subject to such person's direct or indirect instruction, and (3) trusts in which a United States person either has a beneficial interest in more than 50% of the assets or from which such person receives more than 50% of the income. The United States persons who established or settled the trusts described in (1) and (2) would be required to file FBAR reports for the foreign accounts of the trust. However, beneficiaries of trusts described in (3) would be excepted from the FBAR filing obligation if either the trust, the trustee of the trust, or an agent of the trust is a United States person that files an FBAR disclosing the trust's foreign financial accounts.

Under the proposed regulations, United States persons would be required to report the foreign financial accounts of other persons in certain specified situations. For instance, if an agent, nominee, or attorney were to hold legal title to a foreign financial account on behalf of a United States person, the United States person would be required to report the account on an FBAR. The proposed regulations also specify that a United States person would also have to report foreign financial accounts held by a corporation, partnership, or other entity (other than the trusts described above) if the United States person were to own directly or indirectly more than 50% of the voting power or the total value of the shares (in the case of a corporation), more than 50% of the interest in profits or capital (in the case of a partnership), or more than 50% of the voting power, total value of the equity interest or assets, or interest in profits (in the case of an "other entity").

An anti-avoidance rule would provide that a United States person would be considered to have a financial interest in foreign financial accounts held by an entity if the United States person caused such entity to be created "for a purpose of evading this section."

FinCEN also released draft instructions to Form TD F 90-22.1. The instructions generally restate the proposed regulations. The draft instructions are not yet in effect.

## **THE HIRE ACT—NEW TAX RETURN REPORTING REQUIREMENTS**

Under the recently enacted HIRE Act, “any individual” must report on a statement attached to his or her tax return information substantially similar to that required to be disclosed on the FBAR. This disclosure is in addition to the FBAR filing requirement and is effective for tax years beginning after March 18, 2010. The disclosure statement will be due on the due date of the individual’s Federal income tax return. Therefore, in general, taxpayers would not have to file this statement until calendar year 2011.

### ***What Must Be Reported***

Individuals are subject to this reporting requirement if they hold interests in “specified foreign financial assets,” which includes non-U.S. stocks, non-U.S. bonds, financial instruments and contracts issued by non-U.S. persons, interests in foreign entities, and interests in any financial accounts maintained by foreign financial institutions, if the aggregate value of such assets exceeds \$50,000. A “foreign financial institution” is defined as any foreign entity engaged primarily in the business of investing, reinvesting, or trading in securities, partnership interests or commodities, or any interest therein; any entity that accepts deposits in the ordinary course of a banking or similar business; or any entity that, as a substantial portion of its business, holds financial assets for the account of others.

The required disclosures include, for a stock or security, the name and address of the issuer and the class or issue of the stock or security; for a financial instrument or contract, sufficient information to identify the instrument or contract, and the names and addresses of all counterparties; and for a foreign financial account, the name and address of the foreign financial account and the account number.

The U.S. Treasury has the authority to promulgate regulations exempting certain classes of assets from the category of specified foreign financial assets. If an individual does not provide sufficient information to demonstrate the aggregate value of specified foreign financial assets, the HIRE Act presumes that the value is greater than \$50,000. Unlike the FBAR filing requirement, there is no exemption to this reporting requirement for interests in foreign hedge funds, private equity funds, or venture capital funds.

### ***Penalties***

The penalty for failure to disclose is \$10,000 per year plus an additional \$10,000 per month for up to five months if the taxpayer has been mailed a notice of a failure to disclose, such that the total maximum penalty would be \$60,000. The HIRE Act contains a “reasonable cause” exception, but reasonable cause does not include “[t]he fact that a foreign jurisdiction would impose a civil or criminal penalty on the taxpayer (or any other person) for disclosing the required information.” Understatements of tax related to income from undisclosed foreign financial assets will result in a penalty of 40 percent of the underpayment of tax.

***Additional Treasury Department Regulatory Authority***

The U.S. Treasury may provide in regulations exceptions for nonresident aliens and bona fide residents of any U.S. possessions. Regulations may also expand the scope of the required disclosure so that it applies not only to individuals but also to “any domestic entity which is formed or availed of for purposes of holding, directly or indirectly, specified foreign financial assets, in the same manner as if such entity were an individual.”

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If you have any questions regarding this memorandum, please contact Joseph A. Riley (212-728-8715, jriley@willkie.com), Barbara A. Block (202-303-1178, bblock@willkie.com) or the attorney with whom you regularly work.

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