



News From Giordani, Swanger, Ripp & Phillips, LLP

Treasury Issues Final FBAR Regulations

For Clients and Friends of GSRP, LLP

In late February 2011, the U.S. Treasury Department issued final regulations regarding its “Report of Foreign Bank and Financial Accounts,” commonly called the “FBAR.” Although the final regulations make mostly minor changes to the proposed rules put forth a year ago, they do offer welcome clarifications on a number of issues, particularly for trustees and beneficiaries of trusts owning foreign accounts and for owners of retirement accounts.

Background

You are probably aware that U.S. lawmakers in recent years have increased (i) their scrutiny of foreign investment by U.S. persons and (ii) the tax reporting obligations associated with that foreign investment. In its continuing efforts to encourage compliance with U.S. tax laws, the IRS has stepped up its enforcement actions, recently offering two amnesty programs designed to bring in U.S. taxpayers who have unreported income from foreign accounts and who have failed to comply with their reporting obligations, including the FBAR. The most recent program was announced in mid-February and runs through the end of August.¹

The FBAR is one tool used by the IRS to monitor U.S. persons’ foreign holdings and improve tax compliance generally. United States citizens and residents, and entities organized in the U.S., having a financial interest in a foreign financial account are required to file the FBAR annually disclosing identifying information and the maximum value of each foreign account held during the year. In addition, U.S. persons with signature authority over foreign accounts are also required to file the FBAR, even if they have no ownership interest in the account. Failure to file the FBAR can result in substantial civil and criminal penalties.

As a part of the increased focus on foreign compliance, the FBAR and related instructions underwent substantial revision in 2008, raising many questions among taxpayers and advisors. Many of these questions were addressed by last year’s proposed regulations, and although some questions remain, the final rules clarify key issues associated with the FBAR.

¹ For more information, visit the Newsletter section of our website (GSRP.COM) for our 2/17/2011 Newsletter discussing the details of the 2011 Offshore Voluntary Disclosure Initiative.

Definition of U.S. Person

For purposes of FBAR filing, a United States person is a citizen or resident of the United States (determined using the same guidelines as those under the Internal Revenue Code), or an entity (including but not limited to a corporation, partnership, trust or limited liability company) created under the laws of the U.S. or any state. (Note that, for a trust, the IRS did not adopt the same court and control test used in determining a trust's residency for U.S. tax purposes). Although the instructions to the most recent FBAR extended the U.S. person definition to foreign persons in and doing business in the United States, the regulations omit such persons from the FBAR filing requirement.

What is a Foreign Financial Account?

Reportable accounts include the obvious, such as foreign bank and securities accounts. Mutual funds or similar pooled funds which issue shares available to the general public are also included. Life insurance policies issued by a foreign carrier are also reportable if the policy has a cash value. Although some foreign insurance companies elect to be treated as U.S. companies for tax purposes, the final regulations clarify that such an election does not relieve the U.S. owner from reporting the policy on the FBAR.

There continues to be uncertainty as to whether foreign hedge funds and similar investments are considered to be foreign accounts for FBAR purposes. The final regulations have reserved comment on this issue, meaning that these types of investments do not need to be reported on the FBAR until such comments are issued.

What is a Financial Interest?

A U.S. person has a reportable financial interest if that person is the owner of record or has legal title to, a foreign account, even if the account is held for the benefit of others. In addition, a U.S. person will need to report foreign accounts owned by an entity if that person's ownership of that entity exceeds 50%.

The final regulations clarify situations in which U.S. persons are deemed to have a financial interest in a foreign account owned by a trust. If a trust is treated as a grantor trust for federal income tax purposes, the grantor of the trust is considered to have a financial interest in an account owned by that trust. In addition, the regulations provide that a U.S. person who has either a present beneficial interest in more than 50% of the assets or receives more than 50% of the current income has a financial interest in an account owned by the trust. The preamble to the regulations makes it clear that a beneficiary of a discretionary trust does not have a financial interest in a trust's foreign account simply by virtue of the discretionary beneficiary status in the absence of a current year distribution. In addition, a remainder interest in a trust does not constitute a present beneficial interest in a trust. This clarification is welcome relief to trustees and beneficiaries of discretionary trusts with multiple beneficiaries. In addition, the final regulations remove a provision included in the proposed rules that would have treated a U.S. person who established a trust and appointed a trust protector for that trust as having a financial interest in that trust's foreign accounts.

Finally, a beneficiary of a trust is not required to report the trust's foreign financial accounts if a trustee or agent of the trust is a U.S. person who files an FBAR reporting the foreign financial accounts and includes certain required information with the form.

Signature or Other Authority

Individuals with signature or other authority over a foreign financial account are required to file an annual FBAR. The regulations provide a bright line test for determining whether an individual has such authority. If the foreign financial institution will act upon a direct communication from that individual regarding the disposition of assets in the account, the person is required to report the

account on an annual FBAR. There are some exceptions to this rule, including officers and employees of banks subject to examination by federal agencies.

After the issuance of the revised FBAR and the 2010 proposed regulations, there was a great deal of uncertainty as to the circumstances under which an individual holding only signature authority, and no ownership interest, would be exempted from FBAR filing. Accordingly, the IRS issued guidance deferring the due date for filing 2009 and prior FBARs for those persons until June 30, 2011.² With the final regulations now in place, affected individuals will need to file not only 2010 FBARs by this year's due date, but prior year forms as well.

Retirement Plans

According to the final regulations, participants and beneficiaries of retirement plans, as well as owners and beneficiaries of IRAs, are not required to file an FBAR with respect to foreign financial accounts owned by the plan.

GSRP Can Help

The final regulations generally follow last year's proposed regulations, but include welcome guidance in situations where the requirement to file was unclear. This is good news in light of the potentially onerous penalties for failure to comply.

GSRP has extensive experience representing U.S. persons with foreign accounts and other assets and is ready to assist you or your clients in determining filing requirements for the FBAR and other U.S. information returns.

For further information regarding FBAR filing requirements, please contact:

Michael Ripp
512.370.2735
mripp@gsrp.com

Peggy Ugent
512.370.2756
pugent@gsrp.com



² Notice 2009-62, issued 8/31/09; Notice 2010-23, issued 2/28/2010.

IRS Circular 230 Disclosure: To ensure compliance with requirements imposed by the IRS, we inform you that any U.S. federal tax advice contained in this communication (including any attachments) is not intended or written to be used, and cannot be used, for the purpose of (i) avoiding penalties under the Internal Revenue Code or (ii) promoting, marketing or recommending to another party any transaction or matter addressed herein. All of the information herein is further provided for educational purposes only and is not intended to be and cannot be used as legal or tax advice by any person.