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If you have any questions, please contact your regular Groom contact or any of the attorneys listed below:

Jennifer E. Eller
jeller@groom.com
(202) 861-6604

Louis T. Mazawey
lmazawey@groom.com
(202) 861-6608

David W. Powell
dpowell@groom.com
(202) 861-6600

Andrée St. Martin
astmartin@groom.com
(202) 861-6642

Final FBAR Regulations Offer Helpful Relief for Plans – But No Blanket Exception

The Financial Crimes Enforcement Network ("FinCEN") has issued final regulations under the Bank Secrecy Act ("BSA") regarding the "Report of Foreign Bank and Financial Accounts" (Form TD F 90-22.1, or "FBAR"). The final rules appear in today's Federal Register. 76 Fed. Reg. 10234.

The general FBAR requirement is that each U.S. person who has a financial interest in, or signature or other authority over, any foreign financial accounts (broadly defined), if the aggregate value of the accounts exceeds $10,000 at any time during the calendar year, must file FBAR on or before June 30 of the following year. Although the FBAR requirements date back to the 1970's, FBAR's application to plans and plan fiduciaries became a new "hot topic" in the last two years following some informal comments by IRS officials concerning the broad scope of the rules. The three main concerns for plans and plan fiduciaries about FBAR have been: (1) the "signature or other authority" concept as it may apply to investment committee members; (2) whether individual trustees are deemed to have a "financial interest" in plan accounts; and (3) whether offshore hedge funds and private equity funds should qualify as "foreign accounts" for FBAR purposes. Importantly, these concerns extend beyond the FBAR form itself, because a person with either signature authority or a financial interest over a foreign account may be obligated to check a box on his or her own Form 1040, Schedule B, indicating the relationship to the foreign accounts. The civil penalties for a failure to file FBAR can range from $500 per violation up to the greater of $100,000 or 50 percent of the account balance, and criminal penalties may apply in some circumstances.

The final regulations largely follow the proposed regulations published a year ago. 75 Fed. Reg. 8894 (Feb. 26, 2010). As discussed below, the final regulations offer some helpful relief for many plan filers and thus should largely address the Form 1040 issue. However, the rules do not exempt employee benefit-related accounts from the FBAR requirements – notwithstanding arguments that plans do not involve the concerns with money laundering or tax evasion that prompted the FBAR rules.

The effective date of the final regulations is March 26, 2011, and the rules will apply to FBAR filings that relate to the 2010 calendar year. Filers who properly relied on a filing extension granted in IRS Notice 2010-23, which delayed FBAR filing requirements for certain persons for the 2009 calendar year until June 30, 2011, may apply the provisions of the final rule to that earlier year, too. The proposed rules were accompanied by proposed revisions to the FBAR instructions; although the final regulations reference revisions to the instructions to conform them to the final regulations, the instructions themselves are not yet available. While we are continuing to review the final rule, we have identified the following elements of the rule as particularly relevant to employee benefit plans.

- **Relief For Plan Sponsors.** Under the proposed rule, a person would have had a "financial interest" in a trust that was established by the person and for which the person appointed a "trust protector." The final rule eliminates this provision. This means that a plan sponsor who has established a trust to hold assets of an ERISA plan will not have a financial interest in the plan's accounts merely because the plan sponsor also appointed a fiduciary committee or other person who is responsible for monitoring the trustee and who has the authority to replace or recommend replacement of the trustee.

- **Narrower Definition of "Signature or Other Authority."** The final rule adopts a change to the definition of "signature or other authority" that, according to the preamble, is intended to clarify that the scope of this authority is narrower than we and other commenters feared. Specifically, commenters were concerned that any and all persons (including a plan investment committee member) included in a chain of persons with the ability to ultimately cause the disposition of assets from a foreign account might be deemed to have "signature or other authority" over that account. Under the final rule, a person must have the ability to (1) "control the disposition" of assets in a foreign financial account (2) by "direct communication" with "the person with whom the account is maintained." FinCEN apparently intends for this rule to substantially limit the number of persons who are deemed to have "signature or other authority" over an account. This is particularly helpful because, without the requisite authority, committee members and persons in similar positions need not check the box on their individual tax returns indicating that they have a relationship to a foreign financial account.

- **Narrower Interpretation of "Financial Account."** The preamble to the final rule clarifies that a U.S. person will not have to file FBAR with respect to a custody account held outside of the U.S. if the U.S. person cannot "directly access" the foreign holdings in that account (for example, there is an intermediary manager or custodian who has the direct access). Because this clarification narrows the definition of "foreign financial account," it is relevant both to persons who may have a "financial interest" in the account *and* to those who may have "signature or other authority over" the account. While the clarification is potentially very helpful, it too, raises some interpretive questions.

- **Treatment of Offshore Hedge Funds and Private Equity Funds Still "Reserved."** The proposed rule did not include offshore hedge funds and private equity funds within the definition of "reportable accounts" but instead "reserved" treatment of these accounts. The final rule also "reserves" the treatment of these funds. Thus, the only type of commingled investment funds that trigger FBAR filing obligations are foreign "mutual funds" or similar funds which issue shares generally available to the general public, and offer regular redemptions. We note that if a plan (or other investor) owns more than 50 percent of the interests in an offshore corporation, partnership or trust, a filing requirement also may apply.

- **Exception for Plan Participants and Beneficiaries.** The final rule retains the exception in the proposed rule providing that participants in, and beneficiaries of, plans meeting the requirements of Code sections 401(a), 403(a), 403(b) – and owners and beneficiaries of individual retirement accounts under Code section 408 and 408A – are not required to file FBAR with respect to a foreign financial account held by or on behalf of the plan or IRA.

- **Exception for Governmental Plans.** The instructions that accompanied the proposed regulation expressly stated that the foreign financial account of any employee retirement or welfare plan of a government entity is not required to be reported on FBAR *by any person*. The final regulations do not specifically address this, but we expect that the final instructions, when available, will continue to provide this blanket exception for governmental plan filers.

It is particularly important that plan sponsors and financial institutions become familiar with the final rules very soon. Needless to say, the initial tax filing deadline is less than two months away. And the FBAR report itself, if required for 2010, must be filed on or before June 30, 2011.