

## **FBAR: IRS Provides Limited Relief for Foreign Hedge Funds and Private Equity Funds**

The Internal Revenue Service (“IRS”) has granted relief from the onerous FBAR – or Foreign Bank and Financial Account – filing requirements for certain foreign funds. FBAR reporting is generally required under U.S. law to advise the Treasury Department that certain persons have a financial interest in, or signature authority over, a foreign bank or other financial account. FBAR reports are due June 30th for the prior calendar year.

On February 26, 2010, the IRS issued Notice 2010-23 which provides interim guidance on FBAR reporting with respect to foreign hedge funds and foreign private equity funds. Under the Notice, foreign hedge funds and foreign private equity funds will not be subject to FBAR reporting requirements for the calendar year 2009 and prior years. Accordingly, taxpayers that had a financial interest in, or signature authority over, such foreign funds in 2009 or an earlier year do not need to file FBARs.<sup>1</sup>

The Notice also provides additional administrative relief for taxpayers filing their annual income tax returns. Specifically, a taxpayer that qualifies for FBAR relief under the Notice should check the “no” box in response to the FBAR-related questions found on federal tax forms for 2009 and earlier years that ask about the existence of a financial interest in, or signature authority over, a foreign financial account.

The new IRS pronouncement does not apply to the calendar year 2010 (due on June 30, 2011). Owners and advisors must await further guidance to determine their FBAR filing responsibilities for the calendar year 2010.

A brief look at the circumstances under which Notice 2010-23 was issued indicates that the Notice is viewed by the government as a temporary solution to a larger problem which will require additional study and legislation. Notice 2010-23 was issued concurrently with the release of proposed regulations by the Treasury Department. The proposed regulations continue to distinguish mutual funds (which are subject to FBAR reporting) from foreign hedge funds and foreign private equity funds. The proposed regulations state that mutual funds are required to file FBARs because such funds can be used to integrate illegal income into legitimate assets thereby allowing illegal proceeds to appear to have a legitimate source. The Treasury Department is also concerned about the use of foreign hedge funds to effectuate a similar result, but the lack of functional



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regulation over foreign funds makes it difficult to define and distinguish certain types of these funds from others.

In providing this limited relief for foreign hedge funds and foreign private equity funds, the Treasury Department indicated that it is aware of other legislative proposals that would require U.S. persons to report foreign hedge fund and foreign private equity fund holdings to the IRS.<sup>2</sup> Based on the pendency of these legislative proposals, the Treasury Department determined it appropriate to reserve the treatment of investment companies other than mutual funds. The Treasury Department stated that it will continue to study the use of foreign hedge funds to evade U.S. income taxes.

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- <sup>1</sup> Previously, Notice 2009-62 provided that persons with a financial interest in, or signature authority over, a foreign commingled fund had until June 30, 2010 to file FBARs for the 2008 calendar year and earlier years.
  - <sup>2</sup> For example, the Hiring Incentives to Restore Employment Act, included as Senate Amendment 3310 to HR 2847. The foreign account tax compliance provisions of this bill are very similar to those in the "Foreign Account Tax Compliance Act of 2009" introduced in the Senate on October 27, 2009.

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