

# Practitioners' Corner

## IRS Extends FBAR Deadline; Reiterates Foreign Hedge Fund Reporting Requirement

Shortly before the June 30 filing deadline for Form TD F 90-22.1, Report of Foreign Bank and Financial Accounts (known as the "FBAR"), the IRS announced that some taxpayers may have additional time to file. The IRS also clarified that the taxpayers with investments in foreign hedge funds and private equity funds must file FBARs.

■ **Comment.** The FBAR extension takes on new importance this year because of the IRS's heightened interest in curbing offshore tax evasion. The IRS has been heavily encouraging participation in its temporary offshore disclosure initiative by taxpayers with unreported foreign accounts.

### June 30 deadline

Taxpayers with a financial interest in or signature or other authority over any type of financial account in a foreign country may be required to report this information to the U.S. government. Taxpayers use the FBAR if the aggregate value of these accounts exceeds \$10,000 at any time during the calendar year.

### Extension

Some taxpayers may be eligible for an extension beyond June 30 for 2008 FBARs. Taxpayers who reported and paid tax on all of their 2008 taxable income but only recently learned of their FBAR filing obligation and have insufficient time to gather the necessary information to complete the FBAR have until September 23, 2009 to file. The IRS instructed taxpayers to attach a statement explaining why the FBAR is filed late.

### Signature authority

The IRS also announced special FBAR filing rules related to the offshore compliance ini-

tiative for taxpayers with signature authority but no beneficial interest in an account. A taxpayer may cure the FBAR delinquency for the account the taxpayer does not own by filing the FBAR with an explanatory statement by September 23, 2009.

instructions issued in October 2008, the definition of financial account encompasses "any accounts in which the assets are held in a commingled fund, and the account owner holds an equity interest in the fund (including mutual funds)."

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*"The IRS confirmed for CCH that taxpayers with investments in foreign hedge funds and private equity funds are subject to FBAR reporting."*

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This treatment, the IRS explained, applies if there is no unreported income with respect to the account. If the account over which the taxpayer has signature authority is held in the name of a related person, such as a family member or a corporation controlled by the taxpayer, the taxpayer may be liable for a penalty under the offshore disclosure initiative if there is unreported income on the account.

■ **Comment.** "Similar treatment is extended to individuals who need to file Form 3520 for interests in foreign trusts or Form 5471 for interests in foreign corporations under circumstances," James Mastracchio, partner, Caplin & Drysdale, Chartered, Washington, D.C., told CCH. This treatment would apply to taxpayers who have failed to file Form 3520 or Form 5471 but reported and paid tax on all their taxable income with respect to all transaction related to foreign trusts or foreign corporations.

### Hedge funds

The FBAR filing requirement applies to U.S. persons who have a financial interest in or signature authority over any foreign financial accounts. Under revised FBAR

The IRS confirmed for CCH that taxpayers with investments in foreign hedge funds and private equity funds are subject to FBAR reporting. "We believe that generally investors in hedge funds and private equity funds are required to file FBARs since they have equity interests in funds with commingled assets, but each investor must consider his or her specific factual circumstances in determining whether the fund in question falls within the instructions' definition of a Financial Account," an IRS spokesperson told CCH.

### Offshore compliance initiative

The IRS's offshore disclosure initiative offers taxpayers freedom from criminal prosecution in exchange for full disclosure of unreported foreign accounts. The IRS will assess an offshore penalty. The offshore penalty equals 20-percent of the amount in foreign bank accounts/entities in the year with the highest aggregate account/asset value.

■ **Comment.** The IRS is asking taxpayers to come in under the voluntary disclosure initiative but taxpayers will have some options if they disagree with the 20-per-

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## Incentive Payments In Mortgage Modification Program Excluded From Income

◆ *Rev. Rul. 2009-19*

The IRS recently announced that “Pay-for-Performance Success Payments” in the federal Home Affordable Modification Program (HAMP) are excluded from a recipient’s gross income. The IRS determined that the payments qualify for the general welfare exclusion from gross income.

■ **CCH Take Away.** HAMP was created by the Obama administration’s Homeowner Affordability and Stability Plan. Under HAMP, borrowers who are in default, at risk of imminent default, or in foreclosure can modify their loans to a more affordable monthly payment targeted at a certain percentage of their monthly gross incomes. HAMP enables home owners participating in the program who make timely payments on their modified loans to be eligible to have incentive payments made on their behalf to lenders and/or investors. HAMP is available for mortgages originated on or prior to January 1, 2009. The program will expire after 2012.

### General welfare exclusion

Under the general welfare exclusion, certain payments by state and federal governments designed to promote the general welfare are not included in an individual’s gross income. Generally, the payments must be made from a governmental fund, be for the promotion of general welfare (for example,

based on need), and must not represent compensation for services.

### Performance payments

Borrowers who remain current on their mortgage payments are eligible for an incentive in the form of a principal reduction of up to \$1,000 per year for five years, subject to a de minimis threshold. The incentive accrues monthly and is awarded annually.

### Exclusion

The IRS determined that HAMP’s Pay-for-Performance Success Payments qualify for the general welfare exclusion and are not included in the recipient’s gross income. According to the IRS, the

payments meet the definition of payments made under a governmental societal benefit program for the promotion of the general welfare and not for services rendered by the recipient.

The IRS further determined that the payments help home owners who are at risk of losing their homes to pay their mortgage loans, thus promoting the general welfare. Moreover, the payments are not for the performance of services, and also meet the other requirements of the general welfare exclusion.

■ **Comment.** HAMP replaced the Streamlined Modification and the Early Workout programs.

*References: FED ¶(to be reported);  
TRC INDIV: 33,354.*

### Attorney Work Product Privilege Protects Workpapers From Disclosure

A federal district court has denied the government’s motion to compel an auditor to produce documents for a tax refund case involving the auditor’s client. The court found that the attorney work product privilege protected several documents. Other documents held by the auditor’s Swiss affiliate did not have to be disclosed because the auditor had no authority to compel their disclosure.

■ **CCH Take Away.** The decision is another defeat for the federal government in its litigation over the disclosure of workpapers. The district court applied and upheld a generally traditional approach to the work product privilege.

**Court’s analysis.** Disclosure of work-product materials can waive the privilege for those materials if the disclosure, under the circumstances, is inconsistent with the maintenance of secrecy from the disclosing party’s adversary, the court noted. In this case the taxpayer’s disclosure to the auditor was not inconsistent with the maintenance of secrecy. The auditor was not a potential adversary. It was reasonable for the client to expect the auditor to keep the information confidential.

The court also held that the auditor in the U.S. did not have sufficient control over the documents maintained at the client’s Swiss affiliate. The government could not show that the auditor had the legal right, authority or ability to obtain documents upon demand from the Swiss affiliate. “Close cooperation on a specific project does not, *per se*, establish an ability, let alone a legal right or authority...to acquire documents maintained solely by a legally distinct entity,” the court found.

■ **Comment.** The protection given to an attorney’s thoughts and impressions concerning a client’s tax issues under litigation is known as the “work product” privilege. The court relied on two recent tax cases involving attorney work product: *Regions Fin. Corp., DC-Ala., May 8, 2008*, and *U.S. v. Textron, DC-R.I., 2007*. An *en banc* panel of the First Circuit Court of Appeals heard oral argument on the *Textron* appeal in June.

*Deloitte & Touche, USA LLP, DC-D.C., June 8, 2009, FED ¶(to be reported);  
TRC IRS: 21,403.25.*

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cent offshore penalty, Mastracchio noted. The IRS has advised that taxpayers who disagree with the agency’s determination in the closing agreement may request their case be referred for a standard examination with recourse to IRS Appeals.