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Reports of Foreign Financial Accounts Regulations and FinCEN Form 114, Report of Foreign Bank and Financial Accounts (FBAR)

Why Treasury Should Exercise Its Regulatory Authority To Exempt U.S. Citizens Residing Outside The United States From The FBAR – 31 U.S.C. 5314 Requirement

John Richardson – Toronto, Canada – April 29, 2024

Outline:

Treasury should explain precisely what it is about the status of U.S. citizenship (regardless of residence or connection to the United States) that creates a presumption of tax evasion, terrorism and money laundering.

The time has come for Treasury to recognize the obvious injustice and stop requiring an FBAR to report the "local" bank accounts of Americans abroad to the Financial Crimes Division of U.S. Treasury!!

Part I – Introduction and Context- Understanding The April 29, 2024 Deadline For FBAR Commentary Submissions

FinCEN is seeking to renew its authority to require bank and financial account reporting. The statute governing the process states that:

"Before approving a proposed collection of information, the Director shall determine whether the collection of information by the agency is necessary for the proper performance of the functions of the agency, including whether the information shall have practical utility. Before making a determination the Director may give the agency and other interested persons an opportunity to be heard or to submit statements in writing. To the extent, if any, that the Director determines that the collection of information by an agency is unnecessary for any reason, the agency may not engage in the collection of information. (Added Pub. L. 104–13, § 2, May 22, 1995, 109 Stat. 179.)"

https://www.law.cornell.edu/uscode/text/44/3508

Part II – Comment: Statement Of Purpose

There have been many comments describing the hardship and unreasonableness of the FBAR requirement as applied to U.S. citizens living outside the United States. These comments state that the FBAR requirement imposed on Americans abroad is a requirement that they report their "local accounts" (used for everyday activities) to the Financial Crimes Division of U.S. Treasury. In other words: they report bank accounts in a country where they DO LIVE to a country where they DO NOT LIVE. There is no other country in the world that imposes such penalty laden requirements. Incredibly the requirement is NOT based on any physical or economic connection to the United States. Rather the requirement is because and ONLY because of the status of U.S. citizenship. I do NOT intend to duplicate other comments. That said, I do agree with the content of those comments and very specifically would endorse the comments submitted at various times in the process by:

– The Democrats Abroad Taxation Tax Force – April 27, 2024

https://www.democratsabroad.org/taxation_task_force_s_response_to_treasury_department_s_comment_period_for_the_fbar

– AARO ("Association Of Americans Resident Overseas") – April 24, 2024

https://www.aaro.org/images/advocacy/LTR-TO-OMB-FBAR-2024APR18.pdf

– ACA (“American Citizens Abroad”) – September 30, 2023

https://assets.nationbuilder.com/americansabroad/pages/1922/attachments/original/1696083754/aca-s-submission-to-fincen-230929-comment-on-fincen-form-114-fbar.pdf?1696083754

and many other comments from other individuals submitted as part of the process:

https://www.reginfo.gov/public/do/PRAViewDocument?ref_nbr=202403-1506-001

This comment is designed to complement other comments and argue that:

– the application of FBAR is overinclusive because it applies to people it should not apply to because they have no relevant connection to the United States (individuals who are residents of other countries who just happen to be U.S. citizens); and

– the application of FBAR may be underinclusive because it does NOT apply to people who have a stronger connection to the United States than many U.S. citizens. (Although I do NOT advocate expanding the kinds of individuals subject to FBAR, I believe that the FBAR requirement (like “tax residence”) should be based on connection to the United States and NOT based on the status of citizenship.)

To put it another way:

Citizenship is usually conferred by “circumstances of birth”.
Residence is a reality that reflects “circumstances of life”.

Any FBAR requirements should be based on “circumstances of life” (like residence) that indicate a connection to the United States. The requirement should NOT be based on “circumstances of birth” (like citizenship) that often indicate zero connection to the United States.

The Treasury Secretary has the clear statutory authority to exempt Americans abroad from the FBAR requirement. It should exercise its statutory authority to exempt U.S. citizens who reside outside the United States as tax paying residents of other countries.

Part III – Looking For Mr. FBAR – Where are the rules found?

The FBAR rules are found in a combination of the:
– Statute – 31 U.S.C. 5314 – https://www.law.cornell.edu/uscode/text/31/5314
-Treasury Regulations – https://www.law.cornell.edu/cfr/text/31/1010.350
– FBAR Instructions – https://www.fincen.gov/sites/default/files/shared/FBAR%20Line%20Item%20Filing%20Instructions.pdf

The starting point is the statue which reads as follows:

(*a) Considering the need to avoid impeding or controlling the export or import of monetary instruments and the need to avoid burdening unreasonably a person making a transaction with a foreign financial agency,* ***the Secretary of the Treasury shall require a resident or citizen of the United States or a person in, and doing business in, the United States,*** *to keep records, file reports, or keep records and file reports, when the resident, citizen, or person makes a transaction or maintains a relation for any person with a foreign financial agency. The records and reports shall contain the following information in the way and to the extent the Secretary prescribes:*

(1) the identity and address of participants in a transaction or relationship.
(2) the legal capacity in which a participant is acting.
(3) the identity of real parties in interest.
(4) a description of the transaction.

(b) The Secretary may prescribe—

(1) ***a reasonable classification of persons subject to or exempt from a requirement under this section or a regulation under this section;***
(2) a foreign country to which a requirement or a regulation under this section applies if the Secretary decides applying the requirement or regulation to all foreign countries is unnecessary or undesirable;
(3) the magnitude of transactions subject to a requirement or a regulation under this section;
(4) the kind of transaction subject to or exempt from a requirement or a regulation under this section; and
(5) other matters the Secretary considers necessary to carry out this section or a regulation under this section.

(c) A person shall be required to disclose a record required to be kept under this section or under a regulation under this section only as required by law.

(Pub. L. 97–258, Sept. 13, 1982, 96 Stat. 997.)

A reading of the statute reveals that:

– The Treasury Secretary creates/designs the rules
– The Treasury Secretary has broad authority to exempt any group of individuals (including U.S. citizens living outside the United States).

Therefore, to understand the FBAR obligations one must look to the Treasury FBAR Regulations.

Part IV – Understanding FBAR: "U.S. Persons" are required to file an FBAR. Who is a "U.S. Person"?

According to the Treasury FBAR Regulation:

(b) United States person. For purposes of this section, the term "United States person" means—
(1) A citizen of the United States;
(2) A resident of the United States. A resident of the United States is an individual who is a resident alien under 26 U.S.C. 7701(b) and the regulations thereunder but using the definition of "United States" provided in 31 CFR 1010.100(hhh) rather than the definition of "United States" in 26 CFR 301.7701(b)–1(c)(2)(ii); and
https://www.law.cornell.edu/cfr/text/31/1010.350

U.S. citizenship ALWAYS triggers an FBAR filing requirement. But, do all U.S. citizens have a connection to the United States?

U.S. residents are defined as non-citizens who are "resident aliens" under 26 U.S.C. 7701(b). However, not all "resident aliens" (example Green Card holders) have a strong connection to the United States. In addition, many "nonresidents" DO have a substantial connection (students, teachers, Canadian snowbirds, etc.) to the United States.

Should the requirement to file an FBAR be based on one's status as a U.S. citizen or on one's connection to the United States?

Part V – FBAR and U.S. Citizens: The World of Mr. FBAR in 1970 is NOT The World Of Mr. FBAR 2024

The FBAR requirement includes U.S. citizens abroad with no connection to the United States

The language of the statute has not changed in any significant way since 1970. Yet the world has changed. What it means to be a U.S. citizen (both in and outside the United States) has changed in two important ways.

(i) The world has changed – The 21st Century is not like the 20th century

In 1970 there was no internet, there was no email, there were few sources of alternative media, travel outside the USA was expensive and available only to those with sufficient wealth and sufficient time. There was no such thing as "remote work". There were no "digital nomads". Dual citizenship was the exception rather than the rule. U.S. citizens moving abroad could NOT naturalize as citizens of another country without jeopardizing the status of their U.S. citizenship. There was no such thing as an "Accidental American". U.S. citizenship taxation existed in theory, but was largely unknown and certainly not enforced. There was no FATCA and no PFIC. CFC rules were in their infancy. Furthermore, $10,000 was a great deal of money.

(ii) U.S. citizenship has expanded – The impact of Afroyim on U.S. citizens living outside the United States

In 1970 there was a greater overlap between U.S. citizenship and U.S. residency. There was a higher correlation between citizenship and country of residence. If a U.S. citizen moved from the United States and became a citizen of another country, he would likely lose U.S. citizenship. Dual citizenship was less common. One could easily commit expatriating acts. In 1967, the U.S. Supreme Court – in Afroyim v. Rusk – effectively opened the door to dual citizenship by ruling that Congress could not strip people of their citizenship. Dual citizenship meant more U.S. citizens were residing abroad.

As conceived in 1970, the FBAR filing requirement clearly impacted mostly resident Americans with significant amounts in "foreign" bank accounts. In addition, (given the higher correlation between citizenship and residency) it is likely that the 1970 FBAR was

intended to apply to individuals with a physical/economic connection to the United States. *(The FBAR statute applied to individuals who were "a resident or citizen of the United States or a person in, and doing business in, the United States,".)*
As applied in 2024, the FBAR filing requirement clearly impacts mostly U.S. citizens living outside the United States, with local bank accounts, in their country of residence. $10,000 in 1970 is reported to be the equivalent of approximately $80,000 today. The low $10,000 reporting threshold means that in practical impact, the FBAR requirement is a requirement that:

U.S. citizens living outside the United States, regardless of their connection to the United States, are required (under threat of obscene penalty) to report their local bank accounts to the Financial Crimes Division of U.S. Treasury on an annual basis!

Therefore, the FBAR rules of 1970 have evolved in impact and are now completely different from how the FBAR rules are applied in 2024. The practical meaning of "foreign" has changed. The meaning of "citizenship" has changed. The monetary threshold triggering reporting has changed. Yet, U.S. Treasury believes that a 1970 law designed to apply to resident Americans in 1970 (in circumstances that might indicate improper conduct) should be applied to U.S. citizens in 2024 living outside the United States (in circumstances consistent with normal and necessary conduct).

Furthermore, the FBAR requirement applies to all U.S. citizens living outside the United States even if they have no connection to the United States (other than citizenship conferred by the circumstances of their birth).

Why should the FBAR be required of people who (1) have no connection to the United States and (2) reside in other countries and (3) pay taxes to those other countries?

Part VI – Non-application of the FBAR rules to U.S. citizens who reside in U.S. territories

The FBAR requirement does NOT include U.S. citizens living in U.S. territories who (arguably) are similar to U.S. citizens in foreign countries. This means that the FBAR requirement does NOT apply to the local accounts in U.S. territories of U.S. citizens living in those U.S. territories.

Interestingly:

A U.S. citizen living in France is required to report his local French account on an FBAR.

A U.S. citizen living in Guam or the Virgin Islands is not required to report his local accounts on an FBAR. (This is because the definition of "foreign" in the 1010.350 regulations excludes accounts held in U.S. territories.)

Part VII – Four Examples: The application of FBAR to non-citizens who do NOT live in U.S. territories

Example 1 – The FBAR requirement does NOT apply to U.S. "nationals" who reside in American Samoa

U.S. nationals residing in American Samoa are entitled to a U.S. passport. They are (like Green Card holders and U.S. citizens) entitled to live in the United States. Yet because they are NOT U.S. citizens or residents they are exempt from the FBAR requirement.

Example 2 – The FBAR requirement does NOT include large numbers of nonresident aliens who may spend a great deal of time in the United States

Nonresidents aliens (as defined in IRC 7701(b) are not required to file FBARs **even when they spend substantial time in the United States which may include doing business in the United States.**

A non-citizen could spend substantial amounts of time in the United States (120 days each year) and not be a U.S. resident. He might hold a visa (student, teacher, etc.) that could prevent him (as per IRC 7701(b)) from becoming a resident alien. He might rely on the "closer connection" exemption to avoid becoming a U.S. resident. Yet, all of this time he might spend considerable time in the United States. He might have foreign bank accounts that could be used for nefarious purposes.

Example 3 – Green Card holders (who are deemed U.S. residents) may be exempted from the FBAR requirement because they are able to use a "treaty tie break" provision

in a U.S. tax treaty to become a "treaty nonresident" (as confirmed by the recent decision in Aroeste).

Aroeste-v-United-States-Order-Nov-2023
The Treasury Regulations (whether by accident or by design) have exempted individuals who (1) meet the requirements of IRC 7701(b) to be "residents" but are dual residents under a U.S. tax treaty. To put it simply, the treaty allows them to be (1) residents of the United States, but (2) nonresidents pursuant to a tax treaty and therefore not subject to the FBAR requirement.

Example 4 – 31. U.S.C. 5314 includes U.S. "citizens", "residents", "or a person in, and doing business in, the United States" within the scope of FBAR filing requirements.

Treasury has used its statutory authorization to exempt individuals doing business in the United States from the FBAR requirement. It is likely that those doing business in the United States have a stronger connection to the United States than many U.S. citizens living outside the United States. Yet U.S. citizens living outside the United States are required to file an FBAR and those merely doing business in the United States are exempted from the statutory requirement.

Useful commentary may be found at:

https://www.hodgsonruss.com/newsroom-publications-NewGuidanceonForeignBankAccountReportingFBAR.html

https://www.irs.gov/pub/irs-drop/a-09-51.pdf

https://heinonline.org/HOL/LandingPage?handle=hein.journals/jrlfin8&div=28&id=&page=

https://heinonline.org/HOL/LandingPage?handle=hein.journals/jtaxpp13&div=11&id=&page=

These four examples describe individuals with a much greater connection to the United States (who are not required to file FBARs) than many U.S. citizens living outside the United States (who are required to file FBARs).

Part VIII – Conclusion: If ALL U.S. citizens (regardless of connection to the United States) are to be subject to the FBAR requirement …

Treasury should explain precisely what it is about the status of U.S. citizenship (regardless of residence or connection to the United States) that creates a presumption of tax evasion, terrorism and money laundering.

The time has come for Treasury to recognize the obvious injustice and stop requiring an FBAR to report the "local" bank accounts of Americans abroad to the Financial Crimes Division of U.S. Treasury!!