ACA RBT Proposal – Feedback:

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Overview

This feedback addresses the Residence Based Taxation (RBT) proposal from American Citizens Abroad that can be found at these links:

- https://www.americansabroad.org/media/files/page/0aacae5d/Residency-Based_Taxation_ACA_Descr_and_Side-By-Side_Comparison_170207.1.pdf
- https://www.americansabroad.org/advancements-acas-residency-based-taxation-rbt-proposal/
- https://www.americansabroad.org/news/aca-publishes-detailed-descr-of-its-rbt-proposal-and-announces-coalition-to-score-rbt-proposal/
- https://www.americansabroad.org/news/aca-advances-on-residency-based-taxation-rbt/

This proposal starts from the premise that citizenship is an acceptable basis for taxation. Shouldn't that premise be questioned? Allison Christians, tax law professor at McGill University, argues that citizenship alone is not a sufficient basis for taxation (https://ssrn.com/abstract=2924925). Every other country on the planet (bar Eritrea) starts from the premise that countries have the right to tax residents to support the services used by residents.

Qualification for RBT

For Accidental Americans – both those born in the US to foreign parents who have not lived in the US as an adult, and those born outside the US who qualify for US citizenship from birth but have never lived in the US – the justification for citizenship based taxation is non-existent. Do these individuals need to apply for a "Departure Certificate"? If so, at what age?

When a person makes a long-term move out of the US, why should they have to wait for 5 years to qualify for RBT? If I move from California to Texas, once I've established a residence in Texas, California no longer taxes me as a resident, effective immediately. Why should an international move be any different?

While waiting those 5 years, US tax will cost low income earners much more than it does under the current system. The proposal repeals the Foreign Earned Income Exemption (FEIE). While the level of FEIE is quite high, it is most valuable for middle class and lower socio-economic groups. Other countries have much more generous tax free thresholds and lower tax rates at low income levels. In Australia, for example, an individual could earn up to A$20,000 (US$15,000) before any Australian tax is due. Loss of FEIE will mean tax is due to the US for individuals earning US$10-15k. At the other end of the income spectrum, however, FTC is always a better answer than FEIE. Australia's tax rates rise to 45% for incomes above A$180,000 (US$135,000). So, *repeal of Section 911 FEIE will impact those least able to pay additional taxes and exacerbate income inequality*.

The proposal does not address other information returns. Current IRS rules require that forms 8621 (PFICs) and 5471 (controlled foreign corporation) are required even when a tax return is not. For many Americans abroad, the reporting (and associated punitive penalties) is more of a problem than actually paying taxes (most owe no tax to the US anyway). If the reporting continues as long as one is a citizen, then renunciations will continue as well.

Departure Certificate

When applying for a Departure Certificate it appears that the IRS has control over the timing of the issuance of the Certificate and thus the effective date. With the current renunciation process, the potential renunciant has the date of the appointment in advance and can decide on the day whether to complete the process or not. With volatile exchange rates, the timing can affect the US dollar net worth of the individual, potentially subjecting them to the Departure Tax should the value of the US dollar fall relative to their home currency in the time between submission and approval of the application for Departure Certificate. Additionally, lack of control over the timing could cause hardship for those who must be free of US reporting to take up a job, or otherwise have a time-critical need to be free of US taxation.

Annual re-certification is a bureaucratic nightmare. One possible alternative is to collect this information as US citizens enter and leave the country. For those who return to employment in the US, the chance of avoiding taxation is minimal. Similarly, Social Security checks or investment income sent to a US address could be used as a rebuttable presumption that the US citizen is once again residing in the US.

In the Departure Tax section of the proposal it is not clear whether the intention is to use the net worth threshold in section 877(a)(2) and raise that to $5million for both renunciants and citizens opting in to RBT. Given the justification used by legislators for both the exit tax and the Departure Tax, the net worth threshold for both should be linked to the estate tax threshold and similarly indexed for inflation.

At what point does an individual determine that they have been tax compliant. Is it similar to the current Exit Tax procedures where delinquent returns filed before filing form 8854 allow one to certify compliance?

The IRS "User Fee" of $2,350 per person is a lot of money for those on modest incomes – precisely the people who will be hurt most by the repeal of section 911. The renunciation fee, which the IRS User fee is based on, is already the highest such fee in the world, and a financial hardship for many. Forcing citizens to **buy their way out of** Citizenship based taxation at this high price means that only those who are already relatively well-off will be able to buy their freedom. Like the current system, the proposal *exacerbates income inequality* by making it prohibitively expensive for those with incomes below the median to exit the double taxation forced on them by the unfair system of citizenship based taxation. As under current rules, the proposed User Fee also makes it harder and more expensive for US citizens residing outside of the US to leave the US tax system than it is for permanent residents (green card holders) – in this area citizens are treated worse than non-citizens!

Furthermore, setting the IRS User Fee to the same price as renunciation makes renunciation preferable to RBT for many citizens abroad. Those who will not be covered expatriates, who are having trouble maintaining banking relationships, are shut out of jobs due to either FATCA/FBAR reporting or the requirement to report controlled corporations to the IRS, or have no intention of returning to the US will find renunciation preferable.

Anti-Abuse Rules

Under the Anti-Abuse rules – gain from sale of securities taxable in the US for two years after receiving the Departure Certificate: but individuals must have a foreign residence for five years before they are even eligible for a Departure Certificate, and if their net worth is above $5 million they must pay a Departure Tax. What abuse is it if securities are sold within 2 years of receiving the Departure Certificate?

On page 6: “Individuals eligible for the special rule for individuals residing abroad (RBT rules, above) would be subject to the Departure Tax, whether or not they are tax-compliant. The date of departure for such individuals would be the subsequent date of issuance of a valid Certificate.” This appears to contradict the special rule on page 5 which states that these individuals are not subject to the Departure Tax if they are tax-compliant.

On page 6: “If an individual who was a non-resident American for any of the prior 5 years and was a resident American for **any year prior to that period**, and again becomes a resident American, then he or she shall be treated as a resident American for each of the prior five years.” (emphasis added) This appears to be saying that anyone returning to the US who has **ever** been subject to US tax will have to amend their prior 5 years of non-resident returns and file as a resident. The proposal requires individuals to wait for 5 years before they are eligible for RBT, then if their life circumstances change and they move back to the US, they will lose the benefit of up to 5 years of non-resident treatment under RBT?

FATCA and FBAR reporting

There are several reasons FATCA should be repealed beyond the problem of access to banking by US Persons. FATCA costs much more than it will ever generate in revenue. The OECD’s Common Reporting Standard (CRS) has been implemented by financial institutions in many of the countries with FATCA IGAs. Under CRS, institutions collect the tax residence of their clients. If the US were to abandon FATCA and implement CRS (not likely, I know), then financial institutions would not be required to use a separate system for American clients, and they would no longer be subject to the 30% FATCA withholding. Under those circumstances, FFIs would be much more welcoming to American clients. Furthermore, those Americans who qualify for RBT, would be tax-resident only in one country, and only reported to that country. Those who do not yet qualify would be tax-resident in two countries (one being the US) and their data would be reported to the US.

Same Country Exception (SCE): There are many legitimate reasons to hold bank accounts in countries other than where one is resident. In Europe, in particular, it is quite common to bank in another country. SCE does not make compliance any easier for FFIs – they must still keep track of their American account holders and treat them differently should they move across a border or back to the US. Under FATCA, the threat of 30% withholding is so draconian that many banks, especially European banks burned by the DOJ, are not willing to take any risks with US citizen account holders. What concrete evidence does ACA have that banks, especially in Europe, will be any more willing to deal with Americans under SCE?

For taxpayers who qualify for RBT and have received a Departure Certificate, why does the US need to know about their non-US bank accounts and investments? In this circumstance, non-US accounts do not generate income taxable in the US. Requiring FBAR reporting (and form 8938 for any accounts not required to be reported on FBAR) will be seen as a disadvantage to retaining US citizenship. Many NRA spouses and business partners object to joint accounts being reported to the IRS and/or FINCEN.