

## U.S. House Bill Proposes Residency-Based Tax Regime

by Amanda Athanasiou and Jennifer McLoughlin

Seeking to alleviate the unique burden of citizenship-based taxation and provide individuals with some measure of territoriality, a new House bill would introduce a residence-based tax system in the United States.

H.R. 7358, introduced December 20 by Rep. George Holding, R-N.C., would align the United States with many other jurisdictions around the world that have adopted residence-based systems. The move would be a first step to “ending the onerous burdens of citizenship-based taxation,” according to the bill’s description.

American Citizens Abroad supports the proposal as an “extremely important first step,” said Charles M. Bruce, the group’s legal counsel. Ultimately the legislation needs to be revenue neutral and resistant to abuse, he said, adding that “no one should be worse off than they are now.” This is the first time Congress has put residency-based taxation on the table, and it’s very important for Americans abroad, he said.

Dubbed the Tax Fairness for Americans Abroad Act of 2018, H.R. 7358 would allow qualified nonresident citizens to carve out foreign-source income from gross income and exempt that income from U.S. taxation. The exclusion would cover foreign earned income and foreign unearned income, which is defined generally as income sourced outside the United States that does not fall within foreign earned income.

However, qualified nonresident citizens would still be liable for tax on their U.S.-source income.

American Citizens Abroad has wanted to see movement on this subject for a long time and has been working on the details of the legislation for over a year, Bruce said. “Certainly this will give absolute pause to anyone considering citizenship renunciation,” he said. Onerous reporting obligations and penalties under the Foreign Account Tax Compliance Act and foreign bank account reporting rules have been blamed for an upward trend in expatriations since 2012.

U.S. citizens who reside abroad have a complex set of tax rules and burdens, specifically

tax filing obligations that apply to them, although most will actually owe little or no U.S. federal income tax because of the foreign earned income exclusion, said Patrick Martin of Procopio, Cory, Hargreaves & Savitch LLP. Information reporting can be very expensive for U.S. citizens living abroad and can expose them to substantial penalties, he added.

Residence-based taxation is often described as a territorial tax system for individuals. Switching to residence-based taxation would make Americans “more competitive in the international job market and free to pursue opportunities around the world,” according to a December 20 release from the group.

The bill effectively mirrors the group’s approach by excluding from U.S. taxation specified foreign-source income earned when a U.S. citizen is residing abroad, the release says. No revenue estimates were released with Holding’s proposal, but under contract with American Citizens Abroad, the District Economics Group has evaluated residence-based taxation for revenue neutrality.

H.R. 7358 provides that nonresident citizens can secure qualified nonresident citizen status by making an election, which would need to be done annually to certify they still satisfy the eligibility standards.

Under the bill, a nonresident citizen is defined as a U.S. citizen with a foreign tax home who has fully complied with U.S. income tax laws for the previous three years and meets one of two requirements:

- bona fide residency in a foreign country or countries for an uninterrupted period that captures a full tax year; or
- presence in a foreign country or countries during at least 330 full days during the tax year.

“American citizens abroad promote U.S. businesses, support U.S. exports, and represent U.S. interests throughout communities around the globe,” the bill summary states. “By leveling the competitive playing field, this bill will allow more Americans to enter into the global workforce, thus encouraging both domestic job growth and increased reliance on U.S. products and services in global operations.”

Holding and his staff have been working on the legislation since it became clear that residency-based taxation wouldn’t be part of the Tax Cuts and Jobs Act, according to American Citizens Abroad. Several practitioners have expressed doubt about the bill’s chances given U.S. expatriates’ lack of political power and the Republicans’ lost majority in the house.

The bill will take a considerable amount of buy-in from the House Ways and Means Committee and then the Senate Finance Committee, said Marsha-laine Dungog of Moodys Gartner Tax Law LLP. “Since both tax writing committees are bipartisan, there will be significant blocks to getting this passed,” she said.

However, the concept of residency-based taxation is not without support from proponents at both ends of the political spectrum, including Grover Norquist’s Americans for Tax Reform and Democrats Abroad. ■