

Expatriations Persist as FATCA Turns 10

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It's been almost a decade since the Foreign Account Tax Compliance Act was passed, but thousands of individuals are still renouncing their U.S. citizenship each year, a trend that practitioners don't see ending anytime soon.

Since FATCA's passage in March 2010 the number of expatriates reported by the Treasury Department has risen somewhat unsteadily, [reaching a quarterly peak of 2,364](#) in the fourth quarter of 2016. More than 5,400 individuals gave up their citizenship that year. The numbers have come down since then, with totals of over 5,100 in 2017 and almost 4,000 in 2018, but those are still much higher than in the years before FATCA's introduction.

"The demand is still very high," according to Alexander Marino of Moodys Gartner Tax Law LLP, who said he handles hundreds of renunciation cases per year. This is particularly true among U.S. citizens in Canada, Marino said. There are different wait times for citizenship renunciation at the U.S. embassy and consulates in Canada. In Toronto, the wait time is around 13 months, Marino said. The U.S. State Department's nonwaivable fee for processing a certificate of loss of nationality request is \$2,350.

"The turning over of more and more names under FATCA is driving more renunciations," Marino said. In 2019, approximately 900,000 bank records of Canadian residents were sent to the IRS, a spokesperson for the Canada Revenue Agency told *Tax Notes*. That number has increased every year since 2014, when the records numbered 150,000, the spokesperson confirmed.

Wealthy persons are renouncing their citizenship in droves, said Dianne Mehany of Caplin & Drysdale Chtd. "In my opinion, it will continue; it's the perfect storm of [an] unpopular administration, growing knowledge and awareness of what U.S. citizenship or long-term green card holder status means, as well as tax reform and its unintended and unfair impact on individuals living abroad," she said.

"I think what we have seen will probably continue as certain other dual citizens or accidental Americans are growing up and entering the workforce overseas," said Eva Farkas-DiNardo of Withers Bergman LLP. As dual citizens find they have difficulty opening bank accounts or filing U.S. tax returns, "I think there will always be a number of people that for this reason will want to renounce," she said.

Farkas-DiNardo said the idea that American residents are packing up and leaving isn't accurate; the individuals she's assisted with expatriation have all been long-term residents of other countries. "I haven't seen anyone leaving the U.S. who actually lives here," she said. "I don't think it's politically motivated in the vast majority of cases." It's usually motivated by difficulty with compliance, she added.

But Mehany said some high-net-worth individuals did move abroad in the wake of the 2016 presidential election “with perhaps a long-term intent to give up their citizenship, but more to try to test the waters. . . . I’ve only had a handful that have actually decided, ‘Yes, this is a lifetime choice for me and I’m going to relinquish my citizenship,’” she said.

Relief for Some Expats

In September, the IRS announced procedures to help some individuals who have relinquished their citizenship obtain relief from back taxes. The procedures are an “[extraordinary use of the commissioner’s enforcement discretion](#),” according to Daniel N. Price, an attorney with the IRS Office of Chief Counsel (Small Business/Self-Employed). “No tax, no penalties, no interest; it’s truly relief to the taxpayer,” Price said during an October 2019 panel discussion on the relief procedures. But some practitioners consider the scope of the procedures too narrow and don’t expect them to have a measurable effect on expatriations.

Relief from unpaid taxes under the procedures is available only to ex-citizens who have a net worth of under \$2 million and \$25,000 or less in aggregate tax liability for the year of expatriation and the prior five years. Any failure to pay taxes, file tax returns, or file foreign bank account reports must have been non-willful, and in such cases, the individual must have no filing history as a U.S. citizen or resident, according to IRS guidance. “The application of the new program is quite limited,” and the tax liability threshold over which it will not apply is low, Farkas-DiNardo said.

The thresholds for tax owed and net worth and the requirement that an expat have no filing history “unduly restrict the availability of this program to all high-net-worth individuals who may still be accidental Americans,” Mehany said.

“It’s wonderful in that you do not have to obtain a social security number — that is the best news — but it’s still expensive because you still have to engage a professional to prepare returns,” Mehany said. The IRS needs to get rid of the \$2 million net worth threshold and not require five years of prepared returns, Mehany said. “If you’re really targeting your middle-class accidental American, this is not enough relief.”

From the U.S. government’s perspective, U.S. citizenship-based taxation is “sort of a [public relations] nightmare with foreign governments,” Patrick Martin of Procopio, Cory, Hargreaves & Savitch LLP told *Tax Notes*. “I think that’s what drove the government’s policy, and I do think . . . it brings more awareness.” Also, for programs ranging from the relief for some former citizens to the offshore voluntary disclosure program to the streamlined procedures, “one of the absolute biggest goals of the government is to collect information, make no mistake about it,” Martin said.

“Does it encourage people to renounce? No, but I think it’s an olive branch to those who may be sort of caught in the crossfire,” Marino said of the relief procedures. “I think this is just them being kind.”

There has been some question in the tax community about whether individuals who were U.S. citizens at the time the relief procedures were announced can subsequently renounce their

citizenship and then take advantage of the procedures, which refer to "former" citizens. "The relief procedure guidance could be more clear for current citizens who otherwise meet the requirements set forth in the relief procedures — those who are otherwise eligible," Martin said.

A spokesperson with the IRS told *Tax Notes* in an email that "there is no cutoff date by which citizenship relinquishment must have taken place for an individual to be eligible for the Relief Procedures for Certain Former Citizens." Those procedures are available prospectively, so taxpayers can relinquish citizenship after the September 2019 announcement of the procedures and then take advantage of them if they satisfy the other eligibility criteria, the spokesperson said. "The IRS is offering these relief procedures without a specific termination date and will make an announcement prior to terminating the procedures," the spokesperson added.

While filing outstanding FBARs isn't required for eligibility, individuals who are eligible for the program and file late FBARs with their submissions won't be assessed FBAR penalties, Price said. "If you fail to file FBARs, the IRS may assert FBAR penalties if your submission is selected for examination," according to the procedures' FAQs.

But Martin was adamant that if the filing date for an FBAR has passed and an individual can't comply with the law in a timely manner, "all you're doing by filing late is running the risk that the government is going to come out and assess a penalty against you."

"The compliance community is a little bit divided on this . . . if the [IRS] is telling me that this is something that they would recommend, then we would do it," Marino said. "Is it really that onerous to give them what they want in reference to these late FBARs? No, it's not. I don't think that's an unreasonable expectation."

If an individual is denied admission to the program after submitting returns — possibly with Form 8938, "Statement of Specified Foreign Financial Assets" — penalties could be imposed if FBARs aren't correspondingly filed, or even if they are, Mehany said.

Too Soon for Wealth Tax Woes?

Early in 2019, economists Emmanuel Saez and Gabriel Zucman [estimated the effects of a wealth tax proposal](#) by Sen. Elizabeth Warren, D-Mass. In a [letter to Warren](#), they said the tax would raise roughly \$2.75 trillion in a 10-year budget window while affecting fewer than 0.1 percent of American households. Zucman has said the [United States is in a better position to implement a wealth tax](#) than European countries that have tried it. Expatriation isn't a convenient way to avoid taxes in the United States because it involves renouncing U.S. citizenship and a potential exit tax, according to Saez and Zucman's February 5, 2019, paper, "How would a progressive wealth tax work? Evidence from the economics literature."

But practitioners who spoke with *Tax Notes* said the wealth tax doesn't really come up in the context of expatriation conversations. "It's a long ways out if it will ever happen," Marino said. "I hope I don't get struck by lightning, but I certainly don't go around planning my day around it." Farkas-DiNardo also said her [clients haven't asked about giving up citizenship](#) in response to wealth tax proposals.

Pipeline of Expatriates and the Stubborn FBAR Gap

If the wealth tax isn't prompting people to consider renouncing their citizenship, and the IRS's relief procedures aren't expected to bolster interest, from where are the thousands of expats per year coming?

Thousands of people actually aren't that many, according to Martin. Compared with State Department estimates that somewhere around 9 million U.S. citizens live overseas, the number of people renouncing U.S. citizenship is a "tiny, tiny drop in the bucket," he said, especially considering that [many consider the State Department estimates to be conservative](#). Renunciations get "a lot of press, and it's thousands of people, but in the scheme of things — out of millions — that's a tiny, tiny fraction," Martin said.

Comparing the number of U.S. citizens living abroad with annual FBAR filings makes it seem that there's a sizable gap between the number of people with reportable foreign income and those actually reporting it, and some of the individuals in that gap may be among future populations of expatriates. According to the Financial Crimes Enforcement Network, FBAR filings topped 1 million in 2014 for the first time, and the number has risen every year since. There were 1,163,229 FBARs filed in 2015, and there were 1,322,323 through December 15, 2019, less than the number of U.S. citizens estimated to be residing in just Mexico.

Practitioners and IRS officials both have noted that a lack of awareness, income levels, and noncompliance account for much of the gap. There is a population of sophisticated individuals with access to U.S. tax lawyers and CPAs who know the rules and choose not to comply, Martin said. "They're living in Mexico City or Toronto or Johannesburg, Hong Kong, Costa Rica, Honduras." But a greater proportion "simply have no idea of the U.S. tax laws; they are clueless," Martin said. "That does not mean that the U.S. is losing a lot of tax dollars . . . they're not filing under the law as they're supposed to, but it's more of a 'no harm, no foul' category." The estate and gift tax area is where substantial amounts of money are probably going uncollected from high-net-worth individuals, Martin said.

While awareness about U.S. taxpayer obligations abroad has improved, there's "only a small percentage of the citizens overseas who really understand these rules," Martin said. There are numerous individuals who are still discovering what it means to be a U.S. citizen living abroad from a tax reporting perspective, he said. The IRS and Treasury have a misconception that U.S. tax law and FBAR rules are understood around the world, but "the idea that somehow most of these citizens overseas understand how the U.S. tax rules apply to them, it stretches the imagination," Martin said.

"I find it unreasonable that the IRS views FBAR knowledge with such a blanket approach and has such a high degree of skepticism with someone saying they didn't know," Mehany said. The average person working and living in Asia, Germany, or Latin America isn't necessarily finding out about FBAR requirements from the *Financial Times*, she said.

Often, the first notice a U.S. citizen abroad receives about U.S. reporting obligations comes from a bank, not the IRS. Someone goes to a bank and has to certify that they're not a U.S. person, Martin said. Sometimes a bank will tell a dual national that they can certify with their non-U.S. passport that they're not a U.S. person, "and they believe in good faith they're doing what's required of them," he said.

Mehany said she's had clients with businesses and bank accounts who didn't find out the U.S. tax implications until they tried to enter into a business transaction. "In the midst of the due diligence process, then it's raised," she said.

Those for whom renunciation makes sense are often from high-net-worth families who have created wealth over the long term in their country of residence and pass that wealth down generationally, Martin said, adding that estate and gift taxes are typically a bigger driver than other tax considerations. Very wealthy individuals figure they can renounce their citizenship and return to the country as needed with an investor visa, he said.

Individuals who live in politically stable places with high standards of living and job opportunities, like Canada, Australia, or the EU, may consider themselves to be holding onto U.S. citizenship for no good reason, said Farkas-DiNardo. Clients have said that "it's not really what they have to pay in taxes annually; it's really the fact that they have to comply with so many rules," she said. Having to hire U.S. accountants or lawyers to manage tax returns and other required forms "is really a deterrent for them," even if they're living in a country with higher taxes than in the United States, she said. There may be some high-net-worth individuals for whom the tax burden of remaining a U.S. citizen is an issue, but for many dual nationals, relinquishing citizenship doesn't really help them from a tax burden standpoint, she added.

"The vast majority of clients who relinquish U.S. citizenship either have no desire to ever enter our borders again or hold citizenship in a country that allows free access or has methods to expedite visas," Mehany said.

Susan Worm, an immigration attorney with the Law Offices of Jan Joseph Bejar, said she hasn't met anyone who gave up U.S. citizenship for a nontax reason. "I suppose some persons may relinquish for political or ideological reasons, but I have never encountered anyone in that category," she said.

"Obviously, tax is the lion's share of the issues going into an expatriation," Marino said. Understanding immigration rules is also critical, but there is a laundry list of other issues, like whether the expats can still own U.S. real estate, how often they can spend time in the United States, whether they can still collect Social Security or veterans benefits, what happens with Medicare and Medicaid — "what I call all the other life issues," Marino said. "Tax is the main driver in people renouncing U.S. citizenship, but along the way, you have to be careful you don't step on land mines, not only in tax, but beyond."

Immigration Consequences

The small percentage of expats abroad who relinquish U.S. citizenship each year is evidence that it's almost never advisable, according to some practitioners. There are very limited circumstances in which a person should consider giving up U.S. citizenship, Worm said. The person would have very few or no ties to the United States, would have no need to travel there, and would be living in a country that's politically and economically stable, Worm said. "From our perspective, it's a really severe decision to make," she added.

"Keep in mind that it's irrevocable," Worm said. Once an individual relinquishes U.S. citizenship

and is considered a noncitizen or alien from an immigration perspective, returning to the United States could be difficult. “You can’t just get the citizenship back,” she said.

One woman who recently relinquished citizenship had trouble getting a visitor visa because her spouse and children continued to live in the United States. “The consulate did not believe that she intended to return to her country after brief visits,” Worm said.

While many people inquire about the process, when people who live in countries with political instability and rampant violence are advised about the value of being able to come in and out of the United States freely, nontax reasons to keep one’s U.S. passport typically outweigh any tax implications or inconveniences that stem from keeping it, Martin said.

There’s also the Reed amendment, under which individuals who have renounced U.S. citizenship for tax reasons can be denied reentry. While a common refrain is that the amendment is not enforced, some practitioners say that’s an overgeneralization.

A [2003 Joint Committee on Taxation review](#) of immigration and the tax treatment of citizenship relinquishment noted that the Immigration and Naturalization Service and the State Department “have not denied reentry into the United States to a single former citizen” under the Reed amendment, which was part of the Illegal Immigration Reform and Immigrant Responsibility Act of 1996. “There is little or no enforcement of the special tax and immigration rules applicable to tax-motivated citizenship relinquishment and residency termination,” the JCT concluded.

But in 2016 the State Department found that [two applicants for non-immigrant visas](#) were ineligible on grounds that they were former citizens who had renounced citizenship to avoid taxation. “One applicant was able to overcome it, meaning that he or she convinced the Department of State that his or her purpose in renouncing citizenship was not avoiding taxation,” Worm said. In 2017 one person was found ineligible under the Reed amendment but was able to overcome that finding. No one was found ineligible under the Reed amendment in 2018.

There is a question on the current application for permanent resident status asking whether the applicant has “ever renounced U.S. citizenship to avoid being taxed by the United States.” Worm said that “even if you marked yes, I’m not sure they could legally take that into account, and I’ve never seen anyone mark yes on that question.”

“I think it’s definitely something to keep in mind and make sure that clients understand — that that is a real risk,” Farkas-DiNardo said of the Reed amendment.

Even if enforceable, some have said it’s easy to avoid. “Unless the renunciator specifically states his or her motive as tax reasons, then it is very difficult for the U.S. government to assert that avoiding taxes was the purpose behind expatriation,” Worm said.

“I always counsel my clients to not utter the word ‘tax’ in their exit interview unless it’s to say, ‘I am fully tax compliant,’” Mehany said.