

I.R.S. RELEASES RELIEF PROCEDURES FOR CERTAIN EXPATS WHILE WARNING BELLS RING FOR OTHERS

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The I.R.S. recently announced new procedures that will enable certain individuals to come into compliance with their U.S. tax and filing obligations in connection with the relinquishment of their U.S. citizenship. The newly announced Relief Procedures for Certain Former Citizens apply exclusively to individuals who relinquish their citizenship after March 18, 2010, the date the Foreign Account Tax Compliance Act (“F.A.T.C.A.”) was enacted, and who meet other criteria discussed below. The new procedures are a welcome relief that will eliminate back taxes and penalties to those eligible.

At the same time, the I.R.S. also announced that a program to temporarily suspend notifications to the U.S. State Department regarding some severely delinquent taxpayers working with the Taxpayer Advocate Service (“T.A.S.”) has come to an end.

BACKGROUND: THE CRY FOR HELP AND THE COVERED EXPATRIATE

Individuals born outside the U.S. to U.S. citizen parents (although they may lack even a U.S. passport) and those born in the U.S. to foreign parents (although they may have only lived in the U.S. for a few years, months, or even weeks) are U.S. citizens. And, yes, they are subject to the same tax and reporting obligations as those who live in the U.S. their entire lives. This information comes as a shock to many.

When these individuals grasp the gravity of their U.S. citizenship status, often after being ousted by their local bank for being U.S. citizens (thanks to F.A.T.C.A.), they may wish to renounce their U.S. citizenship. However, renouncing U.S. citizenship may not be possible without tax implications.

You may have read the story of U.K. Prime Minister and former Mayor of London Boris Johnson, who was born in the U.S. to foreign parents and has not lived in the U.S. since a very early age. He, purportedly, was surprised to receive a tax bill from the U.S. when he sold his home in London and, to avoid future tax liability, relinquished his U.S. citizenship (after paying the bill).

In addition to any prior tax obligations, when an individual relinquishes U.S. citizenship, an “exit tax”¹ may be imposed if the individual meets the definition of a “covered expatriate.”² Additionally, under the Code, “succession tax”³ may be imposed on gifts and bequests from covered expatriates.

¹ Code §877A.

² See “Pre-Immigration Income Tax Planning, Part II: Covered Expatriates,” *Insights* 4 (2015).

³ Code §2801.

The term “covered expatriate” notoriously applies to the rich (and the “near rich”) under one of two tests:

- An income tax liability test: average annual net income tax liability in the five years prior to the expatriation of \$124,000, adjusted to inflation (\$168,000 for 2019)
- A net worth test: net worth of \$2 million or more

However, the definition also applies to those who cannot certify under penalty of perjury on Form 8854, *Initial and Annual Expatriation Statement*, that they met all applicable tax requirements for the five preceding tax years. In other words, accidental Americans, whose U.S. tax obligation previously escaped their knowledge, may be subject to the exit tax and potentially succession tax notwithstanding that they may be far from wealthy. And, on top of that, they will owe back taxes for years that were not timely filed and are now filed in anticipation of an expatriation under the streamlined procedures or otherwise.

THE RELIEF PROCEDURES

The new procedures allow qualifying individuals who intend to relinquish their U.S. citizenship or who have relinquished their citizenship after F.A.T.C.A. was enacted (March 18, 2010) to comply with their U.S. tax and reporting obligations without paying any outstanding taxes, interest, and penalties and without being treated as covered expatriates.

It should be noted that the exit tax is paid by covered expatriates only if the deemed sale of worldwide assets on the day before expatriation results in a tax liability in excess of \$600,000, adjusted for inflation (*i.e.*, \$725,000 for 2019). Therefore, to most accidental Americans who had no knowledge of their U.S. tax obligation, the covered expatriate status is not as worrisome as the back taxes and late filing penalties they will face if they formally expatriate without these relief procedures.

What Does a Submission Under the Procedures Entail?

Individuals who wish to rely on the new procedures must first renounce their citizenship and ensure they have other citizenship. Following the renouncement of citizenship, taxpayers must submit to the I.R.S. proof of loss of nationality or of cancellation of the certificate of naturalization together with the following documents:

- Identification in the form of a copy of a valid passport or birth certificate and government-issued identification
- Dual-status tax return for the year of expatriation, including Form 1040-NR, *U.S. Non-Resident Alien Income Tax Return*; Form 8854, *Initial and Annual Expatriation Statement*; Form 1040, *U.S. Individual Income Tax Return*, reporting worldwide income up to date of expatriation; and any other required information return, including but not limited to Form 8938, *Statement of Specified Foreign Financial Assets*
- Form 1040, *U.S. Individual Income Tax Return*, for the five tax years preceding the expatriation and all applicable information returns for those years

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In a page dedicated to the new procedures, which includes frequently asked questions,⁴ the I.R.S. states in its answer to Question 18 that, while submission of delinquent F.B.A.R.'s is not required under the procedures, individuals who have an F.B.A.R. filing requirement should file. Eligible individuals who file F.B.A.R.'s before filing or contemporaneously file with their submission under the procedures will not be assessed F.B.A.R. penalties. Those who fail to file F.B.A.R.'s with or prior to their submission under the procedures may be assessed F.B.A.R. penalties (if their submission is selected for examination).

Eligible Individuals

The relief procedures apply to individuals who have not filed U.S. tax returns, either as U.S. citizens or residents. Any past compliance failure must have been non-willful. Non-willful conduct generally includes negligence, inadvertence or mistake, or good faith misunderstanding of the law's requirement. Additionally, eligible individuals must have a net worth of less than \$2 million and must owe a limited amount of back taxes. Specifically, to qualify, one must

- have relinquished his U.S. citizenship after March 18, 2010;
- not have any filing history as a U.S. citizen or resident (except if an individual has previously filed Form 1040-NR, *U.S. Non-Resident Alien Income Tax Return*, believing they were not in fact a U.S. citizen),
- have an average annual net income tax liability for the five taxable years prior to the expatriation that does not exceed the amount stated for the covered expatriate definition,
- have a net worth that is less than \$2 million at the time of expatriation and at the time of making the submission under these procedures,
- have an aggregate total tax liability of \$25,000 or less for the five tax years preceding expatriation and in the year of expatriation (after application of all applicable deductions, exclusions, exemptions and credits, including foreign tax credits but excluding any exit tax, penalties, and interest), and
- agree to complete and submit all required Federal tax returns for the six tax years at issue, including all required schedules and information returns.

If an individual makes a submission under this procedure without qualifying, the I.R.S. will process the returns “using normal processing procedures,” and the individual will be liable for all back taxes, interest, and penalties associated with those returns.

What About Green Card Holders?

In a webinar hosted by the I.R.S. last month, the I.R.S. stated that more guidance on its new tax relief procedures will address individuals who surrendered their green cards.⁵ Lara Banjanin from the Office of Associate Chief Counsel (International) said

⁴ [“Relief Procedures for Certain Former Citizens: Relief Procedures FAQs.”](#) I.R.S., last reviewed or updated October 24, 2019.

⁵ I.R.S., [“Relief Procedures for Certain Former Citizens.”](#) (webinar, October 10, 2019).

that it is anticipated that such additional guidance will address green card holders whose net worth is below \$2 million, whose income tax liability is below the threshold for a covered expatriate, and who has been compliant with U.S. tax obligations for the five years prior to expatriation.

How Long Are the Procedures Available?

There is no set termination date for these procedures. However, the I.R.S. will announce a closing date before the program's end. In the above-mentioned I.R.S. webinar, Daniel N. Price from the Office of Chief Counsel said that taxpayers should use the procedures "sooner rather than later."

EXPATRIATES AND PASSPORT REVOCATION

In December 2015, the Fixing America's Surface Transportation Act ("F.A.S.T. Act") was signed into law. Under the F.A.S.T. Act, the I.R.S. is required to notify the State Department of "taxpayers the IRS has certified as owing a seriously delinquent tax debt."⁶ This means "owing over \$52,000 in back taxes, penalties and interest for which the IRS has filed a Notice of Federal Tax Lien and the period to challenge it has expired or the IRS has issued a levy." Under the F.A.S.T. Act, the State Department is required to deny passport applications or renewals and, in some instances, revoke passports at the I.R.S.'s request. Over the life of this program, more than \$1 billion has been collected from individuals. As of May 2019, based on information published by the T.A.S., the I.R.S. sent out almost 389,000 certification notices to the State Department.

Following a T.A.S. request, the I.R.S. temporarily suspended passport certification procedures for those that had open cases with the T.A.S. However, in mid-October the I.R.S. announced that it will end its temporary suspension of notifications to the State Department for some severely delinquent tax debtors, stating that:

[The I.R.S. has] determined that a blanket, systemic exception for anyone with an open TAS case is overly broad and could undermine the effectiveness of the statute enacted by Congress in the FAST Act to collect a seriously delinquent tax debt.

However, as the I.R.S. points out, taxpayers still have opportunities to avoid certification to the State Department. This certification is not something that happens overnight. Taxpayers can also qualify for a relief program such as a payment agreement or an offer in compromise.

Additionally, in a recent statement, the I.R.S. said it will also not certify a taxpayer to the State Department or will reverse a certification under any of the circumstances below:

- The taxpayer is in bankruptcy
- The taxpayer is identified by the I.R.S. as a victim of tax-related identity theft
- The I.R.S. has determined the taxpayer's account is currently not collectible due to hardship

⁶ I.R.S., "[Update on Passport Certifications and Taxpayer Advocate Service.](#)" news release, October 16, 2019.

- The taxpayer is located within a Federal disaster area
- The taxpayer has a request pending with the I.R.S. for a good faith installment agreement
- The taxpayer has a pending good faith offer in compromise with the I.R.S.
- The taxpayer has an I.R.S.-accepted adjustment that will satisfy the debt in full

CONCLUSION

The relief procedure for certain citizens is considered very taxpayer-friendly and can be a great opportunity for individuals needing to come into tax compliance in order to relinquish their U.S. citizenship. Individuals most likely to qualify and utilize the procedures are those who have lived outside the U.S. for most of their lives, and may not have been aware of tax obligations here in the U.S., and whose net worth and tax liabilities are of (very) limited amounts. Those who do not qualify may come into compliance using the existing offshore and domestic streamlined procedure.

It is interesting to see that at the same time the I.R.S. released a relief procedure they also announced an end to their temporary suspension of State Department certifications under the F.A.S.T. Act. As a result, severely delinquent tax debtors may not be able to get a new U.S. passport (or to renew an existing one). And those with current U.S. passports could find them revoked.

