

Proposal to Save American Citizenship

This document contains a list of the most significant proposed changes to specific legislative provisions whose purpose is to save American citizenship. The changes would move the United States from a worldwide income tax system based both on residence and on citizenship to one based only on residence. The objective is to permit U.S. citizens living outside the United States (who are tax residents of other countries) to opt to sever U.S. tax residency without being required to relinquish U.S. citizenship, while allowing those who wish to remain subject to the existing citizenship-based system to do so. Generally, those who sever tax residency with the United States would be taxable by the United States on only their U.S. sourced income. With this proposal, the United States would stop taxing the non-U.S. source income of persons who do not live in the United States (except for those who opt to remain in the current system).

For further explanation of the context see the following post written by John Richardson: <http://citizenshipsolutions.ca/2021/07/09/take-1-digging-the-foundation-to-build-the-house-of-us-residency-based-taxation/>.

Note that these legislative changes will need to be accompanied by corresponding regulatory changes. We are currently working on amending this proposal to also include those changes.

Questions and comments about this proposal should be directed to Laura Snyder (laura@seatnow.org) and John Richardson (john@seatnow.org).

I. Only Residents Are Subject to Worldwide Income Taxation

26 U.S. Code § 1 – Tax imposed

The objective is to change the scope of application of worldwide taxation from “individual” (everyone on the planet) to “resident” (persons living in the United States, regardless of citizenship). This is done by changing the word “individual” to the word “resident.”

(A) MARRIED ~~INDIVIDUALS~~ RESIDENTS FILING JOINT RETURNS AND SURVIVING SPOUSES

There is hereby imposed on the taxable income of—

(1) every married ~~individual~~ resident (as defined in section 7703) who makes a single return jointly with his spouse under section 6013, and

(2) every surviving spouse (as defined in section 2(a)),
a tax determined in accordance with the following table [...]

(B) HEADS OF HOUSEHOLDS

There is hereby imposed on the taxable income of every head of a household (as defined in section 2(b)) a tax determined in accordance with the following table [...]

(C) UNMARRIED ~~INDIVIDUALS RESIDENTS~~ (OTHER THAN SURVIVING SPOUSES AND HEADS OF HOUSEHOLDS)

There is hereby imposed on the taxable income of every ~~individual~~ resident (other than a surviving spouse as defined in section 2(a) or the head of a household as defined in section 2(b)) who is not a married ~~individual resident~~ (as defined in section 7703) a tax determined in accordance with the following table [...]

(d) Married ~~individuals residents~~ filing separate returns

There is hereby imposed on the taxable income of every married ~~individual resident~~ (as defined in section 7703) who does not make a single return jointly with his spouse under section 6013, a tax determined in accordance with the following table [...]

II. Nonresidents Are Not Subject to Worldwide Taxation but Only Taxation on Their U.S. Source Income

26 U.S. Code § 2 – Definitions and special rules

The objective is to exempt nonresidents (persons living outside the United States, regardless of citizenship) from worldwide taxation. They would continue to be taxable on their U.S. source income. This is done by changing the clause “nonresident alien” to just the word “nonresident.”

(b) DEFINITION OF HEAD OF HOUSEHOLD

(3) LIMITATIONS

Notwithstanding paragraph (1), for purposes of this subtitle a taxpayer shall not be considered to be a head of a household—

(A) if at any time during the taxable year he is a nonresident ~~alien~~; or

[...]

(b) NONRESIDENTS ~~ALIENS~~

In the case of a nonresident ~~alien~~ individual, the taxes imposed by sections 1 and 55 shall apply only as provided by section 871 or 877.

III. The Difference Between Resident and Nonresident (How Does A Nonresident Become A Resident)

26 U.S. Code § 7701 – Definitions

The objective is to mostly sever citizenship from the determination of who is a resident and who is a non-resident.

Note that pursuant to § 7701(b)(11) the Secretary of the Treasury shall prescribe such regulations as necessary to carry out the purposes of this subsection. We suggest using Canada’s rules/regulations as a model for deciding who should be treated as being “ordinarily resident”. (We propose regulations (like the [Canada Revenue Agency folio](#)) for what constitutes “ordinary residence”. In [Canada tax residency is defined largely by “ordinary residence”](#) – a concept that is very sticky).

(b) DEFINITION OF RESIDENT ~~ALIEN~~ AND NONRESIDENT ~~ALIEN~~

(1) In general

For purposes of this Title (other than subtitle B) —

(A) Resident ~~alien~~

An individual shall be treated as a resident of the United States with respect to any calendar year if (and only if) such individual meets the requirements of clause (i), (ii), ~~or~~ (iii) ~~or~~ (iv):

(i) Lawfully admitted for permanent residence

Such individual is a lawful permanent resident of the United States at any time during such calendar year.

(ii) Substantial presence test

Such individual meets the substantial presence test of paragraph (3).

(iii) First year election

Such individual makes the election provided in paragraph (4).

(iv) Ordinary residence

Such individual’s ordinary residence is the United States. For the purposes of this clause, “ordinary residence” means the place where, in the settled routine of an individual’s life, the individual regularly, normally, or customarily lives. If an individual who is a U.S. citizen does not have ordinary residence in another country, that individual’s ordinary residence shall be deemed to be the United States.

(B) Nonresident ~~alien~~

An individual is a nonresident ~~alien~~ if such individual is ~~neither a citizen of the United States nor~~ not a resident of the United States (within the meaning of subparagraph (A)).

[...]

(4) First-year election

(A) ~~An alien~~ A nonresident individual shall be deemed to meet the requirements of this subparagraph if such individual— [to be determined]

IV. Other Definitional Changes

26 U.S. Code § 7701 - Definitions

The objectives are to amend (§ 7701(a)(30)) to ensure that “citizenship” is not a sufficient condition for “residency”. Generally: (I) to ensure that only residents are subject to “worldwide taxation; (ii) (i) to ensure only those who are U.S. tax “residents” are subject to information reporting requirements respecting “foreign entities” (including FATCA) ; and (iii) clarify when the status of an individual changes from resident to nonresident (§ 7701(l)(50)).

(a)

(30) UNITED STATES PERSON

The term “United States person” means—

(A) a ~~citizen or~~ resident of the United States as defined by section 7701(b) [...]

(1)

(50) TERMINATION OF UNITED STATES ~~CITIZENSHIP~~ RESIDENCE

(A) In general

An individual shall not cease to be treated as a United States ~~citizen~~ resident before the date on which the individual’s ~~citizenship~~ residence is treated as relinquished under section 877A(g)(4).

[...]

V. Relinquishment of Residence

26 U.S. Code § 877 – Expatriation to avoid tax

The objective is to index for inflation – both since 2004 and on an ongoing basis – the amount of individual net worth with which a person qualifies as a covered expatriate. (This amount originated in the American Jobs Creation Act of 2004, Pub. L. No. 108-357 §804, 118 Stat. at 1569).

(a)

(2) INDIVIDUALS SUBJECT TO THIS SECTION

This section shall apply to any individual who is a “covered expatriate”. For the purposes of this section an individual is a “covered expatriate” if—

(A) the average annual net income tax (as defined in section 38(c)(1)) of such individual for the period of 5 taxable years ending before the date of the loss of United States citizenship is greater than ~~\$124,000~~**\$178,000**,

(B) the net worth of the individual as of such date is ~~\$2,000,000~~ **\$3,500,000** or more, or

(C) such individual fails to certify under penalty of perjury that he has met the requirements of this title for the 5 preceding taxable years or fails to submit such evidence of such compliance as the Secretary may require.

In the case of the loss of United States citizenship in any calendar year after ~~2004~~**2022**, such ~~\$124,000~~**\$178,000** and ~~\$3,500,000~~ amounts shall be increased by an amount equal to such dollar amount multiplied by the cost-of-living adjustment determined under section 1(f)(3) for such calendar year by substituting “~~2003~~**2021**” for “1992” in subparagraph (B) thereof. Any increase under the preceding sentence shall be rounded to the nearest multiple of \$1,000.

26 U.S. Code § 877A – Tax responsibilities of expatriation

The objectives are: (i) to change from an expatriation tax imposed at the time of relinquishment of U.S. citizenship to a departure tax imposed at the time an individual ceases to be a resident, and (ii) to exempt certain types of assets from the departure tax. Note that, subsequent to departure, the United States retains primary taxing rights over many assets (for example, principal residence).

(c) ~~EXCEPTION FOR CERTAIN PROPERTY~~ PROPERTY NOT SUBJECT TO EXIT TAX

Subsection (a) shall not apply to—

(1) any deferred compensation item (as defined in subsection (d)~~(4)~~),

(2) any specified tax deferred account (as defined in subsection (e)~~(2)~~), ~~and~~

~~(3) any interest in a nongrantor trust (as defined in subsection (f)(3)).~~

~~(3) a foreign retirement arrangement, superannuation, pension fund, employee benefit plan, or other foreign plan or arrangement, whether established under the laws of a foreign country or established under a contractual arrangement governed under the laws of a foreign country,~~

~~(4) Social Security or equivalent program established under the laws of a foreign country,~~

~~(5) cash (including bank deposits),~~

~~(6) real or immovable property situated in the United States, its territories, or possessions,~~

~~(7) any residential real estate, wherever located, that is or has been a principal residence (as defined in § 121) in the three years prior to the year of ending residency, and~~

~~(8) capital property used in, or property described in the inventory of, a business carried on by the covered expatriate through a permanent establishment (as defined by regulation) in the United States at the time of departure.~~

[...]

(d) ~~TREATMENT~~ DEFINITION OF DEFERRED COMPENSATION ITEMS

~~(1) Withholding on eligible deferred compensation items~~

~~(A) In general~~

~~In the case of any eligible deferred compensation item, the payor shall deduct and withhold from any taxable payment to a covered expatriate with respect to such item a tax equal to 30 percent thereof.~~

~~(B) Taxable payment~~

~~For purposes of subparagraph (A), the term “taxable payment” means with respect to a covered expatriate any payment to the extent it would be includible in the gross income of the covered expatriate if such expatriate continued to be subject to tax as a citizen or resident of the United~~

~~States. A deferred compensation item shall be taken into account as a payment under the preceding sentence when such item would be so includible.~~

~~(2) Other deferred compensation items~~

~~In the case of any deferred compensation item which is not an eligible deferred compensation item—~~

~~(A)~~

~~(i) with respect to any deferred compensation item to which clause (ii) does not apply, an amount equal to the present value of the covered expatriate's accrued benefit shall be treated as having been received by such individual on the day before the expatriation date as a distribution under the plan, and~~

~~(ii) with respect to any deferred compensation item referred to in paragraph (4)(D), the rights of the covered expatriate to such item shall be treated as becoming transferable and not subject to a substantial risk of forfeiture on the day before the expatriation date,~~

~~(B) no early distribution tax shall apply by reason of such treatment, and~~

~~(C) appropriate adjustments shall be made to subsequent distributions from the plan to reflect such treatment.~~

~~(3) Eligible deferred compensation items~~

~~For purposes of this subsection, the term “eligible deferred compensation item” means any deferred compensation item with respect to which—~~

~~(A) the payor of such item is—~~

~~(i) a United States person, or~~

~~(ii) a person who is not a United States person but who elects to be treated as a United States person for purposes of paragraph (1) and meets such requirements as the Secretary may provide to ensure that the payor will meet the requirements of paragraph (1), and~~

~~(B) the covered expatriate—~~

~~(i) notifies the payor of his status as a covered expatriate, and~~

~~(ii) makes an irrevocable waiver of any right to claim any reduction under any treaty with the United States in withholding on such item.~~

~~(4) Deferred compensation item~~

For purposes of this subsection, the term “deferred compensation item” means—

- (A) any interest in a plan or arrangement described in section 219(g)(5),
- (B) any interest in a foreign pension plan or similar retirement arrangement or program,
- (C) any item of deferred compensation, and
- (D) any property, or right to property, which the individual is entitled to receive in connection with the performance of services to the extent not previously taken into account under section 83 or in accordance with section 83.

~~(5) Exception~~

~~Paragraphs (1) and (2) shall not apply to any deferred compensation item to the extent attributable to services performed outside the United States while the covered expatriate was not a citizen or resident of the United States.~~

~~(6) Special rules~~

~~(A) Application of withholding rules~~

~~Rules similar to the rules of subchapter B of chapter 3 shall apply for purposes of this subsection.~~

~~(B) Application of tax~~

~~Any item subject to the withholding tax imposed under paragraph (1) shall be subject to tax under section 871.~~

~~(C) Coordination with other withholding requirements~~

~~Any item subject to withholding under paragraph (1) shall not be subject to withholding under section 1441 or chapter 24.~~

(e) TREATMENT DEFINITION OF SPECIFIED TAX DEFERRED ACCOUNTS

~~(1) Account treated as distributed~~

~~In the case of any interest in a specified tax deferred account held by a covered expatriate on the day before the expatriation date—~~

~~(A) the covered expatriate shall be treated as receiving a distribution of his entire interest in such account on the day before the expatriation date,~~

~~(B) no early distribution tax shall apply by reason of such treatment, and~~

~~(C) appropriate adjustments shall be made to subsequent distributions from the account to reflect such treatment.~~

~~(2) Specified tax deferred account~~

~~For purposes of paragraph (1),~~ The term “specified tax deferred account” means an individual retirement plan (as defined in section 7701(a)(37)) other than any arrangement described in subsection (k) or (p) of section 408, a qualified tuition program (as defined in section 529), a qualified ABLE program (as defined in section 529A), a Coverdell education savings account (as defined in section 530), a health savings account (as defined in section 223), and an Archer MSA (as defined in section 220).

[...]

(g) DEFINITIONS AND SPECIAL RULES RELATING TO EXPATRIATION

For purposes of this section—

(1) COVERED EXPATRIATE

(A) In general

The term “covered expatriate” means an expatriate who meets the requirements of subparagraph (A), (B), or (C) of section 877(a)(2).

(B) Exceptions

An individual shall not be treated as meeting the requirements of subparagraph (A) or (B) of section 877(a)(2) if—

(i) ~~the individual—~~

~~(I) became at birth a citizen of the United States and a citizen of another country and, as of the expatriation date, continues to be a citizen of, and is taxed as a resident of, such other country, and~~

~~(II) has been a resident of the United States (as defined in section 7701(b)(1)(A)(ii)) for not more than 10 taxable years during the 15 taxable year period ending with the taxable year during which the expatriation date occurs, or~~

~~(ii)~~

(I) the individual’s relinquishment of United States ~~citizenship~~ residence occurs before such individual attains age 18½, and

(II) the individual has been a resident of the United States (as so defined) for not more than 10 taxable years before the date of relinquishment.

(C) Covered expatriates also subject to tax as ~~citizens or~~ residents

In the case of any covered expatriate who is subject to tax as a ~~citizen or~~ resident of the United States for any period beginning after the expatriation date, such individual shall not be treated as a covered expatriate during such period for purposes of subsections (d)(1) and (f) and section 2801.

(2) EXPATRIATE

The term “expatriate” means—

~~(A) any United States citizen who relinquishes his citizenship~~ resident, within the meaning of section 7701(b), who has been a resident for at least eight of the fifteen years prior to the year of relinquishment of residency who relinquishes their residence, except that a lawful permanent resident of the United States (within the meaning of section 7701(b)(6)) is to be treated as an “expatriate” only if he is a “long term resident” as defined in 877(e).

~~(B) in the case of a long-term resident of the United States, the date on which the individual ceases to be a lawful permanent resident of the United States (within the meaning of section 7701(b)(6)).~~

(3) EXPATRIATION DATE

The term “expatriation date” means—

(A) the date an ~~individual~~ expatriate, who is not a lawful permanent resident, relinquishes United States ~~citizenship~~ residence, or

(B) in the case of a ~~lawful permanent resident, who is a~~ long-term resident of the United States, the date on which the individual ceases to be a lawful permanent resident of the United States (within the meaning of section 7701(b)(6)).

(4) Relinquishment of ~~citizenship~~ residence

~~A citizen shall be treated as relinquishing his United States citizenship on the earliest of—~~

~~(A) the date the individual renounces his United States nationality before a diplomatic or consular officer of the United States pursuant to paragraph (5) of section 349(a) of the Immigration and Nationality Act (8 U.S.C. 1481(a)(5));~~

~~(B) the date the individual furnishes to the United States Department of State a signed statement of voluntary relinquishment of United States nationality confirming the performance of an act of expatriation specified in paragraph (1), (2), (3), or (4) of section 349(a) of the Immigration and Nationality Act (8 U.S.C. 1481(a)(1)–(4));~~

~~(C) the date the United States Department of State issues to the individual a certificate of loss of nationality; or~~

~~(D) the date a court of the United States cancels a naturalized citizen's certificate of naturalization.~~

~~Subparagraph (A) or (B) shall not apply to any individual unless the renunciation or voluntary relinquishment is subsequently approved by the issuance to the individual of a certificate of loss of nationality by the United States Department of State.~~

(A) A resident who is not a lawful permanent resident of the United States, shall be treated as relinquishing his United States residence on the date that the resident certifies under penalties of perjury, on a form prescribed by the Secretary that he:

- (i) no longer meets the "residency requirements" set forth in section 7701(b); and
- (ii) has established tax residency in another country.

(B) A lawful permanent resident of the United States, who is not a long term resident, shall be treated as relinquishing his residence on the date that the resident certifies under penalties of perjury, on a form prescribed by the Secretary that he:

- (i) no longer meets the "residency requirements" in section 7701(b); and
- (ii) has established tax residency in another country.

(C) The date that a lawful permanent resident, who is a long-term resident, ceases to be a "lawful permanent resident" within the meaning of of 7701(b)(6).

(5) LONG-TERM RESIDENT

The term "long-term resident" has the meaning given to such term by section 877(e)(2).

VI. Living Abroad Without Relinquishing U.S. Residence

26 U.S. Code § 911 – ~~Citizens or r~~Residents of the United States living abroad

The objective is to allow those who wish to do so to remain subject to the current citizenship-based tax system, as long as they do not sever tax residency.

(d) DEFINITIONS AND SPECIAL RULES

For purposes of this section—

(1) QUALIFIED INDIVIDUAL

The term “qualified individual” means an individual whose tax home is in a foreign country and who is—

(A) a ~~citizen~~ resident of the United States and establishes to the satisfaction of the Secretary that he has been a bona fide resident of a foreign country or countries for an uninterrupted period which includes an entire taxable year, or

(B) a ~~citizen or~~ resident of the United States and who, during any period of 12 consecutive months, is present in a foreign country or countries during at least 330 full days in such period.