An Overview of the US Exit Tax: Full Transcript

Our main expert was John Richardson, a Toronto-based lawyer with Citizenship Solutions, a boutique firm offering life planning, investment solutions, citizenship and Green Card expatriation, US tax assistance and citizenship solutions in a FATCA world.

Introductory Remarks

MATEO JARRIN: Welcome to TaxLinked's latest webinar. Today we have -- this is basically part of a series of webinars we're doing on US tax issues. We had a first one maybe several months ago with John Richardson and he was accompanied by Karen Alpert from a university in Australia which touched upon the Transition Tax. Today we're doing a follow-up, we're going to touch up on the Exit Tax. And hopefully sometime in early 2019 will do something on GILTI to kind of wrap up the series of US-themed tax webinars.

So before getting started with our 12 questions, let me get some admin issues out of the way. This webinar is being recorded. We'll have an audio recording available for you probably early next week. We will also have a transcript, that'll take us a bit longer to get out to you but we'll share it on social media, send you an e-mail about it, etcetera.

If you have any questions for John as you listen in to what he has to say, use the GoToWebinar Control Panel to submit those questions, I will try to incorporate them as they come in, into the discussion. Also if you want to receive CPD credits for this webinar, make sure you're paying attention. Our system can track everything, so if you're not paying attention and it shows that you have logged on but you weren't actually being attentive then we will not offer you those CPD credits. So just make sure you're participating at least passively in the discussion we're having today.

So without further ado, I would like to hand on the floor to John to introduce himself and we'll get started with our questions. John?

JOHN RICHARDSON: Great! Thanks, Mateo. As Mateo pointed out, this is not the first I'm on a webinar with Taxlinked. My name is John Richardson. I am based in Toronto, Canada. I am a lawyer and I run a very very narrow specialty law practice, which is designed to help US citizens and green card holders who live outside the United States deal with the avalanche -- and I emphasize -- avalanche of problems that follow them because of their status as tax residents of the United States.

I was really quite interested to hear Mateo's introduction because -- as he points out -- in April, Karen Alpert and I did a webinar on the Transition Tax. Today we're doing the Exit Tax, and I'm looking forward to doing the GILTI provisions later. What's important to understand is that these three taxes have one very important thing in common, and what they have in common is that in each of these cases, whether it's transition tax, whether it's exit tax, or whether it's GILTI -- all three of these things are what I would call fictitious tax events created by the US Internal Revenue Code to generate taxable income for the United States that is overwhelmingly -- and exclusively in the cases of GILTI and transition tax -- and overwhelmingly in the case of the exit tax, a way to essentially confiscate foreign assets, assets in other countries.

And make no mistake about it, the 877a exit tax in the Internal Revenue Code, which has been a law since 2008, regardless of intent, operates primarily in relation to Americans abroad who renounce US citizenship or green card holders who hand in their green cards. And in the case of

Americans abroad, especially, what this means is the exit tax is applied to non-US assets, but more significantly that have been accumulated at a time when these people did not even live in the United States.

And that is why the 877a exit tax is so completely different from the exit taxes levied by other countries. They call them departure taxes in other countries that are levied when people pay as tax residents. But the point is that in Canada and in Australia, what happens is that these departure taxes are imposed at the time that they leave Canada or Australia. But as a practical matter for Americans abroad, they have left the United States -- in many cases a lifetime outside of the United States. So these, for all practical purposes, are taxes that -- and this is incredible -- are imposed on non-US assets that were accumulated when the individual was not even an actual resident of United States.

I mean this goes so far beyond any exit or departure tax that's ever been levied in the history of the world. It's astounding. No doubt the United States will be proud of this. Questions, Mateo?

MATEO JARRIN: Thank you for that introduction. We know where you stand John, very clearly, following that introduction.

JOHN RICHARDSON: I think that it's important.

MATEO JARRIN: Yes. To establish your ground and your point of view. That's good to get it out of the way from the beginning. So we have 12 questions here, John. Some of them are more complicated than others, some of them are more I guess, specific than others. Now let's get started with some of the more general questions.

So which people renouncing their US citizenship are subject to the exit tax? Just to kind of get us get started with that.

Question 1: Which people renouncing their US citizenship are subject to the exit tax?

JOHN RICHARDSON: Right. So not everybody. Not everybody. People who are subject to the exit acts are people who are defined in the Internal Revenue Code as covered expatriates. Now, a covered expatriate is a person who triggers one of these three wires. The first would be that person has had an average US tax liability of -- as of today's date is I believe $165,000 per year over the last five years. So an average US tax liability that's not income tax.

And most people in my experience are not part of that because most people live in countries that also impose tax, like Canada or Australia for example. And the taxes they pay in Canada or Australia are used as tax credits against US tax owing, meaning they tend to not owe that kind of tax. However, people in Saudi Arabia, Dubai, that have no income tax imposed by those countries, may be in danger. Interestingly though, it tells you a lot about philosophical underpinnings of the exit tax because by making somebody a covered expatriate -- because of a high US tax liability, it really means that the United States views the people that renounce US citizenship for tax reasons. And they really don't care if you renounce, what they care about is the tax revenue they lose. So that's the first test.

The second test is an asset test. By the way the first test, $165,000 is indexed to inflation -- I believe for 2019 it's $168,000. One would expect though for somebody with that kind of tax liability would have a lot in the way of assets. And what's interesting is --

MATEO JARRIN: Let me jump in, John, one second because I have a question here. Just for clarification basically: When you say a $165,000 in US tax, is that paid per year or is it not $165,000 in assessable income? That's the question we're getting from one of our listeners.

JOHN RICHARDSON: Right. Okay, good question. It has nothing to do with income. It has to do with actual tax paid to the United States -- actual tax paid to the United States, it's a somewhat nuanced test, okay? And it's an average over the five years and that's often very much confused. So it's a tax liability test, not an income test.

MATEO JARRIN: Okay, go ahead with a second test now. Sorry, I interrupted you there.

JOHN RICHARDSON: So the second test is based on assets. Now, one would think that if you were paying that kind of US tax, that you would have a lot in the way of assets. So one would expect a very high asset level triggered the exit tax. Wrong, wrong, wrong. The figure of 2 million US dollars -- assets less liabilities -- 2 million US dollars.

Now, that's not indexed to inflation either. That might sound like a humungous figure to somebody who lives in Middle America in a small town. For anybody who owns a house in any major city of the world, including US cities -- New York, Boston, in Canada -- Toronto, Vancouver, London, etcetera. I mean a house can easily cost over a million dollars.

And people like that, I mean, they can often be covered expatriates just because they happen to live in a certain area and that they bought a house 50 years ago. That's what the house is worth. Add to that a salaried employee with a pension plan at, say, Canada, my example is a University of Toronto professor who owns a house near the University of Toronto in downtown Toronto

and has a University of Toronto pension. I guarantee you, you have over two million in assets in there -- covered expatriate. I also guarantee you that their incomes may not be that high and many of them probably have trouble paying their bills. You know on a cash flow basis. So it's quite an amazing thing.

So that's the asset test and I might pause here and ask if there are any questions about the asset thing. I think it's very clear.

MATEO JARRIN: Let me see. Yes, there is a question about the assets. Do assets include equities of private companies?

JOHN RICHARDSON: Oh absolutely, positively. Absolutely. Assets means everything under the sun. There are some tax preparers when they complete the Form 8854 that even detail, I think, trivial personal possessions. I would not go that far. It does include in its plain terms, things like the value of personal use automobiles, stuff like that. So it goes way beyond investment assets.

Now practically speaking, okay, although it does go beyond that -- I mean you're concerned with financial assets that appears as part of your tax filing for year after year. The answer is absolutely yes. Let me put it another way. If there's a word to describe it in the English language, it is included as part of the asset test. Actually no, there are a couple exceptions -- social security in another country should not be included as an asset. Thank God.

Third. You have to also certify that you were compliant with the obligations imposed by Title 26, which is the Internal Revenue Code of US Law for the five years prior to the expatriation. And that includes paying all taxes, completing all forms, etcetera, etcetera. And this is a very big problem for people because nobody understands US taxes very well. And almost all people have issues -- their tax returns could be improved, etcetera.

So, you know, this becomes a concern. I mean, have they filed all of the right types of information return, etcetera? So that's the third test. If you can't certify five years, then you're also going to be a covered expatriate. And what that means is the people who just renounce US citizenship without having filing taxes are by definition covered expatriates. That's the test. Definitely one of those three, there are a couple exceptions. Do you want to hear the exceptions, or not?

MATEO JARRIN: Sure, go ahead. Let's cover the exceptions too, and let me actually combine it with the next question. Just so we could move ahead too. It's like, how can you avoid becoming covered expatriate?

Question 2: How can you avoid becoming covered expatriate?

JOHN RICHARDSON: Okay. Well, there's three ways to avoid becoming a covered expatriate because there's three ways you can be a covered expatriate.

The first would be -- obviously, make certain that you're not paying that kind of US tax. Now, one point I would make here is that a lot of people file jointly, and it's the amount that appears in the

joint return that would be used to calculate the US tax liability. So for a practical purpose, for some people they want to separate -- no longer file jointly. If they file as individuals, they can reduce their tax liability.

You know, other ways would be -- so how else do you reduce your tax liability? Maybe you stop working. Why not? I mean, you make less money. Now we did a seminar on the transition tax last, I guess, it was April. For somebody with a couple million dollars in retained earnings, they're going to have a transition tax that's so high that their average tax liability could be over $165,000. So anyway, you want to reduce the tax somehow.

Secondly, gifting. You want to get below that 2 million. Now, the general sort of textbook if you read about this -- say, well we make gifts to get below our 2 million.

As you know, the tax cuts and jobs act -- the gifting limitations now up to 11 million. And that gives a lot of room for a lot of people to get below 2 million. Who do make gifts to? Well, one obvious would be the non-US citizen spouse that you maybe give, you have to file your tax return, though. That's a possibility. And that's part of what expatriation planning is.

A third way to avoid the covered expatriate status would be, if you're not tax compliant or if your taxes are in bad shape, get it cleaned up. Do some back filing, that sort of thing.

Now there are two kinds of people, regardless of net worth, who would not be subject to the exit tax provided that they are tax compliant. The first group, I see a lot of this, living in Canada, would be those who are dual citizens at birth. So people who were, for example, a dual Canada/US citizen from birth, living in Canada, is a tax resident of Canada when they renounce, and has not lived in the US for the last 15 years would be able to escape the exit tax. They would not be covered expatriates.

And this is unbelievably arbitrary because let's compare two situations. Let's compare a person who was born in the United States to Canadian parents and was therefore a dual Canada/US citizen from birth. Let's say that person files hundreds of millions of dollars in assets -- hundreds of millions of dollars, decides that because of the US estate tax, he wants to get out of the United States. Well, all that person really has to do is renounce his citizenship, move right back to Canada, live there for 10 years as a tax resident, make sure he is compliant with his taxes, and he will avoid the exit tax.

Compare that to a person born in the United States to American parents then, say, moved to Canada as a kid. Let's say that person compiles hundreds of millions of dollars of assets. That person is stuck, will have to pay the exit tax, is not entitled to dual citizenship exemption, because he didn't have Canadian citizenship at birth.

So Barack Obama once said that in America, the circumstances do not determine the outcome of your life. The truth is that when it comes to the exit tax, not only are the circumstances of your birth, but the circumstances of your parents' birth can likely determine whether you have to pay the exit tax. It's incredibly arbitrary.

So that's one. And the second would be the people who can renounce before the age of 18-and-a-half. And again, they should be compliant, as well.

MATEO JARRIN: Okay. Before we move on, John, I guess you have people enthralled here because they're just dropping questions left and right. So let me backtrack a bit here and ask some of these questions that are coming in. This is going back to, I think, the third test that you answered in the first question. Is the total assets -- cash, equities, et cetera combined at any time over the past five years?

JOHN RICHARDSON: The 2-million-dollar test? No. So it's right at the point of renunciation. On the day of renunciation. So if you have clients, or whoever is listening, if you have clients, or if you're an individual, who's concerned with the 2-million-dollar test. Key point is the date of actual renunciation. So that means that any adjustments need to be done before you renounce. And I can tell you what I encourage people to do. Actually, I insist as gently as I can, is on the day they renounce, they have got to itemize all of these values of all of these things along with the exchange rate. Because don't forget that all of these things need to be converted to US dollars.

MATEO JARRIN: And this is either US-based or foreign-based, right? That's a second question to it, or second addendum to it.

JOHN RICHARDSON: The world view of the United States and the Internal Revenue Code is that every individual and every asset in the world is subject to US taxation, unless there's an exception to it. Okay? And to be very, very, very clear, it is all assets in the world. They are sucked into the vortex of this, I guess, social security would be the exception. And this is the problem. Because it primarily affects assets that were accumulated by American citizens after they moved from the United States.

MATEO JARRIN: Okay. The next question we received here -- regarding the average US tax liability per year, for how many years are they considering this average?

JOHN RICHARDSON: Five years prior to expatriation. So if you renounce next week and say this is what -- 2018, it would be the average liability for 13, 14, 15, 16, 17.

MATEO JARRIN: Okay. And last but not least, and then we'll move on to the questions that we have here. Could you do a gift to a foreign foundation in order to decrease your tax liability, and whatnot?

JOHN RICHARDSON: I don't see any reason why not. I mean, I've never thought about that specifically and I have no experience with that. So I will give you what I think is the answer, but of course, I can't guarantee it's the answer. I see no reason why you could not do that. Remember though, that gifts have their -- the whole transfer tax regime is another section of the Internal Revenue Code. You've got to file the appropriate returns, and filing the appropriate returns would be part of meeting the five-year certification test.

I would also like to add one other possible technical point here, and I consider this to be an unsettled question, but there are people with strong views on this one way or the other. If you're going to make gifts to reduce net worth – which is perfectly legal -- prior to renunciation, I encourage you to separate the year of the gifts from the year of the renunciation. I'm not saying for sure you can't, but I have seen arguments both ways. So my view to avoid potential problems. Make the gift in a year that's different from the year you expatriate.

MATEO JARRIN: Okay. Thanks for that, John. Let's move on to our questions here. Is the exit tax really a collection of four separate taxes? How do these separate taxes work?

Question 3: Is the exit tax really a collection of four separate taxes? How do these separate taxes work?

JOHN RICHARDSON: Right. Well it's at least three and I would say that there's a fourth component to it, yes. So you'll find all this in Section 877a of the Internal Revenue Code where I've written probably at least 30 blog post articles on this one. If you want to e-mail me, I'll send you some links.

But the first tax is what I would call the gain from disposition of property taxes. It's treated like a capital gain. So if you had a piece of real estate and you sold it, you would pay a capital gains tax on that. So for property, things like real estate shares, etcetera, you expatriate, and if you're a covered expatriate, they would pretend that you had sold all your capital property and impose a pretend tax on the pretend sale.

So very simple example, you own a small three-unit apartment building, you bought it for 100,000, you sell it for 1 million one. The fair market value is 1 million 1 hundred thousand, if you renounce, they would simply attribute a one-million-dollar capital gain to you the year that you renounce. So that's how the property sale works.

Now the next two are very interesting, very punitive, very very dangerous. They are taxed differently. These are examples of full income inclusion. The first are what are called specified tax deferred accounts. These are things like IRAs -- that sort of stuff. And the theory there is that -- at least for certain types of these things -- you get a tax deduction when you contribute to them.

So the idea is that it's essentially a payback, if you will, deductions that you had earlier plus the accrued gains. But anyway the problem there with that type of thing is the full income inclusion. Very dangerous. Imagine a million dollar specified tax deferred amount at full income inclusion put on your tax return the year that you renounce. That would not look good. Bear in mind you've got no income realization event to pay for this. So that's the second thing, a specified tax deferred account.

The third is defined as deferred compensation plans. That's tax speak for pensions. Really. So it's a full income inclusion of pensions, so that wouldn't mean full amount would be taxed, because perhaps you've made some contributions to it, etcetera. You'd have run the tax calculation separately, but this is full income inclusion on deferred compensation plans. Now get this. You think this is unfair.

Now let's talk about the difference between domestic deferred compensation plan -- meaning US -- and a foreign one. Well, let's take a professor with a pension from say, the University of California, compare that to say a pension from the University of Toronto. A covered expatriate with a pension from the University of California, which is a US pension, will actually be able to -- it's considered on the expatriation. But they are able to file an election so that the tax is paid as the pension is paid out.

In other words, the capital value of the pension is not attacked. But if it's a non-US pension, it will include the full million dollars, you have to pay a tax on the full million dollars. If you can imagine that. So my view is that this should be viewed as the confiscation of foreign pension plans. All right, so that's the third.

And the fourth is -- I don't know if I'd call it – a separate kind of exit tax. But there is a provision that requires you to consider if you're a beneficiary of a trust. All right? How the future distributions from the trust would be taxed. So those are the four aspects to how the tax is calculated.

MATEO JARRIN: Excellent. I guess you've covered basically the fourth question, which was why is the exit tax particularly confiscatory when applied to non-US pensions. You mentioned that just now. So do you have any additional thoughts on that or I think your point was pretty clear.

JOHN RICHARDSON: Well, I have maybe to clarify. It is particularly punitive. It's over the top. I mean, they're taking your pensions.

MATEO JARRIN: Thanks, John. Okay, next one. Now, more in terms of I guess procedural stuff. What are the exact requirements that must be met in order for those renouncing US citizenship to effectively log out of the US tax system?

Question 4: What are the exact requirements that must be met in order for those renouncing US citizenship to effectively log out of the US tax system?

JOHN RICHARDSON: Okay. So you know, everything about American life is in the Internal Revenue Code, it is the Bible of America.

MATEO JARRIN: Sorry. I'm going to backtrack again. We got a question on the previous question. Someone's asking: It wasn't clear to me if IRA accounts would be included in this exit tax or not, if even total assets under two million?

JOHN RICHARDSON: Okay. Pause. I'm going to try to improve the answer here. Now if we can backtrack, I think the first question this morning was -- what people are subject to the exit tax? And my answer was that only covered expatriates are subject to the exit tax. The inclusion of IRA income is part of the exit tax, so therefore only covered expatriates would be affected by this.

So if you're not a covered expatriate for any reason, then you would not be affected by the IRA inclusion. Okay? Now if the question was if your assets are below two million. Well, if your assets are below two million and you are not a covered expatriate for any other reason, then the IRA would not be included its income.

The test is, if you're a covered expatriate, then these horrendous consequences kick in because the IRA inclusion is one of those horrendous consequences.

MATEO JARRIN: Excellent. I think our listener is happy with that answer because he said perfect. Let's go back now to the question we were discussing about the exact requirements that must be met in order for those renouncing US citizenship to effectively log out of the US tax system.

JOHN RICHARDSON: Okay, so let me give you an example. Let's say that some of you are professionals who are advising clients on expatriation, and let's further hypothesize that you have applied to, getting ready to renounce US citizenship tomorrow. She said you were going to attend the seminar today to make sure they were safe and provide instructions for what they're going to do.

So let's imagine that you have a client who's going to renounce US citizenship tomorrow, December 7. So they walk into the council and renounce US citizenship, I'm a free person. But you have to do some cleanup here. Here's the tax cleanup you have to do. One, you were a US citizen up until December 7, 2018, therefore, you would be taxed on your worldwide income and subject to all the other requirements up until December 7, 2018.

Clearly, you'd have to file a final US tax return for 2018, but as of December 31, 2018, you're no longer a citizen, so you're a non-resident alien. So what you're doing is, when you're filing a non-

resident alien return or at least in most cases you file a 1040 non-resident alien return, but you include a schedule 1040 normal return up until December 7.

So you're filing non-resident return with a schedule that's a 1040. In addition to that, you have to complete this Form 8854. So you'd Google Form 8854. And good news, the 2018 version is already -- your client can even complete it tomorrow, you can help them with it.

Now, remember I said that to avoid covered expatriate status, you have to certify five years of compliance. Form 8854 is clearly where you can certify the five years of compliance. I'm not sure that it's the exclusive way to do it but the Form 8854, among other things, it's where you certify five years of compliance, it is also where you list all your assets, and answer questions that would confirm that you either are a covered expatriate or not a covered expatriate.

Now Form 8854, which is a separate -- what's called an expatriation return. One, needs to be attached to your final tax return and two, must be sent separately to another address somewhere in Philadelphia just to document the filing of that. And then finally, the Internal Revenue Code requires the State Department to turn over to Treasury the names of people who have renounced/relinquished US citizenship. By the way, this also applies to green card applicants although we haven't used that language. And then of course, if they're really really lucky, their name will be published as having renounced US citizenship. Some people regard that as a badge of honor, some people are mortified. But anyway, there's your process.

MATEO JARRIN: Okay, excellent. I think that's pretty clear -- the step-by-step process. Okay, our next question is: How does the US punish future beneficiaries if they receive gifts or bequests from people renouncing their US citizenship? Getting back into the gift –

Question 5: How does the US punish future beneficiaries if they receive gifts or bequests from people renouncing their US citizenship?

JOHN RICHARDSON: Right. Renouncing US citizenship. Okay. So if people renounce US citizenship and are covered expatriates, what they've done is they've established a new gift tax regime for covered expatriates who have the temerity to actually allow their capital to come back into the United States. Who would want to have it taxed again? Anyway, to have it come back into the United States. So what they do is this -- and this has not been imposed yet -- I'm not sure exactly why, but it's totally outrageous.

So let's imagine that, Mateo, let's imagine that you find out that you're a US citizen, you hate it. Or maybe you are. You hate it.

MATEO JARRIN: I'm not.

JOHN RICHARDSON: No, you're not. Okay. Well let's pretend you are, okay?

MATEO JARRIN: My parents are.

JOHN RICHARDSON: Oh my gosh. Well, you better take this to them. Let's imagine that you're a US citizen, you renounce US citizenship, you have five million dollars of cash. Now, you wouldn't pay an exit tax because there's no gain on cash. But if you then say, you know what -- well you know I have a relative or a wife or somebody and I want to give them that five million dollars, well then, the Internal Revenue would say, "not so fast buddy." You're a covered expatriate, you're a bad person, you have dirty assets. If you have dirty assets, go back to the US first, and

we're going to confiscate them as a gift, 40 percent. It's the only time the United States imposes gift tax on the recipient of the gift rather than on the person who makes the gift, because you're no longer a US citizen. They cannot tax you.

So that's the problem there. That's beginning to work its way through regs and stuff like that. I mean, you would not believe what the regs say. So what this does mean, by the way, from a practical point of view. And this is something that I always always, tell people to do because they need to compile what I would call a renunciation file. It shows all their assets and exactly how they got to the valuations and all those sort of stuff. And then what you should do is make copies of it, give it to your family members for generations. If you're not a covered expatriate, it's evidence that you were a good person who renounced and not a tax evader.

MATEO JARRIN: Okay. Excellent. You've covered some of the exceptions to the exit tax regime, so I'm going to skip that question. I would jump into -- these are a bit more specific. They are questions that we received just a few hours ago, and I think some of them pose some interesting questions. So how would foreign and domestic property owned by US citizens be dealt with? Does this change if the property is held by a corporation for which the US citizen is a majority shareholder? How are properties handled where the US citizen relinquishing citizenship is only a significant, but not a majority owner of the property? Any thoughts there? I know it's a long and loaded question.

Question 6: How would foreign and domestic property owned by US citizens be dealt with? Does this change if the property is held by a corporation for which the US citizen is a majority shareholder? How are properties handled where the US citizen relinquishing citizenship is only a significant, but not a majority owner of the property?

JOHN RICHARDSON: Not really, no. I mean, you just analyze it in exactly the same simple-minded way. Remember that all property anywhere in the world owned by the person would be included. I mean, if they are a majority -- I don't know let's say the property owned by the -- okay, if you own the shares in the corporation, the corporation owns the property. You don't own the shares to the property, the corporation does. So your assets that are subject to the exercise would be the shares in the company. That's number one, okay? You know, whether foreign or domestic.

And number two, you just would calculate what share of the property the company owns. So company owns two-thirds of a piece of real estate, then the question is how would that two-thirds ownership of the real estate impact the value of the shares of the company, and it's the shares of the company that are subject to inclusion for net worth determination and for possible exit tax purposes. I think that pretty much answers it.

MATEO JARRIN: Okay, perfect. Thank you. The person who posed that question is listening too. So if you need some follow up, I'll jump in and provide you with a follow-up question. All right let's go on to the next one. If personal loans are taken against retained earnings of a corporation and a person then relinquishes US citizenship, how would these loans be treated? Would they be treated as taxable? And if at some point in the future the loans were forgiven -- essentially making them income -- would they then be taxable by the US, even if the person were no longer a US citizen?

Question 7: If personal loans are taken against retained earnings of a corporation and a person then relinquishes US citizenship, how would these loans be treated? Would they be treated as taxable?

JOHN RICHARDSON: Yeah. I saw that question this morning. I'm not entirely sure, I'd have to think that through, but I'll think it through sort of out loud and do the best I can with it.

All right. So I think we need to begin with the principle that there may be a difference between a loan from a domestic corporation or from a foreign corporation. Particularly, if the foreign corporation is a controlled foreign corporation, my understanding with subpart F rules is that the loan would be included in income at the time it was made if it's a controlled foreign corporation.

But basically, on the perspective of the individual renouncing, if you borrow money from anywhere, it would become a liability. It becomes a liability. So when you complete your Form 8854 balance sheet, presumably, it would just be a liability. So let's imagine, the company with two million dollars of cash and let's say you borrow one million. Okay, shareholder -- at least from the point of view of the corporation has to pay it back. So I guess that would be a liability. But, on the other hand, from the point of view of the corporation, I think the loan would become an asset, wouldn't it? Which means, that you haven't really reduced your net worth because you're still owning the shares and the million-dollar loan, that's an asset from the perspective of

the corporation so it creates the value of a share to you. It's a liability from your point of view, so it decreases your asset level.

Now on the issue of paying things back, so you renounced. I mean, the US has no jurisdiction over you if you're no longer a US citizen unless the forgiveness of the loan was considered somehow to be US source income. Therefore, it would have to be dealt with from that perspective. That's sort of the best I can do thinking out loud. I don't know.

MATEO JARRIN: There was a clarification here by the person who posed the question, basically it's in case you are the majority shareholder of a company which makes the loan.

JOHN RICHARDSON: Well, if you're the majority shareholder and the company makes the loan and it's a foreign corporation, it's clearly a controlled foreign corporation, I think there's income inclusion once the loan is made. So if you've already paid the tax on the income and they forgive it, down the road I mean would it really be called tax? I don't think so.

MATEO JARRIN: Okay. Thanks, John. Now, a different type of question now. More in terms of what options are available to US citizens once they renounce their US citizenship in terms of returning to the country. So the question is what type of citizenship options are available to US citizens wanting to relinquish their citizenship but still have relatively easy access to the US for personal and business visits for 60 to 90 days per year. Would the Grenada plus the E1 or E2 option be the best? What other options are there? What are your suggestions there?

Question 8: What type of citizenship options are available to US citizens wanting to relinquish their citizenship but still have relatively easy access to the US for personal and business visits for 60 to 90 days per year. Would the Grenada plus the E1 or E2 option be the best? What other options are there?

JOHN RICHARDSON: Yeah. Can I break that into two questions, would you mind? We could address that from the point of view of one, once you are no longer a US citizen, how does that affect your ability to come into the United States? Then perhaps we could talk about second, citizenships and how that might affect the other issue.

This is incredibly interesting. Well let's start off with you renounce US -- by the way, I hope to God nobody would renounce US citizenship unless they have another citizenship -- I mean, there are a few people who do. I think that's terrible in any case. So you renounced US citizenship and from the US perspective, you become -- you're just treated as a citizen of whatever country you're now a citizen of. Now what does that mean in terms of entry into the United States? Well, I

live in Canada so it's fairly easy. Canadians, I have discovered, have incredibly generous access to the United States. So I mean as long as they're careful... I think they can stay up to six months, I think. I should know that, I live in Canada. I think it's six months.

But anyway, so they have easy access and a lot of them -- and this is I think a policy decision on the part of the United States -- a lot of Canadians seem to like to winter in places like Florida and Arizona. They want their money obviously. The only capital they don't want coming in is dirty money from Americans who renounced and it's dirty money.

So from the point of view of say, a UK citizen, now we move to what I call visa waiver countries. You know they can come in to the United States, no problem, they don't need a visa. There's an ESTA thing they file, etcetera. Now, there's other citizens of countries where I think it's more dangerous. An Iranian-American dual citizen, if you're trying to come in from Iran, you probably need a visa and all those sort of stuff. So that's the first issue.

The second issue is this: that if you look at the Immigration Nationality Act Section 212, you will find an astoundingly large number of reasons why people are inadmissible in the United States regardless of citizenship status or anything like that.

And I would encourage anybody with any kind of past transgressions with the law, to have a look at that. Because, well, I mean, for example, I was once working with somebody and he was getting ready to renounce and all of a sudden he tells me that he was arrested many years ago. You know, blah blah blah. It's not entirely clear whether that particular thing would have made him inadmissible or not. But I mean, there are reasons why people are not admissible in the United States. I mean, I hate to put it this way. This is not intended to be humorous, but if you're a hardened criminal, do not renounce US citizenship. Well, no. I mean obviously, because if you're a citizen, you have a right to enter the United States. Right?

I mean this stuff can be really perverse. But that's the first thing. So you really need to sit down and say, "What does my life look like as a non-US citizen?" If this is important. All right? Maybe it's not. What sort of visa might I need. Are there any reasons why I would be excludable? And on the excludable thing, as you may or may not know -- cannabis, marijuana, whichever it's called, since October has been legal in Canada. It's been so promoted in Canada, it almost makes me feel like I should be out smoking the stuff. Support the government. I mean it's just so important. But what's interesting is that it's in violation of federal US laws.

So this is a big topic for Canadians right now is, what if I either work in the marijuana industry or smoke it, would that make me excludable from the United States? And the answer is, technically it might. Anyway so that's the first category.

Second one -- citizenships. Now, as you may know, there is a huge market and a growing market for buying second citizenships. And you can also get it through marriage and a variety of other things. Obviously, there are some citizenships that are far better than others. You mentioned the Grenada thing. I think that's really a fascinating option because citizenship in Grenada is -- I think I'm comfortable recommending this -- citizenship in Grenada is relatively easy to get. Yeah, it's not quite a purchase of citizenship, and the money goes a long way and not much of it to get citizenship.

MATEO JARRIN: It's not like getting your Cypriot passport. The investment is 2.5 million Euros, I think. Go ahead, John.

JOHN RICHARDSON: Well but they're very different types of things. Because the one I think, you know it's giving you EU access but the thing that's interesting about Grenada is that they have the kind of treaty with the United States that would allow for a citizen of Grenada to get either an E1 or an E2 -- it's an E-something visa to do business in the United States. And this is a fantastic thing. And the reason it's fantastic is, you can get the visa through Grenadian citizenship and do business in the United States, but you can avoid the green card. The green card is what makes you a US tax resident. It can destroy your life because of worldwide income.

So there's this huge market, all these people are out promoting this EB-5 program in the United States. My personal view is: you should avoid that. Use Grenadian citizenship, you know, E2 option because you get the access to the United States -- I mean if you're really just trying to be able to do business, you can get the access to do business without becoming a tax resident. So you get the best of both worlds.

MATEO JARRIN: Are there any other options out there that you know of, or any other suggestions?

JOHN RICHARDSON: For citizenship?

MATEO JARRIN: Yeah. I mean, that you think would work, or?

JOHN RICHARDSON: Well, you know, I was in a congress in Ottawa, Canada, last week and, you know, Canada acknowledges they need lots of immigrants and citizens largely to take over businesses. I mean, I was talking with somebody from the province of New Brunswick and I said, you know, I don't know why you don't market this in the United States. Imagine, five years, Canadian citizenship and blah blah blah.

Maybe they can get that type of thing and then come back into the United States as Canadians for various reasons. I mean, I think the answer is it depends on why you would want access to the United States. I mean, if it's as simple as I just want to be able to travel there, I wouldn't worry about it that much. If it's -- now I want to run businesses there, I think that's an entirely different matter. And I think you've got to be careful about becoming a tax resident, which can be so -- all these exit tax rules apply to these people too.

MATEO JARRIN: Right. Excellent. Okay, we have about 15 minutes left, John. We have a couple of questions and then I'll let you conclude, give us some concluding remarks which we pretty much all know where they're headed. But let's get done with these last two questions. Trump's new tax law states that foreign entities where a US citizen is a majority shareholder will not be taxed similarly to domestic enterprises. Has this actually been implemented and will it be enforceable in 2019? And then he adds a little bit of information like some jurisdictions such as Dubai have a requirement of 51 percent of domestic partnership of a company. Could one use this type of nominee structure to remove the tax obligation under Trump's new law? If not are other options such as moving the company into a foundation be a viable alternative? What are your thoughts there, John?

Question 9: Trump's new tax law states that foreign entities where a US citizen is a majority shareholder will not be taxed similarly to domestic enterprises. Has this actually been implemented and will it be enforceable in 2019? And then he adds a little bit of information like some jurisdictions such as Dubai have a requirement of 51 percent of domestic partnership of a company. Could one use this type of nominee structure to remove the tax obligation under Trump's new law? If not are other options such as moving the

company into a foundation be a viable alternative?

JOHN RICHARDSON: Okay, yeah, so this is like two, three questions built into one. Let me deal with the first one, which I think — When we answer the first one, I think we probably can guess the answers to two and three. I read that question when you sent it over this morning and -- sorry, could you just read the first part of that again? The Trump's new tax law read it to me again please.

MATEO JARRIN: Yeah. Trump's new tax law states that foreign entities where a US citizen is a majority shareholder will not be taxed similarly to domestic enterprises.

JOHN RICHARDSON: Okay, stop there, thank you. All right. Now, you're talking of entities and I think what you mean are corporations here. Because under US law that the partnership is a sort of a flow through thing. So let's look at it from the perspective of corporations. Here's a picture.

MATEO JARRIN: Sorry John, just a quick clarification here. The question is actually that if CFCs will be taxable?

JOHN RICHARDSON: Yeah, that's what I thought it was. Absolutely, positively, 100 percent, yes. And the shareholders will be absolutely, 100 percent destroyed. So let me explain why that is and how it works. So, basically, the US in tax reform did one thing and it reduced the US corporate tax rate from 35 percent to 21 percent. And they claim to move towards a territorial tax system where the control for corporations owned by US domestic corporations would not be subject to US tax when they repatriated.

To say that the US move to a territorial tax system is sort of like saying that in the old days the Deutsche Demokratische Republik was truly a free democracy. In fact, what they did -- although they called it territorial -- well, the way I put it is, the US move to territorial taxation. What they actually did was vastly increase the territory where they could exercise US tax jurisdiction. It's far worse than it ever was now.

They've established something called the GILTI tax and this applies to controlled foreign corporations and we can get in to -- Karen and I will do this for you, I think we talked about this earlier or something like that. But the bottom line is this, that all of the earnings of the corporation that are not paid out as salary or expenses, the shareholder will now be taxed to the individual shareholder even though the shareholder never received money. So this is another fictitious tax event, aimed at the tax base of other countries.

Now, I do appreciate that there are people who would find what I just said completely offensive. I do agree that it was somewhat of a generalization, but I don't have time to get into the very, very, very small amounts that are deducted from the whole amount that's income inclusion. That's the governing principle.

Now are there workarounds to that? Yeah, possibly, it's called a Section 962 election. But to answer your question, it is now a completely new and vastly more punitive and expensive world, where US citizens are domestic corporations that have the temerity to incorporate a business

outside the United States where it's majority owned by US citizens. And I think that it probably answered -- I think you can guess the answers, extrapolate the rest of that.

Section 951a incidentally of the Internal Revenue Code. You want to look at Section 951a.

MATEO JARRIN: Okay. And we'll get into the GILTI provisions. Hopefully in February or March, we'll run a Webinar on that with you and Karen.

JOHN RICHARDSON: Everybody who's listening to this should come back to that one in February or March. You will love it.

MATEO JARRIN: We'll get everyone riled up, John? Let me see, I think there's a follow up question here. Yes, there is a follow question in terms of what we just discussed. So if the shareholding of the US citizen is less than 51 percent, does that make it no longer a CFC?

JOHN RICHARDSON: No, absolutely not. Okay? It all depends on the totality of the ownership. Let me try this, I think I've got this right. Basically, here's what a CFC is. A CFC, first of all it has to be a foreign corporation. Now, I probably should begin by saying the fact that it is called a corporation under foreign law doesn't make it a corporation under US law. So the very elaborate work called entity classification rules to determine what kind of foreign entities are or not presumptively US corporations.

But so, let's imagine we're dealing with a foreign corporation. A CFC is where more than 50 percent of the ownership or voting power is owned or exercised by United States shareholders. So it's not one person, it's the cumulative ownership. The next question becomes: what's a United States shareholder? It's not just somebody who buys a share of Heineken beer or something like that, right? A United States shareholder is a United States person that owns 10 percent or more of the shares of that foreign corporation.

Okay. So, one, total ownership by United States shareholders by ownership or voting role more than 50 percent. Two, that total ownership must be made up of United States shareholders, to be a United States shareholder, you'd have to have 10 percent or more. Is that clear?

MATEO JARRIN: I think so. It's clear to me. We'll see if we have more follow up questions. Let me follow up then with another question that says -- let me actually read the question in all its totalities so that you can get a better sense. So the shareholding of the US citizen is less than 51 percent, does that make it no longer a CFC and then makes the shareholders not liable to pay taxes under retained earnings?

JOHN RICHARDSON: Okay. Now this question has moved into the transition tax, I think. Is that correct? Can you confirm if the person's there? Are we talking about the transition taxes?

MATEO JARRIN: He's happy with your first answer. And then he says, so if there's only one shareholder who is a US citizen who owns less than 51 percent. Let me see.

JOHN RICHARDSON: Golden, you're golden. One a shareholder only, less than 50 percent, you're golden. At least you're not covered by the CFC rules. I mean there are other problems of being a US citizen. Everywhere you look, there's problems with being a US citizen, okay? You escape one, you got another one. If I could add to this, please for whoever's asking the question.

MATEO JARRIN: He just dropped an LOL, so he's having fun.

JOHN RICHARDSON: Well, let me just add something here for that one individual. You know, these are the most complicated provisions of the Internal Revenue Code and outside treaties of I think international tax, generally. I would encourage you to go to the Internal Revenue Code and read the sub part F revisions every night for, say, the next five or 10 years. Then I think you'll understand them. Okay. But it's incredibly convoluted stuff.

MATEO JARRIN: Okay. That's all you'll need, five to 10 years?

JOHN RICHARDSON: Well, that may not be enough, I don't really know. But you know, I think that if you haven't got it by year 5, I think you need to move on to another hobby.

MATEO JARRIN: You said subpart F right? The subpart F provisions?

JOHN RICHARDSON: They're called the subpart F provisions, they're sections 951 to I think, 965 of the Internal Revenue Code -- the Bible of the United States. You will find it there.

MATEO JARRIN: I think he's downloading them already and he is going to start reading them.

JOHN RICHARDSON: Awesome. Excellent. I've changed a life today, look at this. After December 6, 2018, your bedtime reading was the subpart F rules.

MATEO JARRIN: There you go. He got them. Perfect. One final question, just I guess for comparison purposes. Are there any other countries in the world that imposes similarly onerous exit tax on its citizens when they decide to give up their citizenship? Do you know of other cases, other jurisdictions?

Question 10: Are there any other countries in the world that imposes similarly onerous exit tax on its citizens when they decide to give up their citizenship?

JOHN RICHARDSON: Well, okay, so the United States is the only country that imposes taxation based on citizenship. I know that people talk about Eritrea. But absolutely not. Eritrea is benign. Comparing Eritrea to the United States is a gross insult to Eritrea. There is nothing. Okay. Like the United States citizenship-based taxation system. However, the exit taxes have been a growing phenomenon in quite a number of years, and by exit tax what I mean is tax imposed on somebody when they sever tax residency with a country. Just that in the United States, tax residency is based on citizenship, in other countries, it is based on residence. But that doesn't necessarily make it easy.

So Canada and Australia are examples of countries that have -- I would call them exit tax -- but they would call them departure taxes because they are imposed when you break tax residency, and you break tax residency when you physically -- and in a general sense -- when you physically move from the country. If we compare the Canadian one and the US one, if anybody is interested, email me, I wrote a post on this once, a comparison. All exit taxes are really bad and dangerous. There's no question about it. But the Canadian one, it doesn't impose it on

retirement pensions and things that are equivalent to specified tax deferred accounts. It does impose it on foreign assets.

In other words, in Canada and Australia, what they do is they do not impose exit taxes on things that Canada or Australia would retain tax jurisdiction over. Meaning the only way to get your money -- you can't get the money out without the Canada Revenue Agency knowing about it anyway.

So in that sense, there's no question, they're far more benign in terms of what they tax. There's a second way they're far more benign. This really is related to the whole citizenship taxation thing. I'm not aware of any other departure tax that would impose departure taxes based on the increase in value at a time when the person did not even live in the country. The problem with the US exit tax is that it disproportionately affects Americans abroad. Because I mean you're not renouncing US citizenship or any citizenship unless you have another citizenship. And for many of these people they have been tax compliant for 40 years or 50 years in another country. And literally all of their assets are non-US assets.

So I mean it's bad enough confiscating non-US assets. But imagine confiscating the assets when they were earned or accrued when the person didn't even live in the United States. I mean this is just absolutely over the top.

And it's also, by the way, a direct attack against the tax and capital base of other countries. But some of this stuff can be mitigated by treaties for fictitious tax, you get an artificial pop up in one country. Make no mistake. This is a really bad problem.

MATEO JARRIN: Okay. We have an interesting question. This goes back to what you're saying about you don't recommend renouncing your citizenship when you don't have another citizenship. And the question is what actually happens when someone relinquishes their citizenship if they're not a citizen of another country? What actually happens when someone relinquishes their citizenship if they are not a citizen of another country? If they're out in the limbo, I guess.

Question 11: What actually happens when someone relinquishes their citizenship if they're not a citizen of another country?

JOHN RICHARDSON: Well, so they become stateless. So what does that mean? They're not a citizen of any country. I'm fairly active writing on this stuff on Quora, and there's a guy on Quora who I may interview him for one of my own video series, who renounced US citizenship and is stateless and sometimes chimes in on this stuff. I personally don't think it's a great situation to be in. I mean, at a minimum, you are very, very significantly restricting your ability to -- your mobility to other places that require a passport. But I mean, for a certain type of person it's obviously possible. I mean you know the United States -- if you want to renounce, at least as it stands today, you have the right. A lot of the consulates are very, very, very careful to aggressively make sure that people are citizens of another country, which I think it is a good thing. You can do it. You can renounce. I don't think it's a good idea, but there are people who do it.

Concluding Remarks

MATEO JARRIN: Okay. Some concluding remarks, John? Anything that you want to add that you have not said already? I was going to wrap up with your last words there, you know, you said with a lot of passion. We're going to wrap up there but then we got this extra question so I'm going to give you another chance to kind of get into it again.

JOHN RICHARDSON: You know what? I want to just cut the rhetoric here a little bit. I mean you know how my views are. And by the way, sometimes you can say, "Well, these are my views and I may be wrong, or these are my views and they are not wrong." Okay, for anyone who's actually been affected by this. Let me just say this, that there are advantages to US citizenship. And I do think the United States is a great country with a great history.

I mean if you watched, for example, the funeral of President Bush yesterday, all countries go through ups and downs and sideways, and I do think that US citizenship does have value. The problem with it is that because of FATCA and you know an Internal Revenue Code that is so hostile to anything that's foreign, it's made it practically impossible for US citizens to both be tax compliant, as US tax compliant, and live outside the United States in any kind of normal life.

So in my view, people are being forced to renounce citizenship, I don't think they have any options anymore. If they want any chance of being able to provide for themselves in retirement. In 1967, the United States Supreme Court issued a decision, which really opened the door on these problems. Essentially, gave Americans' constitutional right to dual citizenship, which just led to these problems. But at the end of this decision, Justice Black summarizes the whole thing by saying that basically the reason why the 14th Amendment right to US citizenship is so that one group of citizens, that is Congress, cannot make laws that deprive another group of their citizenship.

And this is actually what's going on right now. I mean the exit tax is a manifestation of what I see really is a forced citizenship thing, and I expect that before the final chapter on this is written, that this may be re-litigated in terms of whether the US can impose these rules, but on the one hand are forcing them to renounce US citizenship, but on the other hand are taking their assets when they do renounce it. So, there you have it, just few thoughts on it. Oddly, it is indescribably horrible for the people who are caught in this.

MATEO JARRIN: Right. We have one final question. We'll wrap up with this one, John. And this will be the last one and then I'll jump into some, you know, just to conclude the Webinar. Final question -- at what level of net worth does it make sense to you for US citizens to relinquish citizenship from a tax perspective? I guess this is opinion, really.

JOHN RICHARDSON: Well, I think that obviously, I mean, the easy answer is before they hit the 2 million. Question is if you're over the 2 million and you're paying an exit tax, when is it worth paying an exit tax, or not?

And I don't think there's any universal answer, I think it depends on people's ages, their ability to regroup things. But the way I generally -- well okay, I was once sitting in the office with somebody and we figured out she'd have to pay $300,000 exit tax. She wanted to renounce US citizenship and she was horrified. And it is horrifying. But I ask you the following question: I mean let's say you had $300,000, and you were looking for an investment return on that money. What could you get in return for that $300,000? So again analyzing now what can she get in return for the $300,000 that would be a benefit by no longer having US citizenship and we got -- it didn't take too long before she concluded that maybe paying that $300,000 was a good investment.

Now, I've helped people renounce for reasons that include they're offered ownership, part ownership in companies and if they're a US citizen now they won't allow them to be owners of the companies. I mean, I think in a case like that obviously, you just compare the exit tax with the benefits of owning the company. I think the answer to the question is: it's not some numerical

level. It's what is the cost? And if you have that money, what kind of a return can you get for putting yourself in that position? I think that US citizenship for people who are entrepreneurs, who want to be mobile, I think it's a very, very dangerous thing to have in a global world.

MATEO JARRIN: Excellent. Thank you very much, John, for being with us. We actually look forward to having you again in February or March with the GILTI provisions, and Karen too. So let me get some admin issues out of the way. We have recorded this Webinar. We will have an audio recording available for all of you probably early next week. We will have a full transcript that we'll share with all of you.

If you have been paying attention and you want your CPD credits, get in touch and we will issue those for you. If you have any follow up questions, just post them on the relevant forum discussion, and we'll make sure that John gets to those and provides you with some additional details.

That's all I have from my end. Thank you, John, on behalf of TaxLinked, and we look forward to our next one. It's always a pleasure having you here with us.

JOHN RICHARDSON: Mateo, I want you to call a series of seminars the Confiscation Series, okay? The Confiscation Series.

MATEO JARRIN: The Confiscation Series? That works. We can make a nice little package.

JOHN RICHARDSON: That's exactly what it should be. Yes.

MATEO JARRIN: Excellent. Thank you very much. And have a good day. Thanks, John.