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Reverse Immigration: How IRS Taxes Giving Up Green Cards

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Giving up a Green Card can involve an unpleasant tax surprise. As the IRS continues its war on offshore tax evasion, many expatriates feel caught in the crossfire. U.S. citizens and permanent residents are required to report their worldwide income on their tax returns. They also must report foreign accounts on annual FBARs. If you have a Green Card, you face the same range of tax and disclosure obligations as U.S. citizens. And [FATCA](#), the Foreign Account Tax Compliance Act, has made it worse. Some U.S. citizens have even given up their citizenship. Permanent residents can give up their Green Cards too, but there may be a tax cost in the form of a U.S. Exit Tax.

For Green Card holders, the question is how *long* they have had it. A long-term resident is a non-U.S. citizen who is a lawful permanent resident of the U.S. for at least eight years during the 15-year period before their residency ends. A “lawful permanent resident” means a Green Card holder. However, you are not a “lawful permanent resident” under this rule for any year in which you are treated as a resident of a foreign country under a tax treaty, as long as you don’t waive the treaty benefits applicable to that country’s residents. Caution: holding a Green Card for even one day during a year taints the entire year.

The Exit Tax is computed as if you sold all your assets on the day before you expatriated, and had to report the gain. Currently, net capital gains can be taxed as high as 23.8%. There are three triggers for the Exit Tax, and any one of them will make you a “covered expatriate.” First, is your net worth over \$2 million? This is the aggregate net value of worldwide assets. It is not just your U.S. assets.

For married taxpayers, each spouse’s net worth is calculated separately from the other. If they own their assets relatively equally, a married couple could have a total net worth of up to \$4 million without triggering the Exit Tax. However, if one spouse owns most of the assets, that spouse could be a covered expatriate, even if the other spouse owns significantly less than \$2 million of assets. Some couples can gift assets to each other to bring both spouses’ net worths below \$2 million. If the spouse receiving the gifts is a U.S. citizen, these gifts may escape U.S. gift tax.

But if the spouse receiving the gift is not a U.S. citizen, spousal gifts may be subject to gift tax, even if the spouse receiving the gift is a U.S. green card holder. For 2017, there is an annual exclusion of \$149,000 for gifts to non-citizen spouses. If you need to transfer more than that amount to your spouse to bring your net worth to below \$2 million, you would have to rely on your unified tax credit to avoid gift tax, or you would need to plan in advance to make the transfers over multiple years before expatriating.

Another exit tax trigger is whether your average net annual income tax liability is over \$162,000. This is not your taxable income, but your *tax liability* on that income. If you are married and filing taxes jointly, you must use your net tax liability on your *joint* returns, even if only one of you is expatriating. This trigger can sometimes be avoided with careful planning. Filing separate tax returns (not joint returns) often makes sense. As the trigger is your *average* tax liability over the last five years, you may need to file separately for several years before you expatriate.

The third way you can be a covered expatriate is if you do not (or cannot) certify five years of U.S. tax compliance. If you haven't filed, or haven't filed properly—say you didn't report an offshore bank account—you will need to fix that too. Fortunately, you can amend your prior tax returns (and other forms) and simultaneously also file a [Form 8854](#) to expatriate. In effect, you sign your Form 8854 last, *after* you've signed the amended tax documents.

If you are *not* a covered expatriate, you do not need to worry about Exit Tax. And if you trip any of these tests, you should calculate the Exit Tax. If you *are* a covered expatriate, the first \$699,000 of gain is shielded from the Exit Tax for 2017 expatriations. For spouses who expatriate, each spouse files a separate Form 8854, and each spouse can exclude \$699,000 of gain (or nearly \$1.4 million of gain combined). The Exit Tax on certain assets, notably 401(k) plans, can be deferred. However, the tax on the future distributions is generally 30%, and you cannot claim a treaty benefit to reduce the tax.

For most other assets, you can make an irrevocable election to defer payment on the Exit Tax owed. Still, the IRS wants a bond or adequate security for any deferred Exit Tax, and interest accrues until it is paid. Even if a covered expatriate has less than \$699,000 of gain in his or her assets, being a covered expatriate has negative consequences. If you have friends or family in the U.S., being a covered expatriate could result in your gifts to them coming with a tax bill that *they* would have to pay. Even if your Exit Tax may be zero or minimal, it is best to avoid being a covered expatriate. A final, clean break from the U.S. tax system is best. In some cases, planning can reduce or even eliminate the Exit Tax, so get some professional advice and plan ahead.

For alerts to future tax articles, email me at Wood@WoodLLP.com. This discussion is not legal advice.