What Is "REAL(ly)" Residence-based Taxation ?

WHO is (a) "subject" to taxing jurisdiction is different from WHAT income is taxed!

John Richardson – July 10, 2024

TaxResidentAbroad.com

All Countries Tax Income Sourced In Their Country Regardless of WHO Is The Recipient!

When it comes to WHETHER income sourced in a country is taxed by that country:

- The "tax residency" of the person is irrelevant

When it comes to HOW income sourced in a country is taxed by that country:

- Residents may be taxed differently from non-residents
- Non-residents may be subject to preferred rates of taxation pursuant to a tax treaty

So, what is "REAL(ly)" Residency Based Taxation?

✨Wednesday Whinging✨

ALL American overseas organisations need to FULLY support REAL Residency Based Taxation.
Only 3 do. Why?

Don't confuse ...

1. **WHO** (residence-based or citizenship-based) is subject to the tax jurisdiction; with
2. **WHAT** income sources (foreign, local, capital gains, employment) are taxed!

Residence-based taxation means that citizenship is NOT relevant to determining WHO is subject to taxation.

Therefore, residence-based taxation means that the U.S. must completely sever citizenship from "tax residency".

Part I – Understanding the difference between WHO vs. WHAT

WHO = the people are subject to full taxation by a country

WHAT = if one is subjection to full taxation by a country, what are the rules that specify **HOW** somebody is taxed

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A thread exploring the WHO and the WHAT:

https://threadreaderapp.com/thread/1512035483919998981.html

Getting started: WHO is subject to a country's tax jurisdiction? (WHO is a "tax resident"?)

Q. If you live in Canada, do you care whether Australian residents are taxable on Capital gains from selling Australian real estate?

Q. If you live in Canada, do you care whether Germany taxes the non-German income earned by German residents?

Q. If you live in Canada do you care that the UK is abolishing its "non-dom" regime?

Q. If you live in Canada do you care that U.S. citizens are subject to taxation on their worldwide income if they reside outside the United States?

Getting started: WHAT income is a "tax resident" of a country taxed on?

Q. If you ARE a tax resident of Canada, do you care whether Canada taxes the gain on the sale of a principal residence?

Q. If you are a tax resident of Canada, do you care whether Canada taxes income sourced outside of Canada?

Q. If you are a tax resident of the UK, do you care whether the UK is abolishing it's "non-dom" regime?

Q. If you are a tax resident of Estonia, do you care whether Estonia has a "worldwide" vs. "territorial" tax system?

Never confuse the "WHO" is subject to tax with the "WHAT" they are subject to tax on!

WHO = What group of persons are subject to a country's tax rules

(residence, domicile, some other connection to a country, etc.)

WHAT = If you are subject to a country's tax rules, WHAT income are you actually taxed on?

(worldwide income, only domestic source income, capital gains?)

Bottom Line: The question of **WHO** is subject to tax is different from the question of **WHAT** kinds of income people are subject to taxation on!!!

WHO is a "tax resident"? Different countries have different rules for "tax residence"

Not all definitions of "tax residence" are the same!

Q. What is the criteria that different countries use to define who is a "tax resident" of the country?

A. The circumstances that constitute "tax residence" will differ from country to country. Generally speaking "tax residence" is based on definitions of (1) "residency" (deemed and actual), (2) "domicile" and (3) "citizenship" (in the case of the United States and Eritrea). Note that different countries define "tax residency" differently.

https://citizenshipsolutions.ca/2018/08/02/so-you-have-received-bank-letter-asking-about-your-tax-residence-for-crs-or-fatca-a-taxresidency-primer/

Part II – Different ways of defining the "WHO" - 50 Shades Of (Tax) "Residency"

John Richardson - Counsellor for US persons abroad

@ExpatriationLaw

Apr 7, 2022 • 35 tweets • 14 min read • Read on X

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In 21st century the most interesting thing about a person is his/her @TaxResidency. For UK residents "non-dom status means #territorialtax! For UK doms there is #worldwidetax and #RBT. For US citizens there is #worldwidetax, @CitizenshipTax and #FATCA.

Rishi Sunak's wife claims non-domicile status

Tax status allows Akshata Murty to avoid tax on foreign earnings

https://www.theguardian.com/politics/2022/apr/06/rishi-sunaks-wife-claims-non-domi...

.@TaxResidency is often confusing and often has a huge impact on ones life. In simple terms, you are a #taxresident of a country which has the right to impose the full force of its tax rules on you. This is different from HOW and on WHAT sources of income tax residents are taxed.

Residence-based taxation is a term that focuses on the WHO and not the WHAT

- Different countries define "residence" in different ways
- Some countries use a " facts and circumstances" test: what is your physical/economic connection to the country?
- Some countries use a **"deeming/statutory"** test: example if you spend more than 183 days in a country
- Some countries use BOTH: Canada – First based on "facts/circumstances" are you "ordinarily resident; Second, do you spend more than 183 days in Canada?
- With the exception of the United States (and Eritrea), **"residency" is based on a physical/economic connection to the country.**

In determining the "WHO" ...

- All countries expect the United States (and Eritrea) focus on whether one meets the economic/physical connection to the country to justify "tax residence"
- The United States and Eritrea (IN ADDITION to the economic/physical connection) deem "citizens" (regardless of economic/physical connection) to be "tax residents"

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Generally this means that the United States defines "tax residency" in terms of the "circumstances of birth", rather than the "circumstances of life".

Part III – What defining the "WHO" by citizenship – AKA "citizenship taxation" - actually means

Citizenship Tax 101: U.S. claims residents of other countries as U.S. tax residents -1/5

U.S. uses citizenship and/or immigration status as a form of deemed tax residency (without regard to physical/economic connection to the United States):

http://citizenshipsolutions.ca/2017/05/21/determining-tax-residency-in-the-united-states-citizenship-and-other-forms-of-deemed-tax-residence/

The ONLY contextual meaning of taxing based on citizenship is that it **allows the US to impose tax rules on income earned outside the United States by people who live outside the United States:**

http://citizenshipsolutions.ca/2023/01/08/toward-a-definition-of-us-citizenship-taxation/

Citizenship Tax 101: U.S. imposes punitive tax and disabilities on tax residents of other countries - 2/5

The U.S. taxes citizens abroad more punitively than it taxes U.S. residents:

https://www.taxconnections.com/taxblog/the-united-states-imposes-a-separate-and-more-punitive-tax-system-on-us-dual-citizens-who-live-in-their-country-of-second-citizenship/

The U.S. burdens the ability of U.S. citizens abroad to engage in meaningful financial and retirement planning:

https://citizenshipsolutions.ca/2017/08/04/the-biggest-cost-of-being-a-dual-canadau-s-tax-filer-is-the-lost-opportunity-available-to-pure-canadians/

Citizenship Tax 101: U.S. citizens abroad will ALWAYS suffer unintended consequences - 3/5

Out of sight and out of mind! "Some" unintended consequences of U.S. citizenship taxation on Americans abroad include:

- Transition Tax
- GILTI
- PFIC
- Foreign Trust rules
- Foreign gift rules
- "Married filing separately" abuse
- The near impossibility of U.S. tax compliance for Americans abroad

http://citizenshipsolutions.ca/2022/02/19/the-road-to-tax-reform-for-americans-abroad-part-1-the-problem-is-the-system-and-not-the-party/

Citizenship Tax 101: U.S. citizenship taxation makes it VERY DIFFICULT to emigrate - 4/5

U.S. citizenship taxation is like an "Invisible Fence". See:

"Land of the Free? The Formidable Fiscal Barriers Americans Face When They Try to Live Outside the United States."

http://seatnow.org/2024/07/05/at-the-intersection-of-taxation-and-migration/

Citizenship Tax 101: The U.S. interferes with the tax sovereignty of other countries - 5/5

The United States – by imposing punitive taxation and reporting - interferes with the ability of other countries to create meaningful financial and retirement planning opportunities for its residents. This is an interference with the tax sovereignty of other countries.

https://citizenshipsolutions.ca/2022/10/28/how-us-tax-treaties-and-the-saving-clause-prevent-countries-from-establishing-retirement-programs-for-us-citizen-residents/

FATCA letter: It's about identifying individuals WHO are citizens of the USA

So, you have received bank letter asking about your tax residence for CRS or FATCA – A @taxresidency primer

Leave a reply

Prologue: In the 21st Century, The Most Interesting Thing About A Person Is His/Her Tax Residency

The consequences of being identified as a "Citizen Of The USA" are ...

- Once identified, those "Citizens Of The USA", who don't live in the USA, will be subjected to the U.S. Internal Revenue Code and taxation on their non-U.S. source income
- The U.S. Internal Revenue Code defines the rules that determine how those "Citizens Of The USA" are required to live their life and what income they may (or may not) be taxed on.

The problem is NOT what income Americans abroad are taxed on!

The problem IS that they the U.S. claims the right to impose taxation on them and regulate their lives at all!

Part IV – What is "REAL(ly)" residence-based taxation and what does it mean?

Take 1: Digging The Foundation To Build The House Of US Residency-based Taxation

http://citizenshipsolutions.ca/2021/07/09/take-1-digging-the-foundation-to-build-the-house-of-us-residency-based-taxation/

Take 2: Residence-Based Taxation – Who, How, When and Where

http://seatnow.org/2022/02/03/residence-based-taxation-who-how-when-and-where/

Residence-based taxation means the jurisdiction to tax ("tax residency") is based on residence!

- Tax residency is based on a physical/economic connection to a country and NOT based on citizenship (which often means little or no connection to a country).
- Ending U.S. citizenship-taxation can be achieved ONLY by a complete severance of U.S. citizenship from U.S. tax residency.
- A complete severance of U.S. citizenship from U.S. tax residency means that all U.S. citizens are freed from the prison of citizenship taxation.

Severing citizenship from tax residency solves the problems of all people, all the time, under all circumstances!!

Residence-based taxation does NOT mean

- Leaving U.S. citizens as U.S. tax residents but changing the rules for WHAT income sources they are taxed on!
- Increasing the FEIE ("Foreign Earned Income Exclusion") so that although they remain U.S. tax residents they are not subject to U.S. taxation on certain kinds of income!
- Excluding non-U.S. source income from U.S. taxation but leaving all of the information return (Form 3520, Form 8938, Form 5471) requirements and penalties intact!
- Creating certain exceptions, "carve outs" for some people some of the time!

When a group/individual claims to advocate for residence-based taxation, ask yourself:

Is the group proposing a complete severance of citizenship from U.S. tax residency? If so, this is what residence-taxation means!!

Is the group proposing leaving U.S. citizens as U.S. tax residents, but simply trying to improve the difficult conditions of U.S. citizenship taxation? If so, they are NOT advocating for residence-based taxation. **They are effectively accepting U.S. citizenship taxation and asking that the conditions be improved!**

No past proposed legislation has proposed residence-based taxation …

- The 2018 Holding bill did NOT sever citizenship from tax residency. It simply expanded the scope of the foreign earned income exclusion
- The proposed Beyer bill does NOT sever citizenship from tax residency
- FATCA same country exemption does NOT sever citizenship from tax residency

These initiatives were for the simple purpose of (1) retaining citizenship taxation and (2) making citizenship taxation more tolerable.

Part V – The primary obstacle(s) to achieving residence-based taxation is Americans abroad

U.S. citizens abroad are NOT unified behind the goal of residence-based taxation!!

Americans abroad and their groups are currently the biggest obstacle to achieving residence-based taxation. This is because:

- They have different interests and financial profiles
- Some actually benefit from the current rules
- Some are happy with "carve outs" but leave the problem generally intact

The biggest determinant is where their "financial center of gravity is".

The biggest victims of citizenship taxation are long term U.S. citizens abroad, with their investments outside the United States, who file their U.S. taxes on an annual basis!

Group 1 – The believe in U.S. citizenship taxation

Reasons may include …
Various individuals and groups support U.S. citizenship taxation regardless of where they live as a symbol of patriotism
Many U.S. residents equate residence and citizenship
Some believe that the opportunity to vote should mean an obligation to pay taxes
They believe that taxation is part of what it means to be a U.S. citizen

Group 2 – After a lifetime of working in the USA, they live as "retirees" outside the USA

Happy with the current US citizenship tax system and do NOT want it changed. They do NOT want citizenship severed from tax residency.

Profile: Retirees abroad – all of their income is from U.S. sources. No non-US source income

Q. Why not interested in residence-based taxation?

- Because they don't want to be taxed as nonresident aliens on their U.S. Social Security/pensions, etc.

Group 3 – Digital Nomads who grew up in the USA and do their work outside the USA

- Digital nomads work outside the United States
- Work done outside the United States is NOT U.S. source income
- Non-U.S. source "earned income" can be excluded from U.S. income taxation by using the IRC 911 "Foreign Earned Income Exclusion"
- If digital nomads can avoid becoming tax residents of another country they will (1) remain U.S. tax residents because they are U.S. citizens and (2) exclude their "foreign source" income from U.S. taxation
- Digital nomads may be able to exploit U.S. citizenship taxation to avoid income taxation completely!

Group 4 – Are not concerned with the general principle, but ONLY with how it affects them

They are happy to have their specific issue solved, but have no interest in ending the U.S. citizenship taxation regime generally.

Typically these groups ask for:

- An expansion to the Foreign Earned Income Exclusion
- FATCA "same country exemption"
- Fewer forms (combining Form 8938 and FBAR into one form)

Group 5 – Concerned with general principle, but would be happy with "territorial tax" for individuals

Can accept U.S. citizenship taxation, but do NOT want to be taxed on non-U.S. source income.

Many people imagine that not taxing foreign source income is residence-based taxation. It is NOT residence-based taxation.

Rather, this is citizenship taxation with a "carve out" for certain "foreign source" income.

This retains citizenship as a sufficient condition for U.S. tax residency but would move the U.S. from a system of worldwide taxation to a system of territorial taxation!!!!

BIG BIG DIFFERENCE!!

Group 6 – Concerned with the general principle and want citizenship severed from tax residency!

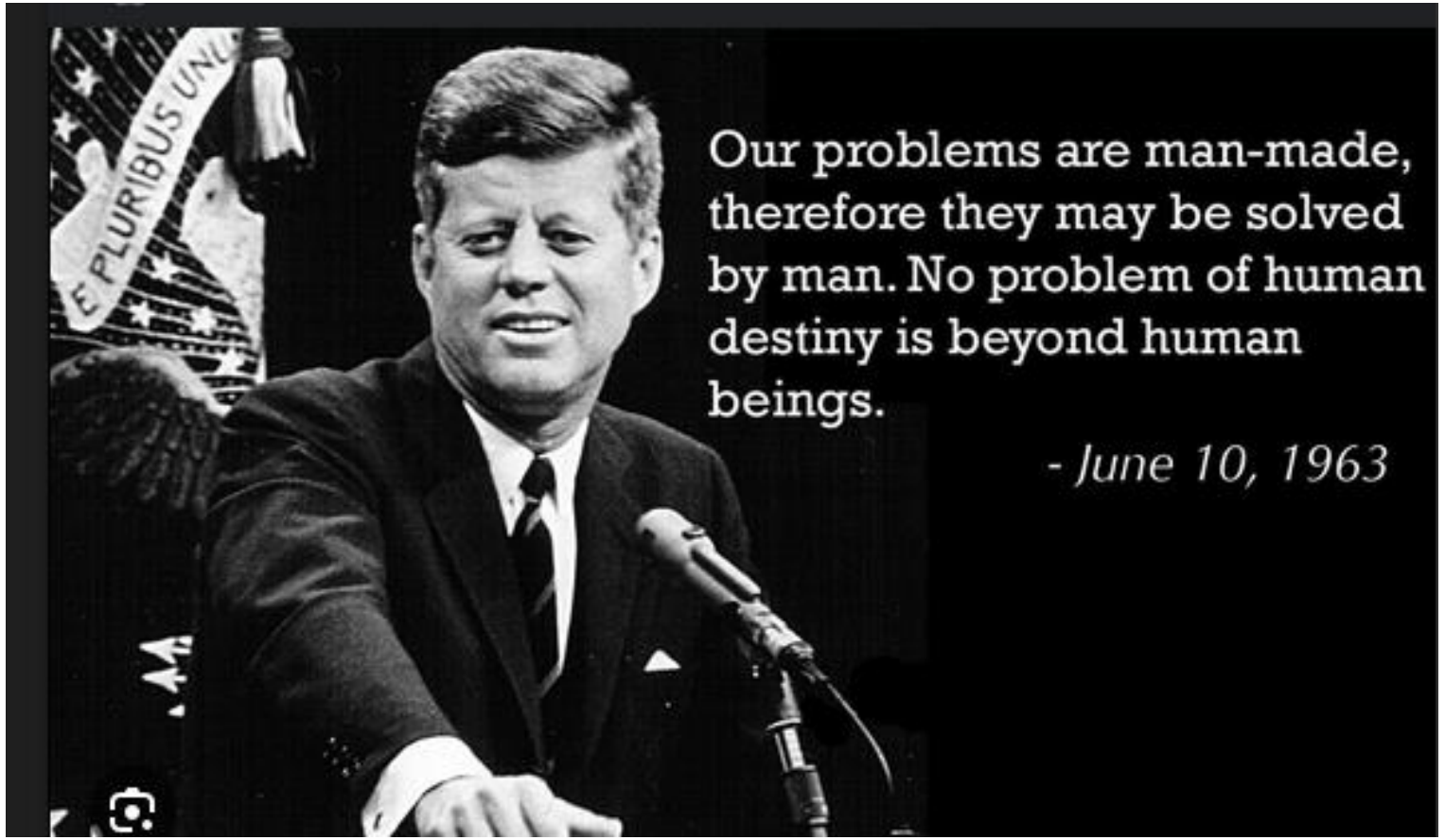
They want citizenship severed from tax residency.

Only by severing citizenship from the definition of tax residency can the U.S. move to the system of residence-based taxation that is the international standard!!

SEAT and Republicans Overseas advocate for "severing citizenship from tax residency". All individuals and groups should adopt "severing citizenship from tax residency" as their goal!!

Part VI – Severing citizenship from tax residency is the only solution that will solve the problem for all people, all the time, under all circumstances!

Ask NOT what your advocacy can do for you, ask what your advocacy can do for your community!



We encourage ALL individuals/groups to join SEAT and Republicans Overseas in advocating for severing citizenship from tax residency!

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