Cross Border Business Law Blog

The Hidden Cost Of "Going Home" — the Expatriation Tax for Long-Term Permanent Residents Who Return to Their Home Countries

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People immigrate to the United States for many different reasons. Many come here for work reasons and, somewhere along the way, obtain permanent resident status, otherwise known as holding a “green card.” They may work in the U.S. for most of their careers, raising children and becoming integrated into the social fabric of their community. But for various reasons, some will wish to “go home” when they retire. Maybe the home country offers better healthcare. Maybe even after many years in the U.S., they feel more comfortable speaking their native language. Maybe their closest relatives are in their home country, and they feel that they need a support network as they age. Maybe the food is better.

Whatever the reason, those who have been green card holders for a long time (specifically, 8 out of the previous 15 tax years) need to be mindful of the so-called “expatriation tax.” The Heroes Earnings Assistance and Relief Tax Act of 2008 (the “HEART Act”) imposes a tax at the time of departure on U.S. citizens who have renounced their citizenship and on those who renounce their long-term permanent resident status after June 17, 2008. The HEART Act expatriation rules apply to those who, at the time of expatriation:

(a) have an average income tax of $161,000 (for 2016) for the preceding 5 years;

(b) have a net worth of $2 million dollars (no inflation adjustments); or

(c) fail to certify under penalty of perjury that they have met their US federal tax obligations for the preceding 5 years.

Unless one of the few exceptions (not discussed here) apply, the individual is deemed a “covered expatriate” if the individual meets any one of the above three conditions. The last one is particularly tricky — even if one does not meet the income tax threshold or the net worth threshold, one can become a covered expatriate by not making the required certification.

Upon exit, a covered expatriate is treated as though he or she sold all worldwide assets at fair market value on the day before expatriation. The resulting deemed gain is taxed to the extent that it exceeds the exclusion amount $693,000 in 2016. Under certain circumstances, the tax may be deferred with appropriate security and interest. There are special rules that apply to retirement accounts, other deferred compensation arrangements, and certain trust interests. The rules are quite complex.

The situation gets worse for those covered expatriates with children (or others they wish to benefit) who are U.S. persons. There is a very common fact pattern for long-term permanent residents. Picture a married couple from another country who settle in the U.S. as permanent residents. The couple has children who are born in the U.S., who have lived their entire lives in the U.S., and are likely to remain in the U.S. The parents eventually return to their home country upon retirement (or perhaps more commonly, after the death of one spouse), and when the parents pass away many years later, they leave their possessions to the U.S.-citizen children. Therein lies the trap for the unwary. Such an inheritance received by the U.S. children will trigger a special inheritance tax. Indeed, the same tax is triggered upon a lifetime gift from covered expatriates to U.S. beneficiaries. The tax is imposed at the highest estate tax rate — currently 40%. Unlike the normal federal gift and estate tax for U.S. citizens and residents, where up to $5.4 million (in 2016) worth of assets are exempted from the tax, this special gift/inheritance tax applies against all gifts and bequests above $14,000 (in 2016) in value received by the U.S. beneficiary. There are some exceptions that apply, but they are rather limited, and again, the rules are quite complicated.

While taxes may sometimes be a factor in deciding where to live, many long-term permanent residents simply want to “go home.” But for some of them, the cost of going home may be greater than they expect. Unlike U.S. citizens who can live abroad for many years without facing such taxation, unless they choose to give up their citizenship, permanent residents cannot keep their resident status without living here (in most cases). Therefore, going home means expatriating. To avoid unpleasant surprises, seeking advice early is key. For those who are already long-term permanent residents, assessing whether they will be covered expatriates, and then planning for the tax consequences is important. For those who have more recently immigrated, keeping track of the eight-year mark is advisable (but note that it is eight *tax* years, not anniversary years). For those who have not yet arrived here, perhaps they should consider whether the green card is really an advisable end goal; perhaps their needs can be met with non-immigrant visas.

Tags: covered expatriate, covered expatriates with children, eight tax years, eight-year mark, expatriation rules, expatriation tax, federal gift and estate tax, green card, green card holders, HEART act, Heroes Earnings Assistance and Relief Tax Act of 2008, high estate tax rate, immigration, inheritance, lifetime gift, long-term permanent residents, permanent resident status, special inheritance tax, U.S. beneficiaries, U.S. residents, U.S.-citizen children