Kate Kalmykov (00:12):

Hello everyone, and welcome to the Immigration Insights Podcast hosted by Greenberg Traurig. My name is Kate Kalmykov. I co-chair the Global Immigration and Compliance Group at GT, and I am your host. Today, we have a very interesting topic to discuss, which is accidental Americans. What does that mean? What are the tax implications? Really, no one talks about this topic, but I'm fortunate enough to be joined by my partner, Barbara Kaplan, who's a tax shareholder in our New York office. She for many years chaired our tax group at GT, and I'm going to let her introduce herself.

Barbara Kaplan (00:56):

Thank you, Kate. It's nice to be here, and thank you for inviting me to speak on this subject, which is an important one and one that we deal with in our practice virtually on a daily basis. My practice is tax controversies and tax litigation. What that means is that I represent taxpayers in connection with their tax compliance matters, bring them into compliance if they've been out of compliance, represent taxpayers in IRS audits and local audits involving their tax matters. We also litigate cases in the United States tax court predominantly when IRS makes adjustments with which the taxpayer doesn't agree and where we feel that we're going to have a better outcome if we go into litigation.

(01:50):

That's pretty much what my practice is. I also help clients on a consulting type basis with sensitive tax issues. Many times people come to us, they're concerned about some position that they may have taken in a tax return or they may have other sensitivities that affect their tax filings. We counsel them on how to proceed, what's the best option for them given their situation. Sometimes that may mean doing nothing. Other times it means being very proactive and moving forward on their behalf.

Kate Kalmykov (02:26):

Thank you, Barbara. Of course, many of our clients are becoming lawful permanent residents, eventually US citizens, and many of them, coming from a foreign jurisdiction, may not even understand all of the tax obligations that come with taking up status in the United States. I know you work very often with the individuals who are in exactly those circumstances, to assist them in remedying many different issues that can come up in the IRS tax landscape. But let's get started on today's topic. What exactly is an accidental American? How can someone be a US citizen without realizing it?

Barbara Kaplan (03:11):

It's actually fairly easy to be an accidental American, depending on where you were born and who you were born to. Most accidental Americans are people who were born in the United States, but probably were here because their parents were students here and they were only here on a temporary basis. They were born here and then quickly left when their parents went back to their home country or to another location. The activity of being born in the United States, physically being born here is what causes you to become a US citizen automatically. Even if you never live here, your mother delivered you here, and the next day left the United States, you are considered an American citizen for tax purposes and immigration purposes.

(04:08):

The other person who is considered an accidental American is somebody who may be born outside the United States, but to American parents. That's more of an immigration analysis. I would refer to Kate when that situation arises because I know the immigration law has changed over the years, and so you have to do a deep dive into the facts and circumstances of that situation. But those people may be US citizens as well, even if they were not born in the United States. Then what might not be really referred to as an accidental American is somebody who's a permanent resident of the United States or who spends enough time in the United States to be considered a US taxpayer.

(05:00):

They're not really accidental Americans in the sense that they have citizenship here, but they have consequences as a result of even obtaining a permanent green card and being a permanent resident, or because they've spent enough time in the United States, that puts them in the category of being a US taxpayer.

Kate Kalmykov (05:24):

That actually happens quite frequently. I'm in South Florida right now, and there's many people that like to winter here, and they're coming from countries like Canada, escaping the cold. They don't realize if they're spending a certain amount of days, I believe it's 180 days, but you can correct me.

Barbara Kaplan (05:43):

183.

Kate Kalmykov (05:45):

183, I was close, that they may be subject to filing as a US resident, even though they're traveling in as a visitor.

Barbara Kaplan (05:54):

Yes, I think the misunderstanding in this area is that people always associate permanent residency with the green card. If somebody has a green card, they understand that they are a permanent resident in the United States and they have obligations associated with that. But people who are here for more than 183 days, and that's a general test, there's actually an averaging that brings that number down. If you're here in the prior two years to the year that you're testing, it will be less than 183 days. But if you're here in excess of those required days, then for all purposes from the tax perspective you are deemed to be a resident of the United States just as if you had a green card.

Kate Kalmykov (06:44):

And I think that not all permanent residents also understand that they may be subject to being taxed as a US person, because sometimes they get bad tax advice or even the tax accountant that they're going to doesn't understand that once you take up a green card, you're considered a US tax resident regardless of the amount of days that you spend here. We in the immigration group see this issue often where now we have someone who wants to apply for citizenship. They've been spending a lot of time overseas. They had permission to do so. Maybe we filed a reentry permit for them, but they never filed taxes as a US resident because they were told they didn't have to by the accountant or that they could take advantage of a tax treaty that existed.

(07:32):

That's a little bit of a tension between the immigration law and the tax law. Yes, a tax treaty exists, but you are obligated to file as a resident.

Barbara Kaplan (07:41):

Yeah, I think there is a lot of misinformation out there. Unfortunately, many of the tax return preparers and accountants don't really understand the obligations and the complications of being a resident of the United States, particularly when it comes to reporting foreign assets. Tax professionals that are in the accounting and tax preparation world, they tend to focus on your 1040 income tax return. You have to report your income and you have to pay tax on that. But there are so many other obligations under the tax code that require reporting in the form of what we call information returns. I think that is where there's a lot of misinformation, misunderstanding.

(08:31):

Even if the taxpayer's been advised that they have to file a tax return, they're often ill-advised or not advised at all about these other forms that are required as consequence of being a US taxpayer. That's where we see in our practice a lot of non-compliance. People file their tax returns, but they're not filing everything else. There are numerous other forms that are required when you have foreign activities, ownership of foreign property, for example. Those filings, even though they don't compute a tax due for the most part, they come with very severe penalties if you fail to report.

Kate Kalmykov (09:16):

I would add that the Trump Administration is very focused on this. For anyone applying for citizenship, anyone applying for a green card, if you're not tax compliant, they are flagging these issues. Even if you've entered into, for example, a payment schedule with the IRS, they're denying those naturalization cases until you satisfy the requirements for any back to taxes. They're working closely. We've never seen anything like it with the IRS. There's a lot of cooperation now with the immigration agencies and Department of State. That leads us to our crux of our topic. What happens with accidental Americans? Somebody was born here, somebody is an American because their parents were, but they've never lived in the US.

(10:08):

They have no idea what the tax requirements are. They certainly don't even have a US passport. They probably have the passport of the country where they are residing. Are they obligated by our tax requirements? If so, what happens?

Barbara Kaplan (10:24):

They definitely are. Many of the taxpayers that I see, it's a rude awakening when they come to learn that they should have been filing tax returns really for all of their economically active period. Not as children necessarily, but once they start making money and they have an obligation to file a tax return, they're really clueless. They really have no idea that they have this obligation. It usually comes to pass that they learn about it from some third-party activity. Ignorance is bliss. So many of these people who have never lived in the United States, as you point out, don't have a US passport, maybe were born here, and they've lived their entire life in a foreign country. Something has to alert them to the fact that they've got a problem.

(11:27):

It's usually some third-party activity. Sometimes it's a bank in their foreign jurisdiction sending them a letter saying, "Are you a US citizen?" Or, "Can you prove that you're not a US citizen?" If they have some other information that suggests that. Sometimes they'll just read an article in the newspaper when there's activity by the Internal Revenue Service pursuing foreigners for US taxes. But once they become aware that they have an obligation to file tax returns and to potentially pay taxes, they really need, I think, good experienced advisors in the United States. I've seen many people go to local advisors who claim to have background in US taxes, and that generally does not end up working well for them.

(12:23):

My advice is that these people need to speak to a US practitioner experienced in this area in order to assess what their options are. There are options to come into tax compliance. There are a number of different ways to do that. Depending on the facts and circumstances of the situation, the practitioner will help evaluate what is the best approach to come forward. What we are always attempting to do is to find an approach that brings these people into tax compliance, but does so with the least amount of cost and potential tax penalties that could be associated with their failure to file a US tax return and these other information returns.

(13:14):

The IRS has a number of programs that exist to basically make it easier for people to come into compliance and to relieve some of the penalties that would be associated with doing so. Those situations have to be evaluated. You have to make a determination as to whether you're eligible to take advantage of one of these programs. Then you have to obviously implement it, file tax returns, pay taxes, pay interest that's due, file all these information returns that need to be filed, and get yourself into compliance so that on a going forward basis, every year from the year when you come into compliance, you stay in compliance and you don't risk having an IRS examination, an audit, or worst case scenario, a criminal investigation as to why returns haven't been filed.

Kate Kalmykov (14:16):

Barbara, a couple of follow-up questions that arise. If someone has been living in a foreign country and paying taxes there on their income, on their interest income, would they still be subject to US taxes? Is it an individualized analysis? Would they get any type of credit?

Barbara Kaplan (14:36):

It's an individualized analysis. It also depends on what country that you're residing in and what country you pay taxes to. Many jurisdictions around the world have treaties with the United States to avoid double taxation, and that's to address the situation that you just described, Kate. In many instances, the treaty will provide benefits so that there is no double taxation. The other thing that can affect reducing the payments that are owed are tax credits, which are allowed for foreign taxes paid to other jurisdictions. There is a mechanism that will try to reduce that exposure to double tax.

Kate Kalmykov (15:24):

Now, what if someone says, "Well, I'm not interested in living in the United States. I'm going to keep living in my own home country. Why should I pay the tax returns? I haven't done it for the last 40, 50 years. Why should I start now?" What is the reach of the IRS?

Barbara Kaplan (15:42):

Well, the reach is pretty broad. Not only are there treaties to avoid double taxation, but there are also treaties that allow for an exchange of information between the foreign jurisdiction and the United States. In many instances, the reach to foreign countries and to gathering information from foreign countries arises out of these treaties so that the Internal Revenue Service, if they were to investigate whether someone should be filing a return and hasn't, they can seek information within the United States about assets that are here. But if there are assets outside the United States that are income producing, for example, and that would give rise to a US tax liability, the auditors can request that a treaty request be made of the foreign country to request information.

(16:40):

The effect of that is that just like a request that would be made locally within the United States, can be pursued outside the United States with the benefit of the treaty and the local tax jurisdictions, which in a sense act like the Internal Revenue Service and gathering information from abroad.

Kate Kalmykov (17:02):

Understood. Also, I think sometimes when people do find out they're an accidental American, then they want to move forward with getting a passport because they understand they have obligations. They have to come into tax compliance, but then they also want to avail themselves of the benefits of being a US person, a US citizen. But they should also understand that the Department of State will not issue a passport to anyone who's not in tax compliance, even if you are an American. They will wait and hold it in abeyance until you come into tax compliance.

Barbara Kaplan (17:43):

Certainly we assist people doing that all the time coming into tax compliance. One of the things that I think people don't understand is that, if you never filed a US tax return and you are obligated to, there's no statute of limitations that applies. That means that the Internal Revenue Service potentially could go back to the beginning of your economic life and insist that you file tax returns or make a determination that you owe taxes for those years. The advantage of coming forward without waiting for the IRS to find you is that under these various programs, you don't have to go back necessarily to the beginning of your economic life.

(18:30):

Typically, the look back period that the IRS generally applies is a six-year lookback. If you've been earning money in a foreign country for 30 years, you're probably only going to file delinquent tax returns for the last six years, which really cuts down on the exposure.

Kate Kalmykov (18:51):

Now, sometimes people are shocked by this news and they don't want to be a US tax person. They don't want to be a US person. Their entire life is overseas. They have no intention to move to the United States. They have no familial ties, no business ties to the United States, and they may happen to live in a jurisdiction where there's low or no taxes. We do a lot of work with people from the Middle East, from the GCC, for example. Most countries don't have a personal income tax requirement that's anywhere comparable to what we have in the United States. Sometimes we may encounter individuals who say, "Well, I didn't know I was, but now that I am I don't want to be. Get me out of it."

(19:40):

In those cases, as an immigration practitioner, we can certainly assist them with relinquishing their US citizenship. We help likewise with abandoning permanent residencies. Sometimes we obtain green cards for clients. Their plans change. Their kids decide they don't want to live and work in the United States. Their business doesn't develop in the US, it develops elsewhere, so they give up the green card, they give up citizenship. They're two very different things. Let's start with relinquishing citizenship. From the immigration point of view, the individual has to go to a US embassy in their home country. They have to go through an interview process and let them know that they want to give up US citizenship.

(20:25):

They will usually make that come back once or twice to make sure that they've thought about it, that the intention remains, because once you give it up, you can process again, but you need a basis to do that and it will take many years. They really want people to weigh that decision, but they also will not allow relinquishment where the US tax obligations are not met. That is really the crux of these types of reviews. Barbara, I know you assist clients with this as well. Can you tell us a little bit about what's involved from the tax side?

Barbara Kaplan (20:58):

Yes, there's a whole expatriation regime under the Internal Revenue Code that dictates various aspects of the consequences of giving up your citizenship. Significantly, people who have substantial assets are going to be subject to an exit tax, and the exit tax can be quite onerous. What it means is that at the day before you expatriate, all of your worldwide assets get essentially marked to market, and any gain or loss attributable to that hypothetical sale that takes place on the day before expatriation is subject to tax and is reported on your final US tax return. The cost to taxpayers is quite great if you fall into one of those categories of being what they call in the code a covered expatriate. Now, there are many exceptions to that consequence.

(22:06):

You have to go through an analysis as to whether or not any of those exceptions apply, so you would not be deemed to be someone who is subject to this exit tax. But that's a process, it requires a significant analysis. If it turns out that you are a covered expatriate and you understand what the tax consequences are, you may decide that it's not worth it to give up your citizenship because the cost is so significant from a tax point of view. For people who fall into one of the exceptions, that's not really a risk. We see a number of taxpayers though, who after evaluating their situation, feel that they still want to expatriate either because they're not going to be deemed subject to the exit tax or they're willing to bear that cost.

(23:03):

For those people, it's important for them to recognize that in order to expatriate, you have to be in tax compliance for the five tax years prior to your expatriation. That means that people who have never filed tax returns or whose tax returns understate their tax liability or who failed to file these information returns that are an obligation under the Internal Revenue Code, they have to take action to basically cure their deficiencies before they do the expatriation. Because on their tax return, there is a penalty of perjury statement that basically says that you are in tax compliance for the prior five years to your expatriation.

(23:52):

In those situations, we assist the clients in coming into compliance for the prior five years so they're not in violation of that provision that they have to be in tax compliance. But it's a complicated situation. There are, as I said, many exceptions. All the facts and circumstances have to be evaluated. To take it one step further, Kate, I think that the most misunderstood part from the tax world of expatriation is not as much with the citizens who were accidental citizens born here, but people who are relinquishing their green card, because the process for relinquishing the green card under the immigration regime is different from what is required under the tax regime.

(24:49):

We see people who think they have expatriated and they haven't. That's when we have to work to bring them into tax compliance for the period when they stop filing, for example, because they thought they weren't permanent residents anymore, and then have to proceed to have them expatriated under the tax code.

Kate Kalmykov (25:13):

Let's delve deeper into that. I think we can break up permanent residents into two different categories. Short-term permanent residents that got the green card, changed their mind, gave it up within a certain amount of period of time, and long-term permanent residents that have had permanent residency for over seven years. Yes, that process is much different. From our point of view, you have to exit the country, send us your green card, and we submit what's called the form I-407 application for abandonment of residency. Usually, we get a response within one to two months saying, "Green card received. In our records, you are no longer a lawful permanent resident."

(25:57):

But as you said, that may not eliminate the tax liability or end your permanent residence status for tax purposes. Can you explain a little bit more on why that is and what clients should be aware of?

Barbara Kaplan (26:13):

Yes. Before I answer that question though, I want to mention that there are people who don't renew their green card, who think that they have expatriated as a consequence of not pursuing renewal of their card. That does not fly under the Internal Revenue Code. Once you're a permanent resident, whether your green card has expired or whether you fail to renew it, that does not terminate your residency for tax purposes. I think that's where the disconnect comes in the most. That people think that, "Well, I didn't renew my green card, so I'm not a permanent resident anymore." Or, "I provided the immigration people with an I-407, I'm done." For tax purposes, that's not true.

(27:11):

Under the Internal Revenue Code, there are additional steps that you need to take in order to basically give up your permanent residence status for tax purposes. As I said, the people that we see most who are out of compliance in that regard are people who just didn't renew their green card and thought, "Okay, I left the country. I didn't renew my green card. I'm finished." We've had to take steps to put them in a position where they actually are expatriating for US tax purposes, because for all those years when they weren't filing after they left, they think they're in compliance and they're not.

Kate Kalmykov (27:54):

I will tell you just in having done this for over two decades, no one has ever really done what you think at one point in time changes. We've had clients, like you said, they travel abroad, they don't renew, and then something happens, job opportunity, their children move, and now they want to return to the United States. They haven't properly terminated their status. They haven't been in tax compliance, and now they want to know, "Well, how do I come back? What status do I come back in? Is it going to be issued to me?" As we just discussed, this administration is looking very closely at all factors now in admissions at the border and in consular processing and issuance of visas.

(28:42):

They may be applying for a non-immigrant visa. They may be overseas for over a year where their status document has expired and they need to get what's called a returning resident visa. Now these questions come up at the consulate. It's very important to consult and get guidance beforehand to make sure that you're doing this properly. Unfortunately, for most clients, they don't. Then afterwards we're cleaning up a problem, which is much harder to do than doing this planning at the outset.

Barbara Kaplan (29:19):

Yeah, I was going to really make that same point, Kate. It's much easier to repair the damage before you've taken some action that's going to precipitate an inquiry, for example. The advice before you come back to the United States or before you pursue any kind of different immigration status, it's important to evaluate your tax filings and your compliance with the tax laws because doing it proactively in advance before there's an examination or an inquiry, whether it be from immigration that's sharing the information with IRS, it's much easier, less painful, and less costly if you address all those issues before you make a move.

Kate Kalmykov (30:11):

I would add that there's a lot of foreign countries now sharing information with the US too. Just assuming that I live halfway around the world, that they'll never know I have these bank accounts, maybe I spelled my name differently. We see that happen sometimes. Clients don't want to file an FBAR. They try to gain the system and unfortunately the reach is very long and there's a lot of cooperation globally.

Barbara Kaplan (30:40):

There is. We see it not only on the civil side of the Internal Revenue Service, but on the criminal side. The IRS special agents who work in making criminal tax cases against taxpayers, they have a lot of relationships around the world with local tax police, Interpol, all the criminal organizations, the anti-criminal organizations around the world. They are interacting with IRS special agents. They have conferences together, they share information, and so, the fact that you're in a foreign country is not protective.

Kate Kalmykov (31:26):

Absolutely. I will tell you that Department of State has also very similar resources. Agents actually will go to a work site to confirm work history that's being presented in an immigration application. They will interview people that you're associated with. They will show up at your residence to make sure that you really live there. Most people don't realize that they have the capability to do that, and they do that. Right now, vetting is extremely robust and a lot of resources are being devoted to it. Barbara, in closing, obviously, US citizenship, being a US person comes with a lot of amazing benefits. You get the ability to work and live in the United States.

(32:17):

You get the ability to take advantage of our educational institutions, which are some of the best in the world. We have a beautiful, large, diverse country, but there's also a lot of responsibilities that come with that as well, and taxation is one of them. In terms of closing thoughts to our viewers and listeners, what would you tell them about being an accidental American and staying in US tax compliance?

Barbara Kaplan (32:51):

I would say that they need to do that. The consequences may be unknown at the time that you're doing all of this, but somewhere down the road, there may be consequences from not being in tax compliance if you're an accidental American out of tax compliance, whether that means it's an audit, an examination. Oftentimes, a lot of this will arise in business transactions that you might be engaged in around the world. Certainly, we see a lot of issues raised when there are disputes among parties, whether they'd be business disputes or personal disputes, matrimonial disputes. Those are situations where disclosure of non-compliance becomes very risky.

(33:42):

In those situations in particular, which you can't anticipate necessarily today, but could be around tomorrow, it's important that you don't have that exposure that can be used against you in other aspects of your life, not just in tax compliance. Certainly, from a tax compliance point of view, the exposure is that you will become the subject of an IRS audit or an IRS investigation in connection with your activities. You don't want to be there, if you can avoid it by coming into compliance and staying in compliance as long as you're a US taxpayer.

Kate Kalmykov (34:23):

I think from what I see is, you can't work with your professionals in a vacuum. If you have an accountant and you're facing such issues, it's very important to get competent tax counsel, competent immigration council, and have them work really in tandem together, because you don't want to make mistakes or get the wrong advice just because somebody doesn't see the full picture of your exposure or liabilities.

Barbara Kaplan (34:51):

Absolutely.

Kate Kalmykov (34:54):

Thank you so much for joining me today, Barbara. We want you to come back and join us for a tax controversy podcast, but I really appreciate your insights.

Barbara Kaplan (35:03):

I'd be happy to do it. I'd be happy to do it. Thank you, Kate.

Kate Kalmykov (35:05):

Thank you.