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FATCA in Canada: The “Cure” for a U.S. Place of Birth

By

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Exhibit 1:

Explanation of Reason Account Holder Does Not Possess a Certificate of Loss of Nationality Despite Having Relinquished U.S. Citizenship

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Roy A. Berg¹

ABSTRACT

This paper provides analysis of one of the foundational elements of the Foreign Account Tax Compliance Act (FATCA) and various intergovernmental agreements (IGAs): an unambiguous place of U.S. birth and the ability to cure (Cure) this element, thereby rendering the account non-reportable. The IGAs generally allow the individual to Cure his unambiguous place of U.S. birth by producing a Certificate of Loss of Nationality (CLN) or by providing a “reasonable explanation” of why he does not have one despite having relinquished U.S. citizenship.

Unfortunately, however, none of the IGAs, FATCA, or legislative history provide guidance as to what might constitute a “reasonable explanation.” Analysis of this issue is deceptively difficult because (beginning in 2004) U.S. law differentiated the loss of U.S. citizenship for nationality purposes from the loss of U.S. citizenship for tax purposes. Further, FATCA and the IGAs use the tax definition of U.S. citizenship (and loss thereof), which incorporates elements of the nationality definition of U.S. citizenship.

This paper provides an analytical framework for determining the reasonableness of the explanation and provides a template that, the author hopes, will be useful in providing guidance on this issue. The paper also addresses the importance of clear guidance and harm that may result if an individual attempts to Cure his U.S. place of birth by seeking to obtain a CLN from the U.S. Department of State.

The harm that may result is based on the fact that a literal reading of current U.S. law deems the individual to lose his U.S. citizenship for tax purposes after, *inter alia*, giving notice to the Department of State which results in the issuance of a CLN, even though the issuance of a CLN is not required (and has never been required) to terminate U.S. citizenship for nationality purposes. Thus the individual who currently applies for a CLN may inadvertently find himself subject to income tax obligations and also the expatriation tax regime, even though he may have lost his U.S. citizenship for nationality purposes years (or decades) earlier.

Specifically the paper analyzes: (1) loss of U.S. citizenship for tax purposes and nationality purposes; (2) unambiguous place of U.S. birth; (3) cure for unambiguous place of U.S. birth; (4) what might constitute a “reasonable explanation” under the Treasury regulations and the IGA; (5) whether Canada has the authority to issue guidance on “reasonable explanation” under the IGA; (6) whether Canada should modify its Guidance Notes to clarify “reasonable explanation;” and (7) U.S. expatriation tax and the consequences of Curing a U.S. place of birth by obtaining a CLN.

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1. Introduction²

a. General introduction

The U.S.’s foreign account tax compliance act (FATCA)³ is an imposing and intimidating bit of legislation. While the statute itself is a spritely 13 pages, the 700 pages of accompanying regulations⁴ possess the type of heft that would impress even former sumo champion (and U.S. citizen) Akebono Tarō.⁵ As attorney Peter Cotorceanu deftly noted: “It’s a leviathan. And it breathes fire.”⁶

Fire-breathing leviathans are nothing new to tax practitioners. For example, Canada’s Foreign Accrual Property Income (FAPI) rules have been blamed for the thinning hair, expanding waistlines, and antacid consumption of scores of Canadian tax practitioners. However practitioners in Canada and world-wide (including the U.S.) have been slow to approach this leviathan. There are many perfectly logical reasons for the professional community’s slow approach, however the days of fiscal transparency are upon us and it is incumbent upon all tax practitioners to be able to identify the issues and advise their clients accordingly. Nobody said practicing tax was going to be easy, and since FATCA is only the start of global fiscal transparency, it is time to grab a sword and shield and approach the leviathan.

When stripped of its soul-crushing complexity, FATCA—including the Canada-U.S. intergovernmental agreement (the IGA) and the Canadian implementing legislation found in Part XVIII of the Canadian Income Tax Act (the Act)—is designed to identify U.S. citizens, U.S. residents, and U.S. entities and encourage them to become compliant with U.S. tax and filing obligations by reporting them either directly or indirectly to the IRS. With the exception of children born of certain diplomats, all persons born in the U.S. become U.S. citizens at birth.⁷ Thus, the

² For an in-depth analysis of Canada’s experience with the Foreign Account Tax Compliance Act, the Intergovernmental Agreement, and Canada’s implementing legislation, see Roy A. Berg and Paul M. Barba, “FATCA in Canada: Analyzing the Canadian Implementing Legislation’s Restriction on the Class of Entities Subject to FATCA,” 62:3 *Canadian Tax Journal* 587 (2014), available at http://www.ctf.ca/CTFWEB/EN/Publications/CTJ_Content/2014CTJ3.aspx.

³ Hiring Incentives to Restore Employment Act, Pub. L. no. 111-147, section 501 (Mar. 18, 2010), codified in sections 1471-1474 of the Internal Revenue Code of 1986, as amended (herein referred to as “the Code” or “IRC”).

⁴ TD 9610, 2013-15 IRB 765 (Apr. 8, 2013); TD 9657, 2014-13 IRB 884 (Mar. 24, 2014); TD 9658, 2014-13 IRB 895 (Mar. 24, 2014).

⁵ At 6 ft. 8 inches (203 cm) and 514 lb. (233 kg), Akebono was one of the tallest and heaviest sumo wrestlers of all time. He was the first non-Japanese-born sumo wrestler to reach *Yokozuna*, the highest rank in the sport. And he is a U.S. citizen, born Chad Rowan in Waimānalo, Hawai’i.

⁶ Peter A. Cotorceanu, “FATCA and Offshore Trusts: The First Nibble,” 139 *Tax Notes* 409, at 417 (Apr. 22, 2013). In addition to the *First Nibble*, Mr. Cotorceanu has undertaken the Herculean task of battling the leviathan in two other excellent expository articles. See Peter A. Cotorceanu, “FATCA and Offshore Trusts: a Second Bite of the Elephant,” 140 *Tax Notes* 1007 (Sept. 2, 2013); Peter A. Cotorceanu, “FATCA and Underlying Companies: Pin the Tail on the Elephant,” 142 *Tax Notes* 957 (Mar. 3, 2014).

⁷ U.S. CONST. amend XIV, § 1 (“All persons born or naturalized in the United States and subject to the jurisdiction thereof, are citizens of the United States.”). See also 8 U.S.C. section 1401(a). Only children born of foreign diplomats with full diplomatic immunity are exempt from this rule. See INS Interpretation 301.1(a)(4)(i).

clearest indicator of U.S. citizenship status is a place of U.S. birth. Once an individual has been identified as having an unambiguous place of U.S. birth, his account becomes reportable unless he “cures” (Cure) this indication of U.S. citizenship. By virtue of the IGA, an individual resident in Canada may Cure his U.S. place of birth by providing certain documentation, including a certificate of loss of nationality (CLN)⁸ or, if he does not possess a CLN, a reasonable explanation for not having one despite having relinquished his U.S. citizenship. To date, no guidance has been issued as to what constitutes a reasonable explanation for not having a CLN.

This paper analyzes a razor-thin slice of the FATCA leviathan predicated upon an individual having an unambiguous place of U.S. birth, and the problems that will likely arise if clear guidance is not provided that would allow financial institutions to efficiently evaluate the reasonableness of the individual’s explanation for not possessing a CLN. To that end, the paper addresses: (1) loss of U.S. citizenship for tax purposes and nationality purposes; (2) unambiguous place of U.S. birth; (3) cure for unambiguous place of U.S. birth; (4) what might constitute a “reasonable explanation” under the Treasury regulations and the IGA?; (5) whether Canada has the authority to issue guidance on “reasonable explanation” under the IGA; (6) whether Canada should modify its Guidance Notes to clarify “reasonable explanation;” and (7) U.S. expatriation tax and the consequences of curing a U.S. place of birth by obtaining a CLN.

The harm that may result to individuals who attempt to Cure their U.S. place of birth by obtaining a CLN is based in the dissonant concepts of loss of U.S. citizenship for nationality purposes and loss of U.S. citizenship for tax purposes. Under current U.S. law, an individual may have lost his citizenship for nationality purposes years ago, however he loses his tax-citizenship only after giving notice to the Department of State and the subsequent issuance of a CLN.⁹ Thus individuals who may have lost their U.S. citizenship for nationality purposes years, or decades, ago may find themselves subject to current income tax obligations or the expatriation tax regime because they failed to properly terminate their citizenship for tax purposes.

Importantly, FATCA and the IGA use the tax definition of U.S. citizen and not the definition that is used for nationality purposes. Specifically subparagraph 1(1)(ee) of the IGA provides that the term U.S. Person means a U.S. citizen “interpreted in accordance with the U.S. Internal Revenue Code.” Thus appreciation of the manner in which citizenship is lost for tax purposes is critical to understanding not only the Cure provision but FATCA in general.

While the topic of this paper is narrow, it addresses a foundational compliance problem currently faced by not only individuals who have a U.S. place of birth, but also the reporting Canadian financial institutions with which they interact.¹⁰

⁸ “Certificate of Loss of Nationality of the United States” is found on U.S. Department of State Form DS-4083.

⁹ Note, CLN is not required if a court in the United States cancels a citizen’s certificated of naturalization. IRC section 877A(g)(4)(D). In that case, citizenship for tax purposes is lost on the date of the court order. Since this is a narrow exception to the requirement for a CLN, and does not affect the analysis herein, it will not be addressed further.

¹⁰ The term “reporting Canadian financial institution” is defined in subsection 263(2) of the *Income Tax Act* (Canada), RSC 1985, c. 1 (5th Supp.), as amended (herein referred to as “the Act”). See also Agreement Between the Government of the United States of America and the Government of Canada to Improve International Tax Compliance through Enhanced Exchange of Information under the Convention Between the United States of America and Canada with Respect to Taxes on Income and on Capital, Feb. 5, 2014, at article 1(1)(f), available at <http://www.fin.gc.ca/treaties->

In order to adequately analyze this topic it is necessary to have an understanding of two technical and complex areas of U.S. law: loss of U.S. citizenship for nationality purposes, and loss of U.S. citizenship for tax purposes. The paper addresses these areas only insofar as they are relevant to FATCA, the IGAs, and the Cure of a place of U.S. birth. It does not provide a global review of either. However, there are numerous references to other resources for the reader to obtain more complete and nuanced understanding of these complex areas.

b. Brief FATCA introduction

On February 5, 2014, Canada and the United States executed the Canadian IGA, which relieves reporting Canadian financial institutions from many of the onerous obligations they would have otherwise faced under FATCA’s default regime.¹¹ That same day, the Department of Finance issued draft legislation required under Canadian law to implement the Canadian IGA. On February 11, 2014, a slightly modified version of the Department’s draft legislation was tabled in Canadian Parliament and the House of Commons Standing Committee on Finance began its meetings regarding the legislation on May 1, 2014, where the author of this paper was called to testify.¹² Subsequently, the Canadian implementing legislation received Royal Assent on June 19, 2014.¹³

FATCA is designed to deter and detect offshore tax evasion by persons subject to U.S. taxation.¹⁴ FATCA accomplishes its purpose by imposing reporting, withholding, and due diligence requirements on certain entities regarding those entities’ U.S. account holders and owners.

To understand the harm FATCA was designed to curtail, a brief overview of the U.S. income tax regime is in order. The United States is unique in that it taxes “United States person[s]” on their worldwide income.¹⁵ The Internal Revenue Code is written broadly to tax every person in the world. Specifically, the United States taxes “every individual” and “every corporation” on their income “from whatever source derived.”¹⁶ This means that they will be subject to U.S. income tax on any item of income they earn, regardless of where they live. Yet other provisions of the Code generally

[conventions/pdf/FATCA-eng.pdf](#) (herein referred to as “Canadian IGA”). The Canadian IGA defines terms by using capital letters; which will be altered in this paper for the sake of clarity.

¹¹ Canadian IGA, *supra* note 10.

¹² Bill C-31, An Act To Implement Certain Provisions of the Budget Tabled in Parliament on February 11, 2014 and Other Measures, first reading March 28, 2014 (herein referred to as either the “Canadian implementing legislation” or “the implementing legislation”).

¹³ Canadian Implementing Legislation, *supra* note 12.

¹⁴ See United States, Senate Committee on Homeland Security and Governmental Affairs, Permanent Subcommittee on Investigations, 110th Cong., 2d sess., *Tax Haven Banks and U.S. Tax Compliance: Staff Report* (Washington, DC: United States Senate, July 17, 2008), at 2 (www.hsgac.senate.gov/imo/media/doc/071708PSIReport.pdf?attempt=2); and statements of Senator Max Baucus, Chair, Senate Committee on Finance, regarding a prior version of FATCA, *Congressional Record*, October 27, 2009, at S10785.

¹⁵ IRC sections 1, 11, 641, 701, and 7701(b)(1); Treasury regulation section 1.1-1(b).

¹⁶ IRC sections 1(a), 11(a), 61(a), 63.

limit worldwide income taxation to United States persons.¹⁷ A United States person is generally a U.S. citizen or resident, a domestic corporation or partnership, or a U.S. resident estate or trust.¹⁸

Notably, U.S. citizenship for tax purposes is determined by reference to U.S. immigration law,¹⁹ which provides that individuals born in the United States are U.S. citizens.²⁰ However an individual is deemed to lose his U.S. citizenship for tax purposes only after he completes specific notification requirements after losing his citizenship for nationality purposes, which result in the issuance of a CLN. This is important to remember while trundling through FATCA’s specific rules because FATCA was largely designed to identify U.S. citizens to fulfill its purpose of detecting and deterring tax evasion.

2. Loss of U.S. Citizenship for Tax Purposes and Nationality Purposes

a. Inconsistent nomenclature: “renounce,” “relinquish,” and “expatriate”

Before addressing the differences between loss of U.S. citizenship for tax purposes and nationality purposes, it is worthwhile to address a confusing aspect of this topic, which is inconsistent nomenclature. The terms renounce, relinquish, and expatriate all have a common vernacular meaning, which is “loss of citizenship,” and when used in the vernacular the terms are frequently used interchangeably.

However, these terms also have independent legal significance when used in the nationality context (U.S. *Immigration and Nationality Act* (the INA))²¹ and an even different meaning when used in the tax context (U.S. Internal Revenue Code (the IRC))²². To make matters even more confounding, it is not always clear whether the terms have their vernacular meaning or their defined meaning under the IRC or INA.

i. “Renounce” citizenship

The least ambiguous defined term to understand is “Renounce.” Under the INA an individual loses his U.S. citizenship when he formally “renounces” before a U.S. Consular official.²³ In order to do

¹⁷ IRC sections 2(d), 11(d), 7701(a)(5), (b)(1), and (a)(30).

¹⁸ IRC section 7701(a)(30).

¹⁹ Treasury regulation section 1.1-1(c), which provides: “Every person born or naturalized in the United States and subject to its jurisdiction is a citizen. For other rules governing the acquisition of citizenship, see chapters 1 and 2 of title III of the Immigration and Nationality Act (8 U.S.C. 1401-1459). For rules governing loss of citizenship, see sections 349 to 357, inclusive, of such Act (8 U.S.C. 1481-1489), *Schneider v. Rusk*, (1964) 377 U.S. 163, and *Rev. Rul. 70-506*, C.B. 1970-2, 1. For rules pertaining to persons who are nationals but not citizens at birth, e.g., a person born in American Samoa, see section 308 of such Act (8 U.S.C. 1408). For special rules applicable to certain expatriates who have lost citizenship with a principal purpose of avoiding certain taxes, see section 877. A foreigner who has filed his declaration of intention of becoming a citizen but who has not yet been admitted to citizenship by a final order of a naturalization court is an alien.”

²⁰ 8 U.S.C. section 1401(a).

²¹ Title 8 of the United States Code (8 U.S.C.)

²² Title 26 of the United States Code (26 U.S.C.)

²³ 8 U.S.C. section 1481(a)(5); see also 7 *Foreign Affairs Manual* 1200 (Loss and Restoration of U.S. Citizenship).

so, the individual is required to appear before a consular official and express his present and voluntary intent to lose his citizenship. Under the IRC, the term “renounce” refers back to the INA.²⁴

ii. “Relinquish” citizenship

Under the INA an individual “relinquishes” his U.S. citizenship by voluntarily performing one of six prescribed acts with the present intent of losing his U.S. citizenship.²⁵ Under the INA, there is little difference between the terms “renounce” and “relinquish.” As noted in the Foreign Affairs Manual:

The distinction [between relinquish and renounce] becomes meaningful when a person who has been found to have lost U.S. citizenship later requests an appeal or administrative review of that decision.²⁶

However, under current U.S. tax law “relinquish” is a defined term, the meaning of which is different than that used in the INA. Under current tax law, an individual does not cease to be treated as a U.S. citizen until the date on which his citizenship is treated as “relinquished,” which requires the individual to notify the Department of State.²⁷

iii. “Expatriate”

The INA does not define the term “expatriate” and it has, and has had, various meanings under the IRC. First, current section 877A(g)(2) provides that the term “expatriate” means: “any United States citizen who relinquishes his citizenship, and any long-term resident of the United States who ceases to be a lawful permanent resident of the United States (within the meaning of section 7701(b)(6)).”²⁸

Second, in 2008 the notification provisions enacted in 2004 were repealed and the current notification requirements were adopted. The notification requirements under current law do not apply to individuals whose “expatriation date” is on or before June 17, 2008. “Expatriation date” now refers to the current notification provisions found in section 877A(g)(4).²⁹

Third, in 2004 the IRC was changed to provide that an individual’s U.S. citizenship for tax purposes did not cease until he notified both the Department of State and the IRS. This new notification provision was effective only for individuals who “expatriated” after June 3, 2004. The term “expatriated” was not defined and, presumably, carried its vernacular meaning.

²⁴ IRC section 877A(g)(4)(a). Note that one of the defined acts is a formal renunciation before a Consular official.

²⁵ 8 U.S.C. section 1481(a). The seven acts that can result in the loss of U.S. citizenship for nationality purposes are listed in section 2(d) of this paper.

²⁶ 7 *Foreign Affairs Manual* 1211, at 3 (Loss and Restoration of U.S. Citizenship: Summary).

²⁷ IRC sections 7701(a)(50)(A) and 877A(g)(4).

²⁸ Note that the “expatriate” definition also includes the term “relinquish.”

²⁹ The defined term “Covered expatriate” is also defined in IRC section 877A(g)(1)(A).

b. Loss of U.S. citizenship for tax purposes

Prior to 2004 an individual’s tax-citizenship terminated at the same time as his nationality-citizenship. However, in 2004, under the American Jobs Creation Act (AJCA)³⁰ Congress changed this by introducing the concept of loss of U.S. citizenship for tax purposes. These new rules in the AJCA that defined loss of U.S. citizenship for tax were amended in 2008 pursuant to the Heroes Earnings Assistance and Relief Tax Act (HEART).³¹ It’s important to understand the manner in which tax-citizenship terminates under these two acts because they have different notice provisions, which apply differently depending on when the individual lost his citizenship for nationality purposes. The following analysis addresses solely the date on which U.S. citizenship is lost for tax purposes. Analysis of the tax consequences of losing U.S. citizenship, including the expatriation tax regime, is addressed in sections 8 and 9.

i. American Jobs Creation Act (AJCA) 2004

The AJCA enacted IRC section 7701(n),³² which provided that an individual would continue to be treated as a U.S. citizen for tax purposes until the individual gave notice that he had committed an expatriating act (with the intent to relinquish citizenship) to the Department of State and the IRS. Specifically the statute provided:

(1) United States citizens. An individual who would (but for this paragraph) cease to be treated as a citizen of the United States shall continue to be treated as a citizen of the United States until such individual

(A) gives notice of an expatriating act (with the requisite intent to relinquish citizenship) to the Secretary of State, and

(B) provides a statement in accordance with section 6039G (if such a statement is otherwise required).

Importantly, however, the new notice requirements applied only to individuals who “expatriated” after June 3, 2004.³³ The term “expatriate” was not defined in the legislative history, AJCA, or Treasury regulations. In context the term made sense only if ascribed the vernacular definition of “loss of citizenship.”

Thus an individual who lost citizenship for nationality purposes after June 3, 2004 would lose his tax-citizenship only after providing the appropriate notice to the Department of State and IRS. Conversely, an individual who lost citizenship for nationality purposes prior to June 3, 2004 would cease to be taxed as a U.S. citizen coincident with his nationality status.

³⁰ American Jobs Creation Act of 2004, Pub. L. no. 108-357, section 804 (herein referred to as “AJCA”).

³¹ Heroes Earnings Assistance and Relief Tax Act of 2008, Pub. L. no. 110-245, section 501(a) (herein referred to as “HEART”).

³² IRC section 7701(n) (repealed in 2008).

³³ Supra note 30 at section 804(f).

ii. Heroes Earnings Assistance and Relief Tax Act (HEART) 2008 – analysis for individuals who were not dual citizens at birth

HEART (which is current law) repealed the notice requirements of 7701(n) and enacted numerous changes to the date on which U.S. citizenship is lost for tax purposes. First, new section 7701(a)(50)(A) provides that an individual shall not cease to be treated as a U.S. citizen before the date on which the individual’s citizenship is treated as relinquished under 877A(g)(4). Second, new section 877A(g)(3) provides that an individual’s expatriation date is the date on which he “relinquishes” U.S. citizenship. New section 877A(g)(4) defines “relinquishment” of U.S. citizenship for tax purposes as follows:

(4) Relinquishment of citizenship. A citizen shall be treated as relinquishing his United States citizenship on the earliest of

(A) the date the individual renounces his United States nationality before a diplomatic or consular officer of the United States pursuant to paragraph (5) of section 349(a) of the Immigration and Nationality Act (8 U.S.C. 1481(a)(5)),

(B) the date the individual furnishes to the United States Department of State a signed statement of voluntary relinquishment of United States nationality confirming the performance of an act of expatriation specified in paragraph (1), (2), (3), or (4) of section 349(a) of the Immigration and Nationality Act (8 U.S.C. 1481(a)(1)-(4)),

(C) the date the United States Department of State issues to the individual a certificate of loss of nationality, or

(D) the date a court of the United States cancels a naturalized citizen’s certificate of naturalization.

Subparagraph (A) or (B) shall not apply to any individual unless the renunciation or voluntary relinquishment is subsequently approved by the issuance to the individual of a certificate of loss of nationality by the United States Department of State.

Thus HEART changed the termination of citizenship for tax purposes in three significant ways.

First, tax-citizenship is not terminated unless a CLN has been issued. The flush language of section 877A(g)(4) provides that either renouncing U.S. citizenship before a diplomatic or Consular officer, or furnishing a statement confirming the voluntary commitment of one of four expatriating acts³⁴ is ineffective to terminate tax-citizenship unless approved by the Department of State’s issuance of a CLN.³⁵

³⁴ IRC section 877A(g)(4)(B), referring to the expatriating acts listed in 8 U.S.C. 1481(a)(1), (2), (3), or (4). Those acts are (1) becoming naturalized in a foreign country, (2) formally declaring allegiance to a foreign country, (3) serving in a foreign army, and (4) serving in certain types of foreign government employment if the individual is a national of the foreign country or takes an oath of allegiance to that foreign country. See *infra*, section 2(d) of this paper.

³⁵ The only exception to the requirement of a CLN would be when a U.S. court cancels a naturalized citizen’s certificate of naturalization. IRC section 877A(g)(4)(D). While an important section for those who obtained U.S. citizenship by naturalization, I will not discuss it further in this paper.

Second, HEART repealed the obligation to give notice to the IRS in order to terminate tax-citizenship status.³⁶

Third, HEART refined the “effective date” for loss of tax-citizenship. Under section 7701(n) tax-citizenship was lost upon giving notice to both the Department of State and the IRS. Since the notice provisions were conjunctive, the later of the two notice provisions established the loss of tax-citizenship. Under HEART, however, tax-citizenship is lost on the earlier of renouncing before a diplomatic or consular officer (provided such results in the issuance of a CLN), delivering a statement confirming a prior expatriating act (provided such results in the issuance of a CLN), or the issuance of a CLN.³⁷

At first blush the new rules for termination of tax-citizenship under HEART appear to apply prospectively. However, a close (and admittedly literal) reading of the statute reveals that, for practical purposes, it applies retroactively as well. Under HEART the new rules for termination of tax-citizenship are effective for individuals whose “expatriation date” is after June 17, 2008.³⁸ The individual’s “expatriation date” (877A(g)(3)) is determined by the date on which the individual “relinquishes” U.S. citizenship (877A(g)(4)), and the individual “relinquishes” citizenship on the earlier of giving notice to the Department of State (either by renouncing before a diplomatic or consular official, or submitting a statement confirming an expatriating act) or the issuance of a CLN.

Thus, the only individuals who are not subject to the new rules for loss of tax-citizenship are those who, before June 17, 2008: 1) received a CLN; or 2) who renounced before a diplomatic or consular officer; or 3) submitted a statement confirming a prior expatriating act; provided such statement or renunciation results in the issuance of a CLN. For example:

Mr. Maple Leaf is born in the United States in 1962 and naturalizes as a Canadian citizen in 1982. At the time of his naturalization in Canada he takes an oath of citizenship and voluntarily intends to lose his U.S. citizenship. He does not inform the Department of State or the IRS and he has not been issued a CLN. For nationality purposes Mr. Maple Leaf’s U.S. citizenship ends in 1982.

Under AJCA Mr. Maple Leaf’s tax-citizenship terminated in 1982 because he “expatriated” (which was an undefined term under AJCA) prior to June 3, 2004.³⁹

However, under HEART (current law), Mr. Maple Leaf is still a tax-citizen because before June 17, 2008 he did not: 1) receive a CLN; 2) renounce before a diplomatic or consular officer; or 3) submit a statement confirming a prior expatriating act that resulted in the issuance of a CLN.⁴⁰

³⁶ However, per IRC section 877(a)(2)(c) the individual must provide a certification to the IRS in order to avoid status as a “covered expatriate” and therefore the expatriation tax, however this requirement does not affect the termination of his tax-citizenship status.

³⁷ IRC sections 7701(a)(50); 877A(g)(4).

³⁸ IRC section 877(h).

³⁹ Supra, note 30.

⁴⁰ See section 9(b) of this paper for criticism of this result.

iii. HEART 2008 – analysis for individuals who were dual citizens at birth

The foregoing analysis applies to U.S. citizens who were not born a dual citizen. However, HEART exempts from that analysis individuals who, at birth, were dual citizens. IRC section 7701(a)(50)(B) provides:

(B) Dual Citizens. Under regulations prescribed by the Secretary, subparagraph (A) shall not apply to an individual who became at birth a citizen of the United States and a citizen of another country.

To date no regulations have been issued to address the loss of tax-citizenship for individuals who were dual citizens at birth. It is important to note, however, that the IRS’s rule-making authority is prescribed by section 7805, which limits the application of regulations issued by the IRS to a prospective basis.

For a limited group of individuals who were dual citizens at birth, however, there is a glimmer of hope. On February 2, 2015 the Obama Administration released its budget proposal for 2016 that contained a proposal that would allow certain dual citizens to renounce their U.S. citizenship without the fear of the consequences of delinquent tax returns, penalties, and the U.S. expatriation tax regime. The proposal could be given the force of law by being either: 1) issued as a regulation pursuant to IRC section 7701(a)(50)(B); or 2) accepted by both houses of Congress and signed by the president. To date, however, there is no indication that the proposal will be given the force of law by either method.⁴¹

c. Loss and restoration of U.S. citizenship because of judicial or legislative action⁴²

U.S. nationality law used to be replete with a multitude of statutes under which an individual would automatically lose his U.S. citizenship by performing, or not performing, certain acts, regardless of the individual’s intent at the time.⁴³ In 1967, however, the Supreme Court of the United States held that the Fourteenth Amendment to the U.S. Constitution precluded the automatic loss of citizenship unless the individual performed the requisite action (or inaction) voluntarily and with the specific intent of relinquishing U.S. citizenship.⁴⁴ Thus many individuals who had been stripped of their U.S.

⁴¹ United States, Department of the Treasury, General Explanations of the Administration’s Fiscal Year 2016 Revenue Proposals, (February 2015), at 283, <http://www.treasury.gov/resource-center/tax-policy/Documents/General-Explanations-FY2016.pdf>. Andrew Velarde, “Budget Proposal May Offer Escape from U.S. Tax for Dual Citizens,” 146 *Tax Notes* 709 (Feb. 9, 2015). See also Roy Berg, “U.S. Proposes Relief for Some who Renounce U.S. Citizenship: is FATCA a Motivating Factor?,” *Moody’s Gartner Tax Law Blog*, Feb. 11, 2015, <http://www.moodysgartner.com/us-proposes-relief-for-some-who-renounce-us-citizenship-is-FATCA-a-motivating-factor/>.

⁴² An excellent, and entertaining, summary of the evolution of U.S. Supreme Court decisions on the loss of nationality can be found in 7 *Foreign Affairs Manual* 1200, Appendix B.

⁴³For example, under the Expatriation Act of 1907, a U.S. citizen woman who married a foreigner would automatically lose her U.S. citizenship if she took the nationality of her husband. 8 U.S.C. 1484, declared unconstitutional in *Schneider v. Rusk*, 377 U.S. 163 (1964); repealed retroactively Pub. L. No. 95-432 on October 10, 1978. Further, a naturalized U.S. citizen would automatically lose his U.S. citizenship if he left the U.S. and became a resident of his country of origin for a period three years. *Ibid*.

⁴⁴ *Afroyim v. Rusk*, 387 U.S. 253 (1967).

citizenship found it to have been restored retroactively. Since the U.S. taxes its citizens on their worldwide income, the problem created by retroactive restoration of citizenship should be apparent. The tax effect of loss of nationality under these circumstances is analyzed below in section 8(a) of this paper.

d. Loss of U.S. citizenship for nationality purposes

Under current law, termination of U.S. citizenship for nationality purposes is addressed in 8 U.S.C. section 1481(a). First impressions of the INA make it appear that loss of citizenship requires relatively straightforward analysis: individuals may lose their U.S. citizenship for nationality purposes by voluntarily performing any of the following acts, provided such act is concurrent with the intent of relinquishing U.S. nationality:

(a) A person who is a national of the United States whether by birth or naturalization, shall lose his nationality by voluntarily performing any of the following acts with the intention of relinquishing United States nationality -

1. obtaining naturalization in a foreign state upon his own application or upon an application filed by a duly authorized agent, after having attained the age of eighteen years; or
2. taking an oath or making an affirmation or other formal declaration of allegiance to a foreign state or a political subdivision thereof, after having attained the age of eighteen years; or
3. entering, or serving in the armed forces of a foreign state if: A) such armed forces are engaged in hostilities against the United States; or B) such persons serve as a commissioned or non-commissioned officer; or
4. A) accepting, serving in, or performing the duties of any office, post, or employment under the government of a foreign state or a political subdivision thereof, after attaining the age of eighteen years if he has or acquires the nationality of such foreign state; or B) accepting, serving in, or performing the duties of any office, post, or employment under the government of a foreign state or a political subdivision thereof, after attaining the age of eighteen years for which office, post, or employment an oath, affirmation, or declaration of allegiance is required; or
5. making a formal renunciation of nationality before a diplomatic or consular officer of the United States in a foreign state, in such form as may be prescribed by the Secretary of State; or
6. making in the United States a formal written renunciation of nationality in such form as may be prescribed by, and before such officer as may be designated by, the Attorney General, whenever the United States shall be in a state of war and the Attorney General shall approve such renunciation as not contrary to the interests of national defense; or
7. committing any act of treason against, or attempting by force to overthrow, or bearing arms against, the United States, violating or conspiring to violate any of the provisions of section 2383 of title 18, or willfully performing any act in violation of section 2385 of title 18, or violating section 2384 of title 18 by engaging in a conspiracy to overthrow, put down, or to destroy by force the Government of the United States, or to levy war against them, if and when he is convicted thereof by a court martial or by a court of competent jurisdiction.⁴⁵

Anyone who asserts loss of nationality (whether the asserting party is the individual or the U.S. Department of State) must prove such by a preponderance of the evidence.⁴⁶ Further, any individual

⁴⁵ 8 U.S.C. section 1481(a).

⁴⁶ 8 U.S.C. section 1481(b).

who commits any of the foregoing seven expatriating acts is presumed to have done so voluntarily, however the presumption may be rebutted by showing by a preponderance of the evidence that such acts were not done voluntarily.⁴⁷

As is frequently the case, simplicity in presentation belies complexity in operation: U.S. law regarding the loss of citizenship for nationality purposes has evolved greatly and all of the expatriating acts listed above have been modified by jurisprudence and administrative interpretation and are not as straight forward as they appear.⁴⁸

For example, since 1990 the Department of State has held an administrative presumption that, despite the language of the INA, U.S. nationals actually intend to retain citizenship when they naturalize in a foreign state, perform a routine oath of allegiance in a foreign state, serve in the armed forces of a foreign state not engaged in hostilities with the U.S., or accept non-policy level employment with a foreign government. Unless a person explicitly asserts that one of these acts was performed with the intent to relinquish U.S. nationality or engages in other conduct inconsistent with retention of U.S. citizenship, he or she will retain U.S. nationality.⁴⁹

Many older statutes have been declared unconstitutional by the Supreme Court of the United States, some have been repealed by Congress, and sometimes the changes to the law are given retroactive effect and sometimes not. Notably, if a person was determined to have lost U.S. citizenship under a prior expatriating statute, their citizenship is not restored by subsequent legislative amendments if the loss was consistent with the constitutional requirement that the act must have been performed with the intention to relinquish citizenship.⁵⁰

In addition to the above, citizenship was unintentionally lost by some as a consequence of residency requirements formerly imposed on children born abroad to one U.S. citizen and one alien parent. Beginning in 1934, such individuals automatically lost U.S. citizenship if they failed to reside in the U.S. for a set period of time (which varied depending on the circumstances) between the ages 14 and 28.⁵¹ These requirements were repealed prospectively in 1978 and the INA now provides that individuals having lost citizenship under these provisions may re-obtain it by taking an oath of allegiance.⁵²

⁴⁷ Ibid.

⁴⁸ Two excellent resources that analyze the detail and nuance surrounding loss of U.S. citizenship for nationality purposes are Steve Trow, *U.S. Immigration and Citizenship Planning for High Net Worth Clients*, International Trust and Estate Planning, American Law Institute (October 20, 2014, San Francisco); and 7 *Foreign Affairs Manual* 1200 (Loss and Restoration of U.S. Citizenship).

⁴⁹ 7 *Foreign Affairs Manual* 1222 (Loss and Restoration of U.S. Citizenship: Administrative Presumption)

⁵⁰ INA section 405(c), 8 U.S.C. section 1101.

⁵¹ Revised Statutes (RS) 797; *repealed prospectively* December 24, 1952, Pub. L. 95-432. See also 7 *Foreign Affairs Manual* 1200, Appendix C (Loss and Restoration of U.S. Citizenship; Taking up Residence abroad, Loss of Nationality, Dual Nationals, and Naturalized Citizens).

⁵² INA section 324(d)

It also use to be the case that citizenship could be lost by dual citizens born in the U.S. who voluntarily sought and claimed the benefit of foreign citizenship and resided in that foreign country for at least three years after their 22nd birthday. This provision was enacted on December 24, 1952 and was repealed on October 10, 1978. It applied to individuals born on or after the date of enactment who resided in the foreign country for at least three years prior to the date of repeal.⁵³

3. Unambiguous Place of U.S. birth

Annex I of the IGA sets forth the due diligence procedures that reporting Canadian financial institutions must undertake in order to identify U.S. reportable accounts. Specifically, if an account holder has an unambiguous place of U.S. birth, the account is a reportable account.⁵⁴ The Guidance Notes⁵⁵ take a bifurcated approach to what constitutes an unambiguous place of U.S. birth depending on the due diligence required under the circumstances.

For preexisting individual accounts that are subject to a digital records search, an individual has an unambiguous place of U.S. birth only if the country of birth is shown. If the country of birth is not shown then the place of birth is not unambiguous.⁵⁶ For example, if the digital records search shows a place of birth to be New York, New York, then the place of birth is not unambiguous (because it does not indicate “USA”) and the account will not be a reportable account. Conversely, if the digital records search shows a place of birth to be New York, New York, USA, then the place of birth is unambiguous and will be a reportable account unless Cured.⁵⁷

For existing high-dollar accounts or where a paper search is required, a U.S. place of birth is unambiguous only if the United States would be the only place of birth “without formal review.”⁵⁸ For example, if “Georgia” is identified as a person’s place of birth, without reference to the United States, the place of birth is ambiguous and not reportable. The Guidance Notes do not yet explain either: 1) what is contemplated by the phrase “without formal review” or 2) whether including a city within Georgia (Atlanta, for example) would cause the place of birth to become unambiguous.

For accounts opened after June 30, 2014 and not otherwise exempt from FATCA’s due diligence requirements, the individual account holder will be required to self-certify his U.S. citizenship status. If the individual certifies that he is not a U.S. person, however account opening information reveals

⁵³ Revised Statutes (RS) 797; *repealed prospectively* December 24, 1952, Pub. L. 95-432. See also 7 *Foreign Affairs Manual* 1200, Appendix C (Loss and Restoration of U.S. Citizenship; Taking up Residence abroad, Loss of Nationality, Dual Nationals, and Naturalized Citizens).

⁵⁴ Canadian IGA, *supra* note 10, annex I (II)(B)(1)(b).

⁵⁵ CRA, *Guidance on Enhanced Financial Account Information Reporting – Part XVIII of the Income Tax Act* (June 20, 2014), available at <http://www.cra-arc.gc.ca/tx/nnrndnts/nhncdrprtrng/gdnc-eng.pdf> (herein referred to as “Guidance Notes”).

⁵⁶ CRA Guidance Notes, *supra* note 55, at 8.28.

⁵⁷ Of course “not unambiguous” does not necessarily have the same meaning as “ambiguous,” however for this discussion the distinction lacks a difference. While the term “not unambiguous” is more precise than the term “ambiguous” abandoning the double negative doesn’t not enhance the clarity the prose (raise your hand if you get the joke).

⁵⁸ CRA Guidance Notes, *supra* note 55, at 8.47.

an unambiguous place of U.S. birth then the account is reportable unless it is Cured.⁵⁹ The relevant standards for determining unambiguity include, among others, the account balance and whether the individual is an existing customer.⁶⁰

4. Cure for an Unambiguous Place of U.S. birth

a. Cure is limited to preexisting individual accounts, though Guidance Notes broaden applicability

Not all accounts are eligible for the Cure provision analyzed herein. The Cure provision is found only in Annex I(II)(B)(4) of the IGA and only in subsection 265(5) of the Act. These areas of the IGA and the Act address due diligence procedures only for pre-existing individual accounts. None of the due diligence procedures for any other type of account (new individual accounts, existing entity accounts, and new entity accounts)⁶¹ expressly contain or refer back to the Cure provision for existing individual accounts, however, notably none of such procedures expressly preclude use the Cure provision either. Notably absent (though not expressly precluded) from application of the Cure provision is the situation where a financial institution has determined that a U.S. citizen is a controlling person of a passive non-financial foreign entity, in that case “the account shall be treated as a U.S. Reportable Account.”⁶²

Importantly, while the relevant provisions of the IGA and Act implicitly limit the Cure provision, the Guidance Notes do specifically allow the financial institution to apply the Cure provision to new individual accounts,⁶³ though new or existing entity accounts in which a U.S. citizen is a controlling person do not specifically incorporate (or preclude) the Cure provision.

While the ability to Cure an unambiguous place of U.S. birth is implicitly limited under FATCA, the IGA, and the Act, the Guidance Notes take a reasonable and practical approach by broadening its applicability. It would be even more reasonable and practical to explicitly amend the Guidance Notes to expand the ability use the Cure provision in any relevant context.

b. Comparison of Cure provisions under the IGA and Treasury Regulations

Under the Treasury regulations, the IGA, and the Guidance Notes, an unambiguous place of U.S. birth may be Cured for individuals if the financial institution obtains (and keeps record of):

1. A self-certification showing that the account holder is not a U.S. citizen (as defined for tax purposes and not for nationality purposes);

⁵⁹ Ibid, Guidance Notes at 9.13.

⁶⁰ Ibid.

⁶¹ Canadian IGA, *supra* note 10 Annex I (III) (*New Individual Accounts*), Annex I (IV) (*Preexisting Entity Accounts*), Annex I (V) (*New Entity Accounts*).

⁶² Ibid annex I(IV)(C)(4)(d). “If any Controlling Person of a Passive NFFE is a U.S. citizen or resident, the account shall be treated as a U.S. Reportable Account.”

⁶³ CRA Guidance Notes, *supra* note 55 at 9.13.

2. Evidence of the individual’s citizenship in another country (e.g., passport or other government-issued identification); and
3. A copy of the individual’s CLN.

If the individual is unable to produce a CLN, he may still Cure under the IGA and the Treasury regulations, however, there are subtle but important differences between the Treasury regulations, the IGA, and the Guidance Notes. The following table highlights these differences.

“Cure” under the Treasury regulations	“Cure” under the IGA and the Guidance Notes
A withholding certificate; ⁶⁴	A self-certification that the account holder is neither a U.S. citizen nor a U.S. resident for tax purposes (which may be on an IRS Form W-8 or other similar agreed form);
a non-U.S. passport or other government-issued identification evidencing the account holder’s citizenship or nationality in a country other than the United States; and	a non-U.S. passport or other government-issued identification evidencing the account holder’s citizenship or nationality in a country other than the United States; and
either a copy of the account holder’s CLN or a reasonable written <i>explanation</i> of: <ol style="list-style-type: none"> 1. the account holder’s <i>renunciation</i> of U.S. citizenship; or 2. the reason the account holder did not obtain U.S. citizenship at birth.⁶⁵ 	either a copy of the account holder’s CLN or a reasonable <i>explanation</i> of: <ol style="list-style-type: none"> 1. the reason the account holder does not have a CLN despite <i>relinquishing</i> U.S. citizenship; or 2. the reason the account holder did not obtain U.S. citizenship at birth.⁶⁶

The two most important differences in the respective Cure provisions are: 1) The Treasury regulations use the term “renunciation” while the IGA uses the term “relinquish;” 2) The subject matter of the “reasonable explanation:” the Treasury regulations require the individual to explain his renunciation of U.S. citizenship; while the IGA requires him to explain the reason he does not have a CLN despite relinquishing U.S. citizenship. Before addressing these differences, however, it is worth noting that both Cure provisions require a reasonable “explanation” and not a reasonable “excuse.”

c. Difference between “explanation and “excuse”

“Excuse” and “explanation” have similar but different meanings and it is logically fallacious to conflate the two. Generally an “excuse” is a justification for an act or omission that relieves the

⁶⁴ Treasury regulation section 1.1471-4(c)(5)(iv)(B)(2)(ii).

⁶⁵ IRC section 1471; Treasury regulation sections 1.1471-3(e)(4)(ii)(C) (accounts opened before January 1, 2014); 1.1471-3(e)(4)(iv)(C)(1) (accounts opened on or after January 1, 2014); and 1.1471-4(c)(5)(iv)(B)(2)(ii) (unambiguous indication of a U.S. place of birth).

⁶⁶ Canadian IGA, *supra* note 10, annex I (II)(B)(4)(a); CRA Guidance Notes, *supra* note 55, 8.27.

individual from culpability for the act or omission,⁶⁷ while an “explanation” is simply a rendition of the facts and circumstances relating to a matter and does not affect culpability. For example, ignorance does not “excuse” an individual from violating the law, however ignorance may “explain” why the individual violated the law. Both Cure provisions require an explanation from the individual and, while the explanation must be reasonable, it need not rise to the level of an “excuse” for the matter addressed.

d. The IGA uses the term “relinquish,” the Treasury regulations use the term “renounce,” however the Guidance Notes omit both terms

i. “Relinquish” is not defined in the IGA

As discussed in section 2(a) of this paper, the terms “renounce” and “relinquish” have both a vernacular meaning and also a meaning with independent legal significance in the INA and IRC, however they are frequently used interchangeably. For nationality purposes, they both refer to the same result, which is the loss of citizenship, however each term refers to a different method of achieving the result.

The Cure provision in the Treasury regulations requires the individual to explain his “renunciation” of citizenship. An individual renounces his citizenship when he formally expresses his present and voluntary intent to lose his citizenship before a U.S. Consular official.⁶⁸

In contrast, the Cure provision in the IGA requires the individual to explain his reason for not possessing a CLN despite having “relinquished” citizenship. In the nationality context, an individual relinquishes his citizenship when he informs the Department of State that he performed an expatriating act (with the proper intent) at some time in the past.⁶⁹

As discussed above, “relinquish” has a unique meaning for tax purposes. Under current U.S. tax law an individual is not treated as having lost his citizenship for tax purposes until he “relinquishes” his U.S. citizenship and satisfies the various notice provisions of 877A(g)(4).⁷⁰ Further, subparagraph 1(1)(ee) of the IGA provides that the term U.S. Person includes a U.S. citizen “interpreted in accordance with the U.S. Internal Revenue Code.”⁷¹ Consequently, an argument could be made that U.S. citizenship, including the termination thereof, should be determined by using tax principles.

However, there is little in the public record that indicates Treasury intended to assign different meanings to “renounce” and “relinquish.” To the contrary, it appears that the terms are used in the vernacular context to mean simply “loss of U.S. citizenship.” If Treasury had intended different

⁶⁷ *West's Encyclopedia of American Law*, 2d (2008), retrieved February 22 2015 from <http://legal-dictionary.thefreedictionary.com/excuse> (“An excuse is essentially a defense for an individual's conduct that is intended to mitigate the individual's blameworthiness for a particular act or to explain why the individual acted in a specific manner”).

⁶⁸ 8 U.S.C. section 1481(5); see also 7 *Foreign Affairs Manual* 1200 (Loss and Restoration of U.S. Citizenship).

⁶⁹ 8 U.S.C. section 1481.

⁷⁰ IRC section 7701(a)(50)(A).

⁷¹ Canadian IGA, *supra* note 10 at article 1(1)(ee).

meanings for the terms, a reasonable person would think that the distinction would be noted clearly in the Treasury regulations, IGA, or someplace in the legislative history. Since there is none, and since the terms are frequently used interchangeably it would be reasonable to conclude that in this context they both simply mean “loss of U.S. citizenship.”

The term “relinquish” is not included in the definitional section of the IGA, however paragraph 1(2) provides:

Any term not otherwise defined in this Agreement shall, unless the context otherwise requires or the Competent Authorities agree to a common meaning (as permitted by domestic law), have the meaning that it has at the time under the law of the Party applying this Agreement, any meaning under the applicable tax laws of that Party prevailing over a meaning given to the term under the other laws of that Party.

In context, the term “relinquish” in the IGA is unclear: it could have the vernacular meaning, the tax meaning, or nationality meaning. Thus the competent authorities would have to agree on a meaning and, if not, the party applying the agreement (Canada or any other IGA jurisdiction) would be free to look to its domestic law to define the term. Fortunately, Canada appears to have done so in its Guidance Notes.

ii. Canada’s Guidance Notes omit the phrase “despite relinquishing U.S. citizenship”

Section 8.27 of Canada’s Guidance Notes addresses the Cure provision and tracks the language of the IGA with one critical exception: it omits the phrase “despite relinquishing U.S. citizenship.” Thus, it appears that Canada has justly, reasonably, and rationally (not to mention boldly) resolved the tangled mess of ambiguous and inconsistent definitions relating to meaning of “relinquish.”

This is not the first time Canada has used domestic law to depart from the rigid strictures of FATCA to arrive at a workable solution. Canada’s domestic definition of financial institution essentially ignores the definitions set forth in the IGA and the Treasury regulations in favor of its own definition. While Canada’s definition in this regard is inconsistent with the letter of the IGA, it is certainly consistent with the spirit of the agreement and, most importantly, accomplishes the intended result in a more efficient, elegant fashion.⁷²

iii. Only the first seven IGAs use the term “renounce,” while all others use the term “relinquish”

It is worth noting that while the Cure provision in Canada’s IGA references “relinquishment” only the first seven signed IGAs use the term “renounce” in their respective cure provisions. All other IGAs (including each version of the model IGAs) uses the term “relinquish.”⁷³ No IGA signed or agreed to after May 31, 2013 uses the term “renounce.” If the distinction between “renounce” and “relinquish” became material and the term “relinquish” in Canada’s IGA were less favorable than

⁷² See, Roy A. Berg and Paul M. Barba, “FATCA in Canada: Analyzing the Canadian Implementing Legislation’s Restriction on the Class of Entities Subject to FATCA,” 62:3 *Canadian Tax Journal* 587 (2014), available at http://www.ctf.ca/CTFWEB/EN/Publications/CTJ_Content/2014CTJ3.aspx.

⁷³ The IGAs that use the term “renounce” are: United Kingdom (September 12, 2012); Denmark (November 15, 2012); Ireland (December 21, 2012); Switzerland (February 14, 2013); Norway (April 15, 2013); Spain (May 14, 2013); and Germany (May 31, 2013). The IGA with France was executed on June 11, 2013 (eleven days after Germany) and uses the term “relinquish”.

the term “renounce” in earlier IGAs, Canada would be entitled to the benefit of the more beneficial term under the most-favored-nation provision of the IGA.⁷⁴

e. Significance of a CLN

The Cure provisions under the Treasury regulations, the IGA, and Canadian law are predicated upon either having a CLN or a reasonable explanation of one kind or another. Further, as discussed in section 2(b) of this paper, current U.S. tax law requires a CLN to be issued in order to terminate tax-citizenship.⁷⁵ Before addressing what might constitute a reasonable explanation, however, it is necessary to address the purpose of a CLN for nationality purposes and when one is issued.

A CLN is the U.S. Department of State’s final determination that an individual has lost his U.S. citizenship for nationality purposes.⁷⁶ The U.S. Department of State makes this determination after an individual either formally renounces his U.S. citizenship before a consular official or relinquishes it by confirming in writing a prior expatriating act.⁷⁷ Once the consular official is satisfied that the renunciation or relinquishment was legally sufficient to lose U.S. citizenship, he prepares a CLN that is then forwarded to the Department of State for approval.⁷⁸

Once the CLN has been approved, IRC section 6039G requires the Secretary of State to provide the Secretary of Treasury with a copy. Treasury then manually reviews the information on the CLN and publishes the names of the renouncers in the federal register.⁷⁹

While the CLN is conclusive evidence that the Department of State has determined that an individual has lost U.S. citizenship (for nationality and not tax purposes), neither the CLN itself nor providing notice to the Department of State terminates nationality citizenship. As noted earlier, U.S. nationality citizenship is lost by voluntarily performing an expatriating act with the intent to lose citizenship.⁸⁰ Moreover currently a CLN is not required under the INA; it is merely confirmation that an individual has lost U.S. citizenship as of a certain date.

U.S. legislative history is replete with commentary that confirms this analysis. In 2003, the Joint Committee on Taxation prepared a comprehensive report that reviewed the state of the law relating to tax and relinquishment of U.S. citizenship. The report provides:

⁷⁴ Canadian IGA, *supra* note 10, at Article 7(1).

⁷⁵ IRC section 877A(g)(4).

⁷⁶ 8 U.S.C. section 1501.

⁷⁷ 8 U.S.C. section 1481(a)(1), (2), (3), (5)-(7). To confirm a prior expatriating act, an individual would file the Department of State Form DS-4079, *Request for Determination of Possible Loss of United States Citizenship*.

⁷⁸ 7 *Foreign Affairs Manual* 1220.

⁷⁹ IRC section 6039G(d).

⁸⁰ 8 U.S.C. section 1401(a); but see notes 52 and 53 *supra* for the two remaining ways an individual could have lost his U.S. citizenship by operation of law, outside of 8 U.S.C. 1401(a).

[T]he loss of citizenship is effective on the date that the act of relinquishing citizenship is committed, *even though the loss may not be documented until a later date...*

Generally, the Department of State documents a loss of citizenship on a certificate of loss of nationality (“CLN”) when the individual acknowledges to a consular officer that relinquishment of citizenship was taken with the requisite intent. *There is no obligation for an individual to obtain a CLN or otherwise notify the Department of State of relinquishing one’s citizenship.*⁸¹

Furthermore, in 1996, when Congress debated changes to the expatriation tax regime, the House of Representative’s conference committee report noted that:

Neither the Immigration and Nationality Act nor any other Federal law requires an individual to request a CLN within a specified amount of time after an expatriating act has been committed, even though the expatriation act terminates the status of the individual as a U.S. person for all purposes.⁸²

5. What Might Constitute a “Reasonable Explanation” Under the Treasury Regulations and the IGA?

a. “Reasonable Explanation” under the Treasury regulations

Recall that the Treasury regulations require the individual to provide a “reasonable explanation of the account holder’s renunciation of U.S. citizenship.” While there is no legislative or interpretative guidance as to what constitutes a “reasonable explanation of renouncing citizenship,” the individual would presumably be required to cite the appropriate nationality and tax law, state the relevant facts, apply the facts to the law, and reach an appropriate conclusion. Next, the financial institution would be in the unenviable position of evaluating the explanation to determine whether it is reasonable under the circumstances.

The complexity of U.S. nationality and tax law (not to mention their meandering evolution) make it unlikely that the average individual would be capable of either preparing the explanation or reviewing it for reasonableness without direction from a professional who has extensive experience in these matters. The difficulty of explaining the renunciation of U.S. citizenship and reviewing it for reasonableness is made even more difficult because the explanation appears to be strict standard, and not subject to the individual’s understanding, best efforts, or the best of his knowledge.

b. “Reasonable Explanation” under the IGA and Guidance Notes

Recall that the IGA requires the individual to provide a “reasonable explanation of the reason the account holder does not have a CLN despite relinquishing U.S. citizenship” and the Guidance Notes prescribe the same standard, however they omit the phrase “despite relinquishing U.S. citizenship.” Since a CLN is not necessary to terminate an individual’s citizenship for nationality purposes, what should constitute a “reasonable explanation”?

The obvious answer could simply be: “I do not have a CLN because I never received one and neither the issuance nor receipt is necessary to effectuate my loss of U.S. citizenship.” However this

⁸¹ Joint Committee on Taxation, *Review of the Present-Law and Immigration Treatment of Relinquishment of Citizenship and Termination of Long-Term Residency*, (JCS-2-03), February 2003, at 51 (emphasis added).

⁸² H.R. Rep. No. 104-736 at 330 (Conf. Rep.) (1996). See also Department of Treasury, *Income Tax Compliance by U.S. Citizens and U.S. Lawful Permanent Residents Residing Outside the United States and Related Issues*, at 30, May 1998 (“any loss of citizenship is considered effective on the date the act is committed, even though the loss may not be documented by DOS until a later date.”).

answer strikes a flat note. It is unlikely that the Department of Treasury, which drafted and the IGAs (while IRS drafted the Treasury regulations), intended the IGA’s Cure provision to be so easily satisfied.

Is there another answer that would constitute a reasonable explanation? Note that, like the Cure provision under the Treasury regulations, the language of the IGA and the Guidance Notes appears to be a strict standard and not limited by the individual’s understanding, best efforts, belief, or good faith.

A logical place to begin the analysis is to consider whether the Cure provision in the IGA assumes that individual had received (or had been issued) a CLN at some time in the past. If that were the case, the reasonable explanation would require to individual to establish both: 1) the CLN had been issued at some time in the past; and 2) an explanation as to why the individual does not currently possess it. Consider the following example:

Assume the law requires an individual who operates a motor vehicle to carry on his person a driver’s license, and if he is found to be operating a motor vehicle without one he will receive a citation unless he has a reasonable explanation for not having one on his person.

The implied condition precedent of this law is that the individual has been issued a driver’s license. If an individual is found to be operating a vehicle without one, he will not receive a citation if he has a reasonable explanation as to why he does not have the driver’s license on his person *provided* one has been issued.

However, if the individual has never been issued a driver’s license, no explanation will be reasonable because he has failed to satisfy the implied condition precedent: that a driver’s license has been issued.

The assumption that a CLN must have been issued in the past produces an illogical result under the IGA because explanation would only be reasonable if the individual could establish both that a CLN had been issued and he has an explanation for not currently possessing one. If that had been the intent of U.S. Treasury and the Minister of Finance, they would have simply required the individual to produce a CLN, and allow him a reasonable amount of time to obtain a replacement.

However, the IGA doesn’t require the individual to obtain a replacement (or prove that a CLN had been issued); it allows the individual to provide an explanation as a proxy for proof of the issuance of a CLN. Thus, it is unlikely that Canada and the United States intended the issuance of a CLN to be an implied condition precedent to the reasonableness explanation of not possessing a CLN.

If the IGA does not imply that a CLN had been issued at some point in the past, then a multitude of explanations could be reasonable for an individual’s failure to produce it: I lost it, I cannot find it, I never received it, the dog ate it, etc. It is unlikely that Canada and the United States intended to relegate the “reasonable explanation” standard to be so easily satisfied.

Notwithstanding Canada’s omission of the phrase “despite relinquishing citizenship” in its Guidance Notes, all IGAs contain a similar provision. Therefore it is likely that any “reasonable explanation” is predicated upon loss of U.S. citizenship for either tax or nationality purposes, or both.

Since the Cure provision under the IGA assumes that citizenship has already been lost and does not require an actual explanation of the loss, the explanation should not need to address the particular law or the specific facts surrounding loss of citizenship, however it should address: (1) that in the past the individual committed one of the seven expatriating acts contained in 8 U.S.C. section 1481(a) and (2) that the expatriating act was performed voluntarily and with the intent to lose U.S. citizenship.

c. Recommendation

Therefore, a “reasonable explanation” should include a combination of foregoing, which should be incorporated into the Guidance Notes with a template that balances certainty, administrative efficiency, and the salient aspects of U.S. law and the IGA. The template should be easy for the individual to complete and easy for the financial institution to review. In particular, the template should contain the following:

1. The individual performed one of the seven expatriating acts listed in 8 U.S.C. section 1481(a);
2. The performance of the expatriating act was voluntary and with the intent of relinquishing U.S. citizenship;
3. The individual does not currently possess a CLN; and
4. One of the following is true:
 - a. The individual received a CLN in the past however it cannot be located;
 - b. The individual notified the United States that he committed an expatriating act however does not recall receiving a CLN;
 - c. The individual did not notify the United States that he committed an expatriating act and did not receive a CLN; or
 - d. The individual does not recall notifying the United States that he committed an expatriating act and did not receive a CLN; or
 - e. The individual was informed by a Canadian official that when he became a Canadian citizen he would lose his U.S. citizenship, and when he became a Canadian citizen he did so voluntarily and with the intent of losing his U.S. citizenship. Further, he may or may not have notified the U.S. Department of State and he may or may not have received a CLN.

Finally, and of critical importance, the template should notify the individual that under current U.S. law, termination of U.S. citizenship for nationality purposes does not necessarily terminate citizenship for tax purposes.⁸³

A template that incorporates the foregoing is attached as **“Exhibit 1.”**

The author does mean to suggest that the foregoing recommendation and template embody an accurate summary and application of U.S. tax and nationality law in the context of the relevant Cure provisions. To the contrary, an analysis of the relevant bodies of law should leave the reader with

⁸³ To its credit, CRA frequently includes notifications and links to the IRS website when addressing U.S. tax issues relevant to Canadian residents. See, e.g., <http://www.cra-arc.gc.ca/tx/nnrstdnts/nhncdrprtng/fq-eng.html>.

only one clear conclusion, which is that there is no clear conclusion. Of course this is little consolation to both the individual who wishes to provide a reasonable explanation, and also the financial institutions that must evaluate it. Thus, the recommendation and template offer a practical solution under Canadian law and Canada’s IGA.

6. Canada has the Authority to Issue Guidance on “Reasonable Explanation” Under the IGA

Of course, Canada is unable to change U.S. law; however it does have the authority under the IGA to enact domestic legislation (including Guidance Notes) to clarify what would constitute a reasonable explanation. First, the IGA provides that any term not defined in it will, unless modified by the competent authorities, be determined under local law.⁸⁴ Second, the IGA also provides that, notwithstanding the definitions provided therein, Canada may elect to use the definitions found in the Treasury regulations provided this use does not frustrate the purposes of the IGA.⁸⁵ Since neither the IGA nor the Treasury regulations address what constitutes a “reasonable explanation,” Canada should have the latitude to provide this clarity.

Further, while the IGA and Canada’s implementing legislation provide guidance to the use of defined and undefined terms, those terms remain subject to Canadian rules of treaty and statutory interpretation. Canada did not cede its legislative and jurisprudential rules of construction upon signing the IGA or enacting Part XVIII of the Act.

To date, no other IGA partner country has issued legislation or guidance on this issue. However, at least one non-U.S. financial institution has recognized the problem of not defining a “reasonable explanation,” and it has crafted an innovative solution. Dah Sing Bank of Hong Kong has simply posted a blank CLN on its website (and apparently has physical copies available at their branches), which account holders may complete in order to Cure their U.S. place of birth. The bank’s self-certification reads as follows:

If you were born in [the] U.S. but in [sic] this form you declare that you are not a U.S. person, please also provide us with a Certificate of Loss of Nationality of the United States , the form is available at any of our branches or for download on our website ...).⁸⁶

Hong Kong⁸⁷ has yet to enact implementing legislation and it has not published regulations or Guidance Notes, so it is unclear whether the bank’s solution will ultimately be consistent with domestic law. Since the term “Certificate of Loss of Nationality” is not defined in Hong Kong’s IGA presumably it would be at liberty to define the term under domestic legislation in a manner consistent with the bank’s solution. Although innovative, that approach appears to be incongruous with the spirit of the IGAs, and is clearly an incorrect application of U.S. law.

⁸⁴ Canadian IGA, *supra* note 10, article 1(2).

⁸⁵ *Ibid*, article 4(7).

⁸⁶ http://www.dahsing.com/en/pdf/common/form/cc_self_certificate_for_FATCA.pdf; and http://www.dahsing.com/en/pdf/common/form/cc_certificate_loss_of_nationality_us.pdf.

⁸⁷ On November 11, 2014 Hong Kong signed a Model 2 IGA, which incorporated its existing tax information exchange agreement with the United States.

7. Canada Should Modify its Guidance Notes to Clarify “Reasonable Explanation”

Unlike the IGA, subsection 265(5) of the Act mandates that reporting Canadian financial institutions attempt to Cure accounts where the holder has an unambiguous place of U.S. birth.⁸⁸ In light of this mandate it would be reasonable to expect that Canada would provide clarification. By providing guidance, Canada could provide comfort to financial institutions by indicating that they are applying the appropriate review of the relevant factors, which would result in consistent standards and consistent results for affected individuals. Further, by providing guidance the CRA would be able to ensure that any forms or templates developed by the financial institutions would include the tax notification contained in **Exhibit “1.”**

Without formal guidance, reporting Canadian financial institutions may simply ask the individual to provide his own free-flowing narration of why he does not have the CLN. In providing this narrative the individual may inadvertently misstate facts or assumptions that would, under U.S. law, call into doubt the efficacy of his loss of U.S. citizenship or compliance with U.S. tax law. As such, the individual may innocently and inadvertently admit to facts that complicate his nationality or tax status.

Finally, without formal guidance the reporting Canadian financial institution may arbitrarily conclude that the individual’s explanation is not reasonable, which could cause the account to be unnecessarily labeled as reportable and thereby result in an unnecessary compliance burden. Further, the affected individual might seek to obtain a CLN without fully understanding the U.S. tax consequences of doing so. As discussed below, under the current U.S. expatriation tax regime, the individual’s mere application for a CLN could trigger substantial U.S. income tax liability.

8. U.S. Expatriation Tax: Danger of Curing a U.S. Place of Birth with a CLN

An individual who attempts to Cure his unambiguous place of U.S. birth by obtaining a CLN would do so by either officially renouncing his U.S. citizenship before a diplomatic or consular office,⁸⁹ or by requesting a determination from the U.S. Department of State that in the past he lost his citizenship by performing an expatriating act with the requisite mental state.⁹⁰ In doing so, the individual has just stepped into one of the most ambiguous, complex, misunderstood, and high-stakes areas of U.S. international individual tax law.

There are two reasons the U.S. expatriation tax regime is a Serbonian bog of legal and tax issues. First, U.S. immigration law has evolved over time: some acts (or omissions) that caused an individual to lose his citizenship at one point in time have been held by the Supreme Court of the United States to be unconstitutional, the legal effect of which is retroactive repeal of the offending legislation and resulting retroactive restoration of U.S. citizenship.⁹¹

⁸⁸ See also CRA Guidance Notes, supra note 55, 8.18 (which states “[w]hen a financial institution identifies one or more U.S. indicia, the financial institution must attempt to cure the indicia by applying the appropriate steps set out in subparagraph B(4) of section II of Annex I of the Agreement. This is mandated by subsection 265(5) of the ITA.”).

⁸⁹ 8 U.S.C. section 1401(a)(5); IRC section 877A(g)(4)(A).

⁹⁰ 8 U.S.C. section 1401(a); IRC section 877A(g)(4)(B).

⁹¹ But see notes 52 and 53, supra, for the two remaining statutes under which an individual may automatically lose U.S. citizenship for nationality purposes.

Second, in 2004 Congress enacted law that bifurcated the loss of citizenship for nationality purposes and loss of citizenship for tax purposes.⁹² This bifurcation has resulted in two fundamentally different regimes applicable to former-U.S. citizens. In 2008, Congress took this bifurcation even further by defining the effective date of an individual’s loss of U.S. citizenship for tax purposes as the date the individual notifies the U.S. government of his or her loss of citizenship, which effectively gives the government an opportunity to apply the expatriation tax that contained this new notification requirement.⁹³ The importance of this bifurcation cannot be over-emphasized. The timing of the individual’s loss of citizenship (for both nationality and tax purposes) will determine the individual’s U.S. tax and filing obligations.

a. Tax consequences when U.S. citizenship has been lost or restored because of unconstitutional legislation

As introduced in Section 2(d) of this paper, U.S. nationality law has evolved over time and many laws that caused an individual to automatically lose U.S. citizenship were held by the U.S. Supreme Court to be unconstitutional, with retroactive effect. Thus, many individuals who had lost their U.S. citizenship in the past found it restored literally overnight.

The question thus arose: since the U.S. taxes its citizens on their worldwide income, is the taxpayer liable for U.S. taxes during the period beginning on the date he lost his U.S. citizenship (under the law at the time) and ending on the date the pertinent law was declared unconstitutional? The IRS’s initial position was that because the law was declared unconstitutional *ab initio*, the individual was always a U.S. citizen and therefore subject to tax on his worldwide income during that entire period.⁹⁴

However, the Federal Court of Appeals for the First Circuit later held that the IRS cannot tax an individual for a period when he had been stripped of U.S. citizenship by an invalid act of the U.S. government.⁹⁵ Using colorful language, the court held that “[the taxpayer] cannot be dunned for taxes to support the United States Government during the years in which she was denied its protection.”⁹⁶

⁹² American Jobs Creation Act of 2004, Pub. L. no. 108-357, section 804 (herein referred to as “AJCA”).

⁹³ HEART *supra* note 31; IRC section 877A(g)(4).

⁹⁴ Revenue Ruling 70-506, 1970-2 CB 1. (holding: “any Certificate of Loss of Nationality of the United States issued by reason of section 352(a) of the Immigration and Nationality Act of 1952 is considered null and void and the individual affected thereby is a citizen of the United States and taxable...on income received from sources within and without the United States.”); see also Revenue Ruling 75-357, 1975-2 CB 5.

⁹⁵ *D’Hotelle de Benitez Rexach v. United States*, 558 F.2d 37 at 39 (1st Cir. 1977). The case illustrates the complexity involved with restoration of U.S. citizenship. In 1949 the taxpayer committed an expatriating act and was unaware of her loss of citizenship until 1952 when she was issued a CLN. In 1965 the statute under which her citizenship was revoked was held by the U.S. Supreme Court (*Schneider v. Rusk*, 377 U.S. 163 (1965)) to be unconstitutional and given retroactive effect. The court held that the taxpayer was responsible for U.S. tax from the period beginning in 1949 (the date of the expatriating act) and ending in 1952 (when she received the CLN). However she was not responsible for U.S. tax from the period beginning in 1952 and ending in 1965.

⁹⁶ *Ibid.*

Currently, the taxability of these individuals is a complex bramble bush that depends on who had asserted the loss of U.S. citizenship, when it was lost, when it was restored, and the particular facts during the intervening period.⁹⁷ However, there are two common factors in the administrative and judicial guidance regarding the tax and filing obligations for these individuals: First, the individual’s tax and filing obligations would be suspended only if *both* the individual and the Department of State concurrently believe that the individual had lost his U.S. citizenship for nationality purposes. This concurrence factor is not separately analyzed in the applicable sources, so it could be merely correlative in nature and not determinative. Second, the individual’s tax and filing obligations continue once U.S. citizenship has been restored by a judicial decision even though the individuals sincerely believed they were no longer a U.S. citizen and were unaware of the restoration of citizenship.⁹⁸

b. Loss of tax-citizenship and the evolution of the U.S. expatriation tax regime⁹⁹

Adding to the complexities of retroactive nationality law, the individual who seeks to Cure his U.S. place of birth must also contend with the evolution of the U.S.’s expatriation tax and the concept of U.S. citizenship for tax purposes. The law in this regard has changed greatly since 1966 and it is critical to match the applicable law with time the individual renounced U.S. citizenship for nationality purposes. Hence, the following trundle through complex legislation and legislative history.¹⁰⁰

i. The Foreign Investors Tax Act of 1966 (FITA)¹⁰¹

In 1966, the U.S. enacted its first set of tax laws directed at individuals who gave up U.S. citizenship. Section 877, as it read at the time, provided that certain former U.S. citizens who gave up their citizenship were subject to an alternate tax regime for a period of 10 years following their loss of U.S. citizenship. Generally, the alternate tax regime took certain types of income that would otherwise have been foreign source (and therefore not taxable to the expatriated individual) and reclassified it as U.S. source and thereby taxable to the individual.

⁹⁷ See, Revenue Ruling 92-109, 1992-2 CB 3. The ruling discusses several different factual situations regarding the retroactive reinstatement of U.S. citizenship, the common theme of which is that the individual will not be subject to U.S. tax only when the individual and the Department of State concurrently believe that the individual’s citizenship has been terminated. Without this concurrent belief the individual is subject to U.S. tax. This result is consistent with the holding in *D’Hotelle de Benitez Rexach* Ibid.

⁹⁸ Ibid.

⁹⁹ Michael Pfeifer, *The Current State of Expatriation*, International Trust and Estate Planning, American Law Institute (October 20, 2014, San Francisco); Michael J. Miller and Ellen Seiler Brody, “Expats Live In Fear of Malevolent Time Machine,” 12 *International Tax Journal* 213 (March 5, 2013); Michael J. Miller “Comments on the Tax Status of Certain Expatriates” American Bar Association Section of Taxation, Letter to Hon. John Koskinen, Commissioner of Internal Revenue (March 2, 2015), 2015 *World Tax Daily* 41-34 (March 2, 2015).

¹⁰⁰ See Patrick Martin, “Accidental Americans” Rush to Renounce U.S. Citizenship to Avoid the Ugly U.S. Tax Web,” 38:6 *International Tax Journal*, (Nov./Dec. 2012). Mr. Martin is a lawyer with the law firm of Procopio, Cory, Hargreaves & Savitch LLP, and his article includes an excellent graphic depiction of the various laws that have changed the U.S. expatriation regime.

¹⁰¹ Pub. L. No. 89-809, section 102(f) (1966) (herein referred to as “FITA”).

Not all former U.S. citizens were subject to the alternate tax regime. Only those who lost their citizenship with a principal purpose of avoiding tax were subject to section 877’s expatriation tax regime, and only if the loss was after March 8, 1965.¹⁰² The date on which citizenship was lost for nationality purposes determined whether the loss was before or after March 8, 1965.

ii. *The Health Insurance Portability and Accountability Act of 1996 (HIPAA)*¹⁰³

For purposes of this paper the most important change HIPAA brought about was that it created a rebuttable presumption that the individual lost his citizenship with a primary purpose of avoiding U.S. tax if: a) his net worth exceeded \$500,000; or b) his average federal tax liability for the five years preceding expatriation exceeded \$100,000.¹⁰⁴

HIPAA also changed the alternate tax regime in two important aspects. First, it expanded the categories of income drawn into the alternate tax regime. Second, Congress made clear that the alternate tax regime was intended to override existing tax treaties for ten years following enactment.¹⁰⁵ But the architecture of the expatriation tax regime was left mostly intact.

Importantly, HIPAA did not distinguish loss of U.S. citizenship for nationality purposes from loss of U.S. citizenship for tax purposes.

iii. *The American Jobs Creation Act of 2004 (AJCA)*¹⁰⁶

The AJCA marked a critical departure from prior law because it introduced the concept of citizenship for tax purposes as something distinct from citizenship determined for nationality purposes. In its 2003 Report, the Joint Committee on Taxation recognized that it would be possible for an individual to lose his U.S. citizenship for nationality purposes and delay reporting this event to the Department of State, thereby retaining the ability to invoke his U.S. citizenship in the case of an emergency, or to avail himself of consular services.¹⁰⁷ Conversely, the same individual could benefit from a financial windfall that is not taxed in his country of residence (e.g., Canadian lottery and gambling winnings) and trigger his loss of citizenship antecedent to that windfall.

¹⁰² IRC section 877(a).

¹⁰³ Pub. L. No. 104-191 (1996) (herein referred to as “HIPAA”).

¹⁰⁴ HIPAA, *supra* note 103, at section 511 (amending section 877(a)(2)). Both figures were indexed for inflation. For the first time, HIPAA also drew into the alternate tax regime long-term green card holders by adding section 877(e). This is a critical event for determining the tax consequences of abandoning green cards. Important as it is, however, it lies outside the scope of this paper.

¹⁰⁵ H. Rep. 145, 104th Cong., 1st Sess. 30 (1995).

¹⁰⁶ AJCA *supra* note 30.

¹⁰⁷ United States, Department of the Treasury, *Income Tax Compliance by U.S. Citizens and U.S. Lawful Permanent Residents Residing Outside the United States and Related Issues*, at 33 (May 1998). Interestingly, this report quotes a popular book in a footnote on the tax benefits of renouncing U.S. citizenship: “if there is any possibility that you might want to become a tax exile from the U.S. at any time in the future you should get another nationality and second passport now.” Langer, *The Tax Exile Report* (2d ed. 1993-1994) at 67.”

The AJCA embodied the concept of U.S. citizenship for tax purposes in IRC section 7701(n) (repealed in 2008) the salient portions of which are as follows:¹⁰⁸

(n) Special rules for determining when an individual is no longer a United States citizen or long-term resident. For purposes of this chapter

(1) United States citizens. An individual who would (but for this paragraph) cease to be treated as a citizen of the United States shall continue to be treated as a citizen of the United States until such individual

(A) gives notice of an expatriating act (with the requisite intent to relinquish citizenship) to the Secretary of State, and

(B) provides a statement in accordance with section 6039G (if such a statement is otherwise required).

Thus, for the first time U.S. law distinguished citizenship for nationality purposes from citizenship for tax purposes. Under section 7701(n), while the individual’s nationality-citizenship may have terminated, his tax-citizenship would continue until he gave notice to both the Secretary of State and the IRS (by filing the form 8854 pursuant to section 6039G).

Critically important for purposes of understanding the next (and final) iteration of the U.S. expatriation regime is the effective date of the notice provisions of 7701(n). The new notification provisions applied only to individuals who “expatriated” after June 3, 2004.¹⁰⁹ In other words, an individual would be considered to lose their citizenship for both nationality and tax purposes (regardless of whether they provided notice to the Department of State or IRS) if the individual “expatriated” before June 3, 2004. Conversely if the individual “expatriated” after that date, his U.S. citizenship for tax purposes ended only after giving the notice required under section 7701(n).

It is important to note that the AJCA introduced a new term: “expatriate.” The notice provisions of section 7701(n) applied only to individuals who “expatriated” after June 3, 2004. Unfortunately neither the AJCA nor the INA define the term “expatriate.” In context, the term makes sense only as a vernacular term for “loss of citizenship” by either renouncing or relinquishing U.S. citizenship. As addressed below, the next iteration of the expatriation tax regime increased the difficulty of comprehension by introducing the defined term “expatriation date.”¹¹⁰

Other changes included removal of the subjective tax avoidance intent to trigger the alternate tax regime, monetary adjustments to the net worth and tax liability tests, and a new certification test that triggered the alternate tax regime.¹¹¹ In addition, full U.S. tax and filing obligations were restored to

¹⁰⁸ IRC section 7701(n) also contained similar requirements for determining the date on which a green card holder is deemed to abandon that status. While critically important in that context, it is outside the scope of this paper.

¹⁰⁹ AJCA, *supra* note 92, section 804(f).

¹¹⁰ IRC section 877A(g)(3).

¹¹¹ The net worth threshold was increased from \$500,000 to \$2,000,000 (not indexed for inflation), and the average tax liability threshold was increased \$124,000 (indexed for inflation). IRC section 877(a)(2)(A), (a)(2)(B).

individuals who were physically present in the United States for more than 30 days during the 10 years following expatriation.¹¹²

The major facet of prior law left unchanged was the alternate tax regime. The mark-to-market regime (what is commonly referred to as the “exit tax”) would not come until 2008.

*iv. The Heroes Earnings Assistance and Relief Tax Act of 2008 (HEART)*¹¹³

The most recent legislative change to the expatriation tax regime occurred under HEART. This is the lynchpin for understanding why individuals who attempt to Cure their unambiguous place of U.S. birth by obtaining a CLN may blithely stroll into the expatriation tax regime.

First, the alternative tax regime, which re-sourced otherwise non-U.S. source income as U.S. source for certain expatriates, was replaced with a mark-to-market regime. Under this regime, the affected individual (a “covered expatriate”) is deemed to have sold all of his property (with some exceptions) at fair market value on the day preceding the “expatriation date.”¹¹⁴ Hence the current “exit tax” entered into current law.

Second, the notification requirements enacted under the AJCA in section 7701(n) were repealed.¹¹⁵

Third, new section 7701(a)(50)(A) made clear that an individual’s U.S. citizenship for tax purposes is terminates only upon relinquishment in accordance with 877A(g)(4). The statute provides:

(A) In General. An individual shall not cease to be treated as a United States citizen before the date on which the individual’s citizenship is treated as relinquished under 877A(g)(4).¹¹⁶

Fourth, the concept of “expatriation date” was introduced. Under new section 877(h) the old expatriation tax regime found in section 877 does not apply to any individual whose “expatriation date,” as defined in new section 877A(g)(3) is on or after June 17, 2008.

New section 877A(g)(3) provides that an individual’s “expatriation date” is the date the individual “relinquishes” U.S. citizenship.¹¹⁷

¹¹² IRC section 877(g).

¹¹³ HEART, supra note 31.

¹¹⁴ IRC section 877A(a)(1).

¹¹⁵ HEART, supra note 31, section 301(a), (c)(2)(C).

¹¹⁶ Supra note 41.

¹¹⁷ Further, the term “expatriation date” also applies to green card holders who have held a green card for eight of the last fifteen years. IRC section 877A(g)(3)(B)

9. Example of the application of the U.S. Expatriation Tax Regime to Individuals Who Cure Their U.S. Place of Birth by Obtaining a CLN

a. The unfortunate case of “Mr. Maple Leaf”

Thus, if we literally apply current law, an individual who seeks a CLN based upon a prior expatriating act will be subject to both the exit tax under IRC section 877A and past tax obligations, if he had not either applied for a CLN or been issued one prior to June 3, 2004. Consider the following example:

Mr. Maple Leaf is born in New York, New York (which happens to be in the “USA”) in 1960. He naturalizes as a Canadian citizen in 1981 at age 21. Mr. Maple Leaf voluntarily takes the Canadian oath of citizenship when he naturalizes and intends to relinquish his U.S. citizenship upon doing so.

In 2015 Mr. Maple Leaf is told by his reporting Canadian financial institution that he has an unambiguous place of U.S. birth and therefore his account is a U.S. reportable account under Canadian law. Since he has a U.S. reportable account, he will be reported to the CRA and therefore the IRS unless he can provide a CLN or a reasonable explanation as to why he does not have one despite having relinquished U.S. citizenship. Mr. Maple Leaf provides what he believes to be a reasonable explanation for why he does not have a CLN, however his explanation is rejected by his financial institution.

In 2015, out of desperation, he applies to the U.S. Department of State for a determination of whether he lost his U.S. citizenship when he naturalized and took the Canadian oath of citizenship.¹¹⁸

In 2016, the Department of State agrees that Mr. Maple Leaf lost his U.S. citizenship in 1981 at age 21 and issues a CLN effective for nationality purposes as of that date in 1981. Mr. Maple Leaf has never filed U.S. income tax returns.

What are the consequences to Mr. Maple Leaf? Under a literal interpretation of current law Mr. Maple Leaf’s U.S. citizenship is terminated for nationality purposes in 1981.¹¹⁹ However under HEART, termination of his U.S. citizenship for tax purposes is determined under section 7701(a)(50)(A), which sends us to section 877A(g)(4). Under section 877A(g)(4), Mr. Maple Leaf’s U.S. citizenship is lost on the earlier of:

1. The date in 2015 on which he submitted a statement that confirmed a prior expatriating act (i.e., becoming naturalized in and formally declaring allegiance to Canada);¹²⁰ or
2. The date in 2016 on which his CLN was issued.¹²¹

¹¹⁸ 8 U.S.C. section 1401(a).

¹¹⁹ 8 U.S.C. 1481(a)(1), (2).

¹²⁰ Ibid; IRC section 877A(g)(4)(A).

¹²¹ IRC section 877A(g)(4)(D).

Because his submission to the Department of State antedated the issuance of the CLN, his tax-citizenship terminated in 2015. Thus, Mr. Maple Leaf is liable for tax and reporting obligations from 1981 through 2015. Further, since Mr. Maple Leaf and the Department of State did not concurrently consider his U.S. citizenship to have terminated, he will not be relieved of tax obligations under *D’Hotelle de Benitez*¹²² or Revenue Ruling 92-109 until 2015.¹²²

Moreover, Mr. Maple Leaf will be subject to section 877A’s exit tax if any of the following are true:

1. His net worth was US\$2 million or more on the date he lost citizenship;¹²³
2. His average U.S. income tax liability exceeds US\$160,000 (for 2015) for the five taxable years ending before the date he lost citizenship;¹²⁴
3. He fails to certify under penalties of perjury that he is compliant with his U.S. tax and filing obligations for the five preceding taxable years.¹²⁵

The foregoing analysis is based on a literal interpretation of the applicable statutory law and is technically sound. However the result shocks the conscience. If Mr. Maple Leaf had simply informed the Department of State of his expatriating act prior to June 3, 2004 (or been issued a CLN before that date) his expatriation date would have antedated HEART and therefore his tax-citizenship would have terminated in 1981 under the AJCA. Alternatively, if he had the foresight to die before June 3, 2004 he would also have been under the AJCA rules and his U.S. tax-citizenship, including potential application of the estate tax, would have likewise terminated.

b. Criticism of literal interpretation of current expatriation tax regime

This inequitable result has not gone unnoticed by the few practitioners who have untangled the Gordian knot that is the law in this regard. Several of these practitioners, including the author, have written articles and engaged in formal and informal discussions with the IRS.¹²⁶ While all are hopeful for guidance on this issue, to date there have been no administrative interpretations or public announcements that would clarify or amend the literal application of the law analyzed above.

While a literal interpretation of the statute clearly produces the foregoing result there are several arguments that could justify departure from the literal interpretation.

i. Result is not reflected in legislative history

¹²² Surpa notes 95 and 97. Note, the concurrence factor is not separately analyzed in the administrative and judicial interpretations. Therefore its relevance could be merely correlative in nature and not determinative of the outcome.

¹²³ Ibid, 877A(g)(1)(A); 877(a)(2)(A).

¹²⁴ Ibid, 877(a)(2)(A).

¹²⁵ Ibid, 877(a)(2)(C).

¹²⁶ Pfiefer, supra note 99; Miller, supra note 99.

The legislative history from 1995 indicates that the Joint Committee on Taxation recognized the problem of a bifurcated termination of citizenship for tax and nationality purposes, and drafted the HIPAA to avoid a similar result. A report by the Joint Committee on Taxation issued that year provides:

The new tax definition of the date of loss of citizenship set forth in the proposals would apply for only two purposes: (1) to determine the date on which the new expatriation tax is imposed, and (2) to determine the date on which an individual’s continuing obligation to pay taxes as a U.S. citizen ceases. The proposals would not change the law applicable to loss of citizenship for any other purpose. The existence of two separate definitions of when citizenship is lost for various purposes would not only be confusing but there could be serious legal and even constitutional problems in taxing an individual as a U.S. citizen long after he or she ceases to have the rights and responsibilities of a U.S. citizen for all other purposes.¹²⁷

Further, a footnote in the report indicates that such a proposal might constitute a retroactive federal income tax increase with respect to such individuals, which would be in violation of the ultra vires rule XXI.5(d) of the Rules of the House of Representatives.¹²⁸

ii. No evidence that HEART should override AJCA

The concept of U.S. citizenship for tax purposes was introduced in 2004 under AJCA, which expressly provided that such concept was to be applied only to those who expatriated for nationality purposes after the effective date of the act (June 3, 2004). Literally interpreted, HEART overrides the prospective application of AJCA for those individuals who had not either informed the Department of State of a prior expatriating act or received a CLN before the date of the act. With the exception of those individuals, a literal reading of HEART would apply retroactively. If Congress had intended such a significant departure from existing law it is reasonable to conclude there would be evidence of this intent. However, there is no evidence of this intent in the legislative history.¹²⁹

Admittedly, retroactive tax legislation is occasionally enacted in the U.S. and there is no explicit preclusion of such in the U.S. Constitution.¹³⁰ The Congressional Research Service produced an excellent report on this topic aptly titled “*Constitutionality of Retroactive Tax Legislation*”¹³¹ that analyzes the issue in depth.

iii. Statute should not be interpreted to produce a ridiculous result

¹²⁷ United States, Joint Committee on Taxation, 104th Cong., 1st Sess., *Issues Presented by Proposals to Modify the Tax Treatment of Expatriation*, (Washington, DC: Joint Committee on Taxation, June 1, 1995), at 50-53.

¹²⁸ Ibid at footnote 95.

¹²⁹ See, e.g., Supra note 109.

¹³⁰ See *United States v. Carlton*, 512 U.S. 26 (1994).

¹³¹ U.S. Library of Congress, Congressional Research Service. 2012. *Constitutionality of Retroactive Tax Legislation*, by Erika K. Lunder, Robert Meltz, and Kenneth R. Thomas. CRS Report R42791. Washington, DC: Office of Congressional Information and Publishing, October 25, 2012.

In U.S. jurisprudence it is well established that a statute must not be interpreted to produce an absurd result.¹³² Further, in light of the constitutional issues alluded to in the 1995 Report the doctrine of statutory construction that provides: “doubtful statutory construction involving possible unconstitutionality should always be rejected in favor of a reasonable construction by which the constitutional conflict can be avoided.”¹³³

10. Conclusion

Identification of the financial accounts held by U.S. citizens lies at the core of FATCA because U.S. citizens are subject to taxation on their worldwide income. It’s not always easy to identify a U.S. citizen, however if an individual was born in the United States he became a U.S. citizen at that time. Whether the individual is currently a U.S. citizen is more difficult to determine because the loss of citizenship has a different meaning for tax purposes than it does for nationality purposes. Under FATCA the relevant citizenship determination is made under tax law and not nationality law. Place of birth is an easily identifiable and readily available factor, and these accounts become reportable under FATCA unless the holder of the account can refute the presumption of his status as a U.S. person by producing a CLN, or has a reasonable explanation for not having one despite having lost his citizenship. The divergence between citizenship for nationality law purposes and tax purposes precipitates three central problems.

First, neither the issuance of a CLN nor notification to the U.S. Department of State is required to lose U.S. citizenship (for nationality purposes). Thus many residents of Canada may not be U.S. citizens for nationality purposes, but do not possess a CLN.

Second, while these individuals may Cure the lack of a CLN with a reasonable explanation for not having one, there is a dearth of direct guidance on what constitutes a “reasonable explanation.” The author is hopeful that this paper has provided the analytical framework for Canada and other IGA partners to issue clear guidance in this regard.

Third, under the current U.S. expatriation tax regime, the date on which an individual is deemed to lose his U.S. citizenship for tax purposes is determined under a different set of rules than those that determine loss of U.S. citizenship for nationality purposes. Thus, an individual who seeks to Cure his inability to produce a CLN by simply applying for one may find himself subject to one of the two expatriation tax regimes discussed at length in this paper.

When FATCA became U.S. law in 2010 the world took a significant step into the new era of global financial transparency, and in 2014 the world took another significant step with the OECD agreement on its Standard for Automatic Exchange of Financial Account Information which incorporates much of the architecture established under FATCA. The rules under both regimes are intimidating, ambitious and voluminous however it is incumbent upon the professional community to become familiar with them in order to properly identify the issues and advise their clients accordingly.

¹³² *United States v. American Trucking Associations, Inc.*, 310 U.S. 534, 543 (1940).

¹³³ *United States v. Carlton*, 512 U.S. 26, 30 (1994).

The fire-breathing leviathan can be tamed however only with time and effort. Tax practitioners must make the investment soon because the leviathan has newly-hatched siblings that are equally as intimidating. Only after FATCA has been tamed will the practitioner be equipped to approach the Common Reporting Standard and the other fiscal transparency hatchlings.

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"Exhibit 1"
**Explanation of Reason Account Holder Does Not Possess a
 Certificate of Loss of Nationality Despite Having Relinquished U.S. Citizenship**

Please check any of the following if applicable:	
<input type="checkbox"/>	I do not currently possess a U.S. Certificate of Loss of Nationality ("CLN").
<input type="checkbox"/>	<p>In the past I voluntarily committed one of the following expatriating acts with the <u>contemporaneous intent</u> of relinquishing my U.S. citizenship:</p> <ol style="list-style-type: none"> 1. I obtained naturalization in a non-U.S. country upon my own application or upon an application filed by my duly authorized agent, after having attained the age of eighteen years; 2. I took an oath or made an affirmation or other formal declaration of allegiance to a non-U.S. country or a political subdivision thereof, after having attained the age of eighteen years; 3. I entered into, or served in, the armed forces of a non-U.S. country and: a) such armed forces were engaged in hostilities against the U.S.; or b) I served as a commissioned or non-commissioned officer; 4. a) I accepted, served in, or performed the duties of any office, post, or employment under the government of a non-U.S. country or a political subdivision thereof, after attaining the age of eighteen years after having acquired the nationality of such non-U.S. country; or b) accepted, served in, or performed the duties of any office, post, or employment under the government of a non-U.S. country or a political subdivision thereof, after attaining the age of eighteen years for which office, post, or employment an oath, affirmation, or declaration of allegiance was required; or 5. I made a formal renunciation of U.S. citizenship before a diplomatic or consular officer of the U.S. in a non-U.S. country, in the form prescribed by the U.S. Secretary of State; 6. While in the U.S. I made a formal written renunciation of my U.S. citizenship the form prescribed by, and before such officer, the Attorney General, when the U.S. was in a state of war and the Attorney General approved such renunciation to be not contrary to the interests of national defense of the U.S.; or 7. I committed an act of treason against, or attempted by force to overthrow, or bore arms against, the U.S., violated or conspired to violate any of the provisions of 18 U.S.C. 2383, or willfully performed any act in violation of 18 USC 2385, or violated 18 U.S.C. 2384 by engaging in a conspiracy to overthrow, put down, or to destroy by force the Government of the U.S., or to levied war against it, and was convicted thereof by a court martial or by a court of competent jurisdiction. <p>If you are unable to affirm committing one of the foregoing seven expatriating acts please do not complete this form and seek independent legal advice.</p>
If applicable, please check one of the following. If you are unable to affirm one of the following statements please do not complete this form and seek independent legal advice.	
<input type="checkbox"/>	In the past I received a CLN however it cannot be located.
<input type="checkbox"/>	I notified the U.S. Department of State that I committed one of the expatriating acts listed above, however I do not recall receiving a CLN.
<input type="checkbox"/>	I did not notify the U.S. Department of State that I committed one of the expatriating acts listed above and I did not receive a CLN.
<input type="checkbox"/>	I do not recall notifying the U.S. Department of State that I committed one of the expatriating act listed above and I did not receive a CLN.
<input type="checkbox"/>	I was informed by a Canadian official that when I became a Canadian citizen I would lose my U.S. citizenship, and when I became a Canadian citizen I did so voluntarily and with the intent of losing my U.S. citizenship. I may or may not have notified the U.S. Department of State and I may or may not have received a CLN.
<p>Please Note: Under U.S. law, tax and filing obligations continue until the later of: a) formally requesting confirmation from the U.S. Department of State that you have lost U.S. citizenship by committing one of the expatriating acts listed above; or b) issuance of a Certificate of Loss of Nationality. For more information, visit the IRS website at http://www.irs.gov/Individuals/International-Taxpayers/Expatriation-Tax. If you wish to contact the IRS by mail or by phone visit the IRS website at www.irs.gov/uac/How-to-Contact-the-IRS-1 for contact information.</p>	

I declare that the information I have provided on this form is, to the best of my knowledge and belief, correct and complete.

Name: _____
 Signature: _____
 Date: _____