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## 2006 Amendments to the Foreign Earned Income Exclusion: Effects, Reactions, and Suggestions for Change

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# 2006 AMENDMENTS TO THE FOREIGN EARNED INCOME EXCLUSION: EFFECTS, REACTIONS, AND SUGGESTIONS FOR CHANGE

*Jill Meyer\**

## I. INTRODUCTION

**T**HE United States taxes its citizens on their world-wide income, regardless of where it is earned. In addition, U.S. citizens living abroad may also be taxed on their income by the country in which they reside. In order to help relieve this potential double-tax burden and to serve other policy goals, the United States tax code has historically provided some relief through the foreign tax credit, foreign earned income exclusion, and foreign housing cost exclusion.

In May 2006, Congress passed amendments to the tax code that reduced the benefits provided by the foreign earned income exclusion and foreign housing cost exclusion. These changes imposed a cap on the amount of deductible housing expenses and introduced a stacking rule, whereby income that is not excluded is taxed at a higher marginal tax rate. The amendments were made to offset tax cuts in other areas. As a result of these amendments, the tax burden on overseas Americans could increase dramatically.

U.S. citizens living abroad, often referred to as *expatriates*, have rallied against the tax increases, particularly in low-tax, high cost-of-living areas such as Hong Kong and Singapore. Many of these groups are calling for repeal of the amendments or even an increase from previous levels in the amount of the foreign earned income exclusion. Some relief was provided by the Internal Revenue Service ("IRS") in a notice issued in October 2006 which increased the amount of deductible housing costs in certain areas. However, the bulletin did not eliminate all of the negative effects of the amendments and did not alter their effects at all for U.S. citizens living in other places.

This Comment examines the foreign earned income exclusion, particularly focusing on the 2006 amendments. It argues that the amendments,

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which increase the tax burden for overseas Americans and their employers, should be repealed because they represent bad international tax policy for the United States and will reduce the competitive position of the United States. Section II provides a brief history of the foreign earned income exclusion. Section III describes the recent controversy surrounding the foreign earned income exclusion. Sections IV and V explain the 2006 amendments to the foreign earned income and housing exclusions and the reactions of Americans living overseas. The IRS notice, which eased some of the effects of the amendments, is examined in Section VI. Section VII considers potential changes to the foreign earned income exclusion, including its total elimination or the removal of any limits on it, and recommends that the 2006 amendments be repealed.

## II. HISTORY OF SECTION 911 FOREIGN EARNED INCOME EXCLUSION

### A. TIMELINE OF THE FOREIGN EARNED INCOME EXCLUSION

The United States employs a “worldwide-system” of taxation.<sup>1</sup> This means that U.S. citizens and green card holders must pay taxes on their worldwide income despite where it is earned or deposited.<sup>2</sup> The Supreme Court upheld this system of taxation in 1924 when it ruled that it was constitutional to tax Americans on their foreign earned income.<sup>3</sup> The United States is the only developed country in the world with this system of taxation.<sup>4</sup> Other countries with this type of tax system include Eritrea, North Korea, the Philippines, and Vietnam.<sup>5</sup> European nations, on the other hand, generally have a “territorial” system of taxation.<sup>6</sup> That is, European nations only tax income earned within their borders.<sup>7</sup>

Because of the worldwide system of taxation employed by the United States, Americans living abroad are subject to double taxation if the country in which they live also taxes them, which is likely.<sup>8</sup> As a result, Congress has enacted two code provisions to help ease the effects of

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1. Kristin Byrd, Comment, *Can We Provide a Level Playing Field for U.S. Corporations and Increase U.S. Jobs While Repealing the Extraterritorial Income Act?*, 5 Hous. Bus. & Tax L.J. 338, 345 (2005).

2. *Id.*; see also Marc J. Strohl, US Citizen Thinking of Accepting a Foreign Assignment? Some US Tax Matters You Should Know Before You Accept!, Expat Focus, <http://www.expatfocus.com/expatriate-taxation-us-citizens-abroad> (last visited Sept. 15, 2007) (comparing “world-wide” and “territorial” income tax schemes).

3. Cook v. Tait, 265 U.S. 47, 56 (1924).

4. Asia-Pacific Council of American Chambers of Commerce, *Taxation of Americans Working Overseas*, (June 2, 2006), <http://www.amcham.org.sg/resources/911-APCACPositionTaxationofAmericansJun06.pdf> [hereinafter Asia-Pacific].

5. *Id.*

6. Byrd, *supra* note 1, at 345.

7. *Id.* at 346.

8. Daniel J. Mitchell, *Tax Me Once, Shame on You. . . Tax Me Twice and the System Needs Fixing*, WASHINGTONPOST.COM THINK TANK TOWN, June 28, 2006, <http://www.washingtonpost.com/wp-dyn/content/article/2006/06/AR2006062701022.html>.

double taxation.<sup>9</sup> First, expatriate taxpayers can utilize the foreign tax credit to reduce their United States tax liability by the amount of foreign income taxes paid.<sup>10</sup> Second, a certain amount of foreign earned income is exempt from U.S. taxation under the foreign earned income exclusion if the taxpayer meets the requirements of section 911 of the Internal Revenue Code.<sup>11</sup> That section also allows certain housing expenses associated with living abroad to be excluded or deducted.<sup>12</sup>

The foreign earned income exclusion was first introduced in 1926.<sup>13</sup> The major policy reason Congress cited for implementing the exclusion was to put Americans working abroad in the same tax position as citizens working in the United States.<sup>14</sup> Several other policies supporting the exclusion have been posited by courts, scholars, and Congress over the eighty years since it was passed. One court has said that the exclusion was intended to allow U.S. citizens to compete in the international marketplace without being subject to double taxation.<sup>15</sup> Another rationale for the exclusion is that expatriates should not be required to pay for domestic federal resources and services that they do not use.<sup>16</sup> Perhaps most importantly, the exclusion is said to encourage American companies and their employees to go abroad, which increases U.S. exports and domestic jobs.<sup>17</sup>

Despite the many policy objectives it is said to serve, the foreign earned income exclusion has been the target of much controversy and debate since it was enacted.<sup>18</sup> As a result, it has been amended numerous times.<sup>19</sup> When it was first enacted, all foreign earned income of expatriates could be excluded if the taxpayer was a bona fide resident of a foreign country for more than six months.<sup>20</sup> The exclusion first came under fire in 1932 because some members of Congress believed it was not nec-

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9. Jeffrey Evans, Note, *911: The Foreign Earned Income Exclusion—Policy and Enforcement*, 37 VA. J. INT'L L. 891, 893 (1997).

10. I.R.C. § 901 (West Supp. 2007); *see also* Evans, *supra* note 9, at 893 (describing foreign tax credit).

11. I.R.C. § 911 (West Supp. 2007); *see also*, Evans, *supra* note 9, at 893 (describing section 911).

12. Hale E. Sheppard, *Perpetuation of the Foreign Earned Income Exclusion: U.S. International Tax Policy, Political Reality, and the Necessity of Understanding How the Two Intertwine*, 37 VAND. J. TRANSNAT'L L. 727, 731 (2004).

13. Renee Judith Sobel, *United States Taxation of Its Citizens Abroad: Incentive or Equity*, 38 VAND. L. REV. 101, 119 (1985).

14. *Id.* at 120.

15. *Brewster v. Comm'r*, 473 F.2d 160, 163 (D.C. Cir. 1972).

16. Sheppard, *supra* note 12, at 747.

17. Jerome J. McGabe, Changes to Section 911 Foreign Earned Income and its Adverse Impact to American Businesses and Citizens Abroad AmCham: Tax Hike Opposition (July 26, 2006), <http://amcham.org.hk/taxhike/?p=38>; *see also* Evans, *supra* note 9, at 895 (noting that such tax benefits historically were deemed improper for use by those who needed no encouragement to go overseas).

18. Jorge L. Riera, Note & Comment, *Agencies for Purposes of Section 911 of the Internal Revenue Code: The Foreign Earned Income Exclusion Survives 2003 Controversial Proposal to Repeal*, 10 ILSA J. INT'L & COMP. L. 161, 161–66, 168–69 (2003).

19. *Id.* at 163–69.

20. *Id.* at 163; *see also* Evans, *supra* note 9, at 895.

essary to reduce the effects of double taxation, given the availability of the foreign tax credit.<sup>21</sup> Nevertheless, the exclusion survived, and the only change made in that year was to disallow the exclusion of compensation paid by the United States.<sup>22</sup> Some scholars believe that this change was made because military personnel and government employees did not need incentives to move overseas, as it was required by their professions.<sup>23</sup>

In 1942, the foreign residency requirement was extended to one year in order to prevent taxpayers from moving overseas for the sole reason of avoiding taxes.<sup>24</sup> However, because the one year residency requirement was hard for expatriates to meet, the exclusion was again amended in 1951 so that a taxpayer qualified for the exclusion if he lived in a foreign country for an uninterrupted period that included a full taxable year.<sup>25</sup> Also in that year, Congress added a "physical presence" test (in addition to the "bona fide residence" test discussed in Section II.B) to encourage Americans with technical knowledge to move overseas.<sup>26</sup> The new requirement allowed expatriates to qualify for the exclusion if they were outside the United States for 510 or more days in eighteen consecutive months.<sup>27</sup>

Shortly after the 1951 changes, Congress realized that the exclusion was becoming a tax haven for many high-income taxpayers, such as movie stars who would qualify for the exclusion by making films in foreign countries.<sup>28</sup> Thus, in 1953, Congress put a \$20,000 cap on the exclusion for taxpayers utilizing the physical presence test to qualify.<sup>29</sup> The foreign earned income exclusion was codified at section 911 of the Internal Revenue Code, as it is now, in 1954.<sup>30</sup> During the 1960s, President Kennedy suggested limiting the exclusion only to Americans living in undeveloped countries.<sup>31</sup> However, Congress declined to impose such a restriction and instead capped the exclusion at \$20,000 for citizens using either the bona fide residence or physical presence test.<sup>32</sup> Expatriates satisfying the bona fide residence test for three years could exclude up to \$35,000 of income, but that provision was repealed in 1964.<sup>33</sup>

Some of the largest changes to the foreign earned income exclusion were made in the 1970s.<sup>34</sup> In 1976, the House suggested repealing the exclusion because of the fear that it treated overseas Americans better

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21. Evans, *supra* note 9, at 895.

22. *Id.*

23. *Id.* at 896.

24. Sobel, *supra* note 13, at 121-22.

25. *Id.* at 123.

26. Evans, *supra* note 9, at 896.

27. *Id.*

28. Sobel, *supra* note 13, at 123.

29. *Id.* at 124.

30. Riera, *supra* note 18, at 164.

31. *Id.* at 165.

32. *Id.*

33. *Id.*

34. Sobel, *supra* note 13, at 126-27.

than citizens living in the United States.<sup>35</sup> The Senate, on the other hand, did not want to totally eliminate the exclusion.<sup>36</sup> A compromise was reached through the Tax Reform Act of 1976 ("1976 Act"), which capped the exclusion at \$15,000 and imposed a stacking rule that taxed non-excluded income at rates as if no foreign income was excluded.<sup>37</sup> In addition, the 1976 Act prohibited overseas taxpayers from claiming a credit for foreign taxes paid on excluded income.<sup>38</sup> American companies with expatriate employees, particularly construction companies, harshly criticized these changes and Congress pushed back the effective date to 1978.<sup>39</sup>

The Foreign Earned Income Act of 1978 ("1978 Act") was passed soon after the 1976 amendments went into effect.<sup>40</sup> This Act made the foreign earned income exclusion available only to expatriates living in hardship areas or working for charities in undeveloped countries.<sup>41</sup> Moreover, the 1978 Act replaced the foreign earned income exclusion for other individuals with a deduction for the additional costs associated with working overseas.<sup>42</sup> The additional costs that could be deducted included the "general cost of living, housing, education, and, home leave costs."<sup>43</sup> However, the system of deductions was incredibly complex and was not well received by expatriates, companies, or even the Internal Revenue Service.<sup>44</sup> Attempts were made to alter the 1978 Act in 1980, but they failed because Congress opposed tax cuts at that time.<sup>45</sup>

The next changes to the foreign earned income exclusion were made through the Economic Recovery Tax Act of 1981.<sup>46</sup> Congress, hoping to promote U.S. business overseas and exports, did away with the deduction system and increased the maximum exclusion amount to \$75,000, with increases of \$5,000 per year, up to a maximum of \$95,000 in 1986.<sup>47</sup> Additionally, the time requirement of the physical presence test was reduced to 330 days in a twelve-month period.<sup>48</sup> Three years later, the provision was amended to provide that the \$95,000 cap would not be reached until 1990.<sup>49</sup>

Through the Tax Reform Act of 1986, the exemption cap was reduced to \$70,000.<sup>50</sup> The exclusion remained the same for over ten years, until it

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35. *Id.* at 127.

36. *Id.*

37. *Id.* at 127-28.

38. Evans, *supra* note 9, at 897.

39. *Id.* at 897-98.

40. Sobel, *supra* note 13, at 130.

41. *Id.*

42. Riera, *supra* note 18, at 166.

43. *Id.* at 166-67.

44. Sobel, *supra* note 13, at 138.

45. *Id.* at 140.

46. Riera, *supra* note 18, at 168.

47. Evans, *supra* note 9, at 898.

48. *Id.*

49. *Id.*

50. Riera, *supra* note 18, at 168.

was increased by \$2,000 per year starting in 1998, until it reached \$80,000.<sup>51</sup> That was the limit of the foreign earned income exclusion until it was amended by the Tax Increase Prevention and Reconciliation Act of 2005 (“TIPRA”).<sup>52</sup>

#### B. REQUIREMENTS AND PROCEDURES TO QUALIFY FOR THE FOREIGN EARNED INCOME EXCLUSION

In order to qualify for the foreign earned income exclusion under section 911, a taxpayer must have his tax home in a foreign country and meet either the bona fide residence test or the physical presence test.<sup>53</sup> A taxpayer’s tax home is his “main place of business or post of duty, regardless of where he maintains his family home.”<sup>54</sup> If a taxpayer does not have a main place of business, his tax home is where he regularly lives.<sup>55</sup> To meet the bona fide residence test, the taxpayer must be a United States citizen and establish that “he has been a bona fide resident of a foreign country or countries for an uninterrupted period which includes an entire taxable year. . . .”<sup>56</sup> The primary consideration in establishing bona fide residency in a foreign country is whether the taxpayer intends to reside there.<sup>57</sup> The IRS considers whether the taxpayer obtains a house or apartment, takes his family to the country, participates in the community, and other factors.<sup>58</sup>

A taxpayer satisfies the physical presence test if he is a citizen or resident of the United States and is present in a foreign country for at least 330 days during a consecutive twelve-month period.<sup>59</sup> Any twelve-month period is sufficient, including vacation and employment time spent in the foreign country.<sup>60</sup> However, only full days count toward the 330 days, which means “a period of twenty-four hours in a row, beginning at midnight.”<sup>61</sup> The minimum time requirements for both the bona fide residence and physical presence test will be waived if the taxpayer leaves the foreign country because of “war, civil unrest, or similar adverse conditions . . .” in that country.<sup>62</sup> In general, the physical presence test is preferable to the bona fide residence test.<sup>63</sup>

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51. *Id.* at 169.

52. *Id.*; see also Tax Increase Prevention and Reconciliation Act of 2005, Pub. L. No. 109-222, 120 Stat. 345 (2006) (codified in scattered sections of 26 U.S.C.) [hereinafter TIPRA].

53. I.R.C. § 911(d)(1) (West Supp. 2007).

54. Lance B. Gordon & E. Daniel Leightman, *Tax Planning for United States Citizens and Resident Aliens Working Abroad*, 15 Sw. U. L. Rev. 1, 7 (1984).

55. *Id.*

56. I.R.C. § 911(d)(1)(A).

57. Gordon & Leightman, *supra* note 54, at 8.

58. *Id.* at 9–10.

59. I.R.C. § 911(d)(1)(B).

60. Gordon & Leightman, *supra* note 54, at 11.

61. *Id.* at 12.

62. I.R.C. § 911(d)(4).

63. See Gordon & Leightman, *supra* note 54, at 11 (opining that, because of the subjectivity of the “bona fide residence” test, most taxpayers will wish to utilize the more objective “physical presence” test).

If an expatriate taxpayer meets the requirements of section 911, he can exclude a certain amount of his foreign earned income and housing costs.<sup>64</sup> Foreign earned income is defined as “the amount received by such individual from sources within a foreign country or countries which constitute earned income attributable to services performed by such individual. . . .”<sup>65</sup> Courts have consistently defined earned income as “all income not representing return on capital.”<sup>66</sup> Earned income includes wages, salaries, and professional fees, but does not include interest.<sup>67</sup> Housing expenses are the “reasonable expenses paid or incurred during the taxable year . . . for housing for the individual,” including his spouse and dependents, if they reside with him.<sup>68</sup> Deductible housing expenses include “rent, utilities, insurance, furniture rental, residential parking and household repairs.”<sup>69</sup> Lavish or extravagant housing expenses are not considered reasonable, and therefore, are not excludable.<sup>70</sup> In addition, the taxpayer’s total foreign earned income and housing cost exclusion under section 911 in a tax year cannot exceed his foreign earned income in that year.<sup>71</sup> Furthermore, no tax credit under section 901 is allowed for foreign taxes paid on income excluded under section 911.<sup>72</sup>

Under the version of section 911 in effect immediately prior to the 2006 amendments, the maximum foreign earned income exclusion was \$80,000 for 2006 and 2007.<sup>73</sup> The cap of \$80,000 would have been indexed for inflation starting in 2008.<sup>74</sup> The taxpayer could also deduct certain foreign housing costs.<sup>75</sup> The only requirement for the housing cost exclusion was that the costs be reasonable.<sup>76</sup> According to one source, this requirement basically allowed for an unlimited foreign housing cost exclusion.<sup>77</sup> The taxpayer could exclude or deduct, if not reimbursed for them by his employer, the excess of his reasonable housing expenses over the base housing amount.<sup>78</sup> The base housing amount for 2006 before the amend-

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64. I.R.C. § 911(a).

65. *Id.* § 911(b)(1)(A).

66. *United States v. Van Dyke*, 696 F.2d 957, 962 (Fed. Cir. 1982); *Robida v. Comm’r*, 460 F.2d 1172, 1174 (9th Cir. 1972).

67. Lesli S. Laffie, *New Rules for Individuals Working Abroad*, J. OF ACCT., Dec. 2006, at 84, 84.

68. I.R.C. § 911(c)(3)(A).

69. Laffie, *supra* note 67, at 84.

70. I.R.C. § 911(c)(3)(A).

71. *Id.* § 911(d)(7).

72. *Id.* § 911(d)(6); see also Arthur H. Kohn et al., *Recent Changes to U.S. Federal Income Tax Rules for U.S. Employees Relocated Abroad*, EMP. BENEFIT PLAN REV., Aug. 2006, at 10, 11.

73. Howard Godfrey & Neil A. J. Sullivan, *The Post-TIPRA Foreign Earned Income and Housing Exclusions for Individuals*, 37 TAX ADVISER 716, 716 (2006).

74. *Id.*

75. Gordon & Leightman, *supra* note 54, at 28.

76. Martin Vaughn, *U.S. Business Groups Abroad Rally Against Tax Increase*, CONGRESS DAILY, June 16, 2006, 2006 WLNR 10505636, available at <http://www.nationaljournal.com/about/congressdaily/>.

77. Anna Teo, *U.S. Tax Law Riles American Expats*, BUS. TIMES (SINGAPORE), June 17, 2006, 2006 WLNR 10714745.

78. Gordon & Leightman, *supra* note 54, at 28.



ments was "sixteen percent of the annual salary of a GS-14, step 1, United States government employee."<sup>79</sup> That salary for 2006 was \$77,793, meaning that any "reasonable" housing costs above \$12,447 (16% of \$77,793) would have been deductible.<sup>80</sup>

In order to elect the benefits of the foreign earned income exclusion, a taxpayer must file Form 2255 with the IRS.<sup>81</sup> The election form must contain enough information so that the IRS can determine if the individual qualifies for the section 911 exclusions.<sup>82</sup> The taxpayer's name, social security number, employer, and amount of foreign earned income for the year should be included, as well as the foreign country that is his tax home, the date on which he established that tax home, and whether he is utilizing the bona fide residence or physical presence test to qualify.<sup>83</sup> An expatriate can use Form 673 to avoid having his employer withhold on his excludable foreign earned income.<sup>84</sup> If a married couple resides abroad, and both the husband and the wife qualify for section 911, it is possible for each to exclude foreign earned income and exclude or deduct housing costs.<sup>85</sup> As a result, the couple may be entitled to twice the maximum deduction in a given year.<sup>86</sup> If spouses file a joint return, they can choose to compute the amount of excludable or deductible housing costs separately or together.<sup>87</sup> As the history and provisions of section 911 indicate, the foreign earned income exclusion is complicated and controversial. This complexity and controversy has continued in recent years, as discussed in Section III.

### III. RECENT DEBATE OVER THE FOREIGN EARNED INCOME EXCLUSION

The debate over the foreign earned income exclusion has been particularly heated in recent years, as repeal attempts have been renewed.<sup>88</sup> For example, President Clinton proposed in his 1996 budget proposal that it be repealed.<sup>89</sup> Moreover, Iowa Senator Chuck Grassley, then Republican chairman of the Senate Finance Committee, moved to repeal the exclusion in 2003.<sup>90</sup> Grassley referred to section 911 as "an unnecessary 'subsidy' and contended that it did little to increase U.S. exports."<sup>91</sup> As a result of Grassley's efforts, a total repeal of the exclusion was actually

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79. *Id.*

80. Godfrey & Sullivan, *supra* note 73, at 716.

81. Gordon & Leightman, *supra* note 54, at 58.

82. *Id.*

83. *See id.* (listing all information required on Form 2255).

84. Strohl, *supra* note 2.

85. Gordon & Leightman, *supra* note 54, at 55.

86. *Id.*

87. Godfrey & Sullivan, *supra* note 73, at 720.

88. Sheppard, *supra* note 12, at 732.

89. Evans, *supra* note 9, at 891.

90. Riera, *supra* note 18, at 162.

91. Dan Bilefsky, *Americans Abroad Face Higher U.S. Tax Bills*, INT'L HERALD TRIB., May 13, 2006, available at <http://www.iht.com/articles/2006/05/12/news/expats.php>.

passed in the Senate as part of the Jobs and Growth Tax Relief and Reconciliation Act.<sup>92</sup> However, this controversial repeal was taken out of the Act before it passed due to the lobbying efforts of corporations, which went all the way up to President Bush.<sup>93</sup> The exclusion was again threatened in the Senate in 2004 when it passed an amendment which would cap the total exclusion, including both the foreign earned income and housing cost exclusions, at \$80,000.<sup>94</sup> However, this provision was not signed into law.<sup>95</sup>

Despite the numerous attempts to eliminate the foreign earned income exclusion over the years, many groups strongly support it.<sup>96</sup> Groups that have called for its continuation include Democrats Abroad, the Center for Freedom and Prosperity, the Section 911 Coalition, and the U.S. Chamber of Commerce.<sup>97</sup> Former Louisiana Senator John Breaux, a Democrat, and former Speaker of the House, Newt Gingrich, a Republican, have also supported the exclusion.<sup>98</sup> Given the significant debate that has surrounded the foreign earned income exclusion over the years, it is not a complete surprise that it was again threatened, this time successfully, in 2006.<sup>99</sup>

#### IV. 2006 AMENDMENTS TO SECTION 911 (TAX INCREASE PREVENTION AND RECONCILIATION ACT)

##### A. OVERVIEW OF TAX INCREASE PREVENTION AND RECONCILIATION ACT

On May 17, 2006, the Tax Increase Prevention and Reconciliation Act of 2005 (“TIPRA”) became law.<sup>100</sup> Overall, TIPRA included \$90 billion in tax cuts and \$20 billion in tax increases.<sup>101</sup> TIPRA did more than amend the foreign earned income and housing cost exclusion; it extended the lower tax rates for capital gains and dividends for two years, extended and increased alternative minimum tax exemption levels, increased the age at which children are subject to the “Kiddie tax” to eighteen, and

92. Sen. Grassley's Finance Committee Staff Issues Background Fact Sheet on Section 911, US FED. NEWS, May 25, 2006, 2006 WLNR 9032277 [hereinafter *Fact Sheet*]; see also Riera, *supra* note 18, at 174 (controversial plan would have eliminated tax exemption for over 358,000 expatriates).

93. Bilefsky, *supra* note 91; see also George G. Jones & Mark A. Luscombe, *TIPRA Raises Price Tag for Americans Working Abroad*, ACCT. TODAY, Aug. 7, 2006, at 10, 16, available at [http://www.webcpa.com/current\\_issue.cfm?issuedate=2006-08-07&pub=ato](http://www.webcpa.com/current_issue.cfm?issuedate=2006-08-07&pub=ato) (2003 effort was the second attempt to repeal the foreign earned income exclusion).

94. *Fact Sheet*, *supra* note 92.

95. *Id.*

96. Sheppard, *supra* note 12, at 754.

97. *Id.* at 754–55.

98. Riera, *supra* note 18, at 175; see also Newt Gingrich & Ken Kies, Op-Ed, *Our Taxed Expats*, WALL ST. J., June 28, 2006, at A14; Jeannine Menzies, *Gingrich Opposes “Expatriate Tax”*, THE ROYAL GAZETTE, BERMUDA, June 1, 2006, <http://www.new.org/backpage.asp?art=3083>.

99. Jones & Luscombe, *supra* note 93, at 10.

100. TIPRA, *supra* note 52. See also Jones & Luscombe, *supra* note 93, at 10.

101. Lawrence W. Kowalski & Phillip J. Schurrer, *Analysis of the Tax Increase Prevention and Reconciliation Act of 2005*, CATALYST, Sept.-Oct. 2006, at 56, 56.

extended section 179 expensing for small businesses.<sup>102</sup> One commentator has noted that changes made by TIPRA are “far-reaching, important, and will affect many different types of taxpayers.”<sup>103</sup> This is certainly true for those changes relating to the section 911 foreign earned income exclusion.

#### B. CHANGES TO SECTION 911 FOREIGN EARNED INCOME EXCLUSION

TIPRA amended the foreign earned income exclusion in three ways.<sup>104</sup> First, the maximum exclusion for foreign earned income is indexed for inflation starting in 2006, as opposed to 2008 under the previous law.<sup>105</sup> As a result of this change, the maximum income exclusion was \$82,400 in 2006.<sup>106</sup> The maximum exclusion in later years will be indexed utilizing the cost of living adjustment.<sup>107</sup> This change is actually beneficial to expatriates, as they were now able to shield \$2,400 more of their foreign earned income from U.S. taxes in 2006. However, that is where the benefits of TIPRA end.

Second, TIPRA capped the exclusion for housing costs under section 911.<sup>108</sup> Under TIPRA, the base housing amount is sixteen percent of the foreign earned income exclusion limit in a given year, rather than sixteen percent of the grade GS-14, step 1, United States government employee salary.<sup>109</sup> This means that only housing costs above sixteen percent of \$82,400, or \$13,184, can be excluded or deducted in 2006.<sup>110</sup> Moreover, excludable housing expenses are limited under TIPRA to thirty percent of the foreign earned income exclusion amount.<sup>111</sup> Thus, the housing exclusion is capped at 30 percent of \$82,400, or \$24,720, for 2006.<sup>112</sup> Overall, these changes mean that the maximum housing exclusion for 2006 is \$11,536.<sup>113</sup> If a taxpayer does not satisfy the bona fide residence or physical presence test for the entire taxable year, this amount will be prorated based on the amount of the daily foreign earned income exclusion and the number of days in which section 911 was satisfied.<sup>114</sup> The Joint Committee on Taxation explained that these changes were meant to “tie the employer-provided housing exclusion to the foreign earned income cap to

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102. *Id.*

103. *Id.*

104. Eileen Sherr & Andrew M. Mattson, *International Provisions of TIPRA*, 37 TAX ADVISER 400, 400 (2006).

105. TIPRA, *supra* note 52, § 515(a); *see also* Sherr & Mattson, *supra* note 104, at 400.

106. Sherr & Mattson, *supra* note 104, at 400.

107. I.R.C. § 911(b)(2)(D)(ii) (West Supp. 2007).

108. Sherr & Mattson, *supra* note 104, at 400.

109. I.R.C. § 911(c)(1); *see also* Sherr & Mattson, *supra* note 104, at 400.

110. Godfrey & Sullivan, *supra* note 73, at 716.

111. *Id.*

112. *Id.*

113. *Id.* The limit can be calculated as follows:  $(\$82,400 \times .3) - (\$82,400 \times .16) = \$24,720 - \$13,184 = \$11,536$ . *See id.*; Jones & Luscombe, *supra* note 93, at 10.

114. Godfrey & Sullivan, *supra* note 73, at 716.

bring the two exclusions into conformity.”<sup>115</sup> In addition, the changes were intended to set an objective cap on “reasonable housing expenses” because the Committee believed that the previous law resulted in “generous interpretation by the taxpayer.”<sup>116</sup>

The housing exclusion cap implemented by TIPRA is much lower than the basically unlimited housing cost exclusion under the prior law.<sup>117</sup> However, TIPRA did give the Secretary authority to “issue regulations or other guidance providing for the adjustment of the percentage . . . on the basis of geographic differences in housing costs relative to housing costs in the United States.”<sup>118</sup> The IRS notice exercising this authority is discussed in Section VI.

The third change made to the foreign earned income exclusion by TIPRA was to impose a stacking rule.<sup>119</sup> Under this provision, “income excluded as either foreign earned income or as a housing allowance is included for purposes of determining the marginal tax rates applicable to non-excluded income.”<sup>120</sup> As a result of this change, if a taxpayer “has \$80,000 of foreign earned income excluded under § 911 and \$20,000 in other income,” he will pay tax “on the \$20,000 at the rate(s) applicable to income in the \$80,000-\$100,000 range.”<sup>121</sup> Under prior law, the taxpayer would have paid tax on the \$20,000 at rates applicable had that been the individual’s only income, which are much lower.<sup>122</sup>

The stacking rule employs a tax method called “exemption with progression,” which causes taxpayers to pay a higher percentage of their income in taxes.<sup>123</sup> The Joint Committee on Taxation explained that the stacking rule was implemented to prohibit “taxpayers from benefiting twice from graduated rate structures, once in the foreign country in the determination of the foreign tax liability on their foreign income, and again in the United States in the determination of their U.S. tax liability on any other income.”<sup>124</sup> Scholars have suggested that the stacking rule will be the most costly TIPRA change for Americans living overseas.<sup>125</sup>

The Joint Committee on Taxation expects that the TIPRA changes made to section 911 will raise \$2.1 billion in the next ten years.<sup>126</sup> These

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115. STAFF OF THE JOINT COMM. ON TAXATION, 109TH CONG., *Options to Improve Tax Compliance and Reform Tax Expenditures* 175 (Jan. 27, 2005), available at <http://www.house.gov/jct/s-2-05.pdf>.

116. *Id.*

117. Teo, *supra* note 77.

118. I.R.C. § 911(c)(2)(B) (West Supp. 2007).

119. Sherr & Mattson, *supra* note 104, at 400.

120. *Id.*

121. Godfrey & Sullivan, *supra* note 73, at 716.

122. Jones & Luscombe, *supra* note 93, at 10.

123. Nancy MacEntee, *No U.S. Tax Relief for American Expats in Russia*, AMCHAM NEWS, Dec. 2006, at 18, 18, available at [http://www.amchamnews.ru/issue74/us\\_expats\\_taxes\\_moscow](http://www.amchamnews.ru/issue74/us_expats_taxes_moscow).

124. *Options to Improve Tax Compliance and Reform Tax Expenditures*, *supra* note 115, at 177.

125. Jones & Luscombe, *supra* note 93, at 10.

126. Vaughn, *supra* note 76.

tax increases were intended to partially offset tax cuts in other areas included in TIPRA.<sup>127</sup> In addition, the Senate Finance Committee felt that the provisions would set “an objective standard for determining the amount that taxpayers working abroad can exclude from income, and also . . . subject such individuals to the same tax rates applicable to those living and working in the U.S. who have the same amount of economic income.”<sup>128</sup> Apparently, the Senate Finance Committee felt that the previous version of section 911 put Americans living overseas “in a better position with respect to taxable income, compared with Americans at home, just because the individual lives and works outside the U.S.”<sup>129</sup> Senator Chuck Grassley, largely responsible for the 2006 changes to section 911, felt that the prior law was too generous for American expatriates.<sup>130</sup> He issued a press release reporting that just over 306,000 American taxpayers claimed the foreign earned income exclusion in 2003, with only about 125,000, or approximately forty percent, of those taxpayers actually owing any taxes to the United States.<sup>131</sup> He also felt that the housing exclusion permitted “highly compensated individuals to exclude large amounts of housing benefits.”<sup>132</sup> Shortly after the amendments were passed, Grassley said that they would equate the amount of taxes owed by overseas Americans with those owed by taxpayers at home “as a matter of tax fairness.”<sup>133</sup>

### C. HOW SECTION 911 CHANGES WERE PASSED

One of the most notable aspects of the 2006 amendments to the foreign earned income exclusion is how they were passed. The section 911 changes were not part of the Senate or House versions of TIPRA.<sup>134</sup> Instead, the amendments were inserted by Senator Grassley at the last minute.<sup>135</sup> As a result, the changes avoided debate by Congress.<sup>136</sup> One source said the changes caught everyone off guard.<sup>137</sup> As a result, American citizens living abroad were blindsided and were not able to voice their concerns to their Congressional representatives before the legislation was signed.<sup>138</sup>

Former Speaker of the House of Representatives Newt Gingrich, who opposed the 2006 changes to section 911 and has suggested that they be

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127. *Id.*

128. Sherr & Mattson, *supra* note 104, at 400.

129. Anna Teo, *Battling the 911 of US Tax Rule*, BUS. TIMES (SING.), Aug. 12, 2006, 2006 WLNR 13928823.

130. Vaughn, *supra* note 76; *see also Fact Sheet*, *supra* note 92.

131. *Fact Sheet*, *supra* note 92.

132. *Id.*

133. Vaughn, *supra* note 76.

134. Jones & Luscombe, *supra* note 93, at 10.

135. *Id.*

136. *Taxing Americans Abroad: Costing More Over There*, ECONOMIST, June 24, 2006, at 66 [hereinafter *Taxing Americans Abroad*].

137. Teo, *supra* note 77.

138. Brian Knowlton, *New Bill Seeks to Ease Expat Income Taxes*, INT'L HERALD TRIB., June 15, 2006, available at <http://www.iht.com/articles/2006/06/15/news/tax.php>.

repealed, commented that the way in which the changes were passed was a “scandal.”<sup>139</sup> Gingrich also noted that quietly putting the amendments into the last version of the bill was “bad legislative procedure.”<sup>140</sup> However, members of Senator Grassley’s staff, in response to suggestions that the changes were a surprise, claimed that they “ha[d] been in the works for at least several years.”<sup>141</sup>

#### D. AMENDMENTS ARE RETROACTIVE

Another important point is that the TIPRA changes to the foreign earned income exclusion are retroactive.<sup>142</sup> Although the law was not effective until May 17, 2006, the changes apply to tax years beginning after December 31, 2005.<sup>143</sup> As a result, the 2006 tax bills of foreign living American citizens will be affected by the TIPRA amendments. The retroactive nature of the change means that these citizens will “face an increased tax burden they are not prepared for.”<sup>144</sup> One commentator said that “people who started out 2006 in another country planning to write off their housing costs suddenly were facing a potentially huge, unexpected IRS bill.”<sup>145</sup> Even if the taxpayer was not planning on excluding substantial foreign housing costs, the new stacking rule may cause his taxes to increase, a change he could not have anticipated when 2006 began.

#### E. EFFECTS OF THE AMENDMENTS AND SUGGESTIONS FOR TAXPAYERS

Overall, the 2006 amendments to the foreign earned income exclusion will cause the tax liabilities of Americans living overseas to increase.<sup>146</sup> This is a result of the new cap on excludable or deductible housing expenses and the stacking rule.<sup>147</sup> Some scholars estimate that taxes could increase by more than \$25,000 for some overseas taxpayers.<sup>148</sup> Taxpayers who must pay the alternative minimum tax may have an even larger tax increase.<sup>149</sup> These changes will have the largest effect on those taxpayers living in countries that impose little or no income tax of their own.<sup>150</sup> In

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139. Menzies, *supra* note 98; Posting of Newt Gingrich to HumanEvents.com, <http://www.humanevents.com/article.php?id=15560> (June 12, 2006) [hereinafter Gingrich].

140. Gingrich, *supra* note 139.

141. Keith Bradsher & David Cay Johnston, *Americans Living Abroad Get a Nasty Tax Surprise*, N.Y. TIMES, May 29, 2006, at C3.

142. TIPRA, *supra* note 52, § 515(d).

143. *Id.*

144. Teo, *supra* note 77.

145. Don't Mess With Taxes, [http://dontmesswithtaxes.typepad.com/dont\\_mess\\_with\\_taxes/2006/10/wide\\_world\\_of\\_t.html](http://dontmesswithtaxes.typepad.com/dont_mess_with_taxes/2006/10/wide_world_of_t.html) (Oct. 9, 2006, 16:01 EST).

146. Godfrey & Sullivan, *supra* note 73, at 716.

147. *Id.*

148. Teo, *supra* note 129.

149. Jessica Cutrera, *US Expats Take Another Hit*, MONEY TALKS, July-Aug. 2006, [http://www.moneytalks-online.com/july-august\\_06/focus\\_on\\_USA.html](http://www.moneytalks-online.com/july-august_06/focus_on_USA.html).

150. John E. Allis et al., *The Increased Costs of Working Abroad*, 37 TAX ADVISER 642 (2006).

addition, taxpayers with “a working spouse, investments or other income will be affected as well.”<sup>151</sup> However, the full effects of the new foreign earned income and foreign housing cost exclusions will not be fully known until 2006 tax returns are filed and examined by the IRS.<sup>152</sup>

There are steps, if taken shortly after learning of the TIPRA amendments, that could help a taxpayer deal with the unexpected tax increases they caused. First, a taxpayer could increase his estimated tax payments or withholding amounts.<sup>153</sup> This would prevent the taxpayer from having to come up with the large excess tax payment when taxes are due for the 2006 tax year. A taxpayer can change the amount of taxes withheld from his salary by changing Form 673, which is filed with his employer in order to determine withholding amounts.<sup>154</sup> In addition, many employers of overseas Americans will need to increase financial accruals for additional tax costs of their employees.<sup>155</sup> This is because most employers have “tax equalization programs,” meaning that they reimburse employees for any additional taxes incurred as a result of working overseas.<sup>156</sup> If a taxpayer and/or his or her company employed these techniques early in response to the section 911 amendments, they will be better positioned to bear the resulting increased tax burden.

## V. REACTIONS TO 2006 AMENDMENTS

Immediately after the TIPRA amendments to the foreign earned income exclusion were passed, the international American community became outraged.<sup>157</sup> Estimates have put the number of American citizens working abroad at around four million, although these individuals are not counted by the United States Census.<sup>158</sup> Regardless of the number, it appears that nearly all American expatriates are upset about the changes.<sup>159</sup> One practicing accountant said that TIPRA is “a misnomer when it comes to certain Americans working abroad.”<sup>160</sup>

One expatriate, Al Costlow, who lives in Singapore, said that these changes “cannot be good for our country.”<sup>161</sup> Rudolph A. Muller, also an American living in Singapore, said, “the United States of America [is] the clear leader of the ‘Taxis of Evil’ for taxing citizens working

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151. *Id.*

152. Mary Swire, *US Expats Look To Home As Tax Changes Bite*, TAX-NEWS.COM, Dec. 1, 2006, [http://www.tax-news.com/asp/story/story\\_print.asp?storyname=25628](http://www.tax-news.com/asp/story/story_print.asp?storyname=25628).

153. Allis et al., *supra* note 150, at 642.

154. *Id.*

155. *Id.*

156. Cheryl de Mesa Graziano, *TIPRA: What It Does. . . and Does Not Cover*, FIN. EXECUTIVE, July-Aug., 2006, at 46.

157. Teo, *supra* note 77.

158. Jones & Luscombe, *supra* note 93, at 10.

159. Teo, *supra* note 77.

160. Don D. Nelson, *New Law Retroactively Hikes Taxes for Americans Working Abroad*, <http://www.taxmeless.com/2006expatlawchange.htm> (last visited Sept. 21, 2007).

161. Expatriates From Around the Region Speak About TIPRA/911 Tax Changes and the Effect on Their Families and Businesses, [http://www.amcham.org.sg/resources\\_quotes.html](http://www.amcham.org.sg/resources_quotes.html) (last visited Sept. 21, 2007).

abroad.”<sup>162</sup> The changes have also been criticized as “[a]nother blow to U.S. competitiveness.”<sup>163</sup> Among the groups and individuals that oppose the changes are the American Chamber of Commerce, the National Foreign Trade Council, Senator Jim DeMint of South Carolina, and former Speaker of the House Newt Gingrich.<sup>164</sup>

#### A. REACTIONS OF EXPATRIATES LIVING IN HIGH-COST, LOW-TAX AREAS

Expatriates who are affected most by the changes to the foreign earned income and housing exclusion, and are thus the most upset by them, are those living in high-cost, low-tax areas of the world.<sup>165</sup> For example, taxpayers in Hong Kong, Singapore, Dubai, Japan, and London have been cited as the hardest hit by the tax changes.<sup>166</sup> The reason that these taxpayers are most affected is that those areas have extremely high housing costs, and, because of TIPRA, housing costs in excess of the \$11,536 cap (absent changes made by the Treasury, discussed in Section VI) must be included in the taxpayer’s gross income if they are reimbursed by the taxpayer’s employer.<sup>167</sup> If they are not reimbursed, the taxpayer must pay these high housing costs without the benefit of a deduction after the \$11,536 cap.<sup>168</sup> Taxpayers in countries that already have high tax rates are not as greatly impacted because they can still utilize the foreign tax credit to offset their U.S. tax liability.<sup>169</sup>

American citizens living in Hong Kong and Singapore have probably been the most outspoken in opposing the changes to section 911.<sup>170</sup> A tax consultant estimated that “a typical American couple living in Hong Kong could see their US tax payments more than triple as a result [of the amendments].”<sup>171</sup> One source estimated that the tax liability for those in Singapore could increase by as much as five times.<sup>172</sup>

The New York Times published an article shortly after the amendments were passed explaining that the owner of a gift shop in Singapore, Kristine Kraabel, expected her family’s taxes to triple.<sup>173</sup> For the Kraabels, this meant they would owe an additional \$20,000 to \$25,000 in American

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162. *Id.*

163. *Id.*

164. Knowlton, *supra* note 138; *Taxing Americans Abroad*, *supra* note 136, at 66; Teo, *supra* note 129; Vaughn, *supra* note 76.

165. Cutrera, *supra* note 149.

166. *Id.*; see also Sherr & Mattson, *supra* note 104, at 400.

167. See Teo, *supra* note 77.

168. See *Options to Improve Tax Compliance and Reform Tax Expenditures*, *supra* note 115, at 175.

169. AmCham Shanghai’s Fast Facts on Section 911: How Changes in the U.S. Tax Code Will Affect You, June 16, 2006, <http://www.hkchcc.org/newsletter1.htm>.

170. Jake Vanderkamp, *American Expats Should Give the Taxman a Call and Raise the Roof*, S. CHINA MORNING POST, Oct. 17, 2006, at 18; see also Teo, *supra* note 77.

171. Vanderkamp, *supra* note 170, at 18.

172. Teo, *supra* note 77.

173. Bradsher & Johnston, *supra* note 141, at C3.



taxes for 2006.<sup>174</sup> The Kraabels were particularly upset by the changes because, before moving to Singapore, they lived in Iowa, the state represented by Senator Grassley, who was largely responsible for the section 911 amendments included in TIPRA.<sup>175</sup> Kraabel wrote an irate letter to Senator Grassley, urging, "We are your constituents, whose interests you condemn and refuse to represent."<sup>176</sup>

The executive director of the American Chamber of Commerce ("AmCham") Singapore chapter, Nicholas de Boursac, has been extremely critical of the changes.<sup>177</sup> He said that the changes were "based on the misguided idea that this would put Americans abroad on equal footing with Americans at home."<sup>178</sup> De Boursac further criticized American taxation of its citizens abroad as "completely out of step with the international norm."<sup>179</sup> An estimated 15,000 to 17,000 American citizens reside in Singapore.<sup>180</sup> De Boursac believes that the amendments will cause many of those Americans, as well as those living in Hong Kong, to return to the United States to avoid the burden of additional taxes.<sup>181</sup> In fact, according to a poll conducted by AmCham Singapore in October and November of 2006, forty percent of American citizens living there were considering returning to the United States because of the higher taxes.<sup>182</sup> De Boursac also indicated that AmCham Singapore has heard from some companies—those that bear the cost of the additional taxes of their employees through tax equalization programs—that they plan on sending American employees back to the United States.<sup>183</sup>

Expatriates in these high-cost, low-tax areas have been encouraged by practitioners and groups like AmCham and American Citizens Abroad to be proactive in opposing the section 911 changes.<sup>184</sup> One practitioner urged Americans living abroad to contact their local congressmen and senators to voice opposition to the amendments.<sup>185</sup> Newt Gingrich also encouraged overseas Americans to lobby their representatives in Washington, saying, "What is important now is for everyone who is busy trying to sell American products world-wide to get the message across to the president and the Congress that they need to repeal this and make it competitive for Americans to work in the world market."<sup>186</sup> Expatriates have

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174. *Id.*

175. *Id.*

176. *Id.*

177. Teo, *supra* note 77; Teo, *supra* note 129.

178. Teo, *supra* note 77.

179. Teo, *supra* note 129.

180. Teo, *supra* note 77.

181. Teo, *supra* note 129.

182. Doreen Carvajal, *Tax Leads Americans Abroad to Renounce U.S.*, N.Y. TIMES, Dec. 18, 2006, at A6; Swire, *supra* note 152.

183. Teo, *supra* note 129.

184. Cutrera, *supra* note 149; *Post-Election Congress Receptive to Tax Relief*, AMERICAN CITIZENS ABROAD NEWS, Dec. 2006-Jan. 2007, <http://www.aca.ch/acan155.htm> [hereinafter *Post-Election Congress*].

185. Cutrera, *supra* note 149.

186. Menzies, *supra* note 98.

also been told to tell their similarly-situated friends, who may not know about the changes or their impact because they were passed quickly.<sup>187</sup> Further, AmCham suggested that overseas Americans ask their employers to pay the additional taxes, if they do not already, and negotiate tax equalization programs when renewing their contracts.<sup>188</sup>

In addition to individual opposition efforts, expatriate groups like AmCham have lobbied in Washington for repeal of the amendments.<sup>189</sup> The American Business Council of Gulf Countries (“ABCGC”), in a response to Senator Grassley’s press release relating to TIPRA’s section 911 changes, argued that housing benefits provided by employers are “necessary to encourage employees to relocate abroad and should be exempt from taxation.”<sup>190</sup> ABCGC further argues that the housing cap was arbitrary and does not relate to the actual cost of housing overseas.<sup>191</sup> As a result, ABCGC calls for removing the cap on the housing cost exclusion.<sup>192</sup> In addition, according to ABCGC, the foreign earned income exclusion should be increased to at least \$150,000 in order to account for inflation and devaluation of the U.S. dollar since 1986, when the exclusion was first limited to \$80,000.<sup>193</sup> Similarly, AmCham Singapore wants to remove any limits on the foreign earned income exclusion.<sup>194</sup> AmCham is raising money from corporations to hire a consultant in order to “educate” Congress and the President on the benefits of the exclusion and to lobby for removal of the limits.<sup>195</sup>

Opposition groups are also pursuing the formation of a bipartisan caucus of congressmen and senators to “address the interests of the estimated 4.1 million American citizens living abroad.”<sup>196</sup> Many overseas Americans feel that the caucus would be a “constructive way of establishing a fruitful two-way dialogue between Washington legislators and the overseas American community.”<sup>197</sup> Nebraska Senator Chuck Hagel, a Republican, supports the idea of a caucus, and the Federation of American Women’s Clubs Overseas recently reported that the idea was well-received by both parties during Overseas Americans Week.<sup>198</sup>

187. Cutrera, *supra* note 149.

188. Teo, *supra* note 77.

189. *Id.*

190. AM. BUS. COUNCIL OF THE GULF COUNTRIES, RESPONSE TO BACKGROUND FACT SHEET ON SECTION 911 2 (July 19, 2006), <http://www.amcham.org.sg/resources/911-grassley-staff-ABCGC-reponse.pdf> [hereinafter ABCGC].

191. *Id.* at 4–6.

192. *Id.* at 6.

193. *Id.*

194. AMCHAM SINGAPORE WHITE PAPER ON THE TAXATION OF THE EARNED INCOME OF US CITIZENS ABROAD 3 (Oct. 11, 2006), [http://www.amcham.org.sg/resources\\_us\\_tax\\_changes.html](http://www.amcham.org.sg/resources_us_tax_changes.html) (follow “AmCham Singapore White paper” hyperlink).

195. *Id.*

196. Dan De Luce, *Americans Abroad See Tough Fight Over Taxes*, INT’L HERALD TRIB., June 22, 2006, <http://www.ihf.com/articles/2006/06/22/news/taxes.php>.

197. The Federation of American Women’s Clubs Overseas, Inc., *Overseas Americans Week 2006—Washington*, [http://www.fawco.org/indes.php?option=com\\_content&task=view&id=240&Itemid=341.html](http://www.fawco.org/indes.php?option=com_content&task=view&id=240&Itemid=341.html) (last visited Sept. 21, 2007).

198. *Id.*; see also De Luce, *supra* note 196.

B. EFFECTS ON CORPORATIONS: ENCOURAGED TO HIRE OTHER NATIONALITIES AND SEND AMERICANS HOME

One of the major arguments made by opponents to the section 911 amendments is that they dissuade corporations from hiring American citizens.<sup>199</sup> The reason for this effect is that most corporations have tax equalization programs under which they reimburse their overseas employees for additional tax costs incurred as a result of living abroad.<sup>200</sup> Corporations will now be required to choose between raising salaries to compensate for the tax increases and decreasing the number of Americans they send abroad.<sup>201</sup> Most corporations will probably be forced to reduce the number of Americans sent abroad in order to avoid the need to raise prices.<sup>202</sup> This is because if companies that employ Americans increase prices, they will be unable to compete with foreign competitors who are able to “charge lower prices for comparable products.”<sup>203</sup> A study performed by economics professor John Mutti found that “each 1% increase in compensation costs reduced demand for Americans employed abroad by 0.4%.”<sup>204</sup> Instead of hiring Americans, expatriates argue that multi-national corporations will hire other nationalities, such as Australians, Britons, or Canadians.<sup>205</sup> This is a result of the fact that companies will not have to pay additional taxes for those employees because their governments do not cap the income they can exclude from taxes.<sup>206</sup>

With fewer Americans working abroad, the United States will experience a reduction in its competitive position.<sup>207</sup> Having Americans present abroad is beneficial to the United States because they promote awareness of the American way of life and foster a positive image of the United States.<sup>208</sup> One expatriate said “We are 4.1 million ambassadors living outside the U.S. We buy American products, fly American airlines, send our children to American universities and improve the image of Americans overseas. Why are we being punished?”<sup>209</sup> Furthermore, the optimistic revenue estimates of \$2.1 billion for the tax increases may not prove true if companies send their American employees home and hire other nationalities, which could defeat one of Congress’s main purposes

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199. Cutrera, *supra* note 149.

200. *Id.*; see also Evans, *supra* note 9, at 911.

201. *Taxing Americans Abroad*, *supra* note 136, at 66.

202. See Sheppard, *supra* note 12, at 744–45.

203. *Id.* at 745.

204. *Taxing Americans Abroad*, *supra* note 136, at 66.

205. Bradsher & Johnston, *supra* note 141, at C3.

206. *Id.*

207. Teo, *supra* note 77.

208. Posting of Jerome J. McCabe, *Changes to Section 911 Foreign Earned Income and its Adverse Impact to American Businesses and Citizens Abroad*, to AmCham: Tax Hike Opposition, <http://amcham.org.hk/taxhike/?p=38> (July 26, 2006, 14:17 EST). But see Sheppard, *supra* note 12, at 748.

209. Dan Bilefsky, *Americans Abroad Outraged Over Tax Changes*, INT’L HERALD TRIB., May 16, 2006, <http://www.iht.com/articles/2006/05/16/business/expats.php>.

in passing the amendments to section 911.<sup>210</sup>

### C. A DECREASE IN EXPORTS

In addition to the incentive that the TIPRA amendments give to corporations to hire other nationalities, expatriates and other supporters of the foreign earned income exclusion argue that they will also result in a decrease in U.S. exports.<sup>211</sup> The theory behind this position is that “Americans working overseas actively promote U.S. exports of goods and services sold by their own companies, as well as ‘buying American’ in overseas markets.”<sup>212</sup> An economic analysis performed by PricewaterhouseCoopers (“PwC”) in 2005 found that total repeal of the foreign earned income exclusion would reduce U.S. exports by \$8.1 billion.<sup>213</sup> That study also estimated that this decrease in exports would correspondingly cause domestic jobs in the United States to decrease by more than 77,000.<sup>214</sup> Because the TIPRA amendments did not completely repeal section 911, their effects on exports will probably not be as drastic as the PwC study predicted. However, TIPRA did greatly reduce the benefits of section 911 that encourage Americans to go overseas, and a significant reduction in exports will likely result.<sup>215</sup>

The PwC study also estimated that removing the cap on the foreign income exclusion, which was \$80,000 at the time of the study, would increase exports by \$14.4 billion and support in excess of 137,000 jobs in the United States.<sup>216</sup> According to the logic of this study, it certainly appears that Congress should have increased the benefits of section 911 through TIPRA, rather than limited them. Instead, the TIPRA amendments to section 911 will likely decrease the number of Americans living abroad, U.S. exports, and, ultimately, the competitiveness of the United States world-wide.<sup>217</sup> In a world where the position of the United States is already declining, and countries like China are gaining significant ground, that cannot be the result that Congress intended. This signifies that the foreign earned income and housing exclusions need to be reconsidered and expanded.

### D. AN INCREASE IN INSTANCES OF NON-REPORTING BY EXPATRIATES

Many opponents also argue that the section 911 amendments will in-

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210. Keith Bradsher & David Cay Johnston, *U.S. Tax Law Sends Expatriates Reeling*, INT'L HERALD TRIB., May 26, 2006, <http://www.iht.com/articles/2006/05/26/business/tax.php>.

211. Swire, *supra* note 152.

212. McCabe, *supra* note 208.

213. PRICEWATERHOUSECOOPERS, ECONOMIC ANALYSIS OF THE FOREIGN EARNED INCOME EXCLUSION E-1 (Nov. 7, 2005), available at <http://www.amcham.org.sg/resources/911-PWC-economic-analy-S911.pdf> (last visited Sept. 21, 2007) [hereinafter ECONOMIC ANALYSIS].

214. *Id.*

215. Swire, *supra* note 152.

216. ECONOMIC ANALYSIS, *supra* note 213, at E-1.

217. De Luce, *supra* note 196; Swire, *supra* note 152.

crease instances of non-reporting and tax evasion by expatriates.<sup>218</sup> Even before these amendments, the IRS struggled with non-compliance of the U.S. tax laws by foreign living citizens.<sup>219</sup> Reports by the IRS have shown that in 2001, of the estimated four million U.S. citizens living abroad, only about 300,000 filed tax returns.<sup>220</sup> With the increased tax liability that will result if expatriates do file after the amendments, some commentators believe “people will go below the radar,” meaning they will decide not to file rather than pay the additional taxes.<sup>221</sup> This incentive applies particularly to Americans working overseas for foreign companies who do not pay U.S. taxes and are not required to file information with the IRS.<sup>222</sup> It also applies to overseas Americans who do not own assets in the United States.<sup>223</sup> The IRS has responded to the possibility of increased tax evasion by expatriates, saying they expect to hire additional employees to handle international returns and to perform additional audits in 2006.<sup>224</sup> However, if the amendments do encourage more expatriates not to file returns, Congress’s revenue estimate for the amendments could be further reduced, largely defeating their objective.

#### E. RENUNCIATION OF CITIZENSHIP

Other sources suggest that the amendments to the foreign earned income exclusion could cause Americans living abroad to renounce their American citizenship.<sup>225</sup> International tax attorneys have said that demand for their services in assisting people to renounce their citizenship is increasing, particularly by U.S. citizens who “held second passports and who had minimal ties to the United States.”<sup>226</sup> The *New York Times* recently ran an article noting that a woman who has lived in Switzerland for sixteen years renounced ties with the U.S. in November 2006 as a result of the increased tax liability she would have faced.<sup>227</sup>

This effect, however, may be somewhat overstated because there are penalties for renouncing citizenship for tax avoidance purposes.<sup>228</sup> As a general rule,

U.S. citizens are presumed to expatriate for a tax avoidance purpose if the taxpayer: (1) has an average annual net income tax for the five preceding years that exceeds \$124,000 (adjusted for inflation after

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218. Bradsher & Johnston, *supra* note 210.

219. *Id.*

220. Jones & Luscombe, *supra* note 93, at 10.

221. Bradsher & Johnston, *supra* note 210.

222. *Id.*

223. *Id.*

224. See Don D. Nelson, IRS Tax Audits of Expatriates May Increase in the Future, <http://www.taxmeless.com/IRSAudits.htm> (last visited Sept. 20, 2007); Don D. Nelson, IRS is auditing Expats Claiming Foreign Earned Income Exclusion (July 17, 2007, 14:29 EST), <http://usexpatriate.blogspot.com/>.

225. Carvajal, *supra* note 182, at A6.

226. *Id.*

227. *Id.*

228. David M. Neuenhaus & Ward Scheiderman, *Nurturing a Nifty Foreign Nest Egg: Tax Issues for Overseas Investments and Retirement*, CONN. L. TRIB., June 12, 2006, at S3.

2004); (2) has a net worth as of the date of expatriate of \$2 million or more; or (3) fails to certify under penalty of perjury that he or she complied with all U.S. federal tax obligations for the preceding five years.<sup>229</sup>

If a citizen is found to have renounced his citizenship for tax-avoidance purposes, he must file tax returns for ten years and is prohibited from visiting the United States.<sup>230</sup> In addition, “special estate and gift tax expatriation provisions apply to reduce or eliminate the benefits of expatriation.”<sup>231</sup> However, sources indicate that U.S. authorities have not enforced the rule preventing these individuals from entering the United States.<sup>232</sup> Nevertheless, expatriates should be careful to avoid these rules if they decide to renunciate their American citizenship, as they can result in large tax liabilities.<sup>233</sup> This option also may not be available to many individuals who are only temporarily assigned overseas and have plans to return to the United States for family, job, or other reasons.

#### F. PROPOSED LEGISLATION TO REMOVE LIMITS ON FOREIGN EARNED INCOME EXCLUSION

In response to the outcry of Americans abroad over the changes made by TIPRA, and because certain lawmakers disagree with those changes, legislation was introduced in both the House and Senate.<sup>234</sup> Not only would this legislation repeal the TIPRA amendments to section 911, it would also remove any cap on the foreign earned income exclusion.<sup>235</sup> If this legislation becomes law, section 911 would be even more favorable to taxpayers than it was before TIPRA. Overseas Americans could exclude the entire amount of their foreign earned income from gross income, thereby avoiding all U.S. taxes on that income.<sup>236</sup> This bill would effectively “end the double taxation of Americans who live and work abroad” and convert the United States from a world-wide system of taxation to a territorial system like the majority of other countries.<sup>237</sup>

The proposed legislation is entitled the Working American Competitiveness Act.<sup>238</sup> The Senate version of the legislation was introduced by South Carolina Senator Jim DeMint, a Republican, on June 13, 2006.<sup>239</sup> The bill has been referred to the Finance Committee.<sup>240</sup> The House ver-

229. *Id.*

230. Carvajal, *supra* note 182, at A6.

231. Neuenhaus & Scheiderman, *supra* note 228, at S3.

232. Carvajal, *supra* note 182, at A6.

233. *Id.*

234. Center for Freedom and Prosperity, Section 911 Reform: Leveling the Playing Field for Overseas Americans to Make the United States More Competitive, <http://www.freedomandprosperity.org/section911/section911.shtml> (last visited Sept. 21, 2007).

235. *Sen. DeMint Bill Would End Double Tax on Americans Working Abroad*, U.S. FED. NEWS, June 13, 2006, 2006 WLNR 10150445 [hereinafter *DeMint Bill*].

236. Working American Competitiveness Act, H.R. 5986, 109th Cong. § 2(a) (2006).

237. Mitchell, *supra* note 8; *see also DeMint Bill*, *supra* note 235.

238. S. 3496, 109th Cong. § 1 (2006); H.R. 5986, 109th Cong. § 1 (2006).

239. S. 3496, 109th Cong. (2006); *DeMint Bill*, *supra* note 235.

240. S. 3496, 109th Cong. (2006).

sion of the legislation was introduced by Indiana Congressman Chris Chocola, a Republican, on July 28, 2006.<sup>241</sup> The bill has been referred to the Ways and Means Committee.<sup>242</sup> Congressman Chocola was not re-elected to Congress in the November 2006 election.<sup>243</sup> However, the bill was co-signed by sixteen other congressmen, including Phil English of Pennsylvania, James Gresham Barrett of South Carolina, Randy Kuhl of New York, John Campbell of California, and Paul Ryan of Wisconsin.<sup>244</sup> Many of the sponsoring congressmen were re-elected and may continue to pursue the passage of this legislation in the House of Representatives.<sup>245</sup>

So far, neither bill has been acted upon by the 110th Congress.<sup>246</sup> It is not clear how the change to a Democrat-controlled Congress after the November 2006 elections will affect the fate of this legislation. Given that the bills were sponsored primarily by Republicans, they may face an uphill battle. However, the expatriate group American Citizens Abroad recently reported that its directors spoke with new congressional leaders, including the new Chairman of the Finance Committee, Max Baucus, about the legislation.<sup>247</sup> After those meetings, American Citizens Abroad said in a news update, "Democrat offices were highly critical of the tax hike on overseas Americans that took place in May of 2006 and indicated general support for overseas Americans. It was suggested that repeal of this tax hike should be given first priority, as an immediate objective."<sup>248</sup>

The Working American Competitiveness Act has been praised by many supporters of the foreign earned income exclusion.<sup>249</sup> One commentator said, "Liberated from the shackles of world-wide taxation, American companies would create more jobs and boost their exports – and most likely end up paying more in taxes as a result of their improved economic performance."<sup>250</sup> The Executive Vice President of AmCham, Bruce Josten, wrote a letter to Representative Chocola commending him for introducing the legislation.<sup>251</sup> Senator DeMint, who introduced the

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241. H.R. 5986, 109th Cong. (2006); *see also* Biographical Directory of the United States Congress, <http://bioguide.congress.gov/scripts/biodisplay.pl?index=C001052> (last visited Sept. 21, 2007) [hereinafter Biographical Directory].

242. H.R. 5986, 109th Cong. (2006).

243. Biographical Directory, *supra* note 241.

244. H.R. 5986, 109th Cong. (2006).

245. *See* Office of the Clerk, Official Alphabetical List of the House of Representatives of the United States, 110th Congress (Sept. 5, 2007), [http://clerk.house.gov/member\\_info/olmbr.html](http://clerk.house.gov/member_info/olmbr.html).

246. The Congressional Actions related to both H.R. 5986 and S. 3496 can be searched through the Library of Congress website at <http://thomas.loc.gov/>.

247. *Post-Election Congress*, *supra* note 184.

248. *Id.*

249. Mitchell, *supra* note 8.

250. *Id.*

251. Letter from R. Bruce Johnston, Executive Vice President for Governmental Affairs, to the Honorable Chris Chocola, U.S. Representative, (Aug. 2, 2006) ([http://www.amcham.org.sg/resources\\_us\\_tax\\_changes.html](http://www.amcham.org.sg/resources_us_tax_changes.html) (follow "US Chamber letter to Rep. Chocola" hyperlink)).

legislation in the Senate, said in a press release, "If we want to create the best jobs in the world, we've got to become the best place in the world to do business. We're not going to encourage global companies to locate in the United States if we continue to double tax their employees who work overseas."<sup>252</sup> DeMint went on to say about the bill he introduced, "This is a small change, but it will help put U.S.-based companies and their workers on a level playing field with the rest of the world."<sup>253</sup>

## VI. INTERNAL REVENUE SERVICE NOTICE 2006-87

As discussed in Section IV, the TIPRA amendments to section 911 gave the Treasury authority to issue regulations or other guidance for adjustment of the housing cap "on the basis of geographic difference in housing costs relative to housing costs in the United States."<sup>254</sup> The IRS exercised this authority in October 2006 by issuing IRS Notice 2006-87, included in Bulletin No. 2006-43.<sup>255</sup> The IRS Notice "increased limits on excludable or deductible housing expenses" in some areas.<sup>256</sup> The increases were accomplished through a list of various cities and a corresponding daily and full-year limitation on housing expenses.<sup>257</sup> The Notice explains that the table was "derived from the Living Quarters Allowance table prepared by the Office of Allowances of the U.S. Department of States as of August 20, 2006."<sup>258</sup> According to the IRS, the table will be updated each year through a notice, amendment to Form 2555, or a revised table on the IRS website.<sup>259</sup> The Notice also requests comments, particularly "[i]f a taxpayer believes that the average housing costs for a specific location differ significantly from the amount provided."<sup>260</sup>

The amounts given in the table represent the new maximum excludable or deductible housing expenses in a particular area.<sup>261</sup> Therefore, in order to determine the amount of excludable or deductible housing expenses, a taxpayer must locate his foreign country and city on the table, determine the full-year limit, and deduct \$13,184.<sup>262</sup> (This is because the base housing amount, as it was set by TIPRA, remains unchanged, and only amounts in excess of that amount are excludable.)<sup>263</sup> If a taxpayer lives in a foreign country for less than a full year, he must use the daily amounts multiplied by the number of days in the country to calculate his

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252. *DeMint Bill*, *supra* note 235.

253. *Id.*

254. TIPRA, *supra* note 52, § 515(b)(2).

255. I.R.S. Notice 2006-87, 2006-43 I.R.B. 766.

256. Lisa M. Nadal, *Notice Provides Upward Adjustment for Overseas Housing Costs*, 44 TAX NOTES INT'L (2006).

257. I.R.S. Notice, 2006-87, 2006-43 I.R.B. 766.

258. *Id.*

259. *Id.*

260. *Id.* at 772.

261. *Id.* at 766.

262. Vanderkamp, *supra* note 170, at 18.

263. I.R.S. Notice, 2006-87, 2006-43 I.R.B. 766.



housing limit.<sup>264</sup> Hong Kong has the highest new housing limit under the table at \$114,300, followed by Tokyo at \$85,700, Milan at \$79,800, and Paris at \$79,300.<sup>265</sup> Singapore's new housing limit is \$42,900 and London's new limit is \$72,100.<sup>266</sup> Dubai is not listed on the table.<sup>267</sup> Any place not listed continues to have the maximum housing limit set by TIPRA at thirty percent of the foreign earned income exclusion amount, which is \$24,720 for 2006, limiting the maximum housing exclusion for these places to \$11,536.<sup>268</sup>

Many expatriate groups and practitioners have welcomed these increases in the housing limitations.<sup>269</sup> The benefits of the increased limits for housing deductions are obviously the greatest in cities with the largest increases, such as Hong Kong, where overseas Americans are now permitted a maximum section 911 exclusion of \$183,516.<sup>270</sup> Americans living in those locations have been the most receptive to the changes.<sup>271</sup> However, not everyone is as happy about the IRS guidance.<sup>272</sup> One commentator noted that "[t]he most obvious feature of the table is that Hong Kong is rated as having by far the highest housing costs in the world, so high as to give us a decided competitive advantage over Singapore in attracting U.S. expatriates. The real difference in expatriate housing costs between the two is obviously nowhere near as great."<sup>273</sup> That writer also noted that no other city in China nor any cities in the Philippines, Indonesia, Taiwan, or Australia were provided an increased housing limit by the IRS Notice.<sup>274</sup> A Senior Manager with Ernst & Young, Nancy MacEntee, noted that, while the Notice provides some relief for taxpayers, "it by no means gets taxpayers back to the pre-TIPRA days."<sup>275</sup>

Although the increased housing limit helps alleviate certain problems that resulted from the TIPRA amendments to section 911, it has several problems. First, the increased housing limit does nothing to change the stacking rule implemented by TIPRA, which may well be the more unfavorable of the two changes.<sup>276</sup> American expatriates everywhere are still subject to higher tax rates on any income that is not excluded.<sup>277</sup> Second, areas that are not included in the IRS Notice are still limited to a maximum housing deduction of \$11,536.<sup>278</sup> While many places affected most

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264. *Id.*

265. *Id.* at 767-69.

266. *Id.* at 770-71.

267. *Id.* at 766-71.

268. MacEntee, *supra* note 123, at 18; Vanderkamp, *supra* note 170, at 18; *see also infra* note 109-13 and accompanying text.

269. Nadal, *supra* note 256, at 184.

270. Calculated by adding the \$82,400 maximum foreign earned income exclusion to the maximum housing exclusion for Hong Kong (\$114,300 - \$13,184).

271. *See* Vanderkamp, *supra* note 170, at 18.

272. *Id.*

273. *Id.*

274. *Id.*

275. MacEntee, *supra* note 123, at 18.

276. *Id.*

277. *Id.*

278. *Id.*

by the housing limit set by TIPRA—those with high-costs and low-taxes—were provided increased limits through Notice 2006-07, the limitations for some such places were not changed at all.<sup>279</sup> For example, Dubai's housing limit was not changed.<sup>280</sup> As a result, overseas Americans living in these places and others where the housing limit was not increased are not affected by the IRS Notice, and are still fully burdened by the TIPRA changes.<sup>281</sup> In addition, in some areas, where the housing exclusion was increased, such as Singapore, the increase was not large enough to reflect the actual cost of living there.<sup>282</sup> Third, it appears that those expatriates with the largest lobbying efforts, such as those living in Hong Kong, tended to get the largest increases in maximum housing limits.<sup>283</sup> This raises questions about whether the methodology for setting housing limits is fair and accurate, and whether changes made in later years will depend in large part on a particular country or city's lobbying efforts in Washington. This is not good tax policy, and the IRS should strive to ensure that its methodology for developing the housing table in future years reflects the actual housing costs in each country or city included.

## VII. OPTIONS FOR CHANGE AND RECOMMENDATIONS

There are several possibilities for changing section 911 foreign earned income and housing exclusions as they stand after the TIPRA amendments. Options include complete repeal of the foreign earned income exclusion, removal of any limitations on it, or something in between.<sup>284</sup> The middle-ground option would involve retaining the foreign earned income and housing cost exclusions and the limits on them, but increasing or decreasing those limits from current levels.<sup>285</sup> For instance, some groups have moved to have the foreign earned income limit "increased to as \$150,000 and then immediately be indexed for inflation."<sup>286</sup>

If the foreign earned income and housing exclusion were completely eliminated, overseas Americans would have only the foreign tax credit to relieve the additional tax burden imposed by living abroad. Senator Grassley, who favors this option, believes this is a favorable result because the foreign earned income exclusion represents a "tax subsidy."<sup>287</sup> Repeal of section 911 would mean any income received by the taxpayer because he lives abroad, such as the costs to secure and maintain a residence in the foreign country or costs to visit relatives and friends at home each year, would be taxed by the United States, even though they do not

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279. See Vanderkamp, *supra* note 170, at 18.

280. I.R.S. Notice, 2006-87, 2006-43 I.R.B. 766, 766-71.

281. See Vanderkamp, *supra* note 170, at 18.

282. *Id.*

283. *Id.*

284. Jones & Luscombe, *supra* note 93, at 10.

285. *Id.*

286. Asia-Pacific, *supra* note 4, at 1.

287. *Fact Sheet*, *supra* note 92.

represent additional economic benefits to the taxpayer.<sup>288</sup> Scholars have argued that repealing section 911 “is in direct conflict with the Bush Administration’s intentions to stimulate the economy.”<sup>289</sup> Studies indicate that this move would reduce U.S. exports by billions of dollars and cut domestic jobs in the United States.<sup>290</sup>

On the other hand, removing the cap on section 911 would effectively convert the United States to a territorial system of taxation, making the U.S. system consistent with that of every other developed country in the world.<sup>291</sup> One commentator, who supports adoption of this option, said that “[r]emoving the cap on Section 911 and instead relying on the common-sense principle of territorial taxation would boost America’s position in the global economy.”<sup>292</sup> Under this option, all foreign earned income and housing costs could be excluded from gross income, thus exempting them from U.S. taxation.<sup>293</sup> This could be accomplished by legislation such as the Working American Competitiveness Act, already introduced in both houses of Congress.<sup>294</sup> Many expatriates, scholars, and practitioners support this option, arguing that it would encourage Americans to go abroad, increase exports, create jobs at home, and improve American competitiveness.<sup>295</sup>

The TIPRA amendments, which considerably decreased the benefits of section 911, were less significant than total repeal of the exclusion.<sup>296</sup> However, as discussed in Section V, the TIPRA changes have been sharply criticized by many individuals and groups. These amendments could have a potentially dramatic impact upon the number of Americans living abroad and the employment of Americans by multi-national corporations.<sup>297</sup> Instead of hiring Americans, those corporations will hire employees of other nationalities, such as Canadians.<sup>298</sup> As a result, American exports will decline, and the competitiveness of the United States will follow.<sup>299</sup>

In a time when the United States already faces great challenges internationally from terrorism, the war in Iraq, and increases in the competitive position of other countries such as China, any legislation that further decreases our global status is bad policy. We should encourage our citizens and corporations to go abroad, and a favorable tax policy is an excellent and effective way to do that. As a result, the section 911 TIPRA amendments, which were introduced underhandedly at the last minute,

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288. ABCGC, *supra* note 190, at 2.

289. Riera, *supra* note 18, at 176.

290. ECONOMIC ANALYSIS, *supra* note 213, at E-1.

291. *Id.* at E-5; *DeMint Bill*, *supra* note 235.

292. *DeMint Bill*, *supra* note 235.

293. *Id.*

294. S. 3496, 109th Cong. (2006); H.R. 5986, 109th Cong. (2006).

295. ECONOMIC ANALYSIS, *supra* note 213, at E-1; *DeMint Bill*, *supra* note 235.

296. Jones & Luscombe, *supra* note 93, at 10.

297. Bradsher & Johnston, *supra* note 141, at C3.

298. *Id.*

299. ECONOMIC ANALYSIS, *supra* note 213, at E-1.

should be repealed. Instead, Congress should strongly consider increasing the benefits of section 911, or even eliminating the cap, to accurately consider the additional burdens placed upon citizens that live and work abroad. If the PwC study is correct in its estimate that removing the cap on the foreign earned income exclusion would increase exports by \$14.4 billion and support more than 137,000 jobs in the United States,<sup>300</sup> these numbers cannot and should not be ignored. Any reduction in tax revenue that would result from removing the cap on section 911 would surely be regained through increased earnings of individuals and corporations, which will be taxed in turn.<sup>301</sup>

### VIII. CONCLUSION

The foreign earned income and housing cost exclusions have been part of the tax code since 1926.<sup>302</sup> Since the beginning, they have been the target of much controversy and debate.<sup>303</sup> In 2006, TIPRA reduced the amount of foreign housing expenses that expatriates can exclude from taxable income and pushed them into higher tax brackets through the stacking rule.<sup>304</sup> As a result, American expatriates, companies, business groups, scholars, and tax practitioners have reacted strongly against these changes.<sup>305</sup> Critics say the tax law changes will decrease the competitiveness of the United States in the international arena.<sup>306</sup> Because the United States cannot afford to undermine its own competitiveness in this way, especially given our current economic position, the TIPRA amendments to section 911 should be repealed. The 110th Congress should strongly consider the benefits of removing the cap on the foreign earned income exclusion in order to further promote America's global position.

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300. *Id.*

301. Mitchell, *supra* note 8.

302. ECONOMIC ANALYSIS, *supra* note 213, at E-1.

303. *Id.*

304. Teo, *supra* note 77.

305. Bradsher & Johnston, *supra* note 210.

306. *Id.*



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