



Wolters Kluwer



GLOBAL TAX WEEKLY

a closer look

ISSUE 254 | SEPTEMBER 21, 2017

SUBJECTS TRANSFER PRICING INTELLECTUAL PROPERTY VAT, GST AND SALES TAX CORPORATE TAXATION INDIVIDUAL TAXATION REAL ESTATE AND PROPERTY TAXES INTERNATIONAL FISCAL GOVERNANCE BUDGETS COMPLIANCE OFFSHORE

SECTORS MANUFACTURING RETAIL/WHOLESALE INSURANCE BANKS/FINANCIAL INSTITUTIONS RESTAURANTS/FOOD SERVICE CONSTRUCTION AEROSPACE ENERGY AUTOMOTIVE MINING AND MINERALS ENTERTAINMENT AND MEDIA OIL AND GAS

COUNTRIES AND REGIONS EUROPE AUSTRIA BELGIUM BULGARIA CYPRUS CZECH REPUBLIC DENMARK ESTONIA FINLAND FRANCE GERMANY GREECE HUNGARY IRELAND ITALY LATVIA LITHUANIA LUXEMBOURG MALTA NETHERLANDS POLAND PORTUGAL ROMANIA SLOVAKIA SLOVENIA SPAIN SWEDEN SWITZERLAND UNITED KINGDOM EMERGING MARKETS ARGENTINA BRAZIL CHILE CHINA INDIA ISRAEL MEXICO RUSSIA SOUTH AFRICA SOUTH KOREA TAIWAN VIETNAM CENTRAL AND EASTERN EUROPE ARMENIA AZERBAIJAN BOSNIA CROATIA FAROE ISLANDS GEORGIA KAZAKHSTAN MONTENEGRO NORWAY SERBIA TURKEY UKRAINE UZBEKISTAN ASIA-PAC AUSTRALIA BANGLADESH BRUNEI HONG KONG INDONESIA JAPAN MALAYSIA NEW ZEALAND PAKISTAN PHILIPPINES SINGAPORE THAILAND AMERICAS BOLIVIA CANADA COLOMBIA COSTA RICA ECUADOR EL SALVADOR GUATEMALA PANAMA PERU PUERTO RICO URUGUAY UNITED STATES VENEZUELA MIDDLE EAST ALGERIA BAHRAIN BOTSWANA DUBAI EGYPT ETHIOPIA EQUATORIAL GUINEA IRAQ KUWAIT MOROCCO NIGERIA OMAN QATAR SAUDI ARABIA TUNISIA LOW-TAX JURISDICTIONS ANDORRA ARUBA BAHAMAS BARBADOS BELIZE BERMUDA BRITISH VIRGIN ISLANDS CAYMAN ISLANDS COOK ISLANDS CURACAO GIBRALTAR GUERNSEY ISLE OF MAN JERSEY LABUAN LIECHTENSTEIN MAURITIUS MONACO TURKS AND CAICOS ISLANDS VANUATU

Foreign Earned Income Exclusion Disallowed In Two More Cases

by Ephraim Moss, Esq. and
Joshua Ashman, CPA



Contact: emoss@expattaxprofessionals.com,
jashman@expattaxprofessionals.com

Ephraim Moss, Esq. is a US attorney specializing in international tax matters. Ephraim has extensive experience in counseling clients on matters such as cross-border tax structures, tax return treaty positions, expatriation matters, and disclosure of foreign financial accounts. In recent years, Ephraim has focused his practice on assisting delinquent taxpayers with utilizing the various IRS disclosure programs and has regularly represented clients before the IRS. Prior to co-founding Expat Tax Professionals LLC, Ephraim held a managerial position in the international tax practice of Ernst & Young.

Joshua Ashman, CPA is a US trained and licensed tax accountant. Joshua specializes in the areas of international taxation and expat taxation. Joshua has extensive experience with international compliance and expat tax returns and the issues that typically arise, such as reporting related to foreign pension schemes, Passive Foreign Investment Companies (PFICs), FATCA and Form 8938, FBAR reporting, foreign trust reporting on Form 3520, and reporting related to ownership of foreign corporations (Form 5471). Prior to co-founding Expat Tax Professionals LLC, Joshua held a senior managerial position in the tax compliance practice of PwC.

This is the first of two articles examining recent developments relating to the foreign earned income exclusion (FEIE).¹ Next week, we will look at the importance of filing an US tax return in a timely manner, even if availing of the FEIE.

Introduction

Following the trend of the past several years, courts continue to review FEIE cases at a relatively high rate. In most of the recent cases, the courts have denied the FEIE claims on a number of different grounds.

Recently, two more cases addressed the FEIE requirements. In one instance, an appeals court denied the FEIE claim based on the fact that the taxpayer resided in Antarctica, which does not have the status of a foreign country. In the other instance, the Tax Court found that the taxpayer airplane pilot's "abode" was in the United States.

Basics Of The Foreign Earned Income Exclusion

Provided that an individual can satisfy either the **bona fide residence test** (substantive change in residence based on facts and circumstances) or the **physical presence test** (present in a foreign country for 330 full days during any period of 12 consecutive months) and is able to establish a **tax home** in a foreign country, such an individual can exclude from income a portion of his or her foreign earned income.

Foreign earned income² is generally pay for personal services performed overseas, such as wages, salaries, or professional fees. It does not include passive income items, such as dividends, royalties, rent, pensions, and capital gains. It also does not include amounts paid by the United States or an agency thereof to an employee of the United States or an agency thereof.

The FEIE amount is adjusted annually for inflation. For tax year 2016, the maximum FEIE is up to USD101,300 per qualifying person. If filing individuals are married and both work abroad and meet either the bona fide residence test or physical presence test, each one can choose the FEIE. Together, they can exclude as much as USD202,600 for the 2016 tax year.

What Is A Tax Home?

In order to qualify for the FEIE, your "**tax home**" must be in a foreign country. The general rule is that a "tax home" is located in the vicinity of the taxpayer's regular or principal (if more than one regular) place of business or employment, regardless of where you maintain your family home.

Your tax home is the place where you are "permanently" or "indefinitely" engaged to work as an employee or self-employed individual. If you do not have a regular or principal place of business because of the nature of your work, your tax home may be the place where you regularly live. If you have neither (no regular place of business or living), then you are considered an "itinerant"³ and your tax home is wherever you work.

The "tax home" rule is subject to an important overriding exception: an individual is not considered to have a tax home in a foreign country for any period during which the individual's "**abode**" is in the United States. "Abode" has been variously defined as one's home, habitation, residence, domicile, or place of dwelling. Thus, in contrast to "tax home", "abode" has a domestic rather than vocational meaning. The location of your abode often will depend on where you maintain your economic, family and personal ties.

***Thompson v. Commissioner* (120 AFTR2D 2017-5146)**

In the *Thompson* case decided last month, the taxpayer excluded wage income earned for services performed in Antarctica. The Court of Appeals affirmed the Tax Court ruling that since Antarctica is not a "foreign country," the taxpayer did not satisfy the "tax home in a foreign country" requirement of the exclusion.

The Tax Court previously reasoned that US citizens generally are taxed on income earned outside the US geographical boundaries unless the income is specifically excluded from gross income under the relevant statute or regulations. The provisions of such exclusions, including the "tax home in a foreign country" requirement, are to be construed narrowly, and taxpayers must bring themselves within the clear scope of the exclusion. In this case, the taxpayers failed to do so.

***Acone v. Commissioner* (T.C. Memo. 2017-162)**

In the *Acone* case decided recently, the taxpayer flew commercial airplanes for a South Korean airline company. During the time he spent in South Korea, where he was officially "stationed," he participated in some social activities with other airplane pilots. However, he spent only about a third of each year in South Korea and more than 40 percent of each year in the US. He spent most of his days off in the US, where both his wife and house were located. When he stayed in South Korea, he always stayed in a hotel provided to him at no cost by his airline employer. The taxpayer also retained his US citizenship, voting registration, driver's license, and US bank accounts.

Under these facts, the Tax Court held that the taxpayer failed the tax home test, because his abode should be considered to be in the US. He therefore did not qualify for the FEIE.

The Tax Court distinguished the facts of this case from two other cases involving pilots who were deemed to qualify for the FEIE, because in those cases the taxpayer either kept his home in the foreign country or very infrequently visited the United States.

The Takeaway For US Expats

In light of the continuing trend of the IRS and courts focusing on the FEIE, it is important for expats to have solid justification for their FEIE claims.

For further information on any of the issues raised above, please contact the authors.

ENDNOTES

- ¹ <https://www.expattaxprofessionals.com/Form-2555-Foreign-Earned-Income-Exclusion>
- ² <https://www.irs.gov/individuals/international-taxpayers/foreign-earned-income-exclusion-what-is-foreign-earned-income>
- ³ *Deamer v. Commissioner*, 752 F.2d 337 (Eighth Circuit 1985).