

INCOME TAX — FOREIGN EARNED INCOME EXCLUSION — EFFECT OF THE ECONOMIC RECOVERY TAX ACT OF 1981 ON CITIZENS OR RESIDENTS OF THE UNITED STATES LIVING ABROAD.

The foreign earned income exclusion is one section of the Economic Recovery Tax Act of 1981 which, in its entirety, is designed to provide the largest tax reduction in United States history.¹ In drafting the 1981 Act, Congress intended to upgrade the nation's industrial base, stimulate productivity and investment throughout the economy, lower tax burdens on individuals and businesses, and restrain the growth of the Federal Government.² The foreign earned income exclusion specifically is designed to "encourage Americans to work abroad to help promote the export of U.S. manufactured goods and services."³

The Economic Recovery Tax Act of 1981⁴ includes a number of substantive revisions of United States taxation of foreign earned income. A taxpayer may exclude a certain amount of foreign earned income from his taxable gross income. The ceiling amount for the exclusion is \$75,000 in the taxable year 1982, and increases by \$5,000 each year until a maximum exclusion of \$95,000 earned income is reached in the taxable year 1986.⁵ In addition to the earned income exclusion, Congress allowed that housing costs provided or paid by an employer be excluded from gross income and that expenses paid by the employee be deducted in computing adjusted gross income.⁶ The housing exclusion is an amount equal to the excess of the reasonable cost of housing.⁷ The 1981 Act makes it clear that such housing expenses shall not be reasonable if they are lavish or extravagant.⁸ The deduction for housing expenses paid by the employee is limited to the amount equal to the excess foreign earned income, over the amount of such income excludable under that year's exclusion rate.⁹

¹ S. REP. NO. 97-144, 97th Cong., 1st Sess. 2 (1981) [hereinafter cited as Senate Report].

² *Id.* at 11.

³ *Id.* at 36.

⁴ Economic Recovery Tax Act of 1981, Pub. L. No. 97-34, §§ 111-115 (enacted Aug. 13, 1981 and codified at I.R.C. §§ 911, 119(c), 208 (1981)).

⁵ *Id.* § 111(a)(2)(A).

⁶ *Id.* § 111(a)(c)(2 & 3).

⁷ *Id.* § 111(a)(c)(1). The excess amount is computed by finding the difference between the housing expenses of a taxpayer for the taxable year, and the amount which equals the product of 16% of the daily salary of a federal employee at a grade level GS-14 step 1 multiplied by the number of allowable days within the tax year.

⁸ *Id.* § 111(a)(c)(2)(A).

⁹ *Id.* § 111(a)(c)(3)(B). For example, if an employee earns \$85,000 in 1982 and elects to exclude \$75,000 from his gross income, he may deduct up to \$10,000 in housing expenses.

For the taxpayer whose expenses exceed this limitation, the excess may be carried over as a deduction, but only for the succeeding taxable year.¹⁰ An election to exclude these expenses is allowed, along with a corresponding privilege to revoke such an election.¹¹ Taxpayers in camps will be allowed to exclude the value of meals and lodging provided by their employer if certain conditions are met.¹² These exclusions are available only upon the satisfaction of the residency requirement, which consists of either bona fide residency¹³ or physical presence.¹⁴ Failure to satisfy the residency requirement would result in a substantial increase in tax liability, as the entire amount of foreign earned income would be subject to United States taxation. Generally, any applicable credits for foreign taxes paid are still available under the 1981 Act.¹⁵ The Act provides a major change, however, in the repeal of Internal Revenue Code section 913.¹⁶ *Economic Recovery Tax Act of 1981*, Publ. L. No. 97-34, §§ 111-115 (enacted Aug. 13, 1981 and codified at I.R.C. §§ 911, 119(c), 208 (1981)).

Prior to 1976, United States citizens living abroad qualified for tax benefits which allowed exclusion from taxable gross income of a limited amount of foreign earned income.¹⁷ The limitation on the amount of exclusion fell into two categories: (1) a \$20,000 exclusion

¹⁰ *Id.* § 111(a)(c)(3)(C). If the taxpayer in n. 8 had actual housing expenses of \$12,000 in 1982, he would be able to carry over to 1983 the \$2,000 of housing expenses not subject to the deduction. However, current housing costs must be deducted before the carryover amount can be considered. For example, if the employee received a raise in income to \$95,000 in 1983, and he had \$14,000 worth of housing expenses that year, he would be able to deduct the entire \$14,000 amount plus \$1,000 of the carryover amount. (\$95,000 - \$80,000 exclusion = \$15,000). The remaining \$1,000 of expenses from 1982 would not be deductible, nor could it be carried over to 1984.

¹¹ *Id.* § 111(a)(e)(1)-(2).

¹² *Id.* § 113. These conditions focus on the definition of a "camp." First, the lodging must be provided for the convenience of the employer. That is, the place the services are to be rendered is in a remote area where satisfactory housing is unavailable. Second, the camp must be located as near as is practicable to the worksite. Third, the camp must be a common area, unavailable to the public and accommodating at least 10 employees. This amendment eliminated the preferential \$20,000 exclusion for expatriates working in hardship area camps; these taxpayers are allowed the amended foreign earned income exclusion of \$75,000 increasing to \$95,000. *Id.*

¹³ *Id.* § 111(a)(d)(1)(A). Bona fide residency requires that the taxpayer reside in a foreign country for an uninterrupted period which includes an entire taxable year.

¹⁴ *Id.* § 111(a)(d)(1)(B). Physical presence requires the taxpayer's presence in a foreign country for at least 330 full days during a period of 12 consecutive months.

¹⁵ I.R.C. § 33.

¹⁶ Economic Recovery Tax Act of 1981, *supra* note 4, § 112. Section 913 included a series of deductions under the Foreign Earned Income Act of 1978 which were intended to compensate the taxpayer for excess foreign living costs. See notes 33 & 34 *infra*.

¹⁷ Int. Rev. Code of 1954, § 911 (amended 1966).

for individuals who met the basic residency requirement,¹⁸ or (2) a \$25,000 exclusion for individuals who had been bona fide residents of a foreign country for an uninterrupted period of three consecutive years.¹⁹ This exclusion was available only upon satisfaction of a residency requirement which was stricter than that of the 1981 Act.²⁰

The Tax Reform Act of 1976 was a compromise measure, enacted to diminish tax disparities between United States expatriates and citizens working in the United States, and to maintain the competitive position of United States firms in foreign countries.²¹ The 1976 Act amended the former section 911 in four major areas. First, it reduced the amount of exclusion from \$20,000 to \$15,000.²² Second, the exclusion in the 1976 Act affected the lower portion of the gross income and left the remaining portion to be taxed at the marginal tax rates which would have been in effect absent the exclusion.²³ This was referred to as an "exemption with progression."²⁴ Third, foreign taxes paid on the excluded income were no longer deductible, nor could they be used as a credit against the expatriate's federal income tax.²⁵ Finally, the taxpayer could elect not to claim the exclusion.²⁶ The effect of this election was binding, however, and its impact in succeeding years unknown, thus the taxpayer was prevented from making a reasoned decision.²⁷

¹⁸ *Id.* § 911(c)(1)(A).

¹⁹ *Id.* § 911(c)(1)(B).

²⁰ Compare *id.* § 911(a)(1)-(2) with Economic Recovery Tax Act of 1981, *supra* note 4, § 111(a)(d)(1)(A)-(B). The bona fide residency test of one uninterrupted taxable year remains unchanged, but prior to the 1981 Act a stricter physical presence test required the taxpayer to have been present at least 510 full days during a period of 18 consecutive months.

²¹ Note, *The Foreign Earned Income Act of 1978—Sections 911 and 913*, 7 SYR. J. INT'L L. & COM. 89, 94 (1979).

²² Tax Reform Act of 1976, Pub. L. No. 94-455, § 1011(a)(1)(A), 90 Stat. 1520, 1610 (1976).

²³ Maiers, *The Foreign Earned Income Exclusion: Reinventing the Wheel*, 34 TAX LAW. 691, 696 (1981). For example, if a U.S. taxpayer working abroad had an income of \$25,000, the \$10,000 income not subject to the exclusion was taxed, not at the \$10,000 rate, but at the \$25,000 rate.

²⁴ Burge, *Impact of the Tax Reform Act of 1976 on Americans Working Abroad*, 6 DENVER J. INT'L L. & POL. 647, 650-51 (1977).

²⁵ Tax Reform Act of 1976, *supra* note 22, § 1011(b)(1).

²⁶ *Id.* § 1011(b)(3).

²⁷ Burge, *supra* note 24, at 653. If the taxpayer chose not to elect the exclusion, he could still apply his foreign taxes paid as a credit against his U.S. tax due. A U.S. taxpayer needed to calculate his tax liability under both the exclusion method and the foreign tax credit method. As a general rule, the greater the amount of foreign income tax paid, the greater the probability that the foreign tax credit method would result in less U.S. tax paid than if the exclusion method were used. However, if the foreign tax rate changed in subsequent years, a taxpayer who had elected not to exclude his income might be forced to pay more U.S. tax, as his election was irrevocable. *Id.*

Due to the adverse response to the foreign earned income provisions of the 1976 Act, Congress postponed the effective date of the amendment.²⁸ Before these provisions of the 1976 Act went into effect, Congress effectively repealed them by enacting the Foreign Earned Income Act of 1978.²⁹ The 1978 Act extensively altered the foreign earned income exclusion and created a series of deductions for the taxpayer who was unable to claim the exclusion under section 911 as amended. The exclusion was limited to an individual who, because of his employment, resided in a camp located in a hardship area for the same periods of time stipulated prior to the 1976 Act.³⁰ The 1978 Act, like the 1976 Act, allowed the taxpayer to elect the exclusion,³¹ and raised the amount of the exclusion from \$15,000 to \$20,000.³²

Section 913 under the 1978 Act eliminated the flat foreign earned income exclusion and replaced it with a series of deductions³³ intended to compensate the taxpayer for excessive costs of living abroad.³⁴ This complex section included deductions for a qualified cost-of-living differential according to geographic location;³⁵ qualified housing,³⁶ school,³⁷ and home leave travel expenses;³⁸ and a qualified

²⁸ Maiers, *supra* note 23, at 700-01. The author points out some weaknesses of the 1976 Act: (1) there existed uncertainty in Congress as to the probable impact of the 1976 Act; (2) Congress relied on "wildly inaccurate" Treasury estimates; (3) the repeal of section 911 would jeopardize the competitive position of U.S. businesses operating in foreign countries; and (4) the amendment doubled the tax liability of U.S. taxpayers working abroad. *Id.* at 697-98.

²⁹ Foreign Earned Income Act of 1978, Pub. L. No. 95-615, 92 Stat. 3097, 3098 (codified at I.R.C. §§ 911 & 913 (amended 1978)).

³⁰ *Id.* § 911(a)(1). Hardship area was defined as "any foreign place designated by the Secretary of State as a hardship post where extraordinarily difficult living conditions, notably unhealthful conditions, or excessive physical hardships exist . . ." *Id.* § 913(h)(2).

The periods of time include one uninterrupted year of residency or 510 days presence within 18 months. Int. Rev. Code of 1954, *supra* note 17, § 911(a)(1)-(2).

³¹ *Id.* § 911(d).

³² *Id.* § 911(c)(1)(A).

³³ *Id.* § 913(a)-(b). Under the 1981 Act this section has been repealed, and the flat foreign earned income exclusion has been reinstated. See note 16 *supra*. The exclusion is "flat" in the sense that it makes no distinction among taxpayers. A "qualified" exclusion, however, might distinguish between taxpayers based on geographic location, local cost of living, or any variety of factors.

³⁴ Comment, *The Taxation of Americans Living Abroad: The Foreign Earned Income Act of 1978 and §§ 911 and 913 of the Internal Revenue Code*, 19 COLUM. J. TRANSNAT'L L. 79, 96 (1981).

³⁵ Foreign Earned Income Act of 1978, *supra* note 29, § 913(d). Under the 1981 Act, no similar provision distinguishes between U.S. expatriates according to geographic location.

³⁶ *Id.* § 913(e).

³⁷ *Id.* § 913(f).

³⁸ *Id.* § 913(g).

hardship area deduction.³⁹ There was little opportunity to test the effectiveness of section 913 before Congress enacted the Economic Recovery Tax Act of 1981.

The 1981 Senate Finance Committee Report concluded that the tax burden imposed by the 1978 Act decreased the competitiveness of United States businesses, because excess tax costs usually are absorbed by the businesses.⁴⁰ The excess tax cost is incurred either in the form of a tax reimbursement or as the cost of preparing an employee's tax return.⁴¹ The Finance Committee also argued that the United States balance of trade is adversely affected when domestically based companies, faced with this increased cost of doing business, are forced to curtail their foreign operations or replace expatriated citizens in their work force⁴² with foreign nationals. A third rationale for change was that the system of deductions under the 1978 Act was too complex.⁴³ It was difficult to estimate tax liability for employment overseas, and costly to employ tax professionals to file a tax return.⁴⁴

In response to these problems with the 1978 Act, Congress enacted a system of incentives, encompassing income and housing exclusions and a relaxed foreign presence test.⁴⁵ However, no explanation is provided by the Committee for the specific dollar amounts allowable under the exclusions, or for the relaxation of

³⁹ *Id.* § 913(h). See generally Maiers, *supra* note 23, at 708.

⁴⁰ Senate Report, *supra* note 1, at 36.

⁴¹ U.S. GENERAL ACCOUNTING OFFICE, DOC. NO. 81-29, AMERICAN EMPLOYMENT ABROAD DISCOURAGED BY U.S. INCOME TAX LAWS (1981) [hereinafter cited as 1981 GAO REPORT]. The GAO found that 95 percent of American companies operating abroad that responded to its survey provided tax reimbursements to their employees for excess U.S. and foreign taxes paid. In Saudi Arabia, for example, the average tax reimbursement for married U.S. employees in the \$45,000 to \$55,000 salary range was \$18,889. At the same time, a third country national from Canada or West Germany required no tax reimbursement because his income was not taxed by his home country and there was no income tax in Saudi Arabia. *Id.* at ii-iii.

The GAO also found that the average estimated cost of preparing a U.S. employee's tax return was \$700 if prepared by the company and more than \$1,100 if prepared by an accounting firm. *Id.* at iv.

⁴² Senate Report, *supra* note 1, at 36.

⁴³ *Id.* See also Iredale, *The Foreign Earned Income Act of 1978*, 1979 S. CAL. TAX INST. 697, 698 for the author's thesis that by substituting the system of deductions under section 913, "Congress sacrificed simplicity for equity. The most significant aspect of the new law may be . . . the comparable burden of examination and litigation which it imposes on the Commissioner." *Id.*

⁴⁴ 1981 GAO REPORT, *supra* note 41, at iv. It should be apparent that an employee who is unable to predict the tax liability which may result from a transfer overseas will be reluctant to make any change.

⁴⁵ See note 37 *supra*.

the foreign presence test. The Committee did not conclude that a specific dollar limitation was needed to prevent abuse of the exclusion,⁴⁶ but the failure to provide specific explanations makes difficult any determination of whether the provisions will resolve the problems arising under the 1978 Act. What has been predicted is the tax revenue effect of the 1981 Act for fiscal year 1981-1986.⁴⁷ Over this period of time, tax revenue losses should increase from 299 million dollars to 696 million dollars.⁴⁸

The effect of the tax revenue losses must be viewed with consideration of two important issues: first, the equitable treatment of domestic and expatriated taxpayers, and second, the impact of the revenue losses on the United States economy.⁴⁹ At no point in either the Senate Finance Committee Report⁵⁰ or the House Conference Report⁵¹ do the Committees mention equitable treatment of United States taxpayers as a policy consideration in the amendment of the foreign earned income exclusions. It can be argued that the flat exclusion grants preferential treatment to all citizens living abroad, whether they live in a foreign country with a lower cost of living than the United States, or in a country with a much higher cost of living.⁵² The 1978 Act was a valid attempt to treat United States citizens abroad equitably by reflecting the actual excess expense incurred by the expatriate.⁵³ However, the 1978 Act failed to treat all United States taxpayers equitably, because it still granted preferential treatment to the expatriate vis-a-vis the domestic taxpayer.⁵⁴ The 1981 Act, by eliminating the complex system of deductions⁵⁵ and by tripling the amount of exclusion allowed prior

⁴⁶ Senate Report, *supra* note 1, at 36. The Committee suggests that: "This limitation prevents abuse of the exclusion by . . . highly paid entertainers or athletes who might move abroad to escape large amounts of U.S. tax on their income." *Id.*

⁴⁷ CONF. REP. NO. 97-215, 97th Cong., 1st Sess. 290 (1981) [hereinafter cited at Conference Report]; Senate Report, *supra* note 1, at 16.

⁴⁸ Conference Report, *supra* note 47, at 290. The Senate Committee estimates were lower than those agreed upon in the Conference Committee. The Senate Committee estimated that tax revenue losses would increase from 277 million dollars in 1982 to 629 million dollars in 1986. Senate Report, *supra* note 1, at 16.

⁴⁹ See Postlewaite & Stern, *Innocents Abroad? The 1978 Foreign Earned Income Act and the Case for its Repeal*, 65 VA. L. REV. 1093, 1095 (1979). This article examined these aspects of the 1978 Act and concluded that Congress should end preferential treatment of Americans working abroad.

⁵⁰ Senate Report, *supra* note 1.

⁵¹ Conference Report, *supra* note 47.

⁵² Postlewaite & Stern, *supra* note 49, at 1101-02.

⁵³ *Id.*

⁵⁴ *Id.* at 1115.

⁵⁵ Economic Recovery Tax Act of 1981, *supra* note 4, § 112.

to 1976,⁵⁶ has abandoned any consideration of tax equity in its approach to taxation of foreign income.

The impact of the 1981 Act on the United States economy through the loss of tax revenue can be considered in light of the three problems cited by the Senate Finance Committee as inherent in the 1978 Act.⁵⁷ First, it appears that by reducing the tax burden of American expatriates (and in turn, the burden on their employers to recompense their loss), the 1981 Act will improve the competitiveness of U.S. businesses abroad. Supply-side economics suggests that the reduction in taxes would free capital for investment domestically and abroad, which in turn would increase the growth rate of the Gross National Product. Proponents of a more complete free enterprise system argue that domestic taxpayers should not be required to subsidize foreign investment.⁵⁸ Market conditions would then be allowed to determine the level of competition and investment in foreign countries.

Closely related to the problem of competition is the adverse effect on the United States balance of trade when, due to heavy taxation of foreign earned income, companies are forced to curtail their foreign operations or replace expatriate employees with foreign nationals.⁵⁹ The Senate Finance Committee did not offer any evidence to support this assumption, however, and one other study suggests that the balance of trade may not be affected adversely.⁶⁰ This is also the conclusion reached in a Government Accounting Office (GAO) Report which assumed that the foreign demand for United States goods would remain inelastic in the face of a reduction in the number of expatriates.⁶¹ The feasibility of this assumption has been refuted, however, on the basis of marketing factors and economic effects of tax changes.⁶² Due to the inadequacy of

⁵⁶ *Id.* § 111(a)(b)(2)(A). Apparently, administrative concerns outweigh the balancing of tax burdens among U.S. domestic and foreign taxpayers. The complexity of the system of deductions was recognized by the Senate Finance Committee. See note 43 *supra*. Also, for an evaluation of the "onerous burden of documentation and substantiation" under the 1978 Act, see generally Iredale, *supra* note 43, at 742.

⁵⁷ See notes 40-43 *supra*.

⁵⁸ Postlewaite & Stern, *supra* note 49, at 1123.

⁵⁹ Senate Report, *supra* note 1, at 36.

⁶⁰ Postlewaite & Stern, *supra* note 49, at 1122. By analogy, the authors argue that the Japanese have been successful in exporting automobiles, televisions and audio equipment to the United States, without an expatriate sales force.

⁶¹ U.S. GENERAL ACCOUNTING OFFICE, DOC. NO. 78-13, IMPACT ON TRADE CHANGES IN TAXATION OF U.S. CITIZENS EMPLOYED OVERSEAS 17-18 (1978) [hereinafter cited as 1978 GAO REPORT].

⁶² Maiers, *supra* note 23, at 702 n. 71. The diversion of overseas purchases away from United States products is one example of the impact of marketing factors. This would oc-

the GAO model, projections under it regarding the United States balance of trade are questionable. It is clear that the reduced tax liability under the 1981 Act will improve the balance of trade deficit, but the questions as to the extent of improvement and the extent to which domestic taxpayers should subsidize the improvement remain unanswered.

The elimination under the 1981 Act of the complex system of deductions will have little effect on the United States economy. It will reduce the amount of money expended by individuals and corporations for filing tax returns, however, and in this sense expatriates may remain abroad in situations where cost-efficient multinational companies otherwise would have replaced the United States taxpayer with his foreign counterpart.⁶³

The role of the foreign national in the operations of American corporations abroad is a crucial factor in a projection of the economic effect of the 1981 Act. In making this prediction, it is useful to compare the manner in which foreign countries tax United States citizens working abroad and the law with regard to their own citizens working abroad. A short survey of the laws of three industrialized European nations in this regard follows. The study includes France, the Netherlands, and the United Kingdom.

France taxes all persons domiciled in France on their entire global income.⁶⁴ The central concept underlying this law is "fiscal domicile",⁶⁵ rather than citizenship.⁶⁶ Under this concept of fiscal domicile, the foreign earned income of both French nationals and foreign nationals is subject to French taxation if the individual is domiciled in France.⁶⁷ French law does provide exceptions to this rule for the French national working abroad: first, the French national is taxed only on that which would have been earned if the work had been done in France; and second, he is not taxed

cur when the United States expatriate, who buys Ford trucks, is replaced by a foreign national who purchases Mercedes-Benz trucks instead.

⁶³ Iredale, *supra* note 43, at 742.

⁶⁴ Law No. 1234 of Dec. 29, 1976, Art. 1 (codified at C. GEN. DES IMPOTS art. 4(A) (1979)). See Forde, *Taxing Transnational Workers in France*, 1978 BRIT. TAX REV. 99, 99. This article explores the impact of Law No. 1234 of Dec. 29, 1976.

⁶⁵ "Fiscally domiciled" is defined as: (a) having a home or primarily living in France, (b) exercising a profession in France, or (c) having the center of one's economic interests in France. See Law No. 1234 of Dec. 29, 1976, Arts. 2, 3 (codified at C. GEN. DES IMPOTS art. 4(B)(1) (1979)).

⁶⁶ 1981 GAO REPORT, *supra* note 41, at i. The United States is the only major industrialized country which taxes foreign source income on a citizenship basis.

⁶⁷ C. GEN. DES IMPOTS art. 156 I, (1979).

at all if abroad longer than 183 days in a year.⁶⁸ This exemption appears to be broader than that contained in the United States 1981 Tax Act in view of the fact that France's physical presence test is 147 days shorter than the United States test. Prior to 1979, foreign nationals domiciled in France were not taxed on their foreign source income if they were also subject to "personal taxation of their global incomes in the State of which they [were] nationals."⁶⁹ This preferential treatment, which would have avoided double taxation for the United States national domiciled in France, was repealed effective January 1, 1979.⁷⁰

French nationals not domiciled in France are taxed only on their French-source income.⁷¹ Similarly, foreign nationals not domiciled in France are taxed only on income or profits realized in France.⁷²

In the Netherlands, income taxation consists of a tax on an individual's world-wide income, except when foreign earned income is subject to foreign income or withholding tax.⁷³ The Dutch have adopted the concept of "exemption with progression" which was employed in the United States Tax Act of 1976.⁷⁴ All foreign income is included in the tax base, but only for the purpose of determining the tax rate to be applied. The formula then applies the tax rate to the total taxable income less the qualifying foreign income.⁷⁵ The Dutch tax system is "neutral" in the sense that Dutch tax laws do not interfere with other nations' tax policies.⁷⁶ This neutral effect is accomplished by combining the taxation of global

⁶⁸ Forde, *supra* note 64, at 108. Provision (a) is intended to exempt from taxation certain incentives provided for working abroad. The official status for exception (b) is known as "detachee."

⁶⁹ *Id.* at 100, citing C. GEN. DES IMPOTS art. 164(1) (1979).

⁷⁰ C. GEN. DES IMPOTS art. 164(1) (1979).

⁷¹ Forde, *supra* note 64, at 106. French source income is defined as: "income earned from work . . . performed in France irrespective of where the employee is based and remuneration paid, by a debtor fiscally domiciled or established in France . . . for any kind of service provided or availed of in France." Law No. 1234 of Dec. 29, 1976, Arts. 5(d) & 6(c) (codified at C. GEN. DES IMPOTS art. 164(B) (1979)).

⁷² Forde, *supra* note 64, at 99. Non-residents are allowed to deduct housing expenses from French income, and to claim exemptions for dependents. *See id.* at 106, citing C. GEN. DES IMPOTS art. 156 II, 1 bis. (1979).

⁷³ van Hoorn, *Unilateral Relief for International Double Taxation in the Netherlands*, 1976 BRIT. TAX REV. 84, 84. This statement should be qualified. The resulting double taxation of global income "is avoided or reduced in a large number of cases." *Id.*

⁷⁴ *See* note 23 *supra*. Compare van Hoorn, *supra* note 73, at 85 with Tax Reform Act of 1976, *supra* note 22, § 1011.

⁷⁵ *See* van Hoorn, *supra* note 73, at 90, for a hypothetical example of "exemption with progression."

⁷⁶ *Id.* at 97-98.

income with the qualified exemption of foreign income.⁷⁷ This could be expected from a country highly dependent on international trade.⁷⁸

In Great Britain, under the United Kingdom Finance Act of 1977,⁷⁹ foreign earned income may be exempt from tax if the duties of employment are performed outside the United Kingdom for a period of 365 days, during which time the taxpayer does not return to the United Kingdom for a period of more than 62 days.⁸⁰ This law allows the British expatriate approximately one more month at home during the year than the present 1981 Tax Act allows the United States expatriate. Furthermore, the 1977 United Kingdom Act allows a 25 percent reduction from taxation for residents performing duties outside the United Kingdom for at least 30 days.⁸¹ This allows some incentive for a British citizen to invest abroad or exchange places with a colleague, for example a visiting professor. The 1981 United States Act offers no such incentive.

CONCLUSION

The Economic Recovery Tax Act of 1981 is designed to: (1) improve the competitiveness of United States businesses abroad, (2) increase exports to achieve a more favorable balance of trade, and (3) simplify the taxation of foreign earned income. The 1981 Act brings United States tax policies with regard to foreign earned income in line with the more liberal treatment characteristic of foreign countries. It appears, however, that Congress, in adopting the 1981 Act, has abandoned the policy of equitable treatment of domestic and expatriated taxpayers.

The Economic Recovery Tax of 1981 should be effective in increasing the competitiveness of United States businesses abroad, due to the additional capital that will be available from the tax reduction. The investment of this capital is not guaranteed to increase the exports of the businesses, however. Too many additional factors influence demand for foreign goods, such as the availability of superior items from other countries, individual taste, and price. It is clear that if the goal of Congress is to achieve a more

⁷⁷ *Id.*

⁷⁸ *Id.*

⁷⁹ U.K. Finance Act 1977, Sch. 7, Para. 1(1).

⁸⁰ Salomons, *Taxation of Earnings from Work Performed Abroad*, 17 EUROPEAN TAX. 353 (1977).

⁸¹ U.K. Finance Act 1977, *supra* note 79, Para. 2(1).

favorable balance of trade, increased investment of capital cannot be foreclosed. Whether the specific changes were carefully drawn to achieve this goal, or in the alternative were less calculated revisions, remains to be seen. Congress should provide further explanation of its rationale for increasing the dollar amounts of the income exclusion to the present limits, and for reducing the requirements of the physical presence test.

From the taxpayer's perspective, the amended foreign earned income exclusion should function as an incentive for United States citizens to work abroad to promote the export of United States goods and services. Employment planning is simplified under the 1981 Act now that a United States businessman can assess his tax liability accurately from employment overseas. Depending on any applicable tax treaties between the United States and a foreign country, it is conceivable that the expatriate may work abroad tax-free. Tax return filing will also be simplified under the 1981 Act which eliminates the complex series of deductions under section 913. However, this unilateral action should evoke some similar tax response from foreign countries which are also attempting to improve their trade networks and economies.

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