
THE ALLIANCE FOR A COMPETITIVE TAX POLICY

SECTION 911: THE FOREIGN EARNED INCOME EXCLUSION

What does Section 911 do?

Section 911 of the Internal Revenue Code of 1986, as amended (the “Code”), allows individuals who meet certain requirements regarding residency or physical presence in a foreign country to exclude from gross income all or a portion of their foreign earned income and also to exclude or deduct certain amounts related to foreign housing costs.

Section 911 allows Americans to accept jobs overseas without having to also accept double taxation – once by the foreign country in which they reside, and again by the U.S. Government. Without it, American businesses would be given the perverse incentive to hire foreigners over Americans. This is because without Section 911, American businesses would have to pay Americans employees more to make up for the double taxation.

Why do we have it?

Section 911 was enacted in 1925 because Congress understood that the tax law had to be tailored so that Americans were not penalized for living overseas. Congress wanted to promote foreign trade and to ensure that U.S. citizens residing abroad are on equal economic footing as their foreign counterparts. *See*, H.R. Rep. No. 69-1, at 7 (1925). It has remained part of the Code for over 80 years because time has shown that this type of protection is necessary “to encourage Americans to work abroad to help promote the export of U.S. manufactured goods and services. Reducing the tax burden on Americans working abroad will make American enterprises more competitive in foreign markets.” H.R. Rep. No. 97-201, at 60 (1981).

Since 2005, Congress has been tinkering with the provision in order to curtail perceived abuses. It severely – and unwisely – limited the tax protection for Americans working and living overseas, and thus effectively raised the cost to American businesses of using American personnel.

What does Section 911(f) do?

Section 911(f) forces taxpayers who have income that would otherwise be excluded by Section 911 to calculate which tax bracket they are in by looking at both their taxable AND excluded income.

For example, if an unmarried taxpayer has \$80,000 in foreign income that may be excluded under Section 911, and \$100,000 of regular, taxable income, Section 911(f) forces the taxpayer to pay taxes on his \$75,000 of taxable income as if he were in the \$160,851-\$349,700 tax bracket instead of calculating them as he would as belonging to the \$77,100-\$160,850 tax bracket. Before this provision was added, our taxpayer would have paid only \$22,110.75 in taxes. Under this provision, our taxpayer must pay \$28,957.50 in taxes. (See next page for calculations.) It will cost an American business an additional \$684,675 to employ 100 such American employees overseas during just one year.

CALCULATIONS IN EXAMPLE

Tax Rates for Single Persons in 2007

<i>Income Level Excess</i>	<i>Base Tax Amount Due</i>	<i>Tax Rate on</i>
\$77,100 – 160,850	\$15,698.75	28%
\$160,850.01 - \$349,700	\$39,148.75	33%

Tax Due Before Enactment of Section 911(f)

$$\begin{aligned}\text{Taxes Due} &= \text{Base Amount} + (\text{tax rate})(\text{excess}) \\ &= \$15,698.75 + (28\%)(\$100,000 - \$77,100) \\ &= \$15,698.75 + (28\%)(\$22,900) \\ &= \$15,698.75 + \$6,412 \\ &= \$22,110.75\end{aligned}$$

Taxes Due Under Section 911(f)

$$\begin{aligned}\text{Taxes Due} &= [\text{Taxes on ALL Income}] - [\text{Taxes on Excluded Income}] \\ &= [\text{Taxes on } \$180,000] - [\text{Taxes on } \$80,000] \\ &= [\$39,148.75 + (33\%)(\$180,000 - \$160,850)] - \\ &\quad [\$15,698.75 + (28\%)(\$80,000 - \$77,100)] \\ &= [\$39,148.75 + (33\%)(\$19,150)] - [\$15,698.75 + (28\%)(\$2,900)] \\ &= [\$39,148.75 + \$6,319.50] - [\$15,698.75 + \$812] \\ &= [\$45,468.25] - [\$16,510.75] \\ &= \$28,957.50\end{aligned}$$