

# American Citizens Abroad (ACA)

## *The Voice of Americans Overseas*

[www.americansabroad.org](http://www.americansabroad.org)  
[info.aca@gmail.com](mailto:info.aca@gmail.com)

The Honorable Max Baucus  
The Honorable John Kerry  
The Honorable Patty Murray  
The Honorable Jon Kyl  
The Honorable Rob Portman  
The Honorable Pat Toomey

The Honorable David Camp  
The Honorable Jeb Hensarling  
The Honorable Fred Upton  
The Honorable Xavier Becerra  
The Honorable James E. Clyburn  
The Honorable Chris Van Hollen

September 30, 2011

### **FEIE, the Foreign Earned Income Exclusion, must be maintained and its cap removed until citizenship-based taxation is abolished and replaced by territorial taxation.**

Dear Members of the Super Committee of Twelve Lawmakers,

In proposing legislation to reduce the U.S. deficit and to enhance U.S. competitiveness to create jobs, the Committee needs to fundamentally reform U.S. taxation by adopting territorial taxation, not only for corporations but also for individuals.

The Joint Committee on Taxation, in its report, “Present Law and Issues in U.S. Taxation of Cross-Border Income”, prepared for the public hearings of the Senate Committee on Finance, September 8, 2011, suggested that residency-based taxation for individuals should be considered.<sup>1</sup> The statement is reproduced here:

#### Treatment of individuals

“Although most commentary on the issues of worldwide and territorial bases of taxing jurisdiction have focused on competitiveness of U.S. companies in comparison to foreign owned companies subject to territorial systems, a shift to a territorial system could also include provisions related to the treatment of individual taxpayers. Such reform would constitute a significant departure from long-standing policies, although it would have the effect of aligning the U.S. basis of taxation more closely with that of its trading partners.

The U.S. has consistently defended its assertion of worldwide jurisdiction with respect to its citizens and residents, both in the structure of the Code and in the terms of various bilateral and multilateral agreements. To the extent the U.S. has ceded such authority in practice, it reflects

acceptance of international norms in favor of relief from double taxation and the policy favoring the facilitation of employment of U.S. citizens or residents abroad.

If the broad assertion of taxing jurisdiction is to be conceded in favor of expanding territorial taxation to individuals, the scope of any such expansion should be considered. For example, the exclusion could apply only to earned income by increasing or removing caps on the foreign earned income exclusion and making the exclusion available to Federal employees. The treatment of unearned income may require revisions to the rules for determining source of such income, and create a need for new rules to establish status as a nonresident citizen. Such rules in turn would require anti-abuse provisions, possibly modeled on rules governing tax-motivated expatriation.”

The current Foreign Earned Income Exclusion, aimed to attenuate citizenship-based taxation, has not kept up with economic reality. It is laudable that the Joint Committee on Taxation statement suggests **removing the cap on the Foreign Earned Income Exclusion**. Representatives Carolyn Maloney and Scott Garrett also recognize the importance of preserving FEIE with their introduction of the “American Tax Fairness Act” calling for the elimination of the FEIE cap. The positions of the JCT and legislators supporting Americans working overseas contrast totally with certain bills before Congress that would eliminate the Foreign Earned Income Exclusion in a delusory aim to increase tax revenue.

U.S. citizenship-based taxation is unique in the world and recent related actions that have been undertaken by the IRS and Congress are literally destroying the community of Americans residing overseas and will consequently do irreparable damage to U.S. competitiveness in world markets.

Already, the number of Americans working abroad for U.S. corporations is very limited because U.S. tax policy makes it too expensive to employ American staff. Consequently, leaders of U.S. companies have little or no direct international experience. This is a major handicap in today’s global economy. Encouraging a significant presence of Americans abroad to represent U.S interests is an essential aspect of enhancing competitiveness. Feet on the ground are needed to promote exports.

Citizenship-based taxation leads to double taxation as Americans overseas must first pay taxes in the country of residence and inherent differences between tax policies systematically discriminate against Americans resident overseas. The need to translate foreign currency earnings into U.S dollars for U.S. tax purposes compounds double taxation and unfair taxation. Citizenship-based taxation also penalizes Americans abroad through associated legislation, the Bank Secrecy Act and FATCA.

The Bank Secrecy Act as amended in 2004 carries confiscatory, anti-constitutional penalties for not filing the FBAR (Foreign Bank Account Report) with the Department of Treasury, which is just an obscure reporting requirement, not linked to taxes, that was dormant for more than 30 years. While Congress may have intended to stop wealthy U.S. residents from hiding assets in overseas banks through higher penalties, the impact on U.S. residents overseas, who by definition must have foreign bank accounts, is devastating. The IRS has created a scam through its voluntary disclosure programs, by changing its rules in mid-stream retroactively and imposing heavy penalties on the assets overseas owned by Americans residing abroad, even when no U.S. income tax is due; this is contrary to fundamental principles of U.S. taxation and fairness. Honest Americans abroad, many of whom have lived most of their lives abroad and ignored the FBAR filing requirement (even many tax preparers were unaware of the requirement),

risk losing their life savings and are emotionally distraught by IRS harassment. FBAR penalties are viewed as an unjustified tax grab.<sup>ii</sup>

FATCA legislation, passed in March 2010 is the most extreme extension of discrimination related to citizenship-based taxation. It requires Americans residing overseas to file all of their foreign assets with their 1040 whereas Americans residing in the United States do not have to report their assets to the IRS. Worst yet, due to the harsh potential penalties of FATCA for foreign financial institutions, investing in the United States is now perceived overseas as very high risk. FATCA will lead to massive disinvestment by foreigners out of the United States, which will be destructive for the U.S. economy and for U.S. jobs. Most disastrous for Americans working and living abroad, foreign banks are shutting down bank accounts, and pension funds and insurance companies are refusing American clients. FATCA has turned Americans into pariahs in the international financial world. How can the United States expect to compete in world markets when it destroys, thorough its own legislation, the investment confidence of the rest of the world and its own community of citizens to living and working outside the United States?<sup>iii</sup>

The only way for the United States to become more competitive is to allow free movement of capital and U.S. citizens and to develop a stable, reformed residency-based tax system.

Citizenship-based taxation brings in insignificant tax revenue to the United States, a small fraction of one percent, yet the cost to the IRS of administering it is disproportionately high. The ill-will and damage created in the community of Americans overseas is enormous. Increasing numbers are forced to renounce their U.S. citizenship because of unfair, discriminatory U.S. tax policy and because FATCA legislation makes it impossible to survive overseas. This is absurd.

ACA urges the Super Committee to recommend to Congress the following fundamental reforms.

- Citizenship-based taxation should be abolished and replaced by residency-based taxation; at a minimum the Foreign Earned Income Exclusion must be maintained and its cap should be removed
- U.S. citizens who are bona fide residents abroad should be excluded from the FBAR filing requirement
- FATCA legislation should be repealed

Sincerely yours,

Marylouise Serrato  
Executive Director  
American Citizens Abroad

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<sup>i</sup> Joint Committee on Taxation, September 6, 2011, (JCX-42-11) prepared for the Public Hearing before the Senate Committee on Finance of September 8, 2011, "Present Law and Issues in U.S. Taxation of Cross-Border Income", p. 93. <http://www.jct.gov/publications.html?func=startdown&id=4355>

<sup>ii</sup> The ACA position paper on the FBAR Scam can be found at <http://www.aca.ch/fbarscam.pdf>

<sup>iii</sup> The ACA position paper on FATCA can be found at <http://www.aca.ch/fatcapp.pdf>