

REFORMING FATCA

A SAME COUNTRY SAFE HARBOR FROM FATCA REPORTING FOR AMERICANS LIVING ABROAD

Democrats Abroad has been working for more than five years to demonstrate to Congress, the IRS and the US Treasury that the financial accounts of law-abiding, tax compliant overseas resident Americans in their countries of bona fide legal residence should be exempted from FATCA reporting because they present none of the dangers the legislation was intended to proscribe. Despite the grave injuries and inconvenience they've suffered¹, Americans living abroad were never the target of the law.

As it happens, Congress is accustomed to rectifying the unintended and unanticipated adverse consequences of legislation they have enacted. To fix errant aspects of ratified legislation Congress subsequently enacts further provisions to protect the law's innocent victims, often termed "safe harbor" provisions. That is what we are seeking for Americans abroad in relation to FATCA: a safe harbor exemption from FATCA reporting.

When a safe harbor exemption is applied to FATCA, the law would treat the financial accounts of Americans abroad in their country of residence the same way as it treats the US accounts of Americans residing in the US. In brief, foreign financial institutions would be exempt from filing FATCA reports on the accounts of US-tax compliant Americans residing legally in the same country. A FATCA safe harbor exemption would only exempt accounts held in the country in which the account holder is *legally* resident¹.

It will preserve the original intent of FATCA to fight illegal tax avoidance by Americans using overseas accounts to hide assessable earnings from the IRS, but alleviate the useless reporting, by Americans *and by their banks*, of ordinary accounts used by law abiding citizens living abroad to pay their bills and save for the future.

- No American would have to file a FATCA report on accounts held in his or her country of residence; and
- No foreign financial institution would be required to file reports on exempt accounts to the IRS.

This FATCA reform resolves the key concerns of Americans living overseas, especially the concern that they will lose access to a diversified supply of banking and brokerage products when financial institutions elect not to do business with American customers because of the FATCA compliance requirements.

Democrats Abroad supports the establishment of a Safe Harbor Exemption from FATCA reporting for law-abiding Americans living legally abroad and is working to generate support from Congress, the IRS and the US Treasury for making this change to the FATCA implementation rules.

Making the case

A FATCA safe harbor exemption for Americans living legally abroad will not affect the battle against tax evasion and money laundering.

¹ A mechanism to determine 'legal residency' is already provided for in the US tax code (Section 911) and is used routinely by Americans abroad when claiming the Foreign Earned Income Exclusion.

- Firstly, the IRS is highly unlikely to miss out on the capture of lost tax revenue by putting a “safe harbor exemption” into the FATCA implementation rules. Tax evaders, after all, do not hide assessable earnings in accounts in the countries where they are resident taxpayers. The same is true of terrorism financiers, money-launderers, gun-runners or drug lords. They funnel their untaxed or illicit earnings into accounts in other jurisdictions. The FATCA “safe harbor exemption” is, therefore, of no use to them as a loophole to avoid detection.
- Secondly, the cost to the financial sector of complying with FATCA, put in the range of \$US7-10b, will be materially mitigated by the FATCA “safe harbor exemption”, depending upon what mechanism is established for claiming the exemption. Because of 1) the cost of implementing reporting regimes and 2) the penalties for compliance failures, the compliance frameworks being created by some foreign financial institutions includes the exclusion of some American customers for certain products. The FATCA “safe harbor exemption” will simplify the compliance exercise, lowering costs and lowering risks. Banks and brokerage houses currently refusing service to Americans will be very pleased to stop turning these customers away and Americans seeking financial products in their country of residency will be very pleased to see the supply of financial products and service providers restored.
- Lastly, honest, law-abiding Americans holding normal savings and investment accounts in countries where they pay local taxes are not FATCA’s target. The data collected through FATCA reporting will be far more useful to Treasury’s efforts to identify and apprehend tax cheats when it is scrubbed of data that is useless and distracting to their efforts. The FATCA “safe harbor exemption” will do that by eliminating reporting on everyday financial accounts that are highly likely to be of no use to tax and law enforcement efforts.

The FATCA Same Country Safe Harbor, also known as the FATCA “same country exemption”, has the support of American Citizens Abroad, the Association of Americans Resident Overseas and the Federation of American Women’s Clubs Overseas. It is endorsed by the IRS National Taxpayer Advocate and it has the support of both 2016 Democratic Party candidates for president of the United States.

For more information please contact the Democrats Abroad FBAR/FATCA Task Force on fatca@democratsabroad.org.

March, 2016

ⁱ See Democrats Abroad published research on the unintended adverse consequences of FATCA, “FATCA: Affecting Everyday Americans Every Day.”