



# DEMOCRATS ABROAD

Senate Committee on Finance  
Attn. Editorial and Document Section  
Rm. SD-219  
Dirkson Senate Office Building  
Washington, DC 20510-6200

March 31, 2021

## HEARING SUBMISSION

### ***How U.S. International Tax Policy Impacts American Workers, Jobs and Investment***

Democrats Abroad is pleased to respond to the Committee's invitation to comment on U.S. international tax policy as it impacts Americans living, work, saving and investing abroad. Americans living abroad manage U.S. businesses and other enterprises, promote U.S. interests, and serve as unofficial ambassadors of American culture and values. We thank Chairman Wyden and Ranking Member Crapo for holding this important full committee hearing and hope that the voices of everyday working-class Americans living abroad may resonate and be remembered in crafting future tax reform.

In the development of international tax policy, too often the community of Americans living abroad suffers from the grave misperception that they are tax cheats and money launderers. The body of tax policy resulting from this stubborn, apocryphal stereotype includes provisions that: double tax many forms of income, including those of low-income, elderly and disabled Americans abroad; create material barriers to banking, saving and investing; and, through their inordinate complexity, force ordinary, middle class Americans abroad to engage expensive tax return preparers able to contend with the convergence of two (and sometimes more) tax jurisdictions.

A large number of individual tax code changes would be required to address the many forms of discrimination against Americans abroad that are inherent in the Internal Revenue Code (IRC). **A switch from the current system of Citizenship Based Taxation to Residency Based Taxation would sweep away most of these tax code injustices** with minimal effort required by Congress. Legislative approaches and proposals for introducing Residency Based Taxation discussed with members of Congress in detail in recent years can be made revenue neutral to the federal government and can be protected with robust provisions for preventing abuse of offshore residence for the purpose of tax avoidance<sup>1</sup>.

As evidenced from our myriad in-person meetings over many years, U.S. lawmakers and regulators, in general, lack an adequate understanding of the Americans abroad community and the personal and financial harm that discriminatory U.S. tax policy causes for individuals who live and work outside the country. **We join our colleague organizations advocating on behalf of Americans abroad in asking the Senate Committee on Finance to conduct hearings on the taxation of Americans living abroad and the implications of a switch to Residency Based Taxation. We encourage you to invite testimony from scholars, economists, regulators, employers, industrialists, investors, agencies and officials with research and expertise on the Americans abroad community, their families, their work and the contribution they make to the U.S. economy, industry, foreign relations, incoming investment and cultural exchange.**

<sup>1</sup> [https://www.americansabroad.org/media/files/files/dc1e1c4e/DEG\\_short\\_memo\\_on\\_RBT\\_proposal\\_11.06.2017.pdf](https://www.americansabroad.org/media/files/files/dc1e1c4e/DEG_short_memo_on_RBT_proposal_11.06.2017.pdf)

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## Understanding Americans Abroad

Research published in 2019 at the behest of Congressional and Congressional committee staff demonstrates that the vast majority of the estimated 9 million Americans living outside the U.S. are not a lot different from Americans living in communities across the country when it comes to age, marital status, employment and household income. They are ordinary, middle class Americans who left the U.S. for a marriage/relationship (32%) or study/adventure (24%). Almost one in four (24.5%) moved abroad for work. Household income data confirms they are not wealthy “fat cats” and high rollers living overseas to game the international tax system. In fact, most Americans abroad live in countries with a higher overall tax burden than the U.S.<sup>2</sup>

Americans abroad face taxation in both the jurisdiction where they live and in the U.S. The U.S. is essentially alone in taxing non-resident citizens on their worldwide income, putting Americans abroad seeking jobs and starting businesses at a competitive disadvantage.

## U.S. Tax Code Discrimination

Although the *Foreign Earned Income Exclusion* ensures that a large amount of ordinary income is not subjected to U.S. taxation, many types of income are left out of the exclusion and so are taxed both by the U.S. and the country where the income is generated. The *Foreign Tax Credit* often does not zero out taxes owed to the U.S. Several types of retirement/investment income are subjected to highly punitive *Passive Foreign Investment Company (PFIC)* tax treatment. The preparation of *PFIC* returns is so complex that advice is known to run into the thousands of dollars. The retirement and investment instruments Americans abroad choose in the countries where they live are not, after all, “foreign” to them and many are mandated by statute. *PFIC* treatment is, therefore, a great injustice to Americans living abroad.

Types of income subjected to double or punitive tax treatment include, amongst others:

- ✓ Distributions from pensions and 401k-style retirement plans
- ✓ Dividends, interest and all investment income
- ✓ foreign retirement, education and other savings plans
- ✓ capital gains
- ✓ non-qualified non-U.S. pension plans
- ✓ social welfare payments (aged, indigent, disability, unemployment, childcare, parental leave) from foreign governments
- ✓ bequests to surviving foreign spouses

## U.S. Tax and Financial Account Reporting Compliance

U.S. taxpayers declare income earned abroad on IRS forms designed to capture detailed information about the source of the earnings, especially investment income. Preparing and filing these forms is stunning in its complexity. 2019 research shows 55% of non-resident filers require the assistance of a specialist tax return preparer experienced in dealing with the tax issues of non-resident Americans. These specialist services cost them more than twice what Americans based in the U.S. pay for tax filing services.<sup>3</sup> For non-resident taxpayers, preparing and filing the forms reporting income earned abroad is inordinately costly, confusing and frightening, even when no tax is due.

IRS outreach to Americans abroad about tax compliance has been woefully inadequate for many years. As a result, many Americans abroad – including officials in U.S. embassies and consulates - are ignorant, misinformed or confused about U.S. tax filing and reporting rules and obligations. IRS

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<sup>2</sup> “Tax Filing From Abroad: Research on Non-Resident Americans and U.S. Taxation”, March 2019. <https://democratsabroad.atlassian.net/wiki/download/attachments/4257416635/Tax%20filing%20from%20abroad%20-%202019%20Research%20on%20Non-Residents%20and%20US%20Taxation.pdf?api=v2>

<sup>3</sup> “Tax Filing From Abroad: Research on Non-Resident Americans and U.S. Taxation”, March 2019.

helplines are expensive and inconvenient to call and are manned by agents without an adequate understanding of the issues particular to non-resident filers. Though some of the free online systems available from IRS Free File partners include Americans abroad in their eligibility criteria, they do not include the full complement of forms needed by non-resident filers. The IRS's *Volunteer Income Tax Assistance (VITA)* and *Tax Counseling for the Elderly (TCE)* programs offering free basic tax return preparation to qualified individuals is also not available to Americans abroad. In summary, Americans abroad do not have easily accessible advice and support from the IRS to fulfil their filing obligations accurately and in a timely manner.

The burden of tax filing under Citizenship Based Taxation is compounded by the foreign financial account reporting requirements that support its enforcement. The *Foreign Account Tax Compliance Act (FATCA)* fully implemented double-disclosure foreign account and financial asset reporting in 2014. Since then, Americans abroad have reported impaired access to even ordinary financial products and services where they live.<sup>4</sup> They are “locked out” by banks choosing not to service U.S. Persons rather than comply with FATCA; this seriously restricts their ability to pay their bills, take out home mortgages and save for the future.

Failure to file the *Report of Foreign Bank and Financial Accounts (FBAR)* (the mandatory, electronic reporting of foreign bank and other financial accounts impacting those with at least \$10,000 in aggregate in foreign financial accounts) carries heavy penalties. *FBAR* compliance penalties are far out of proportion to the violation when the taxpayer lapse is attributable to issues like ignorance born of IRS neglect, language barriers or lack of ability to use or to access electronic devices for filing.

Although individuals who move abroad are on their own in dealing with U.S. tax complexities, companies that hire Americans to fill jobs in other countries often offer “tax equalization” to their American employees, i.e. support to ensure that they do not pay more in U.S. tax than they would if they were still resident in the U.S. Tax equalization, along with support to meet the cost of tax preparation services, makes Americans more expensive to hire and maintain abroad than third country nationals, and thus less competitive. Further, American companies risk being at a competitive disadvantage *vis-à-vis* their foreign competitors, when their U.S. staff is less skilled in the ways of the global marketplace than their foreign counterparts.

In addition, U.S. financial account reporting and compliance requirements make Americans abroad unattractive as business partners to those averse to sending their business’s financial information to the U.S. government.

The *Repatriation Tax* and *GILTI Tax* in the *2017 Tax Cuts and Jobs Act (TCJA)* have caused an enormous crisis for Americans abroad who own small to medium size businesses. The *TCJA* enacted a system of “territorial taxation for corporations” that provides enormous tax relief to U.S. corporations that own companies registered abroad. They can now repatriate profits at a deeply discounted rate with lots of offsets that ensure little to no tax is due. The impact on U.S. citizens abroad that own small to medium sized companies abroad, however, has been devastating. Owners of small to medium sized businesses without access to employer-provided retirement saving schemes often retain profits in their businesses to save for retirement. The *TCJA’s Repatriation Tax* provisions require them to show these unrecognized company profits on their personal tax filings and provides them with none of the offsets or credits available to U.S. corporations that own companies abroad. *Repatriation taxes* will devastate their retirement savings. The *TCJA’s GILTI Taxes* on all future earnings – earnings already taxed in the country where the business is registered - must also be declared on the owner’s personal tax filing, again without the offsets and credits

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<sup>4</sup> “FATCA: Affecting Everyday Americans Every Day”, September 2014.

<https://democratsabroad.atlassian.net/wiki/download/attachments/1986232508/Democrats%20Abroad%202014%20FATCA%20Research%20Report.pdf?api=v2>

afforded to U.S. corporations that own companies abroad. The *GILTI Taxes* will force many to close their small to medium size businesses after years of investment and effort, or to undergo costly corporate re-structuring.

## Conclusion

**Congress enacts laws and regulations without considering the impact on Americans abroad. These laws have grave, unintended consequences for ordinary, non-resident Americans.** Given the harm they suffer, it is not difficult to understand why Americans abroad have come to believe they are being punished for moving away from the U.S. They are proud of their U.S. citizenship and deeply resent the presumption that they are tax cheats and money launderers. They need Congress to understand that filing from abroad is extremely costly and stunning in its complexity. They need Congress to understand that the IRC is highly punitive to ordinary American families living middle class lives abroad and is, therefore, unjust.

Not since the Carter Administration has there been a hearing in the U.S. Congress on Americans living abroad and the range of serious personal and financial problems U.S. taxation causes for them, their families, their businesses and the U.S. and non-U.S. entities they do business with. **Americans abroad believe it is past time that their issues be heard, documented in the public record, and addressed by the government they help elect.**

Thank you for your interest in these matters. Please contact Carmelan Polce of our Taxation Task Force (+61 404 767 088 or [carmelan@democratsabroad.org](mailto:carmelan@democratsabroad.org)) or the undersigned with any questions about the information and recommendations provided herein.

Sincerely,

/S/

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