American Citizens Abroad (ACA)
The Voice of Americans Overseas

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Room 5205,
Internal Revenue Service
PO Box 7604, Ben Franklin Station
Washington, D.C. 20044

ACA comments on the proposed Treasury Regulations concerning FATCA, dated February 8, 2012

April 4, 2012

Dear Sirs,

American Citizens Abroad (ACA) appreciates the opportunity to comment on the Treasury proposed regulations issued February 8, 2012 relating to FATCA legislation. While these specific regulations are essentially addressed to the foreign financial institutions (FFIs) and non-financial foreign entities (NFFEs), they directly impact on Americans and green card holders residing overseas (henceforth collectively referred to as "Americans abroad"). Many Americans working abroad are already experiencing difficulty in opening and maintaining bank accounts, pension plans and life insurance contracts with FFIs as FFIs aim to reduce the administrative burden and perceived legal risk associated with U.S. person clientele under FATCA legislation.

To put this issue in context, ACA will first present what it considers to be the ultimate solution for resolving this problem and will then make specific comments on the Treasury Department's proposed regulations for foreign financial institutions under FATCA.

ACA advocates alternative taxation to resolve the FATCA issue for Americans abroad

FATCA is the straw that has broken the back of Americans and green card holders residing overseas (henceforth referred to as "Americans abroad"). FATCA has turned Americans abroad into pariahs in the international financial world. Americans abroad must have access to foreign bank accounts, pension funds and insurance companies to survive. The dilemma in which these Americans find themselves today would not exist if they were not subject to citizenship-based taxation. Consequently, ACA is urging Congress to adopt residence-based taxation and to tax Americans abroad with a withholding tax on U.S. source income, just as the U.S. currently taxes foreigners on U.S. source income. ACA believes that this solution is revenue neutral for the United States. ACA aims to have appropriate legislation introduced in

order to have it scored by the Joint Committee on Taxation. Adopting residence-based taxation would align U.S. tax policy with that of the rest of the world.

Under residence-based taxation, foreign financial institutions would no longer need to report to the IRS for purposes of FATCA on the accounts of 6 million Americans overseas and many more millions of green card holders residing abroad; they would focus only on U.S. residents. The IRS would benefit from automatic tax collection from Americans abroad on U.S. source income through withholding tax and would be relieved of administering the excessively complicated tax filings from Americans abroad. The IRS would have resources freed up to focus its attention on tax evaders residing in the United States. Americans residing abroad are not de facto tax evaders, because they are already paying taxes on their worldwide incomes to the nations where they reside. With residence-based taxation, Americans abroad would no longer be forced into a position to have to choose between their families and their U.S. nationality, between career opportunities and their U.S. nationality. U.S. tax policy would be aligned with that of the rest of the world.

ACA appreciates that the Treasury Department recognizes the unique situation of Americans abroad

Before entering into this discussion on the proposed regulations, ACA would like to thank the Department of the Treasury and the IRS for having established in the Instructions for Form 8938, issued December 15, 2011, higher thresholds for the reporting requirement of Form 8938 for Americans abroad. Through this approach, the Department of the Treasury has specifically recognized the situation of Americans working and living abroad to be distinct from that of Americans resident in the United States. Although Form 8938 comes under Section 6038D and is not a topic included in the proposed Treasury regulations of February 8, 2012, which focus on FFIs and NFFEs and relate to Sections 1471 and 1472 of the Code, it is a key element of FATCA legislation affecting Americans working overseas.

ACA perspective on the modifications in due diligence requirements in the proposed regulations

The IRS proposed regulations of February 8, 2012 build upon prior FATCA notices issued by the IRS and provide substantial additional guidance regarding due diligence, withholding and reporting obligations and additional carve-outs from—and exceptions to—FATCA's applicability, as well as a new timeline for implementation. The delay in the implementation reflects the utter complexity of instituting FATCA and aims to provide FFIs more time to prepare the administrative and software structures required for compliance.

The Treasury Department has taken several steps to facilitate compliance and reduce the administrative burden for FFIs, in particular with regard to due diligence requirements. Thresholds have been introduced to significantly reduce the administrative burden related to smaller accounts and to increase focus on large accounts.[1]

Most significant, preexisting individual accounts with a balance or value not exceeding $50,000 are exempt from documentation and cash value insurance or annuity contracts with a balance or value of $250,000 or less are also exempt from documentation. Accounts with a balance or value exceeding $50,000 but that do not exceed $1 million are subject only to review of electronically searchable data for indicia of U.S. status.

For new individual accounts (opened after the effective date of an FFI's agreement), review of the information provided at the time the account is opened is required, and if U.S. indicia are identified,

additional documentation must be obtained or the FFI must treat the account as held by a recalcitrant account holder.

Furthermore, the proposed regulations have expanded the categories of deemed-compliant FFIs " to include i) registered deemed-compliant "local" banks, non-reporting members of a participating FFI's affiliated group, qualified collective investment vehicles, restricted investment funds whose interests are sold through certain distributors and FFIs that comply with the requirements of an agreement between the U.S. and a foreign government that, in each case, register with the IRS, meet various requirements for their deemed-compliant status and renew their certification every three years; and ii) certified (but non-registering) deemed-compliant "local" banks, retirement funds, non-profit organizations, certain owner-documented FFIs and FFIs with only low-value accounts that meet various criteria and that certify their qualification as deemed-compliant FFIs by providing certain documentation to a withholding agent."[2]

These measures represent important efforts on the part of the Treasury Department to make FATCA more workable and more acceptable to the FFIs. Nevertheless, collateral damage is already present.

Due to FATCA, foreign bank accounts are being closed

In anticipation of the approaching dates when FATCA will apply, many FFIs have informed American clients that they are closing their accounts. These account closings relate to investment accounts, but also to retail accounts. It is not just bank accounts of Americans resident in the United States, but also Americans working and residing overseas in the country where the FFI operates that are being closed. Americans working abroad are also losing access to foreign pension plans and foreign life insurance contracts. Prepaid credit card companies are refusing Americans. Americans married to foreigners are being taken off of what was formerly a joint bank account, putting the American spouse into a very precarious financial position. American students studying abroad cannot open a bank account to pay tuition and living expenses and receive funds from the United States. Americans moving abroad for professional reasons face the same problem. U.S. companies aiming to establish presence abroad to sell U.S. products find it difficult to access FFIs. Furthermore, foreigners who move to the United States for professional reasons face forced closing of accounts in their country of origin, including demands to immediately liquidate their mortgages. FATCA leads to a severe decrease in the mobility of individuals towards the United States and of Americans towards the rest of the world.

The reaction of the FFIs is normal self-defense on their part. It is comparable to the reaction of U.S. domiciled banks which, following the passage of the Patriot Act, refuse to accept as clients Americans resident overseas because they have a foreign address. The reaction to FATCA is all the more radical because FATCA carries the threat of a confiscatory 30% withholding on the sale value of U.S. securities for the entire institution.

In the **Annex** to this letter are testimonies received by ACA from Americans overseas on their experiences of foreign and U.S. bank accounts being closed. It is a major problem for the community of Americans residing abroad.

Americans residing overseas are being forced to renounce their U.S. citizenship

Increasing numbers of Americans who are long-term residents overseas and have a second nationality are being forced to renounce their U.S. nationality because of FATCA. ACA has listened to multiple

testimonies from citizens who have concluded that renouncing U.S. citizenship is the only practical solution not only to live a normal life overseas but even to survive, although it is done with a heavy heart and regret.

- American women and men married to foreigners have to choose between their families and their U.S. citizenship as their foreign spouses refuse to have their joint bank accounts reported to the IRS and Treasury Department.
- Americans engaged professionally overseas have to choose between the development of their careers and their U.S. nationality as the restriction to banking facilities makes it very difficult to run a business and the reporting requirement on 10% U.S. ownership in a foreign venture scares away foreign partners.
- Americans, who have lived most if not all of their lives overseas, find they have to choose between losing their life savings to the IRS or losing their U.S. nationality. This includes U.S. citizens born abroad to a U.S. parent, who have ever held a U.S. passport, do not have Social Security numbers, who have never lived or even visited the United States.
- Americans find the complexity of filing tax forms with the IRS overwhelming and out of reach. It is impossible to insure that tax returns are totally compliant without competent professional tax specialists. In many foreign countries such services are not available. When they are available, they are very expensive, easily $2,000 or more, creating a heavy, unfair burden on all budgets, particularly since generally no U.S. income taxes are due.
- FATCA brings great fear and anger to the American community overseas because of the negative experience of those who entered the IRS voluntary disclosure programs and were unjustly penalized for not having filed the FBAR, even though thy owed little or no U.S. tax. Americans abroad see FATCA reporting penalties cumulating with very harsh FBAR penalties.
- Americans overseas view Form 8938 and FBAR as discriminatory forms and the reporting requirement as an unjustified invasion of privacy. It is incomprehensible to Americans abroad why two separate reports on foreign financial assets, both carrying heavy penalties for non-reporting, have to be filed with the Treasury Department, particularly since the United States only taxes income, not assets. These reports are perceived as raising a serious risk of identity theft and sufficient reason to renounce U.S. nationality. **ACA recommends that at a minimum the Treasury Department suggest to Congress to modify the law so as to combine Form 8938 and FBAR into one report, to apply the higher reporting thresholds of Form 8938 and to require the report to be sent to the Department of the Treasury in Detroit. ACA also believes that Congress should significantly reduce the penalties for non-filing, penalties which are excessive in comparison with the fault. Similarly ACA strongly recommends that the IRS take a lenient position in determining such penalties for Americans abroad as is possible within the scope of IRS authority. The double reporting has raised concern in Congress as Senators Baucus and Grassley requested a GAO study on the topic.**[3]

U.S. citizenship for many has become a liability. The number of Americans renouncing their U.S. citizenship has increased radically in the last three years and will continue to do so unless U.S. policy changes. This trend is most disturbing as the United States is inflicting upon itself a serious brain drain, as those renouncing are well-educated, speak foreign languages, have experience living in various parts of the world, share and project American values and represent an extremely valuable national asset. The nation is losing not only talent but also excellent diplomats who work for the country for free.

ACA recommendation to alleviate FFI reporting requirements

Through the proposed regulations, the Treasury Department has demonstrated openness to facilitate compliance among FFIs by proposing more flexible guidelines with regard to due diligence and deemed-compliant FFIs.

Since the Treasury Department has recognized the distinction between Americans working overseas and U.S. residents through the different levels of reporting thresholds on Form 8938, ACA would like to suggest that the Treasury Department make a similar distinction in its final regulations by stating that FFIs need not report to the IRS on accounts of U.S. persons who are bona fide overseas residents. This would certainly encourage FFIs to maintain Americans overseas as clients.

If this general exemption appears to the IRS to defeat the purpose of FATCA, then the exception could be limited to those Americans overseas whose maximum balance in the account during the year is below a specific threshold, for example $1,000,000, which is the same threshold required for electronically searchable data for indicia of U.S. status under the proposed regulations. Already under the current proposed regulations, no identification is required for bank accounts under $50,000 and for cash value life insurance policies under $250,000. Hence, bona fide U.S. persons residing overseas with bank accounts between $50,000 and $1,000,000 and with cash value life insurance policies between $250,000 and $1,000,000 would be identified by the FFI, but the FFI would not be required to report to the IRS the account balances and total movements of those accounts, nor would the FFI be threatened with IRS 30% withholding penalties on their own portfolios because of these accounts. This exclusion may require the U.S. person who is a bona fide overseas resident to provide the FFI every year a certificate from the fiscal authorities of the country of residence testifying that the person is tax compliant where he/she resides.

Such a measure would cover the great majority of Americans working and residing overseas. Instead of reporting on millions of Americans and green card holders overseas, the numbers would probably drop to just a couple hundred thousand. Consequently, the FFIs should perceive a significantly lower administrative burden and less threat of penalty from the IRS. They should hopefully be more willing to accept as clients Americans residing overseas.

For the purpose of FATCA in preventing tax evasion, this measure would allow the FFIs and the IRS to concentrate on large accounts overseas, which are more susceptible to tax evasion. Such a measure would allow significant rationalization of IRS efforts and reduction in cost of administering FATCA. In this context, it should be signaled that according to the Taxpayer Advocate Service, 91% of Americans overseas who file Form 1116 with their 1040 owe **no** U.S. taxes.[4] Consequently, massive FATCA reporting on those individuals is not going to increase tax revenue significantly.

Even If FATCA increases tax filing compliance reporting among Americans abroad, it will not significantly increase tax revenues for the United States. A 1998 report of the Treasury Department Office of Policy cited specific studies of involving close to 200 individuals overseas, who had not been filing and were identified by the IRS; only one or two owed any U.S. tax. The report concluded: "Treasury believes the samples do indicate that with respect to U.S. taxpayers working overseas, a taxpayer's failure to file a U.S. tax return does not necessarily indicate that the taxpayer is not paying the taxes he or she owes to the United States. Therefore an initiative aimed merely at increasing overseas filing compliance may not necessarily raise sufficient revenue to justify the cost of such an initiative.[5] The report also concluded that the IRS should focus its overseas compliance resources on compliance measurement and

enforcement projects that are likely to yield sufficient tangible results to warrant the resource expenditure.[6] The Treasury report also discussed that there should be no taxing of individuals who genuinely do not know they are American and who have never taken out a U.S. passport. Similarly those whose U.S. citizenship was stripped and then restored should not be subject to taxation during that period.[7]

Alleviating the reporting burden on FFIs with regard to Americans working and living abroad is essential for Americans overseas to be able to access services of FFIs. The same is true for small and medium-sized U.S. companies to be able to set up structures abroad which will facilitate U.S. exports

The FATCA Partner framework announced with the proposed regulations

Upon release of the proposed FATCA regulations, the U.S. Treasury also announced that it had established a framework under which the United States, France, Germany, Italy, Spain and the United Kingdom will develop an alternative approach to FATCA through automatic exchanges of information which would resolve the issues related to the privacy laws of the countries and the passthru requirements of FATCA for bank transfers within the partner countries. As noted by Alston + Bird LLP, "This intergovernmental approach is intended to help financial institutions deal with costs (estimated to be $100 million for each multinational bank), administrative burdens and legal impediments (e.g., data protection, reporting restrictions) in applying the FATCA provisions."[8]

The U.S. government announced that it is approaching more countries regarding the government partner arrangement to share information. Evidently, the Treasury Department hopes that the partner arrangement will become a model that is generally accepted. If this movement to government partnerships develops, ACA believes that its recommendations stated above remain valid. The FFIs should not be required to report to their governments the accounts of Americans resident in the country up to a specified threshold, or not at all. This would substantially reduce costs and administrative weight on the FFIs, the partner governments and the IRS.

These partnership agreements are conditioned on reciprocity, which is a key element missing in the FATCA legislation. Reciprocity puts the partner agreements on an entirely different level and fundamentally changes the application of FATCA.

Will the U.S. Department of Treasury be able to furnish reciprocity? Reciprocity implies that U.S. financial institutions must be able to determine the country of residence of each of its clients, to create separate lists of clients by country and to report this information to the IRS. This creates a significant administrative burden on U.S. banks because of the highly fractured nature of the U.S. banking system with thousands of small local banks. In addition, all U.S. based mutual funds and ETFs (exchange-traded funds) would presumably have to report to the IRS on the residence of all foreign owners. Insurance companies as well. Will all U.S. based companies have to go through their ownership files to segregate out and report on any foreign resident who owns 10% or more of the company? How will the United States react when Brazil and Mexico request a reciprocity agreement comparable to that of the five European countries? Up to now the United States has refused to provide any information to Mexico on deposits in U.S. banks owned by Mexicans. It is widely recognized that U.S. banks hold large amounts of Latin American money, due to the non-reporting, non-taxation status of bank deposits owned by foreigners. There is major resistance in Congress to allow the IRS to require U.S. financial institutions to report on the accounts owned by foreigners. Can the United States carry out its part of the reciprocity agreements?

Information exchange arrangements are being discussed in several places – through FATCA, the OECD and the European Union. For all countries other than the United States, the tax evasion issue deals only with residents who have not reported all worldwide income on assets held in overseas accounts. Because of citizenship-based taxation, however, for the United States, the exchange relates not only to U.S. residents but also to Americans residing abroad. For this reason, ACA believes that the only long-term viable solution is for the United States to adopt residence-based taxation comparable to that of other nations.

FATCA will negatively impact the United States

ACA reaffirms its position that FATCA should be repealed as it works against the interests of the United States. Foreign investment in the United States will shrivel when FATCA becomes operative. Just the threat of a 30% withholding on sale of U.S. assets is enough to scare away investors. Foreign portfolio managers are already recommending to their foreign clients to avoid U.S. securities. FATCA will bring little additional tax revenue to the United States, but will cost the nation dearly by isolating it from international capital movements. FATCA has already created immense ill-will throughout the world and risks to create systemic weakness in international financial markets due to the passthru requirement, which many banking professionals consider to be unworkable. FATCA will destroy the community of Americans working overseas if access to foreign financial institutions is totally shut off. ACA recognizes that repealing legislation is an issue for Congress, not the Department of the Treasury. However, IRS staff was actively involved in drafting FATCA legislation and the Department of the Treasury is in a position to significantly influence the direction of future legislation.

Request that the Treasury Department and the IRS maintain a dialogue with Americans abroad

The dilemma in which Americans abroad find themselves today would not exist if they were not subject to citizenship-based taxation. Consequently, as announced in the beginning of this letter, ACA is actively encouraging Congress, within the framework of fundamental tax reform, to adopt residence-based taxation for the U.S. citizens and green card holders and to tax them instead with a withholding tax on U.S. source income, just as the U.S. currently taxes foreigners on U.S. source income under double taxation treaties. ACA believes that this solution would substantially broaden the tax base and would be tax neutral for the United States, perhaps even bring in additional revenue for the United States.

American Citizens Abroad would sincerely appreciate maintaining a dialogue with the Department of the Treasury and the IRS on this issue. ACA would appreciate any assistance that the IRS could provide in documenting current revenue flows from citizenship-based taxation vs. projected revenue flows under residence-based taxation with a U.S. withholding tax on U.S. source income, according to existing double taxation treaties.

ACA believes that adopting residence-based taxation would be win-win solution for everyone, starting with the IRS. FATCA reporting or any other platform for international information exchange would deal only with U.S. residents and would greatly simplify the administration for the IRS. The IRS would benefit from automatic tax collection from Americans abroad on U.S. source income through withholding tax and would be relieved of the heavy administrative burden of excessively complicated tax filings from Americans abroad, an inefficient tax collection system which for the most part yields little tax revenue for the United States.

ACA thanks you for your attention given to these lines. ACA remains available at all times to respond to any questions which you may have.

Sincerely yours,

Marylouise Serrato	Jackie Bugnion	Anne Hornung-Soukup
Executive Director	Director	Director

CC: The Honorable Timothy F. Geithner, Secretary of the Department of the Treasury
The Honorable Douglas Shulman, Commissioner of the IRS
The Honorable Nina Olson, Taxpayer Advocate
The Honorable Max Baucus, Chair, Senate Finance Committee
The Honorable Orrin G. Hatch, Ranking Member, Senate Finance Committee
The Honorable Dave Camp, Chair, House Ways and Means Committee
The Honorable Sander M. Levin, Ranking Member, House Ways and Means Committee

Endnotes

[1] This brief review of due diligence guidelines is taken from Alston +Bird, Summary of the Proposed FATCA Regulations, March 15, 2012.
"For preexisting individual accounts, the following guidelines apply:

- Accounts with a balance or value not exceeding $50,000 are exempt from documentation.
- Documentation exceptions and aggregation rules apply for certain accounts that are offshore obligations (other than cash value insurance or annuity contracts) with a balance or value of $50,000 or less and for cash value insurance or annuity contracts with a balance or value of $250,000 or less.
- Accounts that are offshore obligations with a balance or value that exceeds $50,000 but that do not exceed $1 million are subject only to review of electronically searchable data for indicia of U.S. status.
- Accounts with a balance exceeding $1 million are subject to review of electronic files (and non-electronic files to the extent that electronic files do not contain sufficient information about the account holder) for U.S. indicia, including an inquiry of the actual knowledge of any relationship manager associated with the account.

For preexisting entity accounts, the following guidelines apply:

- Accounts with a balance or value not exceeding $250,000 are exempt from documentation requirements until the balance exceeds $1 million.
- For remaining entities, anti-money laundering (AML) and Know-Your-Customer (KYC) records and other existing account information can be relied upon to determine the type of entity to which the account belongs (e.g., whether the entity is an FFI, a U.S. person or a passive investment entity). Depending on the account balance and type of entity, different identification procedures of substantial U.S. owners are required.

For new individual accounts (opened after the effective date of an FFI's agreement), review of the information provided at the time the account is opened is required, and if U.S. indicia are identified, additional documentation must be obtained or the FFI must treat the account as held by a recalcitrant account holder.

For new entity accounts, the following guidelines apply:

- Accounts of another FFI (other than an owner-documented FFI for which the participating FFI has agreed to perform reporting) are exempt from documentation of substantial U.S. owners.
- Accounts of an entity engaged in an active nonfinancial trade or business are excepted from documentation requirements.
- For remaining passive investment entities, FFIs will be required to determine whether the entity has any substantial U.S. owners upon opening a new account."

[2] Ibid.

[3] GAO, Reporting Foreign Accounts to IRS: Extent of Duplication not Currently Known, but Requirements Can Be Clarified, February 2012. http://www.gao.gov/assets/590/588921.pdf

[4] In its 2011 Report to Congress, the Taxpayer Advocate Service reported that in tax year 2009, "After the application of the Foreign Tax Credit, only about nine percent of these taxpayers had a U.S. tax liability." p. 155.

[5] *Income Tax Compliance by U.S. Citizens and U.S. Lawful Permanent Residents Residing Outside the United States and Related Issues*, Department of the Treasury, Office of Tax Policy, May 1998. http://www.treasury.gov/resource-center/tax-policy/Documents/Income-Tax-Compliance-US-Citizens-and-Residents-Residing-Outside-US-5-1998.pdf, p. 4.

[6] Ibid., p. 45.

[7] Ibid., pp. 39-40.

[8] Op. cit. Alston + Bird provide the following sketch of the framework.
"The intergovernmental framework outlines the following objectives:

- The U.S. would enter into an agreement with a partner country (FATCA partner) under which each FATCA partner would implement legislation to require FFIs in its jurisdiction to apply necessary diligence in order to collect and report to the tax authority of the FATCA partner the required information, which would be automatically transferred to the United States.
- The U.S. government would allow certain FFIs to avoid entering into an FFI Agreement with the IRS, and would establish categories of FFIs that would not be subject to U.S. withholding on payments to them and that would be allowed to report FATCA information to the FATCA partner jurisdiction rather than to the IRS.
- The U.S. government would commit to automatic reciprocal collection and reporting of information to FATCA partners.
- FFIs established in the FATCA partner would not be required to (i) terminate the accounts of recalcitrant account holders, (ii) impose passthru payment withholding on recalcitrant account holders or (iii) impose passthru payment withholding on payments to other FFIs organized in any FATCA partner jurisdiction.
- Each FATCA partner would commit to the development of alternative approaches to achieving the policy objectives of passthru payment withholding that would minimize any associated administrative burden and would work with appropriate partners to adapt FATCA to a common model for automatic exchange of information, including the development of reporting and due diligence standards.