

Speech by Jonathan Lachowitz
2011 Overseas Americans Week (OAW) Overseas Taxation Roundtable Discussion
"Reforming Tax Policy for Enhanced Export Promotion"
held in the House Committee on Ways and Means Library Room.

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Ladies and Gentlemen,

It is an honor and a pleasure to be here in Washington D.C. representing American Citizens Abroad and the over 5 Million American patriots living overseas who have a deep respect for our country but who also have deep concerns for the current state of our union and in the direction our country is heading in the 21st century.

Today I am here to guide you on some of the unique aspects of the United States Federal tax code that apply to our citizens and small businesses overseas and unfortunately lead to 1) Increased American Unemployment and 2) Decrease our ability to export our products, services and values around the world.

I have one simple premise: The best people to import America's exports are Americans. With a little imagination, someone in Washington who has never lived overseas may believe that by encouraging more Americans to live and work overseas, set-up companies overseas, and pull American products and services to all corners of the world, we can be much more effective in stabilizing our country's future. Today the US has one the lowest percentage of its citizens living overseas; this in no small part due to our tax code.

If you remember only three things from what I have to say today, I would ask you to remember the following:

1. A country's tax code can be used strategically to enhance the ability of its corporations and citizens to compete in the global economy.
2. The most qualified people to import American products and services into other countries are indeed American Citizens.
3. The current American tax code, as it is written, puts American citizens and American small businesses, at extreme disadvantages leading to increased unemployment and diminishing our ability to export around the world.

Five years ago I decided to start my own small company overseas with the goal of helping people with what I am good at which is working with numbers and solving problems. I specifically chose to become a Certified Financial Planner professional mainly because of the deeply engrained code of ethics which requires CFP professionals to put our client's interests first when giving financial advice.

I specialize in working with American's overseas and have witnessed hundreds of situations where hard-working US citizens and small business owners are needlessly suffering due to the complex financial and tax rules.

If I can summarize my reading of US tax rules, as it relates to American individuals and small businesses overseas, three words come to mind:

1. Complexity
2. Inefficiency
3. Visionless

I am sure most of you have opinions about the US Federal tax code. All I can say is that it is much

worse in all aspects for most Americans living overseas. Based on my experience in working with dozens of CPAs and IRS employees I would say that most American CPAs and most employees of the IRS are unqualified to file or review a tax return on behalf of Americans living overseas.

I believe many of you have seen the recent news stories around large companies, like GE, that are encouraged by the US tax code to earn profits overseas (normally in low tax jurisdictions) and retain those profits overseas, so they avoid being taxed in the US until those profits are repatriated. The two back stories that the journalists miss here are

1) that many of those same large companies have specific policies in place to limit the number of Americans they hire into overseas positions; and in several cases I have heard of, US based companies aim to eliminate all of their overseas American expatriates, for one reason...they cost a lot more to hire than non Americans because of the unique aspects of the American tax code.

2) Small American Owned overseas Businesses are largely excluded from these same tax advantages available to large companies and in fact they or their owners are also punished just like American individuals overseas.

So now, how is it specifically that the American tax code today leads to greater unemployment and decreases exports? I'll give you some of the more common examples:

Depending on the country or the position, it can cost anywhere from 30% to 300% more to employ an American in an overseas position rather than a non American. Why?

1. The United States is the only OECD country in the world to tax its citizens based on their citizenship. ALL other OECD countries tax based on residency.

a. A typical American expatriate on assignment from a US employer will receive benefits such as: A housing allowance, English language schooling for their children, home leave for the family to go back to the US, tax preparation services and often tax equalization so they don't end up paying higher personal income taxes than they would if they stayed in the United States. In most European countries I know of, this leads to an American employee costing 2 to 3 times as much to employ as a non American. So what do Employers do, they find plenty of bright Europeans, Chinese, Indians and other non-Americans, many of whom have studied and worked in the US and they hire them for senior roles because they cost a lot less. Yes, this happens all the time.

2. Every small business owner with an overseas company has to file a form 5471 which is an Information only return that by the IRS's own instructions takes up to 3 weeks per year to fill out. About 300,000 of these forms are filed per year. If we assume only 2 weeks per form on average, our small businesses are paying for the equivalent of 12,500 people's full time salaries for an INFORMATION ONLY RETURN FOR the IRS. What value does this add? It does almost nothing to increase the tax base and adds tremendous costs to small businesses. There are too many forms to fill out, many with the threat of large penalties and forms that no one even looks at.

3. Next is the FBAR, Foreign Bank account Report. As part of these regulations we require American citizens who have signatory power over their employer's foreign bank accounts to fill out FBARs even when the taxpayer has no beneficial interest in the accounts. What does this mean? Any American working in the finance, treasury or senior role requires them to disclose private information about their employer to the IRS. And "breaking a foreign law" is not a reasonable defense in the eyes of the IRS for completing this form. So the IRS encourages Americans to break foreign laws to comply with the FBAR rules which are "information only." What's happening is US citizens are having to choose between their career and their citizenship. Overseas employers don't want to hire Americans in most financial or senior roles when they understand this requirement. The FBAR itself is really a mess, but this one small part, which again leads to no increase in tax revenue, is leading to

American unemployment overseas and a decrease in exports. Why? Companies are finding that doing business with America and Americans has too many financial risks. The US has become a scary place to do business.

4. The FBAR penalty structure was put in place to give the Federal government another weapon to fight international drug cartels and money laundering. No one I know in the overseas American community supports tax evasion (or any other crime) and when used properly this is an effective weapon against financial criminal activity, but before 2008 there were less than 10 FBAR penalties assessed per year from my knowledge. Since about 2008, the FBAR regime combined with the Voluntary Disclosure programs is causing great damage to people whose worst crime in most cases was not being well informed about the American tax code. This is an important factor in many Americans overseas being 1) Denied business opportunities, 2) Denied employment opportunities 3) Getting pressure from non American spouses and/or employers to consider renouncing their citizenship. Why can't we have the same penalties for Americans living overseas as for those who live in the US? Just a level playing field, not a draconian penalty structure, reporting that is "information only" and from 2011 required in multiple places and that puts many overseas Americans in conflicts with their employers. Complying with all of the FBAR rules requires many Americans to break the laws of the countries they live in. This is unjust.

5. Americans overseas pay US taxes but have NO American unemployment insurance, making it even more risky to take an overseas posting. If we are going to tax overseas Americans they should at least get equal benefits.

6. Americans often pay US Payroll taxes and foreign payroll taxes on the same income, but have no ability to use Medicare outside the US. This is especially the case for self employed people who work in countries with no totalization agreement on social security...

7. Americans overseas have to keep all of their records in their local currency for local taxation and for US dollars for US taxation; companies are allowed to have a functional currency, why not American individuals?

8. Our tax treaties have too many inconsistencies which often result in double taxation. For example: Why should retirement accounts in countries like England be considered IRS qualified plans but retirement accounts in most other countries are not and so employer and employee contributions are treated like income. This double taxation hurts the ability of American's working overseas to save effectively for retirement and is another area that makes Americans overseas more expensive for employers.

a. We are even seeing the IRS trying to assess FBAR penalties on overseas pension plans. How is it right to try and take about 25% or more of someone's retirement savings when the individual followed all of the rules of their country of residency and when most IRS agents and CPA's much less ordinary tax payers never really knew how the US tax code worked.

9. Americans buying property overseas and taking a mortgage in a foreign currency end up with a huge risk and REAL taxes on phantom gains. This makes Americans overseas, when they understand the rules, reluctant to invest in real assets for their business and for their home.

10. US Citizens have a \$5million estate tax exemption, non Americans have a \$60,000 estate tax exemption on US property (including stocks in US Companies.) So overseas investors are advised not to use US brokerages and to avoid buying US shares because a 35% or more estate tax is too big a risk, there are better opportunities elsewhere...

11. One of the newest threats to America's place in the financial world, again comes from within, FATCA. Many countries are threatening to pull investments out of the US, to retaliate against US banks with the same reporting requirement or just plain deciding not to do business with US citizens or in the US markets. Americans are finding their access to

banking and financial services overseas limited more and more on both a personal and professional level. Less access to banking means less business overseas and less exports.

12. Americans who are married to non-Americans and who choose to live outside of the US are also punished. They are often forced into choosing a filing status of married filing separately which has punitive tax rates and prevents them from other benefits such as Roth IRA contributions.

13. PFIC, Another 4 letter word. It stands for passive foreign investment company. Virtually every non-US mutual fund, hedge fund, exchange traded fund, money market fund and retirement funds overseas are PFICs. US individuals who want to save and invest are penalized.

In summary, I would like to encourage the US Congress, as they embark on historic deliberations that will influence the financial health and stability of our country for several generations, to look at the American overseas community as a strategic asset, not a liability and to remember:

1. A country's tax code can be used strategically to enhance the ability of its corporations and citizens to compete in the global economy.
2. The most qualified people to import American products and services into other countries are American Citizens.
3. The current American tax code, as it is written, puts American citizens and especially American small companies, at extreme disadvantages leading to increased unemployment and decreased exports

Borrowing from the economist Adam Smith, I encourage the Congress to design a tax code that 1) promotes equality, 2) is easy to understand, 3) is convenient, and 4) is efficient rather than the current system which inhibits the ability of all Americans and American businesses to compete on a level playing field at home and abroad.

Finally, I would like to say a special thank you to the executive committee members of American Citizens Abroad and all of the other organization who have helped to organize overseas Americans week and who have spent countless hours, on a volunteer basis, enlightening and informing Americans overseas of their rights and obligations and generally trying to improve the level of communication between Americans overseas and here in the United States. Keep up the good work.

Thank you.