

I am very heartened to learn that the Senate Finance Committee has embarked on serious bipartisan tax reform. As I am sure the Committee is aware, the only other country to tax its citizens on world-wide income is repressive and undemocratic Eritrea, and the US State Department itself condemned the practice in its 2010 and 2011 Human Rights Reports. Because of citizen-based taxation, I am currently wrestling, as are many thousands of other overseas Americans, with the unwelcome dilemma of choosing between retaining my American citizenship and being able to afford the comfortable old age for which I thought I had carefully provided. If the US were to adopt residence-based taxation, I would no longer face this stark choice.

An outline of my situation will explain the great difficulties that current US tax law causes me and many millions of middle-income Americans who live overseas. I was born in the US but studied in England from 1972 to 1974, and in 1976, at the age of 26, I moved permanently to England, so I have spent my whole adult life living and working in the UK. I became a British citizen in 1987 but was careful to retain my American citizenship, so am a dual national.

In October 2012, I retired after teaching for 26 years at the University of London. As an academic, I have earned a decent living, but, although I always filed US tax returns, as required, I never had to pay US tax on my earnings as they were below the taxable threshold. Because I worked in Britain my entire adult life and my only US earnings were in summer jobs during college and graduate school (1968-73), I am not eligible for US Social Security or Medicare. I am now dependent on my university pension and the British State Pension (the equivalent of Social Security).

Although my pensions are at present adequate to live on, they are not enough to cover any care home fees I may eventually face (which is likely, as my British partner and I have no children). Consequently, since they became available some years ago, I have taken advantage of stocks/shares Individual Savings Accounts (ISAs) in the UK – tax-free savings accounts with a limited yearly allowance for deposit, open only to people resident in Britain, which the government developed as a way of helping people to save. I intended these funds, which have been invested ethically, to serve as a safety net when/if I could no longer live independently.

However, stocks and shares ISAs are invested in mutual funds, and I did not realise that the US regards such investments as Passive Foreign Investment Companies (PFICs). I have since discovered that, because of the draconian way in which the US taxes PFICs, encashment means I would lose between 50% and 100% of the investment to US tax. This is because the US taxes PFICs at the highest ordinary income tax rate (currently 39.6%, plus 3.8% Medicaid surcharge), rather than at the long-term capital gains tax rate (0-15%), without considering other income or expenses. It further assumes that any gain made upon encashment was made evenly over the years the investment was held, so interest charges, compounded daily, are added to the tax due. As the tax adviser I consulted explained, compound interest charged in this respect on a long-term investment can often match the tax charged; in some cases the tax due is actually greater than the total worth of the investment. Furthermore, the US tax ultimately charged will be based on that year's exchange rate, which might be very different from the exchange rates pertaining when the investments and gains were made. Both the false assumption of even growth and the use of final-year exchange rate compound the unfairness of levying the PFIC tax on overseas US citizens. (For further information on how exchange rates can inflate foreign taxable income and create phantom capital gains, see the section titled 'CBT penalizes Americans abroad with unavoidable foreign exchange risks' in the American Citizens Abroad document, 'The United States should adopt Residence-based taxation (RBT)' at <https://americansabroad.org/files/4414/1571/9587/united-states-should-adopt-rbt-oct-2014.pdf>).

For as long as I hold the investment, US tax, interest, and penalties directed at PFICs take c. 50% of annual gains and income. I also have to pay an additional underpayment-of-tax penalty, even though there is no way to pay US tax before my tax return is prepared, at great expense, by a specialist. Any foreign tax credit I have (which I always have, as my UK income tax, at 20%, is higher than my US income tax would be, at 15%) is not applicable to the tax

on PFICs, as the US applies different rules to general income than it does to passive income and investments with a low tax rate. I am therefore currently carrying-over \$14,175.00 worth of Foreign Tax Credit that I cannot apply to the US tax I pay on PFICs.

Although I understand US reluctance to see citizens living in the US put their American dollars into foreign mutual funds, this punitive legislation makes no allowance for American citizens living abroad, like me, who have no financial ties to, or financial benefits from, the US. We live in foreign countries, work for foreign institutions, are paid salaries and pensions in foreign currency, and pay taxes in the countries in which we reside. It is extremely unjust, perhaps even unconstitutional, to tax our hard-earned savings – savings made from foreign earnings that have already been taxed in our countries of residence – in a way designed to punish those who shelter American dollars in tax havens.

In addition, since the introduction of FATCA, US tax filing requirements for Americans living abroad have become increasingly burdensome and expensive. For example, my US tax return for 2012 was 109 pages long, prepared at a cost of \$1200. Forty-eight of those pages comprised 16 separate copies of Form 8621, on which the income and gains of each PFIC fund holding was reported; the sums involved ranged from \$48 to \$422. My total taxable income (entirely from the PFICs) was only \$5473, but the US tax, interest and penalties I paid on it was \$3430 (a tax rate of almost 63%), which meant that I lost all but \$843 (or 15%) of my taxable income to US tax costs (i.e., tax, interest, penalties, and tax preparation). My 2013 return was the same length and cost \$1534 to prepare; the US tax due amounted to \$1121. My 2014 return cost \$1606 to prepare; the tax due was \$1383.

I have worked and saved hard to ensure a dignified old age, but US tax legislation, geared towards Americans living in the US and ignoring the situation of Americans living abroad, is threatening that. In the interest of just and fair taxation, I urge the Senate Finance Committee to adopt the following reforms, as soon as possible:

1. Replace citizen-based taxation (CBT) with residence-based taxation (RBT).
2. If CBT continues, distinguish between PFIC investments made by Americans living abroad and those made by Americans resident in the US in setting a tax rate (e.g., amend the UK/USA double taxation convention to exempt UK ISAs from the PFIC tax).
3. Adopt same-country exceptions for FATCA.

Also, I understand that, if RBT is adopted, there is some thought at present about applying an exit tax when a US citizen is judged to be nonresident and no longer subject to US taxes on non-US income and assets. However, it would be anomalous and against the spirit of the reform to tax non-US assets and income on which foreign tax has already been paid. It would be justifiable to impose an exit tax only on American assets that have been moved overseas.

Because of CBT and FATCA, Americans living abroad are now losing access to local banking facilities, being denied the opportunity to make prudent investments and/or to benefit from them, and dealing with excessively burdensome, complicated, and expensive IRS reporting requirements. As the American Citizens Abroad RBT proposal has made clear, a residence-based tax system would not only provide for fair, equitable, and efficient taxation of Americans domiciled abroad and free them from these problems and difficulties, but it would also increase US Treasury tax receipts, boost the country's export performance, create better employment opportunities for Americans at home and abroad, and align US tax law with that of all other developed nations. Adopting a residence-based tax system would be in the best interests of the country as a whole and of its citizens, wherever they may live. It would also mean that people like me will no longer have to decide between expatriation and financial hardship in old age.

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