

**AN AMERICAN CITIZENS ABROAD
BRIEFING BOOK**



***“ELIMINATING THE EXPORT TAX
ON AMERICAN CITIZENS
IS THE IDEAL WAY
TO LAUNCH THE PRESIDENT’S
LEVEL PLAYING FIELD INITIATIVE”***



A Proposal to

***Enhance the Security and Prosperity
of the United States
by Creating a More Level
Worldwide Playing Field
for the Promotion and Protection of
Freedom, Democracy, and Trade***





**ACA INVITES YOU
TO JOIN WITH US TO
BANISH FOREVER THE EXPORT TAX ON
U.S. CITIZENS AS A KEY COMPONENT OF**

***"THE PRESIDENT'S
LEVEL PLAYING FIELD INITIATIVE"***



When President George W. Bush gave his acceptance speech at the Republican National Convention in early September 2004, he addressed an issue near and dear to the hearts of the overseas American community. He said:

"To create jobs, we will expand trade and level the playing field to sell American goods and services across the globe."

We applaud the President's initiative and looking forward to working with him to make sure that a truly level playing field all over the world is the end result.

We need to work together to make sure that this playing field is not only level for trade, but also for the competitive participation of American ideas and values too. Americans living overseas are fully aware of the reasons why this worldwide playing field is not level today. It is not due to competitive impediments imposed by other governments, but paradoxically due to the myriad of difficulties that have been unilaterally created and imposed on overseas Americans by our own government. The single most egregious of these self-imposed handicaps is the unilateral imposition of an export tax on Americans working abroad.

THE PRECEDENT FOR OUR INITIATIVE

In 1979, Reginald Jones, CEO of General Electric and Chairman of the President's Export Council, appointed a special task force to look at the trade implications of the way U.S. citizens living and working abroad were being treated. Their recommendations were wonderful, but alas, never implemented. A copy of the 1979 Report of the President's Export Council is included with this paper.

THE ACA LEVEL PLAYING FIELD INITIATIVE

It is for this reason that ACA, along with our sister organizations representing overseas U.S. citizens in many other countries of the world, is soliciting support for our "Level Playing Field Initiative". The ACA proposal has been forwarded to the White House, Members of Congress, Senators and contacts in the press to draw their attention to this key problem and to promote an appropriate solution that will enhance the prosperity of all Americans. It has recently been endorsed by the National Foreign Trade Council, which represents many of the largest U.S. exporting companies.

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In order to create a worldwide level playing field for goods and services of every origin, including those from the United States, we are asking President Bush to task his Export Council to undertake a new evaluation of how the U.S. treats overseas Americans and what changes would now be appropriate to help create more jobs for U.S. citizens at home and abroad and to reduce our enormous trade deficit.

President Bush should also be encouraged to enhance the significance of this effort by appointing an appropriate number of overseas Americans to his Export Council. He should also be encouraged to ask the Export Council to make sure that the entire overseas American community has the right to actively participate by specifically inviting them to make inputs to this study.

A new Export Council report would be an important new element in the on-going debate about the most appropriate approach to an increasingly globalized world and the role that overseas Americans could and should be playing within this complex and competitive environment. The report should certainly be made available to the President’s Advisory Panel on Federal Tax Reform, established in January 2005.

The worldwide tax system currently employed by the United States is the world’s most unusual self-destructive economic weapon. The damage this export tax on U.S. citizens causes is immense and grows greater each year.

The decision to introduce this new tax system was brought to Washington with the wave of innovative enthusiasm of the early days of the Kennedy administration. Curiously, it has become so mesmerizing that no Republican or Democratic successor administration has seriously considered just eliminating it. Thus, despite calls to repeal this tax, even by the President’s own Export Council, it has survived and continues to severely damage the American economy, year after year. To justify such a tax despite its obvious negative consequences, the Treasury Department and many in the Congress have now been reduced to alleging that overseas Americans are at best just simply “irrelevant” to U.S. trade.

This is a unique opportunity for all of our organizations to work together on a win-win project. We would be most grateful, therefore, if each of you would consider joining with us in this initiative and forward this suggestion to President Bush for his priority consideration.

MORE BACKGROUND INFORMATION

More background information is provided in following sections:

- The Nature of the Level Playing Field Challenge
- The Un-level Playing Field: How the Export Tax on U.S. Citizens Tilts the International Playing Field to the Disadvantage of its own Citizens Living and Working Abroad and What to do About it
- The 1979 Report of the President’s Export Council
- A Brief Description of American Citizens Abroad (ACA)
- ANNEX 1: The Evolution of U.S. GDP and Trade – 1962 – 2003
- ANNEX 2: The President’s Export Council - 2004

All our very best wishes and our thanks for your most kind consideration.

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THE NATURE OF THE LEVEL PLAYING FIELD CHALLENGE

*How the Major Trading Nations Have Never
Used an Export Tax on Their Overseas Citizens
To Impede Their Ability to
Compete in World Markets*



INTRODUCTION

The major trading nations of the world, most of whom are members of the Organization of Economic Cooperation and Development (OECD), have adopted three basic approaches to the concept of a level worldwide playing field.

Positive Tilt Countries: These countries believe that their overseas citizens should enjoy a privileged competitive position in world trade. Citizens of these countries enjoy the enviable status of “most favored competitors” in all world markets. None of the “positive tilt” countries taxes the foreign source income of its overseas citizens. Furthermore, they have established special benefits that give their citizens considerable advantages in competing when abroad. Such benefits include, for example, subsidizing schools abroad and making provisions for overseas citizens to receive social security and unemployment benefits

Level Playing Field Countries: Other countries believe that international competition should be fair and equal for everyone working in the same local market environment. Citizens of these countries enjoy the ubiquitous status of “equal opportunity competitors”. They do not make any special provisions to provide their overseas citizens with special competitive advantages, but they try to ensure that their overseas citizens do not suffer any competitive disadvantages either. The “level playing field” is assured because these countries do not tax their overseas citizens on foreign source income while they are living and working abroad.

The Negative Tilt Country: The United States alone puts its overseas citizens into a severely handicapped position in world markets. For more than forty years, the U.S. has implemented a worldwide taxation system for individual U.S. citizens (and green card holders) living outside the United States. With this self-imposed negative tilt in the playing field, citizens of the United States, endure the unique status of “least favored competitors” in world markets. This has been a triumph of dogma over competitive equity and common sense. Despite repeated calls to repeal this economically self-destructive tax by the President’s own Export Council, by many American companies, and especially by many overseas American organizations, this stubborn dogma has continued to dominate the debate and damage the American economy.

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THE DIMENSIONS OF THE CHALLENGE

From a domestic economy perspective, foreign trade today represents about 25% of U.S. Gross Domestic Product (GDP). This means that nearly one in every four jobs in the United States now depends directly or indirectly on imports or exports. The United States has now accumulated a trade deficit of more than \$ 3.5 trillion, currently growing at a rate of over \$500 billion per year. The U.S. trade deficit is now running at more than 5 % of US GDP, an alarmingly high level which continues to grow every year. We are, in effect, becoming increasingly dependent on the generosity and indulgence of foreign investors and suppliers to our domestic economy. So far, they have been willing to accept U.S. dollar surpluses, but they also increasingly control the fate of our economy and our future financial stability.

WHAT CAN BE DONE?

Turning this situation around will be very difficult as many dynamic forces of international competition are at play. But one key factor is essential to help reverse the trade gap. The United States must recognize that its overseas citizens in the private sector are its finest and most effective assets in the promotion and protection of American interests everywhere in the world, and treat them accordingly. It should simply give them once again the chance to compete everywhere without any U.S. Government imposed handicaps.

HOW CAN THIS BE DONE?

Legislation to bring about basic changes in the treatment of overseas Americans was introduced several times during the last two decades by former Congressman Bill Alexander (D-Ark). The most recent three such proposals, affecting citizenship, direct representation of overseas Americans in the U.S. Congress, and taxation were introduced in 1992, and co-sponsored by former Congressman Ben Gilman (R-NY). The basic legislative language for these three issues is therefore readily available and can be easily brought up to date. But to bring about legislative change, the need to eliminate taxation of Americans overseas must be put on the agenda of the President's Advisory Panel on Tax Reform.

COSTS AND BENEFITS OF SUCH A LONG OVERDUE CHANGE

While this change in the treatment of overseas Americans might initially cost the United States some modest amount of lost annual revenues (currently about \$ 3.5 billion per year), this is small change compared to the huge value of future benefits to all Americans, and to the U.S. Treasury, that would start to accrue all across the board.

Not only would a larger and more ubiquitous overseas American community put the world on a sounder track toward more democracy, greater respect for fundamental human values, and augmented worldwide peace and prosperity, but there would also be huge benefits in the form of a much higher volume of exports and new jobs created at home as well as abroad.

Greater exports, more jobs? Says who? Well, as a matter of fact, many experts, including the former Chairman of General Electric and other senior American executives. More than twenty-five years ago they publicly stated that a level playing field would result in many billions of dollars of additional exports, and many hundreds of thousands of new jobs in the United States.

The Department of Commerce now estimates that for every \$1 billion in new economic activity about 17,000 jobs are created. Older sources, such as the 1979 Report of the President's Export Council, put the total amount of indirect and direct job creation even higher. These new domestic jobs alone would lead to new tax revenues in the United States that would be more than enough to cover the initial cost of lost revenues from abroad.





"THE UN-LEVEL PLAYING FIELD"

*How the Export Tax on U.S. Citizens
Tilts the International Playing Field
to the Disadvantage of all Americans
and What to do About it*



The export tax on U.S. citizens that is used today by the United States is the most unusual form of self-imposed competitive handicap the modern world has ever seen. The damage it causes is immense and grows greater and greater each year. Most remarkable of all, this punitive legislation it is not targeted against any enemies of the United States, but only against our own citizens. The damage, however, affects our entire national economy, and our ability to promote and sell American products and services in foreign markets.

But it is not just a question of economic competition, or export related jobs, either. It also affects the ability of U.S. citizens, of working age and retirees, in all walks to life, to be able to live and work among all of the peoples of the world, learning from them, sharing our ideas and ideals with them, and helping to bring peace, democracy, understanding and multiple dimensions of prosperity and tranquility everywhere.

The decision to introduce this new draconian approach to expatriate treatment was made early in 1962, but it had been discussed for quite some time, ironically even as a potentially clever way to protect domestic jobs. Today, it has become so enshrined in American practice that no subsequent administration has been able to eliminate it, despite its many evident negative consequences.

Consider, just for starters, the following results from an export and jobs perspective:

- ◆ Worldwide taxation creates an un-level playing field everywhere in the world except the United States itself, and the victims of this competitive infirmity are not foreigners but only Americans.
- ◆ Worldwide taxation is nothing other than "an export tax on American labor". As such, it gives a very strong incentive to both U.S. and foreign corporations to reduce to a minimum the number of U.S. citizens on their payrolls abroad.
- ◆ Because of this passport related penalty, more and more overseas entities of U.S. and foreign corporations are being manned and run by non-Americans.
- ◆ This tax led to the massive destruction of jobs for U.S. citizens abroad. More than twenty years ago estimates of the scale of such job loss put the total in the many tens of thousands. Today they are easily in the millions.
- ◆ This loss of jobs feeds back into the manufacturing and service industries within the United States. Americans working abroad help market and sell American products and services overseas. Loss of jobs hampers the competitiveness of American companies against foreign competition.
- ◆ There is a growing impoverishment of foreign experience within the American workforce itself. More and more domestic U.S. corporations now have to compensate by hiring foreign employees with international market experience to fill export related jobs even in the United States. We are in-

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sourcing foreigners to fill jobs that Americans are no longer qualified to fill at home because there are so few with actual overseas experience.

- ◆ Important decisions about purchasing raw materials and components for assembly by American companies abroad are now being made more and more by non-Americans. These inevitably lead to preferences for suppliers from the home countries of these foreign buyers. This, in turn, means that many jobs that could and should have been created in the United States for inputs to American corporate activities abroad are killed before inception.
- ◆ The United States today has the world's largest and most chronic trade deficit which aggregates now to more than \$3.5 trillion. It is growing at an annual rate of over \$500 billion. In comparison, the revenue gain to the United States from the taxation of the overseas income of US citizens is trivial, equivalent to less than one half of one percent of our current trade deficit, and only about one-tenth of one percent of total annual government revenues.
- ◆ The very concept of worldwide taxation of American citizens is the ultimate irony. The Revolutionary War, which gave birth to the United States, was sparked by a dispute between British expats and their home country over exactly this same issue. It was not right or beneficial then when the stakes were so much smaller. It is truly suicidal today.

In this brief paper, a few of the dimensions of this novel form of self-destructive behavior will be addressed. Such a study should make it clear why no other country in the world has ever been tempted to impose on itself such conditions.

SOME BASIC PROBLEMS OF EQUITY IN TRYING TO IMPLEMENT A WORLDWIDE TAXATION SYSTEM

1. DEFINING INCOME

One of the challenges of trying to tax the income of individuals living in other countries lies in defining what income to tax and how to define this income so as to be relevant to U.S. tax rules and practices. After wrestling with this for several years, it was finally decided that the currency you use on a daily basis abroad does not matter; as a U.S. taxpayer you live in a dollar world. Essentially what you earn or spend in a foreign currency is actually taking place in dollars, in an amount that must be defined at a rate applicable for the day each transaction takes place. There is a massive accounting and bookkeeping challenge involved here.

But this also raises the thorny question of how to treat fluctuations in exchange rates during a given year? For example, during the last couple of years the dollar has risen and fallen considerably within the space of any twelve-month period. If you are paid in a foreign currency and the dollar falls with respect to this currency, it will appear as an increase of taxable income. Meanwhile your foreign situation has not changed at all. In economic reality terms your daily life has not changed - your income is the same and so are your expenses. But once these are translated into U.S. dollars the amounts may change considerably. If it appears that your income has gone up, your U.S. taxes will follow likewise. Hence, overseas Americans are not only subject to double taxation but are also required to assume a foreign exchange risk to cover their tax obligations. Lest this be considered but a trivial problem, exchange rates in Europe and Asia have recently moved up or down by more than 20% in any one year. During the 2 year period from the end of 2001 to the end of 2003, the value of the dollar against the Euro changed by 40%! And in 2004, the dollar declined another 7 % against the Euro.

2. BLOCKED INCOME

Another problem can arise when an overseas American is living and working in a country whose currency is not legally convertible into dollars. While U.S. tax laws recognize that problems can arise in such a

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situation, they also view the use of any blocked income to pay for your normal living expenses as the act of its unblocking. Once unblocked, this foreign currency is subject to U.S. tax payments, which must be paid in U.S. dollars and without delay. In reality terms, however, such a unilateral decision by the U.S. Government does not change the problem: the foreign currency is still blocked and still not legally convertible. If the government of the country of residence does not follow the same bizarre logic and suddenly allow conversion into dollars, what are you supposed to do? There is still no sensible answer today. An overseas American in such a case is forced to violate either the laws of his country of residence, by obtaining dollars on the black market to pay the IRS, or of the United States, by not paying the tax.

3. DEFINING CAPITAL GAINS

Another problem arises when you purchase an asset or some physical property abroad, for example a house. For capital gains purposes, you are assumed to have purchased this asset in dollars at the exchange rate in effect on the day of purchase. But, when you sell the asset you are assumed to have carried out the transaction as of the exchange rate in effect on the date of sale. What happens if you actually lose money on the transaction, but appear to have made money when the purchase and sale are calculated in dollar equivalent values on different dates? You could well end up paying a significant amount of capital gains tax on a gain that in economic reality terms never existed. One interesting example of how this works concerns homes purchased entirely with borrowed money. The amount of phantom capital gain on the sale of a home, which appears when the buying and selling are converted into dollars, is held to be validly taxable. However, the phantom capital loss on the payback of a loan in a foreign currency (with the same exchange rate difference but in the opposite direction) is deemed invalid. The Tax Court has ruled that these are separate transactions and one could not offset the other. This is voodoo taxation of the first rank.

4. DEFINING FOREIGN TAX CREDITS

Ideally, to be really equitable, U.S. tax laws should take into account the economic reality of local conditions in each country of the world. This would be a nearly impossible burden on the IRS, of course, so instead some general rules are used which though relevant in some countries are very inappropriate in others. For example, what foreign tax already paid abroad can be used to offset taxes due to the United States on the same foreign source income?

In some countries, value added taxes are used as the primary source of revenue and may be imposed at a rate of more than 20% of the value of a transaction. Many of these countries collect much more revenue per capita today through these indirect taxes than via any direct income tax. But the United States does not recognize this kind of tax payment as creditable against U.S. tax liabilities on the same income. The U.S. feels it is being consistent with practices in the United States. This may be correct, but it is a comparison of apples and oranges; comparing the U.S. to the U.S. is not a relevant frame of reference for life in a foreign country. In terms of economic reality, such circumstances lead American citizens overseas to be taxed twice on the same income, without any U.S. tax credit given for these foreign tax payments.

Another example concerns individuals living in countries where capital gains are not taxed, but where total wealth is subject to annual taxation. Because the United States taxes capital gains but not wealth, the U.S. citizen will have to declare and pay a U.S. capital gain on all relevant transactions, but cannot claim any credit for taxes that have been paid on their wealth. Here again, in economic reality terms, the U.S. taxpayer is subjected to incompatible norms and comes out the loser, even compared to Americans back home.

THE IMPACT OF WORLDWIDE TAXATION ON CORPORATE PERSONNEL DECISIONS

While corporate personnel decisions are never made solely on the basis of whether or not an individual has a double tax liability, this can nevertheless play a significant role in such decisions.

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- **Americans vs. non-Americans as job candidates:** Consider, for example, the following case. Two individuals have nearly identical educational backgrounds, skill sets and experience. Both have the same gross foreign salary. But one gets to take home a lot more money than the other because one has an income tax obligation only to his foreign country of residence, while the other has a double taxation obligation to two sovereign countries. This may not only leave the overseas American with less take-home pay, but actually make it impossible to survive abroad.
- **Reimbursement:** If the corporation tries to be fair and guarantees all of its employees the same take home pay for the same gross salary, then the corporation has to step in and pick up the additional U.S. tax liability of its overseas American employee. Not only is this an extra cost, but it is escalating with every passing year. When this U.S. tax is reimbursed to the U.S. employee the following year, it too is deemed to be taxable income – a tax must then be paid on the reimbursed tax. Such a process has no end making reimbursement in effect impossible.
- **Allowances:** In addition, many overseas assignments are in conditions that are far below those that a U.S. citizen would have had back home. Corporations, therefore, frequently offer extra allowances for the education of children, home leave, etc. But, here again, these allowances cannot be used to their full value because the U.S. Government wants its share of all of this too - the home leave value, the value of the child's education grant, etc. So these also have to be grossed up. Even modest base incomes abroad, therefore, can quickly become much greater taxable income amounts when these allowances are added in.
- **The only rational choice for corporations:** Now, consider the temptation of a corporate manager abroad under pressure to maintain profitability. By merely replacing an American with someone of any other nationality, a company can save perhaps 30-40% in the personnel budget. This may not only be hard to resist, but might also be essential for the business to remain competitive and survive. And this incentive to get rid of the U.S. employee is due exclusively to the export tax on American labor that has been imposed unilaterally by the U.S. Government.

One only has to look at how the structure of the executive ranks and the work forces of American companies have evolved during the last couple of decades to see how effective this disincentive to hire a U.S. citizen for employment abroad has been. According to the U.S. Department of Commerce, the number of U.S. citizens employed by foreign affiliates of U.S. multinational corporations dropped in half from 1977 to 1999. By 1999 (the latest year available for the statistics), only 20'000 Americans were working for U.S. multinational corporations abroad.

WHY IT MATTERS IF AN AMERICAN FILLS A JOB ABROAD

There are many situations in which it can make a very big difference to the American economy and to the creation or loss of jobs in the United States, if it is an American who plays a key role in the decision-making processes of a company. Here are just a few examples:

1. FACTORY LOCATIONS AND CORPORATE PARTNERSHIPS

One example is the process by which a corporation decides whether to close a factory in the United States or abroad. If the U.S factory is a subsidiary of a foreign corporation, the final decision can depend not only on the rational factors in the decision-making process, but also on the inevitable chauvinism and loyalty factors of the participating decision-makers. Having an American present during such deliberations to defend a factory in the United States can help protect jobs back home. The same set of factors operates in corporate decisions for longer-term development partnerships, acquisitions, divestitures, etc.

2. CORPORATE PROCUREMENT DECISIONS

A similar sensitivity occurs when an American in a key procurement job is replaced by someone of another nationality. While some key raw materials and components are controlled by standard worldwide factors, many others are within the purview of the local procurement department. An American in a key

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job can help steer such decisions toward the American suppliers he/she knows and trusts. His/her replacement by someone of another nationality can just as easily, and will in fact is most likely, steer such purchases to a non-U.S. source better known and trusted.

3. CORPORATE CAREER DECISIONS

Finally, Americans in senior executive positions can have a very important influence on who gets chosen for continuing education, promotion, assignments in emerging markets, and top management positions. Those with significant foreign market experience will often be chosen over those without such experience. By making it highly unattractive for American and foreign companies to hire an American to work abroad, the U.S. puts an additional block on new jobs for Americans in important posts both at home and abroad.

THE PRESIDENT'S EXPORT COUNCIL WARNED OF THE DANGER AND DAMAGE ALREADY IN 1979

In 1962, when Congress introduced the worldwide taxation of the income of U.S. citizens who were bona fide residents of a foreign country, foreign trade (imports and exports combined) represented only 9% of U.S. Gross Domestic Product (GDP). The United States even enjoyed a small positive trade balance of \$3 billion which was the equivalent of 0.6% of GDP.

The toxic effect of this disincentive to working abroad was a slow but steadily accumulating poison in the American economic system. By 1979, the symptoms were becoming much more apparent: the United States had just experienced its seventh trade deficit in nine years and trade had doubled in importance to represent more than 18% of American GDP.

The President's Export Council, whose members included Senators Jacob Javits and Adlai Stevenson, Congressman Bill Alexander, the Governor George D. Busbee of Georgia, and the Chairmen of Sperry Rand, Gould Paper, Jefferson Mills, and Armco, decided it was time to take a closer look at how the taxing of overseas Americans might be contributing to this trade deficit problem. In his cover letter to the President, Reginald H. Jones, Chairman of the Export Council and also CEO of General Electric, stated:

"I am sure it was not the Administration's intent, or that of Congress, to discourage the employment of Americans by U.S. business overseas. The tax law must be one that enables Americans to face the uncertainties of life abroad and serve as the leading edge of the export growth that is necessary if we are to maintain the leading economic role for the U.S. in today's world that is so essential to our welfare."

The accompanying report stated:

"Americans working overseas are essential to a viable export program. An increase in the number of Americans assigned abroad can increase our exports, reduce the negative balance of payments, enhance our country's image, and raise employment in the U.S."

"Recognizing that it is in the best interest of our nation to encourage Americans to work overseas, the Task Force recommends the adoption of tax policies that are comparable to those of major competing industrial nations, none of which now tax citizens who meet overseas residency tests. We urge the development and enactment of new legislation to put Americans who work in the private sector overseas on the same tax footing as citizens of competing industrial nations."

Finally, it was recommended that:

"Work should begin immediately to encourage enactment of a new tax law to put Americans working overseas on the same tax footing as citizens from competing industrial countries."

These statements called in effect for the creation of the same 'level playing field' President Bush now proposes. Indeed, subsequent history has shown that Mr. Jones and his Export Council were correct and the implementation of their recommendations could have made a difference. Consider the following:

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The United States has never since had a trade surplus. Imports and exports continue to grow in importance and now represent nearly 25% of GDP. Between 1980 and 2003, trade deficits aggregated to more than \$ 3.2 trillion. By 2003, the trade deficit alone was equal to more than 4% of US GDP. In 2004, it jumped to nearly 6 % of GDP.

WHAT SHOULD BE DONE?

This is but a very brief overview of a complicated and challenging issue. And, of course, it merits a lot more study and cogitation. Yet, in essence, it can be reduced to a couple of basic principles.

It is not purely by chance that no other major country of the world has chosen to follow in our footsteps. Seen from their point of view, U.S. taxation of its overseas citizens is one of the most self-destructive trade and employment strategies any major country has ever adopted. But at the same time, it is also an extraordinarily generous gift, offered benevolently by the United States to everyone else, allowing their citizens to enjoy a very big competitive advantage over U.S. citizens in all of the markets of the world. Since none of their citizens even have to pay taxes to their home country on their foreign source income while living and working in the United States, they can compete on a level playing field everywhere.

What, then, should be done? Well, we could go back to the wisdom of the founding fathers. We could give U.S. citizens a chance to once again compete on a level playing field everywhere on this little planet of ours.

IT IS A VERY LOW-RISK, HIGH REWARD PROPOSAL

Let's assume that the President's Export Council in 1979 knew what it was talking about. If so, it is at least worth experimenting with some of their recommendation to let overseas Americans compete once again on a level playing field. Indeed, this might really make a difference in creating jobs at home and abroad, and in reducing America's chronic trade deficit. What kind of risk would really be involved? Abandoning the taxation of overseas Americans would be a very minor affair from the point of view of lost revenues received by the U.S. Government each year. The \$ 3.5 billion that overseas Americans pay today in annual U.S. federal income tax is less than 0.1% of total tax revenues of the United States. It was less than 0.5% of the trade deficit in 2003.

But if the Export Council is right, it would unleash a hoard of new Americans onto the world marketplace who would feel free once again to live and work abroad without financial inferiority to anyone of another passport. Companies would no longer have a financial incentive to fire Americans, or replace them with those of other nationalities. American entrepreneurs would be really free for the first time in a very long time to set up new companies to pull American products into foreign markets. And these entrepreneurs would also be able to serve as catalysts in helping developing countries move much faster toward their own economic prosperity than any aid programs could ever hope to achieve.

In essence then, an experiment to see how turning overseas Americans loose, and letting them compete for the first time in more than 40 years on a truly level playing field, is a very low risk and potentially very high reward opportunity. Why not give it a try? A worldwide level playing field for American ideas, culture, national security and prosperity, as well as trade, is where American policy belongs.



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**THE 1979 REPORT OF
THE PRESIDENT'S EXPORT COUNCIL**

Washington, D.C. 20230

December 10, 1979



The President
The White House
Washington, D.C.

Dear Mr. President,

The Executive Committee of the President's Export Council has asked me to express to its strong concern over the adverse effects on exports of the present rules (Section 911 and 913) concerning taxation of foreign earned income of Americans living overseas.

The Foreign Earned Income Act of 1978 has done little to alleviate the problems of differences in tax treatment between American citizens working overseas and their counterparts from competing industrial nations. The result has been that third-country nationals, who generally do not have the burden of paying taxes in their home countries on their foreign earned income, are employed instead of American citizens. This has brought about a sharp loss in the U.S. share of overseas business volume in vital economic sectors, largely because third party nationals tend to specify and order equipment manufactured in their home country, whereas American citizens would specify and order U.S. equipment with which they are most familiar.

A particularly disturbing example is the decline in the position of American contractors on projects in the Mid-East. According to McGraw-Hill, U.S. companies had contracted for \$ 8.9 billion of 10.3% of the total contracts let in the Mid-East from June 1975 through April 1978. During the 13 months ending June 1979, U.S. contractors received only \$ 346 million of 1.6% of the total contracts awarded. The loss of U.S. jobs both overseas and at home to foreign competitors, and the accompanying loss of U.S. exports comes at a time when it is crucial to maintain U.S. prestige and presence overseas and a firm emphasis on increasing our share of the world market.

The President's Export Council appointed a task force to study this problem. The following administrative recommendations, aimed at putting Americans who work in the private sector overseas on a more comparable tax footing with citizens of competing industrial nations, are adapted from this report.

- Regulations and interpretations in force under the current tax law concerning Americans living in camps in hardship areas (Section 911) should be simplified and made less restrictive, in keeping with the intent of Congress.
- The current tax law concerning allowances to employees for excess living costs incurred while working abroad (Section 911) should be interpreted in the least restrictive and simplest manner.

We have discussed these recommendations with Secretary Miller and would appreciate your endorsement of them.

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The final task force recommendation is that work begin immediately to encourage enactment of new tax provisions directed to this problem. We have called upon a broad spectrum of the American export sector for comments on specific legislative points which would relieve the burden under which they now compete, and would be in the national interest.

I am sure it was not the Administration's intent, or that of Congress, to discourage the employment of Americans by U.S. business overseas. The tax law must be one that enables Americans to face the uncertainties of life abroad and serve as the leading edge of the export growth that is necessary if we are to maintain the leading economic role for the U.S. in today's world that is so essential to our welfare.

Respectfully yours,

Reginald H. Jones, Chairman



THE PRESIDENT'S EXPORT COUNCIL
SUBCOMMITTEE ON EXPORT EXPANSION

**"Task Force to Study the Tax Treatment
of Americans Working Overseas".**



I. THE SITUATION

Despite the enactment of the Foreign Earned Income Act of 1978, Americans are still being taxed out of competition in overseas markets. The result is a sharp loss in the United States' share of overseas business volume in vital economic sectors. The current situation contributed to our negative balance of payments, a loss of U.S. jobs to our competitors, and the decline in U.S. presence and prestige abroad.

II. TASK FORCE RECOMMENDATIONS

Americans working overseas are essential to a viable export program. An increase in the number of Americans assigned abroad can increase our exports, reduce the negative balance of payments, enhance our country's image, and raise employment in the U.S.

Recognizing that it is in the best interest of our nation to encourage Americans to work overseas, the Task Force recommends the adoption of tax policies that are comparable to those of major competing industrial nations, none of which now tax citizens who meet overseas residency tests. We urge the development and enactment of new legislation to put Americans who work in the private sector overseas on the same tax footing as citizens of competing industrial nations. In the interim, the following remedial actions should be taken:

1. Regulations and interpretations in force under the current tax law concerning Americans living in camps in hardship areas (Section 911) should be simplified and made less restrictive, in keeping with the intent of Congress.

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2. The current tax law concerning allowances to employees for excess living costs incurred while working abroad (Section 913) should be interpreted in the least restrictive and simplest manner.
3. Work should begin immediately to encourage enactment of a new tax law to put Americans working overseas on the same tax footing as citizens from competing industrial countries.

III. BACKGROUND

Foreign Trade Encouraged

Beginning in the 1920's, after the U.S. emerged from World War I as a major exporting nation, the income of Americans at work in foreign countries was virtually exempt or excluded for U.S. taxes, as a matter of public policy and by specific acts of Congress. The purpose was to encourage foreign trade. It was recognized that the export of U.S. goods and services depended, in large measure, on the presence of Americans in overseas markets.

The U.S. tax policy was not unique. All of our trading partners, and certainly all of the world's major producing nations, had long excluded the income of citizens overseas from their domestic taxation.

In the early 1950's, some revisions were made in the tax treatment of U.S. citizens working overseas. The principal aim was to halt abuses by highly paid movie stars. These revisions altered foreign residency tests and placed a ceiling on the amount of foreign-earned income that could be excluded. The income and allowances of most Americans working overseas was below the \$20,000 limit, so they were not affected. They were not meant to be.

Additional technical adjustments were made during the 1960's in foreign residency tests and in the sums that could be excluded. By the mid-1970's, the effects of inflation - rising living costs and rising salaries and benefits for overseas American workers - had overtaken the amount of foreign-earned income that could be excluded from U.S. taxes.

Policy Shifts in 1976

Responding to misguided arguments that Americans overseas were being granted preferential tax treatment, Congress in 1976 reduced the exclusion to \$15,000 and changed the manner in which it was computed so its maximum practical effect became about \$3,000. The philosophy behind these provisions was directly contrary to the principles which had guided the United States' tax treatment of overseas Americans for more than 50 years. Instead of encouraging Americans to work overseas, the 1976 amendments actually discouraged such employment. In fact, even before the 1976 amendments, it was becoming less attractive to work overseas. Inflation was running at between 50 percent and 300 percent higher than domestic inflation, a fact that should have been recognized by increasing the \$20,000 exclusion rather than decreasing it.

Further, the Tax Court ruled in 1976 that employer furnished housing was taxable to employees at full local rental value, rather than the value of similar housing in the United States. These rulings were interpreted as a strong indication that employer contributions to offset extraordinary overseas living expenses - or so-called "keep whole" contributions - were taxable to overseas employees, whereas such amounts often may have gone unreported up to that time.

These rulings, when combined with the 1976 tax code revisions, produced effects that Congress and the Tax Court did not foresee. For example, in the oil-rich Middle East, the costs to an employer of maintaining an American worker at something approximating the standard of living he or she would have enjoyed at home could exceed the actual salary paid to that worker by three or four times. As a result, some Americans overseas became liable for more taxes than they received in real income.

The 1976 tax policy shifts on foreign-earned income actually amounted to a substantial tariff on our own goods and services by our own government.

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Foreign Earned Income Act of 1978

After belatedly postponing the effective date of the tax code revisions, Congress moved in 1978 to remedy the devastating mistakes of 1976 with the Foreign Earned Income Act. Unfortunately, the 1978 Act is inadequate. The House of Representatives had passed a realistic bill, but the law that was eventually enacted represents a compromise with a more restrictive Senate version. Section 911 of the Act provides a \$20,000 exclusion for overseas Americans living in qualified camps in remote hardship areas. Section 913 provides deductions for certain allowances for extraordinary overseas living expenses under fairly strict qualifications. Both Sections 911 and 913 are very complex. Moreover, regulations drafted by the Internal Revenue Service under the new law effectively reverse the intent of Congress by compounding the complexities beyond reason.

Even if the Foreign Earned Income Act of 1978 is interpreted in the least restrictive way possible, it is clear that overseas Americans are not currently competitive with citizens of other nations in terms of taxes.

IV. RATIONALE FOR RECOMMENDATIONS

Americans at work overseas direct business to our domestic economy. If we are to increase exports in order to bring our trade accounts into balance, we must encourage more U.S. citizens to accept assignments with American business overseas. Concurrently, we must continue to be sensitive to the geopolitical ramifications of having more Americans working abroad. Overseas employees of American business are seen as representatives of our country. Through their participation and visibility in international business affairs, they can function as goodwill ambassadors whose work exemplifies America's ideals and values.

To achieve these benefits will require, among other things, that current tax laws bearing on foreign-earned income be changed. At present, our nation's tax policies discourage the employment of Americans overseas. Many American companies doing business overseas, especially in manpower-intensive industries, are sending American employees home in order to keep some vestige of market share. For example:

- Recruiting firms in France, Germany, Italy and the United Kingdom report they are swamped with requests for qualified citizens of their respective countries to replace Americans who are being forced home by U.S. tax policies.
- Several leading U.S. contractors in the Middle East have reduced their American staffs by more than half, and adopted hiring policies overseas that specifically exclude Americans on future work.
- The University of Petroleum and Minerals in Saudi Arabia says Americans now make up less than 30 percent of its teaching staff, compared to more than 80 percent several years ago.

Replacing American employees with citizens of other countries is the only way American companies can remain competitive. This means that as U.S. companies operating overseas "de-Americanize," sales of goods and services move away from this country and toward the competing industrial nations.

- A report by the Government Accounting Office suggested that the impact of current U.S. tax policies for overseas Americans might be very significant - with a reduction of 5% or more of total exports or a loss in overseas sales of at least \$6 to \$7 billion, based on available data. And the GAO report cautioned that its projections might well prove conservative.
- The Commercial Counselor of the Embassy of Saudi Arabia recently observed:

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"U.S. tax treatment of American companies doing business in foreign countries makes them less competitive *vis a vis* European and Japanese (and other) companies, which receive better tax treatment from their governments. In the case of Saudi Arabia, it is noticed that American companies, in order to overcome the higher costs resulting from the unfavorable tax treatment, have tended to hire non-American engineers and other skilled personnel. Naturally, these prefer equipment and specifications originating in their countries (European or Japanese, etc.), which represent a loss in American exports to Saudi Arabia. Thus, the end result of U.S. tax treatment of American personnel working abroad has been a net loss of American sales abroad."

That means a loss of jobs in our economy. Estimates vary. Using the low end of the Department of Commerce estimate that for every \$1 billion in new economic activity between 40,000 and 70,000 jobs are created, a loss of 5% of our current overseas export volume - or about \$7 billion in economic activity - would produce a job loss of 280,000. Using the same Department of Commerce figures, if the U.S. decided on policies to increase exports by at least \$30 billion annually as a means of bringing the trade account into balance, at least 1.2 million new jobs would result.

If we increase our nation's exports we will increase job opportunities for Americans at home and abroad. In order to achieve such improvement, we must re-assess our tax policies. We also must write new tax laws directed at placing Americans on a competitive footing with other nationals in overseas markets.

V. CONCLUSION

The principle underlying the taxation of Americans working in other countries should be to encourage, rather than discourage, employment with U.S. business overseas. The implementation of this principle through changes to the Internal Revenue Code will increase the number of U.S. citizens who are willing to work overseas, resulting in an increase in American exports.

Respectfully submitted, Robert Dickey III, John Wood Brooks, D.I. Commons, and Maurice Sonnenberg.



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AMERICAN CITIZENS ABROAD



Celebrating 26 Years of Promoting and Protecting the Interests of Americans Overseas



The Birth of ACA: American Citizens Abroad (ACA) was founded in August 1978 in Geneva, Switzerland as a non-profit association under Swiss law. It was the institutional successor to two previous local organizations, the Geneva chapter of Tax Equity for Americans Abroad (TEAA), and the Geneva-based American Children's Citizenship Rights League (ACCRL). Both of these organizations had already been active in trying to address specific problems faced by overseas Americans due to discriminatory U.S. laws on taxation and citizenship.

Why ACA Was Created: The catalyst for ACA's creation was a specific provision in the State Department Authorization Act of 1979, enacted by the U.S. Congress in the summer of 1978, which tasked the President of the United States with the preparation and submission to the Congress of a report which:

- (1) identified all United States statutes and regulations which treat United States citizens living abroad differently from United States citizens residing within the United States, or which may cause, directly or indirectly, competitive disadvantage for Americans working abroad relative to the treatment by other major trading nations of the world of their nationals who are working outside their territory;*
- (2) evaluated each such discriminatory practice; and*
- (3) recommended legislation and any other remedial action the President finds appropriate to eliminate unfair or competitively disadvantaging treatment of Americans living or working abroad.¹*

One of ACA's founders had been instrumental in drafting this legislative language, and he and the other founders thought it would be appropriate for the overseas American community to assist the President in the preparation of his report to the Congress. ACA, shortly after its foundation, prepared a detailed report for the President identifying more than 50 issues that identified U.S. laws and regulations that caused problems for Americans living overseas. When this report was submitted to the President in late 1978, the White House officially endorsed the document and sent it to the relevant Cabinet departments as the frame of reference for their use in the preparation for their components of the President's report to the Congress.

When the President's report was submitted, there was considerable dissatisfaction in the Congress, and overseas, with the way the President had addressed some of the issues, particularly in the area of double taxation of Americans living and working abroad. ACA worked with the Senate committee staff to rewrite the mandate to the President and this time required that the report look not only at problems of

¹ Section 611 of the State Department Authorization Act of 1979 (PL 95-426)

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discrimination against Americans abroad in U.S. legislation and regulations, but also to analyze how U.S. laws and regulations might handicap the ability of overseas Americans to compete in world markets.²

ACA then wrote a second report for the President, commenting on the contents of the President's first report to the Congress, and adding a number of new issues addressing international competitiveness and the inability of overseas Americans to compete on a level world trade playing field.

After the President's second report was submitted to the Congress, both of the ACA reports to the President, together with the President's two Reports to the Congress, were published in a special Senate Foreign Relations Committee report.³

ACA's Continuing Relations with the Executive Branch and the Congress: For the last 25 years, ACA has had very productive relations with both the Executive Branch of the U.S. Government and the U.S. Congress. ACA representatives have testified before Committees in both the House of Representatives and the Senate, and have met regularly with senior Executive Branch officials. ACA has been instrumental in bringing about changes in laws and regulations on citizenship, taxation, social security, voting, the census, medical benefits for military retirees, the hiring of U.S. citizens by the U.S. Government abroad, and a number of other issues. ACA has also help draft a set of legislative proposals that would: (1) give American children born overseas the same rights to U.S. citizenship as foreign children born in the United States; (2) get rid of double taxation of Americans abroad; and (3) create a seat in Congress for a delegate to be directly elected by the overseas American community. These three proposals have been introduced during several recent Congresses.

A Congressional Mandate to the State Department: The Congress expressed a new interest in the generic concerns of overseas Americans during hearings on the Foreign Relations Authorization Act for FY 1994/95.⁴ The Conference Report for this legislation "urged": *"the Department of State, in cooperation with other relevant Departments of the U.S. Government, and with the active participation of the overseas American community, to undertake a review of U.S. laws and regulations that may impede the ability of American citizens abroad to compete in world markets with citizens of other nations on a level playing field"*.

Embassy Town Meetings Abroad: In response to this new Congressional request, the then Deputy Secretary of State instructed U.S. embassies and consulates to recognize: *"the importance of continuing your efforts to incorporate the views and expertise of our overseas private citizens and companies in policy-related activities. Posts should review their consultative arrangements with U.S. business firms, resident U.S. citizens, and their organizations to ensure that they include opportunities for consultation on these issues. Posts may wish to hold "Town Meetings" at which interested U.S. businesses, residents and organizations could express views and provide information."*⁵

The Status of Town Meetings Today and Lessons Learned: In 1998, ACA met with the State Department and the American Foreign Service Association (AFSA) in Washington, and with the U.S. Embassy in Bern, Switzerland, to develop a prototype format for regular embassy-organized town meetings abroad. The first formal issue meeting between ACA and the U.S. Embassy in Bern was held in October 1999, followed by a second a month later in November. Progress has been slow since then, however, because the Congress had only "urged" the State Department and U.S. Embassies and Consulates to hold such town meetings rather than "required" that they do so. This was a very valuable lesson in the importance of crafting legislative language so that the intent is precise and explicit.⁶ In a

² Section 407 of the State Department Authorization Act of 1980 (PL 96-60)

³ Senate Foreign Relations Committee Report on "U.S. Law Affecting Americans Living and Working Abroad", August 1980.

⁴ Conference Report 103-482 to Accompany HR 2333, Foreign Relations Authorization Act for Fiscal Years 1994 and 1995 (PL 103-236).

⁵ Message from Deputy Secretary of State Strobe Talbott to U.S. Embassies and Consulates, SecState 62577-Unclas-20 March 1995.

⁶ Reports of ACA-US Embassy Bern Town Meetings N°1 and N°2, October & November 1999.

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letter to ACA dated August 11, 2004, Maura Harty, Assistant Secretary of State for Consular Affairs, pledged to help renew the Town Hall Meeting concept and expand the scope for such discussions.⁷

ACA Organization and Membership: Since its birth in 1978, ACA has grown to embrace several thousand members in more than ninety countries worldwide including many who have subsequently returned home to live in the United States. In addition to offices in Geneva and Washington, DC, ACA has built up a network of several dozen "country contacts" on five continents. These country contacts are active private sector Americans who serve as links between ACA and the local American communities and provide a very useful two-way flow of information. ACA's officers and country contacts are volunteers and do not receive any regular salary or other compensation from ACA.

ACA Health and Life Insurance Programs: ACA offers access to interesting insurance programs that are available for U.S. citizens living overseas. You can contact us for more information.

ACA Award Programs: ACA has created two annual award programs:

The Thomas Jefferson Award is given to an employee of the U.S. State Department or Foreign Service who has been especially helpful to the American community abroad.

The Eugene Abrams Award is given to an American citizen living outside the United States who has contributed exceptional volunteer service to the local, national or international overseas American community.

ACA News Reports in Print: ACA prepares and distributes printed news reports, press releases, and other forms of communications on news and views of interest to the overseas American community.

ACA on the Internet: ACA has a very rich website (<http://www.aca.ch>) with regularly updated webpages providing news and commentary of interest to Americans abroad. The website has links to many other useful sites. Messages can be sent to ACA via email at acage@aca.ch.

ACA Fundraising: ACA solicits contributions from individuals, corporations and other private sector institutions. ACA does not solicit nor accept any funding from the U.S. Government. Donations from corporations gratefully accepted in both cash and in kind. Although several large donations have been received from generous individuals and corporate donors, most of the funds contributed for ACA's activities have come from small individual donations, and from fund-raising events such as the ACA annual auction in Geneva.

Joining ACA: If you are an American living and working abroad, membership in ACA is the easiest and most efficient way for you to obtain the information you need to understand the U.S. laws and regulations that affect you while you are abroad.

ACA Corporate Memberships: If you are working for an American company, corporate membership in ACA offers you and your employer a uniquely valuable opportunity to become a part of our well-respected education and lobbying efforts. By partnering with ACA, your company can have an even more powerful impact on the evolution of U.S. laws and regulations to make the lives of individual U.S. citizens abroad more prosperous and agreeable. We would welcome your membership, support and contributions.

* * * * *

ACA AS OTHERS SEE US

"American Citizens Abroad is a uniquely American organization, built by volunteers who have come together to accomplish goals of great benefit to Americans living all over the world. ACA's programs and

⁷ Letter of Assistant Secretary of State Maura Harty to ACA, August 11, 2004.

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activities are thoughtful, creative and above all effective. We're pleased to have ACA as a valuable and much appreciated partner of National Public Radio, NPR Worldwide."

Jeff Rosenberg, Director, NPR Worldwide.

"American Citizens Abroad" is a highly valuable resource for companies that have U.S. citizen employees working overseas. This all volunteer group endeavors to ensure that companies that employ Americans abroad do not suffer any competitive inconvenience or handicap because of inappropriate U.S. laws or regulations that affect U.S citizens who live outside their country of origin. ACA has a fine reputation for the diligence of its background work, the creativity of its proposals for reform, the effectiveness of its presentations in Washington, and above all for its more than 20 years of hard work and impressive results. They well deserve our thanks and support for their fine efforts."

Walter H. Diggelmann, CEO, Swiss-American Chamber of Commerce

"In a time of uncertainty in the American immigration system, "American Citizens Abroad" provides timely and critical information to Americans and their families living abroad. Staying on top of the almost daily changes in US laws and regulations is more important than ever and ACA is playing a vital role not only in getting this information to its members but in actively advocating on behalf of its members. "

Greg Siskind, Partner, Immigration Law Offices of Siskind, Susser, Haas & Devine

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