



Adapting the U.S. Tax Code to the 21st Century
RECOGNITION OF FOREIGN PENSIONS AND
GOVERNMENT SPONSORED RETIREMENT SAVINGS PLANS

ACA recommends that foreign pensions which qualify under local laws and foreign government sponsored retirement savings plans be recognized as the “equivalent” of qualified for U.S. tax purposes, thereby applying the “same country rule” to Americans who resides in the same country as the pension and savings plan or to the residence of the foreign employer as long as the American is a bona fide overseas resident; the employer may be located in one country while the American works for that employer in another country, for example oil rig work.

Problems with the current system

Today, only some Canadian and UK retirement savings plans are recognized by the U.S. as “qualified” and equivalent to U.S. plans through specific chapters in the U.S. tax treaties. Retirement plans in other countries are not recognized as qualified, which leads to immediate taxation in the U.S. of the employer’s and employee’s contributions as well as unrealized gains in the plans even when individuals are prohibited from withdrawing these funds; local taxation in the foreign country will be years or decades later in retirement. Non-qualified foreign pensions can be classified as foreign trusts or PFICs, which leads to penalizing U.S. taxation on income and gains in the retirement funds as they accrue, without the tax deferral advantage of qualified U.S. pension funds. This creates costly and uncertain taxpayer filing since foreign pension funds do not provide the breakdown of gains and income required by the IRS. Non-recognition of foreign pension funds hinders effective saving for retirement of Americans working abroad, acts counter to the objective of most income tax treaties to prevent double taxation and is diametrically opposed to the tax treatment of U.S. domestic pension and retirement savings plans.

Working through treaties with individual countries to correct this unfair treatment of Americans abroad is a cumbersome, slow and costly process. The country by country approach accentuates discrimination among Americans abroad, depending on the country where they live.

Recommended changes in the law

ACA recommends that Congress enact legislation that would apply worldwide to all Americans working and retired overseas, to correct the double taxation of foreign pension funds and savings plans. The law would:

- Recognize contributions to foreign pension fund as well as to foreign government sponsored retirement savings plans made in accordance with local law to be “equivalent” to U.S. qualified pension funds and U.S. government sponsored retirement savings plans, such as 401K plans with tax deferral features recognized and accepted by the United States. Foreign pension plans would not be subject to PFIC or Foreign Trust reporting requirements. To prevent abuse, limits may be imposed on the amount of tax deferred contributions allowed for private pension plans, especially if the foreign employer is a Controlled Foreign Corporation.
- Accept that annuities received by Americans abroad from foreign pensions be taxed only by the country of residence.
- Override the savings clause in double taxation treaties with regard to annuities and other income from U.S. source pensions to ensure that they be taxed only by the country of residence.

These measures would greatly simplify IRS tax administration and taxpayer compliance, stop double taxation related for foreign pension and retirement savings instruments and eliminate the discriminatory treatment of Americans overseas. They would enhance U.S. competitiveness and promote U.S. foreign trade.