Center for Freedom and Prosperity

Comments of the Center for Freedom and Prosperity

to the

International and Financial Services Tax Reform Working Groups

Committee on Ways and Means

United States House of Representatives

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The Center for Freedom and Prosperity has opposed the Foreign Account Tax Compliance Act (FATCA) since before it was passed. While these early warnings went largely unheeded, it has since become abundantly clear that passage of the law was a mistake. For the following reasons, and in order to ensure a tax code that is simple and fair while also promoting economic growth, FATCA must be repealed:

- FATCA is not a good solution to the nation's limited tax evasion;
- FATCA is harming the US economy;
- FATCA is devastating for Americans abroad and violates fundamental privacy rights;
- FATCA's intergovernmental agreements undermine separation of powers;
- FATCA is a bad neighbor policy that is alienating the global community.

FATCA is a poor solution to tax evasion

The primary goal of FATCA is purported to be the reduction of tax evasion, yet the law will have little impact in this regard. Rather than target areas at high risk for evasion, FATCA casts a broad and expensive net over the entire foreign financial sector. Its primary victims will simply be law-abiding American citizens living and working abroad. Meanwhile, the Joint Committee on Taxation predicts a mere $792 million in additional revenue per year, or less than 1% of the $100 billion frequently purported as being lost to tax evasion each year.

FATCA duplicates a host of existing programs designed to reduce tax evasion, including but not limited to the Qualified Intermediary program, FBAR forms, and Tax Information Exchange Agreements. There is no justifiable reason to pile on to these existing programs, particularly when recognizing that the US already has one of the highest tax compliance rates in the developed world.

Given the nation's relatively minor problem with tax evasion, FATCA amounts to trying to kill a fly with a sledgehammer.

FATCA is harming the US economy

Foreign financial institutions face the choice of either bearing the large cost of complying with FATCA – estimated at $100 million or more for larger institutions – or facing a 30% withholding penalty on US source payments. Some number of institutions are simply choosing “none of the above” and withdrawing their investments from the United States. This is an extremely undesirable outcome, and thwarts the long-standing Congressional preference of making the US an attractive destination for investment.

Capital is the essential lifeblood for any growing economy, and thanks to large federal deficits the United States is particularly reliant on foreign investment to offset the significant capital devoted to financing the public sector. Discouraging such investment in pursuit of a tiny bit of tax revenue is counter-productive. Depressed tax revenues from the lost economic activity may even entirely offset what FATCA expects to take in.

FATCA is devastating for Americans abroad

Instead of targeting individuals suspected of tax evasion, FATCA treats all Americans who live, work or bank overseas as criminals. FATCA's reporting requirements furthermore eviscerate privacy rights and make a mockery of 4th Amendment protections.

Many Americans abroad have reported being turned away by local financial institutions, having their banks accounts closed, being denied mortgages, and being unable to participate in pension funds all based solely on their American citizenship. As a result, the number of Americans renouncing their citizenship is growing rapidly. This is an unnecessary and unacceptable loss of talent.

Not only are American expatriates and multinational companies more likely to purchase US made goods and raw materials than are foreign individuals and companies, but by example so to do foreigners with whom they come in contact. Americans who live and work overseas thus serve as ambassadors of goodwill, and often times represent the most direct contact foreigners have with the United States. Alienating these individuals and hounding them out of the country is pure folly.

FATCA's intergovernmental agreements undermine separation of powers

For all the problems created by FATCA, the most pernicious may also be the least expected. Because FATCA was impossible to enforce as written – working directly with hundreds of thousands of FFIs proved overwhelming to the IRS – the Treasury Department has taken it upon itself to negotiate directly with foreign governments, a prospect not at all planned for in the actual legislation.

In the course of these negotiations, Treasury has even gone so far as to promise to pursue similar domestic requirements, which would mean significant and costly burdens for domestic financial institutions, in order to entice governments to sign with the offering reciprocal information. Given the lack of authority within FATCA for this course, the IGA process raises serious questions regarding the proper role of the executive branch when it comes to setting domestic and international tax policy. Furthermore, the agreements are seen as treaties by signing partners, yet only considered executive agreements within the US, which allows Treasury to circumvent the Senate's advice and consent responsibility.

FATCA is a bad neighbor policy that is alienating the global community

FATCA imposes requirements on institutions outside of any US political authority, demanding they work on behalf of the IRS even when it conflicts with domestic law. It ignores the basic fiscal sovereignty of other nations and presumes the right to override their policy preferences. This is not how a democracy looking to set an example for the rest of the world should behave.

Similar rules by foreign governments targeted at domestic banks would not be tolerated by the United States. Leaders from a variety of nations, such as Canada, China and Russia, have spoken out against FATCA, while many others are simply too afraid of the international bully to do so, and the law is likely to continue to harm relations with these and other countries.

Conclusion

Increasing tax compliance is a important policy goal, but it is hardly the only one of interest to lawmakers. The costs of tracking down ever last potential tax dollar must be weighed against competing goals, like promoting economic growth and preserving privacy rights. With the United States already sporting one of the world's highest compliance rates, while also still trying to recover from a recession and reduce excessive government spending, it makes little sense to prioritize the high cost of marginal increases in compliance above economic growth.

There is a better way to advance all of these legislative goals. Complex tax codes with high rates have been shown to cause more tax avoidance and evasion. They also stunt economic growth and reduce prosperity. The solution to one problem is the same as the other. Sensible, pro-growth reforms like ending double taxation on savings and investment, simplifying the tax code, lowering rates, and only taxing on a territorial basis will not only enhance national economic well being, they will also make it less likely that individuals will work to avoid paying their appropriate tax burden.

FATCA was passed without proper consideration for its impact. No hearings were ever held, nor was the law ever debated in Congress. Haste is inappropriate when dramatically restructuring national tax policy. The current reform effort clearly recognizes this fact, and should thus consider FATCA repeal an essential part of successfully reforming the nation's taxes.