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Fatca regime may have unintended consequences for financial system

Crackdown on Americans' money in overseas accounts may lead to the growth of shadow banking and the financial power of other countries

By Peter Guy
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Many financial institutions are still completely confused and unable to comply with the US government's Fatca regime. "Foreign Account Tax Compliance Act" sounds like another innocuous tax regulation. But it represents the most ambitious tax and personal data collection strategy in financial history. It will embolden and encourage more global intrusions by US government agencies. More people will be driven underground to seek shadow banking services.

Fatca is controversial because it dramatically shifts the burden of disclosure from the American person to their banks. Foreign financial institutions are now more than just tax bounty hunters for the US Internal Revenue Service (IRS), but pawns in an historical power play for control over the global financial system.

Government agencies possess long, institutional memories. Contempt for what they consider to be rogue bankers in financial centres such as Switzerland and its secrecy laws stretch back to the second world war.

Nazi Germany allowed Spain, Sweden and Switzerland to remain neutral so that they could be used as foreign exchange agents. Reichsmarks, the German currency during the war, were declared non-convertible by Allied nations. By trading with neutral countries, Germany effectively made its currency and gold convertible on the world market. These bankers helped the Nazis extend the war effort by importing goods and materials through converting reichsmarks.

US dollar and financial asset mobility accelerated in the 1950s with eurodollars - offshore deposits of US dollars. Unregulated, offshore US dollar accounts made it possible for the ill-gotten gains of tax evaders and criminals to flow overseas to secret Swiss bank accounts.

September 11 and the "war against terror" motivated all branches of the US government to aggressively pursue any terrorist activity. The US Department of Justice revolutionised the prosecution of offshore tax evasion in 2009 with a breakthrough criminal case against UBS, Switzerland's largest bank.

An American gambler stashes his poker earnings at a Macau casino to avoid Fatca

The bank was accused of conspiring to aid 52,000 American clients to evade US taxes. UBS avoided prosecution and agreed to reveal the identity of 4,450 US customers and paid a US$780 million fine. The IRS successfully ended Swiss bank secrecy and inspired a global crackdown on offshore tax evasion by US persons - embodied by Fatca.

The unintended effects and outcome of Fatca are already manifold, especially in Asia where shadow banking is a growth industry. An American gambler described to me how he stashes his poker earnings at a Macau casino to avoid Fatca's reach into banks.

Another innovative shadow banking service allows clients to deposit their yuan in an onshore, mainland bank account that they specify. For a 22 per cent commission they will exchange and deliver the US dollar equivalent of physical cash in a suitcase anywhere in Vancouver or New York. American residents in Asia seeking to hide assets only have to find a strictly local Asian bank with no links to the US banking system.

Russian billionaire oligarch Gennady Timchenko was recently affected by the policy of travel bans and asset freezes by the US government. He announced he would rip up his Visa and Mastercard and transfer all his personal credit card accounts to China's UnionPay.

He told the Russian press: "In some ways it is more secure than Visa - at least the Americans can't reach it."

The ascendance of parallel financial powers represents a threat to US dollar hegemony. Fatca extends US taxing authority far beyond legally requiring expatriate Americans to file accurate tax returns.

According to Dan Mitchell, senior fellow at the Cato Institute, Fatca is expected to yield only US$870 million a year. "This is a miniscule amount compared to the amounts being spent to implement this law, by the US government and up to 100,000 other institutions who didn't ask to be part of this."

Resistance is futile for any bank that participates in the global money centres and needs to deal in US dollars. But the goal and reward isn't improved tax collection, it is a surveillance exercise made possible through the creation of a massive global database.

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