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An act of economic strangulation

Obama's new tax rules for foreign accounts will punish Americans

By: Richard Rahn
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Do you know why the U.S. economy shrank almost 3 percent in the first quarter of this year? When the news of the dreadful gross domestic product (GDP) number came out last week, many were surprised, but none were more surprised than the folks in the Obama administration. Many of their supporters had been saying this was the year of a real economic recovery.

The quick reaction was to blame the bad GDP numbers on the weather, and it is true that much of the country did have record cold temperatures, but in all likelihood the weather was only a minor factor. (It is rather ironic that the president blames the bad economy on the cold weather, while at the same time he is running around the country saying we have to spend many more tax dollars to prevent warmer weather a hundred years from now. Misplaced priorities?) The excuse-making by the president reminded me of how the rulers of the Soviet Union used to blame bad economic news on the weather — 70 years of bad weather.

However, serious economists such as professor Casey Mulligan of the University of Chicago have better explanations for the downturn. Mr. Mulligan has carefully documented both the explicit and implicit new taxes in Obamacare, many of which came into effect during the first quarter of this year. An implicit tax is a reduction in benefits going to workers, which reduces the rewards for working. Mr. Mulligan argues that Obamacare adds "about six points to the marginal tax rate faced, on average, by workers in the economy . Let's not be surprised that, as we implement a new law that taxes jobs and incomes, we are ending up with fewer jobs and less income."

Economic forecasters are downgrading their outlook for the U.S. economy this year. Yet the administration blames others for these mostly self-created economic headwinds. The United States has the highest corporate tax rate in the world among developed countries. Officers of companies that can produce and sell goods and services in many countries fail in their fiduciary responsibilities if they choose to headquarter them here, other things being equal, when they could save two-thirds or more on their corporate tax bill by moving out of the United States. As a result, almost every week there are announcements of companies moving out of the U.S., which over time will mean fewer jobs, reduced research and development and less total tax revenue. The obvious solution is to reduce the U.S. corporate tax rate to a globally competitive level, but the economic know-nothings in the administration and Congress are proposing to increase penalties for moving — in an oppressive and destructive attempt to make both individuals and companies tax slaves.

Finally, the administration is about to implement on July 1 perhaps the most stupid and destructive piece of tax regulation ever devised — the Foreign Account Tax Compliance Act (FATCA). This one regulation by itself may well cause another drop in GDP during the third quarter of this year, owing to both the uncertainty it engenders and the fact that it will drive out significant amounts of foreign capital. This will, in turn, add to U.S. job woes. The Economist magazine stated that the act "is doing more harm than good," and that "FATCA turns foreign banks and other financial institutions into enforcement arms of America's Internal Revenue Service (IRS). They must choose between handing over information on clients who are 'U.S. persons' or handing 30 percent of all payments they receive from America to Uncle Sam."

The regulations are vague about which non-bank entities are "financial institutions" — a definition that can be infinitely elastic. As The Economist notes, there is confusion about the definition of a U.S. person. "The definition is broad and includes not only citizens, but current and former green-card holders and non-Americans with various personal and economic ties to the United States." Last week, a lawyer who must advise his clients on the act showed me 200 pages of "guidance notes" he had received — many of which were undecipherable. An executive with a major global financial services company told me his firm had 70 lawyers working to try to figure out the Foreign Account Tax Compliance Act. The expected revenue from the act to the Treasury is only about $800 million per year (which is probably exaggerated), while the cost to the 77,000 or so financial institutions and millions of individuals who must comply will be many times that amount. Typically, the Obama administration failed to do a cost-benefit analysis of the act (shades of Obamacare).

In addition to being economically destructive and offensive to America's foreign friends, the Foreign Account Tax Compliance Act is resulting in overseas Americans having their bank accounts closed — owing to the costs and risks to the financial institutions. Owing to its global information-sharing provisions, the act grossly violates the basic human right of reasonable financial privacy for everyone.

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