

# ISSUE BRIEF

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## FATCA Hurts Law-Abiding Americans Living Abroad

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On July 1, the Foreign Account Tax Compliance Act (FATCA) will fully take effect. FATCA is supposed to reduce tax evasion by making it harder for tax cheats to abuse tax havens. In practice, however, FATCA is forcing law-abiding American taxpayers residing overseas to bear enormous financial and legal burdens.

Congress should reform FATCA so that it does not hurt innocent Americans residing and working overseas. More important, Congress should turn its full attention to broader tax reform that would help curtail tax evasion in a more effective way without resorting to onerous and intrusive regulations such as FATCA.

### Empowering the IRS

FATCA sailed through Congress in March 2010 and was signed into law by President Obama as part of the Hiring Incentives to Restore Employment Act.<sup>1</sup> There was little congressional scrutiny or debate of its complex details.

Like another ill-considered piece of legislation enacted that same year (Obamacare), FATCA granted the IRS a new level of intrusiveness into the lives of Americans. According to White House talking points that laid out the blueprint for FATCA:

[One of the proposals] requires foreign financial institutions that have dealings with the United States to sign an agreement with the IRS to become a “Qualified Intermediary” and share as much information about their U.S. customers as U.S. financial institutions do, or else face the presumption that they may be facilitating tax evasion and have taxes withheld on payments to their customers.... As part of the Obama Administration’s budget, the IRS will hire nearly 800 new employees devoted to international enforcement.<sup>2</sup>

Prior to FATCA, the U.S. had many tax information exchange agreements with other countries to help curb the use of foreign accounts to facilitate tax evasion.<sup>3</sup> These agreements require foreign financial institutions to provide certain information on customers to the IRS.

FATCA goes much further, requiring foreign financial institutions—including banks, stock brokers, hedge/pension funds, insurance companies, and trusts—to report more detailed information to the IRS about their American customers each year. Under the legislation, the IRS is granted enhanced regulatory power in determining, based on its judgment, whether Americans with these accounts have wrongfully evaded U.S. taxes.

### FATCA Hurts Law-Abiding American Taxpayers Working Overseas

U.S. tax laws are complex by world standards and highly unusual in their attempt to extend the reach of the IRS beyond the country’s borders. In the case of FATCA, the legal burden falls on foreign financial

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institutions with U.S. customers. Those that do not comply are subject to a variety of serious financial and legal penalties. FATCA's costly IRS reporting requirements and its significant legal and financial risks make it unprofitable and arduous for foreign financial companies to serve Americans. Many have thus been reluctant to work with the IRS in implementing the law.

Others, however, have adopted another strategy for avoiding FATCA: simply denying service to American customers. In fact, some institutions have already closed the pre-existing accounts of their American clients.<sup>4</sup> Lack of access to financial services has made it extremely difficult for Americans living and working abroad to conduct even rudimentary financial tasks such as cashing their paychecks.<sup>5</sup>

Not so surprisingly, a recent poll reveals that almost 70 percent of them have considered giving up their U.S. citizenship because of FATCA.<sup>6</sup> In fact, many of them already have. In 2013 alone, 3,000 Americans living overseas voluntarily gave up their citizenship—a 221 percent rise from the 993 people who gave up American citizenship in 2012.<sup>7</sup>

Democrats Abroad, “the official arm of the Democratic Party for US citizens living outside the United States and its territories,” summarized:

Congress passed FATCA to bring an end to illegal tax avoidance by Americans in the US who use overseas financial accounts to secret untaxed

earnings out of the country. But Congress did not fully anticipate the impact [FATCA] would have on overseas Americans and we, therefore, are now burdened with a tax reporting obligation that treats us like suspected tax cheats and money launderers.... [We] Americans living abroad now find our financial lives exposed to a degree of scrutiny—under threat of severe penalties, fines and even imprisonment—to which Americans living stateside are not subjected. Implicit in this stringent reporting regulation is the unfair and unjustified suspicion that Americans living abroad are tax cheats and/or money launderers, which clearly the vast majority are not.<sup>8</sup>

### Time to Reform FATCA

Reducing tax evasion is a laudable goal, and FATCA may reduce it somewhat. Only time will tell by how much. However, whatever reduction it achieves is coming at a significant cost that could far outweigh the potential benefits. Even IRS commissioner John Koskinen realizes the unfair burden FATCA puts on law-abiding American expatriates. He recently indicated that the IRS is looking to make it easier for them to comply with FATCA. That could be a big improvement if the IRS follows through in a timely manner.<sup>9</sup>

Congress should reform FATCA's heavy-handed approach to tax enforcement now to lessen the burden it is imposing on Americans living abroad and to prevent it from becoming an even bigger problem

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1. Thomson Reuters, “IRS Delays FATCA Financial Institution Registration Deadline and Liberalizes IGA Treatment,” <https://tax.thomsonreuters.com/media-resources/news-media-resources/checkpoint-news/daily-newsstand/irs-delays-fatca-financial-institution-registration-deadline-liberalizes-iga-treatment/> (accessed June 6, 2014).
  2. The White House, Office of the Press Secretary, “Leveling the Playing Field: Curbing Tax Havens and Removing Tax Incentives for Shifting Jobs Overseas,” May 4, 2009, [http://www.whitehouse.gov/the\\_press\\_office/LEVELING-THE-PLAYING-FIELD-CURBING-TAX-HAVENS-AND-REMOVING-TAX-INCENTIVES-FOR-SHIFTING-JOBS-OVERSEAS](http://www.whitehouse.gov/the_press_office/LEVELING-THE-PLAYING-FIELD-CURBING-TAX-HAVENS-AND-REMOVING-TAX-INCENTIVES-FOR-SHIFTING-JOBS-OVERSEAS) (accessed June 6, 2014).
  3. U.S. Department of the Treasury, “Treaties and TIEAs,” <http://www.treasury.gov/resource-center/tax-policy/treaties/Pages/treaties.aspx> (accessed June 6, 2014).
  4. Sophia Yan, “Banks Lock Out Americans over New Tax Law,” *CNN Money*, September 15, 2013, <http://money.cnn.com/2013/09/15/news/banks-americans-lockout/> (accessed June 6, 2014).
  5. Andrew Quinlan, “Coerced Foreign Tax Compliance Is Killing American Jobs,” *Forbes*, November 20, 2012, <http://www.forbes.com/sites/realspin/2012/11/20/coerced-foreign-tax-compliance-is-killing-american-jobs/> (accessed June 6, 2014).
  6. Kim Hjelmggaard, “Americans Abroad Find Citizenship Too Taxing to Keep,” *USA Today*, March 8, 2014, <http://www.usatoday.com/story/news/world/2014/03/08/usa-citizens-relinquish-passports-tax-filing/5859371/> (accessed June 6, 2014).
  7. *Ibid.*
  8. Jason Siegel, “What Is FATCA, What Are Its Impacts and How We Aim to Reform FATCA,” Democrats Abroad, <https://www.democratsabroad.org/group/fbarfatca/what-fatca-what-are-its-impacts-how-we-aim-reform-fatca> (accessed June 6, 2014).
  9. Mackenzie Weinger, “IRS to Ease Pressure on Non-Criminal Tax Dodgers,” *Politico Pro*, June 3, 2014, <https://www.politicopro.com/member/?webaction=viewAlerts> (accessed June 6, 2014).

as it goes further into effect—one that runs the very real risk of exposing law-abiding Americans working overseas to greater IRS exploitation and targeting.

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