

FATCA Turning Local Banks Into IRS Enforcers

During the 18 months I spent in this city in 2005 and 2006 the gargantuan structure of the American embassy was being constructed on a full city block bordering on the hill atop which sits the hallowed temple Wat Phnom.

Looking like one of the cavernous buildings that dominate both sides of Constitution Avenue in Washington, D.C., with security fences, barricades, guard houses and surveillance systems that would be adequate for the White House, I found it hard to not to imagine that—like Dorothy’s Nebraska farm house landing in Oz—this otherworldly made-by-USA fortress had by some sorcery dropped from sky into its unnatural setting.

No doubt, in the post-9.11 world, every U.S. government building everywhere was being built like Fort Knox, at a cost of the contents of one of the gold repository’s vaults. Still, the colossal scale of the thing—dwarfing all but a few Cambodian government buildings—seemed then, and seems now, to be grossly and offensively out of place.

Whether the offense is assuaged or compounded by what goes on inside the embassy will be in the eye of the beholder. A list of the embassy’s offices—provided on its website (obviously not everything, e.g. the CIA station chief’s office)—is: Centers for Disease Control and Prevention; Defense Attaché; Defense Cooperation; POW/MIA; the US Army Medical Component of the Armed Forces Research Institute of the Medical Sciences (USAMC-AFRIMS); FBI Legal Attaché; Consular Office (U.S. Citizens Services/Visa Services); Political/Economic Office; Public Affairs; Regional Security; Peace Corps; United States Agency for International Development (USAID); The U.S. Naval Medical Research Unit-2 (NAMRU-2).

What stands out in this list is the broad footprint of the Pentagon and U.S. involvement with Cambodia’s military. The embassy website describes the activities of the Office of Defense Cooperation thusly: “ODC Cambodia conducts Security Cooperation activities in support of the U.S. Country Team and U.S. Pacific Command (USPACOM) in accordance with the Theater Security Cooperation Plan (TSCP) to advance U.S. national interests and national military objectives.”

It is not apparent from the embassy directory, and may not even be the case, that the U.S. Internal Revenue Service is physically present in Cambodia. But there can be no denying that the IRS is here, with heavy-handed, extraterritorial powers that suggest a kind of financial neo-colonialism.

I am speaking about FATCA—the U.S. Foreign Account Tax Compliance Act—that will come into effect on July 1. This regime, signed into law by President Obama on March 18, 2010, requires foreign banks to report to the IRS information names, tax I.D. numbers, addresses, and transactions of information of U.S. person account holders—individuals or 10% or more “entity shareholders”—and, in some cases to withhold and pay directly to the IRS 30% of the interest earned by these account holders.

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More chilling still, the law turns local banks into IRS investigators, requiring them to perform “due diligence” on “suspicious” account holders or applicants who may have opened accounts using foreign passports but may have dual U.S. citizenship or permanent residence. Banks must report such “suspicious” persons. Failure or insufficient attention to doing so will find the bank “negligent” and subject to sanctions.

Last week the U.S. Treasury Department issued press releases boasting of the near universal compliance of foreign banks with the new law. In fact banks in the ASEAN region were universally opposed to it. They will comply because the regime gives them no choice.

Almost all foreign banks make payments and settle transactions through U.S. correspondent banks in New York. During the past two years these U.S. banks have told the local banks that FATCA requires them to cease providing correspondent services if the local bank does not comply with FATCA. Further, to close the “loophole” of a non-compliant local bank going through a non-U.S. bank, say a Singapore bank, for payments, FATCA will bar U.S. banks from dealing with the Singapore bank.

FACTA requires local banks to sign compliance agreements directly with the U.S. Treasury Department. It is U.S. government-to-financial institution, not government-to-government. Which is to say, FATCA does not recognize other countries’ sovereignty.

Cambodia, along with Singapore, and many other countries—most famously Switzerland—has bank secrecy laws. FACTA in practice unilaterally and arbitrarily overrides other countries’ laws. This is quasi-colonial extraterritoriality. Apparently, the “rule of law in international affairs”—an increasingly tiresome Obama administration refrain—applies only when the law is made in Washington, D.C.

To save its face, and the semblance of sovereignty, the National Bank of Cambodia counseled local banks to ask U.S. account holders to sign “Consent Letters” authorizing local banks to report to the IRS. The inducement would be that the local bank would not withhold 30% of interest, as FACTA requires against “recalcitrant” account holders. Otherwise, they must withhold and pay to the U.S. Treasury.

Any foreign bank that receives payments from U.S. correspondents but has not complied with FACTA will be found “recalcitrant”—meaning that the U.S. payor must withhold and pay to the U.S. Treasury 30% of gross payments, for which the foreign cannot seek a refund or credit.

Having any accounts for U.S. citizens and permanent residents or “entities” will soon create a huge reporting and administrative burden for local banks. Many have simply decided to refuse to open accounts for U.S. citizens.

What about current U.S. account holders? The July 1 FACTA start date applies to new customers. Application to existing customers is phased in: during 2015-2016 for pre-existing high value individual and corporate accounts (\$50,000 and above), 2016-2017 for all accounts.

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One hears much “barbarians at the gates” alarmism about how some—I would say many—countries, like China, are dissatisfied with parts of the largely U.S. made international system of laws and institutions. It is not just that they had no part in building this system. It is that they have different ideas about what a harmonious system requires.

I am quite sure that any country that put a high value on interstate harmony, and its *sine qua non*, respect for other countries’ sovereignty and independence, not to mention the freedom and privacy of its citizens, would not have brought us FATCA.



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