

Internal Revenue Service
Hearing on Proposed Regulations
(REG-146097-09)
Guidance on Reporting of Deposit Interest Paid to Nonresident Aliens

Statement by
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Thank you for the opportunity to share my views with you. I am Andrew Quinlan and I am the President of the Center for Freedom and Prosperity. We are an Alexandria, Virginia-based, 501(c)(4) citizen organization that lobbies Congress and the Administration on tax competition, limited government, financial privacy and fiscal sovereignty.

I also coordinate the activities of the Coalition for Tax Competition, which is made up of more than three-dozen free-market public policy organizations, including taxpayer groups, senior citizen and family organizations, civil liberties activists, and industry and business advocates.

I stand here today commenting for the third time on a proposed regulation that is not in the best interest of the United States. It has been 10 yrs, or 120 weeks, or more than 3,650 days, since the first version of this regulation was proposed by the Service.

As many of the speakers today will highlight, this version of the rule is virtually the same as the first version proposed January 17, 2000, three days before President Clinton left office.

Before I go into my remarks on the regulation, I would like to make a few very important points. At the public hearing held on July 21, 2001, 100 percent of the speakers were against the proposed regulation. At the December 5, 2002 hearing, once again every participant spoke out against the proposed rule. From looking at today's scheduled presenters, once again almost every participant will speak out against the proposed regulation.

The same is true for the written comments. In 2001, the IRS received very few positive comments. In fact, I was told that it was less than one-percent. The same is true for 2002. I recall reading through all the public comments the IRS released to one of my colleagues back then. After going through the 200-plus comments, I finally found one who sent an e-mail in support of the proposed regulation.

Now today's current proposed rule received 71 comment letters with only three in support of the regulation. An overwhelming 95% strongly opposed the regulation.

When we take in to account the strong bi-partisan opposition from at least 38 current lawmakers, the percentage of public comments against the proposed rule nears 97%.

It is hard to discount the effectiveness of the Florida Congressional Delegation letter. The letter was signed by all the Members of the delegation including all six Democratic members. I should point out that Debbie Wasserman Schultz was one of the signers and she is the chairwoman of the Democratic National Committee.

With that being said, I would like to touch on several of the key reasons why the Center for Freedom and Prosperity and the Coalition for Tax Competition oppose this misguided regulation.

First, I plan on punctuating my remarks with several comments from elected officials from the House of Representatives and the U.S. Senate. Unlike the government officials who proposed this regulation, these elected officials have to answer to the American taxpayers on a regular basis. This public hearing, and the comment period that ended in early April, are the only avenues that hard working Americans have to protest regulations proposed by un-elected government officials at the Internal Revenue Service.

Also, all of the excerpted quoted comments below can be found in the appendix of these remarks and I ask that they please be made part of the official record. Thank you.

Introduction

The following statements and comments from lawmakers, regulators and industry representatives describe how the IRS is flouting existing law and Congressional intent, that the proposed regulation will chase investment from the U.S. and harms America's competitiveness, how the IRS failed to perform a cost-benefit analysis, and the proposed rule would endanger human rights.

Proposed Regulation Flouts Existing Law and Congressional Intent. On several occasions, the U.S. Congress has examined the tax treatment of indirect foreign investment in the American economy. In every instance, the desire to attract capital has led lawmakers to decide not to tax bank deposit interest paid to nonresident aliens. Congress also has repeatedly decided not to require the reporting of this income. The proposed IRS regulation, however, seeks to overturn the outcome of this democratic process. This undermines the rule-of-law and makes a mockery of the President's effort to rein in regulatory abuses.

Letter from U.S. Senators Kay Bailey Hutchison and John Cornyn (April 7, 2011)

“Forgoing the taxation of deposit interest paid to certain global investors is a long-standing tax policy that helps attract capital investment to the United States. For generations, these investors have placed their funds in institutions in Texas and across the United States because of the safety of our banks. Another reason that many of these investors deposit funds in American institutions is the instability in their home countries.

“Unfortunately, the IRS's proposed regulation flies in the face of our nation's longstanding efforts to attract capital. According to a 2004 study from the Mercatus Center at George Mason University, a scaled-back version of REG-146097-09 would result in an outflow of at least \$88 billion in deposits from American financial

institutions. Some have reasoned that these investors would withdraw their capital out of concerns that their personal information could end up in the wrong hands, increasing the potential for threats and violence against them and their families.”

Florida Delegation to the U.S. House of Representatives (March 2, 2011)

“The regulation flagrantly violates the intent of Congress. On several occasions, lawmakers have chosen to refrain from taxing the deposit interest paid to nonresident aliens. These actions were made for the explicit purpose of attracting and keeping capital in the U.S. economy. We feel the IRS is abusing its regulatory authority and doing so in a manner that is contrary to Congressional intent and the last ninety years of legislative history.”

Letter from Posey-Meeks-Bachus-Watt and 12 other Members of Congress (May 16, 2011)

This regulation is not needed to enforce American tax law. Indeed, the IRS is using the regulatory process to overturn existing law. For 90 years Congress has sought to attract foreign capital to the US economy with attractive tax and privacy rules. The IRS now wants to disregard congressional intent solely for the purpose of providing information to foreign tax authorities.

Center for Freedom and Prosperity's *Prosperitas* Paper by Dan Mitchell, “Who Writes the Law: Congress or the IRS?” (February 2003)

“The proposed IRS rule is not only bad policy, but it also is a flagrant abuse of the regulatory process. The IRS is unilaterally seeking to change the law. This is neither the agency’s role nor its prerogative.”

Proposed Regulation Chases Foreign Investment out of the U.S. The current tax and privacy rules for foreign investors have been a huge success, attracting about one trillion dollars to U.S. financial institutions. This money helps finance car loans, home mortgages, and small business expansion in America. But if the IRS regulation is approved, foreigners will shift a substantial share of their funds to Panama, Singapore, Hong Kong, and other jurisdictions that protect the interests of investors – and therefore protect their own national interests.

Letter from Posey-Meeks-Bachus-Watt and 12 other Members of Congress (May 16, 2011)

“This misguided proposal would compel U.S. banks to put the interests of foreign tax collectors above U.S. law and before the interests of the American economy. If implemented, this regulation will drive bank deposits directly out of U.S. banks and into

financial institutions located in other countries. We believe this will put at risk our fragile economic recovery by driving foreign capital from our shores.”

Letter from Former Senator Gramm (February 19, 2003)

“[T]he ability of people to move their capital is the most effective check on excessive taxes and oppressive government. The United States of America is the world's greatest beneficiary of such capital movements. Why would we ever want to limit economic freedom and protect over-taxing governments around the world? ...The benefits, if any, of the IRS proposal are so overwhelmed by the dangers it poses as to make its adoption unthinkable.”

Federal Deposit Insurance Corporation (FDIC) (January 2, 2003)

“Bankers have reported that as much as \$1 trillion in U.S. bank deposits derive from foreign nationals. A shift of even a modest portion of these funds out of the U.S. banking system would certainly be termed a significant economic impact.”

Proposed Regulation Hurts America’s Competitiveness. Financial institutions from around the world compete for liquid capital. American banks traditionally have been successful in this environment, attracting about one trillion dollars. But this profitable source of deposits will become very unstable if banks are forced to put foreign tax law above U.S. tax law. Money will flow out of America, making it more difficult for U.S. banks to meet the challenge of foreign competition and also limit ability to loan funds to small businesses, families and farmers. Also, the added cost of collecting and delivering the information will be another barrier to competing.

Florida Delegation to the U.S. House of Representatives (March 2, 2011)

“The regulation will negatively affect the solvency of financial institutions. Should this regulation take effect it will have a negative impact on the balance sheets of U.S. financial institutions and the solvency of those that have a high percentage of non-resident alien deposits may erode. At a time when federal policies should be aimed at enhancing solvency, this regulation would undermine that goal.

“This proposal may be good news for high-tax governments, but it is contrary to American economic interest. The jobs of American workers and the competitiveness of U.S. companies should be our top priorities. This regulation works against both. It will put Americans out of work and it will force dollars out of U.S. financial institutions and into foreign financial institutions.”

Letter from Senator Marco Rubio (April 4, 2011)

“At a time when unemployment remains high and economic growth is lagging, forcing banks to report interest paid to nonresident aliens would encourage the flight of capital overseas to jurisdictions without onerous reporting requirements, place unnecessary burdens on the American economy, put our financial system at a fundamental competitive disadvantage, and would restrict access to capital when our economy can least afford it”

Small Business Administration: Office of Advocacy (November 14, 2002)

“For a small financial institution, the burden associated with setting up a system to monitor and report in accordance with the regulation is a significant burden. It would include the cost of equipment, software and set-up, plus the ongoing costs of operation, maintenance, and/or purchases of services to provide this information. A small financial institution has a smaller customer base over which to defray these costs.”

“...If this regulation is imposed, it will create a barrier to small financial institutions’ ability to compete.”

“[W]e believe that there is ample evidence that the impact of the regulation is significant and that a substantial number of small businesses will be impacted. “

The required cost-benefit analysis was not performed. The IRS is ignoring laws requiring cost-benefit analysis of proposed regulations. It has effectively exempted itself from regulatory oversight by incorrectly declaring most of its regulations either "interpretative" within the meaning of the Administrative Procedure Act or not "major" within the meaning of Executive Order 12866. Yet many IRS regulations impose significant economic costs and should be subject to regulatory review.

The proposed regulation endangers human rights. Innocent people seeking to protect themselves and their assets from tyrannical, corrupt, and venal governments will be thwarted by this regulation. The unfortunate reality is that most of the world still lives in countries where there is persecution based on ethnic, racial, religious, economic and political characteristics. Sharing private financial information about U.S. bank deposits with thugs such as Venezuela’s Hugo Chavez should not be the objective of the U.S. government.

Florida Delegation to the U.S. House of Representatives (March 2, 2011)

“Many nonresident alien depositors are from countries with unstable governments or political environments, where personal security is a major concern. They are concerned that their personal bank account information could be leaked by unauthorized persons in their home country governments to criminal or terrorists groups upon receipt from U.S.

authorities, which could result in kidnappings or other terrorist actions being taken against them and their family members in their home countries, a scary scenario that is very real.”

Conclusion

This is now the third time that the IRS has gotten a bite at this particular apple, and once again both Congress and the public are staunchly opposed. For the reasons I have outlined, I ask that the regulation be withdrawn.

Appendix

Letter from Former Senator Gramm (February 19, 2003)

<http://archive.freedomandprosperity.org/ltr/gramm-irs/gramm-irs.shtml>

Small Business Administration: Office of Advocacy (November 14, 2002)

http://archive.sba.gov/advo/laws/comments/irs02_1114.html

Federal Deposit Insurance Corporation (FDIC) (January 2, 2003)

<http://archive.freedomandprosperity.org/fdic.pdf>

Florida Delegation to the U.S. House of Representatives (March 2, 2011)

<http://posey.house.gov/UploadedFiles/IRS-DelegationLetter-March3-2011.pdf>

Letter from U.S. Senators Kay Bailey Hutchison and John Cornyn (April 7, 2011)

http://freedomandprosperity.org/files/NRAreg/TX_Senators.pdf

Letter from Senator Marco Rubio (April 4, 2011)

http://www.floridabankersassociation.com/docs/links/IRS_NRA_Rubio.pdf

Letter from Posey-Meeke-Bachus-Watt and 12 other Members of Congress (May 16, 2011)

http://freedomandprosperity.org/files/NRAreg/NRA_Letter_to_Geithner_and_Shulman.pdf

Letter from the Coalition for Tax Competition (April 7, 2011)

<http://freedomandprosperity.org/files/NRAreg/CTCltr.pdf>

Letter from Andrew Quinlan, President, Center for Freedom and Prosperity (April 7, 2011)

<http://freedomandprosperity.org/files/NRAreg/CFPletter.pdf>

Prosperitas Paper by Dan Mitchell, Center for Freedom and Prosperity, “Who Writes the Law: Congress or the IRS?” (February 2003)

<http://freedomandprosperity.org/2003/publications/who-writes-the-law-congress-or-the-irs/>