

FATCA...More Fear-Mongering

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We want a nickel for every time we've heard the question: "Aren't you worried that on July 1, when FATCA goes into effect, the dollar and financial system will collapse as a cascade of money leaves the US? FATCA stands for the Foreign Account Tax Compliance Act, and it's the latest, greatest reason to believe the world is coming to an end.

Supposedly, successful billionaire investors know all about this and are quietly moving all their money into gold and obscure foreign currencies. According to breathless advertisements, you should follow the "smart money" because the US stock market is about to collapse.

It's the latest in a never-ending stream of politically-based, fear-mongering during this, now, five-year bull market.

Remember Dubai, the theory that financial problems in a small kingdom halfway around the world were going to unravel the world economy? How about the coming collapse of commercial real estate? Remember the debt limit debate, or the inevitable collapse of the Euro and the return of the Drachma? The government shutdown...the Fiscal Cliff...tapering?

The real truth about all these scare stories, was that none of them were based on economic fundamentals, and, those that acted on them have paid a large price. They almost seem mythological in their source...the Gods are mad and will rain fire down any minute. Through them all, the US economy and equity markets kept marching to new highs.

Needless to say, we expect that to happen again.

FATCA (enacted in 2010) requires US investors to report all foreign accounts to the IRS, and requires foreign financial institutions to report the accounts of US clients. To help enforce the rules, if a US investor wants to transfer money outside the US, to an institution that doesn't comply with IRS rules, the firm making the transfer has to withhold 30% of the money until the IRS confirms that there is no US tax due.

This law exists because of the way the IRS treats US citizens for tax purposes. First, unlike most countries, the US taxes its citizens on all the money they make all over the world, even if every bit of it is earned outside the US. (By contrast, most other countries have a territorial system, which only taxes citizens on earnings they make domestically.) Second, the US double taxes corporate profits, once when the company earns the money and then again when the money is distributed.

In spite of these laws, some US investors have attempted to avoid these taxes by using secret or obscured foreign accounts, basically keeping money overseas, like many corporations do. At the margin, and compared to GDP, the amount of money involved in this activity is relatively small. But the IRS has worked hard to stop it. That's what FATCA is about. The government wants to make sure US taxpayers are complying with the law. It may smack of big brother to some, but it's not capital controls.

Investors can still move their money freely in and out of banks all over the world as long as these institutions report to the IRS so the US government can collect what it thinks it's owed. Want to buy a stock on the Russian market? You can still do that. Want to buy a Greek bond? You can do that, too. But the IRS is determined to measure how much you earn and tax it according to the law.

In certain ways, the new rule resembles what happens when you take money out of an IRA. The IRS requires IRA custodians to withhold 10% of taxable withdrawals, unless the beneficiary fills out paperwork so the IRS can figure out who to tax. Again, it's about tax compliance, not capital controls.

Those spreading the doom and gloom FATCA story have been fear-mongering for months. Now, July 1 is only 15 days away. Don't be surprised when the same pessimists start peddling a new scare story on July 2.

Date/Time (CST)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
6-16 / 7:30 am	Empire State Mfg Survey – Jun	15.0	16.3	19.3	19.0
8:15 am	Industrial Production – May	+0.5%	+0.5%	+0.6%	-0.6%
8:15 am	Capacity Utilization – May	78.9%	78.9%	79.1%	78.6%
6-17 / 7:30 am	CPI – May	+0.2%	+0.2%		+0.3%
7:30 am	"Core" CPI – May	+0.2%	+0.1%		+0.2%
7:30 am	Housing Starts – May	1.030 Mil	1.005 Mil		1.072 Mil
6-19 / 7:30 am	Initial Claims – June 14	313K	314K		317K
9:00 am	Leading Indicators – May	+0.6%	+0.6%		+0.4%
9:00 am	Philly Fed Survey – Jun	14.0	16.5		15.4