

The Washington Times

www.washingtontimes.com

Regulatory malpractice

By Richard W. Rahn

Published March 18, 2004

In today's parlance, George Washington was a victim of medical malpractice. When he became ill, he was bled by his doctors, which almost certainly hastened his death. Like Washington, the financial industry and its customers are now slowly being bled, which will be fatal for some.

The "doctors" in this case are a group of politicians, tax and law enforcement officials, who are operating without the constraint of national boundaries or economic sense.

People around the globe are justifiably concerned about terrorism and ordinary criminality. A certain international political class has used this anxiety to argue that since criminals and terrorists use money, all monetary movements and holdings must be monitored. Yes, it is useful to be able to trace the money trail of al Qaeda operatives. But does that mean all citizens of every country should be subject to having all their financial privacy destroyed? Furthermore, is it cost-effective to monitor almost everyone, or would both public and private law enforcement dollars be more wisely spent monitoring the activities of those individuals or groups known or strongly suspected of engaging in terrorist or criminal activities?

The problem is there are now literally dozens of organizations issuing rules and regulations that apply not only to financial institutions but to all "money service providers," including such activities as pawn shops, used car dealers and real estate agents. The agencies within the U.S. government issuing the new financial rules and regulations include the Internal Revenue Service, the FBI, the Justice Department, the Financial Crimes Enforcement Network (FinCen) and the Federal Reserve.

In addition, U.S. financial institutions and other businesses engaged in operations outside the U.S. or those involved in international transactions are also faced with a barrage of new rules and regulations from many foreign governments, plus the European Union, and from international institutions such as the Organization for Economic Cooperation and Development (OECD), the Financial Action Task Force (FATF) and the U.N.

Millions of businesses are subject to at least some of these rules and regulations, and it is close to impossible to inform them of their obligations. Even the largest international banks, with huge staffs of lawyers and anticrime enforcement personnel, are unable to fully work through this ever-expanding morass of regulation.

Smaller banks and businesses are at a competitive disadvantage because of the disproportionate effect of these regulatory costs. Some of the regulators are aiming at terrorists, others at ordinary criminals, and some at tax avoiders or evaders. Most of the regulations are directed at "money launderers," even though the term has a very elastic definition.

Many of these new rules and regulations are overlapping, some are contradictory, some violate basic civil liberties and many are costly to administer and do not meet reasonable cost-benefit tests. Yet the Bush administration just announced a doubling in the budget for FinCen, as well as budget increases for many of the other financial rulemaking bodies.

The reason we should care is that all of these extra, and in many cases totally unnecessary, costs are passed along to consumers of financial services as higher fees and more expensive and fewer choices in financial products. This directly translates into job losses not only in financial industries but in all businesses that rely on some outside financing.

In addition, it will make it more difficult for low-income people, the young and recent immigrants to open bank accounts. We are now seeing, for the first time in our nation's history, a rise in the portion of our citizens without banking relationships. Costly regulations that force more people into the cash economy not only make life more dangerous for those who cannot open bank accounts, but also have the perverse effect of making it more difficult for law enforcement to trace funds of criminals.

There is little evidence all the new rules and paperwork are having any appreciable effect on crime or terrorism, because there is an almost infinite number of ways to "launder" money, and organized terrorists and criminals can almost always find ways around the regulations. On the other hand, there is considerable evidence of damage to our pocketbooks and civil liberties from these regulations.

The U.S. government should expand the jurisdiction of the "Office of Information and Regulatory Affairs" (OIRA) to include the IRS and the other financial and law enforcement agencies that issue financial regulations, and insist financial regulations meet strict cost-benefit and civil liberties' tests.

In addition, an international organization is needed to apply the same strict cost-benefit and civil liberties' tests to all proposed regulations emanating from international bodies like the OECD, FATF, and the U.N., as well as those from governments that affect nonresident institutions.

If financial institutions and their customers are weakened or bled to death by regulatory malpractice, the war against real criminals and terrorists will only be made more difficult.

Richard W. Rahn is a senior fellow of the Discovery Institute and an adjunct scholar of the Cato Institute.