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HEADLINE: 2015 TNT 192-2 NEWS ANALYSIS: WHAT COMES AFTER THE SWISS BANK PROGRAM IN ENFORCEMENT?. (Section 1471 -- Foreign Financial Institution Withholding) (Release Date: OCTOBER 01, 2015) (Doc 2015-21978)

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ABSTRACT: In news analysis, Marie Sapirie discusses what the IRS and the Justice Department may plan to do next in their efforts to bring U.S. taxpayers into compliance regarding their foreign bank accounts.

SUMMARY:

Published by Tax Analysts(R)

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In the seven years since the United States obtained a John Doe summons in its investigation of UBS AG, the government has compiled an impressive resume in its efforts to bring taxpayers into compliance regarding their foreign bank accounts: further litigation, three voluntary disclosure programs, the implementation of the Foreign Account Tax Compliance Act, and the Swiss bank program. Although much has been accomplished, more remains to be done, both to find other accounts and to take advantage of the information the government already has.

"The government has more tools and more information at their disposal than ever before," said

Jeffrey Neiman of Marcus Neiman & Rashbaum LLP. "They are at the cusp of really breaking through and making it almost impossible for Americans to hide money outside of the U.S."

The UBS investigation and subsequent deferred prosecution agreement established the roadmap for the enforcement campaign that followed. The Justice Department and the IRS have made extensive use of John Doe summonses -- and the information gained from them -- in pursuing new leads. Most recently, the IRS filed a petition (Doc 2015-21004) on September 15 for leave to serve a John Doe summons on Citibank NA and Bank of America NA for correspondent account information related to Belize Bank International Ltd., Belize Bank Ltd., or Belize Corporate Services. According to the memorandum the government filed in support of its summons, the IRS learned through interviews, voluntary disclosures, and records of criminal prosecutions that U.S. taxpayers used these Belizean entities to set up and maintain undisclosed accounts.

As indicated in the government's petition, the IRS's voluntary disclosure programs complement the litigation model that the Justice Department has honed since 2008 and have yielded information critical to expanding enforcement efforts beyond Switzerland. The voluntary disclosure programs have evolved substantially since the first iteration announced in March 2009, and the process has not always been smooth, either for the government or for taxpayers. The programs increased compliance but hit notable snags with issues such as passive foreign investment companies, non-willful violations, and some retirement accounts. (Prior coverage: *Tax Notes*, Aug. 16, 2010, p. 702 (Doc 2010-17826).) The penalty structure of the disclosure programs -- especially the rapid escalation of the base miscellaneous penalty amount from 20 percent to 25 percent to 27.5 percent -- remains one of the biggest obstacles to bringing taxpayers into compliance. "They set the numbers so high, they didn't have much room to go before they outpriced themselves," said Neiman. He said that ideally, the penalty would be based on objective factors, including whether the money was supposed to be taxed in the United States and if a nominee company was involved. Neiman said the IRS has listened to practitioners regarding potential changes to the voluntary disclosure program that would make compliance easier.

Although the government has had significant success combating bank secrecy, uncovering additional account information has been more challenging than might have been anticipated following the UBS litigation. "That was the last time they got bulk files from any bank," said Edward M. Robbins Jr. of Hochman, Salkin, Rettig, Toscher & Perez PC. The new information is primarily statistical data that does not have specific taxpayer names associated with it. To obtain information for prosecutions, the IRS must select accounts from among the data to send through the treaty process. At least in Switzerland, that process seems to be moving along fairly rapidly.

The next geographic frontier for international enforcement is likely to be Asia. Practitioners report that account holders in Asia make up a far smaller percentage of voluntary disclosures than would be expected given the distribution of American citizens worldwide. As a matter of parity, the government needs to finish the job it began with UBS in Switzerland. "They can't stop. They have to go deal with the west-of-the-dateline countries because that is where 70 percent of untapped bank account holders are doing their business," said Robbins.

The Swiss Bank Program as a Model?

Over two years ago, the Justice Department announced the Swiss bank program as a path for Swiss banks to resolve potential criminal violations in the United States. Nearly half of the expected number of banks have signed non-prosecution agreements (NPAs), and the rest of the category 2 banks -- banks that seek to enter into an NPA -- are expected to conclude agreements by the end of the year.

The program is available only to banks that are not under criminal investigation. Banks that enter the program must release detailed information about their U.S. account holders, and the penalty structure ranges from 20 to 50 percent of the maximum aggregate dollar value of undisclosed U.S. accounts, depending on when the accounts were opened.

Neiman said the "one big, glaring question" about the Swiss bank program is what will happen to all the category 1 institutions. Category 1 banks are banks for which the Justice Department had authorized a formal criminal investigation as of the announcement of the Swiss bank program. That threat of prosecution drove many other banks into the Swiss bank program as category 2 banks. If the category 1 banks remain in a holding pattern with cases unfinished, the threat of prosecution may diminish, and other institutions and taxpayers may become more reluctant to enter into future programs.

Although there is no indication that it will be expanded to reach other jurisdictions, the Swiss bank program could serve as a model for future compliance programs directed at institutions. The limited regional scope of the enforcement efforts to date leaves open the possibility -- and likely creates the necessity -- for further enforcement. Most of the 52 institutions on the IRS's published list of foreign financial institutions or facilitators are European. Most of the list consists of the 39 banks that have signed NPAs under the Swiss bank program. Of the banks on the list, only HSBC India is headquartered in Asia, four are headquartered in the Caribbean and Bermuda, and one is headquartered in Israel. "The government has a lot of experience now with how to go about launching one of these programs. They can pick the best pieces of what they've done and come up with new ideas," said Robbins.

Designing an expanded, possibly worldwide, program might not require the same expenditure of government resources that the Swiss bank program has. "If the government took steps to provide as much certainty as they could, other banks in other jurisdictions would be more willing to come forward," said Neiman. A program with a set scope, such as one that covers specific years, requires information on accounts that fit a prescribed fact pattern, and calculates fines in a specified way, would encourage many banks around the world to come in, he said.

The impending conclusion of the Swiss bank program means the government will soon be able to devote those resources to addressing noncompliance in other areas. "Clearly, the IRS and DOJ are starting to refocus some of their efforts outside of Switzerland to other countries," said Dennis N. Brager of the Brager Tax Law Group. He said he does not foresee a major change in the government's approach. "The IRS is totally underfunded. They can't go after the majority of individuals who have offshore accounts, so what I suspect is that the IRS will continue to deal fairly harshly with those persons it does catch to make an example of them to encourage voluntary compliance from others," he said.

Impact of FATCA

Enforcement got an added jolt in 2014 with the launch of on-boarding procedures under FATCA for new accounts at FFIs and the requirement of due diligence on preexisting account holders. The new reporting and withholding paradigm is at least partially responsible for bringing some taxpayers back into compliance, even as it prompts some foreign institutions to jettison American account holders. The first list of registered FFIs included more than 77,000 entities. These developments contribute to enforcement efforts by exposing additional account holders to U.S. reporting requirements. But they may drive others deeper underground. Brager said some taxpayers may have opened their accounts under non-U.S. passports and used non-U.S. addresses, which could make them harder to find.

FATCA significantly broadened the impact of the enforcement drive against undisclosed Swiss bank accounts, said Neiman. It is informing account holders of worldwide reporting requirements that they were likely unaware of, and many of them want to know how to comply, he said, adding that they might be able to come into compliance at a relatively low cost with the streamlined procedures for non-willful taxpayers.

The Lessons of History

The past few decades show that when the IRS's enforcement budget is reduced, noncompliance

becomes a larger problem. That trend is worrisome because the IRS's current resource allocation for enforcement is inadequate. The abusive tax shelters of the 1990s coincided with a drop-off in enforcement because of resource constraints. The shelter shutdown effort was prompted by information from tax practitioners rather than whistleblowers, but as in the international enforcement efforts, the government used disclosures and summonses to detect noncompliance.

International cooperation became an increasingly critical component of enforcement in the wake of the abusive tax shelter schemes, and the offshore account compliance efforts reinforced the importance of the U.S. treaty and tax information exchange agreement network as well as other formal channels for obtaining information, such as the Joint International Tax Shelter Information Centre (JITSIC). JITSIC was formed in 2004 to address tax shelters, and in 2014 the reinvigorated JITSIC Network held its first meeting to work on a framework for multilateral projects to address cross-border tax avoidance and profit shifting. Further collaboration between jurisdictions is likely.

Budget cuts do not necessarily mean that enforcement will suffer, however. "The government has never been able to go everywhere with calculated enforcement, but they can police everywhere they need to be without being on every street corner of every banking capital of the world," said Neiman. He noted that the Justice Department Tax Division's budget was not reduced and that the division has recently hired new attorneys.

The next phase of the government's enforcement efforts for noncompliant offshore accounts will likely involve a change in regional focus as the government finishes the job it began with UBS. But what will the next target be after undeclared accounts? That remains an open question.