

## NEWS ANALYSIS

**Switzerland, Guantanamo, and Tax Evasion**

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The official line is that the Justice Department won't drop its case against Swiss banking giant UBS. But that's not what *The New York Times* is reporting. My hope is that Justice will stick to its guns. But my gut tells me the *Times* will turn out to be right.

It makes so much political sense to appease the Swiss. The Swiss government announced in January that it would be willing to take some Guantanamo prisoners off U.S. hands — providing much-needed relief for one of the superpower's biggest foreign policy headaches. The United States calls on Switzerland to represent it in countries such as Iran where the United States has no diplomatic presence. In this economic crisis and in coming years, good relations with the Swiss will be essential for multilateral actions to promote financial stability. And the Swiss are willing to sign a revised tax treaty with the United States that would make it easier to catch U.S. tax cheats hiding money in Swiss banks.

***Dropping the UBS case would be a huge setback to the Obama administration's efforts to combat offshore tax evasion.***

But dropping the UBS case would be a huge setback to the Obama administration's efforts to combat offshore tax evasion. It would, in essence, be a return to the old status quo: Tax havens will help the United States catch tax evaders only when the United States already knows identity. In the grand scheme of things, that's not much help at all.

The John Doe summons at issue requires UBS — which got caught red-handed aiding and abetting U.S. tax evaders — to reveal the identities of an estimated 52,000 UBS customers who are U.S. citizens. (The IRS did not even withdraw UBS's privilege of participating in the qualified intermediary program, which keeps U.S. withholding taxes low on account holders.)

If UBS officials comply with the summons they would violate Swiss law. Compliance would violate Switzerland's sacrosanct commitment to banking privacy. It's a big deal in Switzerland, and the country's largest political party, the right-wing

Swiss People's Party, wants to retaliate against the United States for the UBS probe.

A John Doe summons is a court-enforced equivalent of an automatic information exchange agreement. Under automatic information exchange, nation A provides information to nation B about nation B citizens with accounts in nation A banks. Until recently this type of exchange was rare, but members of the European Union are now doing it routinely. In the community of tax havens, automatic information exchanges are disparagingly labeled "fishing expeditions."

Although most people — including our own treaty negotiators at the Treasury Department — consider automatic information exchange with tax havens a diplomatic impossibility, it is ultimately the only policy that really can put a stop to cross-border evasion. You don't have to be an international tax expert to understand why.

Every year, every U.S. bank reports information on accounts held by every U.S. taxpayer to the IRS. And so compliance for domestic accounts is nearly perfect. For U.S. citizens who put their money in offshore banks, investment accounts, or hedge funds, there is no reporting to the IRS. The IRS depends on the taxpayer to voluntarily reveal the existence of offshore accounts. Guess what? Compliance is very low.

Now, at this point, apologists for tax evaders and tax havens start to rant about privacy. Privacy is nice. But let's just say two things. First, if by some miracle the IRS does obtain information about offshore accounts held by U.S. citizens, it won't broadcast it over the airwaves. It would be covered by the same severe restrictions on disclosure of taxpayer information that applies to all domestically obtained information. Second, if privacy is so paramount in importance, why are we enabling it only in offshore jurisdictions? Should we repeal information reporting requirements for domestic banks?

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All the jabbering you are now hearing about newly negotiated tax information exchange agreements is really just a lot of show with little substance. The renegotiated Swiss-U.S. protocol is a perfect example. The Swiss, in what they want to characterize as an enormous concession, will now allow the United States to request information about U.S. tax evaders who not only commit tax fraud but also tax evasion.

The distinction between fraud and evasion is an artificial construction from Swiss law. Fraud is

when you actively engage in a tax evasion scheme. It does not include lying on your tax return. Until now, the Swiss would not cooperate in cases in which individuals simply did not report their Swiss accounts.

Under the pending protocol, that would change. All tax evasion — fraudulent or not — would be cause enough to allow information exchange. That would bring the Swiss into alignment with information exchange agreements that conform to the wimpy OECD model tax convention. No big deal — except for the Swiss. It is still miles short of effective, full-blown information exchange.

The havens want to give the appearance of cooperation. And the IRS and other tax collectors don't mind leaving the impression that offshore tax evasion has gotten a lot tougher. But the critical fact remains that all these agreements provide only for information exchange on demand. Information exchange on demand means that the inquiring nation must know the identity of the suspected evader and show probable cause for the suspicion. Also, the inquiring government must in practice go through cumbersome, costly, and timely procedures to be granted access to the requested information in each case.

So only a few of those requests are processed each year, and those are often in cases in which nontax crimes are the primary issue. In other words, unless you are a drug dealer or a terrorist, or unless you are already under investigation by the IRS for tax evasion, your chances of getting caught are very low . . . unless.

Unless there is automatic information exchange of the type the federal court in Miami is threatening to compel from UBS. That's why it is reported that scores of wealthy U.S. individuals are voluntarily coming forward to avoid possible criminal prosecution if UBS does disclose.

Taxes are not everything. There may be good political and diplomatic reasons for appeasing the Swiss. But President Obama and Attorney General Eric Holder should understand that by vigorously pursuing the revelation of wealthy U.S. tax evaders using Swiss bank accounts, they have a unique opportunity to deal a serious blow to offshore tax evasion. By dropping the case, they would be giving it all away. And no matter how much they would argue to the contrary, they would be seriously backtracking on their oft-stated intention to crack down on tax haven abuse.

It is hard to believe that on the UBS issue, the Obama administration would retreat where the Bush administration bravely chose to fight. ■