

**Mutual Agreement of January 23, 2003,  
Regarding the Administration of Article 26 (Exchange of Information)  
of the Swiss-U.S. Income Tax Convention of October 2, 1996**

Whereas Article 26 (Exchange of Information) of the Convention between the United States of America and the Swiss Confederation for the Avoidance of Double Taxation with Respect to Taxes on Income, signed at Washington on October 2, 1996, ("the Convention"), provides that the competent authorities of the Contracting States shall exchange such information as is necessary "for the prevention of tax fraud or the like in relation to the taxes which are the subject of" the Convention;

Whereas paragraph 10 of the Protocol accompanying and forming an integral part of the Convention ("the Protocol") provides that "tax fraud" means "fraudulent conduct that causes or is intended to cause an illegal and substantial reduction in the amount of tax paid to a Contracting State," and provides illustrative descriptions of situations in which fraudulent conduct is assumed;

Whereas the Contracting States have memorialized certain understandings with respect to Article 26 of the Convention;

Whereas the competent authorities of the Contracting States have had several years of experience in implementing and administering the Convention, including the information exchange provisions thereof;

Whereas the exchange of information for the prevention of tax fraud or the like under Article 26 of the Convention is very important to the adequate administration and enforcement of the tax laws of each Contracting State;

Now, therefore, the competent authorities of the Contracting States wish to memorialize the following additional understandings in reference to Article 26 of the Convention and paragraph 10 of the Protocol:

1. It is understood that Article 26 of the Convention and paragraph 10 of the Protocol will be interpreted to support the tax administration and enforcement efforts of each Contracting State to the greatest extent possible.
2. It is understood that, in determining whether information may be provided in response to a request, the requested State shall apply the statute of limitations applicable under the laws of the requesting State instead of the statute of limitations of the requested State.
3. It is understood that, in response to a request, the requested State shall exchange information with respect to matters that the requesting State is pursuing, or may pursue, on a civil or criminal basis.
4. It is understood that the following conduct constitutes "tax fraud or the like" under paragraph 1 of Article 26 of the Convention, which is also illustrated in paragraph 10 of the Protocol:
  - a) Conduct that is established to defraud individuals or companies, even though the aim of the behavior may not be to commit tax fraud;
  - b) Conduct that involves the destruction or non-production of records, or the failure to prepare or maintain correct and complete records, that a person is under a legal duty (tax or otherwise) to prepare and keep as sufficient to establish the amount of gross income, deductions, credits, or other matters required to be shown by such person in any tax return, if the person has not properly reported such amounts in any such tax return; or
  - c) Conduct by a person subject to tax in the requesting State that involves the failure to file a tax return that such person is under a legal duty to file and an affirmative act that

has the effect of deceiving the tax authorities making it difficult to uncover or pursue the failure to file, including the concealment of assets or covering up of sources of income or the handling of one's affairs to avoid making the records that are usual in transactions of the kind.

It is understood that these examples are by way of illustration, and not by way of limitation.

5. It is understood that, in response to a request, the requested State shall exchange information where the requesting State has a reasonable suspicion that the conduct would constitute tax fraud or the like. The requesting State's suspicion of tax fraud or the like may be based on:

- a) Documents, whether authenticated or not, and including but not limited to business records, books of account, or bank account information;
- b) Testimonial information from the taxpayer;
- c) Information obtained from an informant or other third person that has been independently corroborated or otherwise is likely to be credible; or
- d) Circumstantial evidence.

It is understood that these examples are by way of illustration, and not by way of limitation.

6. It is understood that each of the hypothetical examples in the Appendix below involves conduct constituting "tax fraud or the like" under paragraph 1 of Article 26 of the Convention and paragraph 10 of the Protocol. It is understood that these examples are by way of illustration, and not by way of limitation.

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## **Appendix**

### **HYPOTHETICAL 1**

An individual subject to the requesting State's income tax operates a business with substantial cash sales. He keeps one set of books and records in which he records all business expenses; however, he causes a substantial portion of the cash sales of the business to be omitted from this set of books. The individual keeps a second set of books and records that includes the total amount of cash sales, including the cash sales not recorded on the first set of books and records. Because the first set of business books and records are used to prepare the individual's income tax return, a substantial portion of his taxable income is not reported on the tax return. Specifically, the individual's income tax return, and the component to that return on which the individual reports business receipts, expenses, and other items related to the business, understates the gross business receipts and other income related entries.

The individual maintains a bank account in the requested State in his own name into which he deposits the portion of his business income that is not reported on his tax return. Based on information provided by an informant, including a copy of the second set of books and records that the informant secretively took from the business premises, tax officials of the requesting State commence an investigation of the individual for possible tax violations under the laws of the requesting State. The taxpayer provides the first set of books and records to these officials to support the false information on his tax return.

The requested State would obtain and provide information relating to the bank account in the requested State of the individual in response to a specific request by the requesting State under Article 26 of the Convention.

### **HYPOTHETICAL 2**

An individual subject to the requesting State's income tax operates a business with substantial cash sales. He keeps one set of books and records in which he records all business expenses; however, he causes a substantial portion of the cash sales of the business to be omitted from this set of books. The individual keeps a second set of books and records that includes the total amount of cash sales, including the cash sales not recorded on the first set of books and records. Because the first set of business books and records are used to prepare the individual's income tax return, a substantial portion of his taxable income is not reported on the tax return. Specifically, the individual's income tax return, and the component to that return on which the individual reports business receipts, expenses, and other items related to the business, understates the gross business receipts and other income related entries.

The individual maintains a bank account in the requested State in his own name into which he deposits the portion of his business income that is not reported on his tax return. Based on information provided by an informant, authorities of the requesting State conduct a search of the business premises and seize both sets of books and records.

The requested State would obtain and provide information relating to the bank account in the requested State of the individual in response to a specific request by the requesting State under Article 26 of the Convention.

### **HYPOTHETICAL 3**

An individual subject to the requesting State's income tax operates a business which provides a service on a "cash only" basis. He regularly skims a substantial portion of these cash receipts and

deposits these skimmed receipts in a bank account in the requested State maintained in his own name. He deposits the remainder of his cash receipts in a bank account in the requesting State maintained in his business name. He pays his business expenses by drafting checks against the bank account in the requesting State.

He files an income tax return, understating his gross income, taxable income, and tax due, to the extent that he skimmed from his business receipts. Specifically, the individual's income tax return, and the component to that return on which the individual reports business receipts, expenses, and other items related to the business, understates the gross business receipts and other income related entries.

An informant tells the tax officials of the requesting State about the business, including the skimming activities, and the bank account in the requested State, specifically stating that the individual told him that he skimmed no less than 30 per cent of his gross receipts every week and deposited these skimmed receipts in an account under his name in the X Bank located in the requested State. Based on this information tax officials of the requesting State commence an investigation of the individual for possible tax violations under the laws of the requesting State. In response to a request by the tax officials of the requesting State for substantiation of the tax return, the individual provides incomplete books and records that omit the skimmed receipts and therefore support the tax return.

The requested State would obtain and provide information relating to the bank account in the requested State of the individual in response to a specific request by the requesting State under Article 26 of the Convention.

#### HYPOTHETICAL 4

An individual subject to the requesting State's income tax operates a business which provides a service on a "cash only" basis. He regularly skims a substantial portion of these cash receipts and deposits these skimmed receipts in a bank account in the requested State maintained in his own name. He deposits the remainder of his cash receipts in a bank account in the requesting State maintained in his business name. He pays his business expenses by drafting checks against the bank account in the requesting State.

He files an income tax return, understating his gross income, taxable income, and tax due, to the extent that he skimmed from his business receipts. Specifically, the individual's income tax return, and the component to that return on which the individual reports business receipts, expenses, and other items related to the business, understates the gross business receipts and other income related entries.

A former employee of the business tells the tax officials of the requesting State about the business, including the skimming activities, and the bank account in the requested State, specifically stating that the individual told him that he skimmed no less than 30 per cent of his gross receipts every week and deposited these skimmed receipts in an account under his name in the X Bank located in the requested State. Based on this information tax officials of the requesting State commence an investigation of the individual for possible tax violations under the laws of the requesting State. In response to a request by the tax officials of the requesting State for the required substantiation of the tax return, the individual does not provide any books and records.

The requested State would obtain and provide information relating to the bank account in the requested State of the individual in response to a specific request by the requesting State under Article 26 of the Convention.

## HYPOTHETICAL 5

An individual subject to the requesting State's income tax operates a business which provides a service on a "cash only" basis. He regularly skims a substantial portion of these cash receipts and deposits these skimmed receipts in a bank account in the requested State maintained in his own name. He deposits the remainder of his cash receipts in a bank account in the requesting State maintained in his business name. He pays his business expenses by drafting checks against the latter bank account. He keeps no record of business receipts or expenses other than his bank account records in the requesting and requested State.

He files an income tax return, understating his gross income, taxable income, and tax due, to the extent that he skimmed from his business receipts. Specifically, the individual's income tax return, and the component to that return on which the individual reports business receipts, expenses, and other items related to the business, understates the gross business receipts and other income related entries.

An informant tells tax officials of the requesting State about the business, including the skimming activities, and the bank account in the requested State, specifically stating that the individual told him that he skimmed no less than 30 per cent of his gross receipts every week and deposited these skimmed receipts in an account under his name in the X Bank located in the requested State. The informant also tells tax officials of the requesting State that the individual has used proceeds from the bank account in the requested State to purchase assets, formal legal ownership of which has been placed in the names of other persons.

Based on this information tax officials of the requesting State commence an investigation of the individual. Among other things, these officials learn that the individual used cash to buy particular assets, and has with documentation placed legal ownership to these assets in the name of other persons. These officials observe that these assets are always used by the individual.

The requested State would obtain and provide information relating to the bank account in the requested State of the individual in response to a specific request by the requesting State under Article 26 of the Convention.

## HYPOTHETICAL 6

An individual subject to the requesting State's income tax operates a business. Although the business functions primarily within the territory of the requesting State, it does have some international sales. The individual forms a bearer share corporation in a third country and confidentially maintains possession of all the shares. The corporation maintains a bank account in the requested State in the corporate name with the individual as the sole authorized signature authority. The business enters into a contract with the corporation under which the corporation agrees to perform "market research." No market research is performed. The business pays substantial fees for this service which are deposited into the bank account in the requested State. The business records the fees as expenses on the business books and records. As a result, business income is substantially reduced. Because the business books and records are used to prepare the individual's income tax return, his reported gross income, taxable income, and tax due are substantially understated. Specifically, the individual's income tax return, and the component to that return on which the individual reports business receipts, expenses, and other items related to the business, understates the gross business receipts and other income related entries.

Tax officials of the requesting State randomly select the individual for a tax audit. When these officials observe that substantial payments were made to a foreign corporation and claimed as business expenses on the individual's tax return, these officials ask the individual whether he or someone else owns the foreign corporation. The individual denies any ownership interest in the

foreign corporation and claims that it is owned by a third party who has actually conducted market research for the business. Tax officials of the requesting State then initiate an investigation of the individual. Subsequently, an ex-spouse tells these officials that the individual maintains a bank account in the requested State under the name of the foreign corporation and that the payments to the corporation for market research were deposited in this bank account.

The requested State would obtain and provide information relating to the bank account in the requested State of the foreign corporation in response to a specific request by the requesting State under Article 26 of the Convention.

#### HYPOTHETICAL 7

An individual controls a corporation that is subject to the requesting State's income tax and that operates a business which provides a service on a "cash only" basis. The individual regularly skims a substantial portion of these cash receipts and deposits these skimmed receipts in a bank account in the requested State maintained in his own name. The remainder of the cash receipts are deposited in a bank account in the requesting State maintained in the corporation's name. The corporation pays its business expenses with checks drafted against this latter bank account. No record of business receipts or expenses are kept other than the bank account records in the requesting and requested State.

A corporate income tax return is filed, understating gross income, taxable income, and tax due, to the extent of the skimmed business receipts. Specifically, the corporation's income tax return, on which the corporation reports gross receipts, cost of goods sold, dividends, compensation of officers, balance sheet information, and other items related to the corporation, understates gross receipts and other items mentioned above.

An informant tells the tax officials of the requesting State about the corporate business, including the skimming activities, and the bank account in the requested State, specifically stating that the individual told him that he skimmed no less than 30 per cent of the gross receipts every week and deposited these skimmed receipts in an account under his name in the X Bank located in the requested State. Based on this information tax officials of the requesting State commence an investigation of the corporation and the individual for possible tax violations under the requesting State's law.

The requested State would obtain and provide information relating to the bank account in the requested State of the individual in response to a specific request by the requesting State under Article 26 of the Convention.

#### HYPOTHETICAL 8

An individual subject to the requesting State's income tax is employed as the chief executive officer of a publicly held corporation of the requesting State that does subcontract work for other corporations of the requesting State. To ensure that the corporation keeps certain existing contracts and secures new ones, it pays bribes to employees of a major contractor. The funds from which the bribes are paid come from random diverted corporate gross receipts. The chief executive officer instructs the corporate accountant (1) not to report diverted receipts on the corporate books and records and (2) to destroy all documentation of those receipts held by the corporation. The books and records understating gross receipts are used to prepare the corporate income tax return, and, thus, the corporate income tax return understates the gross receipts and other income related entries. (The same books and records are used to prepare inaccurate income statements upon which shareholders and potential investors rely.)

The chief executive officer deposits the diverted funds into a bank account in the requested State over which he has sole signature authority. He periodically authorizes payments from that account to other accounts at the same bank over which the respective bribe recipients have signature authority. Based on information, which includes all the details stated above, provided by a staff accountant that works for the corporate accountant, tax officials of the requesting State initiate an investigation of the chief executive officer and the corporate accountant for their role in assisting in the preparation of a false corporate income tax return, and the bribe recipients for omitting the bribe payments from their individual income tax returns.

The requested State would obtain and provide information relating to the bank account in the requested State over which the chief executive officer has signature authority and the bank accounts in the requested State over which the respective bribe recipients have signature authority in response to a specific request by the requesting State under Article 26 of the Convention.

#### HYPOTHETICAL 9

An individual subject to the requesting State's income tax is a tax shelter promoter. Several tax shelter partnerships in which he sells limited partnership interests involve research and development companies incorporated and ostensibly operating in the requested State. The prospectus issued to investors for each shelter offers "investment opportunities by providing highly leveraged tax deductions." The investment per limited partnership share required for each shelter is \$50,000, which includes a cash payment of \$10,000 and a promissory note for \$40,000 due in 30 years with interest accrued and payable at the end of that period.

Tax officials of the requesting State initiate an investigation of the promoter to determine whether he aided and assisted in the preparation of false individual income tax returns filed by the investors, as well as whether the promoter failed to report the income he made from the promotion of the tax shelter on his individual income tax return. During the course of the investigation, these officials interview numerous investors in each shelter who claim the promoter stated that (1) the only payment ever required from an investor was the \$10,000 and (2) the note was only for tax purposes and would never be collected. During audits of several investors, tax officials of the requesting State discover that all \$10,000 payment checks were deposited to an identifiable bank account in the requested State.

The requested State would obtain and provide information relating to the bank account in the requested State into which the payment checks were deposited in response to a specific request by the requesting State under Article 26 of the Convention.

#### HYPOTHETICAL 10

An individual subject to the requesting State's income tax is a tax shelter promoter. He promotes and sells a movie tax shelter in which a corporation of the requested State ostensibly intends to produce feature films for profit. Limited partnership shares in movies to be produced are sold to investors in the requesting State for \$25,000 per share with assurances that deductions can be taken against income in the amounts of \$100,000 per share (a leverage of 4 to 1). In fact, the corporation in the requested State is a shell and the movie shelter scheme is a fraud. All monies received in the scheme inure to the personal benefit of the promoter. Upon receipt of investors' \$25,000 payments, the promoter deposits the funds into a bank account in the requested State over which he has sole signature authority. The promoter then prepares documentation based upon complete fabrication which he submits to the investors.

The investors, in reliance on such documentation, prepare and file false individual income tax returns claiming tax benefits derived from the movie shelter. Upon audit by the tax officials of the requesting State, these benefits are denied. A tax official of the requesting State initiates an investigation to determine whether the promoter aided and assisted in the preparation of the investors' false tax returns, as well as whether the promoter failed to report income made from the tax shelter promotion on his individual income tax return.

The requested State would obtain and provide information relating to the bank account in the requested State over which the promoter has signature authority in response to a specific request by the requesting State under Article 26 of the Convention.

#### HYPOTHETICAL 11

An individual has income as a salaried employee and earns income by conducting promotional events in which he encourages taxpayers to violate the requesting State's tax laws. Although the individual is subject to the requesting State's income tax, he does not file a tax return. The individual earns income at the promotional events by selling pamphlets in which he illustrates methods of evading income tax that he knows to be unlawful but that he represents to attendees of his promotional events to be lawful. He sells numerous pamphlets, each for a significant price.

Tax officials of the requesting State initiate an investigation of the individual to determine whether he aided and assisted in the preparation of the false individual income tax returns of those attending the promotional events, as well as willfully evaded his individual income taxes. These officials interview several promotional event attendees and purchasers of the pamphlets and discover that numerous checks in payment for the pamphlets were deposited into a bank account in the requested State.

The requested State would obtain and provide information relating to the bank account in the requested State into which the checks for payment were deposited in response to a specific request by the requesting State under Article 26 of the Convention.

#### HYPOTHETICAL 12

An individual maintains a bank account in the requested State into which he deposits income that is subject to the income tax in the requesting State. He makes substantial withdrawals from this bank account, through the use of a credit card tied to such account and issued in the name of a corporation, to pay for his living expenses for the year. The individual does not file an income tax return.

Tax officials of the requesting State commence an investigation of the individual based on information received from a credit card company related to credit cards tied to bank accounts in the requested State, and from various merchants. The tax officials determine that a credit card tied to a bank account in the requested State and issued in the name of a corporation was used throughout the year to purchase numerous personal items that were delivered to the individual. When these officials ask the individual whether he owns or controls the bank account, the individual does not acknowledge any interest in the corporation or the bank account, and provides no explanation regarding the source of the funds in the bank account.

The requested State would obtain and provide information relating to the bank account in the requested State in response to a specific request by the requesting State under Article 26 of the Convention.



### HYPOTHETICAL 13

An individual operates a business which provides a service on a "cash only" basis. He regularly deposits a substantial portion of these cash receipts in a bank account in the requested State maintained in his own name. He deposits the remainder of his cash receipts in a bank account in the requesting State maintained in his business name. He pays his business expenses by drafting checks against the latter bank account. He keeps no record of business receipts or expenses other than his bank account records in the requesting and requested State. Although the individual is subject to the requesting State's income tax, he does not file a return.

An informant tells tax officials of the requesting State about the business, specifically stating that the individual told him that he deposited no less than 30 per cent of his gross receipts in an account under his name in the X Bank located in the requested State. The informant also tells tax officials of the requesting State that the individual has used proceeds from the bank account in the requested State to purchase assets, formal legal ownership of which has been placed in the names of other persons.

Based on this information tax officials of the requesting State commence an investigation of the individual. Among other things, these officials learn that the individual used cash to buy particular assets, and has with documentation placed legal ownership to these assets in the name of other persons. These officials observe that these assets are always used by the individual.

The requested State would obtain and provide information relating to the bank account in the requested State of the individual in response to a specific request by the requesting State under Article 26 of the Convention.

### HYPOTHETICAL 14

An individual instructs his employer to make his salary checks payable to a corporation purporting to provide services as an independent contractor. The employer does not provide the documentation as required under the requesting State's tax law in the case of compensation provided to an employee. The individual opens a bank account in the X Bank located in the requested State in the name of that corporation, and deposits checks from his employer in that account. Although the individual is subject to the requesting State's income tax, he does not file a tax return.

Based on information provided by an informant, tax officials of the requesting State initiate an investigation of the individual. The tax officials contact the individual's employer, and obtain cancelled salary checks payable to the corporation and deposited in the bank account in the X Bank located in the requested State.

The requested State would obtain and provide information relating to the bank account in the requested State in the name of the corporation in response to a specific request by the requesting State under Article 26 of the Convention.