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220 DTR GG-1

Tax Fraud

**IRS Withdraws 'John Doe' Summons
Against UBS Over Tax Fraud Allegations**

The United States and Switzerland announced Nov. 16 that the Internal Revenue Service has withdrawn its legal proceedings against Swiss banking giant UBS over the bank's role in assisting U.S. clients to shield income from U.S. tax authorities.

In a statement, the Swiss government said the IRS "has fully and definitively withdrawn the John Doe summons" against UBS after meeting conditions under a U.S.-Swiss agreement requiring UBS to review some 4,450 secret accounts of U.S. clients for hand over to the IRS on grounds of tax evasion.

However, the Swiss government indicated that several hundred of the targeted accounts would escape exposure to U.S. authorities.

"Overall, approximately 4,000 cases have been supplied to the United States to date," the government said. "Subject to the outcome of pending appeals before the Swiss Administrative Court or in the case of no appeals, information on a number of additional accounts covered by the Agreement and the Treaty request will be delivered to the IRS over the course of the coming months.

"The Agreement thus having been substantially implemented, the Internal Revenue Service (IRS) fully and definitively withdrew the John Doe Summons against UBS on 15 November 2010," it added.

Mario Tuor, spokesman for the Swiss State Secretariat for International Financial Matters, said that details on a "few hundred" targeted accounts would not be handed over to U.S. authorities because the cases in question did not meet the criteria for hand over under an August 2009 U.S.-Swiss agreement setting out the terms for the handover or because the account holders had already declared the money in the accounts to the IRS.

Milestone in New Efforts, Shulman Says

IRS Commissioner Doug Shulman said in a statement he was "pleased to announce" the John Doe summons was being withdrawn.

"We are taking this action in light of our success in obtaining the account holder information we sought through the summons and obtained under the August 2009 agreement with the Swiss government and UBS," Shulman said "We appreciate the help and assistance of the Swiss government and UBS during this process."

"Today's announcement is yet another milestone in our ground-breaking efforts in the international tax compliance arena," Shulman said, adding, "Not only are we breaking through the walls of international bank secrecy, we are producing real results for U.S. taxpayers."

Including accounts already revealed through an earlier voluntary disclosure program as well as those handed over by UBS in February 2009 as part of a deferred prosecution agreement, Shulman said the IRS expects the number of secret bank accounts obtained by the agency to total more than 7,500.

The Nov. 16 announcement brings the curtain down on a legal battle between U.S. and Swiss authorities that threatened to bring Switzerland's largest bank to its knees and undermined the Alpine republic's cherished reputation for banking secrecy.

The 2009 agreement aimed to settle a long-standing feud between U.S. tax authorities and UBS over U.S. claims that UBS encouraged and assisted U.S. clients in hiding billions of dollars in assets from tax due through mechanisms such as offshore companies.

The IRS initiated a "John Doe" (JDS) summons against UBS in 2008 seeking details from the bank on up to 52,000 accounts held by U.S. taxpayers who maintained an "undeclared" account—an account where it did not have an IRS Form W-9 from the account holder—at UBS in Switzerland at any time between 2002 and 2007.

The "big news is that the commissioner clearly stated that the IRS intends to focus on other banks in other countries."

Bryan Skarlatos, Kostelanetz & Fink LLP

Under a worst-case scenario for UBS, the John Doe summons could have resulted in the revocation of the bank's operating license in the United States—a move which could have led to the collapse of UBS.

Accounts Turned Over Under Agreement

The August 2009 agreement required the Swiss Federal Tax Administration (FTA) to review 4,450 targeted accounts to see if they met the requirement for information hand over (159 DTR GG-1, 8/20/09). Under the agreed criteria, information was provided on the following UBS clients suspected of engaging in "tax fraud and the like:"

- U.S.-domiciled clients of UBS who directly held and beneficially owned undisclosed—non-W-9—custody accounts and banking deposit accounts in excess of 1 million Swiss francs (\$1 million) at any point between 2001 and 2008; and
- U.S. persons—irrespective of their domicile—who beneficially owned offshore company accounts established or maintained between 2001 and 2008.

The previous February, UBS reached a deferred prosecution agreement with U.S. authorities in which it admitted that it facilitated tax evasion by setting up shell companies for the U.S. clients through the bank's U.S. offshore branch (31 DTR K-1, 2/19/09). The bank agreed to immediately hand over details on some 250 targeted accounts and to pay fines and penalties totaling \$780 million.

Shulman stressed in his statement that "the John Doe Summons in the UBS case was just one piece of a much larger effort underway here at the IRS on international issues. There are many elements to it."

Greater Stress on International Compliance

He noted IRS has renamed and reshaped its large corporate division into the Large Business and International Division "in order to further emphasize and specialize our international and offshore banking efforts."

IRS also continues to work closely with other governments through the Organization for Economic Cooperation and Development, he said.

Shulman said IRS has had thousands more taxpayers come in through its voluntary disclosure program since a special program ended Oct. 15—about 3,000 voluntary disclosures from individuals with bank accounts from around the world.

"This is a significant development to get this many people—now over 18,000 individuals and counting—back into our tax system," Shulman said, noting that many of these voluntary disclosure cases involve significant amounts of previously unpaid tax.

He said account sizes and taxes vary considerably from case to case, but the closed cases so far have averaged more than \$200,000 in tax collections per case, which includes back taxes, interest, and penalties.

Shulman cautioned that IRS is combing through all the information it is receiving to pursue more taxpayers and financial institutions.

"This could be a great era of cooperation between the IRS and noncompliant taxpayers if the IRS would only provide some guidance. The IRS is missing the boat."

Josh Ungerman, Meadows, Collier, Reed, Cousins, Crouch & Ungerman LLP

"Although more data mining is still to be done, this information has already proved invaluable in supplementing and corroborating prior leads, as well as developing new leads, involving numerous banks, advisors and promoters from around the world," he said. "And this remains just the start. As I have said from the beginning, this has never been about one bank or one country. We've produced results and will continue to produce results."

Attorneys Say Penalty Guidance Needed for Others

U.S. tax attorneys with expertise on the UBS case said Nov. 16 that the withdrawal of the John Doe summons was expected, but stressed comments by Shulman that IRS has other banks in its sights.

Bryan Skarlatos, Kostelanetz & Fink LLP, New York, said, "It is not a surprise that the IRS is withdrawing the UBS summonses because under the settlement agreement with UBS the IRS agreed to drop its summons enforcement proceeding when it received at least 4,450 names from UBS. The IRS recently received that information, so it ended the case and withdrew the summons."

The "big news," he said, "is that the commissioner clearly stated that the IRS intends to focus on other banks in other countries."

Skarlatos told BNA, "There still are many thousands of U.S. taxpayers with unreported bank accounts. If the IRS continues its voluntary disclosure program and announces a set penalty or series of penalties depending on levels of culpability, the IRS is likely to get thousands of additional voluntary disclosures."

He said IRS is working hard to process the wave of voluntary disclosures referred to by Shulman in his statement. "However, under the current program, there is no sense of what penalties the IRS will impose on those coming forward," he said.

"As a result, many taxpayers decide not to pursue a voluntary disclosure and the pace of voluntary disclosures has slowed dramatically. If the IRS does set specific and reasonable penalties, I believe that the flow of voluntary disclosures will begin again."

More Voluntary Disclosures Seen With Guidance

Mark Matthews, Morgan, Lewis & Bockius LLP, Washington, also stressed the penalty issue.

"Potential disclosing taxpayers and their practitioners need further guidance from the IRS on the penalties that will apply to taxpayers coming in subsequent to Oct. 15 2009," the date the original special program for voluntary disclosures ended, Matthews said. "That is the missing ingredient to maximize the compliance and tax administration impact of this program right now."

Josh Ungerman of Meadows, Collier, Reed, Cousins, Crouch & Ungerman LLP in Dallas, said Nov. 16 he believed by not addressing the penalty question, "The IRS is missing a huge opportunity to bring in countless additional taxpayers through its voluntary disclosure program."

He said noncompliant taxpayers are balking at making the disclosures "because the IRS has refused to set forth guidelines on the civil penalties" applicable to post-Oct. 15, 2009 voluntary disclosures. "When a taxpayer hears that the FBAR [Report of Foreign Bank Account] penalty exposure by itself could be up to 300 percent of the amount of the undisclosed offshore account, it has an immense chilling effect on a potential voluntary disclosure," Ungerman said.

'Era of Cooperation' Seen Possible

He said in his view, "[t]his could be a great era of cooperation between the IRS and noncompliant taxpayers if the IRS would only provide some guidance. The IRS is missing the boat." Ungerman said for taxpayers who miss an IRS settlement initiative, there is precedent for the IRS to offer those "late" taxpayers less attractive relief than their counter parts who timely joined the settlement.

He said with civil penalty framework for current voluntary disclosures, "the number of taxpayers who tax professionals bring back in to the system will rise dramatically."

Ungerman also addressed Shulman's comments on IRS's enforcement efforts. "The IRS has carried

through on its promise/threat to expand international enforcement beyond UBS & Switzerland," he said, noting that a recent investigation into HSBC accounts in India is an example.

"The IRS now has so many leads, a big challenge will be how it uses its limited resources to pursue the leads with the highest chance of IRS success," the Meadows Collier practitioner said, noting that UBS and Switzerland "were just the tip of the iceberg for the IRS in their hunt for noncompliant U.S. taxpayers.

Further, he said, " IRS is making no bones about the fact that it intends to pursue the advisors in undisclosed offshore cases. Expect the government to pursue attorneys and accountants in undisclosed offshore arrangements."

By Daniel Pruzin (Geneva) and Alison Bennett (Washington)

Text of Shulman's statement is available in TaxCore.

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