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Swiss Banks No Longer A Safe Haven?

The Editor interviews Lawrence S. Horn and Richard J. Sapinski of Sills Cummis & Gross, P.C. The views and opinions expressed in this interview are those of the interviewees and do not necessarily reflect those of Sills Cummis & Gross P.C.

Editor: Larry Horn and Rich Sapinski, you have extensive experience both on the prosecution and defense sides of the criminal tax spectrum. Would you share some of your backgrounds with our readers?

Horn: After graduating from law school, shortly thereafter I became an Assistant United States Attorney in the District of New Jersey. In my last three years, I was placed in a position of initiating, supervising or handling every single criminal tax case filed in the federal district of New Jersey, and getting immersed in criminal tax work. I left government service on January 1, 1979 joining first with a small civil and criminal tax litigation boutique, which merged into Sills Cummis & Gross in 1981.

Sapinski: After graduating from law school, I went to work for the IRS' Chief Counsel's office as a private attorney in the Newark office. My initial duties were to review criminal tax recommendations for prosecution from special agents and to assist them in developing cases for prosecution. In working with the agents on developing the cases and then evaluating them, many were sent to the Department of Justice where Larry would initiate the criminal proceedings. After promotion to a job of special trial attorney performing civil tax trial cases, in 1987 I joined Larry at Sills Cummis.

Editor: The recent IRS investigation of UBS AG and the Justice Department's demand that UBS disclose the names of its U.S. customers has received major attention. The investigation poses a potential threat to delinquent taxpayers, taxpayers who have filed inaccurate returns, and taxpayers who are hiding income in undisclosed foreign banks. How can a taxpayer mitigate criminal and civil penalties by vol-



Lawrence S.
Horn



Richard J.
Sapinski

untarily disclosing foreign accounts and undeclared income?

Horn: The Voluntary Disclosure Program of the Internal Revenue Service has been around for more than fifty years. However, right now it has been highlighted in the press. The day after the Deferred Prosecution Agreement between the United States and UBS was announced, the Commissioner of the Internal Revenue Service announced the Enhanced Voluntary Disclosure program commencing on March 23, 2009 and extending to September 23, 2009 and encouraged those taxpayers who have accounts either at UBS or at other accounts overseas to get right with their government – to make a voluntary disclosure, to file amended returns, and to file what is known as delinquent FBAR (Foreign Bank and Financial Accounts) Treasury forms. What distinguishes this wave of voluntary disclosures from prior waves is that the Commissioner has given guidance as to what penalties will be assessed, has given a deadline for filing, and has stated that if you are the owner of a foreign bank account, the only way to come under this program is to initiate discussions with the criminal investigation division of the IRS. There are certain requirements of timeliness and cooperation, but there are specific pitfalls for those who aren't as familiar with the voluntary disclosure program as those of us who specialize in this area.

Sapinski: Basically, this program is a little different from the classic voluntary disclosure policy because one of the issues that histori-

cally had been an issue was whether or not a disclosure had qualified under the policy and whether there had been a triggering event. The Service's position is that if failure of disclosure is known to the Service before you came to them, you had no ability to make a voluntary disclosure. The commissioner is requesting holders of foreign accounts to voluntarily disclose. If you come in under this program and qualify, you have an excellent chance of avoiding criminal prosecution and saving money.

The issue of undisclosed foreign bank accounts is much at the forefront. Last summer, when Senator Levin's committee on oversight issued its report, it stated that there were 19,000 U.S. account holders with UBS, but by February of this year the number grew to 53,000. If we take a step back and reflect that UBS is not the only bank in Switzerland, but there are a number of other banks in Germany, Israel, East Asia, as well as banks in the Caribbean, you're talking about significantly more than 53,000 names.

Editor: What about other foreign banks that follow similar practices?

Horn: Three of the clients whom we are advising are clients of other Swiss banks. One of the interesting things that we have found is that we are representing a number of octogenarians, about 50 percent of our clients, who are being encouraged by their adult children not to have this problem left on their doorsteps after their parents die when they have to file truthful and accurate estate tax returns before trying to repatriate funds. There are reasons I give clients: 1) voluntary disclosure by any other name is called amnesty; 2) once you make a voluntary disclosure, you can repatriate the funds because if you do get a wire transfer for a billion dollars and the IRS comes to you a few months later, you can respond that this has already been disclosed in our voluntary disclosure; 3) you remove the problem from the adult children. We have had virtually every ethnicity represented, including Armenians, Holocaust-escapees from Germany and Poland, Russians, people escaping

Please email the authors at lhorn@sillscummis.com or rsapinski@sillscummis.com with questions about this article.

from Iran after the Shah was deposed, Iraqis fleeing when Saddam Hussein came in. Money was placed for safekeeping in Switzerland, Lichtenstein, Asia, and left there.

Sapinski: Why is the focus on UBS and Lichtenstein Global Trust (LGT)? The focus was on these companies because that's where the U.S. government received its initial information which came to Senator Levin's committee. In the case of LGT, a bank officer copied the disk and sold it to Germans who sold the disk to all their trading partners. At roughly the same time, there was an investigation in California of a real estate developer, Igor Plenicoff, who cooperated in naming a UBS banker named Bradley Birkenfeld, who began cooperating with investigators. This led to the John Doe summons and the initial focus on UBS, but by no means is the government unaware that various other Swiss banks and banks elsewhere hold other accounts.

Editor: If this is an amnesty program, will delinquent taxpayers face penalties or will those be waived in part or entirely?

Sapinski: Now under the program that the Commissioner announced on March 23, there is a penalty regime set up if you did not come in. The government could assert the tax owed, interest on the tax, and a 75 percent civil fraud penalty plus interest on that tax deficiency – a significant penalty each year for previous years' delinquencies. There are penalties for a panoply of forms for not filing.

If an account holder comes in and is accepted into the program, he can agree to file amended income tax returns for six years only, pay the tax and the interest at 20 percent, rather than the 75 percent penalty. And there's a separate significant penalty for not filing the foreign bank account reports. Prior to 2004, the penalty was a fixed dollar amount, the maximum being a \$50,000 fine per year, but in 2004 the fine went up to 50 percent of the value of the non-disclosed account. So, after 2004 through 2007, four years of unfilled FBAR's, potentially you could have double the value of the account as a penalty. The government is now saying that if you file the delinquent FBAR's as well, we will take a 20 percent penalty of the highest year's account value. Therefore, that will settle all issues with the government.

Editor: How has the IRS investigation of UBS affected the IRS' policy of voluntary disclosure?

Horn: It has certainly highlighted it and led to more people knowing about it than just those who practice tax controversy work. We're getting calls from CPA's and directly from potential clients who have read articles about it in the newspapers around the world.

There was an article in *Bloomberg* magazine by David Voreacos on Igor Olenicoff, who turned in Bradley Birkenfeld, the UBS representative, which really started the news interest.

Editor: Although the IRS claims that taxpayers may avoid criminal liability and extensive civil penalties, it seems that taxpayers are packaging and delivering to the government virtually all the evidence needed to obtain convictions if the government chooses to prosecute. Should taxpayers be wary of the promises of the IRS' Voluntary Disclosure Policy?

Horn: This is why we say this is not for the uninitiated. The policy of the IRS demands that not only it be kinder and gentler, but that the taxpayer cooperate fully with the IRS. In the earlier voluntary disclosure situations we would give a hypothetical situation to the IRS and ask if everything we said is confirmed, do they think this would be a valid voluntary disclosure? Under the regime now in effect from March to September you have to surface your client's name on day one. So, it is very important for the attorney to interview the client and review the documents very carefully because when you have to cooperate with the government, that cooperation has to be full, complete and truthful.

As an example, we saw two brothers two weeks ago who refused to agree to provide the authorities the names of any person who helped them open a foreign account. In response I advised that unwillingness to provide this information would not admit them to the program. So, have there been examples in the last fifty years where people have been prosecuted? I know of two. Remember, the IRS has a trust here too. It knows that if it plays fast and loose with the tax bar, no one will ever come in again under the Voluntary Disclosure Program.

Sapinski: Before you recommend to a client to voluntarily disclose information, be mindful that every case is different. You should fully explore all the facts with a client to determine whether the voluntary program works for him – is he willing to part with 20 percent of his funds as a fine or is he capable of being truthful in the interviews? The case that is probably the classic of how not to do a voluntary disclosure is *United States v. Tenzer*. Tenzer was a CPA and tax lawyer, who did not file income tax returns for a number of years and owed a significant amount of money and liability in excess of \$100,000 a year. Because of the IRS' collection efforts, Tenzer made a voluntary disclosure under the Voluntary Disclosure Program, was accepted into the program, delinquently filed all of the returns, the IRS agreed not to prosecute him, but he then did not pay the tax liabilities. If you don't pay all that is due, part of your duty is to cooperate in disclosing your financial

assets and to make a good faith payment arrangement. Apparently Tenzer had significant assets. The Collection Division was offering him a deal – pay about ten cents on the dollar, which he refused. Since Tenzer was not cooperating, the IRS treated the payments as delinquent and the amended returns as admissions of guilt and then prosecuted him for income tax evasion. Everyone who goes into this program should be thinking that we are going to be making these payments with interest, are going to be prepared to make full financial disclosure in good faith and be prepared to enter into serious payment negotiations.

Editor: What factors are considered when the IRS refers a case for criminal prosecution?

Sapinski: There are three major tax crimes: tax evasion, filing a false return under the penalties of perjury when you know it is not true and correct as to every material matter, and willful failure to file income tax returns. The common barometer of all of them is criminal intent. That's why you rarely have a criminal tax case of less than three years because the government must prove a pattern of under-reporting, of misstating or a pattern of repetition of non-filing.

Horn: The IRS initiates somewhere in the range of 3,300 criminal tax prosecutions across the country in a given year – not a huge number. The IRS looks for people who are inviting prosecution targets, such as prominent professionals, and who clearly have engaged in conduct that is suggestive of scheming or trying to hide what they are doing. There are some smaller cases as well as blockbusters. In the average criminal tax case, the tax loss is somewhere between \$30,000 and \$300,000.

Editor: An attorney can submit a taxpayer's Voluntary Disclosure Form to either the Internal Revenue Service Center or the Criminal Investigation Division of the IRS. What should an attorney consider before deciding where to send his client's submission?

Horn: The Commissioner has given guidance in the case of the Swiss bank account – you must do it directly with the Criminal Investigation Division. It will not be considered a voluntary disclosure, and you are putting your client at 100 percent peril if you do it through the Service Center. That specific issue was addressed in the FAQ of May 6, and it's another reason why we so strongly believe that the uninitiated should not work with clients who have potential liability. This is something that has to be handled by skilled people who work with the IRS' Criminal Investigation Division every day.