I.R.S. INFORMATION EXCHANGES & THE COORDINATED TAX RAIDS ON CREDIT SUISSE

Authors
Rusudan Shervashidze
Stanley C. Ruchelman

Tags
Exchange of Information
F.A.T.C.A.
I.R.S.

INTRODUCTION

In early April, Bloomberg News reported on coordinated tax raids on three separate offices of Credit Suisse.[1] It is believed that the bank was taken by surprise. However, in light of the global tax efforts to discover and prosecute facilitators of abusive tax planning, one wonders why the raids were not anticipated.

When the raids took place, two people were arrested and valuables such as gold bars, paintings, and jewelry were seized. The raids were part of a joint tax fraud examination by the Netherlands, France, Germany, the U.K., and Australia regarding millions of euros concealed in Swiss accounts. Information collected by one government will be subject to exchange with other governments that are trusted partners in the battle against tax evasion.

Due to the secrecy surrounding tax fraud investigations, no one knows for certain whether the I.R.S. furnished information that was relevant to the tax raids. However, there are many avenues through which the I.R.S. furnishes and receives information. It is clear that the I.R.S. had the means to transfer information to the relevant tax authorities, as will be explained in this article.

BACKGROUND

The I.R.S. website provides a laundry list of financial institutions and advisory firms that have assisted U.S. taxpayers in evading U.S. tax through the use of hidden accounts outside the U.S.[2] Of the 145 institutions listed, the second bank to appear on the list is Credit Suisse.

As of February 6, 2017, 78 Swiss banks had executed non-prosecution agreements under the Swiss Bank Program of the U.S. Department of Justice. Credit Suisse was not among these banks. Instead, on May 19, 2014, Credit Suisse pled guilty to conspiracy to aid and assist U.S. taxpayers in filing false income tax returns and agreed to pay a fine of $2.6 billion. Eight of the bank's employees were also indicted.[3]

It appears that, once the plea bargain was agreed and the fine paid, Credit Suisse believed the "fire drill" was over. In doing so, it failed to consider developments in taxpayer transparency and exchanges of taxpayer information among governments,

1 Jan-Henrik Foerster and Joost Akkermans, "Credit Suisse Taken by Surprise in Five-Nation Tax Probe," Bloomberg.com, March 31, 2017.

2 "Foreign Financial Institutions or Facilitators," IRS.gov, January 31, 2017.

3 "Credit Suisse Pleads Guilty to Conspiracy to Aid and Assist U.S. Taxpayers in Filing False Returns," U.S. Department of Justice, May 19, 2014.

namely those that followed the advent of the Foreign Account Tax Compliance Act ("F.A.T.C.A.") in 2010.

F.A.T.C.A. changed the landscape of the U.S. and global routine exchanges of tax information between governments. Since the legislation was introduced, the U.S. has entered into intergovernmental agreements ("I.G.A.'s") that have facilitated information exchange with over 100 counties. According to the latest numbers, the I.R.S. has collected over $10 billion through the voluntary disclosure program from 55,000 participants.[4]

Although European advisers initially expressed doubts about the participation by E.U. Member States in government-to-government programs that impose information gathering obligations on home country financial institutions, events proved the opposite. European countries instead welcomed the F.A.T.C.A. initiative, and today, the E.U. stands at the forefront of automatic exchanges of information as part of global transparency.

"Credit Suisse was naïve in believing that a firewall was successfully erected against further examination."

In recent years, the O.E.C.D. has published the B.E.P.S. Action Plan attacking perceived tax abuse in cross-border transactions and has developed the Common Reporting Standard (the "C.R.S.") for exchange of financial information. The C.R.S. requires jurisdictions to obtain information from their financial institutions and automatically exchange that information with other jurisdictions on an annual basis. The provision was warmly received by the European Commission, which converted the C.R.S. into a directive and effected the Anti-Tax Avoidance Directive.

In this environment, Credit Suisse was naïve in believing that a firewall was successfully erected against further examination.

MEANS OF OBTAINING INFORMATION

Tax Treaties

Most U.S. tax treaties include articles relating to the exchange of information and mutual assistance in tax matters. These provisions authorize the exchange of tax related information between the treaty countries on an automatic basis and pursuant to specific requests. Information received under a treaty is treated as secret in the same manner as information obtained under the domestic laws of the state making the request.

Information can be disclosed by the requesting state only to persons or authorities that have responsibility for administering the tax collection process in all relevant phases. This includes (i) courts and administrative bodies; (ii) personnel in departments involved in the assessment, collection, or administration of the tax; (iii) personnel involved in the administrative appeals function; (iv) personnel responsible for the investigation and enforcement of the tax laws; (v) legal officers involved in the prosecution those who commit tax offenses; and (vi) persons who oversee each of the foregoing functions.

Persons who receive information can use the information only for the purposes described above. If a criminal or civil trial is pursued by the tax officials, disclosure

---

[4] "Offshore Voluntary Compliance Efforts Top $10 Billion; More Than 100,000 Taxpayers Come Back into Compliance." IRS.gov, October 21, 2016.

is permitted in public court proceedings or in judicial decisions.[5]

Each treaty contains unique language that sets forth the boundaries of who may receive information and how the information may be used.

Mutual Legal Assistance Treaties ("M.L.A.T.'s")

These bilateral agreements authorize the exchange of evidence and information in criminal and related matters. M.L.A.T.'s. cover criminal non-tax matters and, in some instances, criminal tax matters. M.L.A.T.'s. are negotiated by the U.S. Department of State in cooperation with the Department of Justice. They have been used to obtain banking and other financial records from the treaty partners.

To encourage foreign governments to cooperate in joint investigations related to narcotics trafficking and money laundering – for which the penalties include asset forfeiture – the U.S. has offered treaty partners the opportunity to share in forfeited assets.

Multilateral and Bilateral Agreements

The U.S. is a party to several multilateral and bilateral agreements, which authorize exchanges of information for tax purposes. Various agreements and consortia for information exchange are outlined below.

Tax Implementation or Coordination Agreements

These bilateral agreements allow for exchanges of tax-related information between the U.S. and its five territories (*i.e.*, American Samoa, Guam, the Northern Mariana Islands, Puerto Rico, and the U.S. Virgin Islands). All five territories have a local tax system, but some are required to mirror the U.S. Code system and substitutes the name of the territory for the "United States." These territories are U.S. Virgin Islands, Guam, and the Northern Mariana Islands. Although American Samoa is not bound by this system, it has chosen to adopt much of the U.S. Code for its income tax purposes. Puerto Rico, in contrast, has its own income tax system.

Tax Information Exchange Agreements ("T.I.E.A.'s")

The purpose of this type of bilateral agreement is to facilitate the exchange of tax related information with partner countries. It provides for mutual assistance in civil and criminal tax investigations and proceedings. A T.I.E.A. is an executive agreement rather than a treaty. It is entered into by the Treasury without the advice and consent of the Senate and is limited in scope to the mutual exchange of information.

Joint International Tax Shelter Information Center ("J.I.T.S.I.C.")

At its inception, the agreement that formed J.I.T.S.I.C. was signed by the commissioners of the Australian, Canadian, U.K. and U.S. tax administrations, and later by the Japanese commissioner. Today J.I.T.S.I.C. represents the heads of tax administrations from 36 countries. J.I.T.S.I.C. is designed to supplement the ongoing work of tax administrations in identifying and curbing abusive tax avoidance transactions, arrangements, and schemes.

To put its task in perspective, one can look to the meeting of J.I.T.S.I.C. members

[5] U.S. Model Tax Convention, art. 26 (2006).

in January 2017, where 30 countries gathered to exchange information helpful in coordinating collaborative tax investigations. The tax administrations that met have reportedly audited more than 1,700 taxpayers and have made more than 2,550 requests for information. The administrations have also identified a "target list" of 100 intermediaries who help wealthy individuals and companies set up and use entities in tax havens; these include lawyers, bankers, and accountants.[6]

Common Reporting Standard ("C.R.S.")

Although the U.S. is not a signatory to the C.R.S., the C.R.S. should be recognized as representing the international consensus on reciprocal automatic exchanges of financial account information for tax purposes. As of May 7, 2017, 100 jurisdictions have committed to implementing the C.R.S. Of the participating jurisdictions, half will implement initial exchanges in 2017 and the balance will implement initial exchanges in 2018.[7]

The Forum on Tax Administration ("F.T.A.")

The F.T.A. was created in 2002. It represents heads of tax administration from 50 O.E.C.D. and non-O.E.C.D. countries, including members of the G-20.[8] The purpose of the forum is to identify, discuss, and influence relevant global trends and develop new ideas to enhance tax administration around the world. To that end, it attempts to improve taxpayer services and tax compliance by helping tax administrations increase the efficiency, effectiveness, and fairness of tax administration and reduce the costs of compliance.

Inter-American Center of Tax Administration ("C.I.A.T.")

C.I.A.T. is a public, non-profit organization. The goal of C.I.A.T. is to promote mutual assistance and cooperation among the member countries. The organization was founded in 1967 and currently has 39 members in Latin America and other places, not including associate member countries. Among its activities is training tax administrations in tax policy, tax collection, information exchanges, and transfer pricing.[9]

International Tax Dialogue ("I.T.D.")

I.T.D. is a joint initiative of the European Commission, the Inter-American Development Bank, the International Monetary Fund, the O.E.C.D., the World Bank, and the Inter-American Center of Tax Administrations. The I.T.D. aims to facilitate discussion of tax matters among national tax officials, regional tax organizations, international organizations, and other key stakeholders.[10]

EXCHANGE OF INFORMATION PROCEDURES

Generally, an information request by the U.S. results from an on-going examination

6 Will Fitzgibbon and Mar Cabra, "Tax Agencies Draw Up 'Target List' of Offshore Enablers," I.C.I.J., January 20, 2017.

7 "AEOI: Status of Commitments (100 Jurisdictions Have Committed)," (O.E.C.D. Publishing, 2017).

8 "About - Forum on Tax Administration," O.E.C.D.

9 Inter-American Center of Tax Administrations Website.

10 I.T.D. Website.

of a particular tax return. The request may also arise from collection matters, criminal investigations, or other tax administrative procedures covered by the international tax information sharing agreements.

"Treaties and T.I.E.A.'s provide for the exchange information relevant for carrying out the provisions of the domestic laws concerning covered taxes of the requested party."

The Competent Authority or Central Authority is responsible for matters relating to the application of international tax information sharing agreements. This authority may be delegated to one or more subordinate officials. To illustrate, for tax treaties and T.I.E.A.'s, the authority to act as the U.S. Competent Authority has been delegated by the secretary of the Treasury to the deputy commissioner of the Large Business and International Division ("LB&I"). The authority to sign or act on behalf of the deputy commissioner of LB&I has been delegated to the program manager at the Exchange of Information Headquarters, who has the authority to sign or act on all exchanges of information under tax treaties and T.I.E.A.'s. All such exchanges are administered by the Exchange of Information program manager in Washington, D.C.; the revenue service representative in Plantation, Florida; tax attachés stationed at various overseas I.R.S. posts; and the J.I.T.S.I.C. program manager in Washington, D.C.[11] With respect to M.L.A.T.'s and similar law enforcement agreements, the Office of International Affairs in the Criminal Division of the Department of Justice is authorized to act as the U.S. Central Authority.

Protection of Information by the I.R.S.

Information received by the I.R.S. is treated as sensitive and is safeguarded in accordance with the disclosure and confidentiality provisions of the relevant agreement, Code §6103 (in the case of taxpayer-specific information), and Code §6105 (which governs the disclosure and confidentiality of information exchanged under international tax information sharing agreements).

Non-sensitive information may be provided to a foreign tax official without the need to exchange it under a tax information sharing agreement. However, to ensure the information is in fact considered non-sensitive for exchange purposes, no I.R.S. employee other than the employees described above may contact, provide any information to, request any information from, or exchange any information with a foreign tax official.[12]

To ensure compliance with applicable disclosure and confidentiality rules, an I.R.S. office is not allowed to respond to direct contact from a foreign tax official. Rather, it must refer the contact to Exchange of Information Headquarters. If any I.R.S. office in possession of information originally received from foreign tax officials is sought in response to court orders, subpoenas, or Freedom of Information Act requests in the U.S., that office is required to contact Exchange of Information Headquarters.[13] Furthermore, if any I.R.S. office discovers or suspects that an unauthorized disclosure of information has occurred, that office must immediately notify Exchange of Information Headquarters.

Treaty Exchanges

Treaties and T.I.E.A.'s provide for the exchange information relevant for carrying out the provisions of the domestic laws concerning covered taxes of the requested

---

11 I.R.M. 4.60.1.1.2.

12 I.R.M. 4.60.1.1.2.3.

13 I.R.M. 4.60.1.1.2.6.

party. If the U.S. is the requesting party, the I.R.S. examiner must demonstrate the relevance of the requested information and show a connection between the taxpayer and the foreign-based information. The I.R.S. examiner must exhaust all means to access the requested information under domestic law prior to requesting information under a treaty or T.I.E.A.

Types of Exchanges

There are nine basic types of exchanges:

- Specific requests
- Spontaneous exchanges
- Automatic exchanges
- Industry-wide exchanges
- Simultaneous examination program
- Joint audits
- Simultaneous criminal investigation program
- Mutual legal assistance program
- Mutual collection assistance request program

Each has its own set of procedures. The information that can be obtained through these exchanges includes the following:

- Tax returns and return information such as filing status, income/expenses/tax liability, and citizenship/residency
- Bank and brokerage records
- Business records
- Public records such as deeds
- Birth, death, and marriage records
- Witness interviews
- Property ownership information[14]

Foreign Information Request

If a foreign country with which the U.S. has a T.I.E.A. in place forwards a specific exchange of information request to the U.S. Competent Authority, the request is assigned to an I.R.S. employee ("designated agent"). Once the request is received, and determined to be appropriate, the designated agent reviews the request to see if it is within the authorized scope of the relevant agreement and does not violate any secrecy or trade secret exceptions. One determined to be acceptable, the request will be forwarded to the appropriate I.R.S. civil group manager or the executive

[14] I.R.M. 4.60.1.1.3.

director of Criminal Investigation: International Operations, who will then fulfil the foreign-initiated information request.

The I.R.S. Manual governs the manner in which the request is processed by field offices. This includes timelines for each step in the process. If the requested documents are not already in the possession of the field office, an Information Document Request ("I.D.R.") may be issued or a summons may be served. In those cases, the examining agent will provide guidance on how to proceed.

An information request under the exchange of information agreement does not require the existence or initiation of an I.R.S. examination and does not constitute an I.R.S. examination. As previously stated, the field office personnel assisting with a foreign request may not directly contact any foreign tax official regarding the request or any other matter.

All T.I.E.A.'s limit the exchange of trade secrets when disclosure may cause substantial harm to the taxpayer's competitive position. However, information related to transfer pricing is not necessarily protected from disclosure.

Improper disclosure of returns and return information may result in civil or criminal penalties under Code §§7431 and 7213.[15] To ensure compliance with applicable disclosure and confidentiality rules, only I.R.S. employees described above and those having transfer pricing responsibility may contact, provide information to, request any information from, or exchange information with a foreign tax official.[16]

I.R.S.-Initiated Requests

When examiners seek information from a treaty partner, the basic Code and regulatory rules, along with case law, will apply. Under Code §7602, the I.R.S. may examine books, papers, records, or other data that may be relevant to "ascertaining the correctness of any return, making a return where none has been made, determining the liability of any person for any internal revenue or collecting any such liability." This was addressed in an article that appeared in the April 2017 edition of *Insights*.[17]

CONCLUSION

In light of the U.S. investigations and the broad network of U.S. tax treaties, executive agreements in the form of I.G.A.'s or T.I.E.A.'s, and multilateral agreements covering intergovernmental cooperation and exchange information to prevent tax fraud, it is hard to image the I.R.S. did not exchange information developed in the Credit Suisse prosecution with its counterparts the Netherlands, France, Germany, the U.K., and Australia. Indeed, financial institutions should be wary of further examinations. It seems to be only a matter of time before the I.R.S. exchanges information about all facilitators of tax fraud encountered in its prosecution of foreign banks and obtained in the offshore voluntary disclosure programs.

---

15 Code §6103(b).

16 IRM 11.3.25.1.

17 Galia Antebi and Stanley C. Ruchelman, "LB&I Audit Insights: Using a Code §6038a Summons When a U.S. Corporation is 25% Foreign Owned," *Insights* 4 (2017), p. 51.