



Department of Justice

JOINT STATEMENT OF

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DEPARTMENT OF JUSTICE

BEFORE THE

**PERMANENT SUBCOMMITTEE ON INVESTIGATIONS
COMMITTEE ON HOMELAND SECURITY AND GOVERNMENT AFFAIRS
UNITED STATES SENATE**

FOR A HEARING

**OFFSHORE TAX EVASION: THE EFFORT TO COLLECT UNPAID TAXES ON BILLIONS IN
OFFSHORE ACCOUNTS**

PRESENTED ON

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**Joint Statement of
Deputy Attorney General James M. Cole and
Assistant Attorney General, Tax Division, Kathryn Keneally
Before the Permanent Subcommittee on Investigations
United States Senate Committee on Homeland Security and Government Affairs
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Chairman Levin, Ranking Member McCain, and Members of the Subcommittee, thank you for inviting us to testify about the Department's efforts to address Swiss bank facilitation of U.S. tax evasion. The Department is committed to global enforcement against financial institutions that engage in or facilitate cross-border tax evasion. We also continue to track down and hold accountable individuals who sought to evade their tax and reporting obligations by hiding money in foreign accounts, and the individual bankers, accountants, lawyers, and other professionals who facilitated these crimes have also been and continue to be subject to investigation and prosecution. We greatly appreciate the dedicated work of the Subcommittee over many years in exposing this wrongful conduct, and your commitment to this important law enforcement issue.

Enforcement against Cross-Border Tax Evasion

The use of foreign bank accounts to evade U.S. taxes has been a long-standing challenge. These activities came under heightened scrutiny in 2008, with focused law enforcement efforts by the Department and the Internal Revenue Service (IRS). In February 2009, the Department reached a ground-breaking deferred prosecution agreement with UBS. With the agreement of the Swiss government, which invoked emergency powers under Swiss law, UBS disclosed certain account holder records, paid \$780 million in fines, penalties, interest and restitution, and exited this cross-border business. Also as a result of this deferred prosecution agreement, the IRS subsequently obtained additional account holder information from UBS following approval by a federal district court to issue a John Doe summons.

Since 2009, the Department has publicly charged 73 account holders and 35 bankers and advisors with violations arising from offshore banking activities. Sixty-one account holders have pled guilty, seven were convicted at trial, and five await trial. Four bankers and financial advisors have pled guilty; many remain fugitives. Recently one banker, Raoul Weil, formerly the third-highest banking official at UBS, waived extradition following his arrest in Italy and is now awaiting trial in the United States. While the Department's enforcement focused initially on cross-border activities in Switzerland, it has expanded to include wrongdoing by U.S. account holders, financial institutions, and other facilitators globally, including publicly disclosed enforcement concerning banking activities in India, Israel, Liechtenstein, Luxembourg, Barbados, and other Caribbean countries.

These high-profile enforcement actions created pressure on non-compliant taxpayers to correct their tax returns to report previously undisclosed accounts. According to the IRS, since the inception of the investigation against UBS, over 40,000 taxpayers have reported previously secret accounts through the IRS's offshore voluntary disclosure programs, and have paid over \$6 billion in back taxes, interest, and penalties. These enforcement efforts not only remedy past wrongdoing, but also bring into the system tax revenue from taxpayers who become compliant going forward.

The Department is committed to holding foreign banks accountable for their role in facilitating attempts to evade U.S. tax and reporting obligations. We understand that the Subcommittee's focus today is on the cross-border activities of Swiss banks. Since announcing the UBS deferred prosecution agreement in February 2009, the Department has continued to investigate this activity, and has taken public action against two other banks, one in Switzerland and one in Liechtenstein.

In February 2012, the Department indicted Wegelin Bank, one of the oldest financial institutions in Switzerland, for conspiracy to defraud the United States for actions arising from its efforts on behalf of U.S. account holders. Wegelin Bank pleaded guilty in January 2013, to the indictment, including the following allegations: in the wake of U.S. investigations of UBS, Wegelin's senior management decided to take steps to capture the illegal business that UBS had exited; to capitalize on the business opportunity and to increase its assets under management, and the fees earned from managing those assets, Wegelin employees persuaded clients to transfer assets from UBS to Wegelin by emphasizing that, unlike UBS, Wegelin did not have offices outside of Switzerland and was therefore less vulnerable to United States law enforcement pressure. Wegelin Bank was ordered to pay approximately \$58 million to the United States and to forfeit funds in the amount of \$16.2 million previously seized by the government from a correspondent account in the United States, for a total recovery to the United States of approximately \$74 million.

In July 2013, the Department announced that Liechtensteinische Landesbank AG, a bank based in Vaduz, Liechtenstein ("LLB-Vaduz"), agreed to pay more than \$23 million to the United States and entered into a non-prosecution agreement. As noted in the agreement, before the government began the investigation, LLB-Vaduz voluntarily implemented a series of remedial measures to stop servicing U.S. account holders with undeclared accounts. The bank also assisted in changing the law in Liechtenstein retroactively, which enabled the Department to obtain account files of non-compliant U.S. account holders without having to identify by name each account holder whose information was requested.

In addition to these public actions, the Department has on-going criminal investigations concerning the cross-border activities of banks and account holders, as well as bankers and other

professionals who facilitated U.S. tax evasion and reporting violations. In August 2013, the Department publicly stated that investigations have been authorized of fourteen banks concerning the use of Swiss bank accounts. This is in addition to on-going investigations concerning cross-border activities by banks outside Switzerland. While we are not in a position to provide information regarding these non-public matters, the absence of public disclosure should not be construed as a sign of inactivity in this critical law enforcement area.

The Department is also successfully using a variety of law enforcement tools to gather information that we believe will lead to admissible evidence in future enforcement efforts. For example, in January 2013, the federal district court for the Southern District of New York entered an order authorizing the IRS to issue a John Doe summons seeking records for Wegelin Bank's U.S. correspondent account at UBS. In April 2013, the federal district court for the Northern District of California entered an order authorizing the IRS to serve a John Doe summons seeking records of the correspondent account at Wells Fargo for Canadian Imperial Bank of Commerce FirstCaribbean International Bank (FCIB). FCIB is based in Barbados and has branches in 18 Caribbean countries. On November 7, 2013, the federal district court for the Southern District of New York entered an order authorizing the IRS to issue John Doe summonses seeking records of the Zurcher Kantonalbank and its affiliates (collectively ZKB) correspondent accounts at Bank of New York Mellon and Citibank NA for information relating to U.S. taxpayers holding undisclosed accounts in ZKB. A similar order was issued by the same court on November 12, 2013, authorizing the IRS to issue John Doe summonses seeking records of the correspondent accounts held by Bank of N.T. Butterfield & Son Limited and its affiliates in the Bahamas, Barbados, Cayman Islands, Guernsey, Hong Kong, Malta, Switzerland and the United Kingdom at Bank of New York Mellon, Citibank NA, JPMorgan Chase Bank NA, HSBC Bank NA and Bank of America NA. These orders allow the IRS to request the identities of U.S. taxpayers who may hold accounts at banks outside of the United States. We continue to work closely with the IRS to determine when to seek orders authorizing additional John Doe summonses as part of our comprehensive law enforcement strategy in these cases.

The Department has also enforced summonses and subpoenas for records that account holders are required to maintain concerning their foreign banking activities through the successful litigation of the applicability of the "required records" exception to the production privilege under the Fifth Amendment. All six appellate courts that have considered the issue have rejected the argument that witnesses can refuse to comply with a subpoena for the bank records that are required by law to be kept and presented for inspection as a condition of maintaining an offshore account. *In re Grand Jury Subpoena Dated February 2, 2012*, --- F.3d ---, available at 2013 WL 6670733 (2d Cir. Dec. 19, 2013); *United States v. Under Seal*, 737 F.3d 330 (4th Cir. 2013); *In re Grand Jury Proceedings*, No. 4-10, 707 F.3d 1262 (11th Cir. 2013), *cert. denied*, No. 12-1409, 81 U.S.L.W. 3692 (Oct. 7, 2013); *In re Grand Jury Subpoena*, 696 F.3d 428 (5th Cir. 2012); *In re Special February 2011-1 Grand Jury Subpoena Dated September*

12, 2011, 691 F.3d 903 (7th Cir. 2012), *cert. denied*, No. 12-853, 81 U.S.L.W. 3413 (May 13, 2013); *In re M.H.*, 648 F.3d 1067 (9th Cir. 2011), *cert. denied*, 133 S. Ct. 26 (2012).

Swiss Bank Program

The investigation and prosecution of offshore tax evasion requires the IRS and the Department to obtain foreign evidence, most often through a tax information exchange agreement or a mutual legal assistance or other treaty. A fundamental issue with respect to obtaining information about accounts located in Switzerland has been the degree to which Swiss law permits disclosure under 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 on October 2, 1996. Swiss banks have often contended, in response to our investigations, that Swiss law prohibits meaningful cooperation. As part of our efforts to obtain information from these banks, the Department and the IRS engaged in a series of discussions with representatives of the Swiss government. Our central focus in these discussions was on obtaining information from the banks that would serve our law enforcement goals of encouraging voluntary disclosure by account holders, prosecuting account holders who fail to come forward, and learning where else in Switzerland and the world U.S. taxpayers attempted to use secret accounts to engage in tax evasion. We also sought to maintain the integrity of pending U.S. law enforcement matters and the ability to prosecute those persons who assisted U.S. taxpayers in evading the law.

On August 29, 2013, the Department announced the Program for Non-Prosecution Agreements or Non-Target Letters for Swiss Banks (the “Program”), which is designed to encourage Swiss banks to cooperate in our ongoing investigations.¹ The Program allows Swiss banks not currently under investigation to come forward to provide cooperation and information in return for the possibility of a non-prosecution agreement or deferred prosecution agreement. Two significant points about the Program should be noted at the outset. First, the Program expressly excludes the fourteen banks, referred to in the Program as “Category 1 banks,” that were previously authorized for investigation in connection with their Swiss banking activity. Second, the Program expressly excludes all individuals. No Swiss banker or professional advisor is offered any sort of protection or immunity, and no account holder is covered by the Program.

There are three categories of banks that are eligible to participate in the Program. “Category 2” banks are those Swiss banks that are not under investigation but believe that they have committed offenses under the Internal Revenue Code, related offenses under Title 18, or

¹ A copy of the Program and the Joint Statement between the Department and the Swiss Federal Department of Finance that accompanied its announcement are attached to this Statement.

offenses relating to the filing of Foreign Bank Account Reports (FBARs), in connection with U.S. related accounts. The information required to be provided by the cooperating banks is extensive, and includes full disclosure of their activities, the names of culpable employees and third party advisors, and the number of U.S. accounts. For those accounts that banks closed after the Department's investigation became public in mid-2008, the Program requires disclosure, on an account-by-account basis, of the number of U.S. persons related to the account, and the nature of that relationship, monthly balances, and monthly transfers into and out of the account. With this information, the Department will be able to pursue any banks in Switzerland that have not come forward. Equally important for our offshore enforcement efforts, we will have solid information with which to target banks in other countries that continue to hold themselves out as potential tax havens. Banks participating in the Program must also cooperate in treaty requests for account records, which Switzerland has committed to process on an expedited basis.

The Category 2 banks will also be required to pay a penalty equal to 20% of the value of all non-disclosed U.S. accounts that were held by the bank on August 1, 2008 (when our investigations were known), increasing to 30% for accounts opened between August 1, 2008 and February 28, 2009 (the month-end following the announcement of the UBS Deferred Prosecution Agreement), and 50% for accounts that were opened after February 28, 2009. The penalty structure is based on the maximum aggregate values of the undisclosed accounts, and is calibrated to reflect both the magnitude of a bank's involvement in the misconduct as well as the willingness of the bank to continue to service undeclared accounts after our law enforcement activities became known. The Department may require a deferred prosecution agreement in cases of extraordinary culpability.

Category 2 banks were required to take the initial step of expressing their intent to participate in the Program no later than December 31, 2013. The Department has received 106 such letters of intent. We caution, in providing this number, against a conclusion that all 106 of these entities will ultimately meet the requirements of the Program. We are reviewing the letters of intent to determine whether each entity has met the preliminary requirements under the Program. A number of banks have stated in their letters of intent that their internal reviews are not complete, and they reserve the right, as is allowed under the Program, to withdraw their letters of intent. Most significantly, the Program requires that the Tax Division be satisfied that each bank seeking relief provides full cooperation under the terms set out in the Program and payment of the required penalty. Even with these caveats, it is clear that a significant number of banks that were previously not on our radar screen have come forward to accept responsibility for their actions and to offer their cooperation in our law enforcement efforts. Every Swiss bank that comes forward to cooperate under the Program represents an opportunity to obtain valuable law enforcement information from a source that is new to the Department's investigations.

The Program also provides for participation by two additional categories of banks. As defined in the Program, “Category 3” banks are Swiss banks that did not commit any violations of U.S. law but want a determination of their present status regarding their activities. These banks may seek a non-target letter from the Department after providing a report by an independent examiner who conducted an internal investigation and additional information as required by the Program. Category 3 banks must also verify the percent of U.S. related accounts held in the bank, and the existence of an effective compliance program. “Category 4” banks are Swiss banks that meet certain criteria for “a deemed Compliant Financial Institution” based on definitions in the Agreement between the United States of America and Switzerland for Cooperation to Facilitate the Implementation of Foreign Account Tax Compliance Act (FATCA) signed on February 14, 2013. These banks may also request a non-target letter after verification of their information and status. Category 3 and 4 banks may request participation beginning on July 1, 2014.

We anticipate that the Program will further our law enforcement goals in several important ways. To the extent that each Swiss bank was aware that other Swiss banks might provide information under the Program concerning interbank transactions, we expected the Program to motivate culpable banks to come forward. We believe that this prediction is borne out by the response to the Program. For several reasons, we also believe the Program is motivating culpable account holders to make voluntary disclosures of their accounts. First, the Swiss banks that participate in the Program will provide detailed information that is calculated to lead to the discovery of U.S. account holders. Second, participating Swiss banks can reduce their penalties by showing that their account holders participated in an announced IRS Offshore Voluntary Disclosure Program or Initiative following notification by the bank of such a program or initiative; there have already been several public reports of communications to account holders by Swiss banks as a result of this provision. Finally, the Program requires cooperating Swiss banks to provide information that may lead our investigations to banks outside Switzerland, which sends a firm message to U.S. taxpayers with undisclosed accounts anywhere in the world that they should be concerned that their banks may be the next to come under investigation, adding to the pressure to disclose now.

When the Department announced the Program, a Joint Statement was also released in which Switzerland represented that “applicable Swiss law will permit effective participation by the Swiss Banks on the terms set out in the Program.” While the disclosures under the Program will not include the identities of the account holders, the banks will be required to cooperate in treaty requests for account records, and in the Joint Statement, Switzerland committed to process these treaty requests on an expedited basis.

The Joint Statement and the Program are important milestones in our efforts to end the ability of U.S. taxpayers to use bank secrecy laws to hide their tax evasion and other crimes and

to bring tax dollars back into the Treasury from around the globe. In addition to enforcement efforts by the Department and IRS, the enactment of FATCA has fundamentally changed the risk/reward equation for those considering hiding money offshore. Further, the Senate's advice and consent to ratification of the Protocol amending the Convention between the United States of America and the Swiss Confederation for the Avoidance of Double Taxation with Respect to Taxes on Income, which was signed on September 23, 2009, would significantly enhance our ability to identify U.S. account holders who use Swiss banks to evade federal tax laws. Under the existing tax treaty, Switzerland will identify U.S. account holders only if we can show that there is a reason to believe that they have engaged in fraudulent conduct under the particular standard of "fraud or the like" in Article 26 of the treaty. In general, it is not enough that we have reason to suspect a U.S. taxpayer of having engaged in criminal tax evasion. Our request must ordinarily be accompanied by what the Swiss courts refer to as allegations of a "scheme of lies." Under the Program, we are placed in as good a position as we have ever been in to meet this demanding standard. The Swiss banks participating in the program are required to assist us by disclosing to us information about the "scheme of lies" that has helped support the systemic problem of tax evasion through the use of secret Swiss bank accounts.

If the Senate were to approve the Protocol with Switzerland, however, we would no longer be limited to obtaining information in circumstances of "fraud or the like." Instead, the Protocol adopts the modern relevance standard that is found in most other income tax treaties and tax information exchange agreements. Under that standard, information would be exchanged between the governments as may be relevant for carrying out the provisions of the tax treaty or the administration or enforcement of the domestic tax laws of the United States and Switzerland. In other words, under the new treaty, not only will assistance be given in tax evasion matters involving fraudulent conduct, but also in ordinary tax examinations. The Program will get us information needed to make effective treaty requests under the currently governing 1996 treaty, but a ratified Protocol would enable us to obtain the maximum benefit possible from the banks' obligation to cooperate under the Program. This Committee's leadership in pursuing Senate advice and consent to ratification of this key protocol would enhance our ability to obtain crucial evidence.

Thank you again Mr. Chairman for the opportunity to appear this morning to discuss our law enforcement efforts and for your strong support of this vital law enforcement matter. We are happy to answer any questions that you or the other Members of the Subcommittee may have.