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Special Report – US-Swiss agreement puts Swiss banks, US correspondents and FBAR non-filers at great risk

US will get volumes of data on US persons, institutions under 'Non-Prosecution, Non-Target' accord

It is the most far-reaching, expensive and ominous set of obligations, conditions and hazards ever imposed on a nation's banking industry.

Apart from its revolutionary requirements, the most startling aspect of the August 29 agreement between the US Department of Justice and the Federal Department of Finance of Switzerland is that it is a United States creation. It reflects the long-standing desire of the US to end the decades-long practice of Swiss banks, supported by their government, of providing safe haven for US tax evaders through a wall of secrecy and a "don't ask, don't tell" policy.

This secrecy and these related banking practices now seem to have come to an end, thanks to an astounding agreement that leaves all Swiss banks without a place to hide. Switzerland is the world's largest offshore banking center and controls about 30% of global cross-border banking.

The US-Swiss agreement takes the form of a plea agreement as signified by its name, "Program for Non-Prosecution Agreements or Non-Target Letters for Swiss Banks." It was signed for the United States by the US Department of Justice, not by the US Treasury Department, implying that US scrutiny of Swiss banks has progressed from tax matters to prosecution concerns.

If it functions as the US government hopes it will, the agreement could serve as a template for similar documents with other nations that are tax secrecy havens.

'Watershed' moment in US tax evasion crackdown

Daniel Levy, a former federal prosecutor in the Southern District of New York, led the successful 2012 prosecution of the Swiss bank, Wegelin & Co. Now a principal at McKool Smith, in New York, he told ACFCS, "The announcement of the agreement is a watershed moment in the efforts by the Department of Justice to root out tax evasion."

The 274-year-old Wegelin & Co., Switzerland's oldest bank, closed its doors after the US conviction and paid more than $60 million in forfeitures and restitution to the Internal Revenue Service for lost tax revenues from its scheme to lure customers for US tax evasion purposes.

US-Swiss agreement has dangerous signals for US institutions, persons

The new US-Swiss agreement is ominous for US financial institutions, US persons and the intermediaries who guided the US persons, who will all be disclosed to the United States if they are connected with "US Related Accounts" that they maintain.

This exposes the institutions and persons to possible prosecution for conspiracy to commit US tax evasion and, for the individuals, failing to file the Foreign Bank Account Report. Known as the FBAR, the form must be filed by persons who maintain accounts in another country that exceeded more than $10,000 at any time in the prior year. The FBAR is required by the US Bank Secrecy Act and not the tax laws. The BSA is enforced by the US Treasury Department's Financial Crimes Enforcement Network (FinCEN), which may impose its own penalties.

Strong probability not all funds in Swiss accounts were from US tax evaders

There is a major probability that the US persons who have or had accounts at Swiss banks were not all just tax evaders, but who also are or were hiding the proceeds of crimes committed in the United States, such as public corruption, fraud, money laundering and others. These persons now have a higher probability of being prosecuted for these crimes and of having their Swiss money be the subject of asset recovery efforts by the US government or private sector victims.

In any case, all US persons who are Swiss account holders will have to answer to the IRS, which has a wide array of tools to determine the source and destination of funds. In a statement announcing the agreement, Deputy Attorney General, James M. Cole said, “Now is the time for all US taxpayers who hid behind Swiss bank secrecy laws or have undeclared offshore accounts in other… countries to come forward and resolve their outstanding tax issues with the United States.”

US says it may use Swiss data for enforcement, regulatory actions

The new agreement makes clear that "personal data provided by the Swiss banks... will be used and disclosed only for purposes of law enforcement (which may include regulatory action) *[sic]* in the United States or as otherwise permitted by US law."

The agreement is closely aligned to the Foreign Account Tax Compliance Act. Various references to FATCA appear in the “Definitions” section, such as the definition of "US Related Accounts," which is the same as FATCA’s definition.

Banks have three doors to get softer US treatment

The agreement marks four doors by which three categories of Swiss banks may find their way to softer treatment by the US. One category of Swiss banks, Category 1, is told the door to laxer US treatment is

closed because they are under US criminal investigation. The US Justice Department has said 14 banks now fall in Category 1.

The four categories of banks and their treatment follow:

- **Category 1 Bank:** Any Swiss bank under criminal investigation by the US Justice Department as of August 29, 2013. This type of bank is not eligible to participate in the program.
- **Category 2 Bank:** Any Swiss bank that has “reason to believe” it may have committed tax or "monetary transaction offenses" under the US Code, but against which the US Department of Justice has not commenced a "formal criminal investigation." This type of bank may request a Non-Prosecution Agreement (NPA).
- **Category 3 Bank:** Any Swiss bank that has not committed any tax or monetary transaction offenses under the US Code. This type of bank may request a "Non-Target Letter" from the US Department of Justice.
- **Category 4 Bank:** Any Swiss bank that is considered a “Deemed Compliant Financial Institution” as a “Financial Institution with Local Client Base” under FATCA, meaning a local Swiss bank. This type of bank may request a "Non-Target Letter" from the US Department of Justice.

Road to US salvation for Category 2

A Category 2 bank must take 10 steps to request and obtain a Non-Prosecution Agreement, including sending a letter to the US Justice Department's Tax Division committing itself to full compliance with the agreement's requirements within 120 days. The bank must identify and name an "Independent Examiner," promise to keep all pertinent records, and waive the statute of limitations.

A Non-Prosecution Agreement means the Justice Department will not prosecute the bank "for any tax-related " or Bank Secrecy Act offenses linked to the US Related Accounts.

Swiss banks must tell all

A Category 2 bank must "fully" disclose to the Justice Department how it ran its "cross-border business for US accounts," how it was "structured, operated, and supervised," the names of the persons who ran the business, how it "attracted and service account holders," and all US accounts and their "maximum dollar value" at certain key dates.

The bank must also make an "in-person presentation and documentation" providing full details of its operations in English. It must also disclose the US accounts that were closed, their holdings, and identify the "US person or entity affiliated… with each account," including their "beneficial interest." The bank must promise to cooperate in treaty requests by the US for information on the US accounts.

The banks must also tell the US "the name and function of any relationship manager, client advisor, asset manager, financial advisor, trustee, fiduciary, nominee, attorney, accountant, or other individual or entity known to be affiliated with (the accounts)."

It must also provide "information on the transfer of funds into and out of the account on a monthly basis," including cash deposits or withdrawals; if an intermediary, such as a financial adviser, attorney, accountant or others, facilitated transfers; the identity and location of financial institutions that transferred or received funds from the account, and the countries "to or from which funds were transferred."

'Independent Examiner' requirement is consultants' goldmine

The agreement presents a goldmine for lawyers, accountants and others who may be hired as "Independent Examiners." It requires the Swiss banks to hire them in virtually all instances. The Independent Examiners must verify the actions and information-gathering processes of the banks concerning their US accounts. They must also confirm that the Swiss banks met the due diligence standards of the agreement in gathering and producing pertinent information.

The Swiss banks must keep for 10 years pertinent records "relating to their US cross-border business" and, if requested, provide witnesses and information for US treaty requests for other information and documents.

The banks must close the accounts of "recalcitrant account holders," as defined by IRS regulations and prevent employees from "assisting recalcitrant account holders."

Stiff penalties of 20% to 50% of full account balances

To add sting to the agreement, the banks must pay penalties of 20% of the "maximum aggregate dollar value" of all US Related Accounts they held on August 1, 2008, which was, generally, when the UBS US tax evasion conspiracy was exposed.

They must pay 30% of the "maximum aggregate dollar value" of the US accounts opened between August 1, 2008, and February 28, 2009 and 50% of US accounts opened after February 28, 2009.

If a Swiss bank provides "materially false, incomplete, or misleading" material or violates the NPA, the US Justice Department may deny or rescind an NPA. It also "may pursue any and all legal remedies..., including investigating and instituting criminal charges…."

Category 3 banks follow different path for 'Non-Target Letter'

Category 3 banks take a different route to soft treatment by the US. They may request a so-called "Non-Target Letter," a process that starts with a letter to the Justice Department between July 1, 2014 and October 31, 2014. In the letter, a bank must show how it will comply with the agreement

within 120 days, identify and state the qualifications of its Independent Examiner, agree to keep all compliance records, and waive application of the statute of limitations.

If a Category 3 bank finds "belatedly" and in "a timely and good faith manner," that it should have requested an NPA under Category 2 instead of Category 3, the Justice Department may "enter into discussions with the Swiss Bank as if the Bank had timely requested an NPA...."

Independent Examiner must bare all findings

A Category 3 bank must also hire an Independent Examiner to perform an "independent internal investigation" and verify "the percent of the Bank's account holdings and assets that are US Related Accounts." The examiner must verify the Bank has an effective compliance program, describe the program, and submit "a report of (its) internal investigation, in English."

The Examiner must disclose the witnesses she/he interviewed and summarize what each witness provided, identify the files reviewed and state findings and conclusions.

A Category 3 bank must keep for 10 years all notes, correspondence and other documents that were prepared by, or provided to, the Examiner. It must close accounts of recalcitrant customers and prevent its employees from helping these customers conceal or transfer funds. The Justice Department may grant a Non-Target Letter within nine months of the Examiner's report if it is satisfied the bank followed the stated procedures.

The US Justice Department may pursue criminal charges and other legal actions against a bank that submits "materially false, incomplete or misleading information or evidence."

Category 4 banks have easiest road to travel

Category 4 banks hold the least-threatening status under the US-Swiss agreement. They may obtain a Non-Target Letter after sending a letter to the US Justice Department stating how they will comply with the agreement's requirements, and identify their Independent Examiners, promise to keep all pertinent compliance records and waive the statute of limitations.

The Department of Justice may take legal action, including criminal prosecution, against a bank that submits materially false or misleading information, has "materially" violated the terms of "any" agreement with the US or "otherwise demonstrates criminal culpability."

US-Swiss accord comes 124 days before FATCA takes effect

The US-Swiss agreement is a landmark in multinational tax and law cooperation and enforcement. The fallout it causes, through cases by US agencies against US financial institutions and individuals and similar US pressures on other tax havens, may occupy headlines and fill court dockets for years.

The Swiss Federal Department of Finance said in a statement on August 29 that, “Banks that decide to participate in the US programme *[sic]* will have to ask the Federal Council for individual authorisation *[sic]* in accordance with… the Criminal Code.” The US-Swiss agreement does not state what consequences from the US government await banks that do not participate in the program.

"What remains to be seen is how many banks will participate in the program when the price of a resolution for them – 20% to 50% of the undeclared assets – is a heavy one to pay,” Daniel Levy of McKool Smith, in New York, told ACFCS.

Meanwhile, FATCA, the other international dragnet from the United States approaches implementation on June 1, 2014.

Bank secrecy and tax secrecy havens may not disappear quietly, but signs of their demise are unmistakable, thanks to the remarkable US-Swiss agreement and the coming days of FATCA.

Resources:

Signed Joint Statement and Program for Non-Prosecution Agreements and Non-Target Letters for Swiss Banks

US Justice Department Statement from August 29, 2013

Swiss Federal Department of Finance Statement from August 30, 2013

Final FATCA Regulations from US Internal Revenue Service