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Foreign Banks and Bankers Face New Risks From Swiss Bank Amnesty

The first non-prosecution agreement signals expanded US tax enforcement opportunities at home and abroad.

The US Department of Justice (DOJ) has announced the first non-prosecution agreement (NPA) with BSI, SA, (BSI) one of Switzerland's largest banks, under its Swiss Bank Program. The NPA illuminates the Swiss banking community's struggle to comply with US tax laws. The agreement reveals the machinations of US clients and a web of facilitators, and directs US authorities to other financial institutions throughout the world that transferred funds into secret accounts or accepted the funds of US accountholders fleeing Switzerland after 2008. The DOJ and the Internal Revenue Service (IRS) have vowed to "follow the money" in pursuit of additional investigations of both banks and individuals.

The Non-prosecution Agreement

On March 30, 2015, the DOJ announced its execution of a NPA with BSI. This is the first Swiss bank to reach resolution under the Swiss Bank Program launched in August of 2013 by the DOJ and the Swiss Government. The Program focused on Swiss banks not then already under investigation who had reason to believe they may have violated US tax laws in connection with undeclared US-related accounts. The DOJ invited such "Category II" banks to apply by year-end 2013 to participate and begin the process that would lead to full disclosure of their cross-border activities and payment of penalties in exchange for a non-prosecution agreement.

BSI was one of 106 applicants to the Program. Under the NPA, BSI admitted responsibility for its activities in assisting US taxpayers in hiding assets abroad (as described in a detailed Statement of Facts appended to the NPA), paid a penalty of US$211 million and agreed to cooperate fully with US authorities (both federal and state) in law enforcement and civil proceedings that may arise as a result of the bank's disclosures. The bank's cooperation and commitments under the agreement will continue for a period of four years.

The bank has disclosed broad categories of information under the Program, including the total number and maximum aggregate dollar value of US-related accounts existing on, as well as opened or closed after August 1, 2008. The date is when Swiss bank UBS AG (UBS) first announced that US tax authorities had launched a criminal investigation against it. Thus, August 1, 2008 marks the time when the Swiss banking community was arguably on notice that US law enforcement would not tolerate assisting US persons with concealing accounts abroad. Now that BSI's NPA has been executed, more detailed information concerning each account closed since August 2008 must be disclosed, including:

- The number of US persons or entities affiliated with the account
- The name in which the account was held
- The identity and function of all known managers, advisors and fiduciaries

- Whether funds were deposited or withdrawn in cash
- Information concerning transfers into and out of the account
- Whether such transfers occurred through an intermediary
- The identity (and location) of any financial institution that transferred funds into or received funds from the account

BSI also committed to assist the DOJ with US treaty requests designed to identify US accountholders with undeclared accounts. BSI also committed to close as soon as practicable all dormant US-related accounts as well as the accounts of "recalcitrant accountholders," *i.e.,* those who refuse to provide requested information or a waiver permitting disclosure thereof. The bank must prevent its employees from assisting in acts of further concealment and must ensure any new accounts will be declared and subject to disclosure (as is required under the Foreign Account Tax Compliance Act (FATCA), implemented July 1, 2014).

In a DOJ Press Release accompanying the announcement of the NPA, Acting Deputy Attorney General Sally Quillian Yates emphasized the Swiss Bank Program is a rich source of further investigative leads for US tax authorities: "When we announced the program, we said that it would enhance our efforts to pursue those who help facilitate tax evasion and those who use secret offshore accounts to evade taxes. And it has done just that. We are using the information that we have learned from BSI and other Swiss banks in the program to pursue additional investigation into both banks and individuals."[1]

Since 2009 the US DOJ has charged more than 100 offshore bank accountholders, facilitators and financial institutions, and has collected over US$7 billion in fines. The DOJ's related enforcement efforts to date have involved banking and financial services activities not only in Switzerland, but in India, Luxembourg, Liechtenstein, Israel, the Caribbean, Belize, Panama and beyond. IRS-Criminal Investigation (CI) Chief Richard Weber commented, "Fighting offshore tax evasion continues to be a top priority for IRS-CI and *we will trace unreported funds anywhere in the world* [to] enforce our country's tax laws…."[2]

The Risks of the "Flawed Exit"

The Statement of Facts accompanying BSI's NPA reveals what is likely to become a familiar pattern as other Swiss banks finalize the terms of their agreements with the DOJ, which the DOJ hopes to conclude by the end of the year. The Statement describes how, through mid-2008, BSI had a thriving cross-border business that led to the opening of approximately 3,500 US-related accounts, many of which were undeclared, holding as much as US$2.78 billion. The Statement further details the bank's gradual and imperfect attempts to end the offending practices, efforts which were not fully effective until the end of 2012. Ongoing and anticipated US enforcement efforts will focus on conduct during this period by accountholders, bankers and the global banking community.

BSI admitted to avoiding disclosure and withholding requirements imposed under US law by permitting US clients to open accounts using sham offshore business entities, including offshore corporations, trusts and sham insurance companies. These entities would falsely certify on IRS forms that they, and not the US clients, were the beneficial owners of the accounts. The bank offered accounts identified by code names or numbers and arranged to hold mail and deliver account records via personal client visits. BSI also issued pre-paid debit cards to assist US clients with surreptitiously repatriating funds from their undeclared accounts. In some instances, these cards bore no client name, and the client could access additional funds by communicating with the bank using code phrases such as "could you download some tunes for us."

Although BSI was aware of the US crackdown on UBS as of August 2008 and began monitoring the situation, the policies BSI implemented in response allowed the continued opening and maintenance of undeclared US-related accounts for several years thereafter. Pursuant to policy changes implemented in late 2008 and 2009, BSI at first restricted undisclosed accounts for US clients to those over a certain asset threshold that held no US securities and were serviced by external asset managers (EAMs); new accounts required the approval of senior management, and the bank mandated "hold mail" services for such accounts. Not until late 2010 and 2011 did BSI implement more restrictive and effective measures that prohibited opening new undeclared accounts and required closing existing undeclared accounts by the end of 2012.

The bank's "flawed exit" from its cross-border activities in part gave rise to the substantial penalty it paid in connection with the NPA. Under the Program the penalty is calculated (after taking into account certain mitigating criteria) as 20 percent of the aggregate undisclosed account value for US-related accounts existing on August 1, 2008, increasing to 30 percent for accounts opened thereafter and reaching 50 percent for accounts opened after February 2009. In addition, this murky period from mid-2008 through 2014 — when major Swiss banks were forcing out US clients — presents serious and continuing investigatory risks and exposure for other foreign banks that may have accepted funds transferred out of BSI and other Swiss institutions at the time and for those accountholders who have not come forward under the IRS Offshore Voluntary Disclosure Program (see links to related Client Alerts below), their bankers and other advisors.

Focus on Financial Institutions "Beyond Switzerland"

The Swiss Bank Program's requirements include a critical focus on other financial institutions that may have facilitated concealment of US taxpayer's assets abroad. In this regard, upon the execution of the NPA, a bank must provide information concerning the transfer of funds into and out of the subject accounts during the period from August 1, 2008, through the end of 2014. The required information includes whether an intermediary was used (and the identity thereof), and the identification and domicile of any financial institution that transferred funds into or received funds out of the bank, as well as the country to or from which the funds were transferred. US law enforcement will likely find this information in particular a fertile source of leads to financial institutions outside of Switzerland and around the world.

According to a Swiss private banking study which PwC conducted in mid-2014, approximately US$273.3 billion was repatriated or transferred to another financial center after August 1, 2008.[3] The disclosures required under the Swiss Bank Program NPAs will inevitably lead investigators directly to those other financial centers. Having already targeted a number of Swiss banks and one Israeli bank, the DOJ and the IRS acknowledge other ongoing investigations around the globe, but have not specifically identified where their efforts will be focused next. Many Swiss banks have operations in the Caribbean, the Channel Islands, Dubai and Hong Kong, and a recent analysis of major source countries for secret Swiss accounts prior to 2008 also identified locations throughout Europe, South America and the Middle East.[4]

Banks that may be at risk with respect to transfers into or out of Switzerland for US clients over the last seven years should be aware that Swiss banks participating in the Program will transmit vast volumes of relevant data over the next year to US authorities, who have vowed to "follow the money" anywhere in the world.[5]

Executives and Professionals Remain Exposed

Obviously, BSI's NPA (and the dozens that will follow) will lead to the identification and pursuit of those US accountholders still trying to avoid detection. Also, notably, in one of the key features of the Swiss Bank Program, the agreement provides non-prosecution protection only for the banking institution and

specifically excludes any individuals. Yet the agreement requires the bank to reveal the identities of all individuals or entities known to be affiliated with the subject accounts, including any relationship manager (RM *i.e.* private banker), client advisor, asset manager, financial advisor, trustee, fiduciary, nominee, attorney, accountant, or other individual or entity functioning in a similar capacity.

In connection with the approximately 3,500 accounts at issue, the BSI Statement of Facts describes the activities of approximately 265 RMs who served as the primary contact for US accountholders and who affirmatively assisted in concealing the clients' beneficial ownership in the accounts. The bank has also identified approximately 198 EAMs (many employed by other Swiss banks) who referred clients for a fee and independently managed one or more US-related accounts. Under the NPA, BSI has pledged to facilitate truthful statements and testimony of its officers, directors, employees, agents and consultants in a variety of US law enforcement proceedings.

Since 2009, the DOJ has prosecuted more than 30 foreign bankers and other facilitators and likely will continue to pursue additional investigations of this type. In its press release, the DOJ acknowledges that not all individuals identified through the Swiss Bank Program are culpable. However, Acting Assistant Attorney General Caroline D. Ciraolo of the DOJ Tax Division urges individuals with "concerns regarding their potential criminal liability to contact and fully cooperate with the department."[6]

Next Steps

Cognizant of the character of information now making its way to US tax authorities via the Swiss Banking Program, financial institutions and financial service providers outside Switzerland and throughout the world need to evaluate their potential exposure for conduct vis à vis US persons as far back as 2008 and prepare for possible DOJ or IRS inquiries. This analysis must include assessing risks to the institution and risks both for and from its current and former executives, employees and consultants. Financial institutions and financial service providers should consider proactive strategies for approaching US authorities in advance of investigatory or enforcement actions.

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Endnotes

1 *BSI SA of Lugano, Switzerland, is First Bank to Reach Resolution Under Justice Department's Swiss Bank Program*, DOJ Office of Public Affairs Press Release (Mar. 30, 2015) (DOJ Press Release).

2 *Id.* (emphasis added).

3 *Private Banking Switzerland: From Yesterday to the Day After Tomorrow*, PwC (Aug. 2014).

4 *Swiss Leaks – Globalized Finance*, Washington Post (Feb. 18, 2015).

5 Of course, the US is not alone in its expanded efforts to combat offshore tax evasion around the globe. The UK, France and Germany, among others, have announced similar high-profile tax investigations of financial institutions.

6 DOJ Press Release.