For years, a number of American citizens have opened banking and brokerage accounts in what are known as "offshore" jurisdictions. That moniker probably comes from many of these jurisdictions being islands not far from the American coastline, but in fact any foreign country is considered offshore for the purposes of the *Internal Revenue Code*.

It is not illegal now, nor has it ever been, for an American citizen to open a bank account in a foreign country; or to own assets denominated in currencies other than US dollars; or to generally engage in financial transactions in places other than the United States. However, what ***is*** illegal is not to report this activity to the IRS. Unlike just about every other industrialized country, American tax laws mandate that individuals required to file an income tax return must report all income, from any source, wherever located, to the IRS. Whereas an Italian citizen, for example, could escape the reach of Italian income taxes by conducting all her business and having her investments outside of Italy, an American gains no tax advantage by keeping everything outside the United States, because the *Internal Revenue Code* taxes the American's income on a ***world-wide*** basis.

Nevertheless, Americans have moved money outside the United States for years. Often, the move is as benign as the American retiree in Costa Rica who opens a Costa Rican bank account for convenience purposes. But, according to the IRS and law enforcement agencies around the world, much off shore banking activity is done by people whose motives are considerably more suspect – criminals, terrorists and others wishing simply to hide money -- from everybody – including the taxing authorities. Many offshore jurisdictions have historically had banking laws making all financial transactions secret. Some jurisdictions make it an offense under their laws even ***to inquire*** about another person's banking activity. It is against this backdrop that not just the American government and the IRS, but the entire international community, has become much more serious about penetrating the world of secret financial transactions. So, what at one time appeared to be a significant wall of secrecy for these accounts has crumbled, as the international community increases efforts to stem financial secrecy through treaties, jaw-boning and targeted legal actions.

The reality is that any American who has unreported income from a foreign source ought to be worried, as no one can rely any longer on bank secrecy laws in foreign jurisdictions. In May of this year, the United States Justice Department brought charges against a former UBS banker and a Liechtenstein consultant alleging they helped American citizens avoid paying income taxes. The United States is also probing Liechtenstein's long-standing reputation as a haven for U.S. tax cheats, as the IRS has confirmed it is investigating at least 100 U.S. taxpayers who have accounts in Liechtenstein. But a taxpayer should not think the coast is clear because of the lack of a Liechtenstein connection. It has been estimated that offshore tax evasion costs the U.S. Treasury at least $100 billion annually, and the IRS is absolutely intensifying its activities in this area, and all of the well-known offshore jurisdictions are being scrutinized.

If a taxpayer finds himself in the bind of having unreported income from an account in an offshore country, what should he do? The very first thing is to retain an attorney who is well versed in criminal tax matters. Then, the course of conduct to be followed must be chosen. I think there are only three choices: doing nothing and hoping you're

never discovered; or filing amended returns without fanfare; or simply giving up outright. All of these choices have limitations.

The last option mentioned, giving up, will typically involve approaching the IRS on an anonymous basis, initially, to test the waters. If the unreported income is not from an illegal source, such as bribery or fraudulent activities, this can make sense as long as the taxpayer's offshore activities have not been discovered and she is willing to pay all that is owed. However, if the unreported account contains illegal money, then voluntary disclosure is not an option. Also, voluntary disclosure does not offer a guarantee against prosecution, but it generally puts the taxpayer in a favorable light.

Making amended returns, either one year at-a-time, or all at once, is a favorite ploy of many tax professionals, as it seeks to exploit the crush of information the IRS must process all the time, and it hopes the amended returns will pass through the system virtually unnoticed. This strategy can be a good idea because paying all that is owed voluntarily and filing returns correctly may discourage criminal prosecution if the previous improper conduct is discovered. On the other hand, by filing the amended return(s), the taxpayer is making an affirmative statement that the previous return(s) were erroneous – never a good litigating position.

Doing nothing and hoping it all goes away is probably the worst course of conduct, but one that many taxpayers favor because they just think the IRS will never catch them. But with the heightened activity on secret accounts, it appears it is only a matter of when the IRS will catch up with the tax cheat, not if. Once caught, the IRS is likely to unleash its full fury on a taxpayer it feels has thumbed his nose at the system.

However, the heightened level of scrutiny of offshore accounts does not mean that placing money in a foreign account – even in a so-called tax haven jurisdiction – should never be done. Serious financial and asset protection planning for wealthy Americans often involves the utilization of foreign accounts and foreign business entities. As America continues to foster a litigious environment, many high net worth individuals realize an excellent way to establish protection against creditors is to take advantage of the legal protection available in some foreign jurisdictions. Also, various investment products and opportunities may be available overseas that are not available domestically.

Accordingly, there may be valid, legal, reasons for your client to conduct financial activities overseas. Just make certain that the client (and ***you***) understand the rules – all of them – particularly the disclosure rules -- and that they be followed!

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