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The Tide Is Coming In on Offshore Account Enforcement: The Swiss Bank Program and Enforcement of the Foreign Bank Account Report

W. Bradley Russell*

More than a hundred Swiss banks have entered the Department of Justice's Swiss Bank Program and thereby signaled their willingness to provide their American depositors' account information to U.S. authorities under the U.S.-Swiss tax treaty. Once the treaty requests are filled, and American depositors are unmasked, U.S. authorities will undoubtedly begin pursuing civil and criminal penalties against Americans with undeclared accounts. The author of this article discusses the Bank Secrecy Act, the Foreign Bank Account Report, recent enforcement actions, and the Swiss Bank Program, which he believes is likely to greatly increase the number of civil and criminal enforcement actions against Americans with undeclared offshore accounts.

Since the 1970s, Americans have been required to report their offshore financial accounts to the government.[1] However, compliance has been spotty for most of this time.[2] In the last dozen years, though, the government has been trying to improve compliance. The Internal Revenue Service ("IRS") has conducted several amnesties—the IRS calls them offshore voluntary disclosure programs—under which Americans could voluntarily disclose their offshore

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1 *See California Bankers Ass'n v. Shultz*, 416 U.S. 21, 2526, 35 (1974) (describing enactment in 1970 of Bank Secrecy Act and regulations promulgated thereunder requiring Americans to report foreign financial accounts). Title 31 U.S. Code § 5314 authorizes the Secretary of the Treasury to require citizens and residents to report their foreign accounts. And the Secretary promulgated a regulation requiring citizens and residents to file annual reports of their foreign bank accounts. 31 C.F.R. § 1010.350.

2 The Treasury Department determined in 2001 that compliance could be less than 20 percent. *See* Report to Congress in Accordance with § 361(b) of the USA PATRIOT Act at 6 (Apr. 26, 2002). The Treasury Department estimated that there may be as many as one million U.S. taxpayers required to report their foreign accounts. *Id.* But only 177,000 Americans filed reports in 2001. In 2011, 618,000 Americans filed reports of foreign accounts. Government Accountability Office, *Offshore Tax Evasion*, GAO-13-318 at 27 (Mar. 2013). Assuming a million Americans were required to file, the compliance rate was still barely above 60 percent in 2011.

accounts in exchange for reduced penalties and protection from criminal prosecution. And in 2008, the IRS sought to obtain information on American account-holders from the Swiss bank UBS.[3] The government's efforts against UBS ultimately led to changes in the tax cooperation treaty between the United States and Switzerland, making it easier for U.S. authorities to get bank account information out of Switzerland.

But what could be the most effective mechanism for improving compliance—or ominous development, depending on one's perspective—is just now coming into its own. The Department of Justice Tax Division created the Swiss Bank Program in August 2013, to allow Swiss banks to cooperate with the government in exchange for protection from criminal prosecution.[4] The program proceeds in two stages. First, the Swiss bank comes forward and discloses certain general information about accounts held by Americans. The Americans' identities are not yet revealed in this first stage. At the second stage, the government and the bank enter a non-prosecution agreement, and the bank cooperates with the government to formulate requests for details about American account-holders under the tax cooperation treaty with Switzerland. When these treaty requests are honored, the Americans' identities will be revealed. More than a hundred Swiss banks have entered the program,[5] and the very first one entered the second stage at the end of March of this year.[6] The second bank signed a non-prosecution agreement and entered the second stage on May 8 of this year.[7] By early August, 24 other Swiss banks signed non-prosecution agreements. Even more banks in the Swiss Bank Program will likely sign non-prosecution agreements in the near future, and begin cooperating with U.S. government efforts to identify their American account-holders.

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[3] *See* Ex Parte Petittion, *In re Tax Liabilities of John Does*, No. 1:08-mc-21864 (S.D. Fla. June 30, 2008).

[4] *See* Program for Non-Prosecution Agreements or Non-Target Letters for Swiss Banks (Aug. 29, 2013).

[5] David Voreacos, *Swiss Banks Seek Tax Amnesty as Third Accept U.S. Offer*, Bloomberg (Jan. 27, 2014).

[6] Chad Bray, *BSI Becomes First Swiss Bank to Settle Under D.O.J. Disclosure Program*, N.Y. Times (Mar. 30, 2015); *see also* Department of Justice, *BSI SA of Lugano, Switzerland, Is First Bank to Reach Resolution Under Justice Department's Swiss Bank Program* (Mar. 30, 2015) (press release).

[7] Department of Justice, *Vadian Bank AG Reaches Resolution Under Department of Justice Swiss Bank Program* (May 8, 2015) (press release).

THE BANK SECRECY ACT AND THE OBLIGATION TO FILE A FOREIGN BANK ACCOUNT REPORT

Congress passed the Bank Secrecy Act in 1970 in part "to furnish American law enforcement authorities with the tools necessary to cope with the problems created by so called secrecy jurisdictions."[8] Congress authorized the Treasury Secretary to require "a resident or citizen of the United States or a person in, and doing business in, the United States," to report his foreign bank accounts.[9] The Treasury Secretary promulgated a regulation requiring U.S. citizens, residents, and legal entities to file a Treasury Department form called the "Report of Foreign Bank and Financial Accounts."[10] This form is often referred to as the FBAR, for Foreign Bank Account Report. The FBAR used to bear the designation TD-F 90-22.1, and that is the designation referenced in the regulation. Since 2013, however, the form has been designated FinCEN form 114.[11]

The regulation establishing the FBAR is codified at 31 C.F.R. § 1010.350. This regulation requires each "United States person having a financial interest in, or signature authority over, a bank, securities, or other financial account in a foreign country" to report the account to the IRS each year.[12] A "United States person" is a citizen of the United States, a resident of the United States, or an entity formed under the laws of the United States, a state, or a U.S. territory.[13] All types of financial accounts must be reported—even including certain annuities and insurance policies.[14]

A person has a financial interest in an account, and therefore must file an FBAR, if he is the owner of record or has legal title to the account.[15] Thus an

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[8] H.R. Rep. No. 91-975 (1970), *reprinted in* 1970 U.S.C.C.A.N. 4394, 4404. The House of Representatives report further noted that some bank secrecy jurisdictions "simply do not recognize cheating on taxes, violations of securities laws, and many other acts as criminal. Neither their law enforcement authorities nor their banking institutions will afford the slightest cooperation to American authorities." *Id.*

[9] 31 U.S.C. § 5314.

[10] 31 C.F.R. § 1010.350.

[11] *See* Financial Crimes Enforcement Network, BSA Electronic Filing Requirements for Report of Foreign Bank and Financial Accounts (FinCEN Form 114) (June 2014), *available at* www.fincen.gov.

[12] 31 C.F.R. § 1010.350(a).

[13] 31 C.F.R. § 1010.350(b).

[14] 31 C.F.R. § 1010.350(c).

[15] 31 C.F.R. § 1010.350(e).

owner of record must file an FBAR even if the account is held for the benefit of another person.[16] An American who has a beneficial interest in an account must also file an FBAR, as must an American who owns more than half of an entity that itself owns an account.[17] Additionally, an American who has signature authority over an account must file an FBAR.[18] Thus, a corporate officer who has no personal interest in a corporate bank account must file an FBAR if he is on the signature card for that account. Clearly, this regulation errs on the side of over-reporting. It is easy to envision a situation in which multiple FBAR's would be required for a single foreign bank account.

The regulation prevents Americans from creating entities to evade the FBAR requirement. It provides, "A United States person that causes an entity . . . to be created for a purpose of evading this section shall have a financial interest in any bank, securities, or other financial account in a foreign country for which the entity is the owner of record or holder of legal title."[19]

Some important FBAR rules are contained not in the statute or even the regulation, but in the instructions to the FBAR form.[20] These provide that an American must file an FBAR only if he has foreign accounts whose total balance exceeds $10,000 at any time during the year and that the FBAR is due on June 30 of the year following the year reported.[21]

The IRS has been delegated authority to investigate criminal violations and enforce civil penalties.[22] Both civil and criminal penalties for FBAR violations are harsh. The criminal penalty for willfully failing to file an FBAR is up to five years' imprisonment and a $250,000 fine.[23] And if the failure to file is connected to other criminal activity, the maximum criminal penalties rise to ten years' imprisonment and a $500,000 fine.[24]

Despite the harsh maximum penalties, many defendants have received fairly lenient criminal sentences for FBAR violations. One convicted FBAR violator,

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[16] *Id.*

[17] *Id.*

[18] 31 C.F.R. § 1010.350(f).

[19] 31 C.F.R. § 1010.350(e)(3).

[20] *See* Financial Crimes Enforcement Network, BSA Electronic Filing Requirements for Report of Foreign Bank and Financial Accounts (FinCEN Form 114) (June 2014), *available at* www.fincen.gov.

[21] *Id.*

[22] 31 C.F.R. § 1010.810.

[23] 31 U.S.C. § 5322(a).

[24] 31 U.S.C. § 5322(b).

H. Ty Warner, the creator of the popular Beanie Babies toy, studied the recent sentences handed down in FBAR cases in an effort to obtain a lenient sentence for himself. He found that 63 percent of defendants received no sentence of incarceration, although some of these were sentenced to a period of home confinement.[25] Warner himself was ultimately sentenced to probation,[26] a sentence affirmed on appeal.[27] In another noteworthy case, the U.S. District Court for the Southern District of Florida placed an FBAR violator on probation for only five seconds.[28]

While a felony conviction is itself highly damaging, no matter how lenient the sentence, for many FBAR violators the most significant consequence may be the civil penalty. Under 31 U.S.C § 5321(a)(5), a person who willfully fails to file an FBAR faces a maximum penalty of the greater of $100,000 or half the balance of the account, for each violation. Because an FBAR must be filed annually, this penalty could quickly reach enormous proportions for an individual who has failed to file the FBAR for multiple years. A person who willfully failed to file an FBAR to report a million-dollar Swiss account for six years could face a maximum penalty of $500,000 for each year, for a total penalty of $3 million. The government usually pursues a penalty of half the highest balance of the account, but the government has at times pursued the maximum penalty authorized by § 5321(a)(5).

In the case of *United States v. Zwerner*, the government pursued the maximum penalty of 50 percent of the value of a single account for each of four years.[29] The government sought a penalty in excess of $3 million[30] totaling approximately twice the value of the account. Ultimately, following a jury trial, Zwerner and the government settled for a penalty equal to 50 percent of the value of the account for only each of two years.[31] The government has evidently sought penalties greater than the total value of an individual's foreign accounts

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[25] Defendant's Sentencing Mem., *United States v. Warner*, No. 1:13-cr-731 (N.D. Ill. Dec. 31, 2013).

[26] Judgment, *United States v. Warner*, No. 1:13-cr-731 (N.D. Ill. Jan. 14, 2014).

[27] *United States v. Warner*, No. 14–1330, 2015 U.S. App. LEXIS 11938 (7th Cir. Jul. 10, 2015).

[28] Trans. of Sentencing 16:18–17:2 *United States v. Curran*, No. 12-cr-80206 (S.D. Fla. Apr. 25, 2013) (imposing sentence of one year's probation, and then in the next breath terminating probation).

[29] Complaint, *United States v. Zwerner*, No. 1:13-cv-22082 (S.D. Fla. June 11, 2013).

[30] *Id.*

[31] Notice of Settlement, *United States v. Zwerner*, No. 1:13-cv-22082 (S.D. Fla. June 9, 2014).

in other cases as well. In a motion in limine filed in the Zwerner case, Zwerner asserted the government had provided him statistics in discovery to the effect that the government had imposed FBAR penalties totaling more than the aggregate value of a person's foreign accounts 20 times in recent years.[32] And the government had imposed penalties in excess of *four times* the aggregate foreign account value against "at least 8 persons."[33]

To make out a case for the maximum civil penalty, the United States must prove by a preponderance of the evidence that the defendant willfully failed to file an FBAR.[34] The Supreme Court has said "where willfulness is a statutory condition of civil liability, we have generally taken it to cover not only knowing violations of a standard, but reckless ones as well."[35] The lower federal courts have applied this teaching to FBAR cases.[36] In *United States v. Williams*, the Fourth Circuit found that the defendant's tax return put him on inquiry notice of the FBAR requirement.[37] A line on Schedule B to the tax return called for information about foreign bank accounts, and referred to the FBAR form and its instructions.[38] The defendant never consulted the form or its instructions, and the Fourth Circuit found that this failure, combined with other conduct showing the defendant's desire to conceal financial information, showed that the defendant had been at least reckless.[39] This was enough to support liability for the maximum FBAR penalty. In *United States v. McBride*, the Utah district court followed the reasoning of *Williams* and concluded that a taxpayer is reckless if he ignores the instructions on Schedule B referring to the obligation to file an FBAR.[40] Thus, the federal courts appear to accept the argument that anyone who files a federal income tax return is presumptively willful with respect to the obligation to file an FBAR.

THE SWISS BANK PROGRAM AND THE IMPENDING IDENTIFICATION OF AMERICANS WITH OFFSHORE ACCOUNTS

In 2009, the federal government brought a criminal prosecution in Florida

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[32] Motion in Limine, *United States v. Zwerner*, No. 1:13-cv-22082 (S.D. Fla. Feb. 18, 2014).

[33] *Id.*

[34] *United States v. McBride*, 908 F. Supp. 2d 1186, 1202 (D. Utah 2012).

[35] *Safeco Ins. Co. v. Burr*, 551 U.S. 47, 57 (2007).

[36] *United States v. Williams*, 489 F. App'x 655, 658 (4th Cir. 2012); *McBride*, 908 F. Supp. 2d at 1204.

[37] *Williams*, 489 F. App'x at 659.

[38] *Id.*

[39] *Id.* at 659–60.

[40] *McBride*, 908 F. Supp. at 1211.

against the large Swiss bank UBS, alleging that it had conspired to defraud the IRS by helping Americans maintain undisclosed accounts at UBS.[41] Then, in 2012, the government filed a similar criminal case in New York against another Swiss bank, Wegelin & Company.[42] Unlike UBS, Wegelin never had any branch or office in the United States.[43] Even so, it found itself in criminal court, and ultimately convicted, in the United States. These two prosecutions must have been an unpleasant wake-up call to the banks of Switzerland, which now had to consider whether they were exposed to criminal liability for assisting their American depositors to evade taxes.

In that environment, the Department of Justice Tax Division created the Swiss Bank Program in August 2013. The program allowed Swiss banks with reason to believe they may have committed crimes under U.S. law to request non-prosecution agreements in exchange for cooperation with the federal government.[44] Unsurprisingly, a bank was ineligible if the Tax Division had already authorized a criminal investigation against it when the program was announced.[45] To participate in the program, a bank was required to send a letter to the Tax Division expressing its intent by the end of 2013.[46]

The program itself proceeds in two stages. By now, all banks in the program should have completed their obligations under the first stage. At this first stage, a bank was required to provide information on how it conducted business with its American depositors. It was required to identify the individuals who operated and supervised the business, and it had to describe how it attracted American depositors and serviced their accounts.[47] The bank was even required to make an in-person presentation supporting its disclosure of this information.[48] Additionally, the bank was required to provide the total number and maximum total value of all its American accounts during the last seven years.[49] The bank was required to have an independent examiner verify details about

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[41] Deferred Prosecution Agreement ¶ 2, *United States v. UBS*, No. 0:09-cr-60033 (S.D. Fla. Feb. 18, 2009).

[42] Indictment, *United States v. Wegelin & Co., et al.*, No. 1:12-cr-02 (S.D.N.Y. Feb. 2, 2012).

[43] Sentencing Mem. of Wegelin & Co., *United States v. Wegelin & Co. et al.*, No. 1:12-cr-02 (S.D.N.Y. Feb. 25, 2013).

[44] Program for Non-Prosecution Agreements or Non-Target Letters for Swiss Banks (Aug. 29, 2013).

[45] *Id.*

[46] *Id.*

[47] *Id.*

[48] *Id.*

[49] *Id.*

each American account, which details would then be provided to the government at the second stage.[50] And finally, the bank was required to agree to maintain all relevant records.[51]

At the second stage, which the first banks have just entered, the government and the bank sign a non-prosecution agreement, and the bank discloses additional details about its American accounts. The bank must disclose:

- the maximum dollar value of each account;
- the number of Americans potentially affiliated with each account;
- whether each account was held in the name of an individual or an entity;
- whether each account held any U.S. securities;
- the name of any banker, attorney, trustee, advisor, accountant, or similar individual affiliated with the account; and
- details about the transfer of funds into and out of the account, including identification of any financial institution to which funds were transferred.[52]

Perhaps most significantly, the bank must cooperate with the government's efforts to obtain further account information under the tax treaty between the United States and Switzerland.[53]

The tax treaty between the United States and Switzerland, which was signed in October 1996, originally required the exchange of "such information . . . as is necessary . . . for the prevention of tax fraud or the like."[54] However, in the wake of the United States' effort to obtain information from UBS on its American depositors, the United States and Switzerland agreed to amend their tax treaty to allow a broader exchange of financial information.[55] As amended,

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[50] *Id.*

[51] *Id.*

[52] *Id.*

[53] *Id.*

[54] Convention for the Avoidance of Double Taxation with Respect to Taxes on Income, Oct. 2, 1996, U.S.-Switz., art. 26, S. Treaty Doc. No. 105-8.

[55] The Government of Switzerland filed an amicus curiae brief in the United States' summons enforcement action against UBS. Amicus Br. of Gov. of Switz., *United States v. UBS AG*, No. 1:09-cv-20423 (S.D. Fla. Apr. 30, 2009). In its brief, the Government of Switzerland noted that it had recently begun negotiations with the United States to amend the tax treaty. *Id.* at 9. The United States and UBS stipulated to the dismissal of the summons enforcement case on August 19, 2009. Stip. of Dismissal, *United States v. UBS AG*, No. 1:09-cv-20423 (S.D. Fla.

the treaty requires the exchange of "such information as may be relevant . . . to the administration or enforcement of the domestic laws concerning taxes."[56] This new standard "is intended to provide for exchange of information in tax matters to the widest possible extent without allowing the Contracting States to engage in 'fishing expeditions' or to request information that is unlikely to be relevant to the tax affairs of a given taxpayer."[57] Further, the amended treaty now provides that a contracting state may not "decline to supply information solely because the information is held by a bank, other financial institution, nominee, or person acting in an agency or fiduciary capacity or because it relates to ownership interests in a person."[58] The broad information exchange required by the amended tax treaty should allow United States authorities to obtain the identities and account information of Americans with undeclared accounts at any Swiss bank with a non-prosecution agreement under the Swiss Bank Program.

CONCLUSION

More than a hundred Swiss banks have entered the Department of Justice's Swiss Bank Program and thereby signaled their willingness to provide their American depositors' account information to U.S. authorities under the tax treaty. By early August, 26 banks have signed non-prosecution agreements and entered the second stage of the program. The next step for the U.S. government and these banks is to cooperate in requesting American depositors' account information under the treaty. Once these treaty requests are filled, and American depositors are unmasked, U.S. authorities will undoubtedly begin pursuing civil and criminal penalties against Americans with undeclared accounts. It is likely these enforcement actions will be brought on a much greater scale than the occasional enforcement actions brought in the past. The Swiss Bank Program is thus likely to greatly increase the number of civil and criminal enforcement actions against Americans with undeclared offshore accounts. Foreign account-holders not in compliance with FBAR requirements should be forewarned that the tide is coming in on offshore account enforcement.

Aug. 19, 2009). And the amendment to the tax treaty was signed just a month later on September 23, 2009. Protocol Amending Convention for the Avoidance of Double Taxation with Respect to Taxes on Income, Sept. 23, 2009.

[56] Protocol Amending Convention for the Avoidance of Double Taxation with Respect to Taxes on Income, Sept. 23, 2009, U.S.-Switz., art. 3 (amending art. 26 of treaty).

[57] *Id.* art. 4.

[58] *Id.* art. 3.