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U.S. IRS targets Asia for hidden taxpayer funds in 2016

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The U.S. Internal Revenue Service has identified Asia as one of the destinations for hidden tax payers' funds, and this year along with the Department of Justice, it is expected to track down tax cheats with Asian accounts. Singapore and Hong Kong are the two main financial centres being targeted largely because substantial funds flowed into these two jurisdictions in the wake of U.S. prosecutions of major Swiss banks over their role in helping their clients evade taxes, lawyers said.

The U.S. government has seen much success in obtaining compliance from a large number of Swiss banks through the Swiss Bank Agreement, and it has been able to glean considerable information about the destination of American taxpayers' funds following the closure of their accounts in Switzerland. This has given the U.S. tax authorities the motivation to use their civil and criminal powers to bring hidden funds to light, said Nathan Hochman, partner at Morgan, Lewis & Bockius LLP in Santa Monica, California.

Offshore Voluntary Disclosure Program

Hochman said the IRS and the Department of Justice will be moving aggressively in 2016 to promote the Offshore Voluntary Disclosure Program (OVDP) to U.S. taxpayers with Asian accounts. Since 2009, the OVDP has offered criminal amnesty to U.S. taxpayers if they pay back eight years of their unreported foreign account income tax and interest, and a 20-27.5 percent penalty on the maximum value of their unreported foreign accounts. Through the OVDP, the IRS was able to obtain large amount of data on the workings of taxpayers' foreign accounts.

"To date, over 50,000 U.S. taxpayers have entered the program, paid over \$6 billion and provided a large amount of information about their foreign accounts, banks, bankers, and intermediaries such as financial advisors, lawyers [and] trustees," he said.

The Department of Justice has criminally prosecuted U.S. taxpayers who have chosen not to comply, and to date, over 75 U.S. taxpayers had been convicted and sentenced, and more than 25 foreign bankers and financial advisers had been criminally charged for assisting in tax evasion efforts, according to Hochman. He expects the Department of Justice to continue to use this criminal hammer to prosecute those with Asian accounts but have not come forward to report them.

Finding examples in Singapore and Hong Kong

Daniel Chia, director at Morgan Lewis Stamford in Singapore, said that when the IRS started to crack down on Swiss banks in 2008, a lot of money flowed out of Switzerland into Singapore and Hong Kong. He expects the IRS to start looking for examples in those two jurisdictions which it can then show its intention to the rest of world. The target will not be just the international banks but also the local Asian banks, he said.

"If you look at the pattern for the Swiss banks, the international banks that were targeted were UBS, Credit Suisse. The IRS then started to target the second-tier banks. Bank Wegelin doesn't exist anymore. Will the IRS ignore the second-tier banks and only go after the big fish? No," he said.

Asian Bank Program

Hochman said the Department of Justice may offer an Asian Bank Program modelled after the [Swiss Bank Program](#) to force Asian banks to reveal post-2008 U.S. taxpayer accounts that have not been reported.

"Asian banks that are not willing to enter into such a program will be encouraged to look at Wegelin Bank as to what their fate may hold. Wegelin, the oldest bank in Switzerland, founded in 1741, had survived Napoleon, World War I and II, but not the IRS and DOJ," he said.

Hochman said his prediction that there might be an Asian Bank Program was based on the success of the Swiss Bank Program, in which more than 100 Swiss banks participated. The program allowed U.S. authorities to obtain a significant amount of information about the flow of funds outside of the Swiss banks, and to secure more than \$1 billion in fines.

"Since the U.S. criminal tax statute of limitations is six years from the last date of the tax violation and since it takes time to follow up on the information provided by banks, my prediction is that the United States will move to implement such a program in 2016-2017. Asian banks should look to the criteria of the Swiss Bank Program since I posit it will be the model to

be implemented by the DOJ worldwide," he said.

Swiss Bank Program

The IRS launched the Swiss Bank Program in August 2013 and it led to the prosecution of major Swiss Banks including UBS and Wegelin. Hochman said the program offered non-prosecution agreements in exchange for the payment of fines and the provision of information about accounts and where the money went.

The Swiss Bank Program requires Swiss banks to make a complete disclosure of their cross-border activities; provide detailed information on an account-by-account basis for accounts in which U.S. taxpayers have a direct or indirect interest; cooperate in treaty requests for account information; provide detailed information about other banks which transferred funds into secret accounts or which accepted funds when secret accounts were closed; agree to close accounts of account holders who fail to comply with U.S. reporting obligations; and pay appropriate penalties.

"The incentives for entering the program are not to have the United States bring felony criminal charges against the Swiss bank, which could result in the bank paying significantly more fines and penalties and losing its right to operate in the U.S. banking system," he said.

IRS relies on outsourcing of tax investigations

Hochman said the U.S. Congress expected the IRS to prosecute domestic tax evasion as well as assist with investigations into terrorism financing, money laundering, mortgage fraud, narcotics trafficking and even sports corruption such as the FIFA investigation. To undertake such a major task, the IRS increasingly has to rely on outsourcing its international investigative responsibilities to U.S. taxpayers themselves namely through the OVDP, foreign financial institutions and tax authorities through mechanisms such as the Swiss Bank Agreement and the [Foreign Account Tax Compliance Act](#) (FATCA).

FATCA

Hochman said FATCA provides the IRS with a third way of obtaining information on U.S. taxpayers' accounts abroad. The 30 percent withholding penalty is the biggest stick hanging over the heads of foreign financial institutions if they fail to provide taxpayers' account information.

"Thus, making sure that FATCA's automatic exchanges of information works properly to continue this outsourcing of U.S. tax investigations is crucial to U.S. tax compliance," he said.

Hochman said what made FATCA an important tool to the U.S. government is the automatic exchange of foreign financial institutions' information on an annual basis about U.S. taxpayers' accounts. This is a shift from a previous international tax reporting system that was based on individual requests for information, he said.

To date, more than 170,000 foreign financial institutions spanning 200 jurisdictions have registered with the IRS under FATCA. At least 100 governments have signed up to either the Model 1 or Model 2 intergovernmental agreements, with the majority including Singapore, choosing the former.

IRS poorly funded

The recently published [IRS Criminal Investigation 2015 Annual Budget](#) showed that the IRS, despite being tasked with raising \$2.7 trillion every year, is poorly funded and is overshadowed by domestic priorities. It was only allocated \$10.9 billion for the 2015 fiscal year, representing less than one-half of 1 percent of the total U.S. federal budget, to carry out its task.

"One would expect that the U.S. would fund this operation with at least a 10 percent or 5 percent allocation of its budget, the overhead normally required by any collection business in charge of raising such a sum ... [but] the IRS budget has been reducing in the last three years. The IRS has lost over 1,000 criminal investigators rather than gaining agents; it is reducing rather than increasing its foreign presence [the IRS has closed several foreign attaché offices]; and its U.S. domestic priorities," he said.

• **Patricia Lee** is South-East Asia editor at Thomson Reuters Regulatory Intelligence in Singapore. She also has responsibility for covering wider G20 regulatory policy initiatives as they affect Asia.