



Switzerland, Austria, and More Say They Will

A number of countries have announced that they will change their long-standing positions with respect to the application of bank-secrecy laws to information exchanges in tax matters. But, will this change in position make the release of bank account information to the IRS more likely?

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Reservations to Bank Secrecy Override by Certain Countries

In the face of international criticism of bank secrecy laws shielding tax evasion and the prospect of being listed by the Organization of Economic Cooperation and Development ("OECD") as uncooperative tax havens, Switzerland, Luxembourg, Austria, Liechtenstein, Andorra and Belgium all announced their intent to ease their bank secrecy practices and to accept the international standards on the exchange of information in tax matters. Does this mean that UBS is going to turn over the information with respect to the 52,000 accounts which are the subject of the John Doe summons enforcement proceeding by the IRS in Miami? Or that Swiss banks will now turn over information regarding undeclared bank accounts of U.S. persons automatically? Or upon the request of the IRS? Probably no, but the recent announcements are a beginning to obtaining transparency and exchange of information in tax matters.

Bank Secrecy Override

To understand what part bank secrecy laws play in the exchange of information in tax matters, one has to go back to 2004, when the OECD's Model Convention was revised. On June 1, 2004, the Committee on Fiscal Affairs of the OECD revised Article 26, Exchange of Information, of the OECD's Model Convention on Taxation of Income and Capital. The most significant aspect of the revision of Article 26 was the inclusion of an "override" of bank secrecy laws in the requested country, the one from which information is requested. Prior to that time the requested country could decline to supply information that could not be obtainable under the laws of that country. In Section 5 of Article 26, a contracting country party to a bilateral income tax treaty cannot "decline to supply information [to the other contracting country] solely because the information is held by a bank, other financial institution, nominee or person acting in an agency or fiduciary capacity..." The override of the bank secrecy laws in the requested country was already included in the U.S. Model Income Tax Convention, Article 26(3) and the U.S. Model Tax Information Exchange Agreement, Article 4(b).

The revision of Article 26 to include the override of the bank secrecy law of a contracting country was important because it represented the first time that the OECD declared that bank secrecy and other confidentiality laws were no longer acceptable in international tax matters where tax treaties apply. Since the OECD Model Convention is used as a model for income tax treaty negotiation, the bank secrecy override provision becomes the standard.

Austria, Belgium, Luxembourg and Switzerland all expressed reservations to the bank secrecy override. Belgium and Luxembourg reserved the right not to include the bank secrecy override in their conventions. But, with respect to Belgium where the override is included in its convention, the exchange of information held by a bank or financial institution is limited to the exchange on request of information with respect to both a specific taxpayers and a specific financial institution. Austria also reserved the right not to include the bank secrecy override in its conventions, but where it is included, Austria is authorized to exchange information held by a bank or other financial institution "where such information is requested within the framework of a criminal investigation which is carried on in the requesting country concerning the commitment of tax fraud". And Switzerland also reserved its position on the bank secrecy override. It proposed to limit the scope of the Article dealing with the exchange of information only to that information necessary to carryout the provisions of the convention. Further, Switzerland's reservation "shall not apply in cases involving acts of fraud subject to imprisonment according to the laws of both contracting [countries]".

Practical Results of Easing of Bank Secrecy Laws by Certain Countries

Does this mean that these countries will automatically turn over information regarding undeclared bank accounts of U.S. persons? Does this mean that the IRS can issue a John Doe summons requesting these countries to turn over such information? Can the IRS now go on a fishing expedition in those countries? It is clear from the pronouncements of these countries the answer is no! Luxembourg and Austria have stated that they will cooperate with foreign tax authorities on a "case by case basis where there is concrete evidence of tax evasion" What does this mean? First, the foreign tax authority will have to make a request for the sought after information, rather than the country having the information automatically turning over the information. Second, the name of the taxpayer will have to be known to the foreign tax authorities. The foreign tax authority will not be able to use the exchange of information provisions to learn the name of the taxpayer holding the bank account. Finally, there will have to be "concrete evidence" of tax evasion by the specific taxpayer. What will constitute "concrete evidence" of tax evasion is anyone's guess. Only upon a showing of all three of these elements will the bank secrecy override apply to the exchange of information.

Switzerland's announcement is even less clear. The Swiss government announced that it intended to adopt

international standards on exchange of information in tax matters developed by the OECD; and that increased exchange of information will only have practical effects when revised bilateral agreements including such standards come into effect. Consequently the bank secrecy override will not be assumed to be included in each of Switzerland's bilateral agreements from now on, but each country will have to wait until its bilateral agreement with Switzerland is renegotiated. In the past Switzerland declined to offer assistance in matters of tax evasion, which was not subject to criminal penalties in Switzerland. Switzerland now will no longer maintain that distinction between tax fraud and tax evasion in its future bilateral agreements. Under the existing U.S./Switzerland tax treaty, Switzerland is only required to provide assistance where the tax matter offense would constitute fraud under Swiss law. Will the IRS have to wait until the U.S./Switzerland tax treaty is renegotiated to seek information regarding U.S. tax evaders that would not be subject to criminal penalties for tax fraud in Switzerland. Moreover, Switzerland announced that the exchange of information will only be made in "individual cases where a specific and justified request has been made" and no automatic exchange of information on Swiss bank account holders will be made.

Conclusion

So where does that leave the IRS in seeking information from Swiss banks regarding undeclared bank accounts held for US taxpayers? The bank secrecy laws will not prevent the exchange of information, as long as the specific account holder's name is known, the name of the bank is known, it is believed that the account holder is committing tax evasion in the U.S., and the information is with respect to taxes covered by the OECD Model Tax Convention. However, with respect to fishing expeditions or the John Doe Summons in the UBS enforcement proceeding, the privacy of the account holders will continue to be protected by the bank secrecy laws.

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