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Magnifying Deterrence by Prosecuting Professionals

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Magnifying Deterrence by Prosecuting Professionals

SCOTT A. SCHUMACHER*

This Article examines the recent series of criminal prosecutions against tax professionals and offshore bankers. These criminal cases, brought against the largest Swiss bank (UBS), the oldest Swiss bank (Wegelin), one of the largest accounting firms in the world (KPMG), as well as numerous lawyers and accountants, represent a dramatic shift for the U.S. Department of Justice. After decades of tolerating abusive tax shelters and tax haven banks, the government changed its policy. However, rather than indicting the individuals and corporations who invested in tax shelters or hid money in offshore accounts, the Justice Department indicted the lawyers, accountants, and bankers who advised them. This Article will analyze those prosecutions from a theoretical, historical, and practical perspective, and will examine the impact the new prosecution policy will have on the legal professional, the tax system, and international relations.

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INTRODUCTION

The past few years have seen a dramatic shift in the prosecution policies of the U.S. Department of Justice in tax cases. Until recently, the U.S. government rarely prosecuted cases that involved the gray areas of the law, and arguable, if not plausible, interpretations of the Tax Code were rarely the subject of prosecutions.¹

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1. Cf. *United States v. Harris*, 942 F.2d 1125 (7th Cir. 1991).

Indictments of attorneys and accountants were even rarer, and these prosecutions usually accompanied the indictment of the taxpayers themselves.² As a result, the government generally resorted to bringing civil tax cases when going after investors in abusive tax shelters, and the professionals who marketed these scams were rarely brought into even these civil proceedings.³ Likewise, the use of offshore accounts by U.S. taxpayers was tolerated by prosecutors for decades.⁴ Indeed, the tax treaty with Switzerland acknowledged Swiss bank secrecy in tax prosecutions.⁵ This indulgence of tax shelters and tax havens led, at least in part, to their proliferation.⁶

However, beginning with the tax shelter prosecutions in 2005,⁷ the government's policy of restraint has undergone a significant change. Rather than challenging abusive transactions civilly or prosecuting the taxpayers, the government began focusing its criminal resources on the professionals who advised and enabled their clients to evade or avoid taxes. Thus, instead of pursuing taxpayers who claimed hundreds of millions of dollars in phony losses, the government decided to go after the accounting firms, law firms, and professionals who advised these taxpayers.⁸ And these were not just any firms. The government

2. *See, e.g.*, *United States v. Mastropieri*, 685 F.2d 776 (2d Cir. 1982).

3. *See, e.g.*, *Gray v. Comm'r*, 88 T.C. 1306, 1323 (1987) (“IME Gold for Tax Dollars” shelter held to be a fraudulent factual sham; negligence penalties sustained against shelter investors); *Glass v. Comm'r*, 87 T.C. 1087, 1177 (1986) (commodities straddles were “sham[s] in substance”).

4. *See, e.g.*, CHRISTIAN AID, DEATH AND TAXES: THE TRUE TOLL OF TAX DODGING 20–21 (2008) [hereinafter CHRISTIAN AID], available at <http://www.christianaid.org.uk/images/deathandtaxes.pdf>; 1 WALTER H. DIAMOND & DOROTHY B. DIAMOND, TAX HAVENS OF THE WORLD, at Intro. 18 (2013).

5. Convention for the Avoidance of Double Taxation with Respect to Taxes on Income, U.S.-Switz., art. 26, Oct. 2, 1996, S. TREATY DOC. NO. 112-1 (limiting exchanges of information in tax investigations to the “prevention of tax fraud or the like”). Under Swiss law, “tax fraud” is a much more limited concept than under U.S. law, and does not include tax evasion and most violations of U.S. tax laws. Rolf H. Weber, *Swiss Banking Secrecy in Evolution*, 18 BANKING & FIN. L. REV. 317, 337 (2003).

6. *See infra* notes 114–58 and accompanying text.

7. *See, e.g.*, Letter from David N. Kelley, U.S. Attorney, S. Dist. N.Y., to Robert S. Bennett 2 (Aug. 26, 2005) [hereinafter KPMG DPA] (transmitting the KPMG Deferred Prosecution Agreement), available at <http://www.justice.gov/usao/nys/pressreleases/August05/kpmgdpagmt.pdf>. It may be argued that a deferred prosecution agreement is not really a “prosecution.” *See, e.g.*, Editorial, *Too Big to Indict?*, N.Y. TIMES, Dec. 12, 2012, at A38, available at http://www.nytimes.com/2012/12/12/opinion/hsbc-too-big-to-indict.html?_r=0. In many respects, a deferred prosecution agreement has all the hallmarks of a criminal prosecution, at least with respect to entities that cannot be jailed. KPMG, HSBC, and others entering into a deferred prosecution agreement have publicly admitted to conduct that violated the law, and they paid large monetary sanctions. Yet, these entities did *not* plead guilty to a crime. Thus, to the extent that a criminal conviction still carries a stigma, these entities have not been subject to the full force of the criminal law. I will reserve a full discussion on the question of whether a deferred prosecution is truly a criminal prosecution. For purposes of this Article, I will assume that it is.

8. *See, e.g.*, *United States v. Daugerdas*, 757 F. Supp. 2d 364 (S.D.N.Y. 2012); *United States v. Stein*, 435 F. Supp. 2d 330 (S.D.N.Y. 2006).

proceeded criminally against professionals from some of the leading law and accounting firms, including KPMG, Ernst & Young, Brown & Wood, and Jenkens & Gilchrist.⁹ These cases garnered mixed results for the government, with the government getting some notable victories,¹⁰ but also some high-profile losses.¹¹ In the process, however, the government effectively shut down the tax shelter industry and fundamentally changed tax practice.¹²

The government persisted in this policy of pursuing professionals when it decided to go after Swiss banks and bankers, instead of the tens of thousands of U.S. depositors who hid money in undeclared offshore accounts. As with the tax shelter cases, the government targeted some of the biggest players, entering into a Deferred Prosecution Agreement with UBS, Switzerland's largest bank, and indicting some of its bankers.¹³ In 2012, the government indicted Switzerland's oldest bank, Wegelin Bank, and three of its partners, even though the bank had no U.S. office.¹⁴ As a result of the indictment, the bank essentially ceased to exist as an independent entity within a month.¹⁵ Wegelin pleaded guilty to tax crimes in January 2013, and formally ceased operation.¹⁶ While the prosecution of banks and

9. See, e.g., *United States v. Coplan*, 703 F.3d 46 (2d Cir. 2012); *Daugerdas*, 757 F. Supp. 2d 364; *Stein*, 435 F. Supp. 2d 330.

10. See, e.g., Christie Smythe & Bob Van Voris, *Former Lawyer Daugerdas Convicted in Tax-Fraud Scheme Retrial*, BLOOMBERG BUSINESSWEEK (Nov. 1, 2013), <http://www.businessweek.com/news/2013-10-31/ex-lawyer-daugerdas-convicted-in-tax-fraud-scheme-retrial-1>.

11. See, e.g., *Stein*, 435 F. Supp. 2d 330. The *Stein* loss was the result of prosecutorial overreaching and not the underlying substance of accusations in the indictment. See *United States v. Stein*, 541 F.3d 130, 157 (2d Cir. 2008). Indeed, three of the codefendants in *Stein* were convicted. See Lynnley Browning, *3 Convicted in KPMG Tax Shelter Case*, N.Y. TIMES, Dec. 18, 2008, at B11, available at <http://www.nytimes.com/2008/12/18/business/18kpmg.html>.

12. Tax practice was also affected by changes in the ethical rules applicable to rendering tax advice. See, e.g., 26 U.S.C. § 6694 (2012); 31 C.F.R. § 10.35 (2011).

13. See, e.g., Lynnley Browning, *U.S. Indicts Two in Switzerland on Tax Charges*, N.Y. TIMES, Aug. 21, 2009, at B1; Lynnley Browning, *A Swiss Bank Is Set to Open Its Secret Files*, N.Y. TIMES, Feb. 19, 2009, at A1, available at <http://www.nytimes.com/2009/02/19/business/worldbusiness/19ubs.html>; see also *Indictment*, *United States v. Little*, No 1:12-mj-01241 (S.D.N.Y. May 11, 2012) (British attorney indicted for assisting U.S. taxpayers to hide funds in Swiss and other foreign bank accounts); David Voreacos, *Offshore Tax Scorecard: UBS, Credit Suisse, HSBC, Julius Baer*, BLOOMBERG BUSINESSWEEK (Oct. 12, 2011), <http://www.businessweek.com/news/2011-10-12/offshore-tax-scorecard-ubs-credit-suisse-hsbc-julius-baer.html>.

14. David Voreacos, *Swiss Bank Wegelin Charged in U.S. with Aiding Tax Evasion*, BLOOMBERG BUSINESSWEEK (Feb. 3, 2012), <http://www.businessweek.com/news/2012-02-03/swiss-bank-wegelin-charged-in-u-dot-s-dot-with-aiding-tax-evasion>; Christoph Eisenring, *Die Checkliste der US-Justiz*, NEUE ZÜRCHER ZEITUNG (Jan. 19, 2012), <http://www.nzz.ch/aktuell/wirtschaft/uebersicht/die-checkliste-der-us-justiz-1.14406167>.

15. Haig Simonian, *Wegelin Becomes Victim of US Tax Dispute*, FIN. TIMES (Jan 27, 2012), <http://www.ft.com/intl/cms/s/0/864c58ca-48fc-11e1-88f0-00144feabdc0.html#axzz21ZLScv2B>.

16. Rupert Neate, *Oldest Swiss Bank to Close After US Tax Evasion Scam*, GUARDIAN, Jan. 5, 2013, at 32, available at <http://www.guardian.co.uk/world/2013/jan/04/swiss-bank>

bankers was ongoing, the government allowed most U.S. taxpayers to resolve their cases civilly via a series of offshore voluntary disclosure initiatives.¹⁷ These combined actions, along with the actions of other countries, dramatically changed offshore banking and the use and perception of tax havens.¹⁸

In this Article, I will examine the government's decision to pursue the professionals, instead of the clients the professionals represented, and the impact this revised prosecution policy has had on the tax system.¹⁹ In so doing, I will examine these prosecutions in their historical context, analyze whether they represent sound policy, and recommend whether changes in the policy should be made.

In Part I of the Article, I will examine the history of criminal prosecutions in both the tax shelter and tax haven areas. This history demonstrates that very few people, whether taxpayer or professional, were charged criminally for investing in tax shelters or hiding money in tax havens. This tolerance by prosecutors led to their continued use and expansion. Part II will then discuss the recent criminal prosecutions brought against tax lawyers, accountants, and bankers for their role in assisting their clients and customers in evading taxes. These cases will provide the necessary backdrop for what appears to be a fundamental shift in prosecution policy.

Part III of the Article will analyze the theory underlying criminal prosecutions. In this Part, I will show that federal prosecutors enjoy wide discretion as to whom to charge. Given this discretion, it is essential that front-line prosecutors are guided by clear prosecution policies and that those policies be consistently followed. These policies, while not crystalline, require prosecutors to determine the culpability of the person charged, including the person's relative culpability in relation to other actors not charged; the deterrent effect (particularly general deterrence) that would result from the prosecution; the retributive effect of the prosecution, in particular whether the victim of the crime has been compensated and their injuries have been addressed; and whether the prosecution will serve to protect the integrity of the civil tax system.

Finally, in Part IV, I will examine whether the recent prosecutions are consistent with the criminal theory and the government's prosecution goals discussed in Part III. I will argue that both the tax shelter and tax haven cases were generally consistent with criminal theory and the goals of prosecution policies and have for the most part been very successful. The most successful, indeed ingenious, aspect of the policy, whether intended or not, comes from the leveraging of general deterrence. By prosecuting professionals, rather than the taxpayers, the government has magnified the deterrent effect of the prosecutions. In so doing, the revised prosecution policies have fundamentally changed tax compliance.

-wegelin-close-tax-evasion.

17. See, e.g., IRS Notice 2011-54, 2011-29 I.R.B. 53; IRS Notice 2010-23, 2010-11 I.R.B. 441.

18. Thomas Zehnle & George Clarke, *When the Wall Comes Crumbling Down: What to Do with Taxpayers Who Cannot or Will Not Voluntarily Disclose*, 7 WHITE COLLAR CRIME REP. (BNA), Jan. 13, 2013, at 33.

19. It should be noted that the government's decision to go after professionals is not limited to tax prosecutions. See, e.g., Scott A. Schumacher, Stevens: *Is Zealous Advocacy Obstruction of Justice?*, 132 TAX NOTES 1169 (2011).

That being said, the new prosecution policy is not beyond criticism. The tax professionals who marketed the tax shelters created and sold these shelters to their clients as a prepackaged transaction at a handsome profit. Thus, without the professionals, no taxpayer would have invested in these shelters, and they have at least a colorable claim of relying on their professional advisor. By contrast, the tax haven banks are no more culpable (and arguably less culpable) than many of the U.S. taxpayers who hid money in those accounts, and who escaped prosecution. More significantly, while the tax haven prosecutions address the losses suffered by U.S. taxpayers, little has been done for the true victims of tax haven abuse—the developing world. I will provide a brief review of the devastating impact of tax havens on the developing world. Thus, while prosecuting bankers may make sense from a pragmatic standpoint, more must be done to protect the integrity of the tax system and to ensure that the injuries of the true victims of this conduct are redressed.

I. A BRIEF HISTORY OF TAX PROSECUTIONS

A. Tax Shelters

The concept of minimizing one's taxes has existed for centuries, and tax shelters are nothing new.²⁰ Indeed, the 1970s saw a proliferation of shelters, which were invested in by thousands of taxpayers.²¹ These shelters were generally dealt with in civil cases and were ultimately shut down by legislative changes.²² Significantly, many of these shelters involved mostly, if not completely, fictitious transactions.²³ Taxpayers "invested" in mines with no ore,²⁴ cattle that did not roam,²⁵ and videotapes that did not play.²⁶ In the words of Gertrude Stein, "there is no there there."²⁷ And the losses in these cases were not insignificant. Indeed, the estimated current revenue loss from these shelters was not appreciably less than the more recent generations of shelters.²⁸ However, despite the utterly fictitious nature of

20. See, e.g., Donald L. Korb, *Shelters, Schemes, and Abusive Transactions: Why Today's Thoughtful U.S. Tax Advisors Should Tell Their Clients to "Just Say No,"* in 3 MPI Studies on Intellectual Property, Competition and Tax Law 289, 289 (2008) (recounting tax dodges throughout history since the times of Ancient Rome).

21. See, e.g., *Glass v. Comm'r*, 87 T.C. 1087 (1986) (consolidating more than 1000 cases).

22. See, e.g., 26 U.S.C. §§ 465, 469 (2012).

23. See, e.g., *Goldberg v. United States*, 789 F.2d 1341, 1342–43 (9th Cir. 1986) (describing "Margolis transactions" typical of shelters peddled by Harry Margolis, which were characterized by convoluted transfers of overvalued property rights, circular money movements among foreign trusts, delayed drafting, signing and backdating of documents, and client obliviousness to the financial realities of their investments).

24. *Bouskos v. Comm'r*, 54 T.C.M. (CCH) 1117 (1987).

25. *Durham Farms # 1, J.V. v. Comm'r*, 79 T.C.M. (CCH) 2009, *aff'd*, 59 F. App'x 952 (9th Cir. 2003).

26. *Magin v. Comm'r*, 50 T.C.M. (CCH) 208 (1985).

27. GERTRUDE STEIN, EVERYBODY'S AUTOBIOGRAPHY 289 (photo. reprint 1971) (1937).

28. The IRS estimates a revenue loss of \$3.6 billion in 1983. Ann Southworth, *Redefining the Attorney's Role in Abusive Tax Shelters*, 37 STAN. L. REV. 889, 889 n.4 (1985) (citing Randall Smith & Kenneth H. Bacon, *Building Trouble?: Boom in Tax Shelters*

these transactions, very few people were prosecuted. One of the few people to be indicted was Harry Margolis, perhaps the most infamous tax lawyer who marketed tax shelters in the 1970s.²⁹ The government brought two separate prosecutions against Margolis and failed to obtain a conviction in either case. This would understandably have made the government a little gun-shy in prosecuting future cases. The government also lost other high profile criminal tax cases that involved arguable questions of law.³⁰

The result was that cases where a plausible argument could be made were essentially immune from prosecution.³¹ This system, along with the government's general tolerance of tax shelters (at least from a criminal perspective),³² led to a belief that even the hokiest of schemes would not be prosecuted, as long as it had at least a patina of legitimacy.³³ Moreover, the thicker the patina the better. Disguising what essentially was a made-up series of predetermined transactions in a blizzard of paperwork made the transaction at least appear to be legitimate. It also had the perverse effect of making these shelters more difficult to detect.³⁴ Not only did these transactions greatly benefit the clients, they were also incredibly lucrative for the firms who promoted them.³⁵

Moreover, shelters thrived under a system that imposed little downside to either the client or the professional advising the client. Taxpayers are not subject to penalties if they can show they acted with reasonable cause in good faith.³⁶ Reliance on the advice of a professional generally constitutes reasonable cause and good faith.³⁷ If a lawyer or accountant advises a taxpayer that a position has a more-likely-than-not chance of success, then, at least as to that taxpayer and that tax position, the position does meet that standard, since taxpayers are generally allowed to rely on the advice of tax experts.³⁸ Thus, the low audit rate, complex and

Artificially Lifts Prices of Much Real Estate, WALL ST. J., Dec. 27, 1983, at 1). In 2007 dollars, that amount is \$7.6 billion. The IRS estimated \$10 billion in losses from the recent iteration of shelters. Mary Williams Walsh, *Treasury Department Cracks Down on Tax Shelters for Firms*, L.A. TIMES, Feb. 29, 2000, at C-1.

29. See *Goldberg*, 789 F.2d 1341.

30. See, e.g., *United States v. Harris*, 942 F.2d 1125, 1131 (7th Cir. 1991) (finding that criminal prosecutions “must rest on a violation of a clear rule of law”); *United States v. Mallas*, 762 F.2d 361 (4th Cir. 1985) (overturning a conviction that was based on a vague point of law).

31. Cf. *Harris*, 942 F.2d. at 1134–35 (discussing evidence presented at trial that may have supported convictions for various other crimes that were never charged).

32. These shelters were certainly not tolerated altogether. The IRS and Department of Justice engaged in a vigorous civil campaign against these shelters. See, e.g., *Glass v. Comm’r*, 87 T.C. 1087 (1986).

33. Indeed, it was believed that these schemes would not be subject even to civil penalties. Tanina Rostain, *Sheltering Lawyers: The Organized Tax Bar and the Tax Shelter Industry*, 23 YALE J. ON REG. 77, 93–94 (2006).

34. Scott A. Schumacher, *MacNiven v. Westmoreland and Tax Advice: Using “Purposeful Textualism” to Deal with Tax Shelters and Promote Legitimate Tax Advice*, 92 MARQ. L. REV. 33, 90 (2008).

35. See Rostain, *supra* note 33, at 93–94.

36. 26 C.F.R. § 1.6664-4 (2012).

37. *Id.*

38. See Schumacher, *supra* note 34, at 62.

nearly impenetrable transactions, and high-net-worth individuals willing to take a chance on these transactions created a dangerous cocktail indeed.

B. Tax Havens

Tax havens,³⁹ or global financial centers, as they are sometimes called, have existed since at least the 1930s.⁴⁰ Modern tax havens have their origins in Switzerland and that country's bank secrecy laws.⁴¹ Privacy in banking and financial matters is part of Switzerland's historic tradition of protecting all secrets and a general commitment to the preservation and protection of the individual's right of privacy.⁴² Swiss bank secrecy laws date from the 1930s and were designed, at least initially, to protect individuals, particularly those in Nazi Germany, from having their accounts seized.⁴³ When the Swiss Banking Act was enacted in 1934, foreign nations, and not just Nazi Germany, were attempting to confiscate Jewish property. Agents were sent into Switzerland to find bank accounts of Jews and other dissidents. Thus, Swiss banking secrecy laws must be understood in their historical context.

Bank secrecy is enshrined in Article 47 of the Swiss Banking Act⁴⁴ and Article 273 of the Swiss Penal Code.⁴⁵ Under these laws, Swiss bankers must protect their customer's name, the type of bank account, the transactions the client entered into, and any information supplied by the customer in connection with the account.⁴⁶ Article 273 of the Swiss Penal Code makes it a crime for a person to divulge secret business information to a foreign government authority or its agents.⁴⁷ In addition to criminal sanctions, violating confidentiality mandates could also result in civil liability and administrative sanctions, including revocation of a bank's license or suspension of a bank executive convicted of a secrecy violation.⁴⁸ The availability of private and secure banking caused many of the world's wealthy to put their money in Swiss banks. This influx of capital was a boon to Switzerland's economy.

39. There is no one accepted definition of what constitutes a tax haven, nor is there an agreed upon list of the countries that should be considered tax havens. *See, e.g.*, U. S. GOV'T ACCOUNTABILITY OFFICE, GAO-09-157, INTERNATIONAL TAXATION: LARGE U.S. CORPORATIONS AND FEDERAL CONTRACTORS WITH SUBSIDIARIES IN JURISDICTIONS LISTED AS TAX HAVENS OR FINANCIAL PRIVACY JURISDICTIONS 9-17 (2008) [hereinafter GAO REPORT].

40. *See, e.g.*, Anita Ramasastry, *Secrets and Lies? Swiss Banks and International Human Rights*, 31 VAND. J. TRANSNAT'L L. 325, 328 (1998).

41. *Id.* at 328-30.

42. *Id.*

43. Lutz Krauskopf, *Regents' Lectures: Comments on Switzerland's Insider Trading, Money Laundering, and Banking Secrecy Laws*, 9 INT'L TAX & BUS. LAW. 277, 293 (1991).

44. Bundesgesetz [BankG] [Banking Statute] Nov. 8, 1934, SR 952.0, art. 47 (Switz.) [hereinafter Banking Statute], *unofficial translation available at* http://www.kpmg.com/CH/de/Library/Legislative-Texts/Documents/pub_20090101-BankA.pdf.

45. SCHWEIZERISCHES STRAFGESETZBUCH [StGB] [CRIMINAL CODE] Dec. 21, 1937, art. 273 (Switz.) [hereinafter SWISS PENAL CODE], *reprinted in* Krauskopf, *supra* note 43, at 295.

46. Banking Statute art. 47(a).

47. SWISS PENAL CODE, *supra* note 45, at art. 273.

48. *See* Krauskopf, *supra* note 43, at 296-97. The conduct of UBS and its bankers must be viewed in light of this very stringent requirement.

The success of the Swiss banking industry caused other countries around the world to look at banking and financial services as a possible industry. Liechtenstein, for example, saw its neighbor and close ally as a big brother to be emulated. By enacting a combination of strict bank secrecy laws, flexible and nuanced entity structures, and low taxes, Liechtenstein transformed itself from a poor agricultural country into a prosperous, highly industrialized economy with a thriving financial service industry.⁴⁹ The United Kingdom also saw the benefit of low taxes and bank secrecy in attracting capital, which it desperately needed in the decades following World War II. It used its Crown Dependencies, like the Cayman Islands, British Virgin Islands, and Bermuda to attract this capital.⁵⁰ It is no accident that many tax havens are current or former British colonies or dependencies.⁵¹ In the following decades, tax havens sprang up around the world, from Panama to Iceland, Singapore to Monaco—all offering financial security and privacy.

While the label of tax haven is often considered something to be avoided, especially recently,⁵² countries who offered these services usually attained greater financial success. The per capita GDP of haven countries greatly exceeds those of nonhaven countries.⁵³ Liechtenstein has the second highest per capita income in the world, after Monaco (another tax haven).⁵⁴ The Cayman Islands, which prior to its status as a tax haven was poor with few natural resources, now has one of the highest standards of living in the Caribbean.⁵⁵ The benefits of being a tax haven must be fully appreciated if serious reforms are to take place. Wealthy nations rich

49. 2 DIAMOND & DIAMOND, *supra* note 4, at Liech. 4.

50. The UK Crown Dependencies continue to make a significant contribution to the UK financial markets and the British banking system. MICHAEL FOOT, FINAL REPORT OF THE INDEPENDENT REVIEW OF BRITISH OFFSHORE FINANCIAL CENTRES 6 (2009), available at http://webarchive.nationalarchives.gov.uk/+http://www.hm-treasury.gov.uk/d/foot_review_main.pdf.

51. See Dhammika Dharmapala, *What Problems and Opportunities Are Created by Tax Havens?*, 24 OXFORD REV. ECON. POL'Y 661, 671 n.24 (2008); Richard A. Johnson, *Why Harmful Tax Practices Will Continue After Developing Nations Pay: A Critique of the OECD's Initiatives Against Harmful Tax Competition*, 26 B.C. THIRD WORLD L.J. 351, 359 (2006).

52. See Susan C. Morse, *Tax Compliance and Norm Formation Under High-Penalty Regimes*, 44 CONN. L. REV. 675, 678 (2012). Being labeled a “tax haven” can earn a country a spot on the OECD’s “black list,” with the concomitant threat of sanctions. See, e.g., Martin A. Sullivan, *Lessons From the Last War on Tax Havens*, TAX NOTES, Jul. 30, 2007, at 327. In addition, the Foreign Account Tax Compliance Act (FATCA) imposes a strict withholding regime on distributions from the U.S. to foreign financial institutions that have not entered into a tax reporting agreement with the Internal Revenue Service. FATCA, Pub. L. No. 111-147, 124 Stat. 71, 97 (codified at 26 U.S.C. §§ 1471–1474).

53. Dharmapala, *supra* note 51, at 664.

54. Leigh Baldwin & Carolyn Bandel, *Liechtenstein Monarch Will Keep Veto Powers After Referendum*, BLOOMBERG BUSINESSWEEK (July 1, 2012, 8:06 AM), <http://www.businessweek.com/news/2012-07-01/liechtenstein-monarch-will-keep-veto-powers-after-referendum>. See also GAO REPORT, *supra* note 39, at 13–14 (showing both Liechtenstein and Monaco as jurisdictions identified as tax havens).

55. 1 DIAMOND & DIAMOND, *supra* note 4, at Cayman Is. 3.

in natural resources cannot seriously believe that small countries with no natural resources would willingly give up their primary source of revenue.⁵⁶

More recently, other countries have seen the benefits of providing financial services to the world's wealthy. The Netherlands have gained international notoriety for trusts holding the wealth of rock stars like the Rolling Stones and U2, so that these and other multimillionaires do not have to pay U.K. taxes on their royalties.⁵⁷ The combination of treaties and tax laws of Ireland and the Netherlands has caused many international corporations to structure their transactions in what has become known as the rather yummy-sounding name of the "Double Irish with a Dutch Sandwich."⁵⁸ Denmark has become the country of choice to set up a corporation that owns other corporations, thereby facilitating tax avoidance.⁵⁹ Even the Vatican's bank, the Institute for Works of Religion (*Istituto per le Opere di Religione* in Italian), holds billions of dollars of deposits all with strict bank secrecy.⁶⁰ Finally, depending upon how one defines the term "tax haven," several U.S. states, including Nevada, Wyoming, and Delaware, have been labeled tax havens.⁶¹

Of course, there has not been a universal acceptance of tax havens. Concerns about money laundering and terrorism financing triggered many jurisdictions to require banks to "know [their] customer[s]" in an effort to stop the illicit flow of money.⁶² The Organization for Economic Cooperation and Development (OECD) maintains a "black list" and a "gray list" that purport to show the level of cooperation by tax haven countries.⁶³ Various governments have set up task forces to deal with the problems of tax havens.⁶⁴ However, no one could be so naïve as to

56. See generally Dharmapala, *supra* note 51, at 663–64.

57. Lynnley Browning, *Gimme Tax Shelter: The Stars Have Found a Dutch Home*, N.Y. TIMES, Feb. 4, 2007, at B1, available at <http://www.nytimes.com/2007/02/04/business/yourmoney/04amster.html?pagewanted=all>.

58. See, e.g., Adam H. Rosenzweig, *Thinking Outside the (Tax) Treaty*, 2012 WIS. L. REV. 717, 778 (2012).

59. See, e.g., Marcus Hoy, *Denmark Facing New Criticism as Tax Evasion 'Transit Station'*, 9 DAILY TAX REP. (BNA), Aug. 13, 2009, at I-1.

60. 1 DIAMOND & DIAMOND, *supra* note 4, at Intro. 16.

61. See, e.g., Lynnley Browning, *Critics Call Delaware a Tax Haven*, N.Y. TIMES, May 30, 2009, at B1, available at <http://www.nytimes.com/2009/05/30/business/30delaware.html>; *Finance and Economics: Haven Hypocrisy*, ECONOMIST, Mar. 28, 2009, at 86, available at <http://www.economist.com/node/13382279>.

62. See, e.g., Maira Machado, *Similar in Their Differences: Transnational Legal Processes Addressing Money Laundering in Brazil and Argentina*, 37 LAW & SOC. INQUIRY 330, 356 (2012).

63. See, e.g., ORG. FOR ECON. CO-OPERATION AND DEV., TAX CO-OPERATION: TOWARDS A LEVEL PLAYING FIELD (2007), available at <http://www.oecd.org/tax/transparency/44430309.pdf>.

64. One example of this is the Joint International Tax Shelter Information Centre (JITSIC), which is a joint effort by the tax agencies of Australia, Canada, China, Japan, South Korea, the United Kingdom, and the United States. JOINT INT'L TAX SHELTER INFO. CTR., MEMORANDUM OF UNDERSTANDING FOR THE CREATION OF A JOINT INTERNATIONAL TAX SHELTER INFORMATION CENTRE, available at <http://www.irs.gov/pub/irs-utl/jitsic-finalmou.pdf>.

think that the wealthy were not still hiding money offshore. Everyone knew it, but they lacked the will, the ability, or the interest to stop it.

Indeed, as with tax shelters, the government brought few criminal tax prosecutions for the use of tax havens,⁶⁵ and even those few prosecutions did not always result in conviction.⁶⁶ Prosecutors did not pursue the offshore banks themselves. Instead, they sought merely to obtain information from the banks about U.S. depositors,⁶⁷ and even those efforts produced a backlash.⁶⁸

II. A SEA CHANGE

A. *The Tax Shelter War*

With a new century, the government's treatment of both tax shelters and tax havens began to change. On a broader scale, the Justice Department beefed up its "Principles of Federal Prosecution of Business Organizations" in January 2003 by then-Deputy Attorney General Larry Thompson, in what is known as the Thompson Memorandum.⁶⁹ This amplified policy showed that the government would take a harder line against corporate crime.⁷⁰ The government backed up this tough talk with its indictment of Arthur Andersen.⁷¹ This "get tough" approach was also employed in tax cases, with the government going after tax shelters in both civil and criminal cases.⁷²

65. *But see* United States v. Pollen, 978 F.2d 78 (3d Cir. 1992) (defendant convicted of tax evasion for hiding assets in Swiss nominee account).

66. *See, e.g.,* United States v. Dahlstrom, 713 F.2d 1423 (9th Cir. 1983) (law of foreign trusts unsettled and conviction thus overturned).

67. *See, e.g., In re* Grand Jury Proceedings Bank of Nova Scotia, 740 F.2d 817 (11th Cir. 1984).

68. *Id.* at 832.

69. Memorandum from Larry D. Thompson, Deputy Attorney Gen., to U.S. Attorneys, Regarding Principles of Federal Prosecution of Business Organizations (Jan. 20, 2003), available at <http://www.albany.edu/acc/courses/acc695spring2008/thompson%20memo.pdf>.

70. *Id.* Several aspects of the Thompson Memorandum came under attack in the high-profile prosecution of several former partners of the accounting firm KPMG. Most notably, the government used the threat of indictment and prosecution, which in Arthur Andersen's case was in essence a death sentence, to pressure KPMG into waiving its attorney-client privilege and cutting off payment of legal fees for individual partners of KPMG that had been indicted. *See* United States v. Stein, 452 F. Supp. 2d 230, 237-38 (S.D.N.Y. 2006), *vacated sub nom., Stein v. KPMG, LLP*, 486 F.3d 753 (2d Cir. 2007). In response to the criticism, the Thompson Memorandum was revised in 2006 by then-Deputy Attorney General Paul McNulty. This revision has softened some of the more draconian aspects of the Thompson Memorandum. Memorandum from Paul J. McNulty, Deputy Attorney Gen., to U.S. Attorneys, on Principles of Federal Prosecution of Business Organizations (Dec. 6, 2006), available at http://www.usdoj.gov/dag/speeches/2006/mcnulty_memo.pdf.

71. Arthur Andersen LLP v. United States, 544 U.S. 696 (2005).

72. In August 2003, Eileen O'Connor, the then-Assistant Attorney General of the Tax Division, set out the actions taken by the government to combat abusive tax shelters: (1) investigated ninety-nine tax shelter promoters, including law firms, accounting firms, and banks; (2) issued 272 summonses to thirty-five promoters regarding with tax shelter

In Notice 2000-44, the Internal Revenue Service (IRS) stated that certain shelters were considered abusive,⁷³ and that investors in these shelters might be subject to criminal prosecution.⁷⁴ Although similar to the generations of shelters, the breed of tax shelters listed in Notice 2000-44 and other IRS notices differed in size and scope from shelters from the 1970s. While the typical 1970s shelter involved tax savings in the thousands of dollars, the new shelters saved the taxpayers millions of dollars.⁷⁵ However, like the shelters of old, the newer shelters involved taking the tax code provision out of context and inventing facts.

One of the most notorious—and lucrative—of these shelters was the Son of BOSS shelter.⁷⁶ While known by many names⁷⁷ and with different variations, these shelters had essentially the same fundamentals. The taxpayer would enter into a short-sale transaction, which had the corresponding obligation to close the transaction at later date. The initial short sale would produce a large amount of cash, which, along with other cash or property, was transferred into a partnership.⁷⁸ The taxpayer would increase their basis in the partnership by the value of the cash and other property contributed, but the taxpayer would not reduce his basis by the obligation to close the short sale, citing a strained reading of § 752.⁷⁹ The partnership would then close the short sale, thereby reducing the amount of cash in the partnership. Shortly thereafter, the taxpayer would sell his interest in the partnership for a price equal to the cash and property remaining in the partnership. This transaction would generate a loss equal to the difference between the amount realized over the adjusted basis unreduced by the obligation, generating losses in some cases in excess of \$100 million.⁸⁰

These shelters had no business purpose and were entered into solely to generate tax losses. Like the “Margolis transactions,” these transactions were prewired and

registration and investor list requirements; (3) obtained investor lists from at least twenty-five promoters; (4) identified twenty-seven abusive tax shelters through formal notices; and (5) audited taxpayers to determine whether they invested in abusive transactions. *IRS Sues to Enforce Promoter Summonses, Get Investor Names from Jenkins & Gilchrist*, 22 TAX MGMT. WEEKLY REPORT (BNA), Aug. 18, 2003, at 1326.

73. I.R.S. Notice 2000-44, 2000-2 C.B. 255.

74. *Id.* at 256; *see also* I.R.S. Notice 2000-61, 2000-2 C.B. 569; I.R.S. Notice 2002-50, 2002-2 C.B. 98.

75. For example, several KPMG clients claimed fraudulent losses in excess of \$100 million. *See* Superseding Indictment at 64–66, *United States v. Stein*, 452 F. Supp. 2d 230 (S.D.N.Y. 2006), No. S1 05 Cr. 888 (LAK), *available at* http://www.nytimes.com/packages/pdf/business/20051018_kpmgletter.pdf.

76. The Son of BOSS tax shelter is a derivation of the BOSS (Bond Option and Sales Strategy). *Kligfeld Holdings v. Comm’r*, 128 T.C. 192, 194 (2007).

77. These shelters were known by other proprietary names like COBRA, BLIPS and SOS. Leandra Lederman, *A Tisket, a Tasket: Basketing and Corporate Tax Shelters*, 88 WASH. U. L. REV. 557, 590 n.222 (2011) (citing Karen C. Burke & Grayson M.P. McCouch, *COBRA Strikes Back: Anatomy of a Tax Shelter*, 62 TAX LAW 59, 62, 64 n.20 (2008)).

78. *Kligfeld Holdings*, 128 T.C. at 194–95.

79. *Id.* at 195–96; *see also* 26 U.S.C. § 752(b) (“Any decrease in a partner’s share of the liabilities of a partnership, or any decrease in a partner’s individual liabilities by reason of the assumption by the partnership of such individual liabilities, shall be considered as a distribution of money to the partner by the partnership.”).

80. I.R.S. Notice 2000-44, *supra* note 73; Superseding Indictment, *supra* note 75, at 64–66.

predetermined.⁸¹ The promoters drafted all of the documents and executed all of the transactions.⁸² They created false factual recitations setting forth the taxpayer's alleged business purpose in entering into the transactions and presented them to the client for signature.⁸³ This false factual recitation then became the factual basis for the opinion letter drafted by the promoter.⁸⁴ An associate (or co-conspirator, if you will) would then prepare a tax return based on the phony opinion letter drafted by the promoter, which was based on the bogus statement of facts, also drafted by the promoter.⁸⁵

While the prior tax shelter industry involved professionals who were mostly outliers,⁸⁶ the advisors involved in the more recent shelters worked for some of the most prestigious accounting and law firms.⁸⁷ The fees earned by these professionals were equally impressive. KPMG earned \$53 million from just one tax shelter it sold to 186 individuals.⁸⁸ BDO Seidman, through its tax products group known as the "wolf pack," admitted to receiving \$100 million from its tax shelter sales.⁸⁹ Banks like Deutsche Bank, Bear Stearns, and Merrill Lynch also got into the act,⁹⁰ as did law firms like Jenkins & Gilchrist and Brown & Wood.⁹¹ Jenkins & Gilchrist attorney Paul Daugerdas made more than \$95 million from marketing shelters from 1998 through 2002.⁹²

Faced with incredible tax losses, the egregious nature of the transactions, combined with a determination to do something about tax shelters, the government abandoned its long-standing tolerance of shelters. In 2005, the international accounting firm KPMG escaped indictment only by entering into a deferred prosecution

81. See *Goldberg v. United States*, 789 F.2d 1341 (9th Cir. 1986).

82. See, e.g., KPMG DPA, *supra* note 7.

83. *Id.* ¶ 2.

84. *Id.*

85. Superseding Indictment, *supra* note 75, at 9–10.

86. See, e.g., *Ethical Problems of Tax Practitioners: Transcript of Tax Law Review's 1952 Banquet*, 8 TAX L. REV. 1, 24 (1952) (comments of J.P. Wenchel) ("It is the blackleg—and he was always in the profession. What are you going to do about him? He is on the fringe of society.").

87. Rostain, *supra* note 33, at 90–91.

88. Tanina Rostain, *Travails in Tax: KPMG and the Tax Shelter Controversy*, in LEGAL ETHICS: LAW STORIES 89, 101 (Deborah L. Rhode & David J. Luban eds., 2005).

89. See Cassell Bryan-Low, *Unhappy Returns: Accounting Firms Face Backlash over the Tax Shelters They Sold*, WALL ST. J., Feb. 7, 2003, at A1, available at <http://online.wsj.com/article/SB1044568358985594893.html>.

90. *ACM v. Comm'r*, 157 F.3d 231 (3d Cir. 1998); Nathan Vardi, *Deutsche Bank Will Pay \$554 Million for Illegal Tax Shelter Activity*, FORBES (Dec. 21, 2010, 2:11 PM), <http://www.forbes.com/sites/nathanvardi/2010/12/21/deutsche-bank-will-pay-554-million-for-illegal-tax-shelter-activity/>.

91. STAFF OF PERMANENT SUBCOMM. ON INVESTIGATIONS, S. COMM. ON GOVERNMENTAL AFFAIRS, 108th Cong., U.S. TAX SHELTER INDUSTRY: THE ROLE OF ACCOUNTANTS, LAWYERS, AND FINANCIAL PROFESSIONALS (2003); *Jenkins & Gilchrist Admits It Is Subject to \$76 Million IRS Penalty*, I.R.S. News Release IR-2007-71 (Mar. 29, 2007), available at [http://www.irs.gov/uac/Jenkins-&-Gilchrist-Admits-It-Is-Subject-to-\\$76-Million-IRS-Penalty](http://www.irs.gov/uac/Jenkins-&-Gilchrist-Admits-It-Is-Subject-to-$76-Million-IRS-Penalty).

92. Lynnley Browning, *7 Indicted on Charges of Selling Tax Shelters*, N.Y. TIMES, June 10, 2009, at B1, available at http://www.nytimes.com/2009/06/10/business/10tax.html?_r=1&.

agreement and agreeing to pay a \$456 million fine.⁹³ In so doing, it admitted that from 1996 through 2002, it assisted high-net-worth individuals evade income taxes on billions of dollars of income by developing, promoting, and implementing fraudulent tax shelters.⁹⁴ KPMG also admitted that a number of its partners engaged in unlawful and fraudulent conduct, including preparing false tax returns, drafting false factual recitations and representations as part of the documentation supporting the shelters, and issuing opinions that contained these false statements and concealed the true nature of the shelters from the IRS.⁹⁵ KPMG also agreed to shut down its individual, compensation, and benefits tax practices, and employ heightened opinion standards when rendering tax opinions.⁹⁶ Deutsche Bank, Germany's largest bank, agreed to pay a fine of \$554 million for its role in helping KPMG implement these tax shelters.⁹⁷

In 2007, Jenkens & Gilchrist, a Dallas-based law firm, whose Chicago office was one of the hotbeds of tax shelter promotion, entered into a non-prosecution agreement. Under this agreement, Jenkens agreed to pay a \$76 million penalty and to shut down its practice. The firm no longer exists.⁹⁸ In 2012, the accounting firm of BDO Seidman entered into a deferred prosecution agreement in which it agreed to pay a \$50 million fine for helping its clients evade more than \$1.3 billion in taxes on more than \$6.5 billion in income.⁹⁹

The professionals who worked at these firms were not so fortunate. Nineteen individuals, most of whom worked for KPMG, were indicted and charged with conspiracy, tax evasion, and obstructing the IRS.¹⁰⁰ In 2007, four former partners of the accounting firm Ernst & Young were charged with tax fraud, conspiracy, and related crimes arising out of tax shelters promoted by Ernst & Young.¹⁰¹ Paul Daugerdas, the lead tax shelter promoter at Jenkens & Gilchrist, along with six others, was indicted and charged with conspiracy, tax evasion, and obstructing the IRS.¹⁰² Many other professionals have been indicted for their roles in promoting abusive tax shelters. In each instance, these tax professionals were charged with creating transactions that had no business purpose, lacked economic substance, and were papered with false recitations by clients, with the factual recitations having been drafted by the professionals themselves.

93. KPMG DPA, *supra* note 7, ¶ 3.

94. *Id.* ¶ 2.

95. *Id.*

96. *Id.* ¶ 6.

97. Vardi, *supra* note 90.

98. Chad Bray, *Tax-Shelter Case Brings Convictions*, WALL ST. J., May 25, 2011, at C3, available at <http://online.wsj.com/article/SB10001424052702304066504576343882600125752.html>.

99. Janet Novack, *BDO Admits Generating \$6.5 Billion in Phony Tax Shelter Losses, Pays \$50 Million*, FORBES (June 13, 2012, 7:28 PM), <http://www.forbes.com/sites/janetnovack/2012/06/13/bdo-admits-generating-6-5-billion-in-phony-tax-shelter-losses-pays-50-million/>.

100. Superseding Indictment, *supra* note 75.

101. Press Release, Yusill Scribner, U.S. Attorney, S. Dist. N.Y., Four Individuals Charged in Criminal Tax Fraud Related to Ernst & Young Tax Shelters (May 30, 2007), available at <http://www.justice.gov/usao/nys/pressreleases/May07/eyindictmentpr.pdf>.

102. See *United States v. Daugerdas*, 757 F. Supp. 2d 364 (S.D.N.Y. 2010).

Significantly, while the clients of these professionals were often listed as co-conspirators, very few of the clients were actually indicted. Instead, the IRS offered a global settlement to investors in these shelters that allowed taxpayers to resolve their cases by paying civil penalties.¹⁰³

This new prosecution policy has helped to transform tax practice. Of course, criminal sanctions were not the only arrow in the government's quiver. New penalties applicable to tax shelter investors and their advisors were enacted,¹⁰⁴ the IRS adopted new rules for giving written tax advice,¹⁰⁵ and the government won some key victories in civil tax cases against shelters.¹⁰⁶ However, the importance of the criminal prosecutions and shock of seeing the names of prominent professionals after "United States v." in the header of an indictment should not be underestimated. The result of these policies was succinctly stated by former Assistant Secretary of Treasury for Tax Policy, Pamela Olson: "The tax shelter war is over. The government won."¹⁰⁷

B. The Swiss and Liechtenstein Tax Haven Cases

The U.S. government's apparent tolerance of tax havens ended in 2008 when two spectacular cases, replete with international espionage, intrigue, and skullduggery, brought tax havens into the consciousness of governments, policy makers, and the media. Like the tax shelter cases, the egregious nature of these tax haven cases changed the government's policy from one of passive acceptance to active criminal investigation and prosecution.

1. Liechtenstein and LGT

Liechtenstein is an ancient country whose predecessor was founded in 1342.¹⁰⁸ The Principality of Liechtenstein was established within the Holy Roman Empire in 1719, and it became a sovereign state in 1806. Until the end of World War II, Liechtenstein was mainly agricultural and poor. Since then, this tiny country with limited natural resources has developed into a prosperous, highly industrialized, free-enterprise economy with a vital financial service sector and the highest per capita income in the world.¹⁰⁹ Until very recently, Liechtenstein also had strict bank secrecy laws,¹¹⁰ which caused it to be described as "the most dangerous tax haven in Europe."¹¹¹

103. See, e.g., I.R.S. Announcement 2004-46, 2004-21 I.R.B. 964; I.R.S. Announcement 2005-80, 2005-46 I.R.B. 967.

104. See, e.g., 26 U.S.C. §§ 6700, 6707A (2012).

105. 31 C.F.R. § 10.35 (2011).

106. See, e.g., *Kornman & Assocs., Inc. v. United States*, 527 F.3d 443 (5th Cir. 2008); *ACM P'ship v. Comm'r*, 157 F.3d 231, 234 (3d Cir. 1998).

107. Victor Fleischer, "The Tax Shelter War Is Over," CONGLOMERATE (Oct. 28, 2006), http://www.theconglomerate.org/2006/10/the_tax_shelter.html.

108. *About Liechtenstein*, LIECHTENSTEIN: EMBASSY OF LIECHTENSTEIN—WASHINGTON D.C., <http://www.liechtensteinusa.org/index.php?page=history>.

109. *Id.*

110. See 2 DIAMOND & DIAMOND, *supra* note 4, at Liech. 3.

111. *Id.* at Liech. 1.

LGT Group, formerly the Liechtenstein Global Trust, is a large private wealth and asset management group owned by the royal family of Liechtenstein. The LGT Group is wholly owned by the Prince of Liechtenstein Foundation.¹¹² The Prince of Liechtenstein Foundation, in turn, is owned by the Royal Family, with Prince Hans-Adam II as the principal beneficiary.¹¹³ The prince enjoys an estimated net worth of \$5 billion.¹¹⁴ His brother, Prince Philipp von und zu Liechtenstein, is chairman of the Board of Trustees of the Foundation, and his son, Prince Max von und zu Liechtenstein, serves as CEO.¹¹⁵

The status of Liechtenstein as a leading tax haven changed on February 14, 2008, when prosecutors and tax investigators carried out simultaneous raids on the headquarters of Deutsche Post, Europe's biggest postal service, and the private villa of its CEO Klaus Zumwinkel. Zumwinkel was arrested on national television. He was accused of having evaded approximately \$1.5 million in taxes using a foundation in Liechtenstein and secreting money in LGT.¹¹⁶ According to an article in the German periodical *Der Spiegel*: "The investigation has taken on a dimension previously unknown in Germany. It was the first time in history that the CEO of a German blue chip DAX company had been taken from his home by authorities in front of live news cameras."¹¹⁷ Zumwinkel was the CEO of Deutsche Post, and at the time of his arrest was one of Germany's most influential businessmen,¹¹⁸ sitting on the boards of Postbank and Deutsche Telekom.¹¹⁹

The extraordinary investigation and arrest of Zumwinkel was the result of information received by German investigators. Tax investigators of the German government paid a former employee of LGT, Heinrich Kieber, as much as \$7.7 million for bank account data that Kieber had stolen from LGT Group.¹²⁰ The computer discs Germany obtained from Kieber contained about 1400 names, the

112. See STAFF OF S. PERMANENT SUBCOMM. ON INVESTIGATIONS, COMM. ON HOMELAND SEC. AND GOVERNMENTAL AFFAIRS, 110th Cong., TAX HAVEN BANKS AND U.S. TAX COMPLIANCE 32–33 (Comm. Print 2008) [hereinafter SENATE REPORT].

113. *Id.* at 33 & n.103.

114. See Luisa Kroll, *Europe's Richest Royals*, *Forbes* (Apr. 27, 2011, 11:44 AM), <http://www.forbes.com/sites/luisakroll/2011/04/27/europes-richest-royals/>.

115. SENATE REPORT, *supra* note 112, at 33 n.103.

116. Barbara Schmid, *Raid on Zumwinkel's Home and Office: Authorities Investigating Deutsche Post CEO for Tax Evasion*, SPIEGEL ONLINE INT'L (Feb. 14, 2008, 10:41 AM), <http://www.spiegel.de/international/business/raid-on-zumwinkel-s-home-and-office-authorities-investigating-deutsche-post-ceo-for-tax-evasion-a-535230.html>. A foundation or "stiftung" is a creature of statute under Liechtenstein law and has features that are similar to a trust. M. Read Moore, *Tax and Estate Planning Issues for U.S. Clients Who Own Foreign Property*, in TAX AND ESTATE PLANNING ISSUES FOR U.S. CLIENTS WHO OWN FOREIGN PROPERTY 2289, 2297 (ALI-ABA Course of Study, Nov. 16–20, 2009), available at Westlaw SR016 ALI-ABA 2289.

117. Schmid, *supra* note 116.

118. *Id.*

119. *Id.*

120. Alan Katz & Joshua Gallu, *Checkered Past for Fugitive at Center of Liechtenstein Fraud Case*, N.Y. TIMES (June 18, 2008), <http://www.nytimes.com/2008/06/18/business/worldbusiness/18iht-evade.4.13802720.html?pagewanted=all>.

release of which set off investigations in fourteen countries, including the United States.¹²¹

2. The Other Tax Haven Scandal – UBS

At the same time as the LGT case was unfolding, the activities of Swiss banking giant UBS came to light. UBS, formerly Union Bank of Switzerland,¹²² is “one of the largest financial institutions in the world, and has one of the largest private banks catering to wealthy individuals.”¹²³ As with the LGT case, the UBS case broke because of the involvement of a single employee. Bradley Birkenfeld, a U.S. citizen, had worked for UBS as a private banker from 2001 to 2005.¹²⁴ In 2007 he approached the Senate Permanent Subcommittee on Investigations (“Subcommittee”) volunteering data on UBS’s private banking practices.¹²⁵ Birkenfeld ultimately provided detailed information to prosecutors and to the Subcommittee regarding UBS’s solicitation of clients in the United States.¹²⁶

The 2008 report of the Subcommittee describes the lengths to which UBS employees went to obtain new clients in the United States and to hide those activities from the U.S. government. U.S. securities law requires persons who provide securities products or services within the United States to be registered with the Securities and Exchange Commission (SEC).¹²⁷ UBS was licensed to operate as a bank in the United States, and it had 437 offices in the United States that could assist its U.S. clients.¹²⁸ However, UBS’s banking and securities licenses did not extend to its non-U.S. offices.¹²⁹ Nevertheless, UBS instructed its Swiss bankers to find new clients (and new money) in the United States and to encourage those clients to open accounts in Switzerland.¹³⁰ If a foreign financial institution executes sales of non-U.S. securities, the institution must report the transaction to the IRS on a Form 1099 if the sales are affected in the United States.¹³¹

During the years at issue, UBS had “written policies restricting the marketing and client-related activities that could be undertaken in the United States by UBS bankers from outside the country.”¹³² Despite these stated policies, UBS encouraged and even paid for its Swiss bankers to travel to the United States to

121. *Id.*

122. *See About Us: UBS in the World*, UBS, http://www.ubs.com/global/en/about_ubs/about_us/history/ubs-and-the-world.html.

123. SENATE REPORT, *supra* note 112, at 8.

124. *Id.* at 9.

125. *Id.*

126. *Id.*

127. *Id.* at 11–12.

128. Declaration of Daniel Reeves at 2, *United States v. UBS AG*, No. 09-20423 (S.D. Fla. dismissed Aug. 19, 2009) [hereinafter Reeves Declaration], *available at* http://www.justice.gov/tax/UBS_Declaration_DReeves.pdf.

129. SENATE REPORT, *supra* note 112, at 12.

130. *Id.* at 13.

131. *Id.* at 12.

132. *Id.*

develop new business and service existing clients.¹³³ According to the Senate Report, Birkenfeld told the Subcommittee that, during his four years at UBS, the private bankers from Switzerland typically traveled to the United States four to six times per year, using their trips to recruit new clients and to provide financial services to existing clients.¹³⁴ Birkenfeld also testified that UBS provided its Swiss bankers with tickets and funds to go to events attended by wealthy U.S. individuals so that they could solicit new business for UBS in Switzerland.¹³⁵ Indeed, UBS regularly sponsored events in the United States like golf and tennis tournaments, art fairs, and other special events in wealthy areas.¹³⁶ These events were designed to allow UBS bankers access to high-net-worth individuals. According to the Subcommittee report, UBS also assigned its Swiss bankers specific performance goals to bring “net new money” (NNM) into the Swiss bank from the United States.¹³⁷ According to the Subcommittee’s report:

A UBS business plan for the years 2003 through 2005, provides context for the Swiss focus on obtaining U.S. clients. This document observes that “31% of World’s UHNWIs [Ultra High Net Worth Individuals] are in North America (USA + Canada).” It also observes that the United States has 222 billionaires with a combined net worth of \$706 billion. This type of information helps explain why UBS dedicated significant resources to obtaining U.S. clients for its private banking operations in Switzerland. It also explains why the Swiss effort to attract billions to their tax haven may have contributed to the huge tax loss to the U.S. treasury.¹³⁸

UBS also employed systems for its Swiss bankers so that their services for their U.S. clients would not be discovered by U.S. authorities. UBS private bankers were instructed to “keep a low profile during their business trips to avoid attracting attention from U.S. authorities.”¹³⁹ Some UBS Swiss private bankers who visited the United States on business told U.S. customs officials that they were in the country for nonbusiness reasons. UBS even provided its private bankers with training on how to avoid surveillance by U.S. customs agents and law enforcement officers.¹⁴⁰ According to Birkenfeld, Swiss bankers took elaborate measures to disguise or encrypt the account information they brought with them to prevent it from falling into the wrong hands.¹⁴¹ Finally, contrary to U.S. laws and express UBS policies, “some UBS Swiss bankers communicated with their U.S. clients by telephone, fax, mail and email, to market securities products and services, and to carry out securities transactions.”¹⁴²

133. *Id.*

134. *Id.*

135. *Id.*

136. *Id.* at 12–13.

137. *Id.* at 13.

138. *Id.* at 14.

139. *Id.*

140. *Id.*

141. *Id.*

142. *Id.* at 15.

Once accounts were opened, UBS took additional steps to ensure that the accounts of U.S. clients were not discovered by the IRS or the SEC. UBS set up secret bank accounts, so-called “undeclared accounts,” and it assured clients that UBS was not required to disclose those accounts and account information was shielded by Swiss bank secrecy laws.¹⁴³ UBS not only maintained secret undeclared accounts for U.S. clients but also took steps to assist its U.S. clients to structure their Swiss accounts to avoid reporting to the IRS information required by the Qualified Intermediary (QI) program.¹⁴⁴ UBS provided private banking services to approximately 20,000 clients, and nearly 19,000 of these clients concealed their identities and their ownership of the accounts from the IRS.¹⁴⁵ UBS reportedly earned \$200 million in fees per year from these accounts.¹⁴⁶

As a result of the information provided by Birkenfeld, UBS entered into a Deferred Prosecution Agreement (DPA) in which it agreed to pay a fine of \$780 million.¹⁴⁷ As part of the DPA, UBS admitted that from 2002 until 2007, private bankers and managers in the United States participated in a scheme to defraud the IRS by assisting individual taxpayers in establishing accounts at UBS in a manner designed to conceal the taxpayers’ ownership or beneficial interest in these accounts.¹⁴⁸ The private bankers helped create accounts in the names of offshore companies, which allowed U.S. taxpayers to evade reporting requirements on these accounts without being discovered by the IRS.¹⁴⁹ “Although UBS AG signed a QI agreement with the United States in 2001, UBS has never filed 1099 Forms reporting these accounts to the IRS, contending that these U.S. client accounts fall outside its QI reporting obligations.¹⁵⁰ UBS refer[red] to these accounts internally as ‘undeclared accounts.’”¹⁵¹ The IRS has alleged that UBS had 52,000 such accounts.¹⁵² These accounts held billions of dollars that were not disclosed to the IRS.¹⁵³

Despite his contributions to the government’s case against UBS, Birkenfeld was charged and pled guilty to conspiring to defraud the United States (a so-called *Klein* conspiracy).¹⁵⁴ The indictment charged Birkenfeld with falsifying Swiss bank

143. *Id.* at 83.

144. *Id.* at 87. Under the Qualified Intermediary Program, participating institutions signed an agreement where they agreed to report and withhold U.S. taxes with respect to U.S. taxpayers on an aggregate basis, in exchange for not being required to meet the legal obligation to disclose the names of their non-U.S. clients. *Id.* at 3–4.

145. *Id.* at 84.

146. Carlyn Kolker & David Voreacos, *Ex-UBS Banker Birkenfeld Pleads Guilty in Tax Case (Update 3)*, BLOOMBERG (June 19, 2008, 2:47 PM), <http://www.bloomberg.com/apps/news?pid=newsarchive&sid=aLI2YNVAXDLM>.

147. See Deferred Prosecution Agreement ¶ 3, *United States v. UBS AG*, No. 09-60033 (S.D. Fla. dismissed Oct. 25, 2010) [hereinafter UBS DPA], available at http://www.usdoj.gov/tax/UBS_Signed_Deferred_Prosecution_Agreement.pdf.

148. *Id.* at Exhibit B.

149. *Id.* ¶ 21.

150. SENATE REPORT, *supra* note 112, at 9.

151. *Id.*

152. Reeves Declaration, *supra* note 128, ¶ 24.

153. *Id.*

154. Lynnley Browning, *Ex-UBS Banker Pleads Guilty in Tax Evasion*, N.Y. TIMES, June

documents and IRS Forms, failing to prepare and issue required IRS Forms, setting up nominee entities, and failing to comply with the terms of the QI program agreement with the IRS in order to conceal from the IRS U.S.-source income paid into Swiss bank accounts beneficially owned by U. S. taxpayers.¹⁵⁵ Birkenfeld also acted as a personal courier for his clients, at one point smuggling diamonds into the United States in a toothpaste tube.¹⁵⁶ He was sentenced to forty months in jail—an extraordinary sentence for a whistleblower who, it can be argued, single-handedly brought down UBS.¹⁵⁷ However, Birkenfeld received \$104 million as a whistleblower award from the IRS.¹⁵⁸

In 2012, the government indicted Switzerland's oldest bank, Wegelin Bank, and three of its partners. They were charged with assisting U.S. taxpayers, many of whom were former UBS clients, in evading their taxes.¹⁵⁹ The indictments appeared at first to be largely posturing by prosecutors, since Wegelin had no U.S. presence and the individuals were unlikely to make themselves available for extradition.¹⁶⁰ As a result of the indictment, however, the bank essentially ceased to exist as an independent entity within a month.¹⁶¹ In January 2013, Wegelin pled guilty and formally ceased operations.¹⁶² The Department of Justice has investigations pending against at least eleven other Swiss banks.¹⁶³ Charges against additional banks or bankers appear likely.

As with the tax shelter prosecutions, relatively few of the U.S. depositors have been prosecuted.¹⁶⁴ Instead, the IRS and DOJ offered qualified immunity in the

20, 2008, at C1, *available at* <http://www.nytimes.com/2008/06/20/business/20tax.html?gwh=8967C31D46029347101A930F4942DF51>.

155. See Reeves Declaration, *supra* note 128, at Exhibit 31.

156. Browning, *supra* note 154.

157. Dave Ebersole, *Blowing the Whistle on the Dodd-Frank Whistleblower Provisions*, 6 OHIO ST. ENTREPRENEURIAL BUS. L.J. 123, 131 (2011); Morse, *supra* note 52, at 712 n.148.

158. David Kocieniewski, *Get Out of Jail Free? No, It's Better*, N.Y. TIMES, Sept. 12, 2012, at A1, *available at* <http://www.nytimes.com/2012/09/12/business/whistle-blower-awarded-104-million-by-irs.html?gwh=2F068C33CE1A7F435F2D42E2AF339C25>.

159. Christoph Eisenring, *Die Checkliste der US-Justiz*, NEUE ZÜRCHER ZEITUNG (Jan. 19, 2012), <http://www.nzz.ch/aktuell/wirtschaft/uebersicht/die-checkliste-der-us-justiz-1.14406167>; David Voreacos, *Swiss Bank Wegelin Charged in U.S. with Aiding Tax Evasion*, BLOOMBERG BUSINESSWEEK (Feb. 3, 2012), <http://www.businessweek.com/news/2012-02-03/swiss-bank-wegelin-charged-in-u-dot-s-dot-with-aiding-tax-evasion>; Robert W. Wood, *Judge Gives IRS Access to More Accounts at UBS and Wegelin*, FORBES (Jan. 29, 2013, 12:00 AM), <http://www.forbes.com/sites/robertwood/2013/01/29/judge-gives-irs-access-to-more-accounts-at-ubs-and-wegelin/>.

160. See Wood, *supra* note 159.

161. Haig Simonian, *Wegelin Becomes Victim of US Tax Dispute*, FIN. TIMES (Jan. 27, 2012, 5:13 PM), <http://www.ft.com/intl/cms/s/0/864c58ca-48fc-11e1-88f0-00144feabdc0.html#axzz21ZLScv2B>.

162. Christoph Eisenring, *Bank Wegelin: Sich Nicht In Falscher Sicherheit Wiegen*, NEUE ZÜRCHER ZEITUNG (Jan. 5, 2013, 6:00 AM), <http://www.nzz.ch/aktuell/wirtschaft/wirtschaftsnachrichten/-1-1.17922024>.

163. James Shotter, *Pictet Confirms DOJ Investigation*, FIN. TIMES (Nov. 26, 2012, 7:39 PM), <http://www.ft.com/cms/s/0/e77d1aa6-37d7-11e2-8edf-00144feabdc0.html#axzz2JD oEVXvQ>.

164. Between December 2007 and June 2013, the government indicted approximately eighty-five taxpayers for failing to disclose offshore accounts. Jack Townsend, *Offshore*

form of a series of offshore voluntary disclosure initiatives.¹⁶⁵ In an effort to obtain the names of those U.S. taxpayers who held undeclared accounts at UBS, the U.S. government filed a so-called John Doe summons.¹⁶⁶ Significantly, the John Doe summons litigation was resolved by agreement between the U.S. and the Swiss governments (and not UBS).¹⁶⁷

The tax haven bank prosecutions and offshore voluntary disclosure initiatives have dramatically changed the way in which U.S. taxpayers view and utilize tax haven banks.¹⁶⁸ The decision to prosecute tax and banking professionals therefore appears on many levels to be a success. But is the government's new prosecution policy the right one? The next two Parts will address this question.

III. THE NEW PROSECUTION POLICY AND CRIMINAL THEORY

It may seem credulous to ask whether prosecuting lawyers, accountants, and bankers for assisting their clients in evading their taxes is the "right" policy. However, the question of whether conduct should result in a criminal charge is often not easy to answer.¹⁶⁹ Indeed, legal thinkers and philosophers have long

Charges / Convictions Spreadsheet, FED. TAX CRIMES, <http://federaltaxcrimes.blogspot.com> (last modified Sept. 18, 2013). During that same period, the IRS accepted more than 33,000 offshore voluntary disclosures. See *IRS Says Offshore Effort Tops \$5 Billion, Announces New Details on the Voluntary Disclosure Program and Closing of Offshore Loophole*, I.R.S. News Release IR-2012-64 (June 26, 2012), available at [http://www.irs.gov/uac/IRS-Says-Offshore-Effort-Tops-\\$5-Billion,-Announces-New-Details-on-the-Voluntary-Disclosure-Program-and-Closing-of-Offshore-Loophole](http://www.irs.gov/uac/IRS-Says-Offshore-Effort-Tops-$5-Billion,-Announces-New-Details-on-the-Voluntary-Disclosure-Program-and-Closing-of-Offshore-Loophole). But see Alison Bennett, *Former Boeing Sales Manager Pleads Guilty to Filing False Return, Hiding Assets in UBS*, in 191 DAILY TAX REPORT K-1 (2009); *Florida Watchmaker to Pay \$5 Million Fine for Failing to Disclose Swiss UBS Accounts*, 5 WHITE COLLAR CRIME REP. (BNA), Feb. 12, 2010, at 101; Stephen Joyce, *Former UBS Account Holder Admits to Concealing Assets to Evade Taxes*, 5 WHITE COLLAR CRIME REP. (BNA), Dec. 31, 2010, at 926.

165. See, e.g., Jeremiah Coder, *IRS Extends Offshore Voluntary Disclosure Deadline*, in 124 TAX NOTES 1297 (2009).

166. A "John Doe summons" is a summons issued to a third party, like a bank, seeking information regarding taxpayers whose identities are currently unknown to the IRS. *In re Tax Liabilities of John Does*, 671 F.2d 977, 978 (6th Cir. 1982). Thus, the purpose of a John Doe summons is not just to further an investigation of a given taxpayer. Rather, it is to find out who the taxpayers are so that an investigation may be undertaken in earnest. JOHN A. TOWNSEND, LARRY A. CAMPAGNA, STEVE JOHNSON, SCOTT A. SCHUMACHER, *TAX CRIMES* 224-26 (Paul L. Caron et al. eds., 2008). The John Doe summons procedures require the IRS to convince a court that (1) the investigation relates to a particular person or ascertainable group of persons; (2) there is reasonable cause to believe that the person or persons identified may not have complied with the tax laws; and (3) the information sought is not readily available from other sources. 26 U.S.C. § 7609(f) (2012).

167. Lynnley Browning, *I.R.S. to Drop Suit Against UBS Over Tax Havens*, N.Y. TIMES, Aug. 27, 2010, at B6, available at <http://www.nytimes.com/2010/08/27/business/global/27suisse.html>.

168. For a more detailed treatment of this issue, see *infra* notes 297-307 and accompanying text.

169. The government's change in policy might arguably be sufficient to question the propriety of the current policy; that is, if it is so obvious that Swiss bankers should be prosecuted for assisting clients to hide money, why weren't they prosecuted sooner?

struggled with defining precisely what is and what should be criminal.¹⁷⁰ The challenge is to distinguish between actions that warrant criminal prosecution and those that only justify civil penalties or no penalty at all. At its most basic, criminal law should sanction conduct that is only unequivocally wrong or clearly blameworthy.¹⁷¹ As H. L. A. Hart noted, “Why are certain kinds of action forbidden by law and so made crimes or offences? The answer is: To announce to society that these actions are not to be done and to secure that fewer of them are done.”¹⁷²

At a minimum, before criminal liability can be imposed, the conduct in question should be clearly distinguishable from conduct that is not subject to criminal penalties.¹⁷³ This clear distinction is essential to our criminal justice system.¹⁷⁴ Doctrines such as the rule of lenity and void for vagueness,¹⁷⁵ as well as the Ex Post Facto Clause,¹⁷⁶ all essentially ask whether the criminal statute in question has made it reasonably clear that the defendant's conduct was criminal.¹⁷⁷ In addition, only upon criminal investigation or indictment will certain constitutional protections be applied.¹⁷⁸ Thus, a lack of clarity and firm definition of what is and should be criminal is worrisome, given that so many rights and indeed some of the greatest rights—life, liberty, and property—are dependent upon this distinction.¹⁷⁹

Traditional definitions of what conduct is criminal requires that there be both an *actus reus* and *mens rea*.¹⁸⁰ There also must be a public element to the conduct, since it is a violation of the public order of the State, the People, or the United States in whose name the case is brought that makes a matter criminal.¹⁸¹ To

170. *See, e.g.*, 1 JOHN AUSTIN, LECTURES ON JURISPRUDENCE, OR, THE PHILOSOPHY OF POSITIVE LAW 518 (Robert Campbell ed., 4th ed. 1879); JEREMY BENTHAM, THE RATIONALE OF PUNISHMENT 4 (Robert Heward 1830); H.L.A. HART, PUNISHMENT AND RESPONSIBILITY (1968); Antony Duff, *Legal Punishment*, STAN. ENCYCLOPEDIA PHILOSOPHY, <http://plato.stanford.edu/entries/legal-punishment/> (revised May 13, 2013).

171. STUART P. GREEN, LYING, CHEATING, AND STEALING: A MORAL THEORY OF WHITE-COLLAR CRIME 1 (2006).

172. HART, *supra* note 170, at 6.

173. GREEN, *supra* note 171.

174. *See* Wayne A. Logan, *The Ex Post Facto Clause and the Jurisprudence of Punishment*, 35 AM. CRIM. L. REV. 1261, 1275–76 (1998).

175. *See, e.g.*, United States v. Lanier, 520 U.S. 259, 266 (1997) (describing these doctrines as manifestations of a “fair warning requirement”).

176. U.S. CONST. art. I, § 10, cl. 1. The Ex Post Facto Clause ensures that legislative acts “give fair warning of their effect and permit individuals to rely on their meaning until explicitly changed.” Weaver v. Graham, 450 U.S. 24, 28–29 (1981).

177. *Lanier*, 520 U.S. at 266.

178. *See, e.g.*, United States v. Ward, 448 U.S. 242, 255 (1980) (Blackmun, J., dissenting).

179. Landgraf v. USI Film Prods., 511 U.S. 244, 265 (1994) (“Elementary considerations of fairness dictate that individuals should have an opportunity to know what the law is and to conform their conduct accordingly; settled expectations should not be lightly disrupted.”) (citation omitted).

180. GREEN, *supra* note 171, at 10; *see* MODEL PENAL CODE §§ 2.01, 2.02 (1985); *see also* Robinson v. California, 370 U.S. 660, 667 (1962) (holding California law making it illegal to be a drug addict unconstitutional because the mere status of being an addict was not an *act* and thus not criminal).

181. Nonpublic or private wrongs are handled as torts. That said, some tortious actions

borrow a phrase from Henry II's time, it is the King's peace that is being violated.¹⁸² But on closer inspection, even these most basic definitions begin to blur. If we assume that a crime must have some sort of act (*actus reus*), that definition of crime breaks down in practice. For example, it is a crime to fail to file a tax return.¹⁸³ Thus, the "guilty act" in that crime is in reality the failure to act.¹⁸⁴ One can also be guilty of attempts and other inchoate crimes, where the act has not been completed or perfected. In these cases it is the desire to bring about the result, rather than the act itself that is the crime.¹⁸⁵

In conspiracy law the outer reaches of the *actus reus* requirement are encountered. The essence of a conspiracy is the agreement itself.¹⁸⁶ In order to establish the existence of an agreement, the prosecution must show that the defendant and at least one other person reached an understanding or agreement to carry out the objective of the conspiracy.¹⁸⁷ As long as a defendant understands the unlawful nature of the scheme and knowingly and intentionally joins in that scheme, that is sufficient to convict him or her for conspiracy. Thus, while we have traditionally defined a crime as one that requires an *actus reus* and *mens rea*, in modern conspiracy law a person can be convicted of a crime by merely agreeing to participate in some future illegal venture.¹⁸⁸ No act or failure to act by that person is required.¹⁸⁹

The ambiguity of criminal law is even more pronounced in the case of white-collar crimes, where it is often difficult to determine whether the actions in question should be subject to criminal liability. In this regard, Stuart Green stated:

that appear to be only between two private individuals can also be the basis of a criminal case. *See, e.g.*, WASH. REV. CODE § 9A.36.011 (1997) (assault in the first degree).

182. Henry II used this ancient Anglo-Saxon concept to expand his authority over criminal matters. Henry used the concept of the violation of the King's Peace to obtain jurisdiction over legal matters at the expense of the baronial courts. "[I]t was not until the reign of Henry II (1154–1189) in England that national courts were developed, administering law for the entire realm in vindication of the 'King's Peace' through the King's judges." Sheldon Glueck, *The Nuernberg Trial and Aggressive War*, 59 HARV. L. REV. 396, 445 n.136 (1946) (citations omitted).

183. 26 U.S.C. § 7203 (2012).

184. The Model Penal Code defines *actus reus* to include omissions. MODEL PENAL CODE § 2.01(1) (1985).

185. 2 WAYNE R. LAFAYE, SUBSTANTIVE CRIMINAL LAW § 11.5(a)(2) (2d ed. 2003).

186. As Justice Jackson noted: "The modern crime of conspiracy is so vague that it almost defies definition. Despite certain elementary and essential elements, it also, chameleon-like, takes on a special coloration from each of the many independent offenses on which it may be overlaid. It is always 'predominantly mental in composition' because it consists primarily of a meeting of minds and an intent." *Krulewitch v. United States*, 336 U.S. 440, 446–48 (1949) (Jackson, J., concurring) (footnotes omitted) (quoting Albert J. Harno, *Intent in Criminal Conspiracy*, 89 U. PA. L. REV. 624, 632 (1941)).

187. *See, e.g.*, *United States v. Barnes*, 604 F.2d 121, 161 (2d Cir. 1979).

188. *See Iannelli v. United States*, 420 U.S. 770, 777 (1975).

189. *United States v. Kozeny*, 667 F.3d 122, 130–32 (2d Cir. 2011) (holding that while an overt act must be committed in furtherance of the conspiracy, the act need not be illegal in and of itself, jury does not need to agree as to the overt act, and the act is not required to be an element of the offense).

[W]hat distinguishes “white-collar” offenses such as bribery, obstruction of justice, perjury, and insider trading from core “blue collar” offenses such as murder, rape, and assault is that the white-collar crimes tend to be more “morally ambiguous” than the core crimes. That is, in a surprisingly large number of cases there is genuine doubt as to whether what the defendant did was in fact morally wrong. In such cases, the issue is not, as it is with necessity, whether the defendant was confronted with some extraordinary choice between either obeying the law, and allowing significant harm to occur, or violating the law, and preventing such harm. Rather, the question is whether the conduct engaged in was more or less acceptable behavior that should not have been subject to criminal sanctions in the first place.¹⁹⁰

Even if the focus was to shift from whether conduct should be subject to criminal sanctions to whether conduct in fact falls within existing criminal statutes, the answer is little clearer. When looking at the statutes regarding white-collar crimes, the action not to be done¹⁹¹ is far from clear, and the line between what is criminal and what is civil is blurred at best.

A good example is one of the oldest federal crimes, mail fraud.¹⁹² The mail fraud statute provides in pertinent part: “Whoever, having devised or intending to devise any scheme or artifice to defraud, or for obtaining money or property by means of false or fraudulent pretenses, representations, or promises,” uses the mails for the purpose of executing the scheme, is guilty of a felony punishable by up to twenty years in prison.¹⁹³ What constitutes a scheme or artifice to defraud? Pretty much any conduct, it seems. The Fifth Circuit “defined” this as any “conduct which fails to match the ‘reflection of moral uprightness, of fundamental honesty, fair play and right dealing in the general and business life of members of society.’”¹⁹⁴ It has also been summarized as “an effort to gain an undue advantage or to bring about some harm through misrepresentation or breach of duty.”¹⁹⁵

What rights are protected and who should be protected from harm? Property?¹⁹⁶ Honest services?¹⁹⁷ Since the mail fraud statute is a criminal statute—a twenty-year felony no less!—we must assume that it covers only conduct that is clearly blameworthy.¹⁹⁸ However, even a cursory tour through the case law in this area

190. Stuart P. Green, *What Is Wrong with Tax Evasion?*, 9 Hous. Bus. & Tax L.J. 221, 223 (2009) (footnote omitted).

191. HART, *supra* note 170, at 6.

192. 18 U.S.C. § 1341 (2012).

193. *Id.*

194. *Blachly v. United States*, 380 F.2d 665, 671 (5th Cir. 1967) (quoting *Gregory v. United States*, 253 F.2d 104, 109 (5th Cir. 1958)).

195. KATHLEEN F. BRICKEY, *CORPORATE AND WHITE COLLAR CRIME: CASES AND MATERIALS* 88–89 (5th ed. 2011).

196. *See McNally v. United States*, 483 U.S. 350, 360 (1987) (limiting the application of § 1341 to the protection of property rights).

197. *See Skilling v. United States*, 130 S. Ct. 2896 (2010) (applying the updated version of § 1341 to the intangible right of honest services).

198. *See GREEN*, *supra* note 171, at 1.

shows this not to be the case.¹⁹⁹ “The federal criminal code is filled with crimes that have neither common-law analogues nor well-established public meanings. Mail fraud has no public definition, no Platonic form on which to model the relevant criminal statute. Congress is free to define the crime as it wishes.”²⁰⁰

A. The Ambiguity of Tax Crimes

As Stuart Green has noted, tax crimes suffer from ambiguity in spades.²⁰¹ This ambiguity problem is both definitional and moral.²⁰² Reducing one’s taxes through “avoidance” measures or strategies is perfectly legal and long-accepted conduct,²⁰³ while reducing one’s taxes through “evasion” is a crime. However, the line between legal tax avoidance and illegal tax evasion is often not clear.²⁰⁴ For example, it is a crime to move assets out of the reach of the IRS to avoid the payment of taxes.²⁰⁵ If a taxpayer knows the IRS is about to levy on a bank account, is it a crime for the taxpayer not to deposit a paycheck into that bank account? Likely not. Is it a crime to open a new bank account in the taxpayer’s name in the same city and deposit the check in that account? Again, likely not. What about opening an account in another city or another country? At this point, most would probably agree that a crime has been committed. In each instance the taxpayer has taken actions to avoid (and arguably evade) the payment of his or her taxes, and yet only the more egregious actions are deemed to be criminal.

What differentiates legal avoidance from illegal evasion is the mental state of the taxpayer. It is because the taxpayer intentionally violates a known legal duty that his act is criminal.²⁰⁶ Thus, tax crimes, perhaps more than any other type of crime, are illegal solely because of the mental state of the actor.²⁰⁷ While it is true that nearly every crime requires a mens rea,²⁰⁸ the underlying conduct in nontax crimes is at least frowned upon in its noncriminal guise.²⁰⁹ For example, while 18

199. See, e.g., *Skilling*, 130 S. Ct. at 2896 (conviction for honest-services fraud reversed).

200. William J. Stuntz, *Plea Bargaining and Criminal Law’s Disappearing Shadow*, 117 HARV. L. REV. 2548, 2567 (2004). I would add to this, prosecutors and courts are equally free to define mail fraud as they wish. See *Skilling*, 130 S. Ct. at 2936–41 (Scalia, J., concurring).

201. Green, *supra* note 190, at 222.

202. *Id.* at 223, 227.

203. See, e.g., *Helvering v. Gregory*, 69 F.2d 809, 810 (2d Cir. 1934).

204. See, e.g., Joseph Bankman, *The New Market in Tax Shelters*, 83 TAX NOTES 1775, 1782 (1999).

205. 26 U.S.C. § 7201 (2012); *Sansone v. United States*, 380 U.S. 343, 354 (1965).

206. But as Green has noted, this highest state of culpability allows a mistake or ignorance of the law to be a defense, and as a result one can intentionally understate a tax liability and not be guilty of a crime. Green, *supra* note 190, at 228. Thus, even the heightened mental state, which was designed to prevent prosecutions for mere inadvertent or mistaken violations of the tax laws, actually adds to its moral and legal ambiguity.

207. It is true that there is an actus reus, or at least an “omission reus,” element in every tax crime. However, what distinguishes criminal evasion from legal avoidance is the mental state of the actor. Compare 26 U.S.C. § 7201 (2012), with *id.* § 6662.

208. See HART, *supra* note 170, at 17–24 (explaining that those who lack fault should not be liable to criminal punishment).

209. Even conspiracy, the essence of which is the agreement, is an agreement to do

U.S.C. § 1001 criminalizes only knowingly and willfully making a materially false statement to a government official, no one would argue that it is acceptable to make nonwillful false statements to an FBI agent—it might not be a crime, but it is still not acceptable behavior. By contrast, tax minimization is not generally frowned upon and indeed is looked upon by many as a social good. Learned Hand’s aphorism is a perfect example: “Any one may so arrange his affairs that his taxes shall be as low as possible; he is not bound to choose that pattern which will best pay the Treasury; there is not even a patriotic duty to increase one’s taxes.”²¹⁰ Moreover, much of the professional tax services industry is based on the notion that tax minimization is right and proper.²¹¹ Accordingly, precisely the same conduct causing precisely the same harm²¹² can be criminal or not, depending on the mental state of the taxpayer.

Basing prosecution decisions either solely or primarily on the mental state of the person committing the act is even more troubling when the taxpayer is a corporation. More than 100 years ago, the Supreme Court resolved the question of whether corporations can commit crimes and held that if a corporation can enter into contracts and lay railroad tracks, it can commit crimes.²¹³ But in the context of the tax crimes, how does a corporate defendant “know” what the tax laws require and “intentionally” violate these laws? How can a corporation “know” the object of a conspiracy and agree to join in it? In answering these questions, the First Circuit stated:

The acts of a corporation are, after all, simply the acts of all of its employees operating within the scope of their employment. The law on corporate criminal liability reflects this. Similarly, the knowledge obtained by corporate employees acting within the scope of their employment is imputed to the corporation. Corporations compartmentalize knowledge, subdividing the elements of specific duties and operations into smaller components. The aggregate of those components constitutes the corporation’s knowledge of a particular operation. It is irrelevant whether employees administering one component of an operation know the specific activities of employees administering another aspect of the operation²¹⁴

Thus, the legal fiction that a corporation is a person carries over to the “mental state” of the corporate personage in the collective knowledge doctrine.²¹⁵ But as

something illegal. *See, e.g.*, *United States v. Brown*, 587 F.3d 1082, 1089 (11th Cir. 2009).

210. *Helvering v. Gregory*, 69 F.2d 809, 810 (2d Cir. 1934).

211. The role of tax professionals assisting in tax minimization is enshrined in the rules protecting taxpayers from accuracy-related civil penalties. 26 C.F.R. § 1.6664-4 (2012).

212. Whether the “harm” is the same in these instances is debatable, depending upon how one defines harm. The reduction of funds to the Treasury is the same; however, the blatant abuse of the system is not.

213. *New York Cent. & Hudson River R.R. v. United States*, 212 U.S. 481 (1909).

214. *United States v. Bank of New England*, 821 F.2d 844, 856 (1st Cir. 1987) (citations omitted).

215. *See, e.g.*, Gregory L. Diskant, *Trial Balloon: Rethinking Corporate Criminal Liability*, LITIGATION, Winter 2008, at 5; Dick Thornburgh, *The Dangers of Over-Criminalization and the Need for Real Reform: The Dilemma of Artificial Entities and*

Professor David Luban noted, this doctrine “treats employees as synapses in the nonexistent brain of a legal fiction,” where the corporation knows the sum of all of the knowledge of its employees, whether or not they discussed what they knew or actually combined their knowledge.²¹⁶ Such a theory teeters on the “brink of quack metaphysics or mystical science fiction, treating groups of people as single minds.”²¹⁷ Thus, tax crimes, when applied to corporations with multiple actors who must collectively “know” the law and “intentionally” violate it, achieve the acme of ambiguity. It is little wonder the Tax Division of the Department of Justice has a stated policy preferring to prosecute individuals rather than corporations.²¹⁸

B. Inconsistent Enforcement

Adding to the ambiguity of tax and other white-collar criminal statutes is the inconsistent nature of white-collar criminal enforcement. No criminal law is uniformly enforced, but this lack of uniformity is more pronounced in white-collar criminal cases. Inconsistent and uneven enforcement is due not only to the limited availability of resources,²¹⁹ but also to structural reasons. White-collar crimes are not like violent felonies, for which investigation and prosecution are almost mandatory. Rather, for federal white-collar crimes, prosecution is almost always optional.²²⁰ “Federal law is thus a source of options rather than obligations. With very little in the way of legal *or* political constraints, federal prosecutors are the criminal justice system’s free agents.”²²¹ Thus, the “law” that federal prosecutors make is much more likely a result of the prosecutors’ preferences than those of the legislature.²²²

Tax crimes showcase the inconsistent enforcement of federal crimes. As discussed, tax crimes are, in essence, violations of the tax laws where one does so “willfully.”²²³ Thus, one can file an incorrect return and be subject to negligence penalties or no penalties at all.²²⁴ However, if one willfully files an incorrect (read: false) return, that could result in a criminal charge of filing a false tax return or tax evasion.²²⁵ Similarly, if a person fails to file a tax return, a failure to file penalty may be imposed.²²⁶ However, if that failure to file is willful, a criminal charge may

Artificial Crimes, 44 AM. CRIM. L. REV. 1279 (2007).

216. David Luban, *Contrived Ignorance*, 87 GEO. L.J. 957, 963–64 (1999).

217. *Id.* at 963.

218. U.S. DEP’T OF JUSTICE, U.S. ATTORNEYS’ MANUAL § 9-28.400 (2008) [hereinafter USAM], available at http://www.justice.gov/usao/eousa/foia_reading_room/usam/title9/28mcrm.htm#9-28.40.

219. For example, the *Criminal Tax Manual* provides: “Because there are insufficient resources to prosecute all violations, deterring others from violating the tax laws is a primary consideration.” U.S. DEP’T OF JUSTICE, CRIMINAL TAX MANUAL § 1.01[4] (2008), available at <http://www.justice.gov/tax/readingroom/2008ctm/CTM%20Chapter%201.pdf>.

220. See Stuntz, *supra* note 200, at 2566.

221. *Id.* (emphasis in original).

222. See *id.* at 2567.

223. See, e.g., *Cheek v. United States*, 498 U.S. 192 (1991).

224. See, e.g., *Am. Boat Co. v. United States*, 583 F.3d 471, 480–86 (7th Cir. 2009).

225. 26 U.S.C. § 7206(1) (2012).

226. 26 U.S.C. § 6651 (2012).

result.²²⁷ Thus, if a person knows of the legal duty to file and intentionally does not do so, he or she is, under the clear and unambiguous language of the statute, guilty of the misdemeanor of failure to file.

Yet very few tax violations that fit the literal definition are prosecuted or even investigated as criminal cases. The proof of willfulness in a failure to file case can be shown by the fact that the taxpayer filed in prior years, thereby demonstrating the taxpayer knew of the duty to file.²²⁸ Without some excuse like illness or incapacity, a failure to file case should be easy for the government to prove. Nevertheless, remarkably few tax cases are investigated and prosecuted.²²⁹ And this is not attributable to just the allocation of scarce resources, which, as indicated, undoubtedly plays a role. This is not a case in which selling drugs is illegal, but there are too many drug transactions for them all to be prosecuted. In those cases, police and prosecutors do not maintain that the narcotics transaction is legal. However, many cases that would clearly be provable as a tax crime are not even viewed as criminal in nature by IRS personnel. Routine failures to file, even those that have lasted a decade or more, are rarely thought to be criminal, unless the taxpayer had illegal income or had some other aggravating factor.²³⁰ Indeed, in cases of a failure to file of ten or more years, the IRS generally only asks for six years of returns.²³¹ IRS agents have a duty to refer cases for criminal investigation where they have uncovered “firm indications of fraud,”²³² but cases that are clearly within that definition are nonetheless not consistently referred. It is not the mere failure to file or omission of income that warrants a criminal referral.²³³ Rather, it generally must be combined with some other fraudulent or obstructive act.²³⁴

Accordingly, the vagueness of tax crimes and other white-collar crimes must be viewed not only from the perspective of not knowing what is illegal and will be prosecuted, but also from the perspective that what is clearly illegal will not be prosecuted. As discussed more fully below, this failure to prosecute clear violations of the law gave some people the impression that they could act with impunity.

227. 26 U.S.C. § 7203 (2012).

228. *United States v. Daraio*, 445 F.3d 253, 264 (3d Cir. 2006); *United States v. Bok*, 156 F.3d 157, 165 (2d Cir. 1998).

229. In 2011, the IRS initiated only 4720 criminal investigations and recommended prosecution in 3410 of these cases. Of those referred, the Justice Department issued 2998 indictments or informations. INTERNAL REVENUE SERV., 2011 DATA BOOK 44 (2011), available at <http://www.irs.gov/pub/irs-soi/11databk.pdf>. During that same period, the IRS asserted delinquency penalties in 3,736,987 cases. *Id.* at 42.

230. INTERNAL REVENUE SERV., INTERNAL REVENUE MANUAL § 5.1.11.6.1 (2010), available at <http://www.irs.gov/irm/>.

231. *See id.*

232. *See id.* § 25.1.3.1 (2009).

233. *See supra* note 229 and accompanying text.

234. *Id.* at § 4.23.9.6.2 (2008). Interestingly, this is much the same distinction as exists in Swiss law. *See Weber, supra* note 5 and accompanying text.

C. The Problems with All This Vagueness

The vagueness of white-collar criminal statutes does not, of course, render every prosecution immediately suspect. However, it is (or should be) a concern for policymakers and anyone who has an interest in good government. Society will lose faith in the criminal justice system if the law is perceived as being applied arbitrarily or unfairly.²³⁵ The fundamental problem with the vagueness of these statutes is that it shifts who ultimately defines what is criminal from the legislature to prosecutors. This is not a new problem. As was noted more than 250 years ago, “Nay whoever hath an absolute authority to interpret any written or spoken laws it is he who is the lawgiver to all intents and purposes and not the person who first wrote or spake them.”²³⁶

Thus, at one level, regardless of the merits of any given prosecution, the “existence and exercise of prosecutorial discretion are inconsistent with the most fundamental principles of our system of justice and our basic notions of fair play and efficient criminal administration.”²³⁷ If a law is vague, anything or nothing fits the definition. Prosecutors can tolerate conduct and then condemn it without any justification. As Justice Jackson stated: “With the law books filled with a great assortment of crimes, a prosecutor stands a fair chance of finding at least a technical violation of some act on the part of almost anyone.”²³⁸ The number and breadth of federal crimes has exploded in the seventy years since that statement was uttered. The vagueness of criminal statutes allows prosecutors, rather than legislatures, to define what is criminal and what is not.

The presence of judge and jury to prevent convictions does not fully remedy this problem. First, as has become more apparent with the work of programs such as the Innocence Project around the country, innocent people do get convicted of crimes they did not commit.²³⁹ Second, the gravity of the decision to charge cannot be underestimated, for once a person is charged and becomes a “defendant,” his or her life will never be the same again. And, as the prosecution of Arthur Andersen proved, for institutional targets indictment alone can be a death sentence.²⁴⁰

235. PAUL H. ROBINSON & JOHN M. DARLEY, *JUSTICE, LIABILITY, AND BLAME* (1995).

236. H.L.A. HART, *THE CONCEPT OF LAW* 141 (2d ed. 1994) (attributing the quote to Bishop Hoadly).

237. James Vorenberg, *Decent Restraint of Prosecutorial Power*, 94 HARV. L. REV. 1521, 1554 (1981).

238. Robert H. Jackson, *The Federal Prosecutor*, 24 J. AM. JUDICATURE SOC'Y 18, 19 (1940).

239. See, e.g., Sara Jean Green, *3 Convicted in State Cleared*, SEATTLE TIMES, Dec. 21, 2010, at B1, available at http://seattletimes.nwsourc.com/html/localnews/2013726446_innocence21m.html.

240. Arthur Andersen, formerly the world's largest accounting firm, shut down within months of its indictment, even before its trial and conviction. “During such time, there was considerable debate within the DOJ as to the legal, practical, and moral consequences of indictments against corporate defendants. Those discussions emphasized that while corporate wrongdoers needed to be brought to justice, regulators also needed to carefully consider the collateral consequences of corporate prosecutions.” John Ashcroft & John Ratcliffe, *The Recent and Unusual Evolution of an Expanding FCPA*, 26 NOTRE DAME J.L. ETHICS & PUB. POL'Y 25, 31 (2012).

Thus, the pervasive ambiguity in criminal statutes is a cause for concern. Most of the literature in this area addresses overenforcement of criminal law and the disparate treatment that decisions to prosecute entail.²⁴¹ However, it is also necessary to examine the impact of underenforcement and the decision not to bring prosecutions.²⁴² Underenforcement, among other problems, erodes citizens' beliefs in and commitment to follow the law and to the legal system itself.²⁴³ And while much of the scholarship in this area has been focused on the impact enforcement failures have had on so-called "underenforcement zones" and the racial and ethnic minorities within these communities, underenforcement can also impact the laws themselves.²⁴⁴

There is perhaps no better example of the impact of underenforcement on citizens' views of the law than in tax enforcement.²⁴⁵ The decades of tolerating the tax shelter industry contributed to its expansion, leading to a situation in which the best and brightest in the tax field were creating transactions out of whole cloth that generated losses in the hundreds of millions of dollars.²⁴⁶ Likewise, tolerance of, or at least indifference to, offshore bank accounts led at least in part to their expansion.²⁴⁷

D. Prosecution Policies

Given the vagueness of criminal statutes, particularly tax and other white-collar criminal statutes, it is essential that prosecutors be guided by definite prosecution policies. What, then, should prosecutors consider in deciding whether and whom to prosecute? While a full treatment of this subject is beyond the scope of this paper, a few fundamentals can be gleaned. As Professor Antony Duff stated:

[T]he most plausible immediate good that a system of punishment can bring is the prevention of crime: a rational consequentialist system of law will define as criminal only conduct that is in some way harmful; in preventing crime we will thus be preventing the harms that crime causes; and punishment can prevent crime by incapacitating, or deterring, or reforming potential offenders.²⁴⁸

241. See e.g., William J. Stuntz, *The Pathological Politics of Criminal Law*, 100 MICH L. REV. 505 (2001).

242. See Alexandra Natapoff, *Underenforcement*, 75 FORDHAM L. REV. 1715, 1717 (2006).

243. *Id.* at 1750.

244. See *id.* at 1717–18.

245. See, e.g., Jeffrey A. Dubin, *Criminal Investigation Enforcement Activities and Taxpayer Noncompliance*, 35 PUB. FIN. REV. 500, 502 (2007); see also Joshua D. Blank & Daniel Z. Levin, *When Is Tax Enforcement Publicized?*, 30 VA. TAX REV. 1 (2010).

246. The millions of dollars in fees these tax professionals collected undoubtedly had something to do with the popularity of these transactions as well.

247. See Lee Sheppard, *Our Hypocrisy on Tax Havens*, FORBES (July 22, 2010, 5:34 PM), available at <http://www.forbes.com/2010/07/22/tax-finance-havens-economy-opinions-columnists-lee-sheppard.html>.

248. Duff, *supra* note 170, § 3.

Thus, criminal law seeks to incapacitate offenders, deter future offenses, reform offenders, and obtain retribution on behalf of victims.²⁴⁹

The *U.S. Attorneys' Manual* instructs federal prosecutors to pursue a criminal prosecution only if the person's conduct constitutes a federal offense and admissible evidence will "probably be sufficient to obtain and sustain a conviction."²⁵⁰ The only limits placed on this broad grant of authority is that a prosecution should nevertheless not be pursued if there is no "substantial federal interest" involved in the case, the person is subject to effective prosecution elsewhere, or there is a sufficient noncriminal alternative to prosecution.²⁵¹ The definition of "substantial federal interest" instructs prosecutors that in determining whether there is a substantial federal interest, a prosecutor should weigh all relevant considerations, including: federal law enforcement priorities, the nature and seriousness of the offense, the deterrent effect of the prosecution, and the target's culpability.²⁵²

These prosecution policies are further amplified by the policies concerning the investigation and prosecution of business entities. This policy instructs that the prosecution of corporate crime is a "high priority" for the Department of Justice.²⁵³ It then outlines the "critical public interests" that are promoted by the investigation and prosecution of business entities, including: (1) protecting the integrity of the capital markets, (2) protecting consumers, investors, and competing business entities, and (3) protecting the environment.²⁵⁴

The Criminal Tax Case Procedures in the *U.S. Attorneys' Manual* is even more explicit in defining a prosecution policy in tax cases:

The Government helps to preserve the integrity of this Nation's self-assessment tax system through vigorous and uniform criminal enforcement of the internal revenue laws. Criminal prosecutions punish tax law violators and deter other persons who would violate those laws. To achieve maximum deterrence, the Government must pursue broad, balanced, and uniform criminal tax enforcement. Uniformity in tax cases is necessary because tax enforcement potentially affects more individuals than any other area of criminal enforcement.²⁵⁵

Thus, the government's prosecution policies, particularly the Tax Division's policy, follow the traditional bases for criminal liability: retribution and deterrence, particularly general deterrence. The importance of general deterrence in tax cases has been codified in the U.S. Sentencing Commission's sentencing guidelines, which provide:

249. Darryl K. Brown, *Cost-Benefit Analysis in Criminal Law*, 92 CALIF. L. REV. 323, 325 (2004). In recent years rehabilitation of the offender has been abandoned as a justification for punishment. See, e.g., D.A. Andrews & James Bonta, *Rehabilitating Criminal Justice Policy and Practice*, 16 PSYCHOL. PUB. POL'Y & L. 39 (2010).

250. USAM, *supra* note 218, § 9-27.220.

251. *Id.*

252. *Id.* § 9-27.230.

253. *Id.* § 9-28.100.

254. *Id.*

255. *Id.* § 6-4.010.

The criminal tax laws are designed to protect the public interest in preserving the integrity of the nation's tax system. Criminal tax prosecutions serve to punish the violator and promote respect for the tax laws. Because of the limited number of criminal tax prosecutions relative to the estimated incidence of such violations, deterring others from violating the tax laws is a *primary consideration* underlying these guidelines. Recognition that the sentence for a criminal tax case will be commensurate with the gravity of the offense should act as a deterrent to would-be violators.²⁵⁶

The Tax Division's policy, however, departs somewhat from traditional rationales in that the stated purpose of the criminal enforcement program is also "to preserv[e] the integrity" of the civil tax system.²⁵⁷ The policy also specifically provides that maximum deterrence depends upon uniform and consistent criminal enforcement.²⁵⁸ Hence, the Tax Division is the only division authorized to approve an indictment for tax crimes, and an individual U.S. attorney may not bring a tax prosecution without the approval of the Tax Division.²⁵⁹ As discussed above, the government's prosecution policy did not always preserve the integrity of the tax system.²⁶⁰

Finally, in deciding whether to proceed against an entity or the individuals who took the actions on behalf of the entity, the Department of Justice looks at the nature and seriousness of the offense committed, the pervasiveness of wrongdoing within the entity, including whether high-level management condoned the conduct, and the entity's history of similar misconduct.²⁶¹ Examining these factors allows the government to decide whether the actions are those of rogue individuals within the entity or if the conduct is such that it can be said that the entity itself committed the criminal act. The government also examines whether the entity timely and voluntarily disclosed the wrongdoing and cooperated in the investigation, whether the entity had a viable compliance program, and whether the entity took remedial action.²⁶² These factors tend to show whether the problems within the entity are systemic, and therefore should be attributed to the entity, or whether they are isolated instances that have been corrected. Finally, in deciding whether to pursue criminal, rather than civil sanctions, prosecutors will examine the collateral

256. U.S. SENTENCING COMM'N, U.S. SENTENCING GUIDELINES MANUAL, ch. 2, pt. T, introductory cmt. (2012) (emphasis added), available at http://www.ussc.gov/Guidelines/2012_Guidelines/index.cfm.

257. As discussed more fully below, preserving the integrity of the tax system is closely related to general deterrence. See *infra* text accompanying notes 254–68.

258. USAM, *supra* note 218, § 6-4.010.

259. *Id.*

260. See *supra* text accompanying notes 20–38, 65–68, 246–248; U.S. DEP'T OF THE TREASURY, THE PROBLEM OF CORPORATE TAX SHELTERS: DISCUSSION, ANALYSIS AND LEGISLATIVE PROPOSALS 3 (1999) ("A view that well-advised corporations can and do avoid their legal tax liabilities by engaging in these tax-engineered transactions may cause a 'race to the bottom.' If unabated, this could have long-term consequences to our voluntary tax system far more important than the revenue losses we currently are experiencing . . .").

261. USAM, *supra* note 218, § 9-28.300.

262. *Id.*

consequences of a prosecution on third parties such as shareholders, pension holders, employees, and others who are not culpable; the adequacy of the prosecution of individuals responsible; and the adequacy of civil remedies.²⁶³ In addition to the factors applicable to all federal prosecutions, Department of Justice policy provides that the Tax Division has a “strong preference for prosecuting responsible individuals, rather than entities, for corporate tax offenses.”²⁶⁴

Accordingly, if we are to judge—and judge we will—the government’s new prosecution policy regarding professionals using the government’s own articulated bases, the following standards will be weighed: (1) culpability of the person charged, including the person’s relative culpability in relation to other actors not charged; (2) retribution, including compensation of the crime victim; (3) deterrent effect (especially general deterrence) that would result from the prosecution; and (4) protection of the integrity of the civil tax system.

IV. ANALYSIS OF THE NEW PROSECUTION POLICY

Before analyzing the soundness of the tax shelter and tax haven prosecutions, a threshold question must be asked: Were the decisions to bring a series of criminal prosecutions where, in the past, no such prosecution would likely have been brought, a change in policy, or were these decisions based on the egregious facts of these cases? The answer is, I think, a little of both. It was because of the egregious facts, enormous dollar amounts involved, and the complicity of the upper echelons of the tax profession that caused the government to change its policies. Moreover, “the government” is not a monolithic entity detached from the human beings who run it. Thus, the change in policy can in part be traced to the individuals who were the decision makers in the Tax Division and other parts of the Justice Department.²⁶⁵

That being said, these prosecutions do not appear to be isolated instances or anomalies. More than seven years after the KPMG deferred prosecution agreement, the government is still pursuing tax professionals for their roles in peddling abusive tax shelters.²⁶⁶ The government continues to go after Swiss banks; the indictment and conviction of Wegelin Bank,²⁶⁷ and the deferred prosecution agreement with HSBC Bank²⁶⁸ are the most recent examples. While the government continues to

263. *Id.*

264. *Id.* § 9-28.400.

265. *See, e.g.*, Blank & Levin, *supra* note 245, at 22–23 (noting the role of then Assistant Attorney General Eileen O’Connor in tax enforcement policies).

266. *See, e.g.*, Bob Van Voris & David Glovin, *BDO Seidman to Pay \$50 Million in Deferred Prosecution*, BLOOMBERG BUSINESSWEEK (June 14, 2012), <http://www.businessweek.com/news/2012-06-13/bdo-seidman-to-pay-50-million-in-deferred-prosecution>.

267. *See* Neate, *supra* note 16.

268. *See* Press Release, U.S. Dep’t of Justice Office of Pub. Affairs, HSBC Holdings Plc. and HSBC Bank USA N.A. Admit to Anti-Money Laundering and Sanctions Violations, Forfeit \$1.256 Billion in Deferred Prosecution Agreement (Dec. 11, 2012) [hereinafter HSBC Press Release], *available at* <http://www.justice.gov/opa/pr/2012/December/12-crm-1478.html>.

prosecute a few individual taxpayers for hiding money offshore,²⁶⁹ the IRS offered its third offshore voluntary disclosure initiative in 2012.²⁷⁰ Thus, the policy of prosecuting professionals has continued with the change of administrations, and it appears that this policy will continue into the future. Assuming that is the case, are these prosecutions consistent with the goals and theories underlying federal criminal prosecutions in general and tax prosecutions in particular?

A. Tax Shelters

1. Relative Culpability

In examining the culpability of the professionals and their relative culpability vis-à-vis their clients, the decision to go after the professionals and not the taxpayers themselves was the right choice. It is the role of tax professionals to know what is an acceptable structure and what is pure tax fantasy. Circular 230 and the Rules of Professional Conduct impose a duty on tax attorneys and other professionals to advise clients only on legitimate transactions.²⁷¹ And it is the tax professionals who have the background, knowledge, and experience to know which transactions are legitimate and which are not. What was truly egregious about these transactions is that not only did the professionals misapply the law, they created the “facts” underlying these bogus transactions.²⁷²

The tax system has long accepted that taxpayers may rely on the advice of the professionals they hire.²⁷³ And, given the complexity and obtuseness of the tax laws, taxpayers cannot be faulted for relying on their advisors in what appear to be artificial transactions. Taxpayers enter into transactions structured in a way to maximize tax benefits because they have been advised by tax professionals to structure them in that way. For example, businesspeople do not really need structures like S Corporations for their business operations, but they have been advised that this is a tax-efficient way to set up a business. And if they find the documents they sign and the structures they are advised to create a bit strange, they simply believe this is one of the many mysterious things about the way the tax system works. If they are then told that they cannot structure a transaction in a certain way because it was done solely for tax purposes, they may be left more than a little perplexed. As Professor Freedman observed:

269. See, e.g., Press Release, U.S. Dept. of Justice Office of Pub. Affairs, South Florida Woman Pleads Guilty to Failing to Disclose Income from Swiss Bank Accounts and Agrees to \$21 Million Penalty (Jan. 8, 2013), available at <http://www.justice.gov/opa/pr/2013/January/13-tax-030.html>.

270. See *IRS Offshore Programs Produce \$4.4 Billion to Date for Nation's Taxpayers; Offshore Voluntary Disclosure Program Reopens*, I.R.S. News Release IR-2012-5 (Jan. 9, 2012), available at [http://www.irs.gov/uac/IRS-Offshore-Programs-Produce-\\$4.4-Billion-To-Date-for-Nation%E2%80%99s-Taxpayers;-Offshore-Voluntary-Disclosure-Program-Reopens](http://www.irs.gov/uac/IRS-Offshore-Programs-Produce-$4.4-Billion-To-Date-for-Nation%E2%80%99s-Taxpayers;-Offshore-Voluntary-Disclosure-Program-Reopens).

271. See, e.g., 31 C.F.R. §§ 10.22, .34, .35 (2011).

272. See, e.g., KPMG DPA, *supra* note 7, at ¶ 2.

273. See Schumacher, *supra* note 34, at 42–44.

What message are such people being given by the tax system? Are they to think of tax in terms of economic reality, fairness and rationality when it at first appears that incorporation will legitimately save tax and they then find that some of those benefits have been negated in a complex way that will probably cost them considerable amounts in professional fees? The law has real substance here because it has consequences in terms of rights and obligations. . . . Right from the start he has been given a signal that it is necessary to take account of taxation when making commercial decisions and that the rules can change. The culture of artificiality is established and so it continues. . . . In the light of this, it is not surprising that business owners will soon come to believe that it is perfectly natural to do artificial things for tax purposes and that this impression permeates right up the scale to large companies whose directors, used to tax impacting on all their decisions, consider it fair game to take tax into consideration in all planning and then to go on to undertake tax driven activities.²⁷⁴

If the transactions these taxpayers entered into looked artificial and were entered into solely for tax purposes, the response of many of these taxpayers would quite innocently be, “so what’s your point?” Thus, in examining the culpability and relative culpability, the professionals were the appropriate target.

Nevertheless, prosecutors, particularly those with ultimate decision-making authority, must be circumspect in using the prosecution of lawyers to deter the conduct of clients. As discussed above, the line between legal conduct and illegal conduct can be quite slim and vague. Statutes that prohibit impeding “the due administration” of the tax laws²⁷⁵ may apply to legal conduct, as well as nefarious conduct.²⁷⁶ The prosecution of Lauren Stevens is an apt example of the principle that one person’s representation is another one’s fraud.²⁷⁷

2. Compensating the Victim

The strategy of targeting the most culpable for criminal prosecution, while imposing stiff civil penalties on the taxpayers who benefited from these schemes, netted large amounts of money for the government. Approximately 2000 taxpayers

274. Judith Freedman, *Defining Taxpayer Responsibility: In Support of a General Anti-Avoidance Principle*, [2004] B.T.R. 332, 344–45.

275. 26 U.S.C. § 7212 (2012).

276. *See, e.g.*, Schumacher, *supra* note 19.

277. Lauren Stevens, former vice president and associate general counsel of pharmaceutical giant GlaxoSmithKline (GSK), had been charged with obstruction of justice and making false statements during a civil investigation of GSK by the Food and Drug Administration. *Id.* At the close of the government’s case, the district court dismissed the case against Stevens, holding that the statements were made in the course of her bona fide legal representation of a client and in good-faith reliance on both external and internal lawyers for GSK. Transcript of Proceedings at 5, *United States v. Stevens*, 771 F. Supp. 2d 556 (D. Md. 2011) (No. 8:10-cr-00694-RWT). The court further held that “only with a jaundiced eye and with an inference of guilt that’s inconsistent with the presumption of innocence could a reasonable jury ever convict this defendant” and that “it would be a miscarriage of justice to permit this case to go to the jury.” *Id.* at 8–9.

who invested in twenty-one different tax shelters accepted the IRS's global settlement terms and paid over \$2 billion in back taxes and interest.²⁷⁸ In addition, nearly eighty-five percent of taxpayers known by the IRS to have invested in the Son of BOSS tax shelter elected to settle under a different program and paid more than \$4 billion in taxes, penalties, and interest.²⁷⁹ Part of what was so galling about these shelters was the amount of money involved in the transactions and the place the lawyers and accountants occupied in the profession. These were some of the most well-heeled taxpayers and the most successful tax practitioners.²⁸⁰ Ironically, from a restitution perspective, the wealth and success of the professionals, their firms, and the taxpayers themselves allowed the government to be compensated at a relatively high rate.²⁸¹ Thus, while not all shelters were discovered and targeted, the ones that were detected netted a decent return for the government. From the perspective of compensating the victim, the strategy employed was effective.

3. Deterrence

Arguably the strongest and best reason for prosecuting the tax advisors is the deterrent effect of these cases. As discussed above, general deterrence is the primary objective in tax prosecutions.²⁸² Given the large number of taxpayers,²⁸³ and the relatively few tax prosecutions each year, the prosecutions that are brought must dissuade others, many others, from committing a similar crime. Prosecuting tax professionals accomplishes this objective, only more so: the tax shelter transactions would not have been possible without the participation of the lawyers, accountants, and bankers. Even the most sophisticated taxpayers would not have dreamt up the structures and transactions of these shelters. And, without the legal documents and counterparties created by the facilitators, the transactions could not have been carried out. Perhaps even more importantly, the taxpayers would not have entered into these transactions without the tax opinions drafted by the lawyers and accountants.²⁸⁴ Thus, the professionals were central to execution of these schemes.

278. Stephen Joyce, *About 2,000 Taxpayers to Pay \$2 Billion in Global Settlement Initiative*, *Everson Says*, 59 DAILY TAX REP. (BNA), Mar. 28, 2006, at G-2.

279. *Robust Response for Executive Stock Option Initiative; Son of Boss Settlement Heading for \$4 Billion*, I.R.S. News Release IR-2005-72 (July 11, 2005) available at [http://www.irs.gov/uac/Robust-Response-for-Executive-Stock-Option-Initiative;--Son-of-Boss-Settlement-Heading-for-\\$4-Billion](http://www.irs.gov/uac/Robust-Response-for-Executive-Stock-Option-Initiative;--Son-of-Boss-Settlement-Heading-for-$4-Billion); see also I.R.S. Announcement 2004-46, 2004-21 I.R.B. 964; Jay A. Soled, *Tax Shelter Malpractice Cases and Their Implications for Tax Compliance*, 58 AM. U. L. REV. 267, 268 n.1 (2008).

280. See Rostain, *supra* note 33, at 88–93.

281. For example, KPMG paid \$256 million of the \$456 million fine and restitution within a week of signing the Deferred Prosecution Agreement. See KPMG DPA, *supra* note 7, ¶ 3. By contrast, billions of dollars of court-ordered restitution still remain unpaid. See, e.g., Daniel M. Fetso, *Unpaid Restitution: An Under-Enforced Right of Victims and Suggestions to Improve the Collection of Restitution in Wyoming*, 12 WYO. L. REV. 367, 368 (2012).

282. See *supra* text accompanying note 253.

283. More than 234 million tax returns were filed in 2011. INTERNAL REVENUE SERV., *supra* note 229, at 4.

284. See, e.g., Schumacher, *supra* note 34, at 43–44.

Shutting down the professionals effectively shut down the shelters.²⁸⁵ And this, whether intentional or not, is ultimately the wisdom of these prosecutions. Prosecuting professionals deters not only taxpayers, but also other professionals from advising on these types of abusive transactions.²⁸⁶ Since professionals are the enablers and taxpayers cannot enter into these transactions without the professionals, the current prosecution policy is likely to be more effective than pursuing the taxpayers themselves. Moreover, given that there are far fewer professionals than taxpayers, prosecuting professionals can achieve both specific and general deterrence more efficiently than prosecuting taxpayers. Thus, the prosecutions of professionals causes a ripple effect beyond the normal tax prosecution.²⁸⁷

4. Preserving the Integrity of the Tax System

Finally, the decision to bring criminal cases against the lawyers and accountants helped to preserve and indeed restore the integrity of the tax system.²⁸⁸ The long-term decision not to prosecute investors in tax shelters or their advisors led, at least in part, to the rise of shelters.²⁸⁹ During the 1990s, in response to the competitive pressure in the auditing field, the national accounting firms dedicated tremendous amounts of resources to retaining the best and brightest in the tax community.²⁹⁰ These professionals were not put into the traditional auditing roles, but were assigned to the tax shelter “consulting” practices.²⁹¹ Those practices became large profit centers for the firms.²⁹² Without the specter of liability, either civil, criminal, or professional, these shelters grew in complexity and egregiousness. For example, in an internal memorandum, a KPMG partner acknowledged that the strategy at issue was a “tax shelter” and subject to registration as such under 26 U.S.C. § 6111.²⁹³ However, the partner recommended that it not be registered, reasoning that

285. See Fleischer, *supra* note 107.

286. See Susan Cleary Morse, *The How and Why of the New Public Corporation Tax Shelter Compliance Norm*, 75 *FORDHAM L. REV.* 961, 962 n.4 (2006).

287. Of course, the criminal investigations and prosecutions were not the only tool employed by the government against professionals. See *supra* note 263 and accompanying text. The heightened ethical standards in some of the deferred prosecution agreements, which of course were part and parcel of these investigations and prosecutions, further reinforced the lessons of the indictments. See, e.g., KPMG DPA, *supra* note 7, at 7. However, the specter of criminal prosecution of high-level tax professionals was definitely a game changer.

288. Much of the analysis regarding the deterrent effect of these prosecutions discussed immediately above applies with equal force here.

289. See Rostain, *supra* note 33, at 86–94.

290. *Id.* at 89–91.

291. See *id.*

292. See *id.* By 2002, revenues from tax services at the Big Four accounting firms were between 21% and 36% of the firms’ total revenue, representing between \$1.1 and \$1.6 billion. *Id.* at 91.

293. See *Justice Releases 1998 KPMG Memo on OPIS Shelters*, TAX NOTES TODAY, Dec. 15, 2003, available at Lexis, 2003 TNT 240-52 (reproducing a memorandum from Gregg W. Ritchie, KPMG Peat Marwick LLP, to Jeffrey N. Stein, KPMG Peat Marwick LLP (May 26, 1998; released Dec. 11, 2003)).

the firm's financial exposure was minimal, other promoters were not registering tax shelters, registering would put the firm at a "severe competitive disadvantage," and that the IRS had shown a "lack of enthusiasm" for enforcing the registration requirements.²⁹⁴ In the end, firms admitted to creating these transactions out of whole cloth.²⁹⁵

These cases were worse for the system than prior shelters. The involvement of the best professionals in these cases threatened the very fabric of the tax system. The corrosive effect of the sense that "everybody is doing it," especially when "everybody" includes the top professionals, cannot be underestimated. One of the beliefs of many taxpayers is that only a fool pays the full amount of tax, or as Leona Helmsley so eloquently stated, "Only the little people pay taxes."²⁹⁶ And there is a belief that if we only find the right tax advisor, we will only be required to pay that which we are constitutionally obligated to forfeit.²⁹⁷ If tax professionals believe that they are fools if they don't give a tax opinion when everyone else is giving them, the entire system breaks down.

The decision to prosecute helped to restore that equilibrium. Of course, criminal prosecution was not the only arrow in the government's quiver. These prosecutions were accompanied by several changes to the rules governing practice before the IRS, new civil penalties, and aggressive investigations of shelter promoters.²⁹⁸

5. Summary

Accordingly, the decision to investigate and prosecute tax professionals for their roles in marketing abusive tax shelters was consistent with the goals of tax enforcement and with the theories underlying criminal liability. The victim, the American taxpayer, was compensated. Those that caused the harm were punished. Taxpayers could not have dreamed up these transactions or implemented them without the professionals. Thus, from both an allocation of blame and a general deterrence perspective, pursuing the professionals was the right choice. Finally, the change in prosecution policies, along with the other changes in ethical rules and conditions placed in the DPAs, helped to restore the integrity of the civil tax system. No longer will a professional, or at least a sane one, advise a client to enter into a transaction like COBRA, BLIPS, or SOS.²⁹⁹ The fact that some of the most high-profile defendants were not convicted does not diminish the appropriateness of the decision to prosecute.³⁰⁰

294. *Id.*

295. *See, e.g.*, KPMG DPA, *supra* note 7, ¶ 2.

296. *Maid Testifies Helmsley Denied Paying Taxes*, N.Y. TIMES, July 12, 1989, at B2 (quoting Leona Helmsley).

297. *See* Merle H. Miller, *Morality in Tax Planning*, in 10 INST. ON FED. TAX'N 1067, 1074 (1952) ("Most people think of us as having a bag of tricks that greatly reduces our clients' taxes and probably gets us out altogether on our own.").

298. *See, e.g.*, 26 U.S.C. § 6694 (2012); 31 C.F.R. § 10.35 (2011); Blank & Levin, *supra* note 245.

299. *See* Lederman, *supra* note 77 (describing types of these shelters).

300. The methods used by some prosecutors are, of course, subject to criticism. *See* United States v. Stein, 541 F.3d 130, 143 (2d Cir. 2008).

B. Tax Havens

1. Relative Culpability

The soundness of the decision to prosecute Swiss banks and bankers, while largely absolving—at least criminally—the U.S. taxpayers who hid money in these banks, is not so clear. This is not, of course, to excuse the conduct of UBS and other offshore bankers. UBS admitted that it violated its QI agreement and its own express internal policies.³⁰¹ The actions taken by UBS staff, with the apparent complicity of management, were clearly unlawful. UBS used its Swiss bankers to recruit high-net-worth individuals in the U.S. in violation of U.S. securities laws, and it assisted U.S. taxpayers in setting up accounts at UBS in a manner designed to conceal the taxpayers' ownership or beneficial interest in these accounts.³⁰² It failed to issue a Form 1099 for these accounts, in violation of its QI agreement with the IRS.³⁰³ Thus, the culpability of UBS and its bankers cannot be disputed. And it could be argued that UBS got off easy. The \$780 million fine was not crippling,³⁰⁴ and UBS was not, in fact, indicted.³⁰⁵ However, in examining the relative culpability of UBS vis-à-vis the U.S. depositor, it is less clear that offshore banks and bankers should be held criminally responsible, while U.S. taxpayers largely get a pass. Like the tax shelter advisers, the bankers' misconduct is derivative—it occurs only because they helped U.S. taxpayers evade or avoid their obligations under the law. However, unlike the tax shelter cases, where clients relied on the advice of the tax professionals, those taxpayers who intentionally hid money in UBS knew what they were doing was illegal. These wealthy, sophisticated taxpayers cannot legitimately claim that they relied on the advice of Swiss bankers that they need not report the existence of an offshore account or the income from the account.³⁰⁶ There is little gray area in this issue.³⁰⁷

301. SENATE REPORT, *supra* note 112, at 9–13.

302. *Id.*

303. *Id.* at 9.

304. UBS had a net profit for just the first quarter of 2011 of nearly \$2.06 billion. Deborah Ball, WALL ST. J., *UBS Reassures, Despite Fall in Profit* (Apr. 27, 2011), <http://online.wsj.com/article/SB10001424052748703778104576286162911746324.html>. In addition, as of the end of 2008, Swiss Banks held assets of \$1.84 trillion. Mathieu von Rohr, *Bank Secrecy Gives Way in Switzerland*, BLOOMBERG BUSINESSWEEK (Mar. 3, 2009), http://www.businessweek.com/globalbiz/content/mar2009/gb2009033_255906.htm.

305. Compare the fate of Arthur Andersen, which received the “corporate death penalty” by its indictment. *See* Ashcroft & Ratcliffe, *supra* note 240.

306. *See* 26 C.F.R. § 1.6664-4(b) (2012) (Taxpayers may rely on advice of tax professionals if reliance is reasonable. “Circumstances that may indicate reasonable cause and good faith include an honest misunderstanding of fact or law that is reasonable in light of all of the facts and circumstances . . .”). This is not to say that all taxpayers who failed to declare an offshore account did so knowing that it was in violation of the law. Many less sophisticated taxpayers, some of whom inherited accounts from parents or kept accounts in their home country after immigrating to the United States, did not know of the requirement to report these accounts. *See, e.g.,* Janet Novack, *IRS Cuts Middle Class Expats Big (and Deserved) Penalty Break*, FORBES (June 26, 2012, 7:06 PM), <http://www.forbes.com/sites/janetnovack/2012/06/26/irs-cuts-middle-class-expats-big-and-deserved-penalty-break/>.

Thus, in examining the relative culpability of the actors in this transaction, it is difficult to argue that the bankers were more culpable than their U.S. clients.³⁰⁸ This is particularly so when Swiss law is considered. As discussed above, Swiss law makes it a crime for bankers to divulge their customer's name, the type of bank account, the transactions the client entered into, and any information supplied by the customer in connection with the account to a foreign government.³⁰⁹ In addition, failure to report income or the existence of a bank account is not a crime under Swiss law.³¹⁰ The distinction between "tax fraud," which is a crime under Swiss law, and tax evasion, which is not, was included in the Swiss-U.S. Tax Treaty.³¹¹ Under the treaty, the Swiss government had no duty to provide bank account information under cases of "mere" tax evasion.³¹² Thus, while the actions of UBS violated U.S. law, its actions were consistent with Swiss law and arguably not inconsistent with the tax treaty between the United States and Switzerland.³¹³

In addition, it can be dangerous for prosecutors to wade into the murky waters of diplomacy and international relations.³¹⁴ Indeed, the UBS case caused a backlash in Switzerland,³¹⁵ and many have argued that the conduct of the foreign banks and bankers is little different from the conduct of U.S. banks.³¹⁶ Under U.S. tax laws,

307. While U.S. depositors may not have relied on professionals regarding whether hiding money offshore is legal, these depositors often relied on bankers and lawyers to help them structure transactions in order to better hide their money from the IRS. *See, e.g.,* Patricia Hurtado & David Voreacos, *Swiss Lawyer's Guilty Plea Disclosures Help Advance IRS Tax Evasion Crackdown*, 8 WHITE COLLAR CRIME REP. (BNA), Aug. 23, 2013, at 584. In this regard, the professionals are equally as culpable, if not more culpable, than their clients.

308. It is true that U.S. depositors were listed as "unindicted co-conspirators" in the Information filed against UBS. *See* UBS DPA, *supra* note 147, at Exhibit B, at 9. Yet, government policies allowed the vast majority of these depositors to escape criminal prosecution. *Cf. Seven UBS Clients Charged with Hiding More than \$100 Million in Swiss Accounts*, 72 DAILY TAX REP. (BNA), Apr. 16, 2010, at K-1.

309. SWISS PENAL CODE, *supra* note 45.

310. *See* Weber, *supra* note 5.

311. *See* Convention for the Avoidance of Double Taxation with Respect to Taxes on Income, U.S.-Switz., art. 26, Oct. 2, 1996, available at <http://www.irs.gov/pub/irs-trty/swiss.pdf>.

312. *See id.*

313. And as my colleague Anita Ramasastry noted, "Swiss banks are not to be held responsible for being global policemen." Ramasastry, *supra* note 40, at 333.

314. The conduct of the bankers did not violate international law. If they acted appropriately under Swiss law and consistent with then-existing treaties, should prosecutors wade into this area and start prosecuting people? The court in *Arc Ecology v. United States Department of the Air Force* held that when the Executive Branch is the party advancing a construction of a statute with potential foreign policy implications, a court can presume that "the President has evaluated the foreign policy consequences of such an exercise of U.S. law and determined that it serves the interests of the United States." 411 F.3d 1092, 1102 (9th Cir. 2005) (quoting *United States v. Corey*, 232 F.3d 1166, 1179 (9th Cir. 2000)). Nevertheless, notions of international comity would suggest that prosecutors exercise discretion in these cases. There is some indication that these cases have damaged our relationship with Switzerland. *See, e.g.,* Daniel Pruzin, *Anger Grows in Switzerland Over DOJ Efforts to Force UBS to Give Details on U.S. Clients*, 34 DAILY TAX REP. (BNA), Feb. 24, 2009, at I-4.

315. *See* Pruzin, *supra* note 314.

316. *See* Sheppard, *supra* note 247.

interest income on accounts held by nonresident aliens is not taxable.³¹⁷ U.S. banks are therefore not required to, and do not, issue 1099 Forms with respect to these accounts.³¹⁸ Thus, “the United States does not and cannot provide information to any of its tax treaty or [Tax Information Exchange Agreement] TIEA partners (except Canada) concerning interest paid on deposits by their residents in U.S. bank accounts.”³¹⁹ As a result, the United States is one of the favorite places of foreigners to hide their money.³²⁰ In fact, in a letter dated February 9, 2009, the Mexican Secretary of Finance, Agustin Carstens, complained to U.S. Treasury Secretary Timothy Geithner that U.S. banks are being used by Mexican taxpayers, including drug dealers, to hide their ill-gotten gains.³²¹ Commentators have listed states like Nevada, Delaware, and Wyoming as tax havens,³²² and even recent proposals to impose “know your customer” duties on U.S. banks have been met with opposition.³²³ More egregious is the HSBC case, in which the U.S. subsidiary of the British-based bank failed to maintain adequate anti-money-laundering procedures, which allowed hundreds of millions of dollars of narco-profits to be laundered through the U.S. banking system.³²⁴ Accordingly, while the conduct of UBS and others should not be excused, in examining their relative culpability, they are no more culpable than their U.S. clients, most of whom were not prosecuted.

317. 26 U.S.C. § 871(i) (2012). This is part of deliberate strategy to attract foreign capital, and this exemption is maintained knowing full well that the foreign depositors are not paying taxes on the income from these accounts. *See, e.g.*, Michael J. McIntyre, *How to End the Charade of Information Exchange*, 56 TAX NOTES INT’L 255, 258 (2009).

318. *See, e.g.*, Marshall J. Langer, *Pending Stop Haven Abuse Act Would Wrongly Blacklist Cooperating Countries*, 56 DAILY TAX REP. (BNA), Mar. 26, 2009, at J-1.

319. *Id.*

320. *Id.*

321. Letter from Agustin Carstens, Mex. Fin. Sec’y, to Timothy Geithner, U.S. Treasury Sec’y, Requesting Automatic Exchange of Information (Feb. 9, 2009), available at http://faculty.law.wayne.edu/tad/Documents/Country/mexico-carstens_letter.pdf, quoted in McIntyre, *supra* note 317, at 258; *see also* Robert Goulder, *How the U.S. Is a Tax Haven for Mexico’s Wealthy*, TAX ANALYSTS (Aug. 24, 2009), www.taxanalysts.com/www/features.nsf/Articles/522A39903AFD6CFB8525761D004F113B.

322. *See, e.g.*, *The G20 and Tax: Haven Hypocrisy*, ECONOMIST, Mar. 28, 2009, at 86, available at <http://www.economist.com/node/13382279>; *see also* JANE G. GRAVELLE, CONG. RESEARCH SERV., R40623, TAX HAVENS: INTERNATIONAL TAX AVOIDANCE AND EVASION 6 (2013), available at <http://www.fas.org/sgp/crs/misc/R40623.pdf>.

323. *See* Jeff Bater, *FinCEN’s Due Diligence Proposal Criticized During Treasury Hearing*, 7 WHITE COLLAR CRIME REP. (BNA), Aug. 10, 2012, at 631. “Know your customer” rules have been the backbone of anti-money-laundering efforts for years. *See, e.g.*, Ramasastry, *supra* note 40, at 342–45.

324. *See* Press Release, U.S. Dep’t of Justice, HSBC Holdings Plc. and HSBC Bank USA N.A. Admit to Anti-Money Laundering and Sanctions Violations, Forfeit \$1.256 Billion in Deferred Prosecution Agreement (Dec. 11, 2012), available at <http://www.justice.gov/opa/pr/2012/December/12-crm-1478.html>; *see also* S. COMM. ON HOMELAND SECURITY AND GOVERNMENTAL AFFAIRS, PERMANENT SUBCOMM. ON INVESTIGATIONS, U.S. SENATE, U.S. VULNERABILITIES TO MONEY LAUNDERING, DRUGS, AND TERRORIST FINANCING: HSBC CASE HISTORY 2–4 (2012).

2. General Deterrence

While from a relative culpability standpoint the offshore bank prosecutions are suspect, it was clearly more practical for the U.S. government to go after a few banks and bankers than the tens of thousands of depositors. The government indicts less than 3000 defendants for tax crimes per year,³²⁵ and it must therefore choose wisely the targets it will pursue. As part of its Deferred Prosecution Agreement with UBS, UBS agreed to provide bank records on some of its customers.³²⁶ The government opened a parallel John Doe summons proceeding in an attempt to obtain bank account information from a broader population of depositors.³²⁷ It also indicted a few of the depositors.³²⁸ In conjunction with these efforts, the government offered a series of offshore voluntary disclosure initiatives.³²⁹ Thus, depositors were left with the decision of whether to come forward and disclose their account information and pay stiff civil penalties or risk criminal prosecution.³³⁰ This carrot-and-stick strategy encouraged thousands of U.S. taxpayers to come forward under the offshore voluntary disclosure initiatives and garnered the government more than \$4 billion in taxes and penalties.³³¹ Therefore, while the decision to pursue UBS criminally can be attacked from a theoretical point of view, it is difficult to argue with the strategic choice the government made.

Hence, like the tax shelter prosecution policy, the government's tax haven strategy has been, and it appears that it will continue to be, quite successful. The prosecution policy, along with diplomatic initiatives by the United States and other governments, has fundamentally changed the world of offshore banking, at least European offshore banking.³³² An amendment to the U.S.–Switzerland Tax Treaty would broaden the information the Swiss will share in tax cases.³³³ Numerous other

325. *See supra* note 229.

326. Deferred Prosecution Agreement at 6, *United States v. UBS AG* (No. 09-60033-CR-Cohn) (S.D. Fla. 2009), available at http://www.justice.gov/tax/UBS_Signed_Deferred_Prosecution_Agreement.pdf.

327. Press Release, U.S. Dep't of Justice, Justice Department Asks Court to Serve IRS Summons for UBS Swiss Bank Account Records (June 30, 2009), available at <http://www.justice.gov/opa/pr/2008/June/08-tax-579.html>.

328. *See* Shotter, *supra* note 163.

329. *Offshore Voluntary Disclosure Program Frequently Asked Questions and Answers*, INTERNAL REVENUE SERV. (June 26, 2012), <http://www.irs.gov/Individuals/International-Taxpayers/Offshore-Voluntary-Disclosure-Program-Frequently-Asked-Questions-and-Answers>; *2011 Offshore Voluntary Disclosure Initiative Frequently Asked Questions and Answers*, INTERNAL REVENUE SERV., <http://www.irs.gov/Businesses/International-Businesses/2011-Offshore-Voluntary-Disclosure-Initiative-Frequently-Asked-Questions-and-Answers> (last updated July 19, 2013); *Voluntary Disclosure: Questions and Answers*, INTERNAL REVENUE SERV. (Feb. 8, 2011), <http://www.irs.gov/uac/Voluntary-Disclosure-Questions-and-Answers>.

330. *See* Zehnle & Clarke, *supra* note 18.

331. *See* I.R.S. News Release IR-2012-5, *supra* note 270.

332. *See, e.g.*, Bruce Zagaris, *International Tax Enforcement Continues to Rise*, 64 TAX NOTES INT'L 653 (2011).

333. *See* Lauren Gardner & Daniel Pruzin, *Geithner Signs Protocol to U.S.-Swiss Treaty to Provide Greater Tax Information Exchange*, INT'L TAX MONITOR, (BNA), Sept. 24, 2009.

tax information exchange treaties have been signed,³³⁴ and Liechtenstein, which was once known as the “the most dangerous tax haven in Europe,”³³⁵ has begun to ease its bank secrecy rules.³³⁶ Thus, from a deterrence perspective, the strategy appears to have been at least somewhat successful. That being said, despite the number of participants in the offshore voluntary disclosure initiatives, many more taxpayers have chosen not to come forward.³³⁷ Moreover, even with the increased cooperation of Switzerland and Liechtenstein, offshore banks in other jurisdictions have rushed to fill the void, and it is therefore unclear whether tax haven abuse generally has been reduced.³³⁸ Also, it is debatable whether these positive developments necessarily flowed from the prosecution policy. Indeed, many countries, including Britain and Germany, were able to secure similar benefits without resorting to indictments of Swiss bankers.³³⁹

3. Compensating the Victim: The Effect of Tax Haven Abuse on the Developing World

Pursuing UBS and other banks and bankers criminally, while allowing U.S. taxpayers to resolve their cases civilly, has brought in more than \$4.4 billion dollars into the U.S. Treasury.³⁴⁰ These recoveries help to ameliorate the impact of tax haven abuses on the U.S. Treasury. Thus, the government can reasonably assert that, like the tax shelter initiatives, the victim—the U.S. taxpayer—has been compensated, at least to a certain degree. In many respects this position is correct. However, the amount recovered is a small fraction of the estimated \$100 billion in tax revenues that is lost annually due to offshore tax abuses.³⁴¹ More significantly, limiting the “victim” to the U.S. taxpayer is misleading and ignores the true victim of tax haven abuse.

The most profound impact of tax havens and bank secrecy is on the citizens in countries of the developing world whose leaders have used haven banks to steal

334. See, e.g., Alison Bennett, *United States, Monaco Sign Agreement to Allow for Exchange of Tax Information*, 172 DAILY TAX REP. (BNA), Sept. 10, 2009 at I-6; Rick Mitchell, *Island of Jersey, United Kingdom Sign Tax Information Exchange Agreement*, 46 DAILY TAX REP. (BNA), Mar. 13, 2009, at I-3.

335. 2 DIAMOND & DIAMOND, *supra* note 4, at Liech. 1.

336. See, e.g., Haig Simonian, *Liechtenstein Eases Bank Secrecy Rules*, FIN. TIMES (Mar. 12, 2009, 6:24 PM), <http://www.ft.com/cms/s/0/b85d298a-0ed9-11de-ba10-0000779fd2ac.html#axzz22iMLu17a>.

337. See, e.g., Laura Saunders, *Tax-Cheat Showdown: Fess Up or Stay Quiet?*, WALL ST. J. (Aug. 9, 2009), <http://online.wsj.com/article/SB125020653689430645.html>.

338. See, e.g., William Brittain-Catlin, *This Is Not the End for Tax Havens*, GUARDIAN (Sept. 27, 2010, 8:02 AM), <http://www.guardian.co.uk/commentisfree/2010/sep/27/not-end-for-tax-havens>.

339. See, e.g., Rick Mitchell, *France, Switzerland Sign Tax Treaty Rider Aimed at Ending Banking Secrecy*, 165 DAILY TAX REP. (BNA), Aug. 28, 2009, at I-1; Daniel Pruzin, *Germany, Liechtenstein Approve TIEA Incorporating OECD Exchange Standards*, 169 DAILY TAX REP. (BNA), Sept. 3, 2009, at I-1; Daniel Pruzin, *Switzerland and Austria Conclude Accord on Tax Information Exchange*, 134 DAILY TAX REP. (BNA), July 16, 2009, at I-3.

340. I.R.S. News Release IR-2012-5, *supra* note 270.

341. See SENATE REPORT, *supra* note 112, at 1–2.

their countries' wealth. Unlike the use of offshore tax evasion in the developed world, where citizens hide assets and income offshore to avoid paying taxes, in the case of the developing world, it is the leaders themselves that use bank secrecy jurisdictions to hide assets. In some instances, minor kleptocrats accumulate tidy fortunes offshore to ensure a comfortable retirement. Other leaders, however, have engaged in the systematic plunder of their own countries, accumulating massive amounts of wealth in haven countries, leaving their countries and citizens impoverished. Ndiva Kofele-Kale has referred to this practice as indigenous spoliation,³⁴² which he defines as an "illegal act of depredation committed for private ends by *constitutionally responsible rulers, public officials, or private individuals*."³⁴³ As Professor Kofele-Kale notes, the scope of this devastation goes beyond mere embezzlement and corruption.³⁴⁴ While corrupt political leaders have for millennia taken the wealth from their people, the scope and effect of this new form of so-called "grand corruption" is fundamentally different.³⁴⁵

First, the ability in recent years to move money quickly and efficiently out of the country, and then to hide it in a haven jurisdiction, means that the stolen wealth will more likely be put offshore, rather than invested in the leader's country.³⁴⁶ Thus, the massive accumulation of assets abroad has the effect of draining resources that might otherwise have been used in domestic investment.³⁴⁷ If more of those funds stayed in-country, those funds could finance large development budgets.³⁴⁸ The international development organization Christian Aid has estimated that if funds deposited in tax haven countries were instead retained in the countries and spent on areas such as health and education, the lives of poor people in the developing world would be transformed.³⁴⁹ For example, if the same proportion of tax revenues were spent on healthcare in these countries as has been diverted to tax havens since

342. Ndiva Kofele-Kale, *Patrimonicide: The International Economic Crime of Indigenous Spoliation*, 28 VAND. J. TRANSNAT'L L. 45, 56 (1995).

343. *Id.* (emphasis in original). He has also referred to this conduct as "patrimonicide," which he describes as follows:

["Patrimonicide"] comes from combining the Latin words "patrimonium," meaning "[t]he estate or property belonging by ancient right to an institution, corporation, or class; especially the ancient estate or endowment of a church or religious body," and "cide," meaning killing. This term is fitting because indigenous spoliation is the destruction of the sum total of a state's endowment, the laying waste of the wealth and resources belonging by right to her citizens, and the denial of their heritage.

Id. at 58 (footnote omitted).

344. *See id.* at 56–59.

345. *Id.* at 58.

346. *See id.* at 58–59.

347. *Investigation of Philippine Investments in the United States, Hearings Before the Subcomm. on Asian and Pac. Affairs of the H. Comm. on Foreign Affairs*, 99th Cong. 263 (1987) (statement of Rep. Stephen Solarz, Chairman, Subcomm. on Asian and Pac. Affairs).

348. Angel Gurría, *Improve Tax Fairness and Help the Developing World*, ORG. FOR ECON. CO-OPERATION & DEV. (Apr. 24, 2009), <http://www.oecd.org/development/improvetaxfairnessandhelpthedevelopingworld.htm>.

349. *See* CHRISTIAN AID, *supra* note 4, at 2.

2000, then the lives of 350,000 children under the age of five would be saved every year.³⁵⁰

Second, the sheer magnitude of the theft is startling.³⁵¹ Every year, billions of dollars are transferred to havens from the developing world.³⁵² The think tank Global Financial Integrity estimates that in 2006, between \$858.6 billion and \$1.06 trillion left developing countries in illicit financial outflows.³⁵³ The amounts stolen have been described as going “beyond shame and almost beyond imagination.”³⁵⁴ Others have wondered whether the amassing of public wealth has risen “to a point of madness or some form of obsessive or compulsive psychiatric disorder.”³⁵⁵ Even the lowest estimate suggests that the illegal capital outflow exceeds the net legal inflow. The illegal outflow corresponds roughly to ten times the development assistance given to developing countries.³⁵⁶ The government of Norway, in its comprehensive study of tax havens, noted:

Potentially the most serious consequences of tax havens are that they can contribute to weakening the quality of institutions and the political system in developing countries. This is because tax havens encourage the self-interest that politicians and bureaucrats in such countries have in weakening these institutions. The lack of effective enforcement organisations mean that politicians can to a greater extent exploit the opportunities which tax havens offer for concealing proceeds from economic crime and rent-seeking. These proceeds can be derived from corruption and other illegal activities, or be income which politicians have dishonestly obtained from development assistance, natural resources and the public purse. By making it easier to conceal the proceeds of economic crime, tax havens create political incentives to demolish rather than build up institutions, and to weaken rather than strengthen democratic governance processes.³⁵⁷

Finally, the hallmark of contemporary indigenous spoliation is the social and economic devastation that follows when capital of this magnitude is allowed to leave a capital-poor developing country.³⁵⁸ As these funds are put offshore, their

350. *Id.*

351. Kofele-Kale, *supra* note 342, at 59.

352. *Id.*

353. DEV KAR & DEVON CARTWRIGHT-SMITH, GLOBAL FINANCIAL INTEGRITY: A PROGRAM OF THE CENTER FOR INTERNATIONAL PROPERTY, ILLICIT FINANCIAL FLOWS FROM DEVELOPING COUNTRIES: 2002–2006, at 22 (2008), available at <http://www.gfip.org/storage/gfip/economist%20-%20final%20version%201-2-09.pdf>.

354. DARRELL DELAMAIDE, DEBT SHOCK: THE FULL STORY OF THE WORLD CREDIT CRISIS 60 (1984).

355. Sola Odunfa, *African View: Insane with Greed*, BBC NEWS (October 14, 2009, 14:32 UK), <http://news.bbc.co.uk/2/hi/africa/8302729.stm> (quoting Faroda Waziri, Exec. Chairman of Nigeria’s Econ. and Fin. Crimes Comm’n).

356. GOV. COMM’N ON CAPITAL FLIGHT FROM POOR COUNTRIES, TAX HAVENS AND DEVELOPMENT 13 (2009) [hereinafter NORWAY REPORT], available at http://www.regjeringen.no/upload/UD/Vedlegg/Utvikling/tax_report.pdf.

357. *Id.*

358. Kofele-Kale, *supra* note 342, at 59.

countries are required to borrow from foreign lenders, adding to the already crushing debt of these countries. The price of these outflows is “billions of dollars-worth of unsurfaced roads, unpurified water and untreated illnesses.”³⁵⁹ Christian Aid has predicted that between 2000 and 2015, 5.6 million young children in the developing world will die due to this financial devastation.³⁶⁰ Kofele-Kale points out that the impact on the developing world extends beyond those countries’ borders in the form of refugees, regional conflicts, and the diversion of foreign aid to private coffers.³⁶¹ Perhaps the greatest irony is that developed countries and private charities are subsidizing tax havens by allowing international aid to be siphoned off and diverted to tax haven accounts for the benefit of corrupt kleptocrats.

Thus, while the image most connected with tax havens is of sleek yachts in Cayman harbors, the impact of haven jurisdictions falls upon the poorest of the world’s poor. While the U.S. government should not be faulted for making sure U.S. taxpayers are repaid the losses caused by tax havens, compensation of the victim cannot stop there. Any solution that developed countries like the United States can obtain through their superior bargaining power must take into account the effect tax havens have on developing countries. The U.S. government is in the process of establishing a network of information exchange agreements administered through the Foreign Account Tax Compliance Act (FATCA).³⁶² The United States is negotiating intergovernmental agreements with countries like Japan, Denmark, the United Kingdom, and Mexico.³⁶³ The information obtained via FATCA will be much more timely and robust than the information that can be obtained through treaty requests.

359. *African Debt: Borrowed Time*, ECONOMIST, May 22, 1993, at 66.

360. See CHRISTIAN AID, *supra* note 4, at 1.

361. Kofele-Kale, *supra* note 342, at 62–66.

362. The FATCA provisions were enacted on March 18, 2010, under Title V of the HIRE Act. Hiring Incentives to Restore Employment Act, Pub. L. No. 111-147, 124 Stat. 71, 97 (codified at 26 U.S.C. §§ 1471–1474).

363. See Agreement Between the Department of the Treasury of the United States of America and the Ministry of Finance and Public Credit of the United Mexican States to Improve International Tax Compliance Including with Respect to FATCA, U.S.-Mex., Nov. 19, 2012, available at <http://www.treasury.gov/resource-center/tax-policy/treaties/Documents/FATCA-Agreement-Mexico-11-19-2012.pdf>; Agreement Between the Government of the United States of America and the Government of the Kingdom of Denmark to Improve International Tax Compliance and to Implement FATCA, U.S.-Den., Nov. 15, 2012, available at <http://www.treasury.gov/resource-center/tax-policy/treaties/Documents/FATCA-Agreement-Denmark-11-19-2012.pdf>; Agreement Between the Government of the United States of America and the Government of the United Kingdom of Great Britain and Northern Ireland to Improve International Tax Compliance and to Implement FATCA, U.S.-U.K.-N.Ir., Sept. 12, 2012, available at <http://www.treasury.gov/resource-center/tax-policy/treaties/Documents/FATCA-Agreement-UK-9-12-2012.pdf>; Joint Statement from the United States and Japan Regarding a Framework for Intergovernmental Cooperation to Facilitate the Implementation of FACTA and Improve International Tax Compliance, U.S.-Japan, June 21, 2012, available at <http://www.treasury.gov/resource-center/tax-policy/treaties/Documents/FATCA-Joint-Statement-US-Japan-06-21-2012.pdf>.

Including less developed countries in this information exchange would help to reduce the impact of tax havens on these countries. Of course, it would be naïve to believe that mere information exchange would cure the scourge that tax havens impose on the developing world. Indeed, the very nature of indigenous spoliation is that those in power, who would receive the exchanged information, are those who are hiding money offshore. Nevertheless, given the interrelated nature of the banking system and the dangers of not obtaining and supplying this information, excluding the developing world from the network of information exchange is not a viable option.³⁶⁴ It has been noted that “[s]unlight is said to be the best of disinfectants.”³⁶⁵ Shining sunlight on tax haven abuses will help cleanse the wounds in the developed and the developing world.

4. Preserving the Integrity of the Tax System

The criminal cases against Swiss bankers satisfied, at least to a certain extent, the Tax Division’s stated goal of preserving the integrity of the civil tax system. Offshore banks are less likely to assist U.S. taxpayers in hiding their money, and thousands of bank accounts that had been “undeclared” for years have now been reported to the IRS. New tax and information exchange treaties have been negotiated between many nations. Perhaps more significantly, the debate around tax havens has changed.³⁶⁶ Havens are no longer an accepted practice, and governments and policy makers are actively seeking new ways to limit the impact of havens. And this, as Martha Stewart would say, is a good thing. But more must be done. The IRS must continue in its robust civil enforcement of international tax avoidance and transfer pricing cases. The government cannot stop with the Swiss banks and declare victory. There remains an estimated \$21–32 *trillion* secreted in tax haven countries.³⁶⁷ More importantly, the United States and other developed countries cannot posture about the evils of bank secrecy and tax haven abuses, while tolerating similar practices within their own borders. As discussed above, U.S. banks are not required to, and do not, issue tax reporting forms with respect to accounts held by nonresident aliens, and the U.S. government does not provide bank deposit information to any of its treaty partners.³⁶⁸ Hypocrisy does little to boost the integrity of the tax system.³⁶⁹

364. The HSBC case is an excellent example of the perils of ignoring the activities of offshore banks to the U.S. banking system. HSBC Group members facilitated money laundering and terrorism, and provided drug lords, terrorists, and other criminals access to the U.S. banking system. See HSBC Press Release, *supra* note 268.

365. LOUIS D. BRANDEIS, *OTHER PEOPLE’S MONEY AND HOW THE BANKERS USE IT* 62 (Richard M. Abrams ed., Harper & Row 1967) (1914).

366. See, e.g., *Davos: The Tide Is Turning Against Tax Havens*, BANKING BUS. REV., Feb. 16, 2009.

367. John D. McKinnon, *Tax Justice Network: Wealth Held in Tax Havens Skyrockets*, WALL ST. J. WASH. WIRE BLOG (July 22, 2012, 5:05 AM), <http://blogs.wsj.com/washwire/2012/07/22/tax-justice-network-wealth-held-in-tax-havens-skyrockets/>.

368. See *supra* text accompanying notes 283–89.

369. See David S. Miller, *How U.S. Tax Law Encourages Investment Through Tax Havens*, 131 TAX NOTES 167 (2011).

Moreover, the stakes are higher than just the integrity of the U.S. tax system. As the facts of the HSBC investigation demonstrate, there are other dangers of bank secrecy.³⁷⁰ Tax havens are used not only to evade income taxes and hide assets. Bank secrecy allows illegal, as well as legal, income to be hidden, and financial anonymity allows drug dealers, organized crime, and terrorism financing to remain undetected. In this regard, the Norway Report stated:

[T]he damaging structures in tax havens not only influence tax revenues in other states. These structures are also suitable for conducting and concealing a great many forms of criminal activity in which it is important to hide the identity of those involved, where the crimes are being committed and what they involve. This includes such activities as the illegal sale of valuable goods, art, weapons and narcotics, human trafficking, terrorism, corruption, theft, fraud and other serious economic crimes.³⁷¹

Tax havens also contributed to the devastating financial crisis of recent years.³⁷² Thus, any prosecution policy should focus on obtaining information to combat less morally ambiguous crimes—money laundering, terrorism financing, and drug trafficking.

5. Summary

On balance, prosecuting offshore banks and bankers was the right choice. Like the tax shelter prosecutions, the decision to prosecute the professionals was more effective than prosecuting the few depositors that the Department of Justice's resources would permit. While the decision to go after the banks was perhaps suspect from a theoretical perspective, its deterrent effect cannot be disputed. The prosecutorial stick, combined with greater informational exchange and voluntary disclosure initiatives, has brought unprecedented cooperation with respect to offshore bank accounts. Yet, more must be done. The current prosecution policy has made only a small dent in tax haven abuses, and it appears to have done nothing to ameliorate the impact of havens on the developing world. The tax-shelter war may indeed be over, and if it is, the government certainly won.³⁷³ However, the recent prosecutions are not the end of the tax-haven war. At best, we can hope that these prosecutions represent the "end of the beginning."³⁷⁴

370. See SENATE REPORT, *supra* note 112.

371. NORWAY REPORT, *supra* note 356, at 20.

372. See, e.g., Rachel Keeler, *Tax Havens and the Financial Crisis: From Offshore Havens to Financial Centers, Banking Secrecy Faces Scrutiny*, DOLLARS & SENSE, May–June 2009, at 21, available at <http://www.dollarsandsense.org/archives/2009/0509keeler.html>.

373. See Fleischer, *supra* note 107.

374. The full quote from a wartime speech by Winston Churchill is: "Now this is not the end. It is not even the beginning of the end. But it is, perhaps, the end of the beginning." WINSTON S. CHURCHILL, THE END OF THE BEGINNING 266 (1943), available at <http://www.winstonchurchill.org/learn/speeches/speeches-of-winston-churchill/1941-1945-war-leader/987-the-end-of-the-beginning>.

V. CONCLUSION

The decision to bring a criminal prosecution is one of the most significant decisions a government can make. In deciding to employ its limited prosecutorial resources against any person, the government must ensure that it is charging only clear violations of the law and that prosecution goals will be fulfilled by the indictment. Merely because the government *can* successfully bring a criminal prosecution does not necessarily mean that it *should*. In making decisions whether to prosecute or not to prosecute, a determination of guilt by the defendant is not sufficient. Only those cases that satisfy all of the stated goals should be advanced.

Going forward, future investigations and prosecutions should focus more explicitly on the purposes for which criminal tax prosecutions are brought: to punish wrongdoers (the correct ones), to promote the integrity of the tax system (such as it is), and to redress the wrongs inflicted on the victims (all of them). While the tax shelter prosecutions satisfied each of these, the tax haven prosecutions did not; this was not because the offshore bankers were innocent, but because the prosecutions left so many problems unaddressed. Most banks, including U.S. banks, still do not provide information about their depositors to other governments. *Trillions* of dollars remain squirreled away offshore, with much of that money coming from the countries least able to deal with the outflow of cash. Accordingly, despite the Senate Permanent Subcommittee on Investigation's belief that there is "newfound international determination to contest tax evasion facilitated by a tax haven bank,"³⁷⁵ it does not appear that there is unanimity that bank transparency is an attainable, or even a desirable, goal. Until such unanimity can be reached, criminal prosecutions of offshore banks will be suspect.

That being said, significant progress has been made. The recent prosecutions of professionals have introduced—and proven—a powerful new tool for the government. Prosecuting professionals magnifies the deterrent effect of these prosecutions; shutting down the service providers is more effectual than prosecuting the clients. Accordingly, where professionals of any kind facilitate criminal activity, focusing on the enablers should be a viable, if not the primary, target.

375. SENATE REPORT, *supra* note 112, at 2.