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The Stop Tax Haven Abuse Act: A Unilateral Solution to a Multilateral Problem

Anthony D. Todero

Note

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INTRODUCTION

On March 2, 2009, Senator Levin introduced the Stop Tax Haven Abuse Act (the "Act") in the Senate.[1] Like its name implies, the goal of the Act is "[t]o restrict the use of offshore tax havens and abusive tax shelters . . . ."[2] The Obama Administration fully supports the Act.[3] Although the bill is currently in committee (as of Nov. 1, 2009),[4] many speculate

* Anthony D. Todero, M.A., Communication Studies, University of Minnesota, J.D. Candidate, University of Minnesota Law School. This Note would not be possible without the support of my partner, Leslie, and my parents, Joseph and Catherine. I am grateful for all that they have done for me. I would also like to thank Micah Reyner, Elliot Ginsburg, and the staff of the Minnesota Journal of International Law for making this a better Note.

1. FRESHFIELDS BRUCKHAUS DERINGER US LLP, SENATOR LEVIN AND REPRESENTATIVE DOGGETT INTRODUCE STOP TAX HAVEN ABUSE ACT (2009), http://www.freshfields.com/publications/pdfs/2009/mar09/25385.pdf. Representative Doggett introduced an identical bill (H.R. 1265) in the House of Representatives on March 3, 2009. *Id.*

2. Stop Tax Haven Abuse Act, S. 506, 111th Cong. (2009).

3. Kevin Drawbaugh & Corbett Daly, *Obama Administration Backs Congress Tax Haven Crackdown*, REUTERS, Mar. 3, 2009, http://www.reuters.com/article/politicsNews/idUSTRE52271L20090303 ("We fully support the legislation . . . on offshore tax centers . . . ."); *see also* Press Release, Timothy Geithner, U.S. Treasury Secretary, U.S. Treasury Secretary Tim Geithner Written Testimony House Ways and Means Committee Hearing—As Prepared for Delivery (Mar. 3, 2009), *available at* http://www.treas.gov/press/releases/tg47.htm (stating that the Obama Administration "will propose rules to both reform U.S. corporations' ability to defer foreign earnings and deter high income individuals and corporations from using tax havens to avoid taxation.").

4. *See* Govtrack.us: A Civic Project to Track Congress, S.506: Stop Tax Haven Abuse Act, http://www.govtrack.us/congress/bill.xpd?bill=s111-506 (last visited Nov. 2, 2009) (describing the legislative history of the bill). Bills introduced in Congress first go to committees where Senators and Representatives deliberate, investigate,

that the legislation will pass in the current session.[5] In the event of its passage, the Stop Tax Haven Abuse Act will fail to eliminate tax havens and foreign tax evasion.[6] The Act is not geared toward international cooperation. Instead, it uses a "name and shame" strategy, which other countries have an incentive to oppose.[7]

Fortunately, alternative mechanisms for the exchange of international tax information exist, such as an international tax authority with domestic enforcement powers[8] or a market-oriented solution that would use cash as consideration for tax information.[9] Both alternatives could improve the exchange of tax information necessary to enforce U.S. tax laws. These alternatives take into account the needs of tax haven jurisdictions and therefore are more likely to promote international cooperation.[10] Rather than place the United

and revise the bills. Then the bills are sent to the floor for general debate. Most bills do not make it out of committee. *Id.*

5. *See infra* Part III.

6. *See infra* Parts III.B.1–5.

7. The Act refers to targeted tax havens as "foreign secrecy jurisdictions." *See* S. 506 § 101(b). For how the Act defines a "foreign secrecy jurisdiction," see *infra* Part III.B. Other nations' politicians and bankers do not like the stigma attendant with the label of "foreign secrecy jurisdiction" because it might scare away reputable clients. *See* States of Guernsey, Chief Minister Welcomes G20 Summit Outcome, http://www.gov.gg/ccm/treasury-and-resources/press-releases/2009/chief-minister-welcomes-g20-summit-outcome.en?textonly=yes (last visited Nov. 2, 2009) (quoting Guernsey Chief Minister Lyndon Trott after the island signed thirteen Tax Information Exchange Agreements: "This puts to bed, once and for all, the myth that the island of Guernsey is a tax haven . . . . The stigma of tax haven status should be gone forever."); Anthony Faiola & Mary Jordan, *Tax-Haven Blacklist Stirs Nations: After G-20 Issues Mandate, Many Rush to Get Off Roll*, WASH. POST, Apr. 4, 2009, at A7 (giving examples of countries, such as Austria and the Philippines, that promised to exchange tax information after the G-20 countries unveiled a new "list of shame"). Moreover, Swiss banks, for example, face the uneasy choice between violating U.S. law or defying Swiss law's stringent bank secrecy provisions. *See* David S. Hilzenrath, *IRS, Justice Target Undisclosed Assets in Swiss Accounts*, WASH. POST, Nov. 1, 2008, at D01 (describing the predicament of Swiss bank UBS in trying to comply with a U.S. court order that is contrary to Swiss secrecy laws).

8. *See* ZVI DANIEL ALTMAN, DISPUTE RESOLUTION UNDER TAX TREATIES 351 (2005) (explaining that an international mechanism trusted by all treaty partners is inherently necessary for coordination, but that enforcement, because of sovereignty, necessitates an international tax institution capable of domestic enforcement).

9. *See generally* Steven A. Dean, *The Incomplete Global Market for Tax Information*, 49 B.C. L. REV. 605, 658–61 (2008) (discussing the pros and cons of a more complete market for tax shelter information).

10. *See* United Nations Conference on the World Financial and Economic Crisis and its Impact on Development, New York, June 1–3, 2009, *Outcome of United Nations Conference on the World Financial and Economic Crisis and its Impact on Development*, ¶ 35, *available at* http://www.un.org/ga/president/63/interactive/

States in the unenviable position of global tax enforcer, an international tax authority or a more complete market for tax information would better facilitate the exchange of extraterritorial tax information and promote U.S. tax enforcement.

This Note does not consider the entirety of the Stop Tax Haven Abuse Act. Instead, the brunt of the criticism is levied at the Act's list of tax havens.[11] The Act identifies specific jurisdictions as tax havens;[12] mandates heightened scrutiny of financial transactions conducted in those jurisdictions;[13] imposes relaxed evidentiary burdens on prosecutors, in the form of rebuttable presumptions,[14] to make enforcement of tax laws

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financialcrisis/outcomedoc.pdf (highlighting the need for inclusive policies that will allow developing countries to benefit from international tax cooperation); *see also* Steven A. Dean, *End the Barter System*, NAT'L L. J., Aug. 27, 2007, *available at* http://www.brooklaw.edu/news/homepage_news/dean_tax_article.pdf (advocating compensating cooperative countries with cash rather than bartering for the exchange of extraterritorial tax information).

11. See generally Brigitte Unger & Joras Ferwerda, *Regulating Money Laundering and Tax Havens: The Role of Blacklisting* (Tjalling C. Koopmans Research Inst. Discussion Paper Series, Paper No. 08-12, May 15, 2008), *available at* http://www.uu.nl/uupublish/content/08-12.pdf, for more about the strategy of "naming and shaming" tax havens.

12. *See* S. 506 § 101(b). According to the initial list in the Act, each of the following jurisdictions is an offshore secrecy jurisdiction: Anguilla, Antigua and Barbuda, Aruba, Bahamas, Barbados, Belize, Bermuda, British Virgin Islands, Cayman Islands, Cook Islands, Costa Rica, Cyprus, Dominica, Gibraltar, Grenada, Guernsey/Sark/Alderney, Hong Kong, Isle of Man, Jersey, Latvia, Liechtenstein, Luxembourg, Malta, Nauru, Netherlands Antilles, Panama, Samoa, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines, Singapore, Switzerland, Turks and Caicos, and Vanuatu. *Id.* § 101(b).

13. For example, the Act allows more time for investigating transactions conducted within one of the identified jurisdictions. In the instance of a tax return for a year in which the taxpayer received money from a financial account located in an offshore secrecy jurisdiction, "the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time within 6 years after the return was filed." *See id.* § 104(a). The current statute of limitations on international tax enforcement is three years. I.R.C. § 6501(a) (2006); *see also* Press Release, the White House Office of the Press Secretary, Leveling the Playing Field: Curbing Tax Havens and Removing Tax Incentives for Shifting Jobs Overseas (May 4, 2009), http://www.whitehouse.gov/the_press_office/leveling-the-playing-field-curbing-tax-havens-and-removing-tax-incentives-for-shifting-jobs-overseas/ (proposing to increase the statute of limitations on international tax enforcement to six years).

14. *See* S. 506 § 101. The law would amend the Internal Revenue Code by establishing a rebuttable presumption relating to control (§ 7492(a)) and transfers of income (§ 7492(b)) against persons who participated in transactions involving offshore secrecy jurisdictions. For example, the law provides that a U.S. person exercises control over an entity domiciled in an offshore secrecy jurisdiction if she has transferred any assets to the entity. The law also would amend 31 U.S.C. §

easier in those jurisdictions; and enacts other provisions all geared toward boosting the international enforcement of U.S. tax laws.[15] Certain sections of the Act are logical amendments to the tax code. For example, the Act extends the statute of limitations for the Internal Revenue Service (IRS) to assess taxes on tax returns requiring offshore examinations from three years to six years.[16] Government Accountability Office (GAO) studies show that offshore examinations take "a median of 500 more calendar days to develop and examine than other examinations" because of technical complexity and the need to obtain information from foreign sources.[17] The IRS ends some offshore examinations prematurely or opts not to conduct them at all, even with evidence of noncompliance, because of the current three-year statute of limitations.[18] It makes sense, then, to allow the IRS more time to conduct examinations of offshore transactions. However, the decision to blacklist the countries whose cooperation is necessary for the IRS to obtain the necessary information to enforce U.S. tax laws demands scrutiny and is the focus of this Note.

In light of the acknowledged caveat in scope, this Note proceeds as follows. Part I discusses the current international mechanisms (and their limitations) by which the United States attempts to enforce its tax laws abroad. Part II illuminates the impetus behind cracking down on tax havens. Specifically, two recent occurrences—the Liechtenstein and UBS scandals—have catapulted tax abuse to the forefront of the collective conscience.

Part III takes aim at the Stop Tax Haven Abuse Act. This Note does not take a normative position on the benefits or

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5314 (2006) by creating a presumption that any account at a financial institution domiciled in an offshore secrecy jurisdiction contains the minimum funds necessary to require a report prescribed by tax law. *Id.* § 101(d).

15. For a summary of the Act's various provisions, see Cadwalader, Wichersham & Taft LLP, *Clients & Friends Memo: Stop Tax Haven Abuse Act (S. 506 and H.R. 1265)*, Mar. 6, 2009, http://www.cadwalader.com/assets/client_friend/030609_StopTaxHavenAbuseAct.pdf.

16. *See supra* note 13.

17. *Tax Compliance: Offshore Financial Activity Creates Enforcement Issues for IRS: Hearing Before the S. Comm. on Finance*, 111th Cong. 8 (2009) (statement of Michael Brostek, Director, Tax Issues, Strategic Issues Team, Government Accountability Office).

18. *Id.* ("Because of the 3-year statute of limitations on assessments, the additional time needed to complete an offshore examination means that IRS sometimes has to prematurely end offshore examinations and sometimes chooses not to open them at all, despite evidence of likely noncompliance.").

drawbacks of tax havens.[19] Rather, it assumes that taxation, as a mechanism to gather revenues for government programs, is necessary.[20] A legislative attempt to achieve this goal that will fail in practice is worthy of noting.[21] Although increasing government tax revenue[22] is a laudable motivation, the Act does not take into account foreign actors' interests. As a result, it is unlikely to bolster the exchange of tax information, which would improve IRS enforcement of U.S. tax laws.

Part IV concludes this Note by discussing two alternatives to the Stop Tax Haven Abuse Act's "name and shame" strategy of blacklisting tax havens. A policy of paying cash as consideration for tax information would be more successful in eliciting the cooperation of foreign actors, but market failures and privacy issues are potential concerns. An international tax institution might take a long time to create because existing entities, like the Organisation for Economic Co-operation and

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19. Although the term "tax haven" is used frequently, "[t]here is no precise definition of a tax haven." JANE G. GRAVELLE, TAX HAVENS: INTERNATIONAL TAX AVOIDANCE AND EVASION 2 (2009), http://assets.opencrs.com/rpts/R40623_20090709.pdf. I do not use the term in any normative sense, but only in a descriptive sense to indicate a jurisdiction with few or no taxes, a lack of effective information sharing, and a lack of transparency. *See id.* (citing ORG. FOR ECON. DEV. AND CO-OPERATION, HARMFUL TAX COMPETITION: AN EMERGING GLOBAL ISSUE 23 (1998)) (describing features of tax havens).

20. The normative argument in favor of the Stop Tax Haven Abuse Act assumes that tax havens are "abusive." *See, e.g.*, Maria Tihin, Note, *The Trouble with Tax Havens: The Need for New Legislation in Combating the Use of Offshore Trusts in Abusive Tax Shelters*, 41 COLUM. J.L. & SOC. PROBS. 417, 419 (2008) (focusing on abusive tax shelters and discussing the movement of those shelters to offshore jurisdictions).

21. The President's budget request for IRS compliance programs for fiscal year 2010 includes an increase of "$332.2 million for investments in strong compliance programs . . . ." *Fiscal 2010 Appropriations: Financial Services and General Government: Hearing Before the Subcomm. on Financial Servs. and General Government of the S. Appropriations Comm.*, 111th Cong. 5 (2009) (statement of Douglas H. Shulman, Commissioner, Internal Revenue Service). The Act, therefore, does not come without economic costs. Legislators should hesitate before enacting the bill if the likelihood of success is low. Moreover, less controversial proposals are available. In March 2009, shortly after Senator Levin proposed the Act, Senator Baucus proposed a more modest version of the Act that does not contain a blacklist. Baucus favors a more targeted approach that would also give the IRS additional tools to investigate U.S. tax evaders, but would not condemn all offshore tax havens. *See* Edward Tanenbaum, *Stop Tax Haven Abuse Act Has Broad Implications*, INT'L TAX REV., June 2009, *available at* http://www.internationaltaxreview.com/includes/magazine/PRINT.asp?SID=720491&ISS=25409&PUBID=35.

22. *See* Hearing on Fiscal 2010 Appropriations, *supra* note 21, at 6 (noting that new enforcement personnel are expected to generate $2 billion in additional annual revenue and an estimated $6 billion in indirect revenue based on the deterrent effect of the new enforcement programs by FY 2012).

Development (OECD) and the United Nations (U.N.), are not compelling status quo auspices for an international tax authority.[23] Regardless of the potential counterarguments against these alternatives, if implemented, both would be more successful at facilitating the exchange of extraterritorial tax information than the Stop Tax Haven Abuse Act.

I. THE TAX GAP AND CURRENT MECHANISMS OF EXCHANGING EXTRATERRITORIAL TAX INFORMATION

Globalization has collapsed many previously existing legal and technological barriers to international capital flows, making tax evasion easier and tax administration more difficult.[24] The Internal Revenue Service's international enforcement of U.S. tax law thus faces daunting challenges.[25] The largest obstacle in administering U.S. tax law in foreign locales is that much of the information needed to enforce these laws is unavailable.[26] The IRS, for example, has difficulty identifying persons outside of the United States who are taxable as U.S. residents or citizens.[27] The IRS does not cross-check passports against filed returns to locate those outside the United States who fail to file.[28] Even if the IRS could identify U.S. residents or citizens in

23. *See* Justin Dabner, *To Join the International Tax Cartel or Not? How Should Asia Respond to the OECD's Harmful Tax Regimes Project?* 11 N.Z. J. TAX'N L. & POL'Y 299, 302 (2005) ("The lack of a level playing field has become the major issue confronting the OECD."); Jonathan Gaskin, Note, *Policing the Global Marketplace: Wielding a Knife in a Gunfight*, 38 COLUM. J. TRANSNAT'L L. 191, 207 (1999) (noting that the U.N. lacks the authority to implement standards on international tax cooperation).

24. *See* Nancy Birdsall, *Asymmetric Globalization: Global Markets Require Good Global Politics*, BROOKINGS REV., Spring 2003, *available at* http://www.brookings.edu/articles/2003/spring_development_birdsall.aspx (noting that unregulated markets make it easier for taxpayers to evade taxes and more expensive for countries to enforce their own tax systems).

25. *See* David R. Tillinghast, *Issues of International Tax Enforcement*, *in* THE CRISIS IN TAX ADMINISTRATION 38, 39 (Henry J. Aaron & Joel Slemrod eds., 2004) (discussing the "prodigious" number of challenges facing the IRS in enforcing U.S. tax law in foreign jurisdictions).

26. *Id.* The IRS has domestic capabilities, e.g., the powers to investigate, summons, and sue, to enforce tax laws but lacks similar powers in foreign jurisdictions. *Id.*

27. *See generally* Hearing on Tax Compliance, *supra* note 17, at 7–11 (discussing the difficulty the IRS has in collecting tax information from U.S. persons in foreign jurisdictions).

28. *See* Tillinghast, *supra* note 25, at 39–40 (noting that the IRS has no system in place to help administrators perform these cross-checks of passports or green cards against filed returns).

foreign jurisdictions who failed to file their taxes, in many cases the IRS has no enforcement mechanism with which to compel foreign persons to comply.[29] Not surprisingly, few foreign withholding agents properly withhold the required taxes from their client's income.[30] Moreover, foreign laws, such as bank secrecy laws, may limit the disclosure of tax information necessary for IRS enforcement.[31] Largely due to these enforcement difficulties, the United States has a gross tax gap—"the difference between the aggregate tax liability imposed by law for a given tax year and the amount of tax that taxpayers pay voluntarily and timely for that year."[32]

In 2005, the IRS estimated that the gross tax gap was approximately $345 billion.[33] Other countries face similar shortfalls in tax revenues.[34] A fairness issue arises when some

29. *See* Tillinghast, *supra* note 25, at 39 (stating that the IRS has "no practical way to enforce" U.S. tax obligations against foreign persons). In the recent presidential campaign season, there was a debate about whether or not paying taxes is patriotic. *See, e.g.*, Thomas Friedman, Op-Ed., *Palin's Kind of Patriotism*, N.Y. TIMES, Oct. 8, 2008, at A31. If patriotism is not a factor, i.e., if people are foreign to the United States, it is logical that foreign persons would ignore U.S. tax laws, particularly if the IRS had no means of requiring compliance.

30. *See* Tillinghast, *supra* note 25, at 39 (noting that the IRS has had success in "inducing foreign financial institutions to 'volunteer' to act as withholding agents . . . . It has no practical way to enforce this obligation, however, and few foreign persons . . . comply.").

31. For example, Switzerland's bank secrecy is legendary. Switzerland has a "reputation for confidentiality that has helped make a small nation in the Alps a magnet for international deposits." Hilzenrath, *supra* note 7, at D3. Generally, Swiss law limits a bank's ability to breach client confidentiality. More specifically, Swiss law affords account holders the chance "to oppose the release of their names through a judicial process . . . ." *Id. See also Prosecutors Focus on Swiss Bank Accounts*, UNITED PRESS INT'L, Nov. 1, 2008, *available at* http://www.upi.com/Business_News/2008/11/01/Prosecutors-focus-on-Swiss-bank-accounts/UPI-65601225553320/ (noting that "Swiss banks, by law, cannot disclose account holder information . . . .").

32. JAMES M. BICKLEY, TAX GAP AND TAX ENFORCEMENT (Cong. Research Serv. Report No. RL33882, 2007), *available at* http://wikileaks.org/leak/crs/RL33882.pdf (citing ALAN PLUMLEY, INTERNAL REVENUE SERV., PRELIMINARY UPDATE OF THE TAX YEAR 2001 INDIVIDUAL INCOME TAX UNDERREPORTING GAP ESTIMATES 15 (2005), *available at* http://www.irs.gov/pub/irs-soi/05plumley.pdf).

33. U.S. DEP'T OF THE TREASURY, UPDATE ON REDUCING THE FEDERAL TAX GAP AND IMPROVING VOLUNTARY COMPLIANCE 2 (2009), *available at* http://www.irs.gov/pub/newsroom/tax_gap_report_-final_version.pdf; *see also* David R. Francis, *With $100 Billion Lost, U.S. Tolerance for Tax Havens Erodes*, CHRISTIAN SCI. MONITOR, June 9, 2008, at 15.

34. For example, the United Kingdom's (UK) public finances are short billions of pounds because some of the country's biggest corporations have complex, opaque, albeit legal tax schemes by which they avoid paying taxes to the exchequer. UK-based Diageo, which owns Johnnie Walker and Gilbey's gin, "[d]espite average

people pay the taxes required by law and others do not. Furthermore, if noncompliance goes unpunished, there is an added incentive to those who ordinarily comply to stop paying taxes, resulting in "a vicious cycle of increased noncompliance."[35]

A. SOURCES OF THE TAX GAP

Individual income taxes constitute the majority of the U.S. gross tax gap.[36] Unreported or underreported income account for the bulk of these unpaid taxes.[37] Estimates of the annual costs of offshore tax abuses are as high as $100 billion per year, although accurate estimates of individual tax avoidance[38] are more difficult than estimates of corporate tax avoidance.[39] Transparency International France estimated that approximately $10 trillion U.S. dollars, or over four times the amount of France's gross domestic product, are located in secret offshore accounts.[40]

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profits of £2 bn a year . . . paid an average of £43m a year in UK tax – little more than 2% of its overall profits." *Firms' Secret Tax Avoidance Schemes Cost UK billions: Investigation into the Complex and Confidential World of Tax*, GUARDIAN (London), Feb. 2, 2009, at 1. Germany also has a significant problem collecting taxes, as thousands of Germans shelter funds from taxes in the Alpine country of Liechtenstein. *Id.* at 3.

35. *The Causes of and Solutions to the Federal Tax Gap: Hearing Before the S. Comm. on the Budget*, 109th Cong. 1 (2006) (written statement of Nina E. Olson, National Taxpayer Advocate), *available at* http://budget.senate.gov/republican/hearingarchive/testimonies/2006/NinaOlsenTestimony.pdf. Taxpayers who meet their own obligations but witness others' noncompliance go unpunished might feel like "chumps." *Id.*

36. *See* U.S. DEP'T OF TREASURY, *supra* note 33, at 3 (finding that individual income taxes represent more than 50% of the tax gap); *see also* JASON FURMAN, *Closing the Tax Gap*, CTR. ON BUDGET & POLICY PRIORITIES (Wash., D.C.), Apr. 10, 2006, 1–2, http://www.cbpp.org/files/4-10-06tax3.pdf (noting that $244 billion of the $345 billion tax gap comes from individual income taxes).

37. FURMAN, *supra* note 36, at 2.

38. The distinction between "tax avoidance" and "tax evasion" is unclear. *See* GRAVELLE, *supra* note 19, at 1 (noting that avoidance sometimes refers "to a legal reduction in taxes, while evasion refers to tax reductions that are illegal . . . ."). Most international tax reductions by individuals reflect evasion. *Id.*

39. *See* GRAVELLE, *supra* note 19, at 21 (indicating that there are no official estimates of individual tax evasion, and that estimates of individual evasion, as opposed to corporate evasion, are difficult "because the initial basis of the estimate is the amount of assets held abroad whose income is not reported to the tax authorities.").

40. Clea Caulcutt, *France, Germany push for tax haven blacklist*, FRANCE24.COM, Oct. 21, 2008, http://www.france24.com/en/20081021-world-leading-economies-tackle-tax-havens-oecd-france-germany. France's estimated GDP for 2008 was $2.128 trillion. CENTRAL INTELLIGENCE AGENCY, WORLD FACTBOOK

B. BILATERAL AGREEMENTS

Bilateral tax information exchange is the main tool by which the IRS gathers extraterritorial tax information.[41] Using this mechanism, a nation enters into an agreement with another nation that requires both nations' tax authorities to provide relevant tax information to the other nation upon request.[42] Bilateral tax information exchange agreements (TIEAs) are increasing in number.[43] Estimates put the number of bilateral tax treaties at greater than 1700.[44] These agreements find their roots in the model taxation treaties created by the League of Nations in 1927.[45] In 1927, states recognized that bilateral treaties, rather than multilateral conventions, would be more effective in dealing with the international tax evasion problem because fundamental differences in fiscal systems would make multilateral agreements difficult to conclude without intruding on national sovereignty.[46]

There are, however, problems regarding the effectiveness of bilateral tax agreements. In order to request information about a foreign person located outside U.S. territory who has failed to

(2008), *available at* https://www.cia.gov/library/publications/the-world-factbook/geos/fr.html.

41. *See* Dean, *supra* note 9, at 608 (discussing the current barter system by which countries exchange tax information for tax information).

42. *See, e.g.*, U.S. Treasury Dep't, United States Model Income Tax Convention, art. 26 (2006), *available at* http://www.ustreas.gov/press/releases/reports/hp16801.pdf (describing the process of exchanging international tax information in order to carry out domestic laws).

43. *See* ORG. FOR ECON. CO-OPERATION & DEV., TAX CO-OPERATION: TOWARDS A LEVEL PLAYING FIELD—2007 ASSESSMENT BY THE GLOBAL FORUM ON TAXATION 9 (2007) (The OECD, referring to eighty-six countries, noted that "[s]ince 31 December 2005, 86 new DTCs [double taxation conventions] have entered into force . . . resulting in a total of 1814 DTCs in force . . . .").

44. *See, e.g.*, Michael J. Graetz, *Taxing International Income: Inadequate Principles, Outdated Concepts, and Unsatisfactory Policies*, 26 BROOK. J. INT'L L. 1357, 1358 (2001) (referring to the 1920s as the decade in which countries created the system of international income tax enforcement mechanisms that has served as the "basis for more than 1700 bilateral income tax treaties now in force throughout the world.").

45. *See* Dean, *supra* note 9, at 609 ("The roots of today's extraterritorial tax information acquisition system can be traced back to . . . the foundational 1927 League of Nations report on international taxation.").

46. *See Reports Presented by the Comm. of Technical Experts on Double Taxation and Tax Evasion*, League of Nations Doc. C.216M.85 1927 II, at 23 (1927), *available at* http://faculty.law.wayne.edu/tad/Documents/League/League_Tech_Experts.pdf (noting that the Committee realized that a major risk of the Convention was "appearing in some quarters as an extension beyond national frontiers of an organised system of fiscal inquisition.").

pay taxes, the IRS must establish the identity of the taxpayer under investigation in advance.[47] The IRS must also demonstrate that it has exhausted all the available means by which it could have obtained the necessary information domestically.[48] Another problem with bilateral treaties is that they often do not yield the necessary tax information in a particular case.[49] For example, most of the agreements that the United States has in place are limited to criminal matters, which constitute a minor portion of overall tax revenues.[50] In the event the IRS does obtain information via bilateral exchange agreements, the exchange of "bulk taxpayer information"[51] and the trade of personally sensitive information[52] raise profound privacy issues. In one sense, bilateral agreements do not provide enough useful information. In another sense, the exchange of bulk information provides too much sensitive information.

Although bilateral agreements may seem preferable to a multilateral tax treaty in that they more easily accommodate differences in countries' tax systems, this rationale does not

47. *See* GRAVELLE, *supra* note 19, at 20. The agreements do not override bank secrecy laws, making it difficult to identify potential tax evaders.

48. *See* Tillinghast, *supra* note 25, at 42 (noting the "legal and practical impediments to the use of these [exchange-of-information] agreements.").

49. The United States might not have agreements in place, as bilateral agreements often exclude developing countries. *See* Markus Meinzer et al., Tax Information Exchange Arrangements 3 (2009), http://www.taxjustice.net/cms/upload/pdf/TJN_0903_Exchange_of_Info_Briefing_draft.pdf (noting that "TIEAs do not work for developing countries" because developing countries have little leverage and are unlikely to benefit from these agreements). Furthermore, the countries with which the United States has an exchange agreement may have little to no tax information of use. *See id.* at 4 (arguing that TIEAs are ineffective when the "information simply does not exist in the jurisdiction concerned . . . .").

50. *See Hearing on Banking Secrecy Practices and Wealthy American Taxpayers Before the Subcomm. on Select Revenue Measures of the H. Comm. on Ways and Means*, 111th Cong. (2009) (statement of Reuven S. Avi-Yonah, Irwin I. Cohn Professor of Law, University of Michigan Law School), *available at* http://waysandmeans.house.gov/hearings.asp?formmode=view&id=7646 (noting that "most of the existing agreements are restricted only to criminal matters" and that these represent a "very small part of overall tax collections . . . .").

51. ORG. FOR ECON. CO-OPERATION & DEV., COMM. ON FISCAL AFFAIRS, MANUAL ON THE IMPLEMENTATION OF EXCHANGE OF INFORMATION PROVISIONS FOR TAX PURPOSES, MODULE 3 ON AUTOMATIC (OR ROUTINE) EXCHANGE OF INFORMATION ¶¶ 1–4 (2006), *available at* http://www.oecd.org/dataoecd/16/23/36647823.pdf (noting that some tax information is exchanged automatically by law).

52. *See* Cynthia Blum, *Sharing Bank Deposit Information with Other Countries: Should Tax Compliance or Privacy Claims Prevail?*, 6 FLA. TAX REV. 579, 623–33 (2004) (discussing the privacy claims on bank information by foreigners with U.S. bank accounts and U.S. citizens with offshore bank accounts).

withstand scrutiny. First, the IRS needs tax information from countries with radically different tax systems than the United States.[53] As a result, bilateral tax treaties do not necessarily solve the problem of gathering the necessary information for IRS enforcement of U.S. tax laws. The Bahamas, for example, do not levy taxes on personal income, capital gains, corporate earnings, dividends, or sales[54] and thus may not have the information the United States needs to enforce U.S. tax laws if a bilateral treaty was in effect between the two countries. Second, countries from which the United States needs information to enforce its tax laws may not have an agreement in place for the exchange of information. For example, the Bahamas do not have a bilateral tax treaty with the United States, so the U.S. has no means of obtaining even the limited information that is available.[55] Third, with the already large number of tax agreements, conducting future bilateral agreements may add unnecessary complexity, making enforcement more, not less, difficult.[56] Finally, even if compelling arguments for bilateral tax agreements exist, they do not necessitate foregoing multilateral agreements.[57]

53. *See* Gregory Rawlings, *Responsive Regulation, Multilateralism, Bilateral Tax Treaties, and the Continuing Appeal of Offshore Finance Centres* 16 (Ctr. for Tax Sys. Integrity, Working Paper No. 74, 2005), *available at* http://ctsi.anu.edu.au/publications/WP/74.pdf (explaining that because "tax regulation was never internationalised by way of a multilateral agreement," multinational companies "could take advantage of diversity in types, rates and definitions of tax" in different national regimes).

54. Raymond T. Gibson, *The Bahamas – The Tax-Free Alternative to Florida*, VAULT MAG., Sept. 2002, *available at* http://www.henleyglobal.com/fileadmin/pdfs/media-events/articles/bahamas2002.pdf.

55. Despite the existence of hundreds of bilateral tax exchange agreements, the United States does not have agreements in place with many countries from which the United States needs tax information. As of April 2009, the United States had tax treaties in place with only fifty-seven countries. *See* INTERNAL REVENUE SERVICE, U.S. TAX TREATIES (2009), *available at* http://www.irs.gov/pub/irs-pdf/p901.pdf. Of the thirty-four jurisdictions listed as foreign secrecy jurisdictions in the Act, only five—Barbados, Cyprus, Latvia, Luxembourg, and Switzerland—currently have bilateral tax treaties in place with the United States. *Id.*

56. *See* Rawlings, *supra* note 53, at 7–8 (noting that the current international tax regulation scheme is not homogenous; instead, there are many competing regulatory orders that both intersect and diverge at vital moments). Although the regulatory agendas of various bodies (e.g., the IRS and the OECD) do converge at points, they are likely to diverge from each other as well as from the agenda of a tax authority in an offshore financial center. *Id.*

57. *But see* Haruhiko Kuroda, Japan's former Vice Minister of Fin. for Int'l Affairs, Keynote Address at the First International Convention of the Asia-Oceania Tax Consultants Association: Economic Integration and Tax Harmonization in Asia and Oceania (Nov. 6, 2002), *available at* http://www.mof.go.jp/english/if/

C. MULTILATERAL AGREEMENTS

There have been numerous attempts to deal with the problem of international tax evasion on a multilateral level. The OECD, the European Union, the International Monetary Fund (IMF), and the U.N. have all sought ways to spur international cooperation in tax administration by improving transparency or stimulating new exchange agreements.[58] The OECD, for example, established criteria for identifying member countries with preferential tax regimes, identified jurisdictions as "tax havens" if they met certain criteria,[59] and proposed new methods of cooperation with non-member countries.[60] The 2000 OECD Report identified thirty-five jurisdictions that might have been functioning as offshore tax havens. It required those jurisdictions to express a commitment to cooperate by 2005 and threatened to apply sanctions if the jurisdictions did not express commitment before July 31, 2001.[61] The U.N. Financial Action

vmi021106e.htm (suggesting that bilateral tax treaties may need to be integrated into a multilateral one to harmonize taxation).

58. *See generally* Gianluca Pirozzi, *Tax Havens and Relations with Industrialized Countries*, COSMOPOLIS, Feb. 2007, at 1–3, http://agora.qc.ca/cosmopolis.nsf/articles/no2007_2_tax_havens_and_relations_with_industrialized_count?opendocument (stressing the need to broaden the efforts to stymie tax evasion to include the concerns of poorer countries).

59. The OECD identified a tax haven by using four key factors: (1) "no or only nominal taxes (generally or in special circumstances);" (2) "laws or administrative practices which prevent the effective exchange of relevant information with other governments on taxpayers benefiting from the low or no tax jurisdiction;" (3) "lack of transparency;" and (4) "the absence of any requirement for substantial activity." *See generally* ORG. FOR ECON. CO-OPERATION & DEV., HARMFUL TAX COMPETITION: AN EMERGING GLOBAL ISSUE (1998) *available at* http://www.oecd.org/dataoecd/33/0/1904176.pdf [hereinafter OECD, 1998]; ORG. FOR ECON. CO-OPERATION & DEV., TOWARDS GLOBAL TAX CO-OPERATION: REPORT TO THE 2000 MINISTERIAL COUNCIL MEETING AND RECOMMENDATIONS BY THE COMMITTEE ON FISCAL AFFAIRS: PROGRESS IN IDENTIFYING AND ELIMINATING HARMFUL TAX PRACTICES (2000), *available at* http://www.oecd.org/dataoecd/9/61/2090192.pdf [hereinafter OECD, 2000]; ORG. FOR ECON. CO-OPERATION & DEV., THE OECD'S PROJECT ON HARMFUL TAX PRACTICES: THE 2001 PROGRESS REPORT (2001), *available at* http:www.oecd.org/dataoecd/60/28/2664438.pdf; ORG. FOR ECON. CO-OPERATION & DEV., THE OECD'S PROJECT ON HARMFUL TAX PRACTICES: THE 2004 PROGRESS REPORT (2004), *available at* http://www.oecd.org/dataoecd/60/33/30901115.pdf; *see also* Michael Littlewood, *Tax Competition: Harmful to Whom?*, 26 MICH. J. INT'L L. 411, 422 (2005) (highlighting how key terms such as "low" and "nominal" were undefined).

60. OECD, 2000, *supra* note 59, at 6 (noting the positive initial reaction to the OECD project on cooperation to remedy tax evasion).

61. Bruce Zagaris, *Ethical Issues in Offshore Planning*, 17 A.L.I. PROC. 365, 391 (2008), http://files.ali-aba.org/thumbs/datastorage/skoobesruoc/pdf/CP017_chapter_07_thumb.pdf (noting that today, "five offshore financial centers—Andorra, Liberia, Liechtenstein, the Marshall Islands, and Monaco—have refused

Task Force (FATF) also released a report in 2000 on "non-cooperative countries or territories (NCCTs)."[62] The critical enforcement mechanism of the FATF is Recommendation 21 that provides:

> Financial institutions should give special attention to business relationships and transactions with persons, including companies and financial institutions, from countries which do not or insufficiently apply the FATF Recommendations. Whenever these transactions have no apparent economic or visible purpose, their background and purpose, should, as far as possible, be examined, the findings established in writing, and be available to help competent authorities. Where such a country continues not to apply or insufficiently applies the FATF Recommendations, countries should be able to apply the appropriate countermeasures.[63]

The FATF recommends regulations and monitoring to ensure compliance,[64] but leaves it to individual jurisdictions to determine which countermeasures to apply in specific instances of tax abuse.[65] The FATF is not a legal entity, so its recommendations are not binding on governments or on the private sector.[66] The IMF, however, adopted the FATF recommendations in devising its review procedure to assess compliance with international anti-money laundering laws.[67] Furthermore, section 311 of the USA PATRIOT Act authorizes the U.S. executive branch to monitor, regulate, and enforce countermeasures against "jurisdictions, financial institutions, or international transactions of primary money laundering

[to express a formal commitment to cooperate]").

62. *Id.* at 373 (noting that the FATF identified hindrances to money laundering prevention and detection, released the results of judicial inquiries regarding the same, and that FATF members agreed on a process for identifying NCCTs and international methods to incentivize compliance).

63. FIN. ACTION TASK FORCE ON MONEY LAUNDERING, THE FORTY RECOMMENDATIONS 7 (2003), *available at* http://www.fatf-gafi.org/dataoecd/7/40/34849567.pdf.

64. *Id.*

65. *See* Zagaris, *supra* note 61, at 374 (noting that countermeasures may include not processing certain transactions or reporting transactions to tax authorities).

66. *See* Zagaris, *supra* note 61 at 375.

67. Zagaris, *supra* note 61 at 375; *cf.* Kern Alexander, *Global Financial Standard Setting, The G10 Committees, and International Economic Law*, 34 BROOK. J. INT'L L. 861, 877 (2009) (noting that the FATF has played a prominent role in international regulatory standard setting, but also noting that "[i]n recent years, however, the International Organization of Securities Commissions and the International Association of Insurance Supervisors have attracted much more policy attention since their standards have been recognized by the IMF and World Bank as international benchmarks . . . for compliance . . . .").

concern."[68] Therefore, although FATF recommendations are not legally binding, they carry considerable force.

1. *Criticisms of Multilateral Approaches*

Commentators have levied assaults at the OECD's campaign against preferential tax regimes as being too one-sided and unfair to non-OECD members.[69] A U.N. panel's recommendation to establish an international tax organization under the auspices of the United Nations,[70] has similarly received a lukewarm response.[71] Although a "World Tax Organization"[72] could remedy the patchwork of bilateral treaties, and such an authority would have the power to compel compliance and punish malfeasance, "there is no international organization that appears capable of serving as the linchpin of such a regime."[73]

II. THE CURRENT IMPETUS DRIVING THE CRACKDOWN ON TAX HAVENS

Although tax havens are not a new phenomenon,[74] they have grown recently because financial deregulation and globalization promote the international transfer of capital.[75]

68. USA PATRIOT Act of 2001 § 311, 31 U.S.C. § 5318(A) (2008).

69. *See, e.g.*, Littlewood, *supra* note 59, at 442–49 (reasoning that countries operate preferential tax regimes because doing so is in their economic interest); *see also* Pirozzi, *supra* note 58, at 3 (noting that "by asking them [weak-poor jurisdictions] to act 'cooperatively' and 'openly'—the high taxation regimes . . . maintain their privileges and their power . . . .").

70. *See* ERNESTO ZEDILLO, TECHNICAL REPORT OF THE HIGH-LEVEL PANEL ON FINANCING FOR DEVELOPMENT 27–28 (2001), *available at* http://www.un.org/reports/financing/full_report.pdf (describing the functions and benefits of creating an international tax organization).

71. *See, e.g.*, Daniel J. Mitchell, *Radical U.N. Tax Plans Threaten America*, HERITAGE FOUNDATION, Dec. 18, 2003, http://www.heritage.org/press/commentary/ed121803b.cfm (arguing that governments with free market systems, such as the United States, would be a target for persecution).

72. *See* Vito Tanzi, *Is There a Need for a World Tax Organization?*, *in* THE ECONOMICS OF GLOBALIZATION: POLICY PERSPECTIVES FROM PUBLIC ECONOMICS 173, 173–86 (Assaf Razin & Efraim Sadka eds., 1999) (lamenting that domestic legislators cannot keep pace with recent technological developments in financial markets).

73. Dean, *supra* note 9, at 663.

74. *See, e.g.*, Pirozzi, *supra* note 58, at 5 (noting that during the nineteenth century, some territories, currently labeled as tax havens, were harbors of refuge where ships could shelter from pirates and foul weather).

75. *See* Birdsall, *supra* note 24 (noting that open, unregulated markets make

Besides the obvious motive to boost government coffers in a time of economic straits,[76] there are multiple factors driving the initiatives[77] to stem the tide of tax evasion. Financial liberalization generally leads to increased economic instability,[78] because large amounts of capital flow easily into and out of jurisdictions.[79] Furthermore, the attacks of September 11, 2001 highlighted the use of tax havens to finance international terrorism.[80] More recently, global tax scandals erupted in February and May of 2008: the Lichtenstein and UBS scandals, respectively.[81]

tax evasion easier); *see also* Avi-Yonah, *supra* note 50 (highlighting that while the ability to move capital, goods, and services has increased dramatically, tax administrators' tools to combat tax evasion have not changed substantially).

76. *See* Press Release, Senator Levin, Statement of Senator Carl Levin on Introducing the Stop Tax Haven Abuse Act (Mar. 2, 2009), http://levin.senate.gov/newsroom/release.cfm?id=308945 ("I'm introducing the Stop Tax Haven Abuse Act . . . to stop tax cheats who drain our treasury of funds needed to pay for our recovery.").

77. The OECD and the G-20 have both recently targeted tax haven countries. *See* William Boston, *G-20 Leaders to Target Nations Harboring Tax Dodgers*, CHRISTIAN SCI. MONITOR, Mar. 30, 2009, at 6; David Crawford, *OECD Compiles List of Alleged Tax Havens for G-20*, WALL ST. J., Mar. 18, 2009, http://online.wsj.com/article/SB123733504461563913.html. In addition to the Stop Tax Haven Abuse Act, there are other legislative proposals including draft proposals by the Senate Finance Committee, two related bills, S. 386 and S. 569, and a proposal by President Obama. *See* GRAVELLE, *supra* note 19, at Summary.

78. *See* Robert Kuttner, *The Bubble Economy: The Sub-prime Mess, the Huge Risks Taken by Hedge Funds, and the Conflicts of Interest that Led to Enron Are All the Consequences of Serial Bouts of Financial Deregulation. Will We Reverse Field in Time to Prevent Another 1929?*, AM. PROSPECT, Sept. 24, 2007, *available at* http://www.prospect.org/cs/articles?article=the_bubble_economy (noting how the Glass-Steagall Act, which tightly regulated commercial banks, was weakened throughout the eighties until it was outright repealed in 1999).

79. *See* Sol Picciotto, *Tackling Tax Havens and 'Offshore' Finance*, TRANSNAT'L INST. 1–2, June 12–13, 2007, http://www.tni.org/crime-docs/picciotto.pdf (citing attempts to improve coordination of international financial regulation to protect against this systemic risk).

80. Sidney Weintraub, *Disrupting the Financing of Terrorism*, WASH. Q., Winter 2002, at 53, 56 (2002) (noting that tax havens are largely used by "tax evaders, criminals, and money launderers").

81. A disgruntled bank employee in Liechtenstein provided German tax authorities with tax information regarding approximately 1400 persons. *See* STAFF OF S. PERMANENT SUBCOMM. ON INVESTIGATIONS, 110TH CONG., TAX HAVEN BANKS AND U.S. TAX COMPLIANCE 2 (Comm. Print 2008). For more on the UBS scandal, see *infra* Part II.A.2.

A. TWO RECENT SCANDALS

1. The Liechtenstein Scandal

German tax authorities, armed with the names of six hundred to seven hundred German taxpayers who were using Liechtenstein accounts to evade paying the comparatively high German tax rates, executed search warrants and arrested a prominent businessman for evading $1.46 million in taxes.[82] Shortly thereafter, the IRS initiated enforcement action against more than one hundred taxpayers who also had accounts in Liechtenstein banks.[83] Approximately one dozen countries have announced a commitment to investigate potential tax evaders with accounts in Liechtenstein banks, evidencing the global scope of the scandal and the increased determination of countries to crack down on tax evaders.[84]

2. The UBS Scandal

A second worldwide tax scandal flared when the United States arrested a former UBS AG (one of the world's largest banks) employee on conspiracy charges involving defrauding the IRS of $200 million in unpaid taxes on assets in Switzerland and Lichtenstein worth approximately $7.26 billion.[85] The former UBS senior banker pled guilty in June of 2008 to

82. Carter Dougherty & Mark Lander, *Tax Scandal in Germany Fans Complaints of Inequity*, N.Y. TIMES, Feb. 18, 2008, at C1 (reporting that the scandal "brought down one of Germany's most powerful business figures, Klaus Zumwinkel, who resigned . . . as the chief executive of the German postal service after the police raided his home.").

83. IRS News Release, IRS and Tax Treaty Partners Target Liechtenstein Accounts 1 (Feb. 26, 2008) ("The Internal Revenue Service is initiating enforcement action involving more than 100 U.S. taxpayers to ensure proper income reporting and tax payment in connection with accounts in Liechtenstein.").

84. *See* STAFF OF S. PERMANENT SUBCOMM. ON INVESTIGATIONS, *supra* note 81, at 2 ("The national tax administrations of Australia, Canada, France, Italy, New Zealand, Sweden, United Kingdom, and the United States of America, all member countries of the OECD's Forum on Tax Administration (FTA), are working together following revelations that Liechtenstein accounts are being used for tax avoidance and evasion.").

85. Nick Mathiason, *Tax scandal leaves Swiss giant reeling: UBS could lose its licence in America after an official confessed to illicit tactics that helped clients avoid the Revenue*, OBSERVER, June 29, 2008, at Business & Media, 4, *available at* http://www.guardian.co.uk/business/2008/jun/29/ubs.banking (noting that Birkenfeld confessed to hiding diamonds in tubes of toothpaste and intentionally destroying offshore bank records).

conspiracy to defraud the IRS.[86] The Department of Justice detained the U.S. citizen's Swiss co-conspirator, Martin Liechti, as a "material witness" to the investigation.[87] This enforcement action is unprecedented, representing the first time the United States has initiated criminal charges against a Swiss banker for helping a U.S. taxpayer evade taxes.[88] On June 30, 2008, the United States filed a petition with the U.S. District Court for the Southern District of Florida for permission to "file an IRS administrative summons with UBS asking the bank to disclose the names of all of its U.S. clients who have opened accounts in Switzerland, but for which the bank has not filed forms with the IRS disclosing the Swiss accounts."[89] The Court approved service of the summons and the IRS served the summons in July of 2008.[90] The case ultimately settled, as the U.S. Department of Justice deferred prosecution of UBS in exchange for UBS paying $780 million and agreeing to cease its cross-border business in entities not registered with the Securities and Exchange Commission.[91] As part of the settlement, the

86. *See* Statement of Facts at 1, United States v. Birkenfeld, No. 08-CR-60099-ZLOCH (S.D. Fla. 2008). U.S. District Judge William Zloch ultimately sentenced Birkenfeld to forty months in prison. Kevin McCoy, *U.S. officials indict 2 Swiss citizens in UBS case*, USA TODAY, Aug. 21, 2009, at B1.

87. Sean Farrell, *UBS Plans to Shed 5,500 Jobs Amid Market Turmoil*, INDEP., May 7, 2008, *available at* http://www.independent.co.uk/news/business/news/ubs-plans-to-shed-5500-jobs-amid-market-turmoil-822233.html.

88. Judge Alfred J. Lechner Jr. sentenced John Mathewson, the owner and executive of an offshore bank in the Cayman Islands, to only five years of probation, five hundred hours of community service, and a $30,000 fine because Mathewson's cooperation with tax authorities led to an unequaled number of leniency pleas. *See* Ronald Smothers, *In Plea Deal, Banker Outlines Money Laundering in Caymans*, N.Y. TIMES, Aug. 3, 1999, at A1, *available at* http://www.nytimes.com/1999/08/03/us/in-plea-deal-a-banker-outlines-money-laundering-in-caymans.html.

89. *Ex Parte* Petition for Leave to Serve "John Doe" Summons at 1, Case No. 08-21864-MC-LENARD/GARBER (S.D. Fla. June 30, 2008) (asking UBS for the names of U.S. clients for whom UBS "(1) did not have in its possession Forms W-9 executed by such United States taxpayers, and (2) had not filed timely and accurate Forms 1099 naming such United States taxpayers and reporting to United States taxing authorities all reportable payments made to such United States taxpayers."). This petition for leave to serve summons is authorized under 26 U.S.C. § 7609(f), which requires court approval for an IRS administrative summons that does not identify that taxpayer's name under investigation. *See* STAFF OF S. PERMANENT SUBCOMM. ON INVESTIGATIONS, *supra* note 81 at 3.

90. *See* Carrick Mollenkamp, *Behind UBS Case, A Dogged IRS: For Messrs. McDougal and Reeves, 'It's Just a Matter of Detective Work'*, WALL ST. J., July 14, 2009, at C1.

91. Press Release, UBS, UBS Settles US Cross-Border Case with the US Department of Justice (DOJ) and the Securities and Exchange Commission (SEC) (Feb. 18, 2009), http://www.ubs.com/1/e/about/newsalert?newsId=162297.

Swiss government agreed to give the names of 4,450 U.S. citizens suspected of using secret Swiss accounts at UBS to evade taxes.[92] The summons was the first attempt by the United States to "pierce Swiss bank secrecy by compelling a Swiss bank to name its U.S. clients."[93]

III. U.S. LEGISLATIVE INITIATIVE: THE STOP TAX HAVEN ABUSE ACT

In 2007 Senators Barack Obama (D) of Illinois, Carl Levin (D) of Michigan, and Norm Coleman (R) of Minnesota sponsored the Stop Tax Haven Abuse Act,[94] but the legislation languished in committee.[95] Some analysts cite the political power of big commercial banks, such as Citigroup, as the reason why the United States has not previously clamped down on U.S. banks that do business with foreign banks that have neither a physical presence in the United States, nor a connection to regulated banks.[96] Lawmakers may decide whether to enact the Stop Tax Haven Abuse Act or similar legislation as early as the 2009-2010 legislative session.[97] Legislators might also find it politically difficult to oppose legislation that could raise billions of dollars in government revenues by stymieing efforts geared

92. *See* Graham Bowley, *From the Global Financial Crisis, A Push by Counties to Repatriate Cash; Broad Political Trend Underlies UBS Decision to Release Clients' Names*, INT'L HERALD TRIB., Aug. 24, 2009, at 15 (noting that although the settlement is a victory for the United States, "[t]he actual process of recovering the names may become lost in bureaucracy and foot-dragging" and "smaller Swiss banks . . . are confident that they can continue to profit by finding new ways to protect the privacy of their clients . . . ."). *But see* Lynnley Browning, *U.S. Indicts Two in Switzerland on Tax Charges*, N.Y. TIMES, Aug. 22, 2009, at B1 (highlighting that the Justice Department's indictment of Hansruedi Schmacher, a director at NZB Neue Zurcher Bank of Zurich, and Matthias W. Rickenbach, a Swiss lawyer, for conspiring to defraud the United States, signaled that Justice would pursue "smaller players" including professionals who assist individual account holders).

93. STAFF OF S. PERMANENT SUBCOMM. ON INVESTIGATIONS, *supra* note 81 at 3.

94. Stop Tax Haven Abuse Act, S. 681, 110th Cong. (2007).

95. *See* Govtrack.us: A Civic Project to Track Congress, H.R. 2136: Stop Tax Haven Abuse Act, http://www.govtrack.us/congress/bill.xpd?bill=h110-2136 (last visited Nov. 1, 2009).

96. *See* LUCY KOMISAR, TAX JUSTICE NETWORK, CITIGROUP: A CULTURE AND HISTORY OF TAX EVASION (2006), http://www.taxjustice.net/cms/upload/pdf/Citigroup_-_a_culture_and_history_of_tax_evasion.pdf (discussing Citigroup's long history of using offshore shelters to help clients evade taxes).

97. *See* Jackie Calmes & Edmund L. Andrews, *Obama Asks Curb on Use of Havens to Reduce Taxes*, N.Y. TIMES, May 5, 2009, at A1 (noting that the Obama proposal riled powerful business interests).

toward illegal tax evasion.[98] "With the worsening U.S. budget and deficit situation, increased pressure exists . . . to enhance tax enforcement . . . against persons who intentionally deposit income in offshore jurisdictions" making "increased international tax enforcement a likely priority that will receive increased resources and political focus."[99] Passage of the Act may be part of a concerted global effort to crack down on tax havens that "play host to many non-regulated hedge funds that were partly blamed for the global financial crisis."[100] After governments bailed out banks to stave off the global financial crisis, many politicians wonder why some financial institutions are still conducting transactions in countries considered tax havens.[101] Finally, the fact that President Obama was one of the sponsors of the 2007 Stop Tax Haven Abuse Act has fueled speculation that the 2009 Act will pass.[102]

98. *See* Francis, *supra* note 33 ("If the nation's economic woes continue, lawmakers will probably have a more difficult time opposing legislation that could raise billions . . . ."); *see also* Jay Krause & Christopher McLemore, *Pennies from Havens: Obama Pledges Crackdown on Offshore Banking Jurisdictions*, WITHERS LLP, Jan. 21, 2009, *available at* http://www.withersworldwide.com/news-publications/455/pennies-from-havens-obama-pledges-crackdown-on-offshore-banking-jurisdictions.aspx (explaining that President Obama has not indicated he would back down from such a measure despite the sorry state of the economy; highlighting that Congress recently enacted an exit tax on individuals who expatriate, demonstrating a willingness to target this source of revenue; and noting that such an Act might be useful in raising revenue to fund portions of the economic stimulus package).

99. Bruce Zagaris, *Swiss Government Reportedly Will Give U.S. Names of UBS Depositors*, 24 INT'L ENFORCEMENT L. REP., Dec. 2008, at 12.

100. *Tax Havens Face Blacklist Pressure—Global Financial Crisis*, THE AUSTRALIAN, Oct. 22, 2008, at 32.

101. French President Nicolas Sarkozy, for example, questioned, "Is it normal that a bank to which we [France] guarantee loans or allocate our own funds continues operating in tax havens?" President Sarkozy, answering his own question, said, "The answer is no." *Id.*; *see also* Lucia Kubosova, *EU States Crack Down on Tax Evasion*, EUOBSERVER.COM, Oct. 22, 2008, http://euobserver.com/9/26976 ("German finance minister Peer Steinbruck insisted . . . 'Switzerland offers conditions that prompt German taxpayers to evade taxes . . . .'"); Emma Thomasson & Saeed Azhar, *Offshore Under Scrutiny but Secrecy to Survive*, HEDGEWORLD DAILY NEWS, Oct. 15, 2008, *available at* http://www.reuters.com/article/WealthManagement08/idUSTRE49E41S20081015 (noting how the financial crisis will increase the pressure on tax havens because government officials will have to finance large rescue packages and politicians have "decided pursuing offshore centers was politically popular.").

102. *See* Gavin Hinks, *US Launches New Stop Tax Haven Abuse Act: Senator Carl Levin Proposes New Act Claiming Tax Havens Are Engaged in 'Economic Warfare' with US*, ACCOUNTANCY AGE, Mar. 4, 2009, http://www.accountancyage.com/accountancyage/news/2237713/launches-stop-tax-haven-abuse (noting that speculation has begun that the Act will become law now

When Sen. Levin offered testimony in support of the bill, he cited "tax abuses that rob the U.S. treasury of an estimated $100 billion each year, reward tax dodgers using offshore secrecy laws to hide money . . . and offload the tax burden onto the backs of middle income families" as the reasons why Congress should pass the Act.[103] According to Levin, the Act would give the government "powerful tools to end offshore tax haven . . . abuses" and that "[w]ith the financial crisis facing our country today and the long list of expenses we're incurring to try to end that crisis . . . it is long past time for Congress to stop tax cheats . . . ."[104] Such motivation is understandable in light of the fact that the United States has a national debt of greater than $10 trillion[105] and pays almost $500 billion annually in interest on that debt.[106] An objective observer, regardless of her feelings about the fairness of the tax code, might have difficulty siding with tax evaders rather than taxpayers. Before examining the tools the Act gives tax authorities to decrease the incidence of tax evasion, it is useful to examine the current methods by which the IRS enforces U.S. tax policy.

A. THE CURRENT METHODS OF TAX ENFORCEMENT

The IRS generally expects a U.S. taxpayer to voluntarily report all of her income.[107] Nevertheless, if a taxpayer conducts a transaction within the United States, the IRS has methods to procure some information regardless of taxpayer reporting. For example, a U.S. payor or broker must report numerous types of payments, e.g., interest, wages, dividends, and unemployment compensation, to the IRS and the taxpayer.[108] If the taxpayer

that previous bill sponsor Obama is president).

103. Press Release, Senator Carl Levin, *supra* note 76.

104. Press Release, Senator Carl Levin, *supra* note 76, at Part II.

105. Jackie Calmes, *2 Paths, but One Result: Bigger Deficits for U.S.; Analysts Are Critical of Spending Plans; Elections 2008*, INT'L HERALD TRIB., Oct. 30, 2008, at 6.

106. In fiscal year 2006, for example, the U.S. government spent $406 billion in interest on the national debt. U.S. Dep't of Treas. Bureau of the Pub. Debt. Interest Expense on the Debt Outstanding, http://www.treasurydirect.gov/govt/reports/ir/ir_expense.htm (last visited Oct. 2, 2009).

107. *See, e.g.*, Eileen Ambrose, *Canceled Debt May Bring Big Tax Bill from IRS; Amount Forgiven Counts as Income in Many Cases*, CHI. TRIB., May 11, 2008, at C5 (highlighting that the IRS wants and expects people to pay taxes on their income on a "pay-as-you-go basis," including canceled debts worth less than $600 which constitute "other income").

108. *See* I.R.C. §§ 6042 (dividends), 6049 (interest), 6050B (unemployment compensation), 6051 (wages) (2006).

who receives this reported information fails to provide his taxpayer identification number (TIN)[109] to the payor or broker, the IRS requires backup withholding of tax.[110] The IRS may examine relevant books and records to determine a taxpayer's liability and can summon the taxpayer or others to produce such records or give testimony, on penalty of perjury, toward that determination.[111] For example, the IRS may summon a U.S. bank to produce the banking information of an individual the IRS suspects of underreporting her income.[112] Lastly, U.S. banks must report all suspicious banking transactions by filing Suspicious Activity Reports and all currency transactions exceeding $10,000 by filing Currency Transaction Reports.[113] The IRS has access to these reports, can audit bank records, and can sue to impose civil and/or criminal penalties on banks found to be in violation of these reporting requirements.[114]

1. Foreign Enforcement is Difficult

In stark contrast to domestic reporting requirements, IRS reporting obligations generally do not reach foreign payors or brokers.[115] Furthermore, to attract foreign clients, some countries, e.g., Liechtenstein, Singapore, and Switzerland, guarantee client confidentiality and account holdings secrecy.[116]

109. Under penalty of perjury, a U.S. citizen or resident must provide her name, address, and TIN when opening a bank account at a domestic bank. ORG. FOR ECON. CO-OPERATION & DEV., Improving Access to Bank Information for Tax Purposes Appendix I, ¶ 1.5.5.3.1 (2000) [hereinafter OECD BANK REPORT].

110. I.R.C. § 3406(a); *see* Blum, *supra* note 52, at 593 (identifying the means by which the IRS can obtain tax information).

111. I.R.C. § 7602(a)(1)–(3); *see also* Blum, *supra* note 52, at 593.

112. *See* Blum, *supra* note 52, at 593–94 (explaining that U.S. District Courts are "authorized to compel compliance with the summons and to use the contempt power toward this end."). Although the Right to Financial Privacy Act generally safeguards individuals' banking information, there are exceptions for enforcement of I.R.C. provisions, for example, the administrative summons provided in I.R.C. § 7609. *See Id.* at n.49 (citing OECD BANK REPORT).

113. *See* Blum, *supra* note 52, at 594; *see also* OECD BANK REPORT, *supra* note 109, app. I, ¶ 1.4 (citing Reg. § 103.21–22).

114. OECD BANK REPORT, *supra* note 109, Appendix I, ¶ 1.6 (citing 31 U.S.C. §§ 5531 and 5332); *see also* Blum, *supra* note 52, at 594 (explaining that the purpose of such measures is to "protect against money-laundering as well as tax evasion").

115. *See* Reuven S. Avi-Yonah, *Globalization, Tax Competition and the Fiscal Crisis of the Welfare State*, 113 HARV. L. REV. 1573, 1584–85 (2000) (explaining that when neither "withholding at the source or information reporting . . . is available . . . as in the case of foreign income, compliance rates drop dramatically.").

116. *See* Greg Brabec, *The Fight for Transparency: International Pressure to Make Swiss Banking Procedures Less Restrictive*, 21 TEMP. INT'L & COMP. L.J. 231,

In fact, in certain jurisdictions like the Bahamas, where taxes are minimal to nonexistent,[117] the governments may not collect tax information from banks at all. Moreover, some countries might not have the capacity to collect the sophisticated tax information that U.S. tax authorities seek.[118] Regardless of the reason why tax information is unavailable, U.S. tax authorities' requests for information directed to the executives or judiciaries of such countries usually fall on deaf ears.[119] Therefore, bank secrecy jurisdictions have become attractive destinations for illicitly earned monies, funds used for illicit purposes such as money laundering or political corruption, or deposits meant to evade U.S. income reporting requirements.[120] Regardless of whether the source or use of the funds is legitimate, offshore secret accounts shield interest paid on monies held from U.S. tax authorities, and the IRS might find it difficult, if not impossible, to collect taxes based on these sources of funds.[121]

B. THE STOP TAX HAVEN ABUSE ACT'S TREATMENT OF TAX HAVENS

The Stop Tax Haven Abuse Act initially identifies thirty-four offshore secrecy jurisdictions.[122] Most of these jurisdictions are small and some are very small. Anguilla, for example, has a landmass of only ninety-one square kilometers, or about half the size of Washington D.C., and a population numbering 14,436.[123]

232 (2007) (noting that the Swiss take pride in a "highly secure banking system" and have historically touted their banks as places where account holders' identities and holdings are kept secret).

117. *See* Gibson, *supra* note 54.

118. Some developing countries do not have the means to collect tax revenues. It makes sense that countries incapable of collecting taxes would also lack the ability to collect sophisticated tax information. *See* Richard M. Bird & Eric M. Zolt, Introduction to Tax Policy Design and Development 6 (Apr. 2003) (unpublished draft prepared for a course on Practical Issues of Tax Policy in Developing Countries, World Bank, April 28-May 1, 2003), http://www1.worldbank.org/publicsector/LearningProgram/PracticalIssues/papers/introduction%20to%20tax%20policy/WBI%20Module%201(Bird&Zolt)April10.doc ("[G]enerally, the capacity of countries to collect taxes appears to rise as income levels increase.").

119. *See* Blum, *supra* note 52, at 595 (noting that some governments impose penalties on employees who break bank secrecy laws, and that other countries do not have tax treaties with the United States to facilitate information exchange).

120. *Id.* at 596.

121. *See id.* at 596 (noting that even if the source of the funds is legitimate, "it may be impossible for the IRS . . . to collect debts against these assets.").

122. *See* Stop Tax Haven Abuse Act, S. 506, 111th Cong. § 101(b) (2009). The list is based on IRS court filings. GRAVELLE, *supra* note 19, at 3.

123. CENTRAL INTELLIGENCE AGENCY, WORLD FACTBOOK (2008), *available at*

Some of these jurisdictions are relatively rich, such as the Channel Islands (Jersey, Guernsey, Sark, and Alderney),[124] while others are relatively poor.[125] Regardless of their economic status, most of these countries are small in terms of both land and population size, and weak in the arena of international affairs.[126] In other words, they make easy targets.

1. Defining a Tax Haven

The first step to stopping tax haven abuse is to identify tax havens. According to the Act, the term "offshore secrecy jurisdiction" means "any foreign jurisdiction . . . listed by the Secretary [of the Treasury] as an offshore secrecy jurisdiction."[127] Under the Act, the Secretary determines which jurisdictions are offshore secrecy jurisdictions based on the existence of tax secrecy laws that "unreasonably restrict the ability of the United States to obtain information relevant to the enforcement [of the Act], unless the Secretary also determines that such country has effective information exchange practices."[128]

The Act defines secrecy or confidentiality rules and practices as "both formal laws and regulations and informal government or business practices" that inhibit "access of law enforcement and tax administration authorities to beneficial ownership and other financial information."[129] To determine which countries have ineffective information exchange practices,

https://www.cia.gov/library/publications/the-world-factbook/geos/av.html. According to the CIA, per capita GDP at purchasing power parity in 2004 was US$8,800. Anguilla's GDP at purchasing power parity in 2004 was US$108.9 million. *Id.*

124. Jersey is an island in the English Channel, northwest of France. According to the CIA, per capita GDP at purchasing power parity in 2005 was US$57,000. *Id.* at https://www.cia.gov/library/publications/the-world-factbook/geos/je.html.

125. Although Vanuatu is not one of the poorest places in the world, 70% of its population makes its living by subsistence farming. According to the CIA, per capita GDP at purchasing power parity in 2007 was US$4400. *Id.* at https://www.cia.gov/library/publications/the-world-factbook/geos/nh.html.

126. *See generally* Michael Isaacson, *The Tax Haven the OECD Forgot? Harmful Tax Competition? Harmful to Whom? Learn About the Real Agenda Behind OECD's Blacklists of Offshore Tax Havens*, http://www.offshore-fox.com/offshore-corporations/offshore_corporations_0401.html (last visited Oct. 19, 2009) (explaining how politicians target foreign jurisdictions because domestic tax hikes at home are politically unpopular).

127. Stop Tax Haven Abuse Act, S. 506, 111th Cong. § 101(b) (2009) (amending 76 U.S.C. § 7701(a)).

128. *Id.*

129. *Id.*

the Act authorizes the Secretary, on an annual basis, to classify any jurisdiction as an offshore secrecy jurisdiction unless the country: (i) has a treaty or some type of information exchange agreement with the United States; (ii) the exchange of information was adequate in terms of preventing tax evasion or avoidance of U.S. income tax during the 12-month period of review prior to the annual determination; and (iii) such jurisdiction, during the 12-month review period, "was not identified by an intergovernmental group or organization of which the United States is a member as uncooperative with international tax enforcement . . . ."[130] Finally, the Secretary has the authority to add or remove a jurisdiction from the initial list based on whether or not they improve their exchange-of-information practices.[131]

2. *Ambiguous Definitions*

The Act's definition of "tax haven" is ambiguous.[132] While there are standards by which the Secretary must make a determination, there are few concrete criteria by which to make that finding.[133] For example, whether a country has an established tax treaty with the United States is a verifiable criterion. Whether a jurisdiction has rules or practices that unreasonably restrict U.S. access to tax information, however, lies in the eye of the beholder.[134] It is plausible to argue that

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130. *Id.*

131. *Id.*

132. Much of the legal criticism of the Act has focused on the patenting of tax strategies and the implications of the Act for lawyers' professional responsibilities. *See, e.g.*, Max Stul Oppenheimer, *Patents, Taxes, and the Nuclear Option: Do We Need a "Tax Strategy Patent" Ban Treaty?*, 2008 U. ILL. J.L. TECH. & POL'Y 1 (2008); Nicholas Robinson, *Patenting the Tax Code: Monopolizing Basic Tax Strategy*, 5 BUFF. INTELL. PROP. L.J. 50 (2007); Craig E. Groeschel, Comment, *Tax Strategy Patents Considered Harmful*, 8 HOUS. BUS. & TAX L.J. 271 (2008); Stephanie L. Varela, Note, *Damned If You Do, Doomed If You Don't: Patenting Legal Methods and Its Effect on Lawyers' Professional Responsibilities*, 60 FLA. L. REV. 1145 (2008). Instead, I focus on the lack of clarity and equity in the Act's treatment of tax havens.

133. *See* Krause & McLemore, *supra* note 98 (noting the criticism that the initial list of jurisdictions does not differentiate between jurisdictions that do conform to widely accepted international standards, i.e., countries that have recently penned TIEAs with the United States, and those that have not).

134. *See* Rawlings, *supra* note 53, at 3 ("The principles . . . devised by multilateral organisations and offshore financial authorities are subject to divergent interpretations between regulators and regulatees. It is social actors – lawyers, accountants, fund managers, tax compliance regulators – who frame these contests, through their daily deeds and narrated reflections on their practices.").

the mere existence of tax secrecy rules is an objective factor. In that case, Switzerland, famous for its bank secrecy laws,[135] is an obvious choice for the list and does appear as a listed offshore secrecy jurisdiction.[136] Whether those rules "unreasonably restrict the ability of the United States to obtain information relevant to . . . enforcement,"[137] however, is another matter.

The Act does not define what constitutes a reasonable restriction on the exchange of tax information. In that way, it seems discretionary—one might say arbitrary—whether the Secretary believes a country's bank secrecy provisions unduly restrict U.S. tax authorities' ability to obtain the necessary tax information. Additionally, it is unclear how the Secretary would determine whether the bank secrecy laws or some other factor prevented U.S. tax authorities from making use of relevant information to enforce U.S. income tax. For example, Swiss bank UBS told Senate investigators that approximately 20,000 U.S. clients have about $18 billion in deposits in UBS Switzerland.[138] In the summer of 2008, a federal court granted the IRS permission to pierce Swiss bank secrecy laws and demand the identities of 19,000 American clients who "failed to disclose their Swiss-based accounts on U.S. tax returns."[139] If UBS readily defied Swiss bank secrecy laws, did those tax secrecy rules unreasonably restrict IRS access to relevant tax information? Assume UBS agreed to circumvent Swiss bank secrecy laws contingent on a U.S. federal court granting the IRS permission to attempt to pierce bank secrecy laws.[140] If the federal court had not granted the IRS leave to seek the identities of U.S. citizens with accounts in UBS, was it the Swiss tax secrecy laws or the federal court order that restricted U.S. tax authority access to the necessary tax information? Assume that UBS disclosed the identities of the 19,000 individuals who failed to comply with the U.S. reporting requirement, but that the IRS could not handle that volume of tax evaders.[141] Under the Act, this might be a sufficient reason

135. *See* Brabec, *supra* note 116, at 231; Hilzenrath, *supra* note 7.

136. *See* Stop Tax Haven Abuse Act, S. 506, 111th Cong. §101(a)(1) (2009).

137. *Id.*

138. Hilzenrath, *supra* note 7, at D3.

139. *Id.* at D3.

140. *See* Evan Perez, *Guilty Plea by Ex-Banker Likely to Aid Probe of UBS*, WALL ST. J., June 20, 2008, at C1 (stating that prosecutors in the Birkenfield case sought to delay sentencing while they attempted to use Birkenfield's knowledge to "pierce the centuries-old secrecy for which UBS and other Swiss banks are known.").

141. Martin Lobel, Chairman of the Tax Analysts Information Service, argued

to label a foreign jurisdiction a tax secrecy haven.

3. Who the Act Does Not Include—Countries Operating Preferential Tax Regimes

Some jurisdictions not on the Act's initial list, such as the United States, have higher than nominal income taxes, but exempt some forms of income from those taxes as part of a preferential tax regime.[142] In fact, "no major capital-importing country has been able to impose such a tax [on interest paid to foreigners] for fear of driving mobile capital elsewhere. . . ."[143] For that reason, most countries are tax havens. That is, individuals intentionally route transactions through foreign countries because of the savings earned by avoiding taxes on interest.[144] In practice, this means that the Act cannot completely solve the erosion of the U.S. tax base because it only targets countries with bank secrecy laws, rather than countries that operate preferential tax regimes. Because the Act would subject jurisdictions on the list to heightened scrutiny and potential sanctions, it seems hypocritical and inequitable to target tax secrecy jurisdictions, and not countries that operate successful tax preferential regimes.[145] Such hypocrisy could weaken foreign actors' resolve to comply.[146] The absence of

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that the IRS could not handle that many tax evaders. A former federal prosecutor turned tax defense specialist, Edward M. Robbins Jr., countered that the Justice Department, separate from the civil lawyers working for the IRS, could handle such a caseload. *See* Hilzenrath, *supra* note 7, at D01.

142. *See* Avi-Yonah, *supra* note 115, at 1576. As of 1984, the United States exempts taxes on interest paid to non-residents.

143. *Id.* at 1576.

144. *See* Littlewood, *supra* note 59, at 460 ("individuals and firms routinely conduct transactions through such jurisdictions for no other purpose than to escape taxes . . . .").

145. For example, China operates a very successful tax preferential regime. *See* Tola Adewola, *China Approves Bill to End Preferential Tax Treatment for Foreign Companies*, ILL. BUS. L.J., (March 27, 2007), *available at* http://iblsjournal.typepad.com/illinois_business_law_soc/2007/03/will_chinas_new.html. Domestic Chinese companies pay a statutory income tax rate of 33%, but foreign companies, such as foreign service companies, qualify for preferential rates of income tax of 15% or 24%. China enacted a new enterprise income tax law (EIT), effective January 1, 2008, that largely ended preferential tax treatment for foreign companies operating in China. Significantly, however, two categories of companies—foreign high-tech and other important industries, and foreign companies with small profits—still pay preferential income taxes. *Id.*

146. *See generally* Shelter Offshore, *In Support of Offshore Tax Havens*, Nov. 3, 2008, http://www.shelteroffshore.com/index.php/offshore/more/in-support-of-offshore-tax-havens-10147/ (arguing that entities like the OECD and U.N. "make veiled

countries operating preferential tax regimes from the Act's initial list makes sense politically. It is much easier to take on the likes of Vanuatu than China.[147]

4. Musical Havens—The "Shift" Argument

Because of the inherent lag in listing countries as offshore secrecy jurisdictions—the Act specifies a 12-month period preceding the annual determination—the Act is more likely to shift tax evasion to untargeted tax havens rather than eliminate targeted jurisdictions. A country not on the initial list, Liberia for example,[148] might advertise itself as protecting account holders' identities and holding amounts by offering client confidentiality guarantees. During the 12-month lag period, that country is likely to win business that might otherwise have gone to targeted foreign secrecy jurisdictions.[149] This argument may seem like a stretch because the burden of transferring funds or transfer-driven scrutiny would deter shifting funds in the manner described.[150] However, in an era in which it is easier than ever to transfer funds from one jurisdiction to another, unless all tax havens cease to exist at once, the specter of musical havens is a real one.[151]

claims" that tax shelters are corrupt, "yet, there is so much hypocrisy in what many of these entities and bodies say and actually do . . . .").

147. In 2000, the OECD Committee on Fiscal Affairs requested each OECD-member country to self-identify aspects of its tax regime that would constitute a preferential tax regime according to OECD standards for such a regime. The results, perhaps not surprisingly, showed that Australia, Belgium, Canada, Finland, France, Germany, Greece, Hungary, Iceland, Ireland, Italy, Korea, Luxembourg, the Netherlands, Norway, Portugal, Spain, Sweden, Switzerland, Turkey, and the United States all operated a preferential tax regime. OECD, 2000, *supra* note 59, ¶ 5, 11; Littlewood, *supra* note 59, at 428. From this OECD list, generated in 2000, only Switzerland and Luxembourg appear on the Act's initial list of foreign secrecy jurisdictions. Stop Tax Haven Abuse Act, S. 506, 111th Cong. § 101(b) (2009). As long as countries continue to maintain preferential tax regimes, the absence of those countries from the Act guarantees that the U.S. tax base will continue to erode.

148. In 2000, the OECD identified Liberia as a tax haven. OECD, 2000, *supra* note 59, ¶ 17.

149. *See* Littlewood, *supra* note 59, at 463 (noting that if one tax haven is eliminated, "the surviving havens will win business that would have gone through those havens that have been shut down.").

150. *See* Nick Cohen, *At Least Germany Stamps on Tax Havens*, OBSERVER, Feb. 24, 2008, at Comment & Debate, 38, *available at* http://www.guardian.co.uk/commentisfree/2008/feb/24/germany.globaleconomy (noting the increasing global focus in cracking down on tax havens).

151. *See* David Cay Johnston, *Musical Chairs on Tax Havens: Now It's Ireland*, N.Y. TIMES, Aug. 3, 2002, at C1 (highlighting companies that shifted funds to tax-

5. Failing to Account for Other Countries' Interests

The Act will fail to eliminate tax havens for the simple reason that it fails to account for other nations' interests. In terms of taxation, putting U.S. citizens first might not be objectionable.[152] Consider, however, the reasons why a country might enact strict bank secrecy laws or allow transactions that other countries' tax authorities would consider objectionable or suspicious. One underlying rationale is survival. For example, Nauru, a small island in the South Pacific Ocean, has a total area of 21.3 square kilometers (8.2 square miles), and is the world's smallest independent republic.[153] Rich phosphate deposits are the country's main economic resource, but because of mining and the depletion of this resource, the country's per capita GDP is declining.[154] Given the country's size and declining resources, one incentive to operate as an offshore secrecy jurisdiction might be the lack of available alternatives for economic growth.[155] Even countries that do have available alternatives, Singapore for example, lack an economic incentive to comply with the U.S. law.[156] Singapore has said it will not budge, despite pressure to undo its strict bank secrecy provisions, presumably because those provisions are precisely

friendly Ireland following legislative crackdowns on Bermuda).

152. *See* Graetz, *supra* note 44, at 1371–72 (explaining that historically, "the power to tax is rarely delegated to multinational organizations," and "we [U.S. citizens] regard our obligation for the well-being of our fellow citizens as more pressing than for people in need elsewhere in the world."). *But see* Allison Christians, *Sovereignty, Taxation and Social Contract*, 18 MINN. J. INT'L LAW 99, 99 ("[T]his view of sovereign autonomy over taxation is increasingly inconsistent with . . . . global economic reality. . . . Major theoretical developments in tax policy are now arising not through solely national political and legal processes but through the interactions of nongovernmental actors in transnational settings.").

153. REPUBLIC OF NAURU: PERMANENT MISSION TO THE UNITED NATIONS, NAURU COUNTRY PROFILE, http://www.un.int/nauru/countryprofile.html (last visited Oct. 2, 2009).

154. *See* UNITED NATIONS, NAURU, http://www.un.int/nauru/nauru.pdf (last visited Oct. 2, 2009).

155. *See* Anthony B. van Fossen, *Money Laundering, Global Financial Instability, and Tax Havens in the Pacific Islands*, CONTEMP. PAC., Fall 2003, at 237 (explaining that multilateral attempts to exclude Pacific Islands from the international financial system has those jurisdictions "battling for their survival"). One can surmise that those countries would not risk such severe consequences without equally strong motivations.

156. *See* Yesim Yilmaz, *Tax Havens, Tax Competition and Economic Performance*, 6 PROSPERITAS issue III (2006), at 1 n.2, *available at* http://www.freedomandprosperity.org/Papers/taxhavens/taxhavens.pdf (noting how countries like Singapore are in direct competition with the United States for investment from the United States and other countries).

what lure international financial investors.[157] The Boston Consulting Group predicted offshore assets will reach $8.8 trillion by 2012, giving foreign banks a strong financial incentive not to cooperate with U.S. tax authorities.[158]

IV. ALTERNATIVES THAT CONSIDER OTHER COUNTRIES' INTERESTS

The problem is not that the Act puts U.S. interests first.[159] Rather, the problem is that although the United States is dependent on other countries for tax information in order for the IRS to enforce U.S. tax policies,[160] the Act does not consider other countries' interests in promoting bank secrecy.[161] The U.S. motivation is obvious. When other countries hold themselves out as tax shelters and guarantee bank secrecy, U.S. taxpayers cheat on their tax returns.[162] This decreases the U.S. tax base by depleting financial resources that the government can use to support its initiatives.[163]

Motivation for a country like Nauru is relatively simple as well. Because Nauru's resources are declining, one source of economic security is the foreign investment attracted by the country's bank secrecy laws.[164] Alternatives that consider others' economic interests—while not necessarily requiring the subordination of U.S. interests—are a policy that trades cash for tax information and an international tax organization with domestic enforcement powers.

157. *See* Thomasson & Azhar, *supra* note 101, at 1 ("Singapore says it will not budge on its tough bank secrecy laws despite EU demands . . . .").

158. *See* Thomasson & Azhar, *supra* note 101, at 1 ("The Boston Consulting Group has forecast total offshore assets under management will climb to $8.8 trillion by 2012 from $7.3 trillion in 2007 . . . .").

159. *See* Graetz, *supra* note 44, at 1371–72 (arguing that it is natural, both historically and politically, for policy makers to give primacy to U.S. citizens' interests in national policy, including tax policy).

160. *See* Tillinghast, *supra* note 25, at 39.

161. *See supra* Part III.B.5.

162. *See* David Cay Johnston, *Tax Cheats Called Out of Control*, N.Y. TIMES, Aug. 1, 2006, at C1 (giving examples of U.S. citizens who cheat on their taxes, such as Robert Wood Johnson IV, the owner of the New York Jets, and Charles and Sam Wyly, founders of the Center for Public Integrity).

163. *See id.* (proving examples of what governments might use tax revenues for, e.g., infrastructure or providing for the needy).

164. *See* Van Fossen, *supra* note 155, at 237.

A. CASH FOR TAX INFORMATION

If the United States were to purchase tax information, the goal would not be to collect as much information as possible, but to collect only the smallest amount of information necessary to enforce tax laws.[165] Once the United States identified a jurisdiction from which it needed tax information, that jurisdiction's willingness and ability to provide the necessary tax information would become an issue of price negotiation.[166] The final price might include compensation necessary to repay private parties and "to offset the burdens imposed" on foreign governmental actors.[167] This market system of tax information acquisition takes into account another country's non-reciprocal need for tax information or its inability to gather such information. If the U.S. paid less for such information than the amount of tax revenue that information would produce, the system would account for all parties' interests. By doing so, a net importer of tax information, such as the United States, could acquire extraterritorial tax information from a country with relatively small amounts of collected tax information, such as the Bahamas.[168]

The current method of bilateral exchange—trading tax information for tax information—remains fundamentally unchanged since before World War II and is outdated.[169] Rather than using sanctions to force countries into compliance as the Stop Tax Haven Abuse Act would do, the United States might allow the use of cash as consideration for specific tax information.[170] This would allow an importer of tax information

165. The IRS has previously limited the amount of tax information collected. *See* Dorothy A. Brown, *Race and Class Matters in Tax Policy*, 107 COLUM. L. REV. 790, 807 (2007) (noting the end of IRS "general audits" according to the Taxpayer Compliance Measurement Program).

166. *See* Dean, *supra* note 9, at 659 ("[T]he United States could negotiate with the governments of those jurisdictions the specific nature of the information . . . as well as regarding the price at which it would be willing and able to provide it.").

167. *See id.* at 659–60.

168. *See id.* at 611 (noting that a more complete market would allow a country to "maximize its utility and to minimize its impact on privacy" even if they collected little or no information."); *see also* Gibson, *supra* note 54 (stating that the Bahamas does not levy taxes on "capital gains, corporate earnings, personal income, sales, inheritance, or dividends.").

169. *See* Dean, *supra* note 9, at 611 (highlighting for example, that net tax information importers, such as the United States, could acquire specific tax information, rather than import homogenized information en masse, which is less useful and more invasive).

170. *See* Dean, *supra* note 9, at 611.

to acquire tax information ex post, thereby decreasing the privacy concerns associated with the shipment of tax data.[171]

However, the possibility of market failure still exists in this cash-for-information system. For example, the fair price for information might exceed the revenues generated by the acquisition of information or a bilateral monopoly might prevent a more complete market.[172] Even though a purchaser of tax information would acquire tailored information making privacy less of a concern, a nonmarket solution might provide more robust privacy protections than a market alternative.[173] A governmental alternative might avoid market failures.

B. A NEW MULTILATERAL INSTITUTION

Because leaders have political and financial incentives to act in nationally self-interested ways, a transnational body with domestic tax authority could overcome the problem of extraterritorial tax information acquisition.[174] Such a transnational actor would need to have powers on par with the domestic capabilities of national tax authorities, which would impinge on traditional notions of national sovereignty.[175]

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171. With the increasing advent of identity theft and hackers, the case for limiting the information sent to the IRS is strong. *See* ROBERT F. DACEY, GOVERNMENT ACCOUNTABILITY OFFICE, REPORT TO THE SUBCOMMITTEE ON TECHNOLOGY, INFORMATION POLICY, INTERGOVERNMENTAL RELATIONS, AND THE CENSUS: INFORMATION SECURITY: PROGRESS MADE, BUT WEAKNESSES AT THE INTERNAL REVENUE SERVICE CONTINUE TO POSE RISKS (2003), *reprinted in* TAX ANALYSTS, 2003 TAX NOTES TODAY 106-12 at 6–7 (2003); *see generally* Peter P. Swire, *Financial Privacy and the Theory of High-Tech Government Surveillance*, 77 WASH. U. L.Q. 461, 497 (1999) ("The possibility of intrusions . . . is a powerful argument against allowing unlimited government access to sensitive personal information of any kind."). There is also the risk that an IRS employee might conduct an unauthorized search of an individual's tax information. *See* Andrea Coombes, *IRS Employee Sentenced for Snooping: Tax Man Eyes Tax Records of Almost 200 Celebrities, Including Kevin Bacon*, MARKETWATCH, Aug. 20, 2008, http://www.marketwatch.com/news/story/irs-worker-snooped-tax-records/story.aspx?guid={786BACBD-C58F-481B-AE31-28C2101E7CF6}&dist=msr_1.

172. *See* RICHARD A. POSNER, ECONOMIC ANALYSIS OF LAW § 3.8, at 62 (6th ed. 2003) (noting that a bilateral monopoly occurs and causes high transaction costs when neither party has a beneficial alternative to "dealing with the other").

173. *See generally* Peter P. Swire, *Trustwrap: The Importance of Legal Rules to Electronic Commerce and Internet Privacy*, 54 HASTINGS L.J. 847, 860–73 (2003) (discussing the importance of privacy protection in the Internet era).

174. *See, e.g.*, Vito Tanzi, *Globalization and the Work of Fiscal Termites*, 38 FIN. & DEV. 1, Mar. 1, 2008, http://www.imf.org/external/pubs/ft/fandd/2001/03/tanzi.htm (noting the distant, and more utopian, possibility of a world tax organization that would facilitate the international collection and distribution of tax revenues).

175. *See* Ronen Palan, *Tax Havens and the Commercialization of State*

Recently, two existing international organizations, the United Nations and the OECD, have vied for leadership of a new global tax authority.[176] Both the United Nations and the OECD are capitalizing on their history of work aimed at increasing international tax cooperation.[177] In theory, either organization could fill the gaps generated by the current patchwork system of bilateral tax treaties and avoid the inequity of the multilateral conventions on tax information acquisition. In practice, however, the reality is much different.

The OECD's exclusive membership fuels non-members' perceptions of discrimination in the development of international tax rules.[178] This generates a perception of illegitimacy whereby large powerful countries dominate smaller, weaker ones in the realm of tax policy and enforcement.[179] Although the OECD might have more power than the United Nations to enforce an international tax regime, it lacks the necessary international legitimacy because of its membership makeup, which includes historically powerful nations, such as the United States, France, Germany, Portugal, Spain, Italy, Japan, and the United Kingdom.[180] While the United Nations might have greater international credibility as a fair arbiter of

Sovereignty, 56 INT'L ORG. 151, 173 (2002) (noting that such an organization might spell the end of the traditional Westphalian system of sovereignty).

176. Dean, *supra* note 9, at 661–62.

177. *See, e.g.*, U.N. Dep't of Int'l Econ. & Soc. Affairs, *U.N. Model Double Taxation Convention Between Developed and Developing Countries*, U.N. Doc. No. ST/ESA/102 (1980), *reprinted in* STANLEY S. SURREY, *United Nations Model Convention for Tax Treaties Between Developed and Developing Countries: A Description and Analysis*, in 5 HARV. L.SCH. INT'L TAX PROGRAM & INT'L BUREAU OF FISCAL DOCUMENTATION, SELECTED MONOGRAPHS ON TAXATION 87-113 (1980).

178. *See* Arthur J. Cockfield, *The Rise of the OECD as Informal "World Tax Organization" Through National Responses to E-Commerce Tax Challenges*, 8 YALE J.L. & TECH. 136, 185–86 (2006) (arguing that extending OECD membership to different countries will "help to allay concerns that the OECD has been 'captured' by multinational firms based in OECD countries" and noting that "the perceived influence of these firms may be reducing the legitimacy and effectiveness of OECD reform efforts."); Littlewood, *supra* note 59, at 480–85 (describing pitfalls to OECD reform efforts, including the fact that the membership is not viewed as representative of the entire world).

179. *See* Alexander Townsend, Jr., Comment, *The Global Schoolyard Bully: The Organisation for Economic Co-Operation and Development's Coercive Efforts to Control Tax Competition*, 25 FORDHAM INT'L L.J. 215, 251–58 (2001) (arguing that the 1998 and 2000 OECD reports "mark a coercive and intrusive solution that deviates from traditional fiscal remedies.").

180. Dean, *supra* note 9, at n.370; *see also* Littlewood, *supra* note 59, at 480–85. For a list of OECD member nations, see Org. for Econ. Co-operation & Dev., Ratification of the Convention on the OECD, http://www.sb05.com/OECDJ.html (last visited Nov. 2, 2009).

international tax controversies,[181] it lacks sufficient power to be a transnational tax enforcer.[182] Countries, especially the United States, might resist the necessary curtailment of sovereignty for international tax enforcement.[183] Realizing its incentives to resist U.N. enforcement authority, the United States might recognize other countries' similar incentives to work against the successful enforcement of a U.S. dominated multilateral tax regime such as the OECD. Thus, tax evasion is a global problem requiring a global solution.[184]

V. CONCLUSION

Globalization, the September 11th attacks, and two recent scandals have put tax havens in the legislative crosshairs. The Obama Administration fully supports the Stop Tax Haven Abuse Act.[185] Because of President Obama's unqualified support, the political popularity of cracking down on tax evaders in tough economic times, and banks' decreasing ability to fight against such measures, the Act is likely to pass. The centerpiece of the Act is a list of offshore secrecy jurisdictions. Although some of the motives behind enacting such legislation are laudable and some of the Act's provisions are commendable, the Act is unlikely to garner cooperation from countries vital to its success. The Act fails to account for other countries' economic interests. Although alternatives are not perfect, they are preferable. A market solution, such as allowing the United

181. *See* U.N. Ad Hoc Group of Experts on Int'l Cooperation in Tax Matters, *Institutional Framework for International Tax Cooperation*, ¶¶ 5–10, at 4–5, U.N. Doc. ST/SG/AC.8/2003/L.6 (Aug. 19, 2003), *available at* http://daccessdds.un.org/doc/UNDOC/LTD/NO3/481/35/PDF/NO348135.pdf?OpenElement ("The United Nations has recognized for some time the need to give the developing and transitional countries a voice in the formulation of international tax norms.").

182. *See* Oona A. Hathaway, *Between Power and Principle: An Integrated Theory of International Law*, 72 U. CHI. L. REV. 469, 506 (2005) (noting the weakness of the United Nations' ability to enforce compliance).

183. *See, e.g.*, Daniel Mitchell, *U.N. Tax Police Potential*, WASH. TIMES, Feb. 7, 2002, at A18 (expressing concern that a U.N.-led international tax organization would be costly to the United States).

184. *See* Palan, *supra* note 175, at 173 ("[A]ny serious attempt to combat the tax havens phenomenon would have to be conducted on a multilateral level."); *see also* MICHIEL VAN DIJK & FRANCIS WEYZIG, THE GLOBAL PROBLEM OF TAX HAVENS: THE CASE OF THE NETHERLANDS 3 (Stichting Onderzoek Multinationale Ondernemingen [Centre for Research on Multinational Corporations] 2008) (2007) (arguing that the Netherlands must end harmful tax policies but that the tax haven problem requires a global solution).

185. Drawbaugh & Daly, *supra* note 3.

States to purchase tax information from other countries, or an intergovernmental solution, such as a World Tax Organization, would facilitate a greater exchange of extraterritorial tax information and bolster the enforcement of U.S. tax laws.