

2020

## On the Effort to Discover and Eliminate Offshore Tax Abuse

Christian Hodgson

Follow this and additional works at: <https://scholarship.law.missouri.edu/betr>



Part of the [Law Commons](#)

---

### Recommended Citation

Christian Hodgson, *On the Effort to Discover and Eliminate Offshore Tax Abuse*, 4 BUS. ENTREPRENEURSHIP & TAX L. REV. 170 (2020).

Available at: <https://scholarship.law.missouri.edu/betr/vol4/iss1/22>

This Comment is brought to you for free and open access by the Law Journals at University of Missouri School of Law Scholarship Repository. It has been accepted for inclusion in The Business, Entrepreneurship & Tax Law Review by an authorized editor of University of Missouri School of Law Scholarship Repository. For more information, please contact [bassettcw@missouri.edu](mailto:bassettcw@missouri.edu).

# On the Effort to Discover and Eliminate Offshore Tax Abuse

*Christian Hodgson\**

## ABSTRACT

The practice of tax evasion includes dumping money into secretive offshore accounts to shield financial assets from discovery. U.S. taxpayers have used jurisdictions with low tax rates and secretive banking practices to store unreported financial assets. If the taxpayer chose not to report foreign assets, the existence of these accounts often remained undetected by the U.S. The uncollected taxes from these accounts was a justification for congressional action. The ability of the wealthy to take advantage of tax evasion and avoidance could be contributing to wealth inequality.

The congressional response to offshore tax evasion includes the Bank Secrecy Act of 1970 and the Foreign Account Tax Compliance Act (“FATCA”) of 2010. These laws provide for penalties to a U.S. Taxpayer who does not report his foreign transactions, tools for discovering unreported assets. The 2010 law has had an impact on discovering these hidden accounts and immediately preceded the large media publication of the “Panama Papers,” which exposed the inner workings of how these offshore tax shelter can work. Finally, this article discusses possible measures that could further the current government effort to collect revenue from U.S. taxpayer’s offshore assets.

---

\* Christian Hodgson is a second-year student at the University of Missouri School of Law. He interned with the Supreme Court of Missouri and studied comparative law at the University of Western Cape in Cape Town, South Africa. Prior to entering Law School, he was a Sensor Operator and Flight Instructor in the U.S. Air Force. Christian Hodgson has a B.A. in Political Science and a B.A. in International Studies from the University of Missouri School of Arts and Science.

## I. INTRODUCTION

Income inequality is rising in the United States.<sup>1</sup> In just the first decade of the 21st century, the top 10% of earners in America took in about 50% of income.<sup>2</sup> This is a steep increase from the 1970s, when the top 10% took in 35% of income.<sup>3</sup> Governments try to fight income inequality through progressive taxation schemes and government spending,<sup>4</sup> but anti-poverty programs are costly and chronically underfunded.<sup>5</sup> There are numerous and complex causes for inequality,<sup>6</sup> but one major contributing factor for the growing concentration of wealth is the ability of those on the top to evade taxes.<sup>7</sup>

The ability of wealthy citizens to avoid taxes is treated as a fact of life. States lower taxes to attract investment, but increasing taxes raises the specter of capital flight.<sup>8</sup> U.S. states and foreign countries sometimes engage in a race to the bottom in terms of tax rates, in hopes of attracting capital;<sup>9</sup> if the tax rates in the U.S. are low enough, the thinking goes, the U.S. will be a more attractive location for parking capital.<sup>10</sup> The problem with this solution is that some jurisdictions do not tax income at all,<sup>11</sup> and are instead content to benefit from the wealth management positions created in their jurisdiction.<sup>12</sup> It is obviously difficult for the U.S. to compete with such low tax rates. In the past, noble classes were exempt from paying taxes, and it is possible that taxation is headed toward that pattern again.<sup>13</sup>

Since the 1950s, the tax burden on the richest 400 households in American has been on a downward trajectory, with their overall tax rate going from 70% in 1950 to 23% in 2018.<sup>14</sup> The high tax rate on the wealthiest individuals in America during the mid-20th century looks like an exception to the century's history.<sup>15</sup> Taxes on

1. THOMAS PIKETTY, *CAPITAL IN TWENTY-FIRST CENTURY* 24 (2014).

2. *Id.*

3. *Id.*

4. Kay Bell, *Jobs bill includes tax changes*, MSN (March 23, 2010) (In 2010 Congress passed the HIRE act, which included FATCA was a revenue raising plan, and included a payroll tax waiver for hiring unemployed worker as a job creation plan) <https://web.archive.org/web/20120507222929/http://money.msn.com/tax-tips/post.aspx?post=00000065-0000-0000-a34f-1a0000000000>.

5. Jordan Weissmann, *The Failure of Welfare Reform*, SLATE, (June 1, 2016) <https://slate.com/news-and-politics/2016/06/how-welfare-reform-failed.html>.

6. Steven J. Markovick, *The Income Inequality Debate*, COUNCIL ON FOREIGN RELATIONS, (Feb. 3, 2014) <https://www.cfr.org/background/income-inequality-debate>.

7. Helena Kennedy and Hans Corell, *Poverty and inequality is the other side of tax avoidance*, THE GUARDIAN, (Nov. 12, 2017) <https://www.theguardian.com/business/2017/nov/12/poverty-and-inequality-is-the-other-side-of-tax-avoidance>.

8. Kyle Pomerleau, *Tax Competition in New England*, AMERICANS FOR TAX REFORM (July 2, 2012 11:25 AM), <https://www.atr.org/tax-competition-new-england-a7014>.

9. *Id.* (Arguing that the corporate income tax should be lowered to compete internationally and citing the competition for lower state taxes).

10. See Nicholas Shaxson, *How to Crack Down on Tax Havens: Start with the Banks*, FOREIGN POL'Y (Mar./Apr. 2018) <https://www.foreignaffairs.com/articles/2018-02-13/how-crack-down-tax-havens>.

11. *See id.*

12. *See id.*

13. John Bell Henneman, *Nobility, Privilege and Fiscal Politics in Late Medieval France*, 13 DUKE UNIV. PRESS 1, 2 (Spring 1983) (A tax known as the *taille* was styled as a military subsidy and nobles could pay it as a "blood tax" through personal military service and could not be forced to pay the monetary tax).

14. David Leahardt, *The Rich Really Do Pay Lower Taxes Than You*, N.Y. TIMES (Oct. 6, 2019) <https://www.nytimes.com/interactive/2019/10/06/opinion/income-tax-rate-wealthy.html>.

15. *Id.*

the high earners were lower before World War II, and in the decades afterwards, those rates began to rapidly decline.<sup>16</sup> The medieval system of tax exemption for the noble class lasted much longer than America's mid-20th century experience of high taxation on the wealthy. Therefore, it is entirely possible that this trend is taking society back to the future and returning to a previous equilibrium.

Maintaining wealth and earning tax-free income is sometimes even legal. The Cayman Islands, for example, has no direct taxes at all—either income tax or capital gains tax.<sup>17</sup> Even though it is (for the most part) illegal, it is possible to not pay taxes and not get caught. With enough wealth, the elites can use a complex and dubious set of tax avoidance and evasion schemes to effectively lower their tax burden to zero. Within the historical context of shrinking taxes on the wealthiest in society, the ability of a taxpayer to evade taxes altogether is part of a larger trend. In recent years, this issue came to the forefront during the Panama Papers scandal, where a Central American law firm was found to have used a number of crafty techniques for helping wealthy taxpayers hide their income offshore.<sup>18</sup> But what exactly was the law firm doing for its clients? What laws would an American client of a foreign law firm be breaking, and what else could be done to curb this kind of conduct?

Part II of this article provides a historical overview of the problems spurring the creation of laws aimed to capture income wrongly withheld from the IRS. This includes an overview of the Bank Secrecy Act of 1970, the investigation into Union Bank of Switzerland (“UBS”), the creation of FATCA, and the first prosecution under the new law. Part III gives an overview of some of the latent issues with those new laws, including its effect on Americans living abroad, the challenge of getting cooperation from foreign governments, and unexpectedly low amount of revenue collected under the new law. Part IV proposes an additional measure to combat tax havens: a reporting requirement for law firms analogous to FATCA's reporting requirement for financial institutions. Part V concludes.

## II. HISTORY

Tax avoidance is the legal of arrangement of one's affairs with the goal of minimizing the amount of taxes owed to the government.<sup>19</sup> The Supreme Court has long recognized the legality of a taxpayer arranging their affairs in a way that reduces their tax obligation;<sup>20</sup> tax evasion, however, is a felony characterized by efforts to defeat the tax authorities' efforts to detect or collect a tax obligation.<sup>21</sup> Tax evasion has three elements: (1) a tax deficiency, (2) an affirmative act constituting evasion of the tax, and (3) willfulness to commit the affirmative act.<sup>22</sup> The element of

---

16. *Id.*

17. *World Fact Book: Cayman Islands*, CIA, <https://www.cia.gov/library/publications/the-world-factbook/geos/cj.html> (last visited Mar. 15, 2020).

18. Juliette Garside et al., *The Panama Papers: how the world's rich and famous hide their money offshore*, THE GUARDIAN (Apr. 3, 2016) <https://www.theguardian.com/news/2016/apr/03/the-panama-papers-how-the-worlds-rich-and-famous-hide-their-money-offshore>.

19. *Gregory v. Helvering*, 293 U.S. 465, 469 (1935).

20. *Id.*

21. I.R.C. § 7201.

22. *United States v. Boisseau*, 841 F.3d 1122, 1125 (10th Cir. 2016).

willfulness means a taxpayer cannot accidentally commit tax evasion.<sup>23</sup> Forgetting to pay taxes will result in a tax bill, not a criminal charge of tax evasion.<sup>24</sup> After the passage of FATCA in 2010, a voluntary compliance program was introduced to all who did not report their foreign assets to turn themselves in and pay back taxes in a lump sum in exchange for immunity from criminal penalties.<sup>25</sup> This window of immunity allowed the taxpayers who were delinquent under the Bank Secrecy Act of 1970 to separate themselves from the tax evaders discovered by FATCA reporting.

### A. *The Bank Secrecy Act of 1970*

For many decades, the U.S. has taxed the foreign income and property of its citizens.<sup>26</sup> The Supreme Court justified this by reasoning that a person is still enjoying the benefits of citizenship even when domiciled outside the country.<sup>27</sup> While filing their tax returns, U.S. taxpayers are under an obligation to report foreign bank accounts according to the Bank Secrecy Act of 1970 (“BSA”).<sup>28</sup>

The BSA was passed in order to counter the use of financial institutions in crime,<sup>29</sup> because adequate financial records proved useful in investigating all types of criminal, tax, and regulatory investigations.<sup>30</sup> The government was motivated to pass the BSA because some banks had recently stopped the practice of photocopying checks, or completely lost the records of some transactions.<sup>31</sup> The lack of a proper records frustrated the ability of the government to enforce its criminal, tax, and regulatory laws.<sup>32</sup> As a result of the BSA, if a foreign bank account has a cumulative amount of \$10,000 pass through it in a year, the taxpayer must file a Report of Foreign Bank and Financial Accounts (“FBAR”).<sup>33</sup>

While the requirement to report these foreign accounts had been in place since 1970,<sup>34</sup> if the bank itself did not report to the IRS, a taxpayer could simply not report the income. To find the delinquent taxpayers, the government needed foreign banks to voluntarily report American-owned bank accounts to the IRS.<sup>35</sup> As such, the government did not yet have an effective way of knowing if taxpayers were meeting their FBAR obligations. This problem is illustrated by the well-known case involving UBS.

---

23. *Income Tax: Fraud vs. Negligence*, FINDLAW, <https://tax.findlaw.com/tax-problems-audits/income-tax-fraud-vs-negligence.html> (last visited Mar. 15, 2020).

24. *Id.*

25. *Maze v. Internal Revenue Serv.*, 862 F.3d 1087, 1089–90 (D.C. Cir. 2017).

26. *Cook v. Tait*, 265 U.S. 47, 56 (1924); *See also* I.R.C. § 911 (2018).

27. *Cook*, 265 U.S. at 56.

28. *See Bank Secrecy Act*, IRS (Jan. 16, 2020), <https://www.irs.gov/businesses/small-businesses-self-employed/bank-secrecy-act>; *See also Report of Foreign Bank and Financial Accounts (FBAR)*, IRS (Jan. 9, 2020), <https://www.irs.gov/businesses/small-businesses-self-employed/report-of-foreign-bank-and-financial-accounts-fbar>.

29. *California Bankers Ass’n v. Shultz*, 416 U.S. 21, 26 (1974).

30. *Id.* at 27.

31. *Id.* at 26.

32. *Id.* at 27.

33. *Bank Secrecy Act*, *supra* note 28; *Report of Foreign Bank and Financial Accounts (FBAR)*, *supra* note 28.

34. *See Bank Secrecy Act*, *supra* note 28.

35. Shaxson, *supra* note 10.

### B. *The UBS Investigation*

Swiss banks have historically been famous for their strict confidentiality.<sup>36</sup> If a U.S. taxpayer tucked away a large amount of money in a Swiss bank account and did not follow their FBAR obligations, the IRS would not normally be aware of its existence unless a whistleblower came forward. This is what happened in the case of UBS.<sup>37</sup>

In the wake of the 2007 financial crisis, the U.S. government began to scrutinize the banking practices of UBS, a large Switzerland-based investment bank. Treasury took a hard line against the bank, compelling them to report thousands of Americans doing business with the bank. Though UBS originally wanted to only turn over information on customers when there was proof that they had participated in financial crimes, this did not satisfy Treasury because *the existence of the unreported accounts themselves* was the evidence the Treasury sought. In 2009, UBS agreed to turn over financial account information on U.S. account holders.

This action by the taxpayer is of course felony tax evasion; however, if the bank does not report the existence of the account, the tax evasion remains undetected.<sup>38</sup> Realizing how useful this banking information was in investigating financial crimes, lawmakers began to explore ways to compel the delivery of this information in the future.

### C. *The Creation of FATCA*

After the IRS compelled UBS to give over information on American account holders, Congress formulated a plan to get the same kind of disclosures for all Foreign Financial Institutions (“FFI”). In 2010, Congress passed The Foreign Account Tax Compliance Act (“FATCA”), requiring FFIs to report accounts of U.S. taxpayers to the IRS.<sup>39</sup> More specifically, this applied to bank accounts with a certain degree of connection to a U.S. person.<sup>40</sup> For example, U.S. resident aliens are U.S. persons whose accounts a foreign bank needs to report, according to FATCA.<sup>41</sup>

Under FATCA, if the U.S. taxpayer failed to report a qualifying account, the IRS imposed penalties.<sup>42</sup> Foreign financial institutions not in compliance became subject to a 30% tax on their transaction with U.S. financial institutions.<sup>43</sup>

Though FATCA’s penalty pressures FFIs,<sup>44</sup> FATCA is a U.S. law, which means its requirements for FFIs are not legally binding. However, many foreign countries that have decided to comply have agreed to the reporting requirements in

36. Lynnley Browning, *Tax Inquiry Shifts to Small Swiss Banks*, N.Y. TIMES (Dec. 23, 2010) <https://www.nytimes.com/2010/12/24/business/24tax.html?searchResultPosition=4>.

37. Stuart Pfeifer, *Banking*, L.A. TIMES (Oct. 26, 2009, 1200 AM) <https://www.latimes.com/archives/la-xpm-2009-oct-26-fi-swiss26-story.html> (Bank employee broke Swiss whistleblower laws to report that violating US law was routine at UBS).

38. *Id.*

39. *Summary of FATCA Reporting for U.S. Taxpayers*, IRS, <https://www.irs.gov/businesses/corporations/summary-of-fatca-reporting-for-us-taxpayers> (last visited Mar. 2, 2020).

40. *Id.*

41. *Taxing America’s Diaspora: FATCA’s Flaws*, ECONOMIST (June 28, 2014), <https://www.economist.com/leaders/2014/06/28/fatcas-flaws>.

42. *Summary of FATCA Reporting for U.S. Taxpayers*, supra note 39.

43. *Taxing America’s Diaspora: FATCA’s Flaws*, supra note 41.

44. *Report of Foreign Bank and Financial Accounts (FBAR)*, supra note 28.

a series of treaties, which shifts these requirements closer to settled law. The FATCA compliance treaty between Germany and the U.S., for example, is representative of the treaties signed with other countries.<sup>45</sup> Article 2 § 2(a) of the treaty requires German FFIs to report U.S. taxpayer information to the IRS, and Article 2 § 2(b) requires American FFI to report German taxpayer information to the German government.<sup>46</sup> The information is required to be reported annually.<sup>47</sup> This widespread FATCA compliance meant that tax evasion would need to shift to new strategies and warmer climes.

#### D. Initial Prosecutions Related to FATCA

On April 3, 2016, multiple news agencies broke the story of the “Panama Papers.”<sup>48</sup> An anonymous source gave German newspaper *Süddeutsche Zeitung* a vast trove of data detailing the illegal activities of Panamanian law firm Mossack Fonseca.<sup>49</sup> This leak of information exposed the world to the hidden practices of business leaders, heads of states, the rich, the powerful, and the famous.<sup>50</sup> The documents were shared with an international group of journalists that broke the story of these so-called Panama Papers.<sup>51</sup> In 2017, the “Paradise Papers” were published, revealing how large companies were using offshore accounts to avoid taxes.<sup>52</sup> These leaks revealed a large and continuing practice of financial secrecy used by prominent figures in politics and industry, as well as rogue actors.

The first people charged in America with tax evasion based on evidence from the Panama Papers were Ramses Owens, Dirk Brauer, Richard Gaffey, and Harald Joachim Von Der Goltz.<sup>53</sup> Owens worked at Mossack Fonseca,<sup>54</sup> and Brauer worked at Mossfon Asset Management, a firm closely associated with Mossack Fonseca.<sup>55</sup> Both Owens and Brauer were residents of Panama. Mossack Fonseca was a global law firm based in Panama, but with clients who lived all over the world,<sup>56</sup> including the Southern District of New York.<sup>57</sup>

In the first ever indictment for FATCA non-compliance, Von der Goltz was charged with a conspiracy to defraud the United States.<sup>58</sup> Using the information

---

45. *Agreement Between the United States of America and the Federal Republic of Germany to Improve International Tax Compliance and with respect to the United States Information and Reporting Provisions Commonly Known as the Foreign Account Tax Compliance Act*, TREASURY, <https://www.treasury.gov/resource-center/tax-policy/treaties/Documents/FATCA-Agreement-Germany-5-31-2013.pdf> (last visited Mar. 2, 2020) (The German American treaty is a “Model 1” treaty).

46. *Id.*

47. *Id.*

48. Garside et al., *supra*, note 18.

49. Frederik Obermaier et al, *About the Panama Papers*, SÜDDEUTSCHE ZEITUNG <https://panamapapers.sueddeutsche.de/articles/56febff0a1bb8d3c3495adf4/> (last visited Mar. 2, 2020).

50. *Id.*

51. *Id.*

52. *Paradise Papers: Everything you need to know about the leak*, BBC (Nov. 10, 2019), <https://www.bbc.com/news/world-41880153>.

53. *United States of America v. Ramses Owens et al.*, Docket No. 18 Crim 693, at 1 (So. Dist. N.Y., 2018).

54. *Id.*

55. *Id.*

56. *Id.*

57. *Id.* at 2.

58. *Id.*

found in the Panama Papers,<sup>59</sup> Von der Goltz was indicted for allegedly shielding his assets from U.S. tax authorities while living in the U.S. by putting those assets in the name of his non-American elderly mother, with the legal assistance of Mossack Fonseca.<sup>60</sup> When a Swiss bank told Goltz that they were soon going to be reporting U.S. client accounts to the IRS and that he should voluntarily report his assets or withdraw his funds from the bank,<sup>61</sup> Mossack Fonseca created a structure to house his assets in the event of his mother's death and remain secretly under the control of Von der Goltz.<sup>62</sup> These types of foundations, commonly utilized by Mossack Fonseca, gave the appearance of a functional foundation with a board of directors, board meetings, and a record of minutes.<sup>63</sup> Mossack Fonseca would run the sham foundation, but the client remained in control.<sup>64</sup> Client assets would be distributed between the various foundations, companies, and their nominally-held bank accounts.<sup>65</sup> The firm instructed its U.S. clients to use debit cards and fictitious sales to get their money back into the U.S. without paying taxes.<sup>66</sup> Finally, the U.S. client would file their taxes and not report their hidden accounts.<sup>67</sup> Using this system, Van der Goltz was able to donate his money to this foundation, allowing him to continue earning money from the assets for both himself and his children.<sup>68</sup>

Owens and Brauer were charged with conspiracy to defraud the United States for creating, marketing, and servicing sham foundations and shell companies in Panama (as well as other countries) for the purposes of hiding the ownership by U.S. taxpayers of assets stored in overseas banks.<sup>69</sup> Owens and Brauer told their clients that these arrangements brought tax benefits to even those within the U.S.<sup>70</sup> Owens and Brauer met with clients in New York and misrepresented to some of the clients of Mossack Fonseca that this tax-free arrangement was actually legal.<sup>71</sup> The bank accounts were purposefully created in states with strict bank secrecy, so that the U.S. could not discover the accounts.<sup>72</sup> By advising their clients to not report the assets held in these offshore accounts, Mossack Fonseca was alleged to have knowingly advised its clients to violate the provision enacted by the BSA that required U.S. taxpayers to report their foreign assets.<sup>73</sup>

### III. CURRENT ISSUES

With the first indictments of individuals for non-compliance of FATCA, the effects of this legislation are finally being realized.<sup>74</sup> While the intent of the law was

---

59. *Id.* at 31–32.

60. *Id.* at 17.

61. *Id.* at 29.

62. *Id.* at 31.

63. *Id.* at 8.

64. *Id.*

65. *Id.*

66. *Id.* at 9.

67. *Id.*

68. *Id.* at 31.

69. *Id.* at 1.

70. *Id.* at 7.

71. *Id.* at 8.

72. *Id.*

73. *Id.* at 11.

74. *DOJ Secures First Ever Conviction for Violating FATCA*, THE NAT'L L. REV., (Sept. 17, 2018), <https://www.natlawreview.com/article/doj-secures-first-ever-conviction-violating-fatca>; See Jesse



to increase revenue,<sup>75</sup> prosecution will induce those would-be tax evaders to comply with the law. The law, however, is not without criticism.<sup>76</sup> Some banks have taken precautionary measures by closing accounts with Americans or refusing to service Americans so they do not have the added cost of compliance with the reporting requirements.<sup>77</sup> This makes it more difficult for Americans living abroad to find local banking services.

### A. *Many Americans Living Abroad are Unintentionally Harmed by FATCA*

Americans living abroad are also expected to pay U.S. taxes.<sup>78</sup> While the IRS was mostly unaware of unreported foreign income in the past, these Americans have been hit with unexpected tax bills.<sup>79</sup> Some Americans even go so far as to renounce their citizenship to get out of U.S. tax obligations.<sup>80</sup> This increase in renunciation of citizenship was high enough that the IRS increased the cost of doing so in an attempt to make the option less attractive.<sup>81</sup>

On September 17, 2019, a bill was introduced in the U.S. House of Representatives for the purpose of helping Americans living abroad avoid some of the negative, unintended repercussions of FATCA.<sup>82</sup> This proposed law exempts U.S. citizens living abroad from reporting requirements if they are bona fide residents of the foreign country, which also spares them from non-reporting penalties.<sup>83</sup> In other words, if an American is living in a foreign country for an entire tax year, and is earning income that is taxed by that foreign country to an extent that none is taxable under U.S. law, foreign bank accounts owned by that citizen would not have to be reported to the IRS by the relevant FFI.<sup>84</sup> This would make it easier to access local banks and would simplify their tax filings.

---

Drucker, *U.S. Prosecutors Bring Their First Charges Over the Panama Papers*, N.Y. TIMES (Dec. 4, 2018), <https://www.nytimes.com/2018/12/04/business/panama-papers-indictment.html>.

75. 111 CONG. REC. S1633, 1636 (2010), <https://www.govinfo.gov/content/pkg/CREC-2010-03-17/pdf/CREC-2010-03-17-pt1-PgS1633-8.pdf#page=4> (“Right now, thousands of U.S. tax dodgers conceal billions of dollars in assets within secrecy-shrouded foreign banks, dodging taxes and penalizing those of us who pay the taxes we owe. The Permanent Subcommittee on Investigations, which I chair, has estimated that these tax-dodging schemes cost the Federal Treasury \$100 billion a year. But under this legislation, for the first time, foreign banks will be required to disclose their U.S. account holders to the U.S. Government or face significant penalties.”).

76. Geoff Williams, *U.S. Expats find their money is no longer welcome at the bank*, REUTERS, (June 11, 2014) <https://www.reuters.com/article/us-banks-expats/u-s-expats-find-their-money-is-no-longer-welcome-at-the-bank-idUSKBN0EM16V20140611>.

77. *Id.*

78. Nancy Ing & Yuliya Talmazan, *‘Accidental Americans’ living abroad fight tax bill from Uncle Sam*, NBC NEWS (Apr. 22, 2018), <https://www.nbcnews.com/nightly-news/accidental-americans-living-abroad-fight-tax-bill-uncle-sam-n867711>.

79. *Id.*

80. Russell Newlove, *Why expat Americans are giving up their passports*, BBC NEWS (Feb. 9, 2016), <https://www.bbc.com/news/35383435>.

81. *Id.*

82. H.R. 4362, 116th Cong. § 3(3) (2019).

83. Carolyn B. Maloney, *Give overseas Americans the relief they need*, DEAR COLLEAGUE (Sept. 26, 2019), <http://dearcolleague.us/2019/09/give-overseas-americans-the-relief-they-need-support-h-r-4262-the-overseas-americans-financial-access-act/>.

84. *Id.*

HR 4362 is a fair way to adjust the law to prevent the inadvertent negative impact of FATCA on Americans living and working overseas. The downside is that this might open one more loophole to exploit.

The IRS has also created a program for Americans inadvertently taxed as a result of FATCA.<sup>85</sup> Since one of the criteria used by banks to determine which customers are U.S. persons is place of birth,<sup>86</sup> the account information of certain American-born persons *who have not lived in America for any significant amount of time* may be included in FATCA reporting information.<sup>87</sup> As such, these individuals are allowed to renounce their U.S. citizenship without paying the renunciation fee.<sup>88</sup> Additionally, if a U.S. citizen failed to file proper tax returns after the passage of FATCA—and they have both a net worth of less than \$2 million and a total tax bill of less than \$25,000—the IRS may grant relief from penalties if the failure to file was due to non-willful conduct, such as a “good faith misunderstanding of the requirements of the law.”<sup>89</sup>

### B. Jurisdictional Overreach

FATCA has also been criticized for being a form of financial imperialism imposed on the rest of the world,<sup>90</sup> allegedly asserting extraterritorial jurisdiction by the U.S.<sup>91</sup> Any non-compliant bank could have its transactions with a FATCA-compliant bank taxed at a rate of 30%.<sup>92</sup> This level of penalty would be devastating to any bank it was applied to.<sup>93</sup> To avoid this, most countries have entered into intergovernmental agreements (“IGAs”) with the U.S., allowing both countries access to information of the bank accounts of their citizens in the other country.<sup>94</sup> Most countries agreed to these arrangements because the benefits of exchanging this data was apparent; according to Treasury, as of 2020 there are 113 foreign countries that have agreed to provide the information, including Switzerland.<sup>95</sup> Some holdouts include Russia, Iran, and North Korea.<sup>96</sup>

However, there has been an unforeseen catch: Treasury does not have authority to actually release information on U.S. taxpayers to foreign governments. As of the end of 2019, Congress had not passed enabling legislation allowing Treasury to

---

85. *IRS Announces Penalty and Tac Path to Renouncing US citizenship for Accidental Americans*, BRIGHT!TAX (Sept. 16, 2019), <https://brighttax.com/blog/irs-announces-penalty-free-path-renouncing-us-citizenship-accidental-americans/>.

86. *Relief Procedures for Certain Former Citizens*, INT. REV. SERV., <https://www.irs.gov/individuals/international-taxpayers/relief-procedures-for-certain-former-citizens> (last visited Apr. 7, 2020).

87. *Id.*; see also Patrick Wintour, *Boris Johnson among record number to renounce American citizenship in 2016*, GUARDIAN (Feb. 9, 2017), <https://www.theguardian.com/politics/2017/feb/08/boris-johnson-renounces-us-citizenship-record-2016-uk-foreign-secretary>.

88. See INT. REV. SERV., *supra* note 86.

89. *Id.*

90. *Taming IRS Imperialism*, WALL ST. J. (Feb. 3, 2017), <https://www.wsj.com/articles/taming-irs-imperialism-1486166764>.

91. *Taxing America's Diaspora: FATCA's flaws*, *supra* note 41.

92. *Id.*

93. *Id.*

94. *Foreign Account Tax Compliance Act*, U.S. DEPT. TREAS., <https://www.treasury.gov/resource-center/tax-policy/treaties/pages/fatca.aspx> (last visited Apr. 7, 2020).

95. See *id.*

96. See *id.*

disclose information on U.S. persons to foreign governments.<sup>97</sup> As a result, Treasury has not yet reported the relevant information to any foreign government.<sup>98</sup> Therefore, while the agreements appear to be reciprocal, so far, they are not: Treasury is receiving reports from foreign governments, but the U.S. is not giving out the same information to those foreign countries.<sup>99</sup>

An alternative to FATCA exists in the form of an international financial data sharing agreement. In 2014—just four years after FATCA was passed—the Organization for Economic Co-operation and Development (“OECD”) developed the Common Reporting Standard (“CRS”).<sup>100</sup> As of November 2019, the U.S. had not agreed to it,<sup>101</sup> so while most countries in the world share financial data through the CRS, and most countries share the same information with the U.S. through FATCA,<sup>102</sup> U.S. taxpayers are not currently being automatically reported to anyone. Until the U.S. starts automatically reporting—as it agreed to in its IGAs—the only way for foreign governments to get U.S. taxpayer data is upon request. Before FATCA, many argued that providing data upon request was ineffective at rooting out tax evasion.<sup>103</sup> The effectiveness of FATCA’s automatic reporting was so obviously useful that its principles were accepted globally with the rapid development of CRS.

### *C. FATCA Does Not Raise Expected Revenue*

One criticism of FATCA is that it does not raise the revenue it was meant to raise.<sup>104</sup> FATCA was enacted as part of (and to help pay for) the Hiring Incentives to Restore Employment Act,<sup>105</sup> and was projected to capture up to \$100 billion dollars per year in lost revenue.<sup>106</sup> The actual revenue collected from these offshore assets has been dramatically lower. Congress projects annual tax revenue to increase by \$250 million as a result of taxation on previously-untaxed offshore assets.<sup>107</sup> This means that the previous estimates were off by a significant margin. Further, the actual number of accounts in compliance with FATCA is also declining,<sup>108</sup> so it is unlikely that the revenue collected is going to suddenly increase in the coming years.

The initial estimates were high as a result of the elusive nature of the problem. Since these accounts are, by definition, unknown to the federal government before their disclosure or discovery, any estimate of the magnitude of the problem is

---

97. Allison Christians, *What You Give and What You Get: Reciprocity Under a Model 1 Intergovernmental Agreement on FATCA*, CAYMAN FIN. REV., Apr. 12, 2013, at 5.

98. *Id.* at 4.

99. *Id.* at 5.

100. Shaxson, *supra* note 10.

101. Noam Noked, *Should the United States Adopt CRS?*, 117 Mich. L. Rev. 118, 119 (2019).

102. *Id.* at 118–19.

103. See 111 CONG. REC. 1635 (2010).

104. William Brymes, *Is FATCA chasing a leprechaun and his pot of gold?* CAYMAN FIN. REV., Aug. 19, 2015, <https://www.caymanfinancialreview.com/2015/08/19/Is-FATCA-chasing-a-leprechaun-and-his-pot-of-gold/>.

105. See 111 CONG. REC. 1635 (2010).

106. Brymes, *supra* note 104.

107. *Id.*

108. *Id.*

unreliable. Before Congress passed FATCA, the IRS commissioner testified that there was no credible estimate of the lost revenue from offshore tax abuse.<sup>109</sup>

#### IV. SOLUTIONS

The current reporting schemes are proving effective at shedding light on U.S. taxpayer assets in foreign bank accounts,<sup>110</sup> but as the Panama Papers and the Paradise Papers show, the business of hiding wealth is alive and well. Instead of secret bank accounts, people have shifted to secret ownership of shell corporations and sham foundations. With the true ownership of corporate entities shrouded behind a wall of secrecy, the companies can have an account in a bank without the bank knowing the actual owner. By requiring mandatory reporting to the IRS, FATCA may counter these shell companies which facilitate tax evasion. Like what FATCA did for reporting of bank accounts by FFIs, law firms could be required to report the creation or ownership of corporate entities. In a similar setup to registering title to land, unregistered or unreported corporate ownership could be considered invalid. In this scenario, the U.S. could once again pass a law which includes sanctions for non-compliance. The U.S. has the ability to sanction companies by cutting them off from the global financial market by stopping the company from completing financial transactions that go through the U.S.<sup>111</sup> Since the U.S. dollar is used as a global reserve currency, transactions between countries that have nothing to do with the U.S. still have their bank transactions routed through the U.S.,<sup>112</sup> giving the U.S. a unique ability to sanction any person, corporation or individual unilaterally, with global ramifications on their financial interests.<sup>113</sup> By using this leverage, the U.S. will be able to coerce other governments into agreeing to this arrangement.<sup>114</sup>

An ideal law would require law firms to report to Treasury any records concerning the creation, sale or transfer of ownership of corporations, trusts, and foundations (or other such legal entities). While an individual may have a legitimate reason for desiring privacy, the argument that they have a legitimate reason to conceal anything from the IRS is suspicious. Once ownership is reported, the IRS would be able to investigate the structures of shell companies. If failure to report the ownership of a company was itself a violation of the law, shell companies themselves would be illegal. Each link in the chain of ownership would be traceable to the next entity. Any company that does not reveal its owner would be breaking the law.

One possible counter argument to this approach is that it violates attorney-client privilege. According to Model Rule 1.6, an attorney must not reveal information relating to the representation of a client unless the client gives informed consent.<sup>115</sup>

---

109. *Id.*

110. U.S. DEPT. OF TREAS., TREASURY INSPECTOR GENERAL FOR TAX ADMINISTRATION 11 (2018), <https://www.treasury.gov/tigta/auditreports/2018reports/201830040fr.pdf>.

111. Kathy Gilsinan, *A Boom Time for U.S. Sanctions*, THE ATLANTIC (May 3, 2019), <https://www.theatlantic.com/politics/archive/2019/05/why-united-states-uses-sanctions-so-much/588625/>.

112. *Id.*

113. *Id.*

114. *Id.*

115. MODEL RULES OF PROF'L CONDUCT r. 1.16 (AM. BAR ASS'N 1983).

This confidentiality is considered fundamental to the right to advice of counsel.<sup>116</sup> If law firms are required to comply with this disclosure requirement, none would not be able to give their clients the ability to have completely confidential communication. On the other hand, classifying the creation or transfer of a company as a legally significant act may tie it to the disclosure requirement.

Another counter argument is that, since these tax evaders are already breaking the law, and the business of creating and sheltering assets from the tax authorities will merely migrate to non-compliant jurisdictions, compliant firms and countries will take themselves out of the market for these tax shelter services. Tax shelters will move to countries outside of U.S. influence if the U.S. enforces these disclosures everywhere its influence holds sway. Once the U.S. overuses financial sanctions, any part of the world subject to a freeze out of the U.S. financial system will have a strong incentive to contribute toward the creation of a parallel financial system where U.S. influence cannot reach.<sup>117</sup> Pushing the tax havens into parts of the world that are both hostile and separated from U.S. influence would likely cause more harm than good to U.S. interests. Another criticism is that this rule would never produce useful information because an extensive body of law already exists to combat these activities, so passing one more law against it will not incentivize them to report what they are doing. The secret shell companies they create will continue to go unreported because no one participating in tax evasion would report themselves.

By focusing primarily on rooting out tax evasion by its citizens in foreign countries, the U.S. ignores the fact that the same kind of secretive accounts in shell companies are possible within the U.S.<sup>118</sup> Former presidential candidate Ralph Nader once suggested that the U.S. should do away with the state level incorporation of firms and move to a federal system of incorporation.<sup>119</sup> This would eliminate individual states competing to be the most secretive for hiding assets.<sup>120</sup> It would also allow the federal government to collect and share asset information with foreign partners.

## V. CONCLUSION

Since the global financial crises, governments around the world have taken an interest in raising revenues by capturing some of the money lost due to tax evasion.<sup>121</sup> While the revenue collected from the crackdown on tax sheltered assets has been much less than what was hoped for, the effort is bringing some revenue. The U.S. lead this effort with FATCA, which in turn led to the global development of CRS.<sup>122</sup>

---

116. Juliet Boyd, *You Think Your Client is Going to Lie on the Stand—The Classic Dilemma of a Criminal Defense Lawyer*, TRAFFIC LAW & COURTS, March 2012, at 6, Vol. 21, No. 3, [https://www.isba.org/sites/default/files/sections/newsletter/%20March%202012\\_8.pdf](https://www.isba.org/sites/default/files/sections/newsletter/%20March%202012_8.pdf) (last visited Feb. 28, 2020).

117. Gilsinan, *supra* note 111.

118. Shaxson, *supra* note 10.

119. *Id.*

120. *Id.*

121. *Id.*

122. *Id.*

The reporting requirements of FATCA caused many hidden accounts to move from secret bank accounts into exotic shell company schemes.<sup>123</sup> Law firms hid the true ownership of these companies under the guise of privilege. Only through the leak of confidential documents was the public alerted to the extent of the global financial underground, which hints at a larger problem. Similar to the process of rooting out misbehavior in banking, legislators can require law firms to adhere to a system of disclosure in an effort to track ownership of companies and foundations. If the extent of who owns what were revealed and studied, the public would be able to make an informed policy decision and global wealth could be subjected to democratic controls if there is nowhere to hide.

---

123. *United States of America v. Ramses Owens et al.*, Docket No. 18 Crim 693, at 1 (So. Dist. N.Y., 2018).