November 5, 2013

The Tax Division's comments about the *Program for Non-Prosecution Agreements or Non-Target Letters for Swiss Banks*

The Tax Division has received a number of questions about its *Program for Non-Prosecution Agreements or Non-Target Letters for Swiss Banks* (the "Program"). The responses to these questions and commentary can be found in the plain language of the Program. The following comments highlight and address some of these issues, and are not intended to supplant any provision of the Program.

Bank-specific issues and issues concerning individuals. The Tax Division will not respond in advance to fact-specific hypotheticals. Any Swiss bank with specific issues should seek to address those issues in the context of the Program. As the Program states, each non-prosecution agreement may take into account factors specific to a particular bank. And nothing in the Program changes our willingness to hear from individuals and other entities with criminal exposure that are ready to cooperate.

Deadline and address for letters of intent. The deadline for submitting a letter of intent to the Tax Division under category 2 of the Program is December 31, 2013. A letter of intent therefore may be submitted any time between now and December 31. Once a letter of intent is submitted, a 120-day deadline is triggered for category 2 banks to comply with the Program's requirements. The Tax Division wishes to encourage banks to submit their letters of intent as early as possible so that they may begin discussions with the Tax Division. For purposes of the computation of the 120-day deadline for early submissions, unless a bank requests otherwise, it will be computed as if the letter of intent were submitted on December 31. With respect to category 3 and 4 banks, however, the Program specifically prohibits the submission of a letter of intent prior to July 1, 2014. Category 3 and 4 letters of intent will not be accepted before that date.

Letters of intent may be addressed as follows:

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Choosing a category. Each eligible Swiss bank should carefully analyze whether it is a category 2, 3 or 4 bank. While it may appear more desirable for a bank to attempt to position itself as a category 3 or 4 bank to receive a non-target letter, no non-target letter will be issued to any bank as to which the Department has information of criminal culpability. If the Department learns of criminal conduct by the bank after a non-target letter has been issued, the bank is not protected from prosecution for that conduct. If the bank has hidden or misrepresented its activities to obtain a non-target letter, it is exposed to increased criminal liability.

Changing from Category 3 to 2 (or 2 to 3). The Program provides that changes from category 3 to category 2 will be approved by the Tax Division only in extraordinary circumstances, and subject to the limitations set out in the Program. (Program III.C.) If a bank has submitted a letter of intent under category 2 of the Program and belatedly determines that it should have applied under category 3, a bank may withdraw its letter of intent. If the bank later submits a timely letter of intent under category 3, it should expect to be asked to describe why it initially believed that it may have committed tax-related or monetary transaction offenses as described in the Program.

Qualifications of independent examiner. The Program defines an independent examiner as a "qualified independent attorney or accountant." The Tax Division will not pre-approve or pre-certify independent examiners, but has retained the right to object in any particularly problematic situations (for example, if the proposed independent examiner has been indicted or is under criminal investigation). The independent examiner may rely on the assistance of his or her staff when conducting the required examination, but one professional must sign the written product. The Program does not require that the professional be licensed in any particular jurisdiction. The key issue for a bank in selecting an independent examiner is to select one who has the ability to verify and report on the elements required under the Program for that bank. An attorney or accountant who is perfectly suited to act as an independent examiner for a small bank, for example, may not be well suited to act as an independent examiner for a large bank. The bank should ensure that an independent examiner is not merely qualified, but also competent and capable of meeting his or her responsibilities under the Program for that particular bank. No attorney or accountant has, nor should suggest that he or she has, advance approval of the Tax Division, or some special relationship with the Tax Division that may lead to more favorable treatment, either as an independent examiner or as a representative.

Independence of the examiner. The independent examiner is not an advocate, agent, or attorney for the bank, nor is he or she an advocate or agent for the government. He or she must provide a neutral, dispassionate analysis of the bank's activities. Communications with the independent examiner should not be considered confidential or protected by any privilege or immunity. So long as the independent examiner has no ethical prohibition or conflict of interest, an independent examiner is not disqualified merely because of a pre-existing relationship with the bank. The bank's letter of intent should explain any other current or prior relationship between the independent examiner (including his or her firm) and the bank. The Tax Division retains the right to object to any independent examiner based on a conflict of interest or other ethical grounds.

Content of independent examiner report. Reports must be substantive, detailed, and address the requirements set out in the Program. The Tax Division does not require that the written report be made in any particular format. Just as the Program intends flexibility in the selection of an independent examiner, there is likewise flexibility in the contents of a report so long as it is complete. For example, the report of a small bank that is predominantly a local bank may be much different from that of a larger bank with an international clientele. Banks are required to cooperate fully and "come clean" to obtain the protection that is offered under the Program.

Information required under the Program – no aggregate account data. Section II.D.2 of the Program requires specific information about each U.S. related account. If anyone is advising a bank that aggregate data is sufficient under the Program, he or she is mistaken.

Penalty calculation – permitted reductions. The Program allows for the reduction of penalties with respect to three categories of U.S. related accounts. The first category – accounts that are not undeclared – is intended to address issues concerning lines of business that by their nature did not facilitate the evasion of U.S. taxes and reporting requirements. For example, a corporate account that was declared but had U.S. signatories who did not file FBARs is included in the definition of U.S. related accounts under the Program, but may be excluded for the penalty calculation. The second category – accounts that were disclosed by the bank to the Internal Revenue Service – refers only to accounts that were timely disclosed, not accounts that are disclosed under FATCA, as part of the Program, pursuant to treaty requests, as a result of other law enforcement efforts, or similar forms of later disclosure. The third category – accounts as to which the bank notified its account holders of an announced offshore voluntary disclosure program and can establish that its account holder made a voluntary disclosure under that program – includes only those accounts that were reported subsequent to notification by the bank. All forms of voluntary disclosure acceptable to the IRS will meet the voluntary disclosure standard of the Program, including the OVDI/OVDP procedures, the Streamlined Filing Compliance Program, and FBAR compliance under FAQs 9 and 17 of the respective IRS programs. The burden to show the application of penalty reductions rests with the bank. (Program II.H.)

No de minimis exception. There is no *de minimis* exception anywhere in the Program. In particular, category 4 is intended to provide a streamlined procedure for local banks that service Swiss residents. The Program does not allow a bank that has committed tax-related or monetary transaction offenses to qualify as a category 4 bank. (Program IV.E.) Such a bank should seek a non-prosecution agreement under category 2.

Category 4 banks – retroactive application of FATCA Annex II, paragraph II.A.1. The Program requires that banks seeking non-target letters under category 4 of the Program qualify under the U.S.-Swiss FATCA Agreement as a "Deemed Compliant Financial Institution" that is a "Financial Institution with Local Client Base," as if the Program were in force beginning on August 1, 2008, except that the 98 percent residency test in Annex II, Paragraph II.A.1(e) of the Agreement must be met on two dates – December 31, 2009, and August 29, 2013. The same standard applied by the Treasury Department for FATCA implementation will apply. Nonetheless, a bank should make efforts to identify undisclosed accounts to determine whether it is in fact a category 2 bank. Also, although not explicitly stated in the Program, Annex II, Paragraphs II.A.1(g) (which requires the implementation of certain monitoring and reporting provisions on or before January 1, 2014) and (j) (which prohibits discrimination against opening or maintaining accounts for certain U.S. persons who are residents of Switzerland) will not be given retroactive effect under the Program.

Civil penalties. The Program is a Department of Justice program, and as such addresses only potential criminal liability that may be pursued by the Department of Justice. The Program does not address civil issues, and any such issues should be directed to the specific agency involved. If a bank has any issues concerning other current or pending NPAs or DPAs involving other DOJ

components, questions concerning such agreements should be directed to that component, and notice of such agreements should also be provided to the Tax Division.

Bottom line. Each eligible Swiss bank should carefully weigh the benefits of coming forward, and the risks of not taking this opportunity to be fully forthcoming. A bank that has engaged in or facilitated U.S. tax-related or monetary transaction crimes has a unique opportunity to resolve its criminal liability under the Program. Those that have criminal exposure but fail to come forward or participate but are not fully forthcoming do so at considerable risk.