



# Department of Justice

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**STATEMENT OF**

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UNITED STATES DEPARTMENT OF JUSTICE**

**BEFORE THE**

**PERMANENT SUBCOMMITTEE ON INVESTIGATIONS  
COMMITTEE ON HOMELAND SECURITY  
AND GOVERNMENTAL AFFAIRS  
UNITED STATES SENATE**

**HEARING ENTITLED**

**"TAX HAVEN BANKS AND U. S. TAX COMPLIANCE - OBTAINING  
THE NAMES OF U.S. CLIENTS WITH SWISS ACCOUNTS"**

**PRESENTED**

**MARCH 4, 2009**

Chairman Levin, Acting Ranking Member Coburn, and Members of the Subcommittee, thank you for the opportunity to appear before you this afternoon to discuss the Department of Justice's (Department) efforts to combat the use of banks and other entities abroad by United States taxpayers to evade income taxes.

The Department greatly appreciates the extraordinary commitment that the Chairman, Members of the Subcommittee, and staff have made to investigate the often arcane world of offshore tax evasion and avoidance by United States citizens. Your tireless work over the last several years has brought attention to serious misconduct that threatens to undermine the fundamental integrity of our tax system. Although we will vigorously enforce United States tax laws whenever and wherever necessary, enforcement is only one element of successful tax administration. Thanks to your efforts, taxpayers have a greater understanding of their obligations and the consequences of noncompliance. You have also put tax professionals and financial advisors on notice that their efforts to design, market, and facilitate tax evasion schemes will not be tolerated.

The Subcommittee's July 2008 report outlined the role played by UBS AG (UBS), in facilitating the circumvention of federal tax laws by United States taxpayers. UBS is a corporation organized under the laws of Switzerland and is engaged in the global financial services business. In particular, you have expressed an interest in learning more about the progress UBS has made in its commitment to exit its cross-border business involving United States clients, its response to the "John Doe" summons issued by the Internal Revenue Service (IRS), and the status of the parallel criminal and civil investigations undertaken by DOJ's Tax Division.

The criminal investigation into UBS's activities within the United States includes the recently filed Deferred Prosecution Agreement entered into with UBS. The civil investigation is focused on obtaining additional information from UBS about the names of the tens of thousands of United States citizens who may have undeclared accounts with UBS that they may be using to avoid paying United States taxes.

In conducting law enforcement investigations, the Department goes to great lengths to ensure that the government's inquiry is complete, and that testimony and evidence are gathered and fully analyzed outside of the public arena. Our policy of not disclosing non-public information about ongoing matters protects both the rights of individuals who may be assisting in the investigation and the rights of criminal defendants, as well as the integrity of the investigation itself. Our ability to comment is also circumscribed by Federal Rule of Criminal Procedure 6(e), which protects the disclosure of grand jury information. In a tax case, the tax privacy statute, 26 U.S.C. § 6103, further limits the government's disclosure of tax information. Although certain aspects of the UBS matter are public, both the civil and the criminal matters are ongoing, and certain documents relating to the criminal matter remain under court seal. Therefore, my remarks today will be strictly limited to positions the Department has taken on the public record.

On February 18, 2009, the United States District Court for the Southern District of Florida accepted a deferred prosecution agreement between the government and UBS. Under the terms of that agreement, UBS waived indictment and consented to the filing of a one-count criminal information charging UBS in a conspiracy to defraud the United States and the Internal Revenue Service, in violation of United States criminal law. As part of the deferred prosecution agreement, UBS also agreed to pay \$780 million in fines, penalties, interest, and restitution. If UBS carries out its obligations under the deferred prosecution agreement, the government will recommend dismissal of the charge.

Fundamental to the agreement is UBS's acceptance of responsibility for violating United States law. As set forth in detail in the deferred prosecution agreement and accompanying Statement of Facts – the documents are available for public viewing – UBS acknowledged that, beginning in 2000 and continuing through 2007, it participated in a scheme to defraud the United States and the IRS, through its cross-border business. UBS private bankers and managers actively facilitated the creation of accounts in the names of offshore companies, allowing United States taxpayers to conceal their ownership or beneficial interest in the accounts in an effort to evade United States tax reporting and payment requirements. UBS also admitted in the deferred prosecution agreement that it had failed to implement effective controls to detect and prevent the unlawful activity, and that it had failed to initiate an effective investigation into credible allegations of such unlawful activity, and had failed to take effective action to stop such activities.

In looking at this case, it is important to understand both the obligations of United States taxpayers holding assets in overseas accounts, as well as the obligations of UBS when it voluntarily entered into a Qualified Intermediary (QI) Agreement with the IRS. Under United States law, taxpayers are subject to taxation on their worldwide income. A United States taxpayer is free to hold accounts offshore or in a foreign bank. But the United States taxpayer still must report information about those assets and the income they generate, and pay all United States taxes that result from that income. Taxpayers who fail to make disclosure or to report their income are potentially subject to civil penalties and, in appropriate circumstances, criminal prosecution.

In an effort to improve compliance by United States and foreign taxpayers with foreign accounts invested in United States securities, the IRS developed the Qualified Intermediary Program. Under the QI program a foreign bank must document whether its accountholders were United States or foreign owners. If an accountholder is a United States owner, and the account holds United States securities, then the foreign bank agrees to report, and if necessary to backup withhold, on a taxpayer specific basis on each United States accountholder's earnings in their foreign account. The foreign bank is not required to report on a United States accountholder if the account does not hold United States securities.

In 2000, UBS purchased the brokerage firm Paine Webber. In 2001, UBS voluntarily entered into a QI Agreement with the IRS. Under this Agreement, UBS agreed to report to the IRS income and other identifying information for its United States

accountholders who held United States securities in a UBS account. UBS also agreed to report on United States accountholders who directed investment activities in foreign securities from the United States. Under the QI Agreement, United States taxpayers with UBS accounts had two options: (1) report on income from United States paid into their accounts; or (2) divest their UBS account of United States securities. It is important to reiterate that United States law still required taxpayers who chose the second option to identify their ownership of foreign accounts and report the income from those accounts on their tax returns.

Almost from the inception of the QI Agreement, however, UBS began to undermine its purpose. Directly or indirectly, UBS aided some of its United States customers in disguising their ownership in UBS accounts, in order to help those customers evade their United States tax reporting and payment responsibilities. Between 2000 and 2007, UBS violated United States tax and securities laws. UBS bankers routinely traveled to the United States to market Swiss bank secrecy to United States clients interested in attempting to evade United States income taxes. An internal UBS memorandum filed with the court demonstrates that, in 2004 alone, UBS bankers traveled to the United States where they held approximately 3,800 separate meetings with U.S. clients to discuss their clients' Swiss accounts.

UBS used a variety of strategies to conceal their cross-border activities. For example, UBS instructed its bankers who traveled to the United States to falsely represent to United States Customs that they were traveling for pleasure. They also recommended that bankers rotate hotel accommodations while visiting the United States UBS bankers used counter-surveillance techniques to help prevent the detection of their marketing efforts and the identities and offshore assets of their U.S. clients. Clients of the cross-border business in turn filed false tax returns with the IRS which omitted the income earned on their Swiss bank accounts and failed to disclose the existence of those accounts to the IRS. UBS bankers also advised United States clients to misrepresent the receipt of funds in the United States from their UBS accounts as loans from UBS, and to destroy all United States-based records of their offshore accounts. United States clients of UBS's cross-border business have used Swiss bank secrecy laws and steps taken by UBS to conceal from the IRS approximately \$20 billion in assets. For the period 2000 through 2007, UBS failed to withhold approximately \$220 million in income taxes on income earned in those accounts.

Despite the difficulties posed as a result of historical concealment efforts and Swiss bank secrecy laws, the Department's Tax Division, together with the Internal Revenue Service, has been aggressively investigating those who participated in this scheme. In June 2008, former UBS private banker Bradley Birkenfeld pled guilty to a charge of conspiring to defraud the United States for his part in the scheme. Mr. Birkenfeld is scheduled to be sentenced on May 1, 2009. In November 2008, UBS executive Raoul Weil was indicted by a federal grand jury in Fort Lauderdale and charged with conspiring to defraud the United States for his alleged role in overseeing the United States cross-border business. The district court recently declared him to be a fugitive.

As part of the deferred prosecution agreement, UBS has agreed to provide the United States with voluminous and detailed records concerning accounts held directly or through beneficial arrangements by United States persons. UBS has also undertaken a continuing obligation to cooperate with the criminal investigation and any resulting prosecutions, and also to search for and turn over any additional records found concerning such accounts. The specific criteria for account records disclosed, and the number of such accounts as to which records have been disclosed to date are set forth in a document that the District Court has ordered sealed.

UBS has also agreed to the following conditions:

- UBS will terminate its United States cross-border business. Accounts of United States customers covered by the deferred prosecution agreement will be closed and assets liquidated, with proceeds distributed to the United States owners in dollar-denominated instruments. While we are not at liberty to discuss the specific provisions due to the Court's order to seal, the agreement does provide what we believe will be effective means to detect and defeat attempts to transfer and further conceal assets or proceeds from the accounts subject to this Agreement.
- UBS has agreed to pay to the United States \$780 million.
- UBS's challenge to the Government's motion to enforce the "John Doe" summons, including the filing of an appeal from an adverse ruling, will not be considered a breach of the deferred prosecution agreement. However, upon completion of that litigation, if the Court were to order UBS to produce the documents sought and hold UBS in contempt for failure to do so; UBS's non-compliance may be determined to be a material breach of the deferred prosecution agreement, permitting the Government to proceed with the criminal prosecution of UBS.
- UBS's failure to comply with a term of the deferred prosecution agreement may, in the sole discretion of the Government, be deemed a material breach, permitting the Government to proceed with the criminal prosecution of UBS. If UBS fully complies with the deferred prosecution agreement, then the criminal information will be dismissed.
- The deferred prosecution agreement only applies and provides protection for the bank as to the specific conduct set forth in the deferred prosecution agreement. It does not provide any protection for any conduct or as to any matter or proceeding outside the scope of the agreement.

As noted in the deferred prosecution agreement, in addition to addressing UBS's role in designing and facilitating this scheme, the Department is also assisting the IRS in determining the identities of the United States taxpayers involved. On July 1, 2008, the United States District Court in Miami authorized the IRS to serve upon UBS a "John

Doe” summons seeking records that would identify all United States taxpayers with accounts at UBS in Switzerland who have elected to conceal the existence of their accounts from the IRS. On July 21 2008, the IRS served the summons on UBS.

On February 19, 2009, the government filed a petition to enforce the “John Doe” summons with the United States District Court in Miami. The government requested that the court issue an order requiring UBS to disclose to the IRS the identities of the bank’s United States customers with undeclared Swiss accounts. The suit alleges there may be as many as 52,000 undeclared accounts with approximately \$14.8 billion in assets as of the mid-2000s. This case is currently pending with the district court, and therefore, we are not in a position to provide additional information at this time.

It is important to remember that the vast majority of Americans voluntarily pay their taxes on time and in full. At a time when millions of Americans are losing their jobs, their homes, and their health care, it is deeply troubling that thousands of the wealthiest among us have actively sought to evade their civic and legal duty to pay taxes. The Department of Justice is committed to doing all that it can to aid the IRS in locating those who would seek to hide behind secret accounts and in holding them accountable under the federal tax laws and we greatly appreciate your interest in and support of our efforts.

Thank you for this opportunity to testify before the Subcommittee, and I am happy to take your questions, within the parameters that I have outlined.