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A leading Jersey lawyer assesses the possible impact of changes mooted by the President-elect
On 17 February 2007, American Senator Carl Levin introduced a Bill entitled the 'Stop Tax Haven Abuse Act'. It contains provisions aimed at combating what Levin described as the $100 billion per year drain on the US Treasury from offshore tax abuse. When Levin introduced the Bill he did so with the stated support of two other senators: an individual called Coleman and one Barack Obama, the President-elect of the United States.

On 22 September, in a speech in Wisconsin, Obama said, "We lose $100 billion every year because corporations get to set up mailboxes offshore so that they can avoid paying a dime of taxes in America. Imagine if you got to do that……I will shut down those offshore tax havens and corporate loopholes as President, because you shouldn't
have to pay higher taxes because some big corporation cut corners to avoid paying theirs." Since Obama has subsequently made it to the White House many commentators consider the Bill may gather an unstoppable momentum.

The Bill is not only bullish in its aim, which is to prevent tax evasion. Its prime target is 'offshore secrecy jurisdictions'. This is defined as jurisdictions which, in the judgment of the Treasury Secretary, have 'corporate, business, bank, or tax secrecy rules and practices which… unreasonably restrict the ability of the United States to obtain information relevant to enforcement'. As well as providing a statutory framework to determine what an 'offshore secrecy jurisdiction' is, the Bill includes a list of 34 countries which will, upon enactment, be automatically considered as such. The list includes Jersey, Guernsey and Isle of Man.

The 'rules and practices' referred to within the definition are those that inhibit access of law enforcement and tax administration authorities to information on beneficial ownership or 'other financial information'. The latter appears to be a strikingly broad description.

The existence of a treaty on tax information exchange or another agreement will be considered a sufficiently 'effective information exchange practice' where it provides for 'prompt, obligatory and automatic exchange of information foreseeably relevant to the treaty, and such information is adequate to prevent tax evasion in the United States'.
Another quite broad definition. It is clear that the dice are being loaded in favour of the US authorities with limited rights of appeal or challenge, or at least without taking significant personal risk.

The Secretary can also take into account whether or not the country has been identified as uncooperative by an inter-governmental group, or organisation of which the US is a member. Whilst some may argue that this is a sound basis for making such a determination, the fact remains that some of the countries on the list, such as Jersey, have not been identified as uncooperative by any respected international organisation (quite the contrary).

Content of the Bill

Whilst it is not possible to detail every provision contained in the Bill, it is important to outline some of the key measures contained within it. The Bill is split into four sections. The first, and main, section is titled 'deterring the use of tax havens for tax evasion'. It creates a rebuttable presumption, for internal revenue code and securities law purposes, that a US person who either formed, transferred assets to, was beneficiary of or received money or property from an entity in an offshore secrecy jurisdiction exercised control over that entity, irrespective of the corporate veil. Consequently, any amount or thingof value received from an offshore secrecy jurisdiction represents that person's income, and is thereby taxable. The Bill effectively creates a blacklist, inclusion on which would undoubtedly impact upon the ability of a listed jurisdiction to operate in the global financial market, especially where US dollars are involved.

Amongst the array of penal measures, the Bill also combines extensions to time limits for investigations where offshore secrecy jurisdictions are involved. The Bill also proposes heavy evidential burdens of rebutting a presumption, which will act as a powerful disincentive. Such burdens include measures such as not permitting evidence from non-US persons, unless the person appears to testify in proceedings and limiting legal opinion protection. Unregistered investment companies in the form of hedge funds are also not immune from the attentions of the Treasury, requiring AML procedures to be introduced and the same level of record production to be expected.

Whereas the usual rule is that any foreign account holding $10,000 or more has to be reported to the IRS, the Bill creates a presumption that an account in an offshore secrecy jurisdiction does contain sufficient funds to trigger the reporting requirement.

In a further move by the Treasury to extend the reach of US law, the Bill also provides that the Treasury would be able to extend sanctions currently available to it under the Patriot Act in respect of money laundering, to entities which are 'impeding US tax enforcement'. Anyone who is familiar with the Patriot Act will understand the impact this will have.

The second section is titled 'other measures to combat tax haven and tax shelter abuses'. It includes provision to strengthen summonses in cases involving offshore secrecy jurisdictions. It creates a presumption that there is a reasonable basis for believing that any person or group or class of persons who have financial accounts in, or transactions related to, offshore secrecy jurisdictions, may have failed to comply with internal revenue laws. The penalty for every breach of US Security law is increased to $1 million.

Sections three and four are entitled 'preventing abusive tax shelter transactions' and 'requiring economic substance'. As their titles suggest, these stipulations are aimed at restricting the use of creative tax structures through increased penalties and information sharing, whilst codifying and strengthening the requirement to demonstrate meaningful economic substance to transactions which will otherwise be invalidated. Treasury estimates are that this will raise US$17.7bn over 10 years.

Conclusions and comment

In July 2007, Guernsey sent a delegation to the US in protest at its proposed inclusion on the blacklist. The jurisdiction pointed out that it had, in fact, entered into a tax information sharing agreement with the US.

Barbados has pointed out that it has a 24 year old taxation treaty with the US. Guernsey and

Barbados are not alone in feeling that their inclusion is without merit.

The Coalition for Tax Competition, admittedly not an impartial observer, has pointed out that the Bill, if enacted, would actually harm the US. This is because it would place its citizens at a competitive disadvantage with foreign nationals - including those operating within the US - and in any event is anti-competitive and in breach of the US's trade obligations pursuant to the WTO.

From a UK perspective, the Bill should ring alarm bells for all those that represent entities or individuals who have dealings with the US and the blacklisted countries, either directly or through subsidiaries.

There is no doubt that the personal and corporate civil and criminal risk exposure will rise if the Bill is passed into law. For anyone who has dealt with the US authorities, from FCPA violations to Department of Justice actions, the consequences of failing to adhere to US legislation can be extremely costly.

Senator Levin has identified the need for legislation to combat tax evasion. Few would disagree, in light of some of his findings, that the existing law needs to be strengthened. This Bill may well help to reduce the incidence of tax evasion. Unfortunately, it goes too far. It is anti-competitive and will prevent legitimate individuals utilising the services of legitimate financial services.

The main problem is that it combines the creation of an incredibly draconian regime whilst blacklisting countries to which that regime applies on little more than a whim. The automatic listing of 34 countries, made with no clear justification or reasoning, only serves to highlight the potential arbitrariness.

There are dangers in this approach. Many reputable centres including Jersey, Guernsey and Isle of Man have made big strides over the past decade to meet international standards and dispel toxic business. They have been recognised for doing so by numerous international standard setting bodies.

There is nothing in this Bill that recognises or rewards them. Quite the opposite. Neither the Bill nor the Senate Subcommittee report that preceded it makes any mention of the criminal abuse of Delaware LLC's. These are governed by rules on disclosure of beneficial ownership that were outlawed in the Crown Dependencies ten years ago. This inevitably will deepen suspicion that the Bill is not in fact motivated by a desire to stamp out the abuse of offshore financial services, but by a need for the US to begin to exercise control over large pools of development capital. Then again it could be a mere coincidence that the Bill has gathered momentum as the US economy has bombed and Main Street holds more sway than Wall Street.