

Article

The International Response to the U.S. Tax Haven

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The Pandora Papers and recent empirical studies have revealed large movements of capital from traditional tax havens to the United States in the past several years. This Article examines the legal factors that have led to the rise of the United States as one of the world’s preeminent tax havens and considers why previous efforts have failed to change this emerging reality. Drawing upon the U.S. enforcement model vis-à-vis financial institutions in other countries, this Article proposes that several governments adopt a coordinated response of engaging directly with U.S. financial institutions without requiring any action from the U.S. government. This model response could be applied beyond tax to resolve cooperation problems in other international settings.

INTRODUCTION	178
I. THE EMERGENCE OF THE UNITED STATES AS A TAX HAVEN	184
A. U.S. Enforcement Efforts and FATCA	184
B. The International Adoption of CRS	189
C. The Rise of the United States as a Tax Haven	190
1. The United States’ Unique Financial Secrecy Position	191
2. Low or No Taxation of Foreigners with U.S. Structures	193
3. Characteristics of a Tax Haven	195
4. The Pandora Papers and Empirical Evidence	197
5. Parallels between U.S. FIs and Swiss Banks	199
6. The Illegality of Aiding and Abetting Foreign Tax Evasion	200
II. PROPOSED INTERNATIONAL RESPONSE	201
A. The Failure of the EU’s Blacklisting Threat	202
B. Proposal for CRS Enforcement Model	203
1. Coordinated Response of Like-Minded Countries	204
2. Registration and CRS FI Agreement	205
3. Due Diligence Obligations	206
4. Reporting Obligations	207
5. Penalties on Non-Participating FIs	208
6. Ensuring Compliance among Participating FIs	210

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C. Advantages, Critiques, and the Potential U.S. Response	212
III. WIDER APPLICATIONS	216
A. Regulatory Fail-Safes, Advantages, and Concerns	218
B. Potential Applications.....	220
CONCLUSION.....	222

INTRODUCTION

When the National Assembly of Ecuador passed a law in 2017 prohibiting politicians from holding assets in tax havens, presidential hopeful Guillermo Lasso promptly moved his shares of tax haven companies from secretive foundations in Panama to trusts he settled in South Dakota.¹ Lasso's move was revealed in the Pandora Papers, published in October 2021.² Following the publication of the Pandora Papers, Lasso, who has served as the president of Ecuador since May 24, 2021, was investigated by Ecuador's attorney general for possible tax fraud.³ Lasso has denied any wrongdoing.⁴ Irrespective of the legality of Lasso's actions, holding financial assets in the United States would generally affect the Ecuadorian authorities' ability to ever learn about these South Dakota trusts and the assets they hold. While the Ecuadorian tax authorities receive information from various countries, including Panama, on the financial accounts of Ecuadorian tax residents holding financial assets abroad, they do not receive similar information from the United States.⁵ Absent leaks, the holding of assets under a U.S. trust would likely keep information about them out of the eye of the authorities.⁶

Lasso is not alone. The Pandora Papers, published in October 2021,⁷ have revealed that wealthy individuals from Latin America and beyond have shifted their assets from "traditional" tax havens to the United States⁸—a trend confirmed by empirical data.⁹ Some of these individuals have checkered pasts

1. Int'l Consortium of Investigative Journalists, *Offshore Havens and Hidden Riches of World Leaders and Billionaires Exposed in Unprecedented Leak* (Oct. 3, 2021), <https://www.icij.org/investigations/pandora-papers/global-investigation-tax-havens-offshore/>.

2. For more on the Pandora Papers, see Int'l Consortium of Investigative Journalists, *Pandora Papers*, <https://www.icij.org/investigations/pandora-papers/> (last visited July 7, 2023).

3. See Ellen Francis, *Ecuador's President Faces Tax Investigation After Pandora Papers*, WASH. POST (Oct. 22, 2021), <https://www.washingtonpost.com/world/2021/10/22/ecuador-president-tax-investigation-pandora-papers/>. The consequences of this and other investigations have been mixed. See Brenda Medina, *Ecuador President Survives Removal Effort by National Assembly Following Pandora Papers Revelations* (Dec. 8, 2021), <https://www.icij.org/investigations/pandora-papers/ecuador-president-survives-removal-effort-by-national-assembly-following-pandora-papers-revelations/>.

4. See Francis, *supra* note 3.

5. Panama commenced exchanges with CRS members in 2018. See OECD, PEER REVIEW OF THE AUTOMATIC EXCHANGE OF FINANCIAL ACCOUNT INFORMATION 2020, at 271 (2020).

6. Ecuador committed to beginning automatic exchanges of information in 2021. See OECD, TAX TRANSPARENCY IN LATIN AMERICA 2021, at 66 (2021). The transfer of assets in 2017 predated Ecuador's adoption of the automatic exchange of information standard.

7. See Int'l Consortium of Investigative Journalists, *supra* note 2.

8. See Int'l Consortium of Investigative Journalists, *supra* note 1.

9. See *infra* Section I.C.3.

and finances with murky origins. For example, one Colombian textile magnate opened a South Dakota trust despite his earlier involvement in a drug trafficking and money laundering operation.¹⁰

The United States' surprising rise as a tax haven has occurred at a time when tax havens have faced increasing scrutiny for their role in facilitating global tax abuse. Since the 2007–2008 Global Financial Crisis, the United States has undertaken decisive action demanding greater transparency from some of these tax havens by penalizing their financial institutions (FIs) and pressuring them to comply with the U.S. tax transparency regime.¹¹ However, as discussed below, the U.S. government's rejection of international tax transparency standards has allowed the United States itself to emerge as the world's preeminent financial secrecy destination.¹² One Bloomberg editorial stated that “[w]hile the rest of the world provides the transparency that the [United States] demanded, the [United States] is rapidly becoming the new Switzerland.”¹³ The United States now tops the Tax Justice Network's financial secrecy list, above places such as Switzerland and the British Virgin Islands.¹⁴

How did the United States—once the world's principal advocate for tax transparency and a leader in the fight against tax evasion—become the tax haven it is today? Much of it boils down to the United States' refusal to join the Common Reporting Standard (CRS), a multilateral tax standard for the automatic exchange of financial account information (AEOI), designed by the Organisation for Economic Co-operation and Development (OECD) to increase global tax transparency.¹⁵ Ironically, CRS was modeled after the United States' own Financial Account Tax Compliance Act (FATCA).¹⁶ Enacted by Congress in 2010 and effective since July 2014,¹⁷ FATCA helps ensure that the Internal Revenue Service (IRS) receives information on the overseas financial accounts of U.S. persons by requiring foreign financial institutions (FFIs) to share data on accounts held by U.S. persons with the IRS. The ultimate objective of this law was to make it difficult for U.S. persons to hide their income and assets from the

10. See Will Fitzgibbon, Debbie Cenziper & Salwan Georges, *Suspect Foreign Money Flows into Booming American Tax Havens on Promise of Eternal Secrecy* (Oct. 4, 2021), <https://www.icij.org/investigations/pandora-papers/us-trusts-offshore-south-dakota-tax-havens/>.

11. See *infra* Section I.A.

12. *Id.*

13. *The U.S. Is Becoming the World's New Tax Haven*, BLOOMBERG (Dec. 28, 2017), <https://www.bloomberg.com/opinion/articles/2017-12-28/the-u-s-is-becoming-the-world-s-new-tax-haven>; see also John Richardson, *The Pandora Papers, FATCA, CRS and How They Have Combined to Create Tax Haven USA*, TAX CONNECTIONS (Oct. 6, 2021), <https://www.taxconnections.com/taxblog/the-pandora-papers-fatca-crs-and-how-they-have-combined-to-create-tax-haven-usa/>; John Richardson & Jimmy Sexton, *Tax Haven USA: Why the USA is a Great Place to Invest for Nonresident Aliens and How These Investments Might Be Structured*, PREP PODCASTER (Nov. 12, 2020), https://www.podbean.com/media/share/pb-zzjyb-f5184b?utm_campaign=w_share_ep&utm_medium=dlink&utm_source=w_share#.YV2VrPFA7Mo.twitter.

14. See *infra* note 155 and accompanying text.

15. See OECD, STANDARD FOR AUTOMATIC EXCHANGE OF FINANCIAL ACCOUNT INFORMATION IN TAX MATTERS (2014) [hereinafter CRS].

16. See *infra* Section I.B.

17. Hiring Incentives to Restore Employment Act, Pub. L. No. 111-147, §§ 501–535, 124 Stat. 71, 97–115 (2010).

IRS through the holding of offshore financial accounts.¹⁸ FFIs were pressured to comply with FATCA obligations under the threat of steep penalties in the form of withholding taxes.¹⁹

After the United States enacted FATCA, other countries became interested in developing similar transparency standards. The OECD took the lead and developed CRS, which was published in 2014.²⁰ CRS was quickly adopted by more than one hundred jurisdictions globally.²¹ Under CRS, countries share data with each other regarding the financial accounts of their respective tax residents. Unlike FATCA, CRS is generally reciprocal.²² For example, under the CRS exchange relationship between France and Japan, the Japanese tax authority provides the French government with information about French tax residents who hold financial accounts in Japanese FIs, and vice versa. FATCA, on the other hand, is primarily unidirectional, with nearly all of the data flowing into the United States. FATCA does allow for some reciprocity, but the information the United States shares with partner countries is very limited.²³ Consequently, foreigners holding financial accounts in the United States can easily avoid reporting.²⁴ Attempts by the Obama Administration to make FATCA fully reciprocal did not materialize.²⁵ A pressure campaign launched by the European Union (EU) to force the United States to adopt CRS has also failed.²⁶

This Article examines the legal factors that have led to the United States arriving at its current status as a tax haven. First, non-U.S. FIs can no longer offer financial secrecy due to CRS, thereby making them less attractive secrecy destinations.²⁷ Second, the United States itself offers financial secrecy and provides no meaningful information reporting to other countries. Third, foreigners with no ties to the United States can hold assets through U.S. structures while paying little to no U.S. federal, state, and local tax on their profits.²⁸ This stands in stark contrast to the treatment of U.S. taxpayers holding similar structures.²⁹ This Article examines the United States' characteristics as a tax haven³⁰ as well as the evidence documented in the Pandora Papers and new empirical studies.³¹ It also draws parallels between the conduct of Swiss banks a

18. *Id.*

19. *Id.*

20. *See infra* Section I.B.

21. For an updated list of CRS-implementing countries and jurisdictions, see OECD, *CRS by Jurisdiction*, <https://www.oecd.org/tax/automatic-exchange/crs-implementation-and-assistance/crs-by-jurisdiction/> (last visited July 7, 2023).

22. *See* CRS, *supra* note 15, ¶ 3. Under CRS, jurisdictions that do not wish to receive the CRS information of their tax residents' offshore financial accounts (e.g., jurisdictions with no income tax) can agree to provide CRS data to other countries unilaterally. The majority of countries that implement CRS do so on a reciprocal basis.

23. *See infra* Section I.A.

24. *See infra* Sections I.A and I.C.

25. *See infra* note 97 and accompanying text.

26. *See infra* Section II.A.

27. *See infra* Section I.C.1.

28. *See infra* Section I.C.2.

29. *See id.*

30. *See infra* Section I.C.3.

31. *See infra* Section I.C.4.

decade ago, as documented in the U.S. Department of Justice's Swiss Bank Program, and that of U.S. FIs today.³²

These developments underscore an unresolved challenge in the international governance framework: How can countries respond when another country's non-participation in an international standard threatens the efficacy of that standard and harms them? This Article proposes a solution that could address this problem in certain contexts such as global tax transparency. A considerable advantage compared to other proposals is that this proposed policy response does not require any action from the U.S. government.³³

This Article proposes that CRS take a page out of the U.S. playbook. Although CRS was inspired by the United States' FATCA, it does not contain many of FATCA's enforcement provisions.³⁴ The United States has been able to achieve compliance with FATCA by taking a dual approach to enforcement that engages both FFIs and foreign governments. The United States has entered into over one hundred bilateral intergovernmental agreements (IGAs) with other governments who have become responsible for enforcing FATCA within their borders through domestic legislation.³⁵ However, where governments did not enter into IGAs, the United States has demanded compliance from FFIs directly. The FATCA regulations require that FFIs register with the IRS and comply with the terms of an "FFI Agreement."³⁶ An FFI Agreement is a standard agreement between each FFI and the IRS for the implementation of the FATCA compliance obligations.³⁷ FFIs that do not enter into an FFI Agreement or those that enter into the agreement but fail to comply with its terms are subject to steep penalties in the form of withholding taxes on payments made to them. In contrast, CRS

32. See *infra* Section I.C.5.

33. For proposals that aim to pressure the U.S. government into adopting reciprocal information exchange, see Tax Just. Network, *Why Europe Should Impose Withholding Taxes on Payments, to Crack Open Secretive Tax Havens* (Jan. 21, 2016), <https://www.taxjustice.net/wp-content/uploads/2013/04/TJN2016-WithholdingTax.pdf>; Markus Meitzer, *Automatic Exchange of Information as the New Global Standard: the End of (Offshore Tax Evasion) History?*, at 1, 19-20 (Feb. 27, 2017). However, gaining leverage over the U.S. government on financial matters can be a difficult, if not impossible, task for less powerful countries given the central importance of the United States in global capital markets. See LUKAS HAKELBERG, *THE HYPOCRITICAL HEGEMON: HOW THE UNITED STATES SHAPES GLOBAL RULES AGAINST TAX EVASION AND AVOIDANCE* 104 (2020). As an alternative, this Article suggests targeting U.S. FIs themselves and avoiding a confrontation with the U.S. government directly.

34. See *infra* Section I.A and Part II for a discussion on the differences between FATCA and CRS and the required adaptations.

35. U.S. Dep't of Treasury, *Foreign Account Tax Compliance Act*, <https://home.treasury.gov/policy-issues/tax-policy/foreign-account-tax-compliance-act> (last visited July 7, 2023).

36. Treas. Reg. § 1.1471-4.

37. An FFI Agreement is also required for FFIs in Model 2 Jurisdictions. See U.S. Dep't of Treasury, *Model 2 IGA, Preexisting TIEA or DTC*, art. 3, §1 (June 6, 2014), <https://www.treasury.gov/resource-center/tax-policy/treaties/Documents/FATCA-Model-2-Agreement-Preexisting-TIEA-or-DTC-6-6-14.pdf> [<https://perma.cc/G3H5-3SUP>]. It is important to emphasize the significance of FFI Agreements as an extraterritorial extension of the IRS's regulatory power. See HAKELBERG, *supra* note 33, at 89 ("Congress had conceived FATCA as a domestic law with extraterritorial reach, establishing a direct regulatory link between FFIs and the IRS."). Later, the United States would adopt an intergovernmental approach with the direct link between FFIs and the IRS as a backstop. See *infra* Section I.A.

obligations are imposed by each government on its domestic FIs.³⁸ Countries do not engage directly with FIs in other jurisdictions.³⁹ Consequently, FIs in countries that have not joined CRS can hide behind the intransigence of their governments.

Building on the FATCA model, this Article proposes that a group of several CRS-implementing countries could incentivize FIs in non-cooperative countries—such as the United States—to comply with the CRS due diligence and reporting obligations.⁴⁰ An FI that agrees to undertake the CRS obligations will need to enter into a “CRS FI Agreement” detailing the applicable due diligence and reporting obligations, similar to the FFI Agreement under FATCA.⁴¹ FIs that do not comply with the CRS obligations would be subject to withholding taxes or other penalties established by the countries that adopt this mechanism.⁴²

This approach could lead to the compliance of U.S. FIs with CRS without requiring any action from the U.S. Congress or Treasury.⁴³ The same would be true for FIs in any other country that refuses to cooperate with CRS.⁴⁴ The implementation of this mechanism by several CRS-implementing countries could be accomplished through a multilateral agreement in the same manner as other recent changes to CRS.⁴⁵ Achieving U.S. reciprocal financial account reporting would make it harder for foreigners to use the U.S. financial system for tax evasion. It would also enable further scrutiny of funds hidden within the United States that, as suggested by the Pandora Papers, may be associated with money laundering, corruption, and other illicit activities.⁴⁶

38. See *infra* Section I.B.

39. CRS uses the term FI, or financial institution, whereas the United States uses FFI, or foreign financial institution (i.e., an FI that is not a U.S. FI).

40. See *infra* Part II.

41. *Id.*

42. The importance of including such defensive measures in a multilateral system of AEOI has been advocated in the literature previously. See Itai Grinberg, *The Battle Over Taxing Offshore Accounts*, 60 UCLA L. REV. 304, 379-80 (2012) (“A multilateral regime that realistically intends to ensure global compliance should require all participating jurisdictions to impose some defensive measure. . . . Otherwise, noncooperative jurisdictions and institutions benefit from defecting from the emerging regime because they can become repositories of choice for tax evader assets without paying a significant price for making that business decision.”); Itai Grinberg, *Taxing Capital Income in Emerging Countries: Will FATCA Open the Door?*, 5 WORLD TAX J. 325 (2013).

43. While this proposal would expand compliance with CRS, it would not resolve other loopholes within the CRS framework that should be addressed. See, e.g., Noam Noked, *Tax Evasion and Incomplete Tax Transparency*, 7 LAWS (2018); Menusch Khadvaji & Marjolein Vertelman, *Closing Pandora’s Box: How to Improve the Common Reporting Standard* (Kiel Inst. for the World Econ., Working Paper No. 2223, 2022).

44. Exceptions can and should be made for developing countries that do not join CRS for external reasons such as a lack of resources to implement the standard. See *infra* notes 112, 194.

45. For example, the automatic exchange of information framework for the Model Mandatory Disclosure Rules for CRS is being implemented via a multilateral competent authority agreement (MCAA). See OECD, INTERNATIONAL EXCHANGE FRAMEWORK FOR MANDATORY DISCLOSURE RULES ON CRS AVOIDANCE ARRANGEMENTS AND OPAQUE OFFSHORE STRUCTURES (2019). Also, the Crypto-Asset Reporting Framework (CARF) will be implemented through “a framework of bilateral or multilateral competent authority agreements or arrangements for the automatic exchange of information collected under the CARF.” OECD, CRYPTO-ASSET REPORTING FRAMEWORK AND AMENDMENTS TO THE COMMON REPORTING STANDARD 7 (2022).

46. See, e.g., Fitzgibbon et al., *supra* note 10; see also *infra* Section II.C.

There are several reasons to believe that this proposal could succeed where previous attempts, such as the EU's blacklisting threat in 2019, have failed.⁴⁷ First, this focused measure only applies to U.S. FIs and FIs in other non-cooperative countries. The proposed mechanism aims to elicit the compliance of these FIs with CRS's due diligence and reporting obligations; it does not penalize them for their governments' inaction. Second, this proposal's success does not require any action by the U.S. Congress or Treasury. Based on the experience with FATCA, the U.S. government is more likely to enact legislative changes *after* other countries adopt the mechanism proposed here. Third, as this mechanism is a focused and constructive measure, it is unlikely to rattle financial markets and damage the economies of the United States and other countries. For these reasons, it is less likely to prompt retaliatory actions by the U.S. government. Moreover, the U.S. government has repeatedly acknowledged "the need to achieve equivalent levels of reciprocal automatic information exchange."⁴⁸ It is unclear on what grounds it could object to the mechanism suggested here, which levels the playing field and achieves reciprocal information exchange by adopting the same enforcement model that the United States itself applies to other countries.

While the proposed mechanism may be more effective than other measures, it is still uncertain whether a group of countries would adopt it. Some countries harmed by tax evasion and illicit financial flows may be unable or unwilling to act. This Article expands on these considerations and assesses other potential critiques and objections.

The model response explored here potentially has applications well beyond tax transparency. As discussed in Part III, this model has several key elements, none of which are specific to tax. First, a group of like-minded countries adopts rules imposing obligations on certain non-governmental actors in a non-cooperative country or countries.⁴⁹ Second, these actors can either comply with these obligations or face penalties imposed by the group of countries. Third, the obligations facilitate direct engagement between the group and the participating actors. Fourth, participating actors are monitored to ensure their compliance with the applicable requirements.⁵⁰ A mechanism comprising these elements could be adopted in other tax reporting regimes and non-tax regimes, such as corporate climate disclosures.⁵¹ This discussion expands the scholarship which has recently identified the importance of fiscal and regulatory "fail-safes" in the enforcement and broad application of recent international tax reforms.⁵²

This Article is divided into three parts. Part I examines how the United States has emerged as one of the world's preeminent tax havens. Part II details

47. See *infra* Section II.C.

48. See *infra* text accompanying note 94.

49. For further discussion on how like-minded countries can coordinate their tax policies, see H. David Rosenbloom, Noam Noked & Mohamed S. Helal, *The Unruly World of Tax: A Proposal for an International Tax Cooperation Forum*, 15 FLA. TAX REV. 57 (2014).

50. See *infra* Part III for a discussion of these elements.

51. See *infra* Section III.B.

52. See Ruth Mason, *The Transformation of International Tax*, 114 AM. J. INT'L L. 353, 376-80 (2020); see also *infra* Section III.A.

the Article's proposal for how several countries can adopt a mechanism modeled after FATCA in order to extend the application of the international transparency standard to U.S. FIs without requiring any action from the U.S. government. Finally, Part III considers how the model response discussed here could apply to other international standards.

I. THE EMERGENCE OF THE UNITED STATES AS A TAX HAVEN

In the wake of the Global Financial Crisis, the United States took decisive action against financial institutions in overseas tax havens and introduced FATCA to curb offshore tax evasion by U.S. taxpayers. Section A discusses FATCA and the Department of Justice's enforcement actions. Section B describes how the rest of the world followed the United States by adopting CRS, a globalized version of FATCA. Section C then examines the legal factors that have led to the United States becoming a top destination for foreigners wishing to hide funds. It also considers whether the United States has the characteristics of a tax haven, emphasizing the evidence documented in new empirical studies and the recently published Pandora Papers.⁵³ Finally, it compares the conduct of Swiss banks a decade ago, as recorded in the U.S. Department of Justice's Swiss Bank Program, to that of U.S. FIs today.⁵⁴

A. U.S. Enforcement Efforts and FATCA

The U.S. government's efforts to curb offshore tax evasion intensified in the aftermath of the Global Financial Crisis. As discussed below, these efforts included investigating and prosecuting tax evaders and the financial institutions that aided and abetted their tax crimes. In 2009, UBS, a Swiss bank, entered into a deferred prosecution agreement with the U.S. Department of Justice.⁵⁵ Under this agreement, the bank agreed to pay a fine of 780 million U.S. dollars and disclose the information of its 52,000 U.S. clients, many of whom had failed to comply with their U.S. tax reporting obligations concerning their offshore accounts.⁵⁶ The UBS scandal was only the first act of the Department of Justice's Offshore Compliance Initiative, an ongoing program that has since expanded to investigate and prosecute various financial institutions and tax evaders.⁵⁷

The Department of Justice announced the "Swiss Bank Program" in 2013.⁵⁸ Under this program, eighty-four Swiss banks entered into non-

53. See *infra* Section I.C.

54. See *id.*

55. See U.S. Dep't of Just., *UBS Enters into Deferred Prosecution Agreement* (Feb. 18, 2009), <https://www.justice.gov/opa/pr/ubs-enters-deferred-prosecution-agreement>; see also J. Richard (Dick) Harvey Jr., *Offshore Accounts: Insider's Summary of FATCA and Its Potential Future*, 57 VILL. L. REV. 471, 476-79 (2012).

56. See *id.*

57. See U.S. Dep't of Just., *Offshore Compliance Initiative*, <https://www.justice.gov/tax/offshore-compliance-initiative> (last visited July 7, 2023).

58. See U.S. Dep't of Just., *Swiss Bank Program*, <https://www.justice.gov/tax/swiss-bank-program> (last visited July 7, 2023). The U.S. prosecution of Swiss banks was important in ending abuses in Switzerland and in galvanizing international efforts for tax transparency. See Patrick Emmenegger,

prosecution agreements under which they were required to:

[m]ake a complete disclosure of their cross-border activities; [p]rovide detailed information on an account-by-account basis for accounts in which U.S. taxpayers have a direct or indirect interest; [c]ooperate in treaty requests for account information; [p]rovide detailed information as to other banks that transferred funds into secret accounts or that accepted funds when secret accounts were closed; [a]gree to close accounts of account holders who fail to come into compliance with U.S. reporting obligations; and [p]ay appropriate penalties.⁵⁹

In addition to Swiss banks, the Department of Justice investigated and imposed hefty fines on financial institutions in other countries.⁶⁰

In conjunction with these enforcement efforts, the U.S. government sought to adopt a mechanism to ensure the routine identification and reporting to the IRS of U.S. persons holding financial accounts offshore. For this purpose, Congress enacted FATCA in 2010 as part of the Hiring Incentives to Restore Employment Act.⁶¹ FATCA became effective in July 2014.⁶² Many of the FATCA obligations were detailed in the U.S. Treasury's FATCA regulations.⁶³ FATCA requires FFIs to comply with certain registration, due diligence, reporting, and withholding obligations with the aim of identifying U.S. account holders and reporting them to the IRS annually.⁶⁴ The reported information must include the U.S. account holder's personal information, account balance, and income information.⁶⁵ There is evidence indicating that FATCA has reduced offshore tax evasion by U.S. persons.⁶⁶

FATCA creates strong incentives for FFIs to comply with it: if they fail to comply, they will face a withholding tax of 30% on certain payments made to

Swiss Banking Secrecy and the Problem of International Cooperation in Tax Matters: A Nut Too Hard to Crack?, 11 REG. & GOVERNANCE 24 (2017); Patrick Emmenegger & Katrin Eggenberger, *State Sovereignty, Economic Interdependence and US Extraterritoriality: The Demise of Swiss Banking Secrecy and the Re-Embedding of International Finance*, 21 J. INT'L REL. & DEV'T 798 (2018).

59. *Id.* For further discussion on the Swiss Bank Program, see Marnin Michaels et al., *The DOJ's Swiss Bank Program*, PRACTICAL L. (2016).

60. For example, three Israeli banks entered into non-prosecution agreements with the Department of Justice and paid substantial fines. See U.S. Dep't of Just., Tax Division, FY 2022 Congressional Budget (2022), <https://www.justice.gov/jmd/page/file/1398551/download>.

61. Pub. L. No. 111-147, § 501-35, 124 Stat. 71, 97-115 (2010). For further discussion on FATCA, see Reuven S. Avi-Yonah & Gil Savir, *Find It and Tax It: From TIEAs to IGAs* (Mich. Law Pub. Law & Legal Theory Research Paper Series, Paper No. 443, 2015); Joshua D. Blank & Ruth Mason, *Exporting FATCA*, 142 TAX NOTES 1245, 1245 (2014); WILLIAM H. BYRNES, LEXISNEXIS GUIDE TO FATCA AND CRS COMPLIANCE (2021); Grinberg, *The Battle over Taxing Offshore Accounts*, *supra* note 42, at 334-39; S. Bruce Hiran, *Overview of FATCA*, 152 TAX NOTES 1297, 1298 (2016); Young Ran (Christine) Kim, *Considering "Citizenship Taxation": In Defense of FATCA*, 20 FLA. TAX REV. 335, 359-70 (2017); Shu-Yi Oei, *The Offshore Tax Enforcement Dragnet*, 67 EMORY L.J. 655, 682-84, 689-93 (2018); Niels Johannesen, Daniel Reck, Max Risch, Joel Slemrod, John Guyton & Patrick Langetieg, *The Offshore World According to FATCA: New Evidence on the Foreign Wealth of U.S. Households* (Nat'l Bureau of Econ. Rsch., Working Paper, No. 31055, 2023).

62. IRS, Summary of FATCA Timelines, <https://www.irs.gov/businesses/corporations/summary-of-fatca-timelines> (last visited July 7, 2023).

63. Treas. Reg. §§ 1.1471-1.1474.

64. *Id.* FATCA requires reporting of accounts held by "specified U.S. persons." Treas. Reg. § 1.1473-1(c).

65. Treas. Reg. § 1.1471-4(c); Rev. Proc. 2017-16, 2017-3 I.R.B. 501.

66. See, e.g., Lisa de Simone, Rebecca Lester & Kevin Markle, *Transparency and Tax Evasion: Evidence from the Foreign Account Tax Compliance Act (FATCA)*, 58 J. ACCOUNT. RES. 105 (2020) (documenting a decrease in round-tripping investments associated with tax evasion by U.S. persons).

them.⁶⁷ FFIs are required to register with the IRS through the IRS FATCA webpage.⁶⁸ As part of the registration, the FFI is assigned a Global Intermediary Identification Number (GIIN)⁶⁹ and accepts the terms of the standard FFI Agreement, including the FATCA due diligence, reporting, and withholding obligations.⁷⁰ Where a corporate group comprises more than one FFI, FATCA generally requires the whole expanded affiliated group (EAG)⁷¹ to comply with FATCA in order for any particular relevant FFI in the group to be considered compliant.⁷² Additionally, certain withholding obligations may apply when compliant FFIs make payments to non-participating FFIs.⁷³

The due diligence obligations under FATCA center around the identification and documentation of U.S. account holders and controlling persons of financial accounts.⁷⁴ Participating FFIs (i.e., FFIs compliant with FATCA) are required to review all of their accounts to determine whether they are held by U.S. persons, non-participating FFIs, or recalcitrant account holders.⁷⁵ FFIs must follow specific procedures when opening new accounts to determine if they are reportable, and they must screen preexisting accounts for various U.S. indicia.⁷⁶ If such indicia are identified, or if the FFI has some other indication that the account holder may be U.S.-affiliated, the FFI must report the account to the IRS.⁷⁷ Variations on these requirements exist for individual, entity, preexisting, and new accounts.⁷⁸ There are different requirements for preexisting high-value and low-value accounts. For example, a preexisting individual account that exceeds one million U.S. dollars is subject to an enhanced review.⁷⁹ FFIs are generally required to obtain self-certification from any new

67. I.R.C. § 1471(b)(1)(D). The rules concerning FATCA withholding are further discussed *infra* Section II.B. FFIs frequently require FATCA self-certifications from other contractual parties and require that other FFIs make contractual representations and warranties that are FATCA compliant. In an interconnected financial industry, non-compliance with FATCA is not a viable option for the vast majority of FFIs. For the practical implications of FATCA for commercial parties, see Slaughter & May, *The ACT Borrower's Guide to the LMA's Investment Grade Agreements* (Sept. 1, 2017). For further discussion, see the text accompanying *infra* note 231.

68. See IRS, FATCA Foreign Financial Institution Registration System, <https://www.irs.gov/businesses/corporations/fatca-foreign-financial-institution-registration-system> (last visited July 7, 2023).

69. Treas. Reg. § 1.1471-1(b)(57).

70. For further discussion on FFI Agreements, see Noam Noked, *FATCA, CRS, and the Wrong Choice of Who to Regulate*, 22 FLA. TAX REV. 77, 85 (2018).

71. Treas. Reg. § 1.1471-5(i). An expanded affiliated group generally includes all the subsidiaries and branches that are owned (more than 50%) under the same parent entity. *Id.*

72. Treas. Reg. § 1.1471-4(a)(4).

73. See *infra* text accompanying notes 227-31.

74. Treas. Reg. § 1.1471-4(c).

75. *Id.* Recalcitrant account holders are account holders that do not fully comply with FATCA-related information requests sought by the FFI. Treas. Reg. § 1.1471-5(g).

76. Treas. Reg. § 1.1471-4(c). These indicia include a designation of the account holder as a U.S. citizen or resident, a U.S. birthplace, a U.S. address, a power of attorney granted to a person with a U.S. address, and others. Treas. Reg. § 1.1471-4(c)(5).

77. Treas. Reg. § 1.1471-4(c)(2). This reporting is required unless the FFI is provided with specific evidence that the account holder is not a U.S. person.

78. Treas. Reg. § 1.1471-4(c).

79. The enhanced review requires FFIs to review additional documents associated with the account. Treas. Reg. § 1.1471-4(c)(5).

account holder.⁸⁰ This self-certification should include specific information, including the account holder's U.S. or non-U.S. status.⁸¹ As noted, FFIs must report information about their U.S. account holders to the IRS annually. For each account holder, the information generally includes their name, address, tax identification number, account number, account balance, and income.⁸²

The FATCA regulations, described at a high level above, provide a framework for the IRS to engage with FFIs directly through FFI Agreements, thereby allowing the United States to implement and enforce FATCA unilaterally.⁸³ Foreign government involvement is not required under this framework. Nevertheless, around July 2014, when FATCA became effective, many governments negotiated and entered into bilateral intergovernmental agreements (IGAs) with the U.S. Treasury for FATCA implementation by FFIs in their countries. The IGAs fall under two categories: Model 1 IGAs and Model 2 IGAs.⁸⁴ Under Model 1 IGAs, FFIs are required to file disclosures with their domestic tax authority, which then shares the information with the IRS.⁸⁵ This reporting mechanism addresses the problem for FFIs that could not report directly to the IRS because doing so would violate local law.

Under Model 2 IGAs, on the other hand, FFIs must enter into an FFI Agreement with the IRS and file their disclosures directly with the IRS.⁸⁶ While the majority of IGAs are Model 1 IGAs, there are a number of important financial centers, such as Hong Kong and Switzerland, that utilize Model 2 IGAs.⁸⁷

The main advantage of IGAs from the perspective of FFIs is that they reduce the risk of FATCA withholding, which is unlikely to apply to compliant FFIs in IGA jurisdictions.⁸⁸ The wide adoption of IGAs means that FATCA is implemented primarily through intergovernmental cooperation. Nonetheless, the unilateral option remains as a backstop when governments refuse to cooperate by entering into IGAs. Part II below discusses several additional FATCA provisions pertinent to the proposal in this Article.

Importantly, FATCA provides for little or no information reporting from the United States to foreign countries. While some IGAs under FATCA are described as "reciprocal," these agreements leave a lot unaccounted for.⁸⁹ For

80. Treas. Reg. § 1.1471-4(c)(4)(i).

81. *Id.*

82. Treas. Reg. § 1.1471-4(d); Form 8966 (available at <https://www.irs.gov/pub/irs-pdf/f8966.pdf>).

83. See Ronen Palan & Duncan Wigan, *Herding Cats and Taming Tax Havens: The US Strategy of 'Not in My Backyard'*, 5 GLOBAL POL'Y 1 (May 2014).

84. See U.S. Dep't of Treasury, *supra* note 35.

85. *Id.*

86. *Id.*

87. *Id.*

88. See Noked, *supra* note 70, at 86.

89. See Peter A. Cotorceanu, *Hiding in Plain Sight: How Non-US Persons Can Legally Avoid Reporting Under Both FATCA and GATCA*, 21 TRS. & TRS. 1050, 1052 (Dec. 2015). For a further breakdown of the asymmetries found in "reciprocal" FATCA IGAs, see Meinzer, *supra* note 33, at 17-19. For a discussion on how the United States' unilateral approach with FATCA hinders full global reciprocity, see Richard Eccleston & Felicity Gray, *Foreign Accounts Tax Compliance Act and American Leadership in the Campaign Against International Tax Evasion: Revolution or False Dawn?*, 5 GLOBAL POL'Y 321 (2014).

instance, FATCA's reciprocal IGAs do not require the United States to share data with partner countries regarding cash accounts that earn less than ten U.S. dollars in interest annually, non-cash accounts that do not earn U.S. source income, or the controlling persons of any entities.⁹⁰ Thus, foreigners can easily avoid reciprocal FATCA reporting. For example, they can avoid reporting by holding U.S. accounts through entities such as U.S. or foreign companies.⁹¹

The way in which FATCA was implemented is partially responsible for the lack of full reciprocity in FATCA IGAs. FATCA, a U.S. tax law, imposes obligations on FFIs unilaterally.⁹² These FFIs then pressured their governments to enter into IGAs with the United States to formalize and simplify the FATCA reporting process and to reduce the risk of withholding.⁹³ While foreign governments could have demanded full reciprocity when negotiating IGAs, the U.S. Treasury was not in a position to deliver it because it would require Congress to pass legislation. If a foreign government refused to adopt an IGA because of the lack of full reciprocity, it would harm its domestic FIs which would still need to comply with FATCA or face penalties. Thus, foreign governments were unable to demand reciprocity from the United States when negotiating the IGAs. All that U.S. officials could do was to include a commitment in the IGAs to strive for full reciprocity in the future. This clause in the IGAs is titled "Reciprocity" and provides the following:

The Government of the United States acknowledges the need to achieve equivalent levels of reciprocal automatic information exchange with [FATCA Partner]. The Government of the United States is committed to further improve transparency and enhance the exchange relationship with [FATCA Partner] by pursuing the adoption of regulations and advocating and supporting relevant legislation to achieve such equivalent levels of reciprocal automatic information exchange.⁹⁴

Despite this stated commitment, the U.S. government has taken no meaningful action to achieve such reciprocity. Notably, achieving reciprocal information exchange would require Congress to enact legislation mandating that U.S. FIs carry out due diligence and report information about their foreign account holders. President Obama proposed legislative amendments to achieve full reciprocity under FATCA.⁹⁵ In a letter to then-House Speaker Paul Ryan, Treasury Secretary Jack Lew stated:

Finally, we must ensure that the United States can live up to its end of the bargain on foreign tax reporting. While the United States led the world by enacting FATCA, currently, the United States does not provide its FATCA partners with the same information about U.S. financial institutions that foreign financial institutions must

90. See Cotorceanu, *supra* note 89, at 1052.

91. See *id.*

92. *Id.* at 1051.

93. *Id.* at 1052.

94. U.S. Dep't of Treasury, Model 1A IGA Reciprocal, Preexisting TIEA or DTC, art. 6, § 1 (Nov. 30, 2014).

95. President Obama included reciprocal FATCA as a component of his 2015, 2016, and 2017 budget proposals. See The White House Office of the Press Secretary, *Fact Sheet: Obama Administration Announces Steps to Strengthen Financial Transparency, and Combat Money Laundering, Corruption, and Tax Evasion* (May 5, 2016); BRUCE ZAGARIS, THE INTERNATIONAL FINANCIAL REGULATION AND ENFORCEMENT REGIME: IMPLICATIONS FOR FINANCIAL INTERMEDIARIES (2017).

provide to the IRS. This is because legislation is needed to require U.S. financial institutions to provide this level of detail. Reciprocity with other jurisdictions is a key component of any successful strategy for combating international tax evasion.⁹⁶

However, the Obama Administration's proposals failed to materialize in Congress.⁹⁷ In fact, these proposals did not even make their way into the Obama Administration's Green Books, the documents detailing the administration's budget proposals.⁹⁸ According to one tax scholar, this indicates that, "[t]he Obama Administration was thus sending a double message on reciprocity: reassuring its international partners by including corresponding requests in the budgets, while appeasing domestic interests by not retaining them in the Green Books."⁹⁹ As further discussed below, foreign countries, civil society organizations, and commentators have criticized the United States for its one-sided approach to information exchange.¹⁰⁰

B. The International Adoption of CRS

Following the United States' adoption of FATCA, other countries wished to implement a similar standard to protect their tax bases from offshore tax evasion.¹⁰¹ CRS was the culmination of this effort. While FATCA was conceived unilaterally by the United States and implemented globally under the threat of withholding taxes, CRS was designed and implemented multilaterally.¹⁰² The OECD and Group of 20 (G20) introduced CRS in 2014.¹⁰³ It provides for reciprocal automatic information exchange between participating jurisdictions. By design, CRS is modeled after the FATCA Model 1 IGA, and many of its terms and compliance obligations mirror those under FATCA.¹⁰⁴ Similar to the requirements under a Model 1 IGA, a local FI must comply with certain due diligence obligations and disclose reportable account holders (i.e., foreign tax residents of reportable jurisdictions) to the domestic tax authority, which passes

96. See Letter from Sec'y of the Treasury Jacob Lew, to Speaker of the House Paul Ryan (May 5, 2016).

97. The final 2015, 2016, and 2017 spending bills lacked Obama's reciprocal FATCA provisions. See Consolidated and Further Continuing Appropriations Act of 2015, Pub. L. No. 113-235, 128 Stat. 2130; Consolidated Appropriations Act of 2016, Pub. L. No. 114-113, 129 Stat. 2242; Consolidated Appropriations Act of 2017, Pub. L. No. 115-31, 131 Stat. 135.

98. See HAKELBERG, *supra* note 33, at 100-04.

99. *Id.* at 101. In contrast, the Biden Administration has retained FATCA reciprocity in its Green Book for 2023. However, it is unclear what path, if any, this proposal has in the Senate. See *infra* note 119.

100. See, e.g., Tax Just. Network, *Financial Secrecy Index 2018, Narrative Report on USA* (2018), <http://www.financialsecrecyindex.com/PDF/USA.pdf>; Nick Shaxson, *Loophole USA: the Vortex-shaped Hole in Global Financial Transparency*, TAX JUST. NETWORK (Jan. 26, 2015), <https://taxjustice.net/2015/01/26/loophole-usa-vortex-shaped-hole-global-financial-transparency-2/>; Craig Rose, *The Biggest Tax Haven of Them All? The U.S., FATCA and the CRS*, BNA (Mar. 29, 2016); Andres Knobel, *The Role of the U.S. as a Tax Haven: Implications For Europe*, TAX JUST. NETWORK (May 11, 2016); Noam Noked, *Should the United States Adopt CRS?*, 118 MICH. L. REV. ONLINE 118 (2019).

101. See CRS, *supra* note 15, at 9-10.

102. See *id.*

103. See *id.*

104. OECD, STANDARD FOR AUTOMATIC EXCHANGE OF FINANCIAL INFORMATION IN TAX MATTERS: IMPLEMENTATION HANDBOOK, at 25 (2015).

on the information to the relevant jurisdictions.¹⁰⁵

Despite their similarities, FATCA and CRS have two key differences relevant to this discussion. One critical distinguishing factor between FATCA and CRS is the former's lack of reciprocity. As noted, the FATCA IGAs do not provide reciprocal information reporting about foreigners holding financial accounts in U.S. FIs.¹⁰⁶ Under CRS, on the other hand, all jurisdictions with an AEOI relationship generally share similar information.¹⁰⁷ Another key difference is that CRS does not include an enforcement mechanism to address situations where a country does not implement CRS. Under FATCA, if a country does not enter into an IGA for the implementation of FATCA, FFIs in that country still need to comply with FATCA; otherwise, they will be subject to FATCA withholding.¹⁰⁸ CRS does not include any similar mechanism.

With the support of the OECD, the G20, and the EU, CRS spread rapidly around the globe, eventually accumulating over 110 participating countries and jurisdictions.¹⁰⁹ Nearly all major economies, including every EU member state, the United Kingdom, China, Russia, India, Brazil, and many others, have been implementing CRS for several years now.¹¹⁰ Even traditional tax havens and financial centers such as the Cayman Islands, British Virgin Islands, Panama, Singapore, and Hong Kong have yielded to international pressure and now implement CRS.¹¹¹ As discussed in the next section, the United States is the glaring exception.¹¹²

C. The Rise of the United States as a Tax Haven

Several legal factors are responsible for the United States' rise as a tax haven for foreigners. First, non-U.S. FIs can no longer offer financial secrecy as a result of CRS. Second, the United States itself offers financial secrecy and no

105. *See id.*

106. *See infra* text accompanying notes 89-91.

107. As noted *supra* note 22, some jurisdictions choose to provide CRS information unilaterally because they are not interested in receiving CRS information about their tax residents.

108. *See supra* text accompanying notes 67, 69, 70.

109. *See* OECD, *CRS by Jurisdiction*, <https://www.oecd.org/tax/automatic-exchange/crs-implementation-and-assistance/crs-by-jurisdiction/> (last visited July 7, 2023).

110. *Id.*

111. *Id.* It is likely that many of these jurisdictions lacked the economic and political clout to ignore international pressure to adopt CRS. Moreover, the threat of EU and OECD blacklisting was likely a potent motivating factor. This can be seen, for example, in the case of Hong Kong. *See, e.g.*, Legislative Council Brief for Inland Revenue (Amendment) Bill 2016, https://www.legco.gov.hk/yr15-16/english/bills/brief/b201601081_brf.pdf ("The legal framework for AEOI is necessary for Hong Kong to pass the peer review conducted by the Global Forum, and to avoid being labelled as an uncooperative tax jurisdiction.") For an analysis of how two other financial centers gave in to international pressure to adopt AEOI, see Katrin Eggenberger & Patrick Emmenegger, *Economic Vulnerability and Political Responses to International Pressure: Liechtenstein, Switzerland and the Struggle for Banking Secrecy*, 21 SWISS POL. SCI. REV. 491 (2015).

112. The United States' significant political and economic influence has allowed it to avoid international pressure (including blacklisting) to adopt reciprocal AEOI. *See infra* Section II.A. It is important to note that many developing countries also do not implement CRS. *See infra* note 115. However, this is likely due to a lack of sufficient resources to effectively collect and share the data required to be exchanged under CRS. The United States does not lack such resources. For more on developing countries and CRS, see Kerrie Sadiq & Adrian Sawyer, *Developing Countries and the Automatic Exchange of Information Standard — A "One-Size-Fits-All" Solution?*, 31 AUSTL. TAX FORUM 99 (2016).

meaningful information reporting to other countries.¹¹³ Third, foreigners can hold assets through U.S. structures while paying little to no U.S. federal, state, and local tax on the profits from these assets.

Sections 1 and 2 below elaborate on these factors. Section 3 examines whether the United States meets the characteristics of a tax haven. Section 4 explores the recent revelations in the Pandora Papers regarding the use of the U.S. financial industry by foreigners who aim to conceal assets from their home countries. It also considers empirical findings documented in several recent studies. Section 5 draws parallels between the conduct of some U.S. FIs today and that of Swiss banks that participated in the U.S. Department of Justice's Swiss Bank Program. Finally, Section 6 discusses the potential legal exposure of U.S. FIs that assist foreigners hiding funds in the United States.¹¹⁴

1. The United States' Unique Financial Secrecy Position

Before FATCA and CRS, there were many financial centers in which tax evaders could hide their funds. However, the combined effect of the first two factors mentioned above is that the United States is now the *only* established financial center in the world that offers financial secrecy. While there are some developing countries that do not implement CRS, none of them are considered attractive financial centers.¹¹⁵ This affords substantial benefits to the U.S. financial sector at the expense of other countries.¹¹⁶

113. See Cotorceanu, *supra* note 89, at 1054; Allison Christians, *What You Give and What You Get: Reciprocity Under a Model 1 Intergovernmental Agreement on FATCA*, 31 CAYMAN FIN. REV. 24 (2013).

114. This Part aims to provide a comprehensive yet concise discussion of this topic by building on the existing literature. Several publications have identified that the United States' rejection of CRS and a fully reciprocal FATCA would make it an attractive destination for undeclared funds. See, e.g., Rachel E. Brinson, *Is the United States Becoming the New Switzerland: Why the United States' Failure to Adopt the OECD's Common Reporting Standard Is Helping It Become a Tax Haven*, 23 N.C. BANKING INST. 231 (2019); Christians, *supra* note 113; Cotorceanu, *supra* note 89; HAKELBERG, *supra* note 33. This Article emphasizes the importance of the third factor mentioned above, which is often overlooked in publications that focus on the financial secrecy factors. The discussion in this part is informed by recent empirical studies and evidence from the publication of the Pandora Papers. The discussion also goes beyond general statements found in prior publications on the rise of the United States as the "new Switzerland" by considering whether U.S. FIs may be involved in conduct similar to that of Swiss FIs as detailed in non-prosecution agreements between the U.S. Department of Justice and Swiss FIs.

115. The countries that have not yet committed to implementing CRS are the following: Algeria, Angola, Belarus, Benin, Bosnia and Herzegovina, Botswana, Burkina Faso, Cabo Verde, Cambodia, Cameroon, Chad, Congo (Republic of the), Côte d'Ivoire, Djibouti, Dominican Republic, Egypt, El Salvador, Eswatini, Gabon, Guatemala, Guinea, Guyana, Haiti, Honduras, Lesotho, Liberia, Madagascar, Mali, Mauritania, Namibia, Niger, North Macedonia, Palau, Papua New Guinea, Paraguay, Philippines, Senegal, Serbia, Sierra Leone, Tanzania, Togo, Uzbekistan, Vietnam, and Zimbabwe. See OECD, *Automatic Exchange of Information (AEOI): Status of Commitments as of 9 June 2023*, <https://www.oecd.org/tax/transparency/AEOI-commitments.pdf>.

116. As more and more countries adopt CRS, the United States is poised to benefit further from its intransigence. See HAKELBERG, *supra* note 33 ("As soon as a tax haven makes concessions on secrecy or tax rates, so the logic predicts, investors will move their assets to a location that continues to offer the desired benefits. The payoff to remaining a tax haven thus increases with the number of governments complying with global standards. Hence, the last tax haven will benefit so much that it becomes impossible for other governments to offer equivalent side payments.").

As noted, the United States has repeatedly refused to adopt CRS or implement fully reciprocal information exchange under FATCA. There is no substantial difference between adopting CRS and a fully reciprocal FATCA because CRS is modeled after the FATCA Model 1 IGA, and the compliance obligations are largely similar.¹¹⁷ Under both options, U.S. FIs would need to identify foreign account holders and report their information to the IRS, which would pass it on to the relevant countries.

Why has the U.S. government objected to reciprocal information exchange? As discussed above, previous attempts by the Obama Administration to satisfy the IGAs' commitment to full reciprocity were rejected.¹¹⁸ The opposition in the U.S. government to reciprocal information exchange is probably the result of lobbying efforts by the U.S. financial industry, which is poised to incur higher compliance costs and lose business if the United States adopts the international tax transparency standard and foreigners (including foreign tax evaders) transfer funds out of U.S. FIs.¹¹⁹ Some members of Congress have even suggested that the United States should aspire to be a tax haven, while others have rejected information reporting rules for the purpose of helping foreign tax authorities.¹²⁰ Similarly, voices in the U.S. financial industry, such as the American Bankers Association, have been wary of expanded information reporting rules.¹²¹ A 2019 Government Accountability Office (GAO) report on

117. While there are several technical differences between FATCA and CRS, as detailed in Noked, *supra* note 70, at 84-99, the compliance obligations under both regimes are largely similar.

118. See *supra* note 95 and accompanying text.

119. See Christians, *supra* note 113, at 5-7; see also Cotorceanu, *supra* note 89, at 1054 ("The U.S. banking lobby has many friends on both sides of the aisle . . . Expanding data exchange would only drive this money offshore and destroy the U.S.'s current competitive advantage."); HAKELBERG, *supra* note 33 (analyzing how U.S. domestic interests, including the financial sector, have shaped the Obama and Trump Administrations' approaches to reciprocity in international tax transparency); Brinson, *supra* note 114, at 242 ("Efforts to prevent the United States from participating in more aggressive reforms of offshore financing are led by hugely influential lobbying groups, which are backed in turn by some of the world's biggest corporations."). Capital flight from tax havens that adopt AEOI has also been documented. See Jost H. Heckemeyer & Aaron K. Hemmerich, *Information Exchange and Tax Haven Investment in OECD Securities Markets*, 73 NAT. TAX J. 291 (2020). More recently, the Biden Administration has outlined several proposals to increase FATCA reciprocity in its 2023 Treasury Green Book. See U.S. DEP'T OF THE TREASURY, GENERAL EXPLANATIONS OF THE ADMINISTRATION'S FISCAL YEAR 2023 REVENUE PROPOSALS, at 87-89 (2022). On the whole, the Biden Administration has been much more vocal about fighting tax evasion than its predecessor. See, e.g., Jonathan Ponciano, *Biden Blasts Billionaires and Corporations Evading Taxes in Push for Democrats' \$3.5 Trillion Budget*, FORBES (Sept. 16, 2021). However, it appears unlikely that President Biden's proposals will pass in Congress. See *supra* note 95 and accompanying text.

120. See Christians, *supra* note 113, at 5-7. Some Republicans have been particularly vocal in their opposition to FATCA and the 2016 Republican Party platform specifically called for its repeal. In the early days of the Trump Administration there were rumors that such a repeal was supported by the president and could be imminent. This never materialized nor did the Trump Administration take a firm stance on FATCA or tax evasion in general. However, in 2018, the EU issued an ultimatum to the Trump Administration to adopt reciprocal AEOI or face blacklisting. The administration demurred and the EU ultimately backed down. Furthermore, given that many Republicans already opposed non-reciprocal FATCA, there was likely little pressure on the administration to expand its scope. The EU blacklisting threat is discussed in detail in Section II.A. See also 2016 Republican Party Platform (July 18, 2016); Tad Stoner, *FATCA Repeal on Agenda of US Republicans*, CAYMAN COMPASS (Mar. 15, 2017); Brinson, *supra* note 114, at 247.

121. See Christians, *supra* note 113, at 7.

this question did not recommend the adoption of CRS.¹²² The GAO report noted that CRS's reporting obligations would impose additional costs on U.S. FIs.¹²³ The GAO report also recognized that the United States' adoption of CRS may benefit foreign governments. Still, the report noted that it would not bring more data to the IRS, given that the IRS already receives the relevant information under FATCA.¹²⁴

Nevertheless, the U.S. government's failure to reciprocate information exchange may harm U.S. interests on net. For example, the U.S. government's stance may weaken its position in international tax negotiations.¹²⁵ Moreover, the continued provision of financial secrecy could enable illicit activities abroad, particularly in Latin America, which could have adverse effects on the United States.

2. *Low or No Taxation of Foreigners with U.S. Structures*

The next factor concerns the low or no taxation of foreigners holding U.S. and foreign assets through U.S. structures. This is a necessary condition for these structures' appeal to foreigners.¹²⁶ In general, foreign taxpayers are subject to U.S. federal income tax on two income categories. The first type is fixed, determinable, annual or periodical (FDAP) income, which includes various U.S. source payments such as dividends, interest, rental income, and royalties from a U.S. payer.¹²⁷ The second type is income from a U.S. trade or business.¹²⁸ Foreign persons are subject to federal income tax on income effectively connected with the conduct of a U.S. trade or business. Unlike U.S. taxpayers, foreigners are generally not taxed on their capital gains when selling U.S. assets other than U.S. real estate.¹²⁹ Moreover, as discussed below, foreigners can use U.S. structures that are not subject to U.S. tax.

122. U.S. Gov't Accountability Office, GAO-19-180, FOREIGN ASSET REPORTING: ACTIONS NEEDED TO ENHANCE COMPLIANCE EFFORT, ELIMINATE OVERLAPPING REQUIREMENTS, AND MITIGATE BURDENS ON U.S. PERSONS ABROAD (2019). For further discussion of this report, see Noked, *supra* note 100.

123. U.S. Gov't Accountability Office, *supra* note 122 at 33-34 ("Additionally, [CRS] could generate additional costs and reporting burdens to U.S. financial institutions that would need to implement systems to meet CRS requirements. The extent of these costs is unknown.").

124. *Id.* ("While having the United States adopt the CRS reporting system in lieu of FATCA could benefit FFIs that may otherwise have to operate two overlapping reporting systems, it would result in no additional benefit to IRS in terms of obtaining information on U.S. accounts.").

125. See Diane Ring, *The 2021 Corporate Transparency Act: The Next Frontier of U.S. Tax Transparency and Data Debates*, 18 PITT. TAX REV. 249, 272 (2021) ("A policy maker need not be naïve about international tax relations to be concerned about the impact of unprincipled positions on the continued ability to negotiate in an international tax system.").

126. Foreigners' incentives to hold assets through U.S. structures would be substantially lower if these assets were subject to the same tax treatment that applies to U.S. taxpayers with similar structures.

127. I.R.C. §§ 871, 881; IRS, *Fixed, Determinable, Annual, Periodical (FDAP) Income* (Nov. 5, 2019).

128. I.R.C. §§ 871(b), 882(a).

129. For further discussion on the taxation of foreigners' capital gains from selling U.S. assets, see Noam Noked, *A Cut of the TikTok Sale: U.S. Taxation of Inbound Foreign Direct Investments*, 41 VA. TAX REV. 1 (2021) (proposing to tax foreigners' capital gains from selling direct investments in U.S. companies); Stanley Veliotis, *Equating U.S. Tax Treatment of Dividends and Capital Gains for Foreign Portfolio Investors*, 56 AM. BUS. L.J. 345, 365 (2019) (proposing to tax foreigners' capital gains from portfolio investments in U.S. companies).

Foreigners' U.S. holding structures frequently involve U.S. limited liability companies (LLCs).¹³⁰ U.S. LLCs are considered passthrough entities for U.S. tax purposes unless they file an election to change their entity classification for tax purposes.¹³¹ By default, a U.S. LLC with one member (i.e., the owner) is treated as a disregarded entity, and a U.S. LLC with two or more members is treated as a partnership. The owner of a disregarded entity is treated as directly owning the U.S. LLC's assets and liabilities.¹³² A partnership is also a flow-through entity for U.S. income tax purposes, so the owners are taxed on the partnership's income.¹³³ No U.S. federal income tax applies if a foreign member or members use the U.S. LLC to hold U.S. or foreign assets as long as the LLC does not generate FDAP income or income effectively connected with a U.S. trade or business.¹³⁴ Similarly, no U.S. tax applies to these U.S. LLCs' capital gains from selling U.S. stocks. Therefore, a foreigner can hold a brokerage account through a U.S. LLC and generate capital gains from investing in U.S. and non-U.S. shares without paying U.S. federal income tax on these profits.¹³⁵

Foreigners can also escape U.S. federal income taxation of U.S. and foreign assets held within trusts, even if these trusts are settled under U.S. law and have a U.S. trustee.¹³⁶ This is because it is easy to structure a trust that would be considered a "foreign trust" for U.S. federal tax purposes. In general, a trust is regarded as a "U.S. trust" only if a U.S. court can exercise primary supervision over its administration and U.S. persons have the authority to control all substantial decisions concerning the trust.¹³⁷ Trusts that do not meet these requirements are foreign trusts for U.S. federal tax purposes, even if they are settled under U.S. law and have a U.S. trustee.¹³⁸ Therefore, to be considered a foreign trust, a foreign person needs to hold the power to make investment decisions or any other substantial decision for the trust. A foreign trust is subject to U.S. tax only on its U.S.-source income under the above rules. Even if a trust is a U.S. trust, it is not subject to U.S. federal income tax on its income if that

130. See, e.g., Jacob Stein, *Structuring Foreign Investment in the US*, FINANCIER WORLDWIDE MAG. (2015).

131. Treas. Reg. § 301.7701-3(b).

132. See Martin J. McMahon, Jr., *Now You See It, Now You Don't: The Comings and Goings of Disregarded Entities*, 65 TAX LAW. (2012).

133. See James A. DiGabriele, *The Moderating Valuation Effects of the Organizational Form of Flow Through Entities*, 7 J. BUS. VALUATION ECON. LOSS ANALYSIS (2012).

134. Foreigners can mitigate U.S. federal estate tax exposure by holding investments in U.S. situs assets through a foreign corporation that would hold the U.S. LLC and the U.S. situs assets. For further discussion, see G. WARREN WHITAKER, DINA KAPUR SANNA & CARL A. MERINO, *U.S. TAX PLANNING FOR NON-U.S. PERSONS AND TRUSTS: AN INTRODUCTORY OUTLINE* (2021).

135. Dividends from U.S. companies and interest payments from U.S. payers would be subject to a withholding tax of 30% unless this rate is reduced under a tax treaty. I.R.C. §§ 1441-64; see also IRS, *LB&I INTERNATIONAL PRACTICE SERVICE CONCEPT UNIT, FDAP PAYMENTS* (Jan. 7, 2016). However, foreigners can adopt strategies that maximize capital gains. For example, foreigners can invest in companies that do not pay substantial dividends or sell the relevant shares before dividends are paid. See Noked, *supra* note 129, at 22-23.

136. For further discussion on trust law in the United States, see John H. Langbein, *Why Did Trust Law Become Statute Law in the United States?*, 58 ALA. L. REV. 1069 (2007).

137. Treas. Reg. § 301.7701-7(a)(1). These "substantial decisions" include decisions regarding investments, distributions, terminating or revoking the trust, adding or removing beneficiaries, and other decisions. *Id.*

138. Treas. Reg. § 301.7701-7(a)(2).

income is not from a U.S. source and is distributed to a foreign beneficiary in the same year the income is earned.¹³⁹ Therefore, foreign settlors and beneficiaries can use trusts organized under U.S. law with a U.S. trustee while paying no U.S. federal income tax.¹⁴⁰ U.S. taxpayers cannot benefit from these rules: U.S. settlors are taxed as the owners of the assets they settle into a foreign trust.¹⁴¹ Also, U.S. beneficiaries of foreign non-grantor trusts are generally taxed on trust income paid to them.¹⁴²

3. *Characteristics of a Tax Haven*

While the United States is generally not a tax haven for U.S. persons, the country *is* a tax haven for foreigners hiding funds in U.S. FIs and U.S. holding structures. This is like several traditional tax havens that impose tax on their residents. For example, Swiss individuals and businesses are subject to substantial income taxes in Switzerland.¹⁴³ As discussed below, the United States meets the characteristics of a tax haven under several definitions.

In general, tax havens possess several common characteristics. According to the OECD, tax havens generally have zero or nominal tax rates, no obligation to exchange information, a lack of transparency in “the operation of the legislative, legal or administrative provisions,” and no need for a substantial local presence in the tax haven.¹⁴⁴ The OECD further notes that non-tax conditions such as a relaxed regulatory framework and the presence of a solid business infrastructure can also contribute to tax haven conditions in a country.¹⁴⁵ As discussed above, foreigners can adopt U.S. structures resulting in low or no U.S. taxation of the underlying assets. When compared to countries that implement CRS, the United States offers unparalleled levels of secrecy and limited

139. The U.S. trust will be able to claim a deduction for current year distributions. I.R.C. § 651. The distribution to the foreign beneficiary is only required if the U.S. trust is a non-grantor trust. If the U.S. trust is a grantor trust, all the income and assets will be attributed to the foreign grantor, and no U.S. federal income tax should apply if the trust has no U.S. source income.

140. The income of the U.S. trust company that provides services as trustee would be subject to U.S. federal income tax because it is a U.S. business. However, this tax is only on the fees the trust pays to the trust company for its services as trustee.

141. I.R.C. § 679.

142. For an overview of the taxation of U.S. beneficiaries of foreign trusts, see Paul DePasquale & Glenn Fox, *U.S. International Trust Reporting and Planning*, 29 NYSBA INT’L L. PRACTICUM 33-35 (2016).

143. See OECD, Revenue Statistics 2021 — Switzerland, <https://www.oecd.org/tax/revenue-statistics-switzerland.pdf>.

144. OECD, HARMFUL TAX COMPETITION: AN EMERGING GLOBAL ISSUE (1998). The OECD identifies no or only nominal taxation as a “necessary condition” for a tax haven. It further argues that a lack of transparency is doubly bad since it can facilitate illicit activities other than tax evasion such as money laundering. Overall, these four conditions are similar to those used by the EU to determine its blacklist of non-cooperative jurisdictions. See *infra* note 184 and accompanying text. For further discussion on how to define a tax haven, see U.S. GOV’T ACCOUNTABILITY OFFICE, GAO-09-157, INTERNATIONAL TAXATION: LARGE U.S. CORPORATIONS AND FEDERAL CONTRACTORS WITH SUBSIDIARIES IN JURISDICTIONS LISTED AS TAX HAVENS OR FINANCIAL PRIVACY JURISDICTIONS (Dec. 2008); Gary Tobin & Keith Walsh, *What Makes a Country a Tax Haven? An Assessment of International Standards Shows Why Ireland Is Not a Tax Haven*, 44 ECON. SOC. REV. 401, 403 (2013) (reviewing the literature and concurring with the 2008 GAO report that concluded that the OECD’s list of four key tax haven indicators is “representative” of most existing definitions).

145. See OECD, *supra* note 144, at 22-25.

information exchange. Moreover, foreigners do not need any presence or nexus to the United States to hold U.S. financial assets, entities, or trusts.¹⁴⁶ Thus, the United States would appear to meet the OECD's criteria.¹⁴⁷

Another common characteristic is self-promotion as an offshore financial center.¹⁴⁸ Such promotion campaigns are being carried out by relevant actors in the U.S. financial industry to attract foreign clients. These actors are highlighting the advantages of the United States as an offshore financial center in seminars, online publications, and other marketing efforts. For example, one U.S. trust company stated that one of the benefits of U.S. trusts is that “[t]here is currently no FATCA or CRS reporting requirement for U.S. trustees or U.S. financial institutions for clients who hold U.S. situs accounts.”¹⁴⁹ It also noted that there may be “no U.S. reporting requirements” where a U.S. law trust settled by a foreign grantor is considered as a “foreign trust” for U.S. tax purposes and it has no U.S. source income.¹⁵⁰ Another U.S. advisor stated that “[o]ften overlooked, the U.S. is well positioned to be the premiere jurisdiction for privacy-minded nonresident aliens (i.e., non-U.S. persons) looking to form a trust—it offers no registration requirement for trusts, no automatic exchange of banking information, and a 0% U.S. tax rate (on non-U.S. source income).”¹⁵¹ In addition, U.S. trust companies’ websites and seminars market U.S. trusts for foreign clients.¹⁵²

Other studies on the characteristics of tax havens also stress the importance of good governance, a strong service sector, a developed financial system, minimal currency controls, robust infrastructure, and stability, in addition to low levels of taxation.¹⁵³ Once again, the United States meets all of these criteria. Thus, according to several definitions, the United States has the characteristics of a tax haven.

146. Foreigners with no ties to the United States can purchase U.S. shares, set up U.S. LLCs, corporations and trusts, and purchase U.S. assets of various types. Only certain types of transactions by foreigners are subject to the federal government’s scrutiny on national security grounds; for further background, see U.S. Dep’t of Treasury, The Committee on Foreign Investment in the United States (CFIUS), <https://home.treasury.gov/policy-issues/international/the-committee-on-foreign-investment-in-the-united-states-cfius> (last visited July 7, 2023).

147. See also Brinson, *supra* note 114, at 243–45.

148. James R. Hines & Eric M. Rice, *Fiscal Paradise: Foreign Tax Havens and American Business*, 109 Q. J. ECON. 149 (1994). Other characteristics in this study include low taxes, secrecy laws, and advanced communication facilities. *Id.*

149. US Trust Advisory Services LLC, *US Trusts For US And Non-US Clients* (July 10, 2019), https://web.archive.org/web/20211129111802/https://www.lowtax.net/articles/US_Trusts_for_US_and_nonUS_clients_-595315.html.

150. See *id.*

151. Jimmy Sexton, Esquire Group, *Why America Is the Leading Jurisdiction For Trusts* (Feb. 1, 2021), <https://news.bloombergtax.com/daily-tax-report/why-america-is-the-leading-jurisdiction-for-trusts>.

152. See Will Fitzgibbon & Debbie Cenziper, *The “Cowboy Cocktail”: How Wyoming Became One of the World’s Top Tax Havens* (Dec. 20, 2021) (“One trust company 8,700 miles away in downtown Singapore recommended Wyoming on its website as a go-to tax haven that would ‘completely shield’ clients’ names and assets. ‘Offshore Wyoming, USA,’ noted another firm, this one near the Dnieper River in Ukraine’s bustling capital, Kyiv.”).

153. Dharmika Dharmapala & James R. Hines Jr., *Which Countries Become Tax Havens?*, 93 J. PUB. ECON. 1058 (2009); Eugenia Ramona Mara, *Determinants of Tax Havens*, 32 PROCEDIA ECON. 1638 (2015); Mykola Orlov, *The Concept of Tax Haven: A Legal Analysis*, 32 INTERTAX 95 (2004).

Indeed, several studies and rankings reflect that the United States now ranks among the top tax havens in the world. Several scholars have ranked the United States as the world's top financial secrecy jurisdiction.¹⁵⁴ The Tax Justice Network, an advocacy group that campaigns against tax evasion and avoidance, has recently moved the United States to the top of its Financial Secrecy Index (FSI).¹⁵⁵ The FSI measures the level of secrecy in a jurisdiction and considers its ability to enable aggressive tax behaviors.¹⁵⁶ Remarkably, the United States now ranks above traditional tax havens and bank secrecy jurisdictions such as Switzerland, the Cayman Islands, and the British Virgin Islands.¹⁵⁷ Unlike the United States, these jurisdictions implement CRS, so foreigners cannot easily hide funds in them to circumvent CRS reporting.¹⁵⁸

4. *The Pandora Papers and Empirical Evidence*

A growing body of economic literature has documented evidence showing how the United States is increasingly used as a tax haven. These studies show that following the implementation of FATCA and CRS, there has been a flow of financial assets from traditional tax havens into the United States.

Using data on financial assets held in tax havens and non-tax havens, Lukas Hakelberg and Max Schaub found that the automatic exchange of information reduced foreigners' incentives to evade tax in traditional tax havens while also increasing the attractiveness of the United States as a place to hide wealth.¹⁵⁹ Another study by Elisa Casi, Christoph Spengel, and Barbara Stage found that after the adoption of CRS, cross-border deposits in the United States increased while similar deposits in traditional tax havens decreased.¹⁶⁰ Other studies have

154. See Petr Jansky, Markus Meinzer & Miroslav Palansky, *Is Panama Really Your Tax Haven? Secrecy Jurisdictions and the Countries They Harm*, REG. & GOVERNANCE 1, 17 (2021) (ranking the United States as the top secrecy jurisdiction for European countries).

155. Tax Just. Network, *Financial Secrecy Index 2022*, <https://fsi.taxjustice.net/> (last visited July 7, 2023).

156. *Id.*

157. The United States has steadily moved up the list in recent years. See, e.g., Tax Just. Network, *Financial Secrecy Index — 2020 Results* (2020) (ranking the Cayman Islands above the United States). As noted, the United States tops the list in the 2022 results, which is the most recent list at the time of this publication. See Tax Just. Network, *supra* note 155.

158. As noted, tax evaders may still circumvent CRS reporting even for funds in CRS-implementing jurisdictions by exploiting weaknesses, loopholes, and non-compliance opportunities. See Noked, *supra* note 43; Noked, *supra* note 70; Jeanne Bomare & Segal Le Guern Herry, *Will We Ever Be Able to Track Offshore Wealth? Evidence from the Offshore Real Estate Market in the UK* (EU Tax Observatory, Working Paper No. 4, 2022).

159. See Lukas Hakelberg & Max Schaub, *The Redistributive Impact of Hypocrisy in International Taxation*, REG. & GOVERNANCE 353, 366 (2018) (“This strongly suggests that [FATCA] was not only effective in curbing the evasion of taxes on capital income through the exploitation of financial secrecy in traditional tax havens, it also increased the attractiveness of the [United States] as a destination for hidden capital, as a result of the country’s refusal to reciprocate [automatic exchange of information].”).

160. Elisa Casi, Christoph Spengel & Barbara M.B. Stage, *Cross-border Tax Evasion After the Common Reporting Standard: Game Over?*, 190 J. PUB. ECON. 1, 11 (2020) (“Moreover, we do not find that the CRS truly put an end to cross-border tax evasion. Instead, we document a change in the dynamics of cross-border tax evasion. We add to the prior literature by providing evidence that after the CRS took effect, an unexpected country seems to have begun to attract wealth and related income, namely, the

confirmed a reduction of financial assets in traditional tax havens.¹⁶¹ One study even shows that the conclusion of a FATCA agreement between the United States and an offshore financial center increased deposits in the United States.¹⁶²

While troubling on their own, these studies likely substantially underestimate the amount of funds foreigners hold in the United States. The studies are based on deposit data collected by the Bank of International Settlements, which includes aggregate information on deposits *directly* held by foreigners.¹⁶³ A deposit held by a foreigner indirectly through a U.S. entity or trust is not reported as a foreign-owned deposit in these data. As noted, foreigners frequently hold U.S. deposits and other assets through U.S. LLCs and other U.S. entities.¹⁶⁴ As a result, a large proportion of foreign-owned financial assets in the United States might not be captured in these studies.

These economic studies substantiate abundant evidence from leaks and investigative journalism concerning the movement of capital from traditional tax havens into the United States since the implementation of FATCA and CRS. Most recently, the Pandora Papers have revealed various transactions of this nature.¹⁶⁵ For example, Horst Happel, one of Brazil's top orange juice producers, kept his assets in a trust in the British Crown Dependency of Jersey, a well-known tax haven, for thirty years.¹⁶⁶ However, the Pandora Papers revealed that in 2018, Happel opened a trust in South Dakota, perhaps because of Jersey's uncertain future as a tax haven, given that the territory "in recent years has faced international pressure to require trust providers to collect and share more

United States. . . . In this analysis, we show that over our sample period, cross-border deposits held by residents of nonhaven countries in the United States increased by 10% after the CRS took effect."); see also Agustin Benetrix, Lorenz Emter & Martin Schmitz, *Automatic for the (Tax) People: Information Sharing and Cross-Border Investment in Tax Havens* (Trinity Coll. Dublin, TEP Working Paper No. 1321, 2021) (finding that the adoption of AEOI leads to the shifting of deposits to non-participating haven countries); Niels Johannesen & Gabriel Zucman, *The End of Bank Secrecy? An Evaluation of the G20 Tax Haven Crackdown*, 6 AM. ECON. J. ECON. POL'Y 65 (2014) ("[T]ax evaders shifted deposits to havens not covered by a treaty with their home country.").

161. See, e.g., Pierce O'Reilly, Kevin Parra Ramirez & Michael A. Stemmer, *Exchange of Information and Bank Deposits in International Financial Centres* (OECD, Taxation Working Papers No. 46, Nov. 2019); Sebastian Beer, Maria Delgado Coelho & Sebastian Leduc, *Hidden Treasure: The Impact of Automatic Exchange of Information on Cross-Border Tax Evasion* (IMF, Working Paper WP/19/286, Dec. 2019); see also Tijmen Tuinisma, *Do Foreign Tax Evaders Use the United States as a Tax Haven?* (master thesis, 2019) (failing, unlike the aforementioned studies, to definitively conclude that funds have flowed to the United States).

162. Beer et al., *supra* note 161, at 27 (documenting a decrease in deposits held in tax havens but cautioning that "a reduction in presumably tax evading deposits in one offshore jurisdiction could imply an increase in tax evading deposits elsewhere. . . . What is more, the conclusion of a FATCA agreement with an offshore center seems to have increased deposits into the [United States], a result consistent with prior findings . . . that the [United States] may have become a more attractive location in which to hold—and perhaps conceal—income.").

163. See Hakelberg & Schaub, *supra* note 159, at 357; Casi et al., *supra* note 160, at 2; O'Reilly et al., *supra* note 161, at 7; Beer et al., *supra* note 161, at 4.

164. Holding assets under a U.S. entity would circumvent the reporting under reciprocal IGAs. See Cotorceanu, *supra* note 89, at 1052.

165. For more on the Pandora Papers, see Int'l Consortium of Investigative Journalists, *Pandora Papers*, <https://www.icij.org/investigations/pandora-papers/> (last visited July 7, 2023); Int'l Consortium of Investigative Journalists, *supra* note 1.

166. Happel also settled a \$88 million case with the Brazilian government for "allegedly colluding to underpay local farmers." See Fitzgibbon et al., *supra* note 10.

information about their customers.”¹⁶⁷ The same, of course, could not be said of South Dakota.

Evidently, many of the individuals taking advantage of the United States’ favorable tax haven conditions come from Latin America.¹⁶⁸ However, this phenomenon is not limited to that region or the developing world. There is substantial evidence that Europe and other regions are affected as well.¹⁶⁹ One study found that the United States is the most popular secrecy jurisdiction for taxpayers from EU member states.¹⁷⁰ Additionally, an article from the publishers of the Pandora Papers states, “[i]n recent years, families from India to Italy to Venezuela abandoned international financial centers for law firms in Wyoming’s ski resorts and mining towns, helping to turn the state into one of the world’s top tax havens.”¹⁷¹ Advertisements for using Wyoming as a tax haven even emerged as far away as Ukraine and Singapore.¹⁷²

5. *Parallels between U.S. FIs and Swiss Banks*

As noted, the United States aggressively pursued FFIs that made use of secrecy jurisdictions abroad. However, there is reason to believe that some U.S. FIs are engaging in behaviors similar to those of the FFIs targeted by U.S. authorities. This means that U.S. FIs may be violating the United States’ own standards that U.S. authorities enforce internationally.

Compare, for instance, the conduct of U.S. FIs today to that of the Swiss banks that participated in the U.S. Department of Justice’s Swiss Bank Program.¹⁷³ As part of their non-prosecution agreements, many Swiss banks admitted to committing acts that are likely similar to those carried out by some U.S. FIs today. For example, these are the facts admitted by Falcon Private Bank AG, a Swiss bank with U.S. clients, in its statement of facts as part of its non-prosecution agreement:

[T]he Bank retained at least ten accounts where beneficial owners were known to have U.S. domicile without proper documentation of tax compliance. Through its managers, employees and/or others, Falcon knew that some U.S. taxpayers who had opened and maintained accounts at the Bank were not complying with their U.S. income tax and reporting obligations. Falcon also offered a variety of standard Swiss banking services which it knew could assist, and did assist, its U.S. clients in the concealment of assets and income from the IRS. . . . Falcon was aware that U.S. taxpayers had a legal duty to report to the IRS, and pay taxes on the basis of all their income, including income earned in accounts that these U.S. taxpayers maintained at Falcon. Despite being aware of this legal duty, the Bank permitted accounts for

167. *Id.*

168. See Cotorceanu, *supra* note 89, at 1054 (“It is no secret that U.S. banks, particularly in Miami, are awash in undeclared Latin American money.”).

169. For further discussion on how the U.S. tax policies may affect Europe, see Knobel, *supra* note 100.

170. See Jansky et al., *supra* note 154, at 17.

171. See Fitzgibbon & Cenziper, *supra* note 152.

172. *Id.*

173. For a comparison between U.S. FIs and Swiss banks, see Brinson, *supra* note 114 (providing further information on the U.S. crackdown of overseas banks, highlighting the United States’ hypocrisy on this matter, and discussing how the United States could adopt AEOI and why it should).

U.S. taxpayers to be opened and maintained without investigating whether such accounts were undeclared.¹⁷⁴

Similar statements of fact were included in non-prosecution agreements with many Swiss banks that participated in the Department of Justice's Swiss Bank Program.¹⁷⁵ The Department of Justice likely considered these facts as constituting criminal offenses. Otherwise, non-prosecution agreements would not have been required.

How do U.S. FIs compare to Swiss banks in the past? First, U.S. FIs hold many accounts of beneficial owners known to be foreigners.¹⁷⁶ However, it is unclear if and to what extent U.S. FIs require any "proper documentation of tax compliance" from their foreign clients.

Second, when dealing with foreign clients—especially those who moved funds from tax havens to the United States shortly before or after the implementation of CRS—it is hard to believe that U.S. FIs neither knew nor suspected tax non-compliance as a plausible reason for moving the funds to the United States.

Third, U.S. FIs know about the implications of the United States' non-participation in CRS. U.S. FIs who serve foreign account holders with no ties to the United States know that holding funds in the United States could assist their foreign clients "in the concealment of assets and income" from the tax authorities in their home countries by circumventing CRS reporting.

Fourth, U.S. FIs should be aware of the duties many tax authorities impose on their tax residents to report and pay tax on their worldwide income, similar to the tax obligations that apply to U.S. persons. It is unclear if U.S. FIs investigate "whether such accounts were undeclared."

Therefore, it is likely that at least some U.S. FIs currently engage in conduct similar to that of Swiss banks prior to the U.S. crackdown on the Swiss banking industry. If such behavior by Swiss banks was unacceptable to the United States in 2013, then the same behavior by U.S. FIs should be equally intolerable today.

6. *The Illegality of Aiding and Abetting Foreign Tax Evasion*

U.S. FIs that assist foreign tax evaders may be violating U.S. law. The U.S. Supreme Court held in *Pasquantino v. United States*¹⁷⁷ that a plot to defraud a foreign government of tax revenue violated the federal wire fraud statute.¹⁷⁸ Carrying out a financial transaction with the proceeds of wire fraud might constitute a money laundering offense because wire fraud is a predicate offense

174. U.S. Dep't of Just., Non-Prosecution Agreement with Falcon Private Bank AG (July 20, 2015), <https://www.justice.gov/opa/file/641596/download>.

175. See U.S. Dep't of Just., *supra* note 58.

176. U.S. FIs must identify the beneficial owners of the accounts as part of their customer due diligence, which is mandated under the U.S. anti-money laundering regime. 31 C.F.R. § 1010.230.

177. 544 U.S. 349 (2005).

178. 18 U.S.C. § 1343.

for money laundering.¹⁷⁹ Following this precedent, criminal charges can be brought against U.S. FIs and their employees for aiding or abetting wire fraud or money laundering.¹⁸⁰ Thus, it may constitute a criminal offense under U.S. law if a U.S. FI aids or abets foreigners' tax evasion vis-à-vis their home countries.

Despite the potential criminal exposure, revelations from the Pandora Papers and empirical evidence indicate that the U.S. financial industry has been largely undeterred when dealing with foreigners who use U.S. FIs to avoid information reporting to foreign tax authorities. It is also unclear if the Department of Justice has pursued any enforcement actions against U.S. FIs for aiding and abetting foreign tax evaders. The U.S. government's inaction could be due to any number of reasons including a lack of resources, a lack of sufficient interest, or pressure from the financial sector. However, it is important to note that the Department of Justice could change its position at any time and begin bringing charges against U.S. FIs and employees involved in such conduct. That said, there are limits to the ruling in *Pasquantino*. While the ruling affirmed that defrauding a foreign government of tax revenue in that case violated U.S. criminal law, it leaves in place the "revenue rule," which may limit the ability of U.S. courts to enforce foreign tax judgments.¹⁸¹

Some U.S. FIs and their employees may also have substantial legal exposure in other countries for aiding and abetting tax evasion by these countries' tax residents. Such countries may investigate and penalize U.S. banks, similar to how the U.S. Department of Justice has investigated and penalized foreign banks for aiding and abetting tax evasion by U.S. taxpayers.¹⁸²

II. PROPOSED INTERNATIONAL RESPONSE

What can countries do when the non-participation of one country undermines the effectiveness of an entire international tax transparency regime? One option would be to carry out a pressure campaign against the uncooperative government in order to force it to adopt the international standard. As discussed in Section A below, the EU tried this approach and failed. Following that attempt, it appears unlikely that foreign governments' pressure would result in Congress enacting legislation that imposes fully reciprocal FATCA or CRS obligations on U.S. FIs.

If such pressure campaigns are unlikely to succeed, what can other countries do to protect their tax bases from tax crimes committed with the

179. 18 U.S.C. §§ 1956, 1957. For a discussion on the federal money laundering offense and related issues, see CHARLES DOYLE, CONG. RSCH. SERV., RL33315, MONEY LAUNDERING: AN OVERVIEW OF 18 U.S.C. § 1956 AND RELATED FEDERAL CRIMINAL LAW (2017).

180. 18 U.S.C. § 2(a).

181. See William J. Kovatch Jr., *Recognizing Foreign Tax Judgments: An Argument for the Revocation of the Revenue Rule*, 22 HOUS. J. INT'L L. 265, 267 (1999) ("Under the 'revenue rule,' the courts of the United States are under no obligation to recognize or enforce a foreign tax judgment."). More specifically, it has been argued that enforcements of foreign tax judgments must first follow a "permissible legal action" within the United States (such as a criminal prosecution). For a detailed discussion of the revenue rule, see generally Samuel D. Brunson, *The U.S. as Tax Haven — Aiding Developing Countries by Revoking the Revenue Rule*, 5 COLUM. J. TAX L. 170 (2014).

182. See *supra* text accompanying notes 55-60.

assistance of a foreign financial industry? This Part proposes a mechanism that several CRS-implementing countries could adopt to extend the reach of CRS when some countries refuse to reciprocate reporting. This mechanism, which constitutes a regulatory “fail-safe” as discussed below, is inspired by the measures imposed by the U.S. Treasury’s FATCA regulations.¹⁸³ At their core, these measures seek to elicit compliance from FIs directly, thereby circumventing the need for governmental action.

A. The Failure of the EU’s Blacklisting Threat

The most notable attempt to force the United States into adopting reciprocal information exchange was carried out by the EU. The EU has maintained a list of non-cooperative jurisdictions in taxation since 2017.¹⁸⁴ Jurisdictions blacklisted by the EU may be subject to defensive measures by EU member states, including withholding taxes.¹⁸⁵ The EU’s criteria for which jurisdictions should be blacklisted include jurisdictions that do not implement CRS.¹⁸⁶

In 2018, the EU gave the Trump Administration until June 2019 to agree to reciprocate information exchange or be blacklisted, the implication being that the FATCA bilateral agreements were inadequate.¹⁸⁷ Valere Moutarlier, the EU Commission’s head of direct taxation and tax cooperation, said that the EU’s criteria for tax transparency are clear and that “the June 2019 deadline must be respected.”¹⁸⁸ While EU representatives and the U.S. government likely communicated on this matter, there has not been any reporting on the content of any such communications.

In October 2019, the EU quietly backed down from its blacklisting threat, stating that the United States satisfied its information exchange obligations

183. See Mason, *supra* note 52; *infra* Section III.A.

184. Council of the European Union, *Taxation: EU List of Non-cooperative Jurisdictions* (Oct. 7, 2021), <https://www.consilium.europa.eu/en/policies/eu-list-of-non-cooperative-jurisdictions/>. A jurisdiction must meet three sets of criteria to be considered a non-cooperative jurisdiction. The first set of criteria are the “tax transparency criteria,” which primarily concern compliance with international AEOI standards. The second set of criteria is the “fair taxation criteria,” which require that cooperative jurisdictions have no harmful preferential tax measures (as defined by the EU) and that they do not facilitate offshore structures without any substantial economic activity in the territory. Finally, the third set of criteria requires that cooperative jurisdictions satisfactorily implement all BEPS minimum standards. See Council of the European Union, *Criteria and Process Leading to the Establishment of the EU List of Non-cooperative Jurisdictions for Tax Purposes — Council Conclusions* (Nov. 8, 2016), <https://bit.ly/2SeWfWM>.

185. For a full list of the EU’s suggested sanctions for blacklisted jurisdictions, see Council of the European Union, *Taxation: EU List of Non-cooperative Jurisdictions*, *supra* note 184.

186. *Id.* The three criteria for tax transparency are: to implement CRS or establish adequate bilateral agreements with all Member States (Criterion 1.1), to be largely compliant with respect to the OECD Exchange of Information Request (EOIR) standard (Criterion 1.2), and to ratify (or be in the process of ratifying) the OECD Multilateral Convention on Mutual Administrative Assistance (MCMAA) in Tax Matters or adopt an equivalent network of exchange arrangements (Criterion 1.3). Council of the European Union, *Criteria and Process Leading to the Establishment of the EU List of Non-Cooperative Jurisdictions for Tax Purposes—Council Conclusions*, *supra* note 184, at 4-6.

187. See Michael Klein, *EU Threatens US Tax Blacklisting*, CAYMAN COMPASS (June 5, 2018); Naomi Fowler, *Will the EU Really Blacklist the United States?*, TAX JUST. NETWORK (June 11, 2018).

188. See Fowler, *supra* note 187.

through FATCA.¹⁸⁹ The EU noted that “the FATCA competent authority agreements (CAA) between the [United States] and all Member States were deemed sufficient to meet [the] EU’s requirement.”¹⁹⁰ This position is entirely inconsistent with the EU’s blacklisting criteria and the EU’s own statements discussed above. Regardless, the EU has given no explanation for the reversal of its position.¹⁹¹

It is possible that the EU chose not to blacklist the United States for failing to meet the international tax transparency standard because of the potential ramifications of such an action.¹⁹² First, the mere blacklisting of the United States could have shocked financial markets and harmed the economies of both the United States and Europe. One analyst described the United States as “too big to be listed.”¹⁹³ Second, the United States might have retaliated or threatened to retaliate against EU member states. Third, despite the potentially harmful consequences for the United States and the EU, there is no guarantee that blacklisting the United States would result in the U.S. government adopting CRS or a fully reciprocal FATCA. Even if the EU blacklisted the United States, it is questionable if Congress would pass any legislation adopting tax transparency.

After the EU’s failed attempt to force the United States to adopt the international tax transparency standard, it appears unlikely that exerting international pressure on the U.S. government can succeed. The following sections consider how countries can safeguard their tax base and enforce their tax laws without requiring any action from the U.S. Congress or Treasury.

B. Proposal for CRS Enforcement Model

When a country fails to join CRS, the FIs within that country are under no obligation to share data with foreign governments. Under the status quo, those FIs can hide behind their intransigent governments and conceal foreigners’ assets. However, in an interconnected and globalized world, it is possible to target FIs directly without the involvement of their home governments. FATCA’s legislation and regulations took advantage of this reality. We now explore how the FATCA enforcement model could be adapted to CRS and applied to FIs in countries that refuse to implement CRS. While the discussion

189. See COUNCIL OF THE EUROPEAN UNION, REPORT BY THE CODE OF CONDUCT GROUP (BUSINESS TAXATION) SUGGESTING AMENDMENTS TO THE ANNEXES OF THE COUNCIL CONCLUSIONS OF 12 MARCH 2019, INCLUDING THE DE-LISTING OF TWO JURISDICTIONS, AND THE ENDORSEMENT OF A GUIDANCE NOTE 6 (2019).

190. *Id.*

191. The anti-poverty organization Oxfam independently applied the EU criteria to the United States and determined that it failed to meet the EU’s standards and should have already been blacklisted in 2017. See Johan Langerock, *Assessing Jurisdictions Against EU Listing Criteria*, OXFAM (2019) (“The United States should have already been listed for failing criterion 1 in December 2017. . . . The CRS is a clear requirement for the EU, and the EU members’ tax authorities do not receive as much information from the [United States] under their bilateral FATCA agreements as they do from countries participating in the multilateral CRS.”).

192. There have been suggestions that the OECD similarly changed its blacklist rules to avoid listing the United States. See Andres Knobel, *Blacklist, Whitewashed: How the OECD Bent Its Rules to Help Tax Haven USA*, TAX JUST. NETWORK (July 27, 2018).

193. Johan Langerock, *Off the Hook: How the EU is About to Whitewash the World’s Worst Tax Havens*, OXFAM 1, 3 (2019).

below focuses on U.S. FIs, the same mechanism should be applied to FIs in any jurisdiction that does not implement CRS.¹⁹⁴

I. Coordinated Response of Like-Minded Countries

The United States acted unilaterally when it imposed FATCA obligations on FFIs around the world.¹⁹⁵ CRS, in contrast, is an international, multilateral standard. When considering what CRS-implementing countries can do to enforce the compliance of FIs in non-cooperative jurisdictions unilaterally, there is no need for any particular government to act alone. Several CRS-implementing countries can agree on and apply enforcement measures together.

The OECD, which developed the entire CRS framework, including the standard and guidance materials,¹⁹⁶ is a natural forum for developing an extension of CRS. However, as the United States is a member of the OECD and its biggest funder,¹⁹⁷ it is unclear whether this body could lead this effort.¹⁹⁸ Alternatively, several CRS-implementing countries could set up an ad hoc and informal coordination forum to consider their coordinated response to the tax evasion facilitated by the U.S. financial industry.¹⁹⁹ The EU, in particular, could lead this initiative.²⁰⁰ The OECD's recent tax reforms provide a blueprint for such cooperation. First, these countries could adopt model rules that they would agree to enact as domestic laws and regulations.²⁰¹ Second, the countries could enter into a multilateral agreement, facilitating collaboration between them and setting up a relevant mechanism, as further discussed below.²⁰²

All countries that implement CRS could be part of this coordinated response. However, realistically, it is likely that some governments would not be willing or able to participate. This could result from U.S. pressure against initiatives subjecting U.S. FIs to the international transparency standard. Alternatively, it could be the result of political pressure or corruption in countries where influential actors use U.S. FIs to evade tax and reporting. Nonetheless, the

194. It would be appropriate to consider an exemption for developing countries that pose little risk of facilitating offshore tax evasion and that lack sufficient infrastructure to implement CRS. See *supra* note 115 for the list of countries that have not yet committed to implementing CRS.

195. The United States can act unilaterally on such matters given the central role of its financial sector and currency in international transactions. See Patrick Emmenegger, *The Long Arm of Justice: U.S. Structural Power and International Banking*, 17 *BUS. POL.* 473 (2015).

196. For the OECD's CRS guidance materials, see OECD, *Automatic Exchange Portal: Common Reporting Standard*, <https://www.oecd.org/ctp/exchange-of-tax-information/standard-for-automatic-exchange-of-financial-account-information-for-tax-matters-9789264216525-en.htm> (last visited July 7, 2023).

197. See OECD, *Member Countries' Budget Contributions for 2023*, <https://www.oecd.org/about/budget/member-countries-budget-contributions.htm> (showing that the United States contributed 19.1% of the OECD's budget in 2023).

198. For similar concerns about the OECD, see Rosenbloom et al., *supra* note 49.

199. See *id.* (a proposal for a tax coordination forum for like-minded countries).

200. However, an EU directive facilitating the proposed mechanism would require the unanimous agreement of all EU member states which may be difficult to achieve.

201. See, e.g., OECD, *MODEL MANDATORY DISCLOSURE RULES FOR CRS AVOIDANCE AND OPAQUE OFFSHORE STRUCTURES* (2018) (hereinafter *CRS MODEL MANDATORY DISCLOSURE RULES*); OECD, *TAX CHALLENGES ARISING FROM THE DIGITALISATION OF THE ECONOMY — GLOBAL ANTI-BASE EROSION MODEL RULES (PILLAR TWO)* (Dec. 20, 2021) [hereinafter *PILLAR TWO MODEL RULES*].

202. See, e.g., the multilateral agreements described *supra* note 45.

CRS enforcement model outlined here could be implemented as a coordinated response by several countries.²⁰³ The hypothetical group of CRS-implementing countries that adopt this coordinated response is referred to as the “CRS Group.”

The EU is in the best position to initiate or join the CRS Group. The EU possesses both the economic size and the political desire to rein in overseas tax havens.²⁰⁴ While the bloc has proven incapable of challenging the United States directly via blacklisting, it may be more likely to implement the less confrontational measures outlined in this Article. This proposal does not require that the CRS Group single out the United States individually. Instead, this proposal could be adopted by the CRS Group as a measure against all non-cooperative countries, thereby avoiding a direct confrontation with the United States. As discussed in Section II.C below, when compared to a potential blacklisting of the United States, this proposal is less likely to prompt a retaliatory response from the United States or rattle financial markets. These considerations may make the proposal more palatable to EU policymakers.

Moreover, the EU does not need to stand alone and could instead partner with other large economies such as Japan, the United Kingdom, or Canada. Alternatively, if the EU as a bloc does not join the CRS Group, several individual EU countries may form the CRS Group among themselves and other like-minded non-EU partners.²⁰⁵ Binding these countries together would be a shared interest in expanding international tax transparency to protect their own revenues.

Furthermore, it is important to note that to be effective, the CRS Group only needs to attract a handful of large economies that carry sufficient collective weight to pressure U.S. FIs into cooperating. It is unclear how large this group would need to be in order to be effective.²⁰⁶ If several sizeable economies such as France, Germany, the United Kingdom, Japan, and others formed the CRS Group, it could be large enough to compel U.S. FIs to comply. The critical mass required of the CRS Group may also be affected by the penalty policy and design.²⁰⁷ If penalties were steeper and harder to avoid, then this proposed standard could achieve its goals even with a smaller CRS Group.

2. *Registration and CRS FI Agreement*

The CRS Group would engage with U.S. FIs directly. Similar to the FATCA portal on the IRS website, the CRS Group would set up a CRS portal on

203. See Rosenbloom et al., *supra* note 49.

204. It is clear from the EU’s blacklisting threat of the United States that it views U.S. non-cooperation as a serious issue. See *supra* Section II.A.

205. Within the EU, there is a mechanism known as “enhanced cooperation” which allows “advanced integration or cooperation” among nine or more like-minded EU member states. See EUR-Lex, Glossary of Summaries, <https://eur-lex.europa.eu/EN/legal-content/glossary/enhanced-cooperation.html>.

206. The mechanism described could be considered to be effective if U.S. FIs comply with the reporting demands of the CRS Group (independent of U.S. national policy) or if the United States reverses policy and adopts reciprocal AEOL.

207. As discussed in Section II.B.5, it would be harder for U.S. FIs to avoid penalties if they are applied to payments from participating U.S. FIs to non-participating U.S. FIs and if compliance is required on a group basis, similar to FATCA.

a dedicated website that U.S. FIs would use to register with the CRS Group as “participating FIs” (i.e., CRS-compliant FIs).²⁰⁸ Each registered FI would be assigned a unique number, similar to FATCA’s GIIN, which is assigned to FFIs.²⁰⁹ The CRS portal would include a search tool with the name, country, and number of each participating FI. FIs resident in CRS-implementing countries would not be required to register; this requirement would only apply to FIs in non-cooperative jurisdictions. U.S. FIs registered as participating FIs on the CRS portal would not be subject to the penalty provisions discussed below. An FI’s registration could be revoked if it were found that it had failed to comply with the CRS obligations through the monitoring measures discussed below.

Additionally, as part of the registration, U.S. FIs would be required to accept the terms of a “CRS FI Agreement” under which they agree to undertake the CRS obligations to identify and report foreign tax residents.²¹⁰ These obligations would generally mirror the obligations of FIs under CRS as discussed below. This would be similar to how FATCA obligations apply to FFIs in countries that have not entered into Model 1 IGAs with the U.S. government.²¹¹

3. *Due Diligence Obligations*

The due diligence obligations would be similar to those in CRS, which in turn are similar to FATCA. In summary, participating U.S. FIs would need to follow specific procedures aiming to identify account holders who are foreign tax residents. One design question is whether the identification and reporting should be limited only to foreign tax residents of countries in the CRS Group. While this approach would reduce the attractiveness of the United States as a tax haven for residents of the countries in the CRS Group, residents of other countries would be able to continue using the U.S. financial industry to avoid reporting. Moreover, there would be a risk that taxpayers in countries in the CRS Group could use this incomplete tax transparency by holding funds in the United States through structures in countries that are not members of the CRS Group.²¹² This could undermine the effectiveness of this mechanism even with respect to the countries in the CRS Group.

To address this concern, an alternative approach would be to require that U.S. FIs identify all foreign tax residents. The information on tax residents of countries that have not joined the CRS Group could be retained and made available to these jurisdictions when they join this initiative. This approach is already implemented under CRS.²¹³ This would reduce the risk of taxpayers

208. IRS FATCA Portal, <https://sa.www4.irs.gov/fatca-rup/reg/login/userLogin.do> (last visited July 7, 2023).

209. See *supra* note 69 and accompanying text.

210. This would be similar to the FFI Agreement under FATCA that requires FFIs to comply with the U.S. FATCA obligations. See *supra* text accompanying note 70.

211. See *supra* Section I.A.

212. See *Noked*, *supra* note 43. These attempts may fail where the entities in these structures are passive non-financial entities and the U.S. FIs report these entities’ controlling persons.

213. For example, FIs in Hong Kong are required to identify and report accounts held by residents of 126 jurisdictions, many of which have not yet activated the AEOI relationship with Hong Kong. See Inland Revenue (Amendment) (No. 2) Ordinance 2017.

avoiding reporting by holding structures in countries that have not joined the CRS Group and would incentivize countries to join the CRS Group.

4. *Reporting Obligations*

The content of the required reporting by U.S. FIs would generally be similar to the reporting requirements under FATCA and CRS. However, unlike CRS, which requires that FIs report to their domestic tax authority, the reporting mechanism under this proposal involves direct reporting from the FIs to the relevant governments. Under the FATCA regulations, FFIs must file an annual FATCA Report (IRS Form 8966) electronically with the IRS.²¹⁴ The reported data must follow the specific requirements of the FATCA XML schema.²¹⁵ Similarly, the CRS Group would require U.S. FIs to electronically file an annual CRS report with the CRS Group.

Instead of requiring U.S. FIs to make multiple separate filings with tax authorities in different countries, the CRS Group could set up an electronic system facilitating the centralized filing of the information. Each FI would need to file the information only once in one report. The electronic system would give each country “read” privileges only with respect to the information concerning its tax residents. This system could be modeled after an existing system used for information exchange under CRS and other international reporting standards. The exchange of information between countries under CRS is currently supported by the Common Transmission System, an encrypted centralized filing system maintained by the OECD.²¹⁶ This system is also used for country-by-country reporting (CbCR) and the automatic exchange of tax rulings.²¹⁷ A similar system allowing U.S. FIs to report CRS information to relevant governments could be developed and maintained by the CRS Group.²¹⁸

Notably, FATCA provides detailed rules on what FFIs should do where there are restrictions on the reporting under the applicable local law.²¹⁹ In these situations, FFIs should generally request that account holders provide a waiver of the legal restrictions.²²⁰ If such a waiver is not provided within a reasonable period, the FFI is required to close the account.²²¹ Additionally, the FFI is required to impose withholding on certain payments made to such recalcitrant account holders and report information about their accounts on an aggregate

214. IRS Form 8966, <https://www.irs.gov/forms-pubs/about-form-8966>.

215. IRS, Pub. 5124: FATCA XML Schema v2.0, <https://www.irs.gov/pub/irs-pdf/p5124.pdf>.

216. For more on the Common Transmission System, see OECD, Forum on Tax Administration, <https://www.oecd.org/tax/forum-on-tax-administration/> (last visited July 7, 2023); Eliza Mik & Noam Noked, *Blockchain and Tax Administration: A Critical Assessment*, 50 AUSTL. TAX REV. 180 (2021).

217. See OECD, *supra* note 216.

218. The details regarding the development and the maintenance of this electronic system could be provided in the multilateral agreement between the members of the CRS Group.

219. These situations typically arise where FFIs are subject to bank secrecy obligations, privacy protection rules, or other restrictions on their ability to report information to the IRS. I.R.C. § 1471(b)(1)(F).

220. *Id.*

221. Treas. Reg. § 1.1471-4(i)(1).

basis.²²² The reporting obligations under the proposed mechanism could include similar rules to address similar issues.²²³

5. *Penalties on Non-Participating FIs*

The penalties for non-participating FIs (i.e., FIs that do not enter into a CRS FI Agreement and comply with its terms), could be modeled after FATCA's penalties for non-participating FFIs. FATCA's penalties for non-participation come in the form of withholding. First, FATCA subjects non-participating FFIs to 30% withholding on certain withholdable payments from a U.S. source.²²⁴ Withholdable payments include FDAP income and the gross proceeds from the sale of any property that can produce FDAP income.²²⁵ The institutions responsible for this withholding are defined broadly as "withholding agents" and often involve U.S. FIs.²²⁶ The possibility of losing such a large fraction of U.S. source income creates a significant disincentive against FATCA non-participation among FFIs that receive these types of payments.

The second type of relevant withholding under FATCA involves so-called "passthru payments." Passthru payments are generally understood to mean payments between different FFIs. However, the definition of "passthru payments" has not yet been provided by the U.S. Treasury.²²⁷ The FATCA FFI Agreement requires participating FFIs to withhold a 30% tax on all passthru payments made to non-participating FFIs.²²⁸ This withholding obligation will become effective after the definition of "passthru payments" is provided in the FATCA regulations. Those participating FFIs that are prohibited from withholding under non-U.S. law must close, block, or transfer the relevant accounts.²²⁹

The threat of potential withholding on yet-to-be-defined passthru payments between FFIs has proven to be an effective deterrent against doing business with non-participating FFIs.²³⁰ As a result of this possible withholding, even FFIs that do not receive any U.S. source payments require that other FFIs with which they do business must be FATCA compliant.²³¹ The resulting market practice is that

222. Treas. Reg. §§ 1.1471-4(a)(1), 1.1471-5(g)(1), 1.1471-4(d)(6).

223. CRS does not include these rules because FIs should be required to report under local law, and thus these complications should not arise. However, the proposed mechanism would apply to U.S. FIs and FIs in non-cooperative countries which may be subject to legal restrictions on the reporting of their clients.

224. I.R.C. §§ 1471(a), 1472(a); Treas. Reg. §§ 1.1471-2(a)(1), 1.1472-1(a).

225. Treas. Reg. § 1.1473-1(a).

226. A withholding agent is defined as "any person, U.S. or foreign, in whatever capacity acting, that has the control, receipt, custody, disposal, or payment of a withholdable payment or foreign passthru payment." Treas. Reg. § 1.1473-1(d).

227. Treas. Reg. § 1.1471-5(h) (reserving the definition of "foreign passthru payment").

228. Treas. Reg. § 1.1471-4(b).

229. Treas. Reg. § 1.1471-4(a)(1).

230. For further discussion on the practical implications of the risk of FATCA withholding on transactions, see Slaughter & May, *supra* note 67, at 20.

231. Participating FFIs would incur costs when dealing with non-participating FFIs. First, costs would be incurred when complying with the withholding requirements and determining whether such

agreements between FFIs frequently include representations that they are FATCA compliant and warranties if they incur damages due to another party's FATCA non-compliance. Consequently, in an interconnected financial industry, non-compliance with FATCA is not a viable option for foreign banks, funds, insurance companies, and many other FFIs.

FATCA's withholding provisions are even more potent when one considers the requirements placed on FFIs that are members of an expanded affiliated group (EAG). As previously mentioned, under the FATCA regulations, "in order for any FFI that is a member of an expanded affiliated group to be a participating FFI, each FFI that is a member of the expanded affiliated group must be a participating FFI" or exempt from FATCA.²³² Thus, to avoid withholding, the group must ensure that all of its FFIs are compliant.

The CRS enforcement mechanism could include penalties similar to FATCA: withholding taxes on payments from the CRS Group's withholding agents to non-compliant U.S. FIs and payments from compliant U.S. FIs to non-compliant U.S. FIs.²³³ While it is possible to adopt identical withholding taxes to FATCA withholding on withholdable payments and the yet-to-be-defined passthru payments, this is not necessary. Like FATCA, the purpose of these withholding obligations is not to tax income and raise revenue but to create a strong incentive to comply with the CRS obligations.²³⁴ Therefore, it is possible to impose costs on non-compliant FIs by adopting simpler forms of withholding.

Similar to FATCA, CRS could require FIs to be compliant on a group basis. Where an EAG includes two or more U.S. FIs, all of them must comply with CRS in order to avoid penalties. Another common situation occurs where an EAG comprises a U.S. FI and an FI in another country that implements CRS. It is possible to pressure the latter FI and the relevant group to ensure compliance by the whole group, including the U.S. FI. For example, regulators in CRS-implementing countries could consider revoking or not renewing a regulatory license for an FI if its affiliates in other countries do not comply with CRS.

Also, anti-money laundering (AML) rules could provide that non-participating FIs should be considered as posing a high money laundering risk because they maintain financial accounts that are not subject to the international

withholding is required. Second, participating FFIs may not be able to shift the withholding tax to the non-participating FFIs. Third, dealing with FFIs that do not comply with FATCA would probably raise red flags about legal exposure from doing business with a party that does not comply with FATCA. *See id.*

232. Treas. Reg. § 1.1471-4(a).

233. The imposition of withholding taxes by the EU on non-compliant U.S. FIs has been suggested before. *See* Mark Morris, *Proposal to Withhold EU Source Payments on US FI Unless Agree to FATCA Reciprocal AEI* (2015), <https://web.archive.org/web/20220303182429/http://www.the-best-of-both-worlds.com/support-files/non-fatca-reciprocal-proposal.pdf>; Knobel, *supra* note 100, at 18; Noked, *supra* note 100, at 125. This Article is the first to develop this proposal, explore the design considerations, and analyze this policy response in detail.

234. *Cf.* Melissa A. Dizdarevic, *The FATCA Provisions of the HIRE Act: Boldly Going Where No Withholding Has Gone Before*, 79 *FORDHAM L. REV.* 2967, 2976 (2011) (arguing that the use of withholding to elicit compliance with a set of reporting requirements is "both undesirable and unacceptable").

tax transparency standard.²³⁵ This classification would result in greater difficulties doing business with other FIs and parties subject to AML customer due diligence requirements.²³⁶

Finally, it is important to introduce anti-avoidance rules to counter attempts to avoid these withholding taxes and other penalties. For example, FIs might try to avoid the imposition of withholding in the following manner: an FI within one of the countries of the CRS Group could make a payment to a non-U.S. FI in another country; the latter FI could then make a back-to-back payment to a non-participating U.S. FI, thereby avoiding any withholding penalties. This type of avoidance scheme can be prevented through an anti-avoidance rule that requires withholding on any payment made as part of a plan to be paid directly or indirectly to a non-participating U.S. FI. Similar anti-avoidance rules have been adopted in different countries, including the United States, to prevent step transactions and the use of conduits to avoid tax.²³⁷ CRS requires that jurisdictions have “rules to prevent any Financial Institutions, persons or intermediaries from adopting practices intended to circumvent the reporting and due diligence procedures.”²³⁸ In 2018, the OECD published the CRS Mandatory Disclosure Rules, which require intermediaries to report schemes that facilitate the avoidance of CRS reporting.²³⁹ Similar anti-avoidance rules could apply to the avoidance of the application of the proposed mechanism.

6. *Ensuring Compliance among Participating FIs*

Registering and accepting the terms of the CRS FI Agreement are only the first steps a participating FI should undertake. A compliant FI must satisfy the CRS due diligence and reporting obligations on an ongoing basis. Under CRS, the domestic tax authority is usually responsible for ensuring the ongoing CRS compliance of domestic FIs by carrying out audits and imposing penalties where appropriate. However, a different mechanism should be adopted to ensure compliance of FIs in non-cooperative countries.

The CRS FI Agreement could require the consent of U.S. FIs to audits by accounting firms to confirm that they are in full compliance with the applicable CRS obligations. The Big Four accounting firms have been assisting their FI

235. In general, the Financial Action Task Force (FATF), an intergovernmental organization, develops international standards (referred to as the “FATF Recommendations”) to tackle money laundering and terrorist financing. Many countries have adopted the FATF Recommendations into their domestic laws. Under the FATF Recommendations, FIs and other parties required to carry out AML customer due diligence must follow a risk-based approach under which the AML obligations are generally greater when the money laundering risk is higher. See Financial Action Task Force (FATF), <https://www.fatf-gafi.org/>.

236. See *id.*

237. See, e.g., Ray A. Knight & Lee G. Knight, *A Walk Through the Step-Transaction Doctrine*, TAX ADVISER (May 1, 2021); Treas. Reg. § 1.643(h)-1 (a specific anti-avoidance rule for distributions from foreign trusts through an intermediary).

238. See CRS, *supra* note 15, at 61.

239. OECD, MODEL MANDATORY DISCLOSURE RULES FOR CRS AVOIDANCE AND OPAQUE OFFSHORE STRUCTURES (2018). For further discussion, see Noam Noked, Zachary Marcone & Alison Tsang, *The Expansion and Internationalization of Mandatory Disclosure Rules*, 13 COLUM. J. TAX L. 122 (2022).

clients to comply with their CRS obligations in many countries. The U.S. offices of these and other accounting firms can audit U.S. FIs and report findings of compliance or non-compliance to the CRS Group. Alternatively, U.S. FIs may agree in the CRS FI Agreement to audits by other countries' tax authorities. FATCA takes a similar approach: under the FFI Agreement, the IRS can request additional materials and information from the FFI in cases of suspected non-compliance.²⁴⁰ However, this approach may raise concerns because foreign governments will have access to documents and records of U.S. FIs.²⁴¹ A mechanism that relies on U.S. auditors may raise fewer objections while ensuring ongoing monitoring.

Compliance failures could lead to the FI losing its status and registration as a participating FI, which would lead to the challenges associated with being a non-participating FI.²⁴² As this outcome is harsh, this penalty should be imposed carefully after considering the FI's relevant conduct and remediation actions. The decision regarding penalties for material compliance failures can be made by a committee set up by the CRS Group, following rules and procedures detailed in the multilateral agreement. This is similar to the equivalent penalty under FATCA—revoking FATCA status as a reporting FFI—which the IRS can impose upon the finding of non-compliance.²⁴³

In addition, CRS enforcement provisions could include the FATCA requirement that each FI appoints a responsible officer (RO) who must ensure compliance with the applicable requirements.²⁴⁴ FATCA requires participating FFIs to establish a compliance program led by an RO.²⁴⁵ Typically, the RO is the FFI's chief compliance officer or another senior executive, who may designate others to assist in fulfilling the FFI's compliance responsibilities.²⁴⁶ The RO must ensure that the FFI complies with the FATCA due diligence and reporting requirements.²⁴⁷ The RO is also required to periodically certify to the IRS that the FFI has complied with its FATCA obligations or disclose any non-compliance.²⁴⁸ In case of non-compliance, the certification must detail how the failure will be corrected and how it will be prevented from occurring again.²⁴⁹

Under these rules, there is a clear identification of who is responsible for the organization's FATCA compliance and who will need to report and provide explanations to the IRS in case of a failure to comply. An RO that makes

240. Treas. Reg. § 1.1471-4(f)(4).

241. Also, it is unclear how countries in the CRS Group would coordinate audits of U.S. FIs if such audits are carried out by the tax authorities of these countries.

242. See *supra* Section II.B.3.

243. Treas. Reg. § 1.1471-4(g).

244. Treas. Reg. § 1.1471-4(f). This requirement also applies under Model 2 IGAs. Model 1 IGAs do not require the appointment of an RO and the filing of certifications of compliance with the IRS.

245. *Id.*

246. *Id.*

247. Treas. Reg. § 1.1471-4(c)(7).

248. The RO must file a "certification of effective internal controls" (certifying that a compliance program has been established and reviewed) or a "qualified certification" (disclosing a material failure or potential event of default has been identified and has not yet been rectified). The RO should submit the certifications electronically to the IRS through the FATCA portal. Treas. Reg. § 1.1471-4(f).

249. *Id.*

misleading or fraudulent certifications to the IRS may have legal exposure, as demonstrated in previous instances where the U.S. Department of Justice prosecuted foreign bankers for aiding and abetting tax crimes.²⁵⁰ The CRS FI Agreement could include similar requirements for the appointment of ROs and their responsibilities, including requirements for periodic certifications to be made to the CRS Group through the CRS portal.

C. Advantages, Critiques, and the Potential U.S. Response

As noted, the United States has successfully fended off previous attempts to force it to adopt the international tax transparency standard. In particular, the EU's efforts to pressure the United States to adopt CRS under the threat of blacklisting have failed.²⁵¹ Thus, it is possible that the United States could use its political and economic clout to sink any attempt to implement the proposal in this Article. Why could this proposal succeed where the EU's blacklisting threat failed?

There are several reasons why this proposal is likely to be more successful.²⁵² First, this Article proposes a focused measure that only applies to FIs in non-cooperative countries. In contrast, blacklisting the United States would identify the whole country as a non-cooperative tax jurisdiction, potentially triggering adverse tax measures against a broad spectrum of industries, including those whose actions are unrelated to the tax issues at hand.²⁵³ This might lead to undesirable disruptions to international markets.

Second, the mechanism proposed here is constructive, not punitive; it aims to achieve compliance of U.S. FIs with CRS.²⁵⁴ The role of penalties is limited to incentivizing participation and fulfillment of the CRS due diligence and reporting obligations. U.S. FIs will be able to comply with the CRS requirements without incurring penalties. Unlike blacklisting and other pressure campaigns, which generally try to elicit official state cooperation, the mechanism proposed here gives individual FIs a way to escape penalties even without governmental action.²⁵⁵ This is a key difference between the proposal in this Article and previous calls to impose withholding taxes on all U.S. FIs as a pressure measure

250. See, e.g., U.S. Dep't of Just., *Four Swiss Bankers Charged with Helping U.S. Taxpayers Use Secret Accounts at Swiss Banks to Evade U.S. Taxes* (Feb. 23, 2011), <https://www.justice.gov/opa/pr/four-swiss-bankers-charged-helping-us-taxpayers-use-secret-accounts-swiss-banks-evade-us>.

251. See *supra* note 189 and accompanying text.

252. See *supra* Section II.A for a discussion of the possible reasons for the EU walking back its blacklisting threat.

253. For more on the EU's defensive measures, see Council of the European Union, *supra* note 184.

254. Opinions may differ on what exactly counts as a "punitive" measure. For instance, some may view the imposition of any form of penalty for non-participation as punitive. In contrast, the authors do not view this Article's proposal as punitive because it does not unfairly penalize FIs for the inaction of their governments (as might occur under blacklisting) nor does it deny FIs a reasonable path to avoid penalties.

255. The EU states that the purpose of its blacklist is "to encourage positive change in [countries'] tax legislation and practices," referencing the jurisdictions singled out on the blacklist. *Id.*

until the United States agrees to adopt CRS.²⁵⁶

Third, as a related matter, this proposal's success does not require any action by the U.S. Congress and Treasury. With proper incentives, U.S. FIs will comply with the CRS due diligence and reporting requirements even without any U.S. legislation or regulation mandating it. As noted, it is highly uncertain whether EU blacklisting or similar international pressure campaigns would have moved Congress to enact legislation adopting CRS or reciprocal FATCA.²⁵⁷ Thus, this focused and targeted approach of engaging directly with U.S. FIs without requiring any action from the U.S. government is more likely to succeed than measures that aim to pressure the U.S. government into action.

Furthermore, based on the experience with FATCA, the U.S. government is more likely to enact legislative changes *after* other countries adopt the mechanism proposed here. After the United States adopted FATCA as a unilateral measure, financial industries in many countries lobbied their governments to enter a Model 1 IGA with the United States under which the governments agreed to adopt domestic laws implementing FATCA.²⁵⁸ Similarly, once U.S. FIs become aware of their new CRS responsibilities, it may be in their interest for the United States to join CRS or implement a fully reciprocal FATCA because this would eliminate withholding risks. For these reasons, after the mechanism suggested here is adopted, U.S. FIs may lobby Congress for legislation implementing CRS or a fully reciprocal FATCA.

Finally, as the mechanism suggested here is a focused and non-punitive measure, it is less likely to affect financial markets and the economies of the United States and other countries.²⁵⁹ For this reason, it is less likely to prompt retaliatory action by the U.S. government. This proposed mechanism, unlike blacklisting, need not single out any particular state in a highly publicized list. Instead, it would apply to *all* non-CRS participating countries without singling out the United States. This could help avoid a diplomatic incident between the adopting countries and the United States, thus making the proposal more attractive than blacklisting. Of course, it would also be rather difficult for the United States to argue against countries who adopt a CRS enforcement model that mirrors the United States' own FATCA. U.S. FIs will be required to comply with essentially the same obligations that the United States imposes on all FFIs.²⁶⁰

The U.S. government has repeatedly acknowledged “the need to achieve equivalent levels of reciprocal automatic information exchange” with its IGA partners.²⁶¹ The U.S. government has also stated in the IGAs that it is “committed

256. For proposals that aim to pressure the U.S. government into adopting reciprocal information exchange, see *supra* note 33.

257. See *supra* notes 192-193 and accompanying text.

258. See *supra* notes 84-88 and accompanying text.

259. It is important to note that the United States' adoption and implementation of FATCA did not significantly disrupt financial markets. Given that this Article's proposal is substantially similar to FATCA, it could reasonably be argued that markets will react in a similar way. In contrast, the potential implications of blacklisting the United States are uncertain.

260. See *supra* text accompanying note 61.

261. See *supra* text accompanying note 94.

to further improve transparency and enhance the exchange relationship with [its IGA partners] by pursuing the adoption of regulations and advocating and supporting relevant legislation to achieve such equivalent levels of reciprocal automatic information exchange.” Yet the U.S. government has failed to live up to these commitments.²⁶² With that background, it is unclear on what grounds the United States could object to measures that provide a way for U.S. FIs to fulfill this commitment by applying a similar enforcement mechanism to that which the United States applies to other countries.²⁶³ Also, as a multilateral standard, this Article’s proposal would not be subject to the same forces which disincentivized the U.S. government from making FATCA fully reciprocal.²⁶⁴ Thus, it does not have the same unidirectional inequities as FATCA.

Concerns regarding the infringement of sovereignty have been the main objection countries have raised against the U.S. imposition of FATCA on their financial institutions.²⁶⁵ However, sovereignty has more dimensions than just territorial jurisdiction: tax evasion limits countries’ sovereignty because it reduces their ability to raise revenues.²⁶⁶ Under this rationale, measures such as FATCA could be justified where a non-cooperative country creates the conditions that enable offshore tax evasion, thereby harming other countries.²⁶⁷ While concerns regarding the infringement of sovereignty have been raised against FATCA, it is hard to see how the United States could raise a similar argument against countries demanding that U.S. FIs comply with the same obligations that the United States imposes on FFIs.

Separately, it is important to note that the expansion of CRS compliance not only contributes to the fight against tax evasion, but also supports efforts against non-tax crimes involving illicit funds.²⁶⁸ As is evident from the Pandora

262. As noted *supra* in the text accompanying notes 97-98, the Obama Administration’s attempts to make FATCA fully reciprocal were half-hearted and ultimately not passed by Congress.

263. Compare this to the United States’ objection to other countries’ digital services taxes, where it has argued that these taxes unfairly target U.S. MNEs. *See, e.g.*, U.S. Trade Representative (USTR), Status Update on Digital Services Tax Investigations of Brazil, the Czech Republic, the European Union, and Indonesia (Jan. 13, 2021); Ruth Mason & Leopoldo Parada, *The Legality of Digital Taxes in Europe*, 40 VA. TAX REV. 175, 184, 187 (2020). In contrast, the proposal here only levels the playing field.

264. FATCA was designed and imposed on the world unilaterally. Many countries did not have a choice and simply had to accept an IGA designed by the United States. The proposal here, like CRS, would be developed multilaterally by several countries. *See supra* Section I.A.

265. *See, e.g.*, J. Richard (Dick) Harvey, *FATCA — A Report from the Front Lines*, TAX NOTES 713 (Aug. 6, 2012); Scott D. Michel & H. David Rosenbloom, *FATCA and Foreign Bank Accounts: Has the U.S. Overreached?*, 62 TAX NOTES INT’L 709 (May 30, 2011); Peter Nelson, *Conflicts of Interest: Resolving Legal Barriers to the Implementation of the Foreign Account Tax Compliance Act*, 32 VA. TAX REV. 387, 399 (2012) (“Commentators have suggested that in addition to posing compliance problems for FFIs, FATCA could be viewed as a challenge to the sovereignty of foreign countries over their own financial services industries.”).

266. *See* Leo Ahrens & Fabio Bothner, *The Big Bang: Tax Evasion After Automatic Exchange of Information Under FATCA and CRS*, NEW POL. ECON. (2020) (“[T]ax evasion deprives governments of urgently needed revenue because of missed capital taxes . . . and low tax rates due to international tax competition. . . . It thus undermines their ability to implement distributive policies as they see fit, which in effect limits their sovereignty[.]”).

267. *See id.*

268. *See, e.g.*, Bello Umar, Martins Mustapha Abu & Zayyanu Mohammed, *Strategies for Preventing Illicit Financial Flows in Developing Countries*, 23 J. MONEY LAUNDERING CONTROL 601

Papers, some of the individuals who have funneled funds into the United States may have been involved in corruption, money laundering, and other crimes.²⁶⁹ Eliciting CRS compliance from U.S. FIs would increase financial transparency in the United States and help to expose these crimes, which tend to remain hidden without leaks and journalistic investigation. The OECD has noted that the adoption of CRS supports existing multilateral efforts to target money laundering, terrorist financing, and the financing of weapons of mass destruction.²⁷⁰ Therefore, applying CRS to U.S. FIs is not solely a matter of tax enforcement. The implementation of the measures outlined in this Article would make it more difficult for criminals to conceal and profit from their illicit activities. This has important implications for developing countries affected by corruption and money laundering.²⁷¹ Moreover, the potential of this proposal to rein in non-tax crimes may increase the perceived benefits a country will receive if it joins the CRS Group.

While the mechanism proposed in this Article may be more effective than other measures, it is still uncertain whether a sufficiently large group of countries would adopt it. As noted earlier, this mechanism would be effective only if it were adopted by a group of countries that carry sufficient collective weight to pressure U.S. FIs into cooperating.²⁷² Some countries harmed by tax evasion and illicit financial flows may be unable or unwilling to act. For example, some governments might be captured or influenced by local elites that benefit from the opacity of the U.S. financial system. Other governments may not be interested in adopting a mechanism because of concerns about the potential U.S. response or doubts about substantial revenue gains. U.S. FIs will undoubtedly object to

(Oct. 25, 2020) (arguing that automatic exchange of tax information will support efforts to fight illicit financial flows); ANDRES KNOBEL & MARKUS MEINZER, AUTOMATIC EXCHANGE OF INFORMATION: AN OPPORTUNITY FOR DEVELOPING COUNTRIES TO TACKLE TAX EVASION AND CORRUPTION (June 2014); Vokhid Urinov, *Developing Country Perspectives on Automatic Exchange of Tax Information*, L. SOC. JUST. GLOB. DEV. (2015); Sadiq & Sawyer, *supra* note 112.

269. See, e.g., Fitzgibbon et al., *supra* note 10.

270. See OECD, TOOLKIT FOR THE IMPLEMENTATION OF THE STANDARD FOR AUTOMATIC EXCHANGE OF FINANCIAL ACCOUNT INFORMATION 13 (2021) (“Consequently, [CRS] requires compliance with key elements of the FATF recommendations and supervision of the implementation of the obligations by Financial Institutions.”). The FATF recommendations are part of a growing international effort to target “money laundering, terrorist financing and the financing of proliferation of weapons of mass destruction.” See Financial Action Task Force (FATF), *International Standards on Combating Money Laundering and the Financing of Terrorism & Proliferation* (2012, updated Mar. 2022).

271. See, e.g., Dev Kar & Joseph Spanjers, *Global Financial Integrity, Illicit Financial Flows from Developing Countries: 2004–2013* (Dec. 2015) (finding that cumulative illicit financial flows from developing countries between 2004 and 2013 amounted to nearly eight trillion U.S. dollars and recommending the widespread adoption of tax information exchange); Global Financial Integrity, *Illicit Financial Flows to and From 148 Developing Countries: 2006–2015* (Jan. 2019). There is also evidence that developing countries are more exposed to tax avoidance and profit shifting. See Niels Johannesen, Thomas Torslov & Ludvig Wier, *Are Less Developed Countries More Exposed to Multinational Tax Avoidance? Method and Evidence from Micro-Data*, 34 WORLD BANK ECON. REV. 790 (2020).

272. The United States may be the only country that possesses sufficient economic power to effectively impose a unilateral standard, such as FATCA, globally. Thus, it would likely be insufficient for a single country to unilaterally adopt the proposal we have outlined in this Article. In order for the proposal to carry enough weight to force U.S. FIs to comply (or to compel the U.S. Congress to act), several countries should act in concert, thereby reaching levels of economic power that are much greater than any individual country in the group would possess. This is why multilateral action against the United States is preferred over unilateral or bilateral moves.

this proposal and will likely lobby against it if countries consider it.²⁷³

Thus, we cannot make any prediction regarding the likelihood that countries will adopt the proposal here or any policy to address this problem. If and when countries decide to seriously tackle this issue, our view is the proposal developed here would be more effective than other measures.²⁷⁴

III. WIDER APPLICATIONS

The United States' emergence as a tax haven is a result of a weakness in global governance.²⁷⁵ In recent years, the OECD has taken the lead in the development of international tax standards.²⁷⁶ However, OECD decision-making requires consensus among its members.²⁷⁷ The EU has played a key role in requiring broad international implementation—under the threat of blacklisting—of the standards developed by the OECD and other EU requirements.²⁷⁸ As recent experience suggests, while the EU may be able to pressure countries such as South Korea and smaller jurisdictions to comply with its requirements, it has failed to do so with the United States.²⁷⁹ This underscores a major challenge in the international governance framework: how can countries respond when another country's non-participation in an international standard threatens the efficacy of that standard?

273. Notably, FATCA was enacted very quickly as a revenue raising measure in a spending bill. See Byrnes, *supra* note 61. The proposal in this Article would require a longer time to materialize, during which a stronger opposition could form.

274. The proposal outlined here could be complemented by other measures. For example, governments could explore adopting a multilateral whistleblower program or coordinating domestic whistleblower programs to incentivize disclosures by employees and insiders of FIs that aid and abet offshore tax evasion. For further discussion on tax whistleblower programs, see David Masclet, Claude Montmarquette & Nathalie Viennot-Briot, *Can Whistleblower Programs Reduce Tax Evasion? Experimental Evidence*, 84 J. BEHAV. EXP. ECON. 1, 10 (2019); Jaron H. Wilde, *The Deterrent Effect of Employee Whistleblowing on Firms' Financial Misreporting and Tax Aggressiveness*, 92 ACCOUNT. REV. 247 (2017); Alon Faiman, *No One Likes a Tattle Tale, or Do They: Why the Implementation of Broad Definition of Collected Proceeds under the Tax Whistleblower Program is a Major Win for Whistleblowers and Taxpayers*, 12 CHARLESTON L. REV. 173 (2018).

275. See generally MICHAEL BARNETT & RAYMOND DUVALL, *POWER IN GLOBAL GOVERNANCE* (2004); ANTHONY MCGREW & DAVID HELD, *GOVERNING GLOBALIZATION: POWER, AUTHORITY AND GLOBAL GOVERNANCE* (2002); TIMOTHY SINCLAIR, *GLOBAL GOVERNANCE* (2013).

276. 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 (2005); Arthur J. Cockfield, *Shaping International Tax Law and Policy in Challenging Times*, 54 STAN. J. INT'L L. 223 (2018); Allison Christians & Laurens van Apeldoorn, *The OECD Inclusive Framework*, BULLETIN FOR INT'L TAX'N 226 (2018); Mason, *supra* note 52, at 369.

277. For further discussion, see Rosenbloom et al., *supra* note 49, at 61-66.

278. See *supra* Section II.A and the evidence documented in Shu-Yi Oei, *World Tax Policy in the World Tax Policy? An Event History Analysis of OECD/G20 BEPS Inclusive Framework Membership*, 47 YALE J. INT'L L. 199 (2022).

279. To date, South Korea is the largest economy that was listed by the EU as a non-cooperative jurisdiction for tax purposes. See Noam Noked, *From Tax Competition to Subsidy Competition*, 42 U. PENN. J. INT'L L. 445, 474-78 (2020) for further discussion. The list adopted by the EU on February 14, 2023 includes: American Samoa, Anguilla, Bahamas, British Virgin Islands, Costa Rica, Fiji, Guam, Marshall Islands, Palau, Panama, Russia, Samoa, Trinidad and Tobago, Turks and Caicos Islands, U.S. Virgin Islands, and Vanuatu. See Council of the European Union, *Taxation: EU List of Non-Cooperative Jurisdictions*, <https://www.consilium.europa.eu/en/policies/eu-list-of-non-cooperative-jurisdictions/> (last visited July 7, 2023). For further analysis on when blacklisting can be an effective policy tool, see Katrin Eggenberger, *When is Blacklisting Effective? Stigma, Sanctions and Legitimacy: The Reputational and Financial Costs of Being Blacklisted*, 25 REV. INT'L POLIT. ECON. 483 (2018).

The model response discussed in this Article has potential applications in other international settings. A similar mechanism could be adopted where a legal standard aims to affect the actions of certain actors in a recalcitrant country. The key elements of this model are distilled below. Notably, none of these elements are specific to tax transparency or tax law in general.

First, a group of like-minded countries could adopt rules imposing obligations on certain actors in non-cooperative countries.²⁸⁰ These rules may be adopted in domestic laws, regulations, and multilateral agreements.²⁸¹ This mechanism is more likely to succeed if it requires the cooperation of non-governmental actors in globally interconnected industries given that such actors are more likely to respond to penalties on cross-border transactions.²⁸²

Second, under these rules, the relevant foreign actors can either comply with these obligations or face penalties. These penalties could include withholding taxes and other regulatory and pecuniary disincentives. In addition to withholding taxes, other possible disincentives for non-participation should be considered. There should be an administratively easy way to distinguish between participating and non-participating actors, so that only the latter are subject to penalties. This could be achieved by assigning a unique, publicly searchable identification number to participating actors.²⁸³ The administration of penalties such as withholding taxes on non-participating actors could be part of the compliance obligations of participating actors.²⁸⁴

Third, such a mechanism should facilitate direct engagement between the participating governments, or a body representing them, and the participating non-state actors.²⁸⁵ This direct engagement could be formalized in agreements under which relevant actors commit to fulfill the applicable obligations. None of the obligations under the agreement would require the involvement of non-cooperative governments.

Fourth, participating actors should be monitored to ensure compliance with the applicable requirements. Third parties, such as local accounting firms, could conduct such monitoring.²⁸⁶ The participating actors could also be required to establish compliance programs, identify individuals responsible for compliance, and file periodic certifications regarding their compliance or compliance missteps.²⁸⁷

280. These are countries who refuse to adopt the international standard and impose these obligations on the relevant actors under their domestic laws.

281. *See supra* Section II.B.1.

282. The financial industry is an example of a largely private sector and globally interconnected industry. Multinational enterprises are another example. If the actors are governmental entities, the effect of this mechanism would be similar to a government-to-government pressure campaign. If the relevant actors are insulated from the rest of the world, it might be hard to create a disincentive for non-participation.

283. *See supra* Section II.B.2.

284. *See supra* Section II.B.5.

285. *See supra* Section II.B.2.

286. The proposal here suggests that participating U.S. FIs' compliance with the CRS obligations be monitored by U.S. accounting firms. *See supra* Section II.B.6.

287. *See id.*

This mechanism would no longer apply if the relevant country adopts the international standard and requires its domestic actors to comply with the relevant obligations under its domestic law. This means that this mechanism acts as a regulatory fail-safe, as discussed in Section A below. Section B explores potential applications of this model in other tax and non-tax contexts.

A. Regulatory Fail-Safes, Advantages, and Concerns

As coined by Ruth Mason, fiscal and regulatory fail-safes are policies that ensure the enforcement of international tax regimes even when full global cooperation cannot be attained.²⁸⁸ Fiscal fail-safes function to prevent double non-taxation. For example, the newly introduced global minimum tax regime incorporates a fiscal fail-safe.²⁸⁹ Under this recent international tax reform, countries agree to a minimum tax of 15% on multinational enterprises (MNEs).²⁹⁰ The design of the global minimum tax is generally similar to a controlled foreign corporation regime under which the residence country of the MNE's ultimate parent entity imposes a top-up tax on low-taxed subsidiaries and branches in other countries.²⁹¹ However, suppose an MNE tries to avoid the top-up tax by locating its headquarters in a non-participating country. In that case, a secondary tax rule takes effect: the top-up tax will apply to the MNE's subsidiaries in participating countries.²⁹² Consequently, MNEs will pay a similar global top-up tax irrespective of whether they are headquartered in a participating country. Moreover, MNEs headquartered in non-participating countries would likely have higher compliance burdens because they may need to pay the top-up tax in multiple jurisdictions instead of one.²⁹³

288. See Mason, *supra* note 52, at 376-80.

289. PILLAR TWO MODEL RULES, *supra* note 201.

290. OECD/G20 BASE EROSION AND PROFIT SHIFTING PROJECT, STATEMENT ON A TWO-PILLAR SOLUTION TO ADDRESS THE TAX CHALLENGES ARISING FROM THE DIGITALISATION OF THE ECONOMY 4 (Oct. 8, 2021).

291. OECD/G20 Base Erosion and Profit Shifting Project, *Tax Challenges Arising from Digitalisation — Report on the Pillar Two Blueprint: Inclusive Framework on BEPS*, at 14 (2020). This description refers to the Income Inclusion Rule (IIR), which is the primary rule under GloBE. For further background on GloBE, related matters and critiques, see Rueven Avi-Yonah, *Build Back Better and Pillar Two: Two Alternative Scenarios* (U. Michigan Pub. L., Research Paper No. 22-012, 2021); Joachim Englisch, *International Effective Minimum Taxation — Analysis of GloBE (Pillar Two)* (Apr. 18, 2021), available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3829104; Joachim Englisch & Johannes Becker, *International Effective Minimum Taxation — The GLOBE Proposal*, 11 WORLD TAX J. 483 (Sept. 20, 2019); Cedric Dollefeld et al., *Tax Administrative Guidance: A Proposal for Simplifying Pillar Two*, 50 INTERTAX 231 (Dec. 13, 2021); Jefferson VanderWolk, *OECD Statement on Pillars One and Two Leaves Many Questions Unanswered*, BLOOMBERG TAX (Oct. 13, 2021); Vikram Chand et al., *Tax Treaty Obstacles in Implementing the Pillar Two Global Minimum Tax Rules and a Possible Solution for Eliminating the Various Challenges*, 14 WORLD TAX J. 3 (2022); Susan C. Morse, *The Quasi-Global GILTI Tax*, 18 PITT. TAX REV. 273 (2021); Richard M. Bird, *Are Global Taxes Feasible?*, 25 INT'L TAX PUB. FIN. 1372 (2018); Ruth Mason, *The Transformation of International Tax*, 114 AM. J. INT'L L. 353 (2020); Kimberly Clausing et al., *Ending Corporate Tax Avoidance and Tax Competition: A Plan to Collect the Tax Deficit of Multinationals* (UCLA Sch. L., Law-Econ Research Paper No. 20-12, 2021); Leopoldo Parada, *Full Taxation: The Single Tax Emperor's New Clothes*, 24 FLA. TAX REV. 729 (2021); Daniel Shaviro, *What Are Minimum Taxes, and Why Might One Favor or Disfavor Them?*, 40 VA. TAX REV. 395 (2021); GARY CLYDE HUFBAUER, DANGERS LURKING IN THE OECD TAX PROPOSALS (2021).

292. PILLAR TWO MODEL RULES, *supra* note 201, art. 2.5.2.

293. HM TREASURY, OECD PILLAR 2: CONSULTATION ON IMPLEMENTATION 53-54 (Jan. 2021).

Another fiscal fail-safe can be found in the anti-hybrid rules of Action 2 of the OECD's project on base erosion and profit shifting (BEPS).²⁹⁴ These rules include primary rules that aim to achieve consistency in the tax treatment of certain cross-border payments and defensive rules that allow participating countries to impose taxes where other countries do not exercise their taxing rights under the primary rules.²⁹⁵

A similar concept could also apply to regulatory and reporting requirements. BEPS Action 13, which requires the filing of a country-by-country report (CbCR), includes a regulatory fail-safe.²⁹⁶ Under this standard, MNEs are required to file a CbCR in the country where they are headquartered.²⁹⁷ However, if the MNE is headquartered in a non-participating jurisdiction, then each of the MNE's subsidiaries in participating jurisdictions will be required to file the CbCR locally.²⁹⁸ As a result, these reporting obligations cannot be avoided by locating the MNE's headquarters in a non-participating country; such an MNE would need to report the same information in multiple jurisdictions.²⁹⁹ This could be the reason why the United States accepted the CbCR standard despite its potentially adverse impact on U.S. MNEs.³⁰⁰

The proposal in this Article constitutes a similar regulatory fail-safe for CRS. Under current rules, an FI can avoid CRS reporting by locating in a non-participating country such as the United States. The proposed mechanism would only apply to FIs in non-cooperative jurisdictions that do not implement CRS. As discussed in detail in Part II, FIs in these jurisdictions would need to comply with the CRS obligations by reporting the required information directly to the relevant CRS-implementing governments or face penalties. This mechanism would make it difficult for FIs in non-cooperative countries to avoid CRS reporting. Interestingly, FATCA has evolved from a unilateral regime based on the enforcement provisions discussed here into a largely bilateral regime with many IGA partners implementing FATCA under their domestic laws. In other words, the U.S. government first introduced the unilateral regulatory fail-safe and only then adopted the bilateral framework. In CRS, the regulatory fail-safe can be added to the existing CRS regime. Nonetheless, the effect would likely be similar.

While this may be an effective mechanism, the main concern is the potential infringement of other countries' sovereignty.³⁰¹ As noted, this has been a significant concern in the debate about FATCA.³⁰² However, as argued in the

294. OECD, *NEUTRALIZING THE EFFECTS OF HYBRID MISMATCH ARRANGEMENTS* (2015).

295. *Id.* For further discussion, see LEOPOLDO PARADA, *DOUBLE NON-TAXATION AND THE USE OF HYBRID ENTITIES: AN ALTERNATIVE APPROACH IN THE NEW ERA OF BEPS* (2018).

296. OECD, *TRANSFER PRICING DOCUMENTATION AND COUNTRY-BY-COUNTRY REPORTING, ACTION 13 – 2015 FINAL REPORT* (2015).

297. *Id.*

298. *Id.*

299. See Mason, *supra* note 52, at 378.

300. For the U.S. government's opposition to the BEPS project, see, e.g., Jeremy Scott, *Can the United States Kill BEPS?*, FORBES (June 16, 2015).

301. However, as noted by Mason, under fiscal and regulatory fail-safes, this is a feature, not a bug. See Mason, *supra* note 52, at 376-80.

302. See *supra* note 265 and accompanying text.

context of offshore tax evasion, a country infringes on the sovereignty of other countries when it enables tax evasion that limits other countries' ability to raise taxes.³⁰³ The justification for adopting this mechanism would be stronger where its purpose is to eliminate substantial negative externalities, such as in the context of offshore tax evasion.

Moreover, adopting this mechanism as a regulatory fail-safe as part of multilateral agreements for the implementation of these standards could decrease the "competitiveness" threat for participating countries. Countries may be concerned that if they adopt a standard that one or more competitors do not implement, investors will move to countries that do not follow this policy or that local businesses may be at a disadvantage when competing against actors in other countries.³⁰⁴ The mechanism suggested here could reduce this concern and prevent a harmful race to the bottom.³⁰⁵

B. Potential Applications

How can a similar mechanism be implemented in other contexts? This Section discusses two potential applications. The first concerns mandatory disclosure rules (MDRs). In general, MDRs require intermediaries (such as lawyers, accountants, tax advisors, and trustees) to disclose information about their clients' tax schemes to the relevant tax authority. Since MDRs were introduced in the United States in the 1980s, they have been adopted in many countries—more than thirty countries have adopted new MDRs in the past five years alone.³⁰⁶ However, existing MDRs suffer from a significant limitation: these reporting obligations do not generally apply to *foreign* enablers of tax avoidance and evasion.³⁰⁷ As revealed in the Pandora Papers, tax avoidance and evasion are frequently enabled by the services of intermediaries located in foreign countries.³⁰⁸ While the U.S. MDRs require U.S. lawyers to report certain transactions, how can the IRS obtain information from the relevant advisors if they are located in another country?

As a solution, countries can adopt an international, multilateral MDR standard with information exchange among participating countries.³⁰⁹ However, what should participating countries do if a country refuses to join the international agreement and implement the standard? By being a holdout, a country could even benefit from more capital and business flowing to its intermediaries if it becomes the only country that does not implement the standard. As a solution, similar to the proposal in this Article, the international MDR standard could include a regulatory fail-safe that would apply where a

303. See Ahrens & Bothner, *supra* note 266.

304. For further discussion on these considerations, see Rosenbloom et al., *supra* note 49, at 85.

305. See *id.*

306. For further background on MDRs, see OECD, MANDATORY DISCLOSURE RULES, ACTION 12 - 2015 FINAL REPORT (2015); Noked et al., *supra* note 239.

307. See Noam Noked & Zachary Marcone, *Targeting Tax Avoidance Enablers*, 13 UC IRVINE L. REV. (forthcoming).

308. See *id.*

309. See *id.*

country refuses to participate. Under the solution proposed here, intermediaries in the non-participating country would be able to comply with the regime by reporting directly to the participating countries or face penalties.³¹⁰

The application of this model is not limited to tax reporting regimes either. While a detailed discussion on how this mechanism could be extended to specific non-tax standards is outside the scope of this Article, it is worth considering what international standards could benefit from it. One area that is notoriously plagued by government non-cooperation is climate change.³¹¹ Large polluting nations have mixed records on climate action.³¹² Moreover, the importance of corporate action has been recognized, given that corporations undertake and oversee activities that lead to substantial carbon emissions.³¹³

Some have proposed a corporate climate disclosure framework to monitor these activities and hold corporations accountable.³¹⁴ The Task Force on Climate-Related Disclosures (TCFD) and other organizations have proposed the adoption of mandatory climate disclosure laws by countries around the globe.³¹⁵ Individual companies can file disclosures even if their home governments do not mandate them.³¹⁶ Corporations can, for example, submit disclosures to the Carbon Disclosure Project (CDP), a non-profit organization that publishes disclosures and develops standards for them.³¹⁷ Some corporations have faced pressure from investors, customers, and others to file disclosures with CDP.³¹⁸ Although the number of corporations filing disclosures is growing each year, many businesses still do not report, and those who do so voluntarily may not submit high-quality disclosures.³¹⁹ As such, calls remain for more forceful action, such as mandatory disclosure.³²⁰

However, what can be done if a large economy refuses to implement mandatory corporate climate disclosures? The mechanism explored in this Article is a possible solution. A group of countries could require all corporations of a certain size, type, and industry to comply with climate disclosure obligations or face withholding taxes and other penalties. The reporting infrastructure

310. *See id.*

311. *See, e.g.,* Aaditya Mattoo & Arvind Subramanian, *Greenprint: Three Big Changes for Countries to Cooperate on Climate Change*, CTR. GLOB. DEV. (Jan. 2013).

312. *See, e.g.,* Navin Singh Khadka, *COP26: Did India Betray Vulnerable Nations?*, BBC (Nov. 16, 2021). For an overview of the United States' mixed history on climate, see Vicki Arroyo, *Keynote Address: A Brief History of U.S. Climate Policy and a Call to Action*, 34 MD. J. INT'L L. 1 (2019).

313. *See* Lucy Colback, *The Role of Business in Climate Change*, FIN. TIMES (Dec. 18, 2020).

314. *See* TASK FORCE ON CLIMATE-RELATED FINANCIAL DISCLOSURES, FINAL REPORT: RECOMMENDATIONS OF THE TASK FORCE ON CLIMATE-RELATED FINANCIAL DISCLOSURES (June 2017).

315. *See, e.g.,* TASK FORCE ON CLIMATE-RELATED FINANCIAL DISCLOSURES, TASK FORCE ON CLIMATE-RELATED DISCLOSURES: 2021 STATUS REPORT 6 (2021); John Armour, Luca Enriques & Thom Wetzer, *Mandatory Corporate Climate Disclosures: Now, but How?*, 2021 COLUM. BUS. L. REV. 1085 (2021).

316. *See* CARBON DISCLOSURE PROJECT, <https://www.cdp.net/en> (last visited July 7, 2023).

317. *Id.*

318. *See* CLIMATE DISCLOSURE PROJECT, *Why Disclose as a Company?*, <https://www.cdp.net/en/companies-discloser> (last visited July 7, 2023).

319. *See* ERNST & YOUNG, COVERAGE AND QUALITY OF CLIMATE-RELATED DISCLOSURES REMAIN BELOW GLOBAL AVERAGES IN INDIA: EY GLOBAL CLIMATE RISK DISCLOSURE BAROMETER 2021 (July 25, 2021).

320. *See* *G7 Backs Making Climate Risk Disclosure Mandatory*, REUTERS (June 5, 2021).

already developed by TCFD and CDP provides a potential framework for the reporting obligations.³²¹ Furthermore, this mechanism could extend beyond disclosure obligations. The requirements for participating corporations may include adhering to certain environmental standards. Audits or other inspection measures could be applied to ensure compliance.

MDRs and corporate climate disclosures are just two examples of how the regulatory fail-safe explored here can be applied in other contexts. These contexts are not limited to tax and climate, and, more generally, this mechanism may be applicable to multilateral regimes that require actors in different jurisdictions to adhere to certain standards. This mechanism could serve as a backstop that would incentivize countries to enter into multilateral agreements, which remain the preferred way to adopt and implement international standards.

CONCLUSION

The United States' emergence as one of the world's preeminent tax havens is a cause for international concern. The path to this reality, as examined in this Article, has been facilitated by the United States' refusal to reciprocate financial account reporting, coupled with the no or low taxation of foreigners holding U.S. structures. Ironically, the U.S. financial industry's conduct, as revealed in the Pandora Papers, mirrors that of the Swiss bank industry more than a decade ago. With more information revealed on the global problem emanating from the United States' role as a tax haven, it is a matter of time until countries seek an effective response to protect their tax bases.

This Article has made three contributions. First, it examined the legal factors that have led to the rise of the United States to its current position as a tax haven. Second, it proposed a comprehensive and workable policy response that does not require any action by the U.S. Congress or Treasury. This solution, if implemented, could extend the international transparency standard to the U.S. financial industry and prevent abuse by foreign tax evaders. Third, it argued that the model response developed here could extend well beyond tax to resolve cooperation problems in other international settings.

321. See Task Force on Climate-related Financial Disclosures, *supra* note 314; Climate Disclosure Project, Guidance and Questionnaires, <https://www.cdp.net/en/guidance> (last visited July 7, 2023).