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In Reversal, IRS Gives Amnesty To Owners Of Secret Israeli Bank Accounts

Yesterday, as the Department of Justice was trumpeting its latest criminal case charging offshore tax evasion—this one against [billionaire Beanie Babies creator](#) Ty Warner—the Internal Revenue Service was quietly faxing letters to lawyers for some other folks with once secret offshore accounts, informing them they would meet a happier fate. The letters are noteworthy because they represent an about face for the IRS. In the letters, the IRS readmitted to its criminal amnesty program several dozen former customers of Bank Leumi le-Israel Ltd. that it had abruptly [kicked out of the program last March](#), after they had been cleared to participate.

The disqualifications, [first reported by Forbes](#), drew howls of protest from tax defense lawyers, who warned that other miscreants would now be reluctant to participate in the Offshore Voluntary Disclosure Program (OVDP), which has been a big money maker for the shrinking and beleaguered IRS. Since the OVDP was launched in February 2009, some 39,000 taxpayers have disclosed their hidden accounts and have paid \$5.5 billion in back taxes, interest and penalties, in return for amnesty from prosecution. **“I think 100%, definitely, it (the March disqualifications) kept people from cooperating,”** said Los Angeles tax attorney [Pedram Ben-Cohen](#), who had more than a half dozen clients reinstated to the amnesty program yesterday. He added that he believed IRS officials, in the midst of the controversy over the agency’s handling of tax exemption requests from Tea Party affiliated groups, may have decided that they did not need **“another thing damaging their reputation.”**

“Common sense prevailed,” exalted Robert E. McKenzie, a partner at Chicago’s Arnstein & Lehr, who has one client who was kicked out of the program in March and reinstated yesterday. “It’s hard enough to convince a client to trust IRS absent a situation where it arbitrarily revokes a clearance,” he added. Charles Rettig, of Hochman, Salkin, Rettig, Toscher & Perez, the big West Coast tax defense firm, confirmed that several of his firm’s Bank Leumi clients were also readmitted to the program. “The government has obviously reviewed their prior decision and decided to do the right thing by accepting these taxpayers back into the OVDP,” he wrote in an email. (Both Rettig and McKenzie are contributors to the [IRS Watch](#) blog on Forbes.com.)

Failing to disclose on your 1040 that you have a foreign account or accounts

totaling more than \$10,000 is itself a criminal offense and is often accompanied by even more serious tax evasion. Yesterday, the government said that Warner, 69, has [agreed to plead guilty](#) to one count of tax fraud for failing to report \$3.2 million in earnings from a secret account at Swiss bank UBS AG on his 2002 return. With a net worth [Forbes estimates at \\$2.6 billion](#) (along with Beanie Babies-maker Ty, Inc., he owns resorts and hotels, including the New York Four Seasons), Warner ranks as the 209th richest person in the United States. When he enters his plea, he will become the third current member of the Forbes 400 with a felony conviction involving offshore accounts. In 2007, California real estate developer Igor Olenicoff ([#184](#)) [pleaded guilty](#) to filing a false return and admitted hiding more than \$200 million at UBS and other banks. Leandro Rizutto ([#296](#)), founder of Conair, was [convicted in 2002 of depositing millions in kickbacks from suppliers into foreign accounts](#).

Being on the 400 list obviously makes someone a tempting target for prosecutors. In fact, while tens of thousands of Americans had unreported accounts before the current crackdown began, the government has so far criminally charged fewer than 100. Notably, since the start of this year, five who used Israeli banks to evade taxes have pleaded guilty. Others who have recently pleaded guilty had accounts at UBS and at an Indian subsidiary of HSBC Holdings.

The Bank Leumi customers who got their “do not go to jail” cards yesterday will not get off for free. Taxpayers accepted into the current version of the OVDP must file eight years of amended tax returns, pay all back taxes, interest and penalties due (including a 20% accuracy penalty on offshore-related underpayments) and also pay a penalty for failing to file a Report of Foreign Bank and Financial Accounts (or FBAR) with the Treasury—a penalty that in most cases equals 27.5% of the maximum held in the undisclosed offshore accounts during the eight year period. For taxpayers not in the OVDP, the FBAR penalty can be up to half the value in a foreign account for every single year they failed to file; Warner, according to a statement from his attorney, has agreed to pay a \$53.6 million FBAR penalty for his undisclosed which [prosecutors say](#) was worth about \$94 million in late 2002 when he transferred it from UBS to another Swiss bank, Zürcher Kantonalbank. The penalty represents half the account’s highest balance.

Warner himself tried unsuccessfully to enroll in the OVDP in 2009, his lawyer, Gregory Scandaglia, indicated in a statement. But if the government already has a taxpayer under audit, is investigating him, or has his name on a list of taxpayers with secret accounts, he isn’t eligible for the OVDP. The government hasn’t said why Warner was turned down for the OVDP, but by the time he applied, it already had the names of a few hundred UBS customers.

Citing taxpayer confidentiality, an IRS spokesman declined yesterday to say why the Bank Leumi customers were kicked out of the OVDP or why they have now been readmitted. To determine eligibility for the OVDP, defense lawyers first provide the name and Social Security number of a client to the IRS. If the client is given a pre-clearance—meaning he isn’t yet on the IRS’ radar—he sends in a completed and signed questionnaire disclosing his accounts and other details. Providing his answers are considered full and truthful, he then gets a final clearance and pays his money. Some of those kicked out in March had already gotten a final clearance and even paid up,

defense lawyers say.

While an individual accepted taxpayer can be thrown out of the OVDP for lying or for not cooperating with the government, tax lawyers believe the March group expulsions were most likely the result of a communications or administrative glitch within the government; the DOJ or IRS may already have had the taxpayers' names, without the IRS agent who reviewed the Bank Leumi applications knowing it. "I think somebody didn't code the computer (right)," said McKenzie. Last year, several clients of Rettig's firm who had undisclosed accounts at another Israeli bank, Mizrahi Tefahot Bank Ltd., were also kicked out of the OVDP after having been accepted. In an email, Rettig said that so far only Bank Leumi customers have been readmitted, "but we believe others will be readmitted as well."

In April, [Kathryn Keneally](#), the Assistant Attorney General for the Tax Division, [told Forbes that the DOJ would consider "fairness"](#) before deciding whether to prosecute taxpayers kicked out of OVDP. But in a May letter to the IRS, the chair of the New York City Bar's Personal Income Taxation Committee said Keneally's fairness promise was "insufficient at best and injects an aspect of arbitrariness that is inconsistent with the principal benefits of the program: clarity and certainty." Moreover, that letter argued, DOJ would have a tough time winning convictions of any taxpayers who had disclosed information under the OVDP, since defense lawyers would fight to exclude from evidence any information that had been turned over to the IRS after taxpayers got pre-clearance.

While UBS was the first big foreign bank to be targeted for its role enabling U.S. tax cheats (in February 2009 it [paid \\$780 million in fines, penalties and restitution to the U.S.](#) to avoid prosecution), it has since gained lots of Swiss and non-Swiss company. In March, Bank Leumi announced it would take a charge of 340 million shekels (\$91 million) to cover the expense "of investigations that are being conducted by the U.S. authorities concerning customers who are U.S. taxpayers." In addition to the [five individuals who have pleaded guilty](#) to hiding money overseas with the assistance of Israeli banks, three men are awaiting trial in the Central District of California on [charges](#) they ran a tax service with branches across the country that helped clients hide income in secret accounts at the Swiss and Luxembourg branches of two Israeli banks.

[According to Ben-Cohen and to the statement of facts filed in two customers' plea deals, two Israeli banks used their U.S. branches to make so-called back-to-back loans—loans to U.S. residents secured by their secret offshore accounts.](#) In March, Zvi Sperling, an Israeli-born Los Angeles businessman, pleaded guilty to hiding \$4 million in unreported corporate profits in an account at Israeli "Bank A"—an account he opened around 2001 and owned through a front Island of Nevis corporation. According to the statement of facts, he then tapped into that money through loans from Bank A's Los Angeles office. In 2008, Bank A closed its LA office and Sperling moved the money to Israeli Bank B. A representative of Bank B allegedly bragged at a meeting in a Beverly Hills hotel that it "was better able than Bank A to keep the accounts secret." According [to Bloomberg](#), Bank A is Mizrahi Tefahot, and Bank B, Bank Leumi.

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