

*Task Force on Information Exchange
and Financial Privacy*

***REPORT
ON
FINANCIAL PRIVACY,
LAW ENFORCEMENT
AND TERRORISM***

March 25, 2002

Prepared by:



333 N. Fairfax St., Suite 302
Alexandria, VA 22314
www.prosperity-institute.org

Task Force on Information Exchange and Financial Privacy

Statement of Purpose

The Task Force on Information Exchange and Financial Privacy was formed to systematically research and analyze information exchange laws, organizations, mechanisms and proposals and their implications for financial privacy. The Task Force will develop specific proposals that will meet the legitimate needs of the national security and law enforcement communities and the reasonable requirements of tax administration while respecting privacy, including financial privacy.

The Prosperity Institute is an educational and research organization which is tax-exempt under section 501(c)(3) of the Internal Revenue Code. The Prosperity Institute is dedicated to supporting and disseminating research examining the causes of, and impediments to, worldwide prosperity, economic growth and a higher standard of living.

Task Force on Information Exchange and Financial Privacy

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Task Force on Information Exchange and Financial Privacy

Introduction

Prior to the September 11 attacks on the United States, information exchange and money laundering were topics of increasing concern and focus. The primary government initiatives, however, were in the tax administration arena. These initiatives included the OECD harmful tax competition initiative, the proposed United Nations International Tax Organization, the proposed IRS interest reporting regulations, the IRS qualified intermediary (QI) rules and the effective incorporation of “know your customer” (KYC) banking regulations into the U.S. QI rules. After the attacks, there was a renewed interest in money laundering statutes and regulations as a means of aiding government in its anti-terrorism efforts. This was demonstrated, most notably, by the enactment in late October of the International Money Laundering Abatement and Financial Anti-Terrorism Act of 2001.¹

Although there has been a flurry of administrative and legislative activity, it has become clear from Congressional testimony and reports in the U.S. and European news media that the current international information sharing framework is simply inadequate and misdirected for purposes of addressing the threat that terrorism poses to the United States and allied countries. Priorities should be refocused in light of the heightened terrorist threat and the mechanisms that will aid the effort to combat global terrorism should be reviewed.

When the Prosperity Institute convened the Task Force on Information Exchange and Financial Privacy (the “Task Force”), it realized that the needs of law enforcement to combat serious crimes, prevent terrorism and protect national security were of the highest concern.² Accordingly, we considered it necessary to include former high level law enforcement officials on the Task Force. We were also aware that the true agenda of many proponents of greater information exchange had little or nothing to do with criminal law enforcement or national security. Moreover, we believed that protecting the privacy of innocent individuals was an important goal. Finally, we found it troubling that existing information exchange programs and those proposed showed little or no concern about ensuring the information obtained and shared would not be inappropriately used or used by enemies of the United States, to enable terrorism, to promote human rights violations or for other inappropriate purposes.

This report represents the culmination of much work and research during the past nine months. The recommendations contained in this report are “outside of the box.” They constitute a new and different approach to the problem that will simultaneously improve the security of the United States while enhancing the rights of individuals.

¹ Enacted as a component part of the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism (USA PATRIOT ACT) Act of 2001 (H.R. 3162; Public Law No: 107-56, October 26, 2001).

² See, Press Release, July 1, 2001, Prosperity Institute to Form Task Force on Information Exchange and Financial Privacy.

Because implementation of the recommendations would involve a change of course, they may be politically more difficult to achieve than more orthodox approaches. There are many in governments throughout the world that have made a heavy political investment in justifying the current system. In fact, many governments are attempting to exploit the political atmosphere existing in the aftermath of the September 11th attacks to promote a series of information exchange policies designed primarily to enforce tax laws that in practice impede international efforts to apprehend terrorists and criminals. Nevertheless, the Task Force is convinced, for the reasons outlined in this report, that these recommendations would advance the dual objectives, usually portrayed as competing, of improving law enforcement and national security while respecting the rights, enhancing the privacy and maintaining the standard of living of law-abiding Americans.

Task Force on Information Exchange and Financial Privacy

Membership

Chairman

Hon. Mack F. Mattingly

Senior Advisors

Hon. Jack F. Kemp
Hon. Edwin Meese, III, Esq.

Executive Director

David R. Burton, Esq.

Members

Dr. Veronique de Rugy (Cato Institute)
Stephen J. Entin (Institute for Research on the Economics of Taxation)
James W. Harper, Esq. (PolicyCounsel.com, Privacilla.org)
Dr. Lawrence A. Hunter (Empower America)
J. Bradley Jansen (Free Congress Foundation)
Dan Mastromarco, Esq. (Prosperity Institute, Argus Group)
Dr. Daniel Mitchell (Heritage Foundation)
Andrew Quinlan (Center for Freedom and Prosperity)
Dr. Richard W. Rahn (Discovery Institute)
Solveig Singleton, Esq. (Competitive Enterprise Institute)
Mark A. A. Warner, Esq. (Hughes, Hubbard & Reed)
Hon. John Yoder, Esq. (Burch and Cronauer)

Task Force on Information Exchange and Financial Privacy

Bios

Hon. Mack F. Mattingly (Chairman)

Former United States Senator Mack Mattingly is Chairman of the Task Force.

In 1980, Mack Mattingly was elected the first Republican U.S. Senator from Georgia since 1871 and spent six years in the Senate, from 1981 to 1987. He served on the Appropriations Committee, the Banking and Housing Committee, the Ethics Committee, the Joint Economic Committee, and was Chairman of two Senate sub-committees. In 1987, President Ronald Reagan appointed Sen. Mattingly to become the Assistant Secretary General for Defense Support at NATO Headquarters in Belgium. As the highest ranking American at the International Headquarters of NATO, he served from 1987 to 1990. In 1992, President George Bush appointed Sen. Mattingly to become the Ambassador of the United States of America to the Republic of the Seychelles. He served there until March 1993.

Sen. Mattingly graduated from Indiana University. He served four years in the United States Air Force during the Korean War. For twenty-one years, he worked as a Marketing Manager with IBM Corporation.

Hon. Jack F. Kemp (Senior Advisor)

Jack Kemp is one of the United States' leading voices promoting the potential and importance of the digital economy. His work in defense of the information sector of the U.S. economy is based on the premise that government's role in a thriving new enterprise should be very limited at most, leaving the free market to sort things out whenever possible. Throughout his career, Kemp has also been one of the nation's leading advocates for strong economic growth, free markets, free trade, and tax simplification and lower tax rates on both work and investment. Mr. Kemp serves on the Boards of several technology companies including Oracle and Proxicom.

In 1996, Jack Kemp gained even further prominence in the national spotlight when Senator Bob Dole named him as the Republican Party's vice presidential candidate. Mr. Kemp was Chairman of the National Commission on Economic Growth and Tax Reform.

Prior to founding Empower America, Mr. Kemp served for four years as Secretary of Housing and Urban Development, and proved to be one of the most innovative leaders in that role. Before his appointment to the Cabinet, Mr. Kemp represented the Buffalo area and Western New York for 18 years in the United States House of Representatives. Mr. Kemp spent 13 years in professional football, playing quarterback for the San Diego Chargers and the Buffalo Bills. He led the Buffalo Bills to the American Football League championship in 1964 and 1965 when he was named the

League's most valuable player. He also co-founded the AFL Players Association and was elected president for five terms. He is on the Board of Habitat for Humanity and Chairman of Habitat's National Campaign for Rebuilding our Communities.

Hon. Edwin Meese, III, Esq. (Senior Advisor)

Mr. Meese is Rector and Chairman of the Executive Committee of the Board of Visitors of George Mason University. He also holds the Ronald Reagan Chair in Public Policy at the Heritage Foundation. As U.S. Attorney General and, prior to that position, counselor to the President, he was among President Ronald Reagan's most important advisors. As Chairman of the Domestic Policy Council and the National Drug Policy Board, and as a member of the National Security Council, he played a key role in the development and execution of domestic and foreign policy. During the 1970s, Mr. Meese was Director of the Center for Criminal Justice Policy and Management and Professor of Law at the University of San Diego. He earlier served as Chief of Staff for then-Governor Reagan and was a local prosecutor in California. Mr. Meese is a Distinguished Visiting Fellow at the Hoover Institution, Stanford University, and a Distinguished Senior Fellow at the Institute of United States Studies, University of London. Mr. Meese is a retired colonel in the U.S. Army Reserve. He earned his B.A. from Yale University and his J.D. from the University of California, Berkeley.

David R. Burton, Esq. (Executive Director)

Mr. Burton is an attorney. He is the Chief Executive Officer of the Prosperity Institute. He is a principal in the Argus Group, an Alexandria, Virginia based law and government relations firm. He is one of the United States' leading advocates for fundamental tax reform. Mr. Burton has testified before Congress and regulatory agencies, regularly appeared on television and radio programs and written on tax policy matters for many major policy organizations and in a wide variety of publications including the *Wall Street Journal*, *Washington Times*, *Baltimore Sunpapers*, and *Human Events*. He is an adjunct scholar of the Ludwig von Mises Institute and has written on tax policy for Cato Institute and the Heritage Foundation. He was previously employed as the Vice President, Finance and General Counsel for New England Machinery and as Tax Manager of the United States Chamber of Commerce.

He is a graduate of the University of Chicago (B.A., Economics) and the University of Maryland School of Law (J.D.). He is admitted to practice law in Maryland and the District of Columbia. He is admitted to practice before the U.S. Supreme Court, the U.S. Circuit Court of Appeals (Fourth Circuit, D.C.), the U.S. District Court (Maryland, D.C.), and the U.S. Tax Court.

Dr. Veronique de Rugy

Veronique de Rugy is a fiscal policy analyst at the Cato Institute. Her research interests include tax competition, financial privacy, and fiscal sovereignty issues. She is the coauthor of *Action ou Taxation*, published in Switzerland in 1996. De Rugy is currently on the Board of Directors of the Center for Freedom and Prosperity. She holds a Ph.D. from the University of Paris-Sorbonne and previously directed academic programs for the Institute for Humane Studies -- Europe in France.

Stephen J. Entin

Mr. Entin is President of the Institute for Research on the Economics of Taxation. He is a former Deputy Assistant Secretary for Economic Policy at the Department of the Treasury. He joined the Treasury Department in 1981 with the incoming Reagan Administration. He participated in the preparation of economic forecasts for the President's budgets, and the development of the 1981 tax cuts, including the "tax indexing" provision that keeps tax rates from rising due to inflation. Mr. Entin represented the Treasury Department in the preparation of the Annual Reports of the Board of Trustees of the Social Security System, and conducted research into the long-run outlook for the system.

Prior to joining Treasury, Mr. Entin was a staff economist with the Joint Economic Committee of the Congress, where he developed legislation for tax rate reduction and incentives to encourage saving. Mr. Entin is a graduate of Dartmouth College and received his graduate training in economics at the University of Chicago, majoring in macroeconomics, monetary policy, and international economics.

James W. Harper, Esq.

James W. Harper is the Editor of Privacilla.org, a Web-based think-tank devoted exclusively to privacy. He is also the Founder and Principal of PolicyCounsel.com, an Information Age public policy consulting firm. Mr. Harper is a native of California and a member of the California bar. He serves as an Adjunct Fellow with the Progress and Freedom Foundation and as a member of the Advisory Committee to the Congressional Internet Caucus.

During the 105th and 106th Congresses, Mr. Harper served as counsel to the House Judiciary Committee. During the 104th Congress, he was counsel to the Senate Committee on Governmental Affairs. The issues he dealt with during these periods included telecommunications, Internet taxation, federal regulation, liability reform, immigration, campaign finance, intergovernmental relations, property rights, bankruptcy, and criminal justice.

Mr. Harper earned a bachelor's degree in political science at the University of California, Santa Barbara, where he focused on American politics and the federal courts. At Hastings College of the Law, he served as Editor-in-Chief of the Hastings Constitutional Law Quarterly.

Dr. Lawrence A. Hunter

Dr. Lawrence A. Hunter is Chief Economist at Empower America and political advisor to Jack Kemp. He also acts as an independent consultant for United Seniors Association and the Competitive Enterprise Institute. During the 1996 presidential campaign, he served as a member of Senator Bob Dole's Task Force on Tax Reduction and Tax Reform. Dr. Hunter works closely with the Congressional leadership, testifies before Congress, speaks frequently before business and citizens groups, is quoted often in major newspapers and makes frequent television and radio appearances.

During the 103rd and 104th Congresses, Dr. Hunter served on the staff of the Joint Economic Committee, first as Republican Staff Director and later as the Chief Economic Advisor to the Vice Chairman where he was the lead staff person in charge of putting together the economic growth and tax cut component of the *Contract With America*. Prior to joining the JEC staff in 1993, Dr. Hunter was with the U.S. Chamber of Commerce for five years where he served first as Deputy Chief Economist and later as Chief Economist and Vice President. In this capacity, Dr. Hunter managed a major division of the association and represented the Chamber on Capitol Hill, with the executive branch and in the media. Dr. Hunter has published extensively on such topics as economic growth, privatization of social security, tax reform and constitutional reform. Dr. Hunter is a graduate of the University of Wisconsin-Milwaukee and holds a Ph.D. from the University of Minnesota.

J. Bradley Jansen

Mr. Jansen is the Deputy Director of the Center for Technology Policy at the Free Congress Foundation. He focuses on technology, privacy and financial issues and is widely quoted on these issues in many prominent publications including the *Financial Times*, *Wall Street Journal*, and *Wired News Online*. He is one of the leading advocates of the privacy implications of many financial issues including money laundering, Government Sponsored Enterprises, Equal Credit Opportunity Act, database exchange and other issues.

Prior to joining the Free Congress Foundation, Mr. Jansen worked for U.S. Rep. Ron Paul as the legislative staffer for banking and monetary affairs for over four years. While on Capitol Hill, he initiated and led the fight against the "Know Your Customer" proposal. Mr. Jansen previously worked at the Cato Institute and on the two Forbes for President campaigns where he was a Republican National Convention delegate candidate. He is a former editor of the International Currency Report and the Asia/Pacific Currency Report. He graduated with a B.A. in International Studies from Miami University (Ohio)

after studying Spanish at the Pontificia Universidad Javieriana (Colombia) and did his graduate studies in economic history at the Universidad Catolica de Valparaiso (Chile).

Dan R. Mastromarco, Esq.

Mr. Mastromarco is President of the Prosperity Institute and a principal in the Argus Group. Mr. Mastromarco graduated from Albion College, B.A. and Georgetown University, L.L.M (*L. Legum Magister*) in Taxation. He is admitted to practice law in Michigan and the District of Columbia.

Mr. Mastromarco served as Assistant Chief Counsel for Tax Policy with the U.S. Small Business Administration, the sole appointed advocate for small business tax policy in the Federal government. Before that, Mr. Mastromarco worked as a Special U.S. Trial Attorney in the Tax Division, Department of Justice and as staff counsel to the Permanent Subcommittee on Investigations (PSI) under the Chairmanship of Senator Roth, where he focused on offshore banking and commodity fraud, advising the Committee Members and fashioning Senate and staff reports. More particularly, he co-authored the PSI's staff report, "Crime and Secrecy: The Use of Offshore Banks and Tax Havens." Mr. Mastromarco was Director of the Trade and Tax Division of the Jefferson Group, then the largest advocacy firm in the United States. He has appeared numerous times on both television and radio and has testified many times before House and Senate Committees. He has published more than 30 articles, in a wide variety of academic and other publications. He has also taught international tax law at the University of Maryland, International Management Program.

Dr. Daniel Mitchell

Dr. Mitchell is the McKenna senior fellow in political economy at The Heritage Foundation. He serves as Heritage's chief expert on tax policy and Social Security privatization. A former advisor on budgetary and tax matters to the Senate Finance Committee, Dan Mitchell's by-line can be found regularly in such national publications as *The Wall Street Journal*, *Washington Times* and *Investor's Business Daily*. He is a frequent guest on radio and television and a popular speaker on the lecture circuit.

Prior to joining The Heritage Foundation in 1990, Dr. Mitchell was Director of Tax and Budget Policy for Citizens for a Sound Economy. He holds a Ph.D. in economics from George Mason University and master's and bachelor's degrees in economics from the University of Georgia.

Andrew Quinlan

Andrew F. Quinlan is the President and co-founder of the Center for Freedom and Prosperity and the Center for Freedom and Prosperity Foundation. CFP is a leading voice in the international fight for tax competition, financial privacy, and fiscal sovereignty.

Mr. Quinlan has traveled and lectured on tax competition and information exchange all over the world including London, Paris, Brussels, Panama City, New York and Miami. The efforts of Mr. Quinlan and CFP have been profiled in several international publications including *The Wall Street Journal*, *The New York Times*, *International Herald Tribune*, *The Financial Times*, *Time*, *U.S. News and World Report*, *Money*, *National Review* and the *National Journal*. Mr. Quinlan publishes a weekly newsletter that is read all over the world and he is quoted often in major newspapers and has appeared on several television and radio shows.

Mr. Quinlan served as a Senior Economic Analyst for the Republican National Committee before working for more than seven years as a top staff member for New Jersey Congressman Jim Saxton -- the last four years as senior advisor to the Joint Economic Committee.

Dr. Richard W. Rahn

Richard W. Rahn is Chairman of Novecon Financial and Chairman of the Prosperity Institute. He was founding Chairman of the company which is now the Sterling Semiconductor division of Uniroyal Technology.

In the 1980s, Dr. Rahn served as Vice President and Chief Economist of the Chamber of Commerce of the United States, and Executive Vice President and member of the board of the National Chamber Foundation. Previously, he served as the Executive Director of the American Council for Capital Formation, and taught at several leading universities, including the New York Polytechnic University, where he became head of the graduate Department of Management. Dr. Rahn has advised senior government officials on tax and monetary issues in a number of countries, including Russia, Estonia, and Hungary. He served as the U.S. co-chairman of the Bulgarian Economic Growth and Transition Project in 1990.

Dr. Rahn is a member of the Mont Pelerin Society. He serves as a member of the Board of: the American Council for Capital Formation, the Small Business Survival Committee, the Southeastern Legal Foundation, the Institute for Research on the Economics of Taxation, the Institute for Political Economy, and on the Advisory Board of the Private Sector Council and the Center for the American Founding. Also, he is a senior fellow of the Discovery Institute and an adjunct scholar of the Cato Institute. He was appointed by President Reagan in 1982 as a member of the Quadrennial Social Security Advisory Council, and he served as an economic advisor to President G.H.W. Bush during the 1988 Presidential campaign.

Dr. Rahn is a frequent radio and television commentator. He has written hundreds of articles on tax and economic issues for newspapers such as the *Wall Street Journal*, and for professional journals, and is the author of the recent book *The End of Money and the Struggle for Financial Privacy*. He has testified before the U.S. Congress on economic issues more than seventy-five times.

Dr. Rahn earned his B.A. in economics at the University of South Florida, an M.B.A. from Florida State University, and a Ph.D. in business economics from Columbia University. He was awarded an honorary Doctor of Laws by Pepperdine University.

Solveig Singleton, Esq.

Solveig Singleton is a Senior Policy Analyst handling financial privacy issues at the Competitive Enterprise Institute.

Prior to joining CEI in October 2000, Ms. Singleton served as Director of Information Studies at the Cato Institute, specializing in privacy policy, encryption, and telecommunications law. Ms. Singleton also served as vice chairman of publications for the Telecommunications and Electronic Media Practice Group of the Federalist Society for Law & Public Policy Studies. Her articles have appeared in the *Journal of Commerce*, the *Washington Post*, the *Philadelphia Inquirer*, the *Washington Times*, the *Wall Street Journal*, *Internet Underground*, and *HotWired*. Her undergraduate degree is from Reed College, where she majored in philosophy. She graduated cum laude from Cornell Law School.

Mark A. A. Warner, Esq.

Mark A. A. Warner is Special Counsel in the New York and Washington, D.C. offices of Hughes Hubbard & Reed LLP. He is a member of the Bars of New York State and Ontario, Canada. Prior to joining HHR, he was a legal advisor in the Trade Directorate of the Organisation for Economic Co-operation and Development. Earlier in his career, he was an Assistant Professor at the University of Baltimore School of Law, and Assistant Director of its Center for International and Comparative Law. Mr. Warner has also taught trade and competition law at: the University of Leiden, Netherlands; the University of Western Cape in Cape Town, South Africa; and the International Law Institute in Kampala, Uganda. Mr. Warner holds: an LL.M. in International and Comparative Law from Georgetown University Law Center, an LL.B. from Osgoode Hall Law School/ York University; an M.A. in Economics from the University of Toronto; and a Joint Honours B.A. in Economics and Political Science from McGill University. Mr. Warner's publications include articles on competition, trade and investment law and policy in: *Antitrust*, *World Competition*, *International Trade Law and Regulation*, *the American Journal of International Law*, *Law & Policy in International Business*, *the Vanderbilt Journal of Transnational Law*, *the Northwestern Journal of International Law & Business*, *the Brooklyn Journal of International Law*, *the Canadian Business Law Journal* and in *The Legal Times*. Mr. Warner is co-author of the leading Canadian trade law treatise. He has also published several chapters in books.

Hon. John Yoder, Esq.

Senator Yoder is Of Counsel to the Washington, D.C. law firm of Burch and Cronauer, P.C. For the past 12 years, he has specialized in constitutional law cases and in litigating complex civil cases.

In 1976, Yoder was selected as a District Court Judge in Kansas. Judge Yoder was then selected in 1980, in national competition, as a Judicial Fellow to work at the Supreme Court of the United States. After serving for one year as a Judicial Fellow, the Chief Justice of the United States asked Judge Yoder to continue working at the U.S. Supreme Court as a permanent staff member in the position of Special Assistant.

In 1983, Judge Yoder was appointed by the Attorney General of the United States as the first Director of the Asset Forfeiture Office. In that capacity, as a federal prosecutor, he set up, staffed, and managed a new subdivision at the U.S. Department of Justice, receiving a Senior Executive Service Outstanding Performance rating from the Attorney General for successfully setting up the Asset Forfeiture Office.

In 1992, Yoder was elected as a State Senator, representing the Eastern Panhandle of West Virginia as a Senator until the end of his term in 1996, when he ran for State Supreme Court as the Republican Nominee. Senator Yoder was rated for two years in a row as the most effective Senator by the state's largest newspaper.

Yoder holds a B.A. degree with majors in economics and government from Chapman College, a Juris Doctor degree from the University of Kansas School of Law, and an M.B.A. degree from the University of Chicago Graduate School of Business.

Task Force on Information Exchange and Financial Privacy

Executive Summary

The Task Force is convinced, for the reasons outlined in this report, that its recommendations, if implemented, will achieve the dual objectives, usually portrayed as competing, of improving law enforcement and national security and respecting the rights, enhancing the privacy and maintaining the standard of living of law-abiding Americans.

The Task Force finds that the United States should:

- take the lead in forming an effective international Convention on Privacy and Information Exchange composed of democratic governments that respect the rule of law.

The Convention proposed by the Task Force would streamline and improve the exchange of information for law enforcement, national security and anti-terrorism purposes and establish under international law enforceable restrictions on the use to which collected information could be put. Moreover, the Convention would establish a private right of action to enforce individual legal rights under the Convention.

- better target its money laundering laws.

Rather than bury investigators in a mountain of millions of currency transaction reports with respect to law-abiding citizens, a more effective system should be developed where the activities of persons on a government watch list are provided by financial institutions to the appropriate federal authorities. Persons could be placed on the watch list if the government had a reasonable and significant suspicion of unlawful activity.

- prioritize national security, anti-terrorism and serious crime in its information exchange efforts.
- take more aggressive steps to prevent sensitive information from reaching hostile hands.
- withdraw its proposed interest reporting regulation.

This regulation is unnecessary to enforce U.S. tax law and is likely to cause a substantial degree of capital to leave U.S. capital markets if implemented.

- oppose the creation of a United Nations International Tax Organization.

The proposed UN ITO would result in the private information of U.S. nationals being provided to governments throughout the world, would make it easier for repressive governments to oppress political opponents and minorities and violate fundamental human rights by allowing states to tax persons on future income even after they have emigrated from that state. Moreover, allowing the UN to collect taxes directly from persons within member states would be the first step toward establishing a world government, to the detriment of the American people.

- oppose the OECD Harmful Tax Competition initiative.

The U.S. should not be a party to applying rules against small countries that it is not willing to abide by itself. Countries that honor financial privacy and maintain low tax rates should not be sanctioned merely for doing so. The United States, as a low tax country and as a country that attracts capital by offering foreign investors the opportunity to invest in the U.S. free of tax, would be severely harmed by a generalization of the proposed OECD rules. Moreover, the OECD initiative represents a major step toward the unrestricted disclosure of private financial and tax information, including from the U.S. and other OECD countries, to a wide array of countries that can be expected to misuse the information.

- modify its qualified intermediary rules to the extent the rules require information unnecessary to enforce U.S. law; and
- reject the European Union's Savings Tax Directive.

Task Force on Information Exchange and Financial Privacy

Policy Factors

The Task Force believes that a number of factors should inform U.S. policy on financial privacy and information exchange:

1. Obtaining information about the global financial activities of terrorists and criminals is critical to the security of the American people.
2. The current international framework for information sharing is inadequate to achieve the needs of law enforcement and national security.
3. Bi-lateral and multi-lateral international information sharing agreements are a central part of the U.S. program to obtain information about the financial activities of terrorists and criminals.
4. Information, including financial information, about terrorists and criminals should be routinely shared among the U.S. and reliable democratic countries.
5. The U.S. and reliable democratic countries should not routinely provide information obtained to countries that (1) cannot be expected to always use the information in a manner consistent with U.S. national security interests or (2) do not have in place (in law and in practice) adequate safeguards to prevent the information from (a) being obtained by hostile parties or (b) being used for inappropriate commercial, political, civil, tax or other purposes.
6. The U.S. and reliable democratic countries should work with other countries to obtain information, including financial information, about the activities of terrorists and criminals.
7. Current information reporting mechanisms are overbroad, untargeted and insufficiently effective.
8. Obtaining information for tax and civil purposes should not impede the ability of the U.S. to obtain information about the financial activities of terrorists and criminals. Obtaining information for national security purposes and about the financial activities of terrorists and criminals should have priority over obtaining information for tax and civil purposes.
9. Information sharing programs in which the United States participates must respect the privacy of innocent persons, particularly U.S. nationals.
10. Information sharing programs must not unnecessarily impede the competitiveness of U.S. firms nor unnecessarily impede the ability of the U.S. to attract foreign capital to U.S. markets.
11. Information sharing programs must consider the private sector compliance costs and government program costs compared to the likely national security and law enforcement benefits of obtaining the information when assessing whether it is worthwhile to collect the information sought.
12. The U.S., and multilateral institutions in which it participates, must respect the national sovereignty of other countries unless those countries pose a danger to the national security of the U.S.

Task Force on Information Exchange and Financial Privacy

Information Exchange: Current Practice and Proposals

There are a wide variety of U.S. and foreign government agencies and international agencies involved in the collection and dissemination of information about private persons. This report divides the discussion into two basic areas: (1) National Security, Terrorism and Law Enforcement, and (2) Tax Administration.³ The lines between these areas are not bright and various agencies are involved in collecting information for more than one purpose. The Task Force, however, believes that the priorities, the methods and the policy choices in each area are different.

National Security, Terrorism and Law Enforcement

The major agencies involved in collecting and disseminating information about private persons for national security, anti-terrorism and law enforcement purposes in the United States are the Federal Bureau of Investigation (FBI), the Criminal Division of the Justice Department, the Central Intelligence Agency (CIA), the National Security Agency (NSA)⁴ and the Financial Crimes Enforcement Network of the U.S. Treasury Department (FinCEN). Internationally, the primary organizations involved are the Financial Action Task Force on Money Laundering (FATF) and the International Criminal Police Organization (Interpol). FATF is housed at the Organization for Economic Cooperation and Development (OECD) in Paris but is independent. Interpol is headquartered in Lyons, France. FinCEN, FATF and Interpol are the primary agencies involved in monitoring financial transactions and enforcing laws against money laundering.

FinCEN was created in 1990. Its Money Laundering working group is composed of representatives from many other agencies including the Internal Revenue Service, the Customs Service, the Secret Service, the Federal Law Enforcement Training Center, the Department of Justice, the Federal Bureau of Investigation, the Drug Enforcement Agency, the United States Postal Inspection Service, the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the National Credit Union Administration, the Federal Reserve, the Securities and Exchange Commission, and the Commodity Futures Trading Commission.

The primary source materials for FinCEN investigations are suspicious activity reports (SARs) and currency transaction reports (CTRs) provided by U.S. financial institutions. SARs are filed when a financial institution detects activity that it believes may constitute unlawful activity. CTRs are filed with respect to cash transactions of

³ A supplementary analysis by the Task Force may examine these issues in non-tax civil matters.

⁴ The NSA routinely monitors electronic communications abroad and communications between U.S. residents and persons abroad.

\$10,000 or more.⁵ 156,931 SARs were filed in 2000.⁶ 12,000,000 CTRs were processed by FinCEN in 2000.⁷

FATF was established in 1989 by an agreement reached at a G-7 summit. FATF is a very informal group working under minimal formal restrictions or guidelines. Twenty-eight countries now participate in FATF. FATF's primary role has been to establish standards relating to money laundering laws and practices and work to implement these standards around the world. Its basic standards are outlined in its "40 recommendations." Those recommendations include (1) the criminalization of the laundering of the proceeds of serious crimes, (2) the enactment of laws to seize and confiscate the proceeds of crime, (3) the imposition of obligations for financial institutions to identify all clients, including any beneficial owners of property, and to keep appropriate records, (4) the imposition of a requirement for financial institutions to report suspicious transactions to the competent national authorities, and the implementation of a comprehensive range of internal control measures at financial institutions, (5) the creation of adequate systems for the control and supervision of financial institutions, (6) the entering into force of international treaties or agreements relating to money laundering, and (7) the enactment of national legislation which will allow countries to provide prompt and effective international co-operation. FATF periodically publishes a report listing non-cooperating countries and territories (NCCTs).⁸ These countries and financial institutions located in these countries are subject to greater review, and countries that do not comply with FATF's recommendations may be subjected to potentially severe sanctions by FATF member countries.

In the aftermath of the September 11th attacks, Interpol established a September 11th Task Force. On December 11th, Interpol and the U.S. Treasury announced the creation of a new partnership that would, most notably, establish an international terrorist financing database. The Interpol database is designed to consolidate international and national lists of terrorist financiers and make it available to police around the world to prevent the flow of funds to terrorist groups and to assist in criminal investigations. Participants would include all 179 members of Interpol.

⁵ Internal Revenue Code section 6050I and the Bank Secrecy Act, Pub. L. 91-508, title II, Oct. 26, 1970, 84 Stat. 1118 and Currency and Foreign Transactions Reporting Act, Pub. L. 97-258, Sec. 5(b), Sept. 13, 1982, 96 Stat. 1068, especially at 31 USC 5313.

⁶ The SAR Activity Review, Trends, Tips and Issues, June 2001, p. 4.

⁷ Testimony of Jimmy Gurule, Under Secretary of the Treasury for Enforcement, before the U.S. Senate Committee on Banking, Housing and Urban Affairs, on Domestic and International Money Laundering, September 26, 2001.

⁸ In its June 22, 2001 report, it listed Cook Islands; Dominica; Egypt; Guatemala; Hungary; Indonesia; Israel; Lebanon; Marshall Islands; Myanmar; Nauru; Nigeria; Niue; Philippines; Russia; St. Kitts and Nevis; and St. Vincent and the Grenadines as NCCTs.

Tax Administration

The United States imposes income taxes on U.S. persons (including corporations, citizens and resident aliens) on their income from throughout the world.⁹ Accordingly, the United States Internal Revenue Service has a strong interest in obtaining financial information from abroad. To assist the IRS in obtaining this information, the United States has entered into a wide array of bi-lateral income tax treaties and information sharing arrangements. In addition, the United States requires its financial institutions to report interest and dividends paid to U.S. residents and with respect to other financial transactions. With the advent of the recent qualified intermediary (QI) rules and the proposed interest reporting regulation (both discussed below), the U.S. has become increasingly aggressive in requiring foreign financial institutions to make similar reports. Finally, under the previous administration, the U.S. supported the OECD harmful tax competition initiative, which would impose severe sanctions on non-OECD low tax countries that do not disclose financial information with respect to customers doing business in those countries. In addition, Robert Rubin, former U.S. Secretary of the Treasury in the Clinton administration, was instrumental in developing the proposal to create a UN International Tax Organization that would generalize the OECD initiative to apply to all countries, including the U.S.

OECD Harmful Tax Competition

The Organization for Economic Cooperation and Development (OECD) is an international organization with 30 member countries, including the U.S., Canada, Japan and most European countries. In May of 1996, Ministers instructed the OECD to “develop measures to counter the distorting effects of harmful tax competition on investment and financing decisions and the consequences for national tax bases.” In April of 1998, the OECD Council adopted a Recommendation to the Governments of Member Countries¹⁰ and issued a report entitled “Harmful Tax Competition: An Emerging Global Issue.” In that report, the OECD adopted the position that it was necessary to engage in a collective international effort to stop harmful tax competition by harmful tax regimes. The OECD is worried that low tax countries would attract too much capital from high tax countries.¹¹ The OECD considers a country a harmful tax regime if the country (1) has low or zero income taxes, (2) allows foreigners investing in the country to do so at favorable rates, and (3) affords financial privacy to its investors or citizens. The OECD identified 41 countries (mostly developing countries) as “harmful tax regimes.”

⁹ Those interested in a relatively brief introduction to U.S. taxation of international income may wish to examine *International Taxation*, 3rd Edition, Richard L. Doernberg (West Publishing, 1997).

¹⁰ Luxembourg and Switzerland abstained. The Clinton Administration supported the OECD initiative.

¹¹ For example, the report states, “Globalization has, however, also had the negative effects of opening up new ways by which companies and individuals can minimize and avoid taxes and in which countries can exploit these new opportunities by developing tax policies aimed primarily at diverting financial and other geographically mobile capital,” *Harmful Tax Competition: An Emerging Global Issue* (1998), p. 14, section 23.

The OECD was demanding that the low tax countries sign a Memorandum of Understanding (MOU). Originally, the deadline for compliance was July 31, 2001 and then November 2001. Now, a jurisdiction must have made a “commitment” by February 28, 2002 to eliminate “harmful tax practices” to avoid being blacklisted as a “non-cooperating jurisdiction.” A commitment involves agreeing to an “implementation plan.” The OECD has been forced to be less aggressive because the Bush administration support for the initiative has been more qualified, in contrast to the Clinton administration’s strong support.¹² Countries that refuse to either raise their tax rates or to comply with OECD demands relating to the routine and comprehensive disclosure of private financial information will be blacklisted.¹³ The OECD will then work to ensure that OECD member states impose sanctions on the blacklisted countries. Sanctions proposed by the OECD for imposition on the targeted low tax countries include the termination of tax treaties, denying income tax deductions for purchases made from targeted countries’ businesses (thereby dramatically raising the cost of buying goods from that country), imposing withholding taxes on payments to residents of targeted countries, and denying the foreign tax credit for taxes paid to the targeted government. The OECD also proposes to explore measures designed to disrupt normal banking and business operation.

United Nations International Tax Organization

On June 25, 2001 UN Secretary-General Kofi Annan provided the report of the High Level Panel on Financing for Development to the General Assembly. He appointed the panel in December of 2000.¹⁴ Annan described the report as a “solid piece of work” and commended the panel for the “energy, imagination and effort that they brought to their task.” The recommendations of the report will be considered at the Conference on

¹² See, Statement of Paul H. O’Neill before the Senate Committee on Governmental Affairs Permanent Subcommittee on Investigations, OECD Harmful Tax Practices Initiative, July 18, 2001. See also, “U.S. to Abandon Crackdown on Tax Havens, OECD Effort Is Too Broad and Could Raise U.S. Taxes, Treasury’s O’Neill Says,” Washington Post, By Dana Milbank, Washington Post Staff Writer, Friday, May 11, 2001; Page A29.

¹³ As of the February 28, 2002 deadline for compliance, the following countries have entered into some type of commitment or understanding with the OECD: Antigua and Barbuda, Aruba, Bahrain, Barbados, Bermuda, Cayman Islands, Cyprus, Grenada, Guernsey, Isle of Man, Jersey, Malta, Mauritius, Netherlands Antilles, St. Christopher (St. Kitts) and Nevis, Saint Lucia, St. Vincent and the Grenadines, San Marino, the Seychelles and Tonga.

¹⁴ The U.N. report is available at <http://www.un.org/esa/ffd/a55-1000.pdf>. The members of the panel were:

Abdulatif Al-Hammad, President, Arab Fund for Economic Development, Kuwait;
David Bryer, Director of OXFAM, United Kingdom;
Mary Chinery-Hesse, Former Deputy Director-General of the International Labor Organization, Ghana;
Jacques Delors, former Finance Minister of France and President of the European Commission;
Rebeca Grynspan, former Vice-President, Costa Rica;
Aleksander Livshitz, Chairman of the Board of the Russian Credit Bank;
Majid Osman, former Finance Minister of Mozambique, who now heads a commercial bank;
Robert Rubin, former Secretary of the Treasury, United States;
Manmohan Singh, former Minister of Finance, India; and
Masayoshi Son, President and Chief Executive Officer of Softbank Corporation in Japan.

Financing for Development, which will take place in Monterrey, Mexico between March 18 and March 22, 2002.

The report recommends the creation of an International Tax Organization (ITO).¹⁵ The proposed ITO would “sponsor a mechanism for multilateral sharing of tax information, like that already in place with OECD, so as to curb the scope for evasion of taxes on investment income earned abroad.”¹⁶ The proposed UNITO would result in every UN member government having routine unqualified access to the financial information of the citizens of all UN member states.

The primary purpose of the UNITO would be to limit tax competition. The report states:

The taxes that one country can impose are often constrained by the tax rates of others: this is true of sales taxes on easily transportable goods, of income taxes on mobile factors (in practice, capital and highly qualified personnel) and corporate taxes on activities where the company has a choice of location. Countries are increasingly competing not by tariff policy or devaluing their currencies but by offering low tax rates and other tax incentives, in a process sometimes called ‘tax degradation’.¹⁷

It [the ITO] might engage in negotiations with tax havens to persuade them to desist from harmful tax competition. It could take a lead role in restraining the tax competition designed to attract multinationals – competition that, as noted earlier, often results in the lion’s share of the benefits of foreign direct investment accruing to the foreign investor.¹⁸

Another task that might fall to an ITO would be the development, negotiation and operation of international arrangement for the taxation of emigrants. At present most emigrants pay taxes only to their host country, an arrangement that exposes source countries to the risk of economic loss when many of their most able citizens emigrate.¹⁹

The report recommends that a currency transactions tax or carbon (CO₂) tax be imposed to finance the various spending programs it recommends.²⁰ The report recommends that foreign aid from developed countries be 0.7 percent of GDP (or \$70 billion for the U.S., a nearly 8 fold increase).²¹ The report endorsed steps to create a global council to promote global governance because “modern globalization calls for global governance.”²²

¹⁵ Report of the High Level Panel on Financing for Development to the General Assembly, pp. 27-28, 64-66.

¹⁶ Ibid, p. 28.

¹⁷ Ibid, p. 65.

¹⁸ Ibid, p. 65.

¹⁹ Ibid, p. 66.

²⁰ Ibid, pp. 26-27.

²¹ Ibid, p. 21.

²² Ibid, pp. 24, 26.

U.S. Qualified Intermediary Rules

Payments from the U.S. to foreigners are often subjected to a withholding tax. Fixed or determinable annual or periodical (FDAP) income (i.e. rents, royalties, interest, dividends, and the like but not capital gains) paid from U.S. sources is subject to a 30 percent withholding tax, unless a treaty between the U.S. and the country of the foreign payee reduces the rate.²³ Treaties generally reduce the withholding tax rate to the five to fifteen percent range.²⁴ However, if the interest is portfolio interest, Internal Revenue Code sections 871(h) and 881(c) exempt most interest paid to foreigners.

The “qualified intermediary” rules, effective January 24, 2000, are designed to enforce the withholding taxes on U.S. source income paid to foreigners and to ensure that income paid to foreign financial institutions with respect to assets beneficially owned by U.S. persons is taxed.²⁵ They are quite complex.²⁶

A “qualified intermediary” is defined as (1) a foreign financial institution, (2) a foreign branch or office of a U.S. financial institution or (3) a foreign corporation presenting claims under a tax treaty that has entered into a withholding agreement with the Internal Revenue Service.²⁷

The agreement that the qualified intermediary must sign is set forth in Rev. Proc. 2000-12. This agreement establishes the “QI’s rights and obligations regarding documentation, withholding, information reporting, tax return filing, deposits, and refund procedures under sections 1441, 1442, 1443, 1461, 3406, 6041, 6042, 6045, 6049, 6050N, 6302, 6402, and 6414 of the Internal Revenue Code with respect to certain types of payments.”²⁸ In order to become a qualified intermediary (a ‘QI’), an institution must apply. The application requires dozens of lists, statements and documents.²⁹ In addition,

²³ IRC §1441 (regarding individual payees) and IRC §1442 (regarding corporate payees); also see IRC §871 and §881.

²⁴ See IRS Publication No. 515, Withholding of Tax on Non-resident Aliens and Foreign Corporations.

²⁵ See generally IRC §1441-1443.

²⁶ The QI rules are primarily set forth in Treasury Regs. §1.1441-1(e)(5), Rev. Proc. 2000-12 (2000-4 Internal Revenue Bulletin 387) effective January 24, 2000 and Notice 2001-4 (Internal Revenue Bulletin 2001-8, January 8, 2001). See also Announcement 2000-48. It is, at some level, remarkable that such a short statutory provision can give rise to so many hundreds of pages of rules, including the regulations under section 1441, the various information reporting requirements related to withholding, Revenue Procedure 2000-12 relating to QIs, and the many country specific attachments and approved KYC rules.

²⁷ §1.1441-1(e)(5)(ii).

²⁸ See Preamble, QI Agreement, Rev. Proc. 2000-12.

²⁹ A prospective QI must submit an application to become a QI. The application must establish to the satisfaction of the IRS that the applicant has adequate resources and procedures to comply with the terms of the QI withholding agreement. An application must include the information specified in the Revenue Procedure and any additional information and documentation requested by the IRS. The information required includes:

- (1) A statement that the applicant is an eligible person and that it requests to enter into a QI withholding agreement with the IRS.
- (2) The applicant’s name, address, and employer identification number (EIN), if any.
- (3) The country in which the applicant was created or organized and a description of the applicant’s business.

the QI is required to fully inform the IRS about the details of its home country know your customer rules.³⁰

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- (4) A list of the position titles of those persons who will be the responsible parties for performance under the Agreement and the names, addresses, and telephone numbers of those persons as of the date the application is submitted.
 - (5) An explanation and sample of the account opening agreements and other documents used to open and maintain the accounts at each location covered by the Agreement.
 - (6) A list describing the type of account holders (e.g., U.S., foreign, treaty benefit claimant, or intermediary), the approximate number of account holders within each type, and the estimated value of U.S. investments that the QI agreement will cover.
 - (7) A general description of U.S. assets by type (e.g., U.S. securities, U.S. real estate), including assets held by U.S. custodians, and their approximate aggregate value by type. The applicant should provide separate information for assets beneficially owned by the applicant and for assets it holds for others.
 - (8) A completed Form SS-4 (Application for Employer Identification Number) to apply for a QI Employer Identification Number (QI-EIN) to be used solely for QI reporting and filing purposes. An applicant must apply for a QI-EIN even if it already has another EIN. Each legal entity governed by the QI withholding agreement must complete a Form SS-4.
 - (9) Completed appendices and attachments that appear at the end of the QI agreement.

³⁰ The IRS will not enter into a QI withholding agreement that provides for the use of documentary evidence obtained under a country's know-your-customer rules if it has not received the "know-your-customer" practices and procedures for opening accounts and responses to the 18 specific items presented below. If the information has already been provided to the IRS, it is not necessary for a particular prospective QI to submit the information. The IRS may publish lists of countries for which it has received know-your-customer information and for which the know-your-customer rules are acceptable. The 18 items are as follows:

1. An English translation of the laws and regulations ("know-your-customer" rules) governing the requirements of a QI to obtain documentation confirming the identity of QI's account holders. The translation must include the name of the law, and the appropriate citations to the law and regulations.
2. The name of the organization (whether a governmental entity or private association) responsible for enforcing the know-your-customer rules. Specify how those rules are enforced (e.g., through audit) and the frequency of compliance checks.
3. The penalties that apply for failure to obtain, or evaluate, documentation under the know-your-customer rules.
4. The definition of customer or account holder that is used under the know-your-customer rules. Specify whether the definition encompasses direct and indirect beneficiaries of an account if the activity in the account involves the receipt or disbursement of funds. Specify whether the definition of customer or account holder includes a trust beneficiary, a company whose assets are managed by an asset manager, a controlling shareholder of a closely held corporation or the grantor of a trust.
5. A statement regarding whether the documentation required under the know-your-customer rules requires a financial institution to determine if its account holder is acting as an intermediary for another person.
6. A statement regarding whether the documentation required under the know-your-customer rules requires a financial institution to identify the account holder as a beneficial owner of income credited to an account.
7. A list of the specific documentation required to be used under the know-your-customer rules, or if those rules do not require use of specific documentation, the documentation that is generally accepted by the authorities responsible for enforcing those rules. Generally, the IRS will not permit a QI to establish the identity of an account holder without obtaining documentation directly from the account holder.
8. A statement regarding whether the know-your-customer rules require that an account holder provide a permanent residence address.
9. A summary of the rules that apply if an account is not opened in person (e.g., correspondence, telephone, Internet).
10. Whether an account holder's identity may be established, in whole or in part, by introductions or referrals.

Once an institution has become a QI, the institution becomes a withholding agent within the meaning of Internal Revenue Code §3406 for amounts it pays to its account holders. QI's may, but need not, assume primary responsibility for non-resident alien withholding under IRC §1441.³¹ A QI does have the primary responsibility to issue Form 1099s, although it can designate another payor to undertake this function.³² The withholding agent must withhold 30 percent of any payment of an amount subject to NRA withholding made to an account holder that is a foreign person unless the withholding agent can reliably associate the payment with documentation upon which it can rely to treat the payment as made to a payee that is a U.S. person or as made to a beneficial owner that is a foreign person entitled to a reduced rate of withholding.³³ In general, the QI is a payor under section 3406 and is required to deduct and withhold 31 percent from the payment of a reportable payment to a U.S. non-exempt recipient if the U.S. non-exempt recipient has not provided its TIN in the manner required by U.S. law.³⁴ The QI can, however, avoid this responsibility by avoiding primary Form 1099 responsibility and by providing Forms W-9 for its U.S. non-exempt recipient account holders together with the withholding rate pools attributable to those account holders.³⁵

QIs agree to collect and maintain information on their account holders in accordance with the specified “know-your-customer” requirements.³⁶ A QI may generally treat an account holder (including an account holder that is a collective investment vehicle) as a foreign beneficial owner of an amount if the account holder provides a valid Form W-8 (other than Form W-8IMY) or other valid documentary evidence. A QI may treat a documented foreign beneficial owner account holder as entitled to a reduced (or zero) rate of non-resident alien (NRA) withholding if all the requirements to a reduced rate are met and the documentation provided by the account holder supports entitlement to a reduced (or zero) rate. In addition, the QI may not treat an account holder that provides documentation indicating that it is a bank, broker,

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11. The circumstances under which new documentation must be obtained, or existing documentation verified, under the know-your-customer rules.
 12. A list of all the exceptions, if any, to the documentation requirements under the know-your-customer rules.
 13. A statement regarding whether the know-your-customer rules do not require documentation from an account holder if a payment to or from that account holder is cleared by another financial institution.
 14. A statement regarding how long the documentation remains valid under the know-your-customer rules.
 15. A statement regarding how long the documentation obtained under the know-your-customer rules must be retained and the manner for maintaining that documentation.
 16. Specify whether the rules require the maintenance of wire transfer records, the form of the wire transfer records and how long those records must be maintained. State whether the wire transfer records require information as to both the original source of the funds and the final destination of the funds.
 17. A list of any payments or types of accounts that are not subject to the know-your-customer rules.
 18. Specify whether there are special rules that apply for purposes of private banking activities.

³¹ QI Agreement, sections 3.02-3.03, Rev. Proc. 2000-12.

³² QI Agreement, section 3.05, Rev. Proc. 2000-12. See also section 4.01.

³³ QI Agreement, section 3.01, Rev. Proc. 2000-12.

³⁴ QI Agreement, section 3.04, Rev. Proc. 2000-12.

³⁵ QI Agreement, section 3.06, Rev. Proc. 2000-12.

³⁶ QI Agreement, section 5.01, Rev. Proc. 2000-12.

intermediary, or agent (such as an attorney) as a beneficial owner unless the QI receives a statement, in writing and signed by a person with authority to sign such a statement, stating that such account holder is the beneficial owner of the income.³⁷

A QI may not reduce the rate of withholding based on a beneficial owner's claim of treaty benefits unless the QI obtains the documentation required by section 5.03 of the QI Agreement. That section requires, among other things, that the account holder properly complete Form W-8BEN, the account holder has provided know-your-customer compliant documentation and the account holder has provided a statement to the effect that the account holder has met all of the legal requirements entitling the account holder to the benefit of the treaty, provided however, that the QI is excused from the statement requirement if the account holder is an individual resident of an applicable treaty country. The QI must comply with a variety of rules concerning what is and is not valid documentation.³⁸

The QI agreement establishes the presumption that amounts subject to withholding paid to an account that is maintained outside the United States is presumed made to an undocumented foreign account holder. Therefore, the QI must treat the amount as subject to withholding at a rate of 30 percent on the gross amount paid and report the payment to an unknown account holder on Form 1042-S. The QI may presume that foreign source income paid outside the U.S. is not subject to withholding or reporting.³⁹

The QI agreement obligates the QI to file Form 1042-S for each pool of income.⁴⁰ The QI, however, must file separate 1042-S Forms in the case of non-qualified intermediary account holders, unknown recipients and each QI or foreign partnership account holder that receives amounts subject to non-resident agent withholding.⁴¹ The QI must file Form 1099s, in general, for unknown owners and U.S. non-exempt recipients.⁴²

In general, the IRS agrees not to audit QIs but to accept instead the audit conducted by an approved external auditor.⁴³ These auditors verify that the QI's employees are properly trained, that the QI's withholding responsibilities have been properly discharged, that the reporting pools rules have been properly complied with, that the proper forms have been filed and so forth. The external auditor provides a report to the IRS.

The IRS has taken some steps to streamline this cumbersome process. It has issued a list of countries with approved KYC rules, so that each institution within that jurisdiction does not have to individually satisfy the IRS with respect to its country's

³⁷ QI Agreement, section 5.02, Rev. Proc. 2000-12.

³⁸ QI Agreement, section 5.10, Rev. Proc. 2000-12.

³⁹ QI Agreement, section 5.11, Rev. Proc. 2000-12.

⁴⁰ QI Agreement, sections 6.03 and 8.01, Rev. Proc. 2000-12.

⁴¹ QI Agreement, section 8.02, Rev. Proc. 2000-12.

⁴² QI Agreement, section 8.04, Rev. Proc. 2000-12.

⁴³ QI Agreement, section 10.01, Rev. Proc. 2000-12.

KYC rules.⁴⁴ The QI withholding agreement permits a qualified intermediary to use documentary evidence of the same type as that obtained under the KYC rules applicable to the QI, but only if the documentation is listed in an attachment to the QI withholding agreement. The IRS is developing country-specific attachments for countries that have approved KYC rules.⁴⁵

U.S. Interest Reporting Regulations

As noted, payments from the U.S. to foreigners are often subjected to a withholding tax. FDAP income (i.e. rents, royalties, interest, dividends, and the like) is subject to a 30 percent withholding tax, unless a treaty between the U.S. and the country of the foreign payee reduces the rate.⁴⁶ Treaties generally reduce the withholding tax rate to the five to fifteen percent range.⁴⁷ FDAP income includes interest and dividends but not capital gains. To attract foreign capital to the United States, in 1984 Congress enacted the portfolio interest exception, which repealed this tax on interest received by non-resident aliens on most portfolio debt instruments (including interest on bank deposits and bonds).⁴⁸ This exception only applies to unrelated borrowers and lenders and is otherwise restricted but is quantitatively very important.⁴⁹ Although it is difficult to know for certain, analysts generally believe that this provision has attracted somewhat over \$1 trillion in foreign capital to the United States.

According to IRS Statistics of Income, in 1997 \$2.5 billion was withheld on \$132.8 billion of U.S. source income paid to foreigners. Withholding taxes, therefore, amount to somewhat under two percent of the U.S. source income paid to foreigners. Interest amounts to nearly three-quarters of the payments. Dividends and interest account for 87 percent of the payments. Most interest is portfolio interest exempt from tax under section §871(h) or §881(c) and most dividends are subject to 5 to 15 percent tax rates rather than the standard 30 percent rate because of tax treaties.

⁴⁴ Jurisdictions with approved Know-Your-Customer rules include Andorra, Argentina, Aruba, Australia, Austria, Bahamas, Barbados, Belgium, Bermuda, British Virgin Islands, Canada, Cayman Islands, Chile, Cyprus, Czech Republic, Denmark, Finland, France, Germany, Gibraltar, Greece, Guernsey, Hong Kong, Ireland, Isle of Man, Israel, Italy, Japan, Jersey, Korea, Luxembourg, Liechtenstein, Malta, Monaco, Netherlands, Netherlands Antilles, Norway, Panama, Portugal, Singapore, Spain, St. Lucia, Sweden, Switzerland, Turks and Caicos Islands, Uruguay and the United Kingdom. Jurisdictions awaiting approval of Know-Your-Customer Rules include Antigua, Bahrain, Colombia, Iceland, Lebanon, Saudi Arabia, Slovenia and the United Arab Emirates.

⁴⁵ Approved country specific attachments are available for these countries: Austria, Barbados, Belgium, Bermuda, Canada, Cayman Islands, Denmark, Finland, France, Germany, Gibraltar, Guernsey, Hong Kong, Ireland, Isle of Man, Israel, Italy, Japan, Jersey, Korea, Luxembourg, Monaco, Netherlands, Netherlands Antilles, Norway, Portugal, Singapore, Spain, Sweden, Switzerland, and the United Kingdom.

⁴⁶ IRC §1441 (regarding individual payees) and IRC §1442 (regarding corporate payees); also see IRC §871 and §881.

⁴⁷ See IRS Publication No. 515, Withholding of Tax on Non-resident Aliens and Foreign Corporations.

⁴⁸ PL 98-369 (July 18, 1984), The Deficit Reduction Act of 1984.

⁴⁹ IRC §881(c)(3).

On January 17, 2001, immediately prior to the change in U.S. administrations, the U.S. Internal Revenue Service (IRS) issued a proposed regulation entitled "Guidance on Reporting of Deposit Interest Paid to Nonresident Aliens."⁵⁰

The IRS previously had issued a regulation concerning information relating to interest paid on deposits from U.S. bank accounts to nonresident alien individuals who are residents of Canada, saying that these regulations would significantly further, in unspecified ways, its compliance efforts. Reg. §1.6049-8(a) requires the reporting of such interest on a Form 1042-S.

The regulations proposed in January 2001 would extend the information reporting requirement for bank deposit interest paid to nonresident alien individuals who are residents of foreign countries. The regulations would require all payors of interest to non-resident aliens to file a Form 1042-S. This form, among other things, would require the reporting of the payee's name and address, tax numbers and the amount paid. Under current rules, once a foreigner has filed a W-8 establishing foreign status, there is no need to file a Form 1042-S with respect to interest payments since there is no U.S. tax imposed. The IRS regards this extension as appropriate for two reasons. First, requiring routine reporting to the IRS of all bank deposit interest paid within the United States would minimize the possibility of avoidance of the U.S. information reporting system (such as through false claims of foreign status). Second, several countries that have tax treaties or other agreements that provide for the exchange of tax information with the United States have requested information concerning bank deposits of individual residents of their countries. Treasury and the IRS believe it is important for the United States to facilitate, wherever possible, the effective exchange of all relevant tax information with our treaty partners because of the importance that the United States government attaches to exchanging tax information pursuant to income tax treaties or tax information exchange agreements as a way of encouraging voluntary compliance and furthering transparency.

European Union Savings Tax Directive

The European Union has proposed that nations automatically exchange information on the investment earnings of foreign investors.⁵¹ This pact would apply to all EU member nations as well as six non-EU nations (the United States, Switzerland, Liechtenstein, Andorra, Monaco, and San Marino). In order to go into effect, the Directive must receive unanimous support from all EU member nations, and all six non-EU jurisdictions must agree to participate.

The Savings Tax Directive was proposed at the European Council meeting in Feira, Portugal in June 2000 and approved by the EU's Council of Finance Ministers in

⁵⁰ REG-126100-00.

⁵¹ The European Union is a Brussels-based international organization representing the 15-member European Community. A description of the European Union's "Savings Tax Directive" can be found at http://europa.eu.int/comm/taxation_customs/publications/official_doc/IP/ip011026/memo01266_en.pdf

November 2000. The agreement replaced an earlier proposal that would have permitted nations to choose between information exchange and a withholding tax.

While the EU's Directive has not yet received final approval, negotiators are seeking final implementation by 2011 and have already sought negotiations with the six non-EU nations. The EU openly acknowledges that the Savings Tax Directive will fail without the participation of non-member nations, since "the proposal could incite paying agent operations to relocate outside the EU."⁵² The Savings Tax Directive seeks to overturn existing international practices. Nations would have no choice but to collect information on foreign investors, even if there was no need to amass that data for purposes of domestic laws or administrative practices.⁵³

⁵² Ibid, p. 2.

⁵³ Ibid, p. 3.

Task Force on Information Exchange and Financial Privacy

Analysis

National Security, Terrorism and Law Enforcement

The current international information exchange system is inadequate. It is ad hoc and relatively undeveloped. It has only been since the attack on September 11 that attempts to systematize the international exchange of information have begun. Interpol, for example, has undertaken to establish an international terrorism database.

This database, however, will not be fully successful in accomplishing its aims for two primary reasons. First, Western agencies will not be able to fully share information through this mechanism because Interpol includes many governments that are either known sponsors of terrorism or are otherwise hostile to the U.S. and its allies. It would be foolhardy to trust sensitive information to such a system, knowing that officials in certain governments would have free access to it and may provide it to terrorists or otherwise abuse the information.

Interpol has made it clear in its public pronouncements that all of its members will participate in the database. Interpol members, for example, include Algeria, Belarus, Bosnia-Herzegovina, Bulgaria, Chad, China, Colombia, Cuba, Iran, Iraq, Kazakhstan, Libya, Mozambique, Myanmar, Nigeria, Pakistan, Somalia, Sudan, Syria, Tanzania, Vietnam, Yemen and Yugoslavia. These countries have one or more of the following characteristics: major corruption problems, hostility to the West, have sponsored terrorism in the recent past, or have important factions within their governments that are friendly to groups that support terrorism.

Second, there is every reason to believe that many Interpol member governments may use, to the extent that they can, the financial and other information obtained by means of the database for other purposes, particularly if it is as wide-ranging and comprehensive as it should be to be effective. They are likely to use the database to obtain information on political opponents or problematic religious or ethnic minorities in order to oppress them. It is not difficult to imagine member governments or persons within certain governments using the information to assist terrorists.

The Financial Action Task Force (FATF) faces similar problems. FATF membership and observers, while somewhat more restricted than Interpol, include many governments that are not democratic and some that are problematic.⁵⁴ Western agencies

⁵⁴ Current FATF members are Argentina, Australia, Austria, Belgium, Brazil, Canada, Denmark, European Commission, Finland, France, Germany, Greece, Gulf Co-operation Council, Hong Kong, China, Iceland, Ireland, Italy, Japan, Luxembourg, Mexico, Kingdom of the Netherlands, New Zealand, Norway, Portugal, Singapore, Spain, Sweden, Switzerland, Turkey, United Kingdom, and the United States. Member states of the Gulf Co-operation Council include Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates. Observers include the Asia / Pacific Group on Money Laundering (APG), Caribbean Financial Action Task Force (CFATF), Eastern and Southern Africa Anti-Money Laundering Group (ESAAMLG),

cannot engage in a full and free exchange of information in this environment. As with Interpol, there is no enforceable restriction on the use to which member governments can put the information. In fact, FATF, as an informal group with little oversight, faces few restrictions on its activities and little accountability.

There is the need to restrict the information shared to national security, law enforcement and anti-terrorism purposes. This restriction is important even in the case of friendly governments to ensure that the information is not used for inappropriate purposes (e.g. commercial, political, tax administration or civil purposes). Only by imposing these restrictions will participants' confidence in the system be high enough that they will freely provide information. It is important to restrict the information to reliable friendly governments so the information is not used against the United States or its citizens or to thwart its foreign or law enforcement policies. There is the need to make these restrictions legally enforceable and to monitor that they are being honored in practice.

A system that does not allow the U.S. and its allies to freely exchange relevant information will not be effective in preventing terrorism or enhancing national security. Yet the FATF and Interpol systems are so inclusive and free of meaningful restrictions that it would not be prudent to provide full information to these databases for fear that some government or some official in a corrupt or potentially hostile government will use the information to thwart the anti-terrorism or national security purposes of the database.

The Task Force believes that establishing a new Privacy and Information Exchange Convention, subject to meaningful, enforceable restrictions on membership and the use to which information can be put, is the best means to facilitate the kind of free exchange of information necessary to effectively combat terrorism. The new convention would internationalize traditional U.S. legal principles such as protections against unreasonable search and seizures and due process of law. It would provide for enforceable restrictions on the use to which information can be put and provide persons within adhering states a private right of action to enforce the Convention.

The United States, and its international partners through the new Privacy and Information Exchange Convention, should aggressively work with banking secrecy jurisdictions to obtain information related to crime and terrorism. The dual criminality principle should be honored. In other words, the person about whom information is sought or provided should be reasonably suspected of an act that is a crime in both jurisdictions. Countries that honor requests for information about criminals and terrorists should not be harassed or sanctioned because they honor financial privacy in civil controversies or matters that are not a crime in their jurisdiction (e.g. tax evasion). Misguided anti-competitive efforts like the OECD initiative against harmful tax competition should not be allowed to impede efforts to obtain information about terrorists or criminals.

Financial Action Task Force on Money Laundering in South America (GAFISUD) and by extension their member states which include, for example, Mozambique, the Seychelles, Tanzania, and Pakistan.

With changing technologies, ever-higher standards for information and data integrity must be recognized. Any information system can be compromised. It is important to recognize that it is easier to compromise a system from within. Data needs to be protected from natural disasters or accidents (requiring backup, distribution, redundancy), human error and input problems (concerning verification and validation), and unauthorized access (constantly examining access control and security with an eye toward deterrence, traceability and investigative preparation).

U.S. domestic law also must be revised. Existing money laundering rules currently generate so many “suspicious activity reports” (156,000 in 2000) and “currency transaction reports” (12,000,000 in 2000) that reports about the activities of criminals and terrorists are lost in a mountain of useless reports about law-abiding citizens. The Currency Transaction Report system is particularly ineffective because of the sheer volume of reports generated and because the system is so simple to evade by even moderately sophisticated criminals.⁵⁵

Generating still more untargeted reports by reducing the reporting threshold or broadening the reporting network, as has been proposed, would hinder rather than aid law enforcement efforts. To make the system more effective, the current CTR and SAR system should be replaced. Instead, the authorities should generate a confidential “watch list” consisting of individuals and organizations (and their known aliases, identifying numbers and addresses) suspected of involvement in terrorism, other threats to national security, or serious crimes. The law should provide that persons could only be placed on the watch list if there was a reasonable and significant suspicion that the person was a threat to national security or was involved in terrorist activities or serious ordinary law crimes.

The federal government should employ computer technology to compare this watch list with the accounts maintained in financial institutions in the U.S. and abroad (by means of the proposed Privacy and Information Exchange Convention and otherwise) and if a match is made, the government would obtain a report of the financial transactions involving the accounts in question.

To effect such a system, financial institutions and government would need to cooperate to establish systems that allow an automated matching of the financial institution account databases and the watch list database. The matching program should examine names, identifying numbers and addresses.

Useful information can be gleaned from aggregate capital flows to provide indications for law enforcement and intelligence personnel. However, the reporting of aggregate information in place of the CTRs without personally-identifiable information on customers would offer comparable benefits while greatly diminishing the regulatory burden and better protecting financial privacy.

⁵⁵ This evasion may be accomplished by either making transactions under the \$10,000 reporting threshold or by inflating the cash receipts of an otherwise legitimate business.

The current adversarial approach taken by regulators towards financial institutions regarding the money laundering requirements has been counterproductive. Subjective and ever-changing requirements -- coupled with disproportionately heavy and arbitrary fines -- have instituted an economic incentive to over-report, even in cases where there is no reasonable suspicion of wrong-doing. Current practice in effect institutes a “report to protect yourself from fines” approach rather than a “report transactions which should be investigated” one.

The new FinCEN approach following the passage of the USA PATRIOT Act suggests a greater emphasis on minimizing burdens on financial institutions and unwarranted intrusions on individual privacy. The Task Force welcomes this increased concern. Allowing financial institutions to send more urgent information to FinCEN by e-mail or via FinCEN’s toll-free hotline is a constructive move. It represents a move toward providing less but better information to law enforcement.

Penalties for non-compliance of money laundering requirements are often more severe than requirements for maintaining the safety and soundness of the financial institutions and should be reduced. Such a change would result in the reporting of better information, rather than just more information, for law enforcement and intelligence purposes.

The Task Force supports the efforts of the 2001 National Money Laundering Strategy to begin objectively evaluating which strategies are most effective. We also agree with the sentiment expressed in the report that policies that are not making a significant difference in disrupting criminal activities should be discontinued.

Tax Administration

OECD Harmful Tax Competition

Tax competition is a highly desirable limit on the degree to which governments can tax and a check on the inefficiency and corruption of government. Countries that wish to attract investment from abroad by providing low taxes have every right to do so and neither the OECD nor the UN should dictate tax levels to sovereign states.

When evaluating the appropriateness of support for the OECD Harmful Tax Competition initiative, it is important to note that the United States, the United Kingdom and Switzerland would also be on the OECD blacklist except that OECD members were excluded. The U.S., for example, has relatively low taxes. Moreover, the U.S. allows foreigners to invest confidentially in the U.S. free of tax and provides those foreigners with a preferential tax regime when compared to the taxation that U.S. nationals have to bear.⁵⁶ This kind of preference, designed to attract capital from abroad, is precisely the kind of harmful tax provision that the OECD decries.⁵⁷

⁵⁶ See the discussion of the portfolio interest exemption in the Tax Administration section above.

⁵⁷ In OECD parlance, it is often called “ring-fencing.”

In time, however, the U.S. can expect the high-tax European Union to bring pressure to bear through the OECD, the WTO, the UN and otherwise (as has been done by the EU in the past with respect to U.S. Domestic International Sales Corporation law and, more recently, the U.S. Foreign Sales Corporation law). This process has, in fact, already begun and the proposed interest reporting regulations represent an effort by the U.S. Treasury to accede to that pressure. If the U.S. has been a party to bringing extreme pressure to bear on small countries that do nothing more than the U.S. does, resisting that pressure will be intellectually and politically difficult. It is wrong for the U.S. to be demanding that the small targeted countries live by tax and financial privacy rules by which the U.S. itself is not willing to abide.

The OECD initiative targets certain countries while exempting the U.S. and others. It is therefore inconsistent with our national treatment and most favored nation treaty commitments as a member of the World Trade Organization (WTO). By virtue of its membership in the WTO, the U.S. will soon be forced to choose between the OECD initiative and its own privacy and tax policies. If the Bush administration has followed the Clinton administration's lead in pressuring small countries to accept the OECD initiative, it is quite possible that the U.S. will bend to European pressure and comply with the OECD initiative itself. This would sacrifice U.S. taxpayer privacy, as U.S. taxpayer information started flowing to other governments. It would also result in a massive capital outflow because many foreigners invest here to take advantage of the tax-free investment environment. This may sound alarmist, but if, in light of the trade problems with the OECD plan, the Bush administration continues the previous administration's strong support of the OECD plan, then either the administration plans to ignore the WTO or it plans to sacrifice U.S. taxpayer privacy. It is more likely the administration will sacrifice privacy than sacrifice the WTO.

The OECD MOU provides for the total abolition of any financial privacy in the 41 targeted countries as it relates to the 30 OECD member countries. The targeted countries would be under an obligation to routinely share banking, tax and other financial information with OECD member countries. There would be no requirement for the recipient country to show probable cause to believe that a crime had been committed in either country. There would not even be a requirement to show that some civil wrong had been committed or was even suspected. The information would simply be routinely sent to any OECD country that asked for it. There are absolutely no restrictions on the use to which the information may be put.

Once that step has been taken, there will be no principled reason for the exchange of information not to be generalized so that any government in the world will be entitled to the information. The logic of the OECD proposal is the total abolition of financial privacy and a world where all governments can access the financial information of any individual living anywhere in the world. That, in fact, is exactly what the proposed UNITO would do.

Even OECD countries like Turkey and Greece have questionable human rights records and may use the information against political opponents and to further their

foreign policy goals. Outside of the OECD, such abuse of the information is a virtual certainty. European intelligence services routinely help their large firms today, and there is nothing to prevent OECD countries' intelligence services from sharing this kind of information with private companies because there are no restrictions in the OECD proposal to ensure that this does not happen.

United Nations International Tax Organization

One of the proposed purposes of the proposed UNITO would be to enable a government to tax people on their wages or investment even after they have emigrated from the country. The idea that a government should be able to impose taxes on the future income of those that have emigrated from its jurisdiction is repugnant and a violation of fundamental human rights. It rests on the premise that the state retains a right to the fruits of its former national's future labor and investment income even after they have emigrated. It should be viewed as a violation of Article 13 of the Universal Declaration of Human Rights, adopted by the UN General Assembly in 1948, which states in relevant part that "[e]veryone has the right to leave any country."

The proposed UNITO would result in every UN member government having routine unqualified access to the financial information of the citizens of all U.N. member states. It would undoubtedly result in governments that receive this information using it not only for tax purposes but for intelligence purposes and to oppress minorities and political opposition. It is extraordinarily naïve to believe that governments, particularly those known to systematically violate human rights, will not use sensitive information provided to them by the UN to achieve political objectives within their own countries. If the UN enables them to track the financial activities of their political opponents, then it will make it much easier for oppressive governments to identify and oppress their opposition.

Providing the United Nations itself with the ability to tax directly the nationals of its several states would effectively create the first global government. It would begin a process of centralization similar to that currently being undertaken by the European Union and would necessarily exact a steep price in terms of reduced freedom and limits on U.S. national sovereignty.

Information is power. Given the propensity for harm that the modern state has demonstrated time and again during the last century, it is not prudent to trust governments across the globe with that much unbridled power. It would be unwise to give governments the means to identify, defund and cripple their political opponents, to suppress religious freedom and to control the lives of their citizens. The OECD initiative should give pause to anyone who attaches even the slightest value to financial privacy.

U.S. Qualified Intermediary Rules

The United States qualified intermediary (QI) rules are overbroad. They contain provisions that other countries find objectionable because they represent an invasion of

privacy or because they would require a violation of the foreign country's domestic law. Furthermore, these rules are not necessary to enforce U.S. law. For example, the QI rules allow the IRS to impose country by country reporting on the QI.⁵⁸ Such reporting is objectionable to many QIs because it constitutes an invasion of privacy (by potentially allowing the identification of clients) and may constitute a violation of a foreign country's domestic law. Yet, if a QI client is receiving dividends for residents of non-treaty countries, there is no need to break the clients down by country since all non-treaty country payees are subject to the same withholding rates and no withholding tax rate could be higher. By way of further example, all non-resident alien or foreign corporation recipients of U.S. source portfolio interest income are exempt from tax. There is also no need to segregate these recipients by country or, for that matter, to report the amount received.

The QI rules should not require QIs to do administrative work that is unnecessary to enforce U.S. laws and that may require them to violate their own laws or the privacy of their clients. This is particularly true since QIs are subject to independent third-party audits to ensure that their characterizations of their clients' nationalities are accurate.⁵⁹ Country by country analysis (although not reporting) is required only in those cases where the income is subject to tax and the client wishes to take advantage of treaty provisions to achieve a lower withholding tax rate. It would be sufficient for U.S. purposes to report by withholding rate pools rather than by country.

Neither QIs nor non-QIs should be required to file Form 1042-S with respect to foreign beneficial owners that are either receiving income exempt from U.S. tax or are paying the maximum U.S. tax.⁶⁰ In neither case does receipt of the form further a U.S. interest. In the former case, the U.S. has disclaimed any interest in taxing the income and therefore no information relating to that person is necessary, other than establishing the foreign nationality of the recipient (which is accomplished otherwise under the QI rules). In the latter case, the recipient would be paying the maximum amount allowed by law, so there is no need to report any information relating to that person since no such information could result in greater tax liability.

The QI rules should be narrowed to require only information and administrative tasks necessary to enforce U.S. law. The current QI provisions unnecessarily intrude on financial privacy, unnecessarily violate the national sovereignty of foreign states, unnecessarily place foreign financial institutions in the untenable position of being asked to violate their domestic law, and will cause an unnecessary and undesirable flight of capital from the United States.⁶¹

⁵⁸ Rev. Proc. 2000-12, at section 8.03 of the QI Agreement, with respect to QIs entering into agreements after December 31, 2001 or whose agreements expire or otherwise, if the IRS so decides.

⁵⁹ See QI Agreement, section 10.01, Rev. Proc. 2000-12 and the discussion above related to QI audits and KYC rules.

⁶⁰ Pursuant to sections 8.01 through 8.03 of the QI Agreement, QIs generally need not do so but must in certain instances. Non QIs, however, must generally do so.

⁶¹ As is more fully discussed below with respect to the proposed interest reporting regulation, the provisions of the QI rules that are unnecessary to enforce U.S. law may be challengeable in court and should be reviewed by the Office of Management and Budget.

U.S. Interest Reporting Regulations

The proposed IRS regulation on deposit interest paid to nonresident aliens is unnecessary to enforce U.S. law. For nearly two decades, U.S. law has encouraged foreigners to invest in U.S. banks and debt securities by imposing no tax on interest earned by foreigners, except in very narrow circumstances. Accordingly, there is no need for the U.S. government to track the amounts paid to these persons to enforce U.S. law. All that needs to be established is that the payments are indeed being made to foreigners.

It is axiomatic that the executive branch has no authority to issue regulations except pursuant to law.⁶² The regulation should, therefore, be void as being unauthorized by statute. It is also void as arbitrary and unreasonable since it is not “reasonably related to the purposes of the enabling legislation.”⁶³

The regulation is also bad policy. It imposes an unnecessary major compliance burden on U.S. financial institutions. This compliance burden imposes a needless burden on the U.S. economy and impedes the competitiveness of U.S. financial institutions. Moreover, the regulation operates at cross purposes with the successful Congressional policy inaugurated in 1984 of attracting foreign capital to the United States. The regulation, if implemented, will have a substantial adverse impact on U.S. capital markets and the U.S. economy by encouraging a significant portion of the estimated one trillion dollars attracted by the portfolio interest exception to be withdrawn from U.S. capital markets. Many foreign investors will no longer find U.S. debt securities an attractive investment if their interest income is reported to their government by the IRS.

The Congressional Review Act and Executive Order 12866 clearly apply to this regulation. This IRS regulation would impose a significant cost on the economy and should be subject to the regulatory review process. Although the Internal Revenue Service, by a combination of declaring most of its regulations “interpretive” within the meaning of the Administrative Procedure Act and not “major” within the meaning of Executive Order 12866, has effectively exempted itself from regulatory oversight, this regulation is an appropriate case for the Office of Management and Budget (OMB) to exercise its lawful powers. OMB should review this regulation and stop it if the Treasury does not withdraw it.

The real reason the proposed regulation was released is that the IRS bureaucracy and the Clinton Treasury Department wanted the United States to become a full player in a global tax information exchange network such as those proposed by the OECD and UN designed to thwart tax competition. In the Background and Explanation section of the regulation, the IRS very nearly comes out and says as much. They want to help enforce

⁶² “The exercise of quasi-legislative authority by government departments and agencies must be rooted in a grant of such power by the Congress,” *Chrysler Corp. v. Brown*, 441 U.S. 281, 302 (1979). See also *Morrill v. Jones*, 106 U.S. 466, 467 (1883).

⁶³ See, e.g., *Mourning v. Family Publication Serv.*, 411 U.S. 356, 369 (1973), *Bowen v. American Hosp. Assn.*, 476 U.S. 610, 626 (1986).

foreign government tax systems to prevent tax competition.⁶⁴ Tax competition, as explained in the OECD discussion above, however, is a very positive force globally and especially positive for the United States since the U.S. has relatively low taxes compared to most industrialized countries.

European Union Savings Tax Directive

The European Union Savings Tax Directive is perhaps even more aggressive than the OECD's so-called harmful tax competition initiative. The EU wants automatic exchange of information relating to all earnings by foreign investors. There would be no due-process legal protections.

Advocates of the European Union Savings Tax Directive understand that the proposed cartel will not work so long as there are jurisdictions hospitable to foreign investment. As such, they require that six non-EU nations – including the United States – participate before the Directive can take effect. In addition to the other five nations, the Directive assumes participation by British and Dutch possessions in the Caribbean.⁶⁵

As the world's biggest beneficiary of foreign investment, the United States would suffer some degree of capital flight. The larger concern is that U.S. legal protections would be undermined by automatic information exchange.

⁶⁴ This desire is a function of a sense of solidarity among international tax bureaucrats and, perhaps, adherence to a flawed policy of capital export neutrality (a policy rejected by the Congress in this area of the law).

⁶⁵ http://europa.eu.int/comm/taxation_customs/publications/official_doc/IP/ip011026/memo01266_en.pdf

Task Force on Information Exchange and Financial Privacy

Recommendations

I. Form an Effective International Convention for Information Exchange Composed of Democratic Governments that Respect the Rule of Law

It has become apparent that the current international framework for information sharing is inadequate to achieve the needs of law enforcement and national security. This is true of FATF, Interpol, EU and U.S. efforts (most notably FinCEN). Moreover, the current framework does not adequately protect information to ensure that it does not fall into hostile hands, that the information is used appropriately and that legitimate privacy concerns are honored.

The United States should take the lead in forming an effective international convention composed of democratic governments that respect the rule of law to enable the United States to obtain and routinely share information about the financial and other activities of terrorists and criminals.

The Task Force recommends that the U.S. enter into a Convention on Privacy and Information Exchange to (1) make information exchange for national security, anti-terrorism and law enforcement purposes more effective, (2) prevent the information obtained and shared from falling into hostile hands, and (3) protect, in a legally enforceable manner, the privacy of innocent persons. A draft Convention is part of this report.

The membership in this Convention should be restricted to governments that:

1. are democratic;
2. respect free markets, private property and the rule of law;
3. can be expected to always use the information in a manner consistent with U.S. national security interests;
4. have in place (in law and in practice) adequate safeguards to prevent the information from being obtained by hostile parties or used for inappropriate commercial, political or other purposes.

Examples of governments that would appear to meet these requirements would include the governments of Australia, Canada, Germany, Japan, South Korea, Taiwan, and the United Kingdom (and its dependencies). Certain NATO allies, most notably Greece and Turkey, do not currently provide adequate safeguards with respect to information and also have inordinate difficulties with corruption and protecting civil rights. Certain countries (e.g. Switzerland, Liechtenstein and Austria) that are financial centers but have not been involved in the Western Security network may be candidates for involvement.

The activities of the Convention's adherents should be limited to obtaining and sharing information for national security, law enforcement and anti-terrorism purposes. The Convention should develop and enforce protocols to ensure the information is not provided to hostile parties or used for inappropriate commercial or political purposes or for other purposes unrelated to law enforcement or anti-terrorism efforts. Protocols should ensure that private information of innocent persons is protected. The Convention should provide a private right of action for persons in member states to enforce their legal rights under the Convention in member state courts.

II. Better Target Money Laundering Laws

Existing money laundering rules currently generate so many "suspicious activity reports" (156,000 in 2000) and "currency transaction reports" (12,000,000 in 2000) that reports about the activities of criminals and terrorists are lost in a mountain of useless reports about citizens going about their law-abiding activities. The Currency Transaction Report system is particularly ineffective because of the sheer volume of reports generated and because the system is so simple to evade by even moderately sophisticated criminals. Suspicious Activity Reports are problematic because of the necessary lack of clear and objective guidelines. Unfortunately, the U.S. Congress just made the situation worse with the passage of the USA PATRIOT Act which further expands the reporting system and, in effect, increases the size of the haystack which the law enforcement community must search for the terrorist and criminal "needle."⁶⁶

The last thing that would be constructive in the effort to apprehend terrorists and criminals would be to generate even more untargeted reports by, as has been proposed, reducing the reporting threshold or broadening the reporting network. To rationalize the effort to apprehend terrorists and criminals, the current CTR and SAR system should be replaced. Instead, the authorities should generate a confidential "watch list" consisting of individuals and organizations (and their known aliases, identifying numbers and addresses) about which there is reasonable and significant suspicion of involvement in terrorism, other threats to national security or serious crimes.

A mechanism should be established whereby the government can employ computer technology to compare this watch list with the accounts maintained in financial institutions in the U.S. and abroad (by means of the proposed Privacy and Information Exchange Convention and otherwise) and if a match is made, the government would obtain a report of the financial transactions involving the accounts in question.

To effect such a system, financial institutions and government would need to cooperate to establish high legal standards and practices, and systems that allow an automated matching of the financial institution account databases and the watch list

⁶⁶ The Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism (USA PATRIOT ACT) Act of 2001 (which includes the *International Money Laundering Abatement and Financial Anti-Terrorism Act of 2001*, the *First Responders Assistance Act*, the *Crimes Against Charitable Americans Act of 2001*, and the *Critical Infrastructures Protection Act of 2001*) (H.R. 3162; Public Law No: 107-56).

database. The matching program should examine names, identifying numbers and addresses.

Since some terrorist organizations have used financial fraud to finance their activities, increased attention to information integrity and systems security, including improved personnel training, could help prevent incidences of identity fraud and other problems. FinCEN and other financial regulators should encourage the adoption of better data security and encrypted e-mail and other communications.

III. Prioritize National Security, Anti-Terrorism and Crime

The United States should aggressively work with banking secrecy jurisdictions to obtain information related to crime and terrorism. The dual criminality principle should be honored. In other words, the person about whom information is sought or provided should be suspected of an act that is a crime in both jurisdictions. Countries that honor requests for information about criminals and terrorists should not be harassed or sanctioned because they honor financial privacy in civil controversies or matters that are not a crime in their jurisdictions (e.g. tax evasion). Misguided efforts like the OECD initiative against harmful tax competition should not be allowed to impede efforts to obtain information about terrorists.

IV. The United States Must Prevent Sensitive Information From Reaching Hostile Hands

Proposals such as the proposal by the United Nations High Level Panel on Financing for Development to create a UN International Tax Organization, which would provide sensitive U.S. private financial information to hostile states or states without adequate privacy safeguards, should be opposed. Interpol, for example, includes countries known to sponsor terrorism (e.g. Iran, Iraq, Libya, Somalia, Syria, Sudan), other countries that may be hostile to the West (e.g. the People's Republic of China, Cuba, Yugoslavia) and countries with major corruption problems (e.g. Bulgaria, Colombia, Nigeria). Financial Action Task Force members (particularly its regional and observer status participants) also pose unacceptable security risks.⁶⁷

Accordingly, no existing international organization has both the breadth to be effective and the standards to ensure that both our national security and the privacy of our citizens are protected. It is impossible for any of these organizations to serve as a genuine clearing house for information since the security threat posed by member

⁶⁷ Current FATF members are Argentina, Australia, Austria, Belgium, Brazil, Canada, Denmark, European Commission, Finland, France, Germany, Greece, Gulf Co-operation Council, Hong Kong, China, Iceland, Ireland, Italy, Japan, Luxembourg, Mexico, Kingdom of the Netherlands, New Zealand, Norway, Portugal, Singapore, Spain, Sweden, Switzerland, Turkey, United Kingdom, and the United States. Member states of the Gulf Co-operation Council include Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates. Observers include the Asia / Pacific Group on Money Laundering (APG), Caribbean Financial Action Task Force (CFATF), Eastern and Southern Africa Anti-Money Laundering Group (ESAAMLG), Financial Action Task Force on Money Laundering in South America (GAFISUD) and by extension their member states which include, for example, Mozambique, the Seychelles, Tanzania, and Pakistan.

countries is simply too high. A more restrictive organization is necessary in order for the project to work effectively.

With changing technologies, ever-higher standards for information and data integrity must be recognized. Any information system can be compromised. It is important to recognize that it is easier to compromise a system from within. Data needs to be protected from natural disasters or accidents (requiring backup, distribution, redundancy), human error and input problems (concerning verification and validation), and unauthorized access (constantly examining access control and security with an eye toward deterrence, traceability and investigative preparation).

V. The United States Should Withdraw Its Proposed Interest Reporting Regulation

This regulation would cause large amounts of foreign capital to leave the United States, impose large compliance costs on U.S. financial institutions that are unnecessary to enforce U.S. law, and reduce the competitiveness of U.S. financial institutions. The regulations are not authorized by statute and should be found arbitrary and unreasonable within the meaning of the applicable Supreme Court jurisprudence.

If the Treasury Department does not withdraw this regulation on its own initiative, the Office of Management and Budget should exercise its authority under the Congressional Review Act and Executive Order 12866 to stop the regulation.

VI. The United States Should Oppose the Creation of a United Nations International Tax Organization

The proposed UNITO would be destructive. It would impede tax competition and it may lead to a dramatic reduction in U.S. sovereignty. The proposal to allow the UN to directly tax persons in UN member states is the first step toward a world government and would inevitably have an adverse economic impact on relatively free countries like the United States. The proposal to use the UNITO to enable governments to tax people on future earnings even after they have emigrated would violate fundamental human rights and would be fundamentally against the interest of a nation of immigrants such as the United States. Finally, and perhaps most importantly, the proposal to share routinely all financial information, including banking and tax return information, among all UN member governments would constitute a gross violation of U.S. citizens' privacy rights and would aid the most repressive regimes on the planet by enabling them to more fully track the activities of their political opponents and oppressed minorities.

VII. The United States Should Oppose the OECD Harmful Tax Competition Initiative

The United States should oppose the OECD Harmful Tax Competition initiative. It represents an attempt by high tax European countries to extraterritorially enforce their high tax rates. The United States itself would qualify as engaging in harmful tax competition under the rules laid out by the OECD. Were the OECD rules also applied to OECD countries, the U.S. would be subject to draconian international sanctions. The

U.S. should not be a party to applying rules against small countries that it is not willing to abide by itself. Countries that honor financial privacy and maintain low tax rates should not be sanctioned merely for doing so.

The United States, as a low tax country and as a country that attracts capital by offering foreign investors the opportunity to invest in the U.S. free of tax, would be severely harmed by a generalization of the proposed OECD rules.

Moreover, the OECD initiative represents a major step toward the unrestricted disclosure of private financial and tax information, including from the U.S. and other OECD countries, to a wide array of countries that can be expected to misuse the information for commercial, political or intelligence purposes.

VIII. The United States Should Modify its Qualified Intermediary Rules

The qualified intermediary (QI) rules should not impose burdens on foreign financial institutions that are unnecessary to enforce U.S. law. To do so unnecessarily limits financial privacy, intrudes on the national sovereignty of other states and will result in unnecessary and undesirable flight of capital from U.S. markets.

The QI rules should be amended so reporting pools are by withholding tax rate (including a pool for the maximum rate and for income exempt from U.S. tax (most notably portfolio interest)).

Neither QIs nor non-QIs should be required to file Form 1042-S with respect to foreign beneficial owners that are either receiving income exempt from U.S. tax or are paying the maximum U.S. tax. In neither case does receipt of the form further a U.S. interest. In the former case, the U.S. has disclaimed any interest in taxing the income and therefore no information relating to that person is necessary, other than establishing the foreign nationality of the recipient (which is accomplished otherwise under the QI rules). In the latter case, the recipient would be paying the maximum amount allowed by law, so there is no need to report information relating to that person since no such information could result in greater tax liability.

IX. The United States Should Reject the European Union's Savings Tax Directive

For the same reasons outlined above in the section on the OECD's "harmful tax competition" initiative, the United States should decline to participate in the European Union's Savings Tax Directive. The United States is a capital-inflow country. It is not in America's interest to facilitate foreign taxation of U.S.-source income.

Convention on Privacy and Information Exchange

General Explanation

The current patchwork of international information exchange treaties, organizations and networks has two important flaws. First, the current system is not nearly as effective as it could and should be in aiding law enforcement and anti-terrorism efforts. Second, it imposes little or no legally cognizable restrictions on the use to which governments can put the information obtained and insufficiently protects individuals' privacy rights.

The proposed Convention would address both problems by making the international information exchange system much more effective and, for the first time, legally commit leading countries to the respect of individual privacy and provide enforceable restrictions on the use to which obtained information can be put.

The Convention would facilitate the exchange of information among Member States for national security, anti-terrorism and law enforcement purposes and only these purposes. In stark contrast to present practice, the Convention would establish legally enforceable rules to ensure this information is adequately protected and to prevent that information from being obtained by hostile parties, potentially hostile parties, parties that do not have adequate safeguards under domestic law or parties that in practice do not observe those safeguards. It would ensure that the information is not used for inappropriate commercial, political or other purposes.

The Convention would establish a private right of action, enforceable in Member State courts, with respect to the legal rights afforded to individuals under the Convention.

Convention on Privacy and Information Exchange

PREAMBLE

Whereas, the individual right to life, to liberty and to possess property are fundamental human rights and governments have an obligation to protect these rights;

Whereas, to better protect these rights, there is a need for greater cooperation among democratic states to obtain information and to facilitate the exchange of information for national security, law enforcement and anti-terrorism purposes;

Whereas, there is a need to protect individual privacy under international law;

Whereas, there is a need to ensure that sensitive private, national security, law enforcement and terrorism-related information is safeguarded,

Therefore, the States party to this Convention have agreed as follows:

Article I

ESTABLISHMENT OF CONVENTION

The Contracting States undertake to respect and to ensure respect for the present Convention on Privacy and Information Exchange in all circumstances.

Article II

PURPOSE

The purpose of this Convention shall be:

- (1) to facilitate the exchange of information among Member States for national security purposes;
- (2) to facilitate the exchange of information among Member States to detect, prevent or defend against terrorism and to apprehend persons who have committed acts of terrorism;
- (3) to facilitate the exchange of information among Member States to detect, prevent or defend against serious ordinary law crimes and to apprehend persons who have committed serious ordinary law crimes;
- (4) to protect the privacy of citizens of Member States and other innocent persons;
- (5) to ensure that information obtained by Member States or exchanged among the Member States by means of the Convention is adequately protected and to prevent that information from being obtained by hostile parties, potentially hostile parties, parties that do not have adequate safeguards under domestic law or parties that in practice do not observe those safeguards;

- (6) to ensure that information obtained by Member States or exchanged among the Member States by means of the Convention is used solely for purposes set forth in subparts (1) through (3) of this Article; and
- (7) to ensure that information obtained by Member States or exchanged among the Member States by means of the Convention is not used for inappropriate commercial, political or other purposes.

Article III

PRINCIPLES

The Member States reaffirm the following principles:

- (1) The right to life, to liberty and to possess property are fundamental human rights;
- (2) The governments of the Member States have an obligation to protect the national security of the Member States and to protect the lives, liberty and property of the citizens of the Member States from attack from hostile parties;
- (3) The governments of the Member States have an obligation to detect, prevent or defend against terrorism and to apprehend persons who have committed or planned acts of terrorism;
- (4) The governments of the Member States have an obligation to detect, prevent or defend against serious ordinary law crimes and to apprehend persons who have committed serious ordinary law crimes;
- (5) The governments of the Member States have an obligation to respect and protect the privacy of citizens of Member States and other innocent persons.

The Convention shall be guided by these principles.

Article IV

DEFINITIONS

For purposes of this Convention the following terms shall be defined as follows.

- (1) *Establishment* means any private:
 - (a) place of employment,
 - (b) office,
 - (c) place of assembly, or
 - (d) house of worship.
- (2) *National Security Purposes* means action reasonably calculated to detect, prevent or defend against:

- (a) an attack by a hostile state or other hostile party on the territory of a Member State resulting in the loss of life or destruction of property;
 - (b) an attack by a hostile state or other hostile party on the civilian or military personnel of a Member State government without the territory of a Member State;
 - (c) an attack by a hostile state or other hostile party on the citizens of a Member State without the territory of a Member State;
 - (d) an attack by a hostile state or other hostile party on the information systems infrastructure of a Member State; and
 - (e) espionage directed against a Member State or citizens of a Member State.
- (3) *Party or Parties* means one or more international organizations, states, belligerents, private entities, individuals or other organization, entity or institution and their respective agents, employees, personnel, citizens or residents.
- (4) *Person* means a natural person, a corporation, a private business entity or a private non governmental organization.
- (5) *Protected Person* means any person that is a national of a Member State, a lawful resident of a Member State or domiciled in a Member State.
- (6) *Serious Ordinary Law Crime* means conduct that (a) constitutes an offence in all Member States and (b) is punishable by a maximum deprivation of liberty of four years or more in all Member States.
- (7) *Terrorism* means (a) any act intended to cause death or serious bodily injury to a civilian, or to any other person not taking an active part in the hostilities in a situation of armed conflict, when the purpose of such act, by its nature or context, is to intimidate a population, or to compel a government or an international organization to do or to abstain from doing any act, or (b) an act which constitutes an offence within the scope of and as defined in one of the following treaties:
1. Convention for the Suppression of Unlawful Seizure of Aircraft, done at The Hague on 16 December 1970.
 2. Convention for the Suppression of Unlawful Acts against the Safety of Civil Aviation, done at Montreal on 23 September 1971.
 3. Convention on the Prevention and Punishment of Crimes against Internationally Protected Persons, including Diplomatic Agents, adopted by the General Assembly of the United Nations on 14 December 1973.
 4. International Convention against the Taking of Hostages, adopted by the General Assembly of the United Nations on 17 December 1979.
 5. Convention on the Physical Protection of Nuclear Material, adopted at Vienna on 3 March 1980.
 6. Protocol for the Suppression of Unlawful Acts of Violence at Airports Serving International Civil Aviation, supplementary to the Convention for the

Suppression of Unlawful Acts against the Safety of Civil Aviation, done at Montreal on 24 February 1988.

7. Convention for the Suppression of Unlawful Acts against the Safety of Maritime Navigation, done at Rome on 10 March 1988.
8. Protocol for the Suppression of Unlawful Acts against the Safety of Fixed Platforms located on the Continental Shelf, done at Rome on 10 March 1988.
9. International Convention for the Suppression of Terrorist Bombings, adopted by the General Assembly of the United Nations on 15 December 1997.

Article V

MEMBERSHIP

- (1) The Contracting States shall be Members of the Convention, subject to this Article.
- (2) Each Member State is obligated to:
 - (a) maintain a democratic form of government;
 - (b) maintain adequate domestic laws against corruption in government;
 - (c) maintain adequate domestic law protecting individuals against deprivation of life, liberty or property without due process of law;
 - (d) maintain adequate domestic anti-terrorism laws;
 - (e) maintain domestic law that allows for the extradition of persons to other Member States that stand accused of committing or conspiring to commit under the law of another Member State one or more acts of terrorism or one or more serious ordinary law crimes;
 - (f) maintain domestic law that complies with Article VIII of this Convention relating to privacy;
 - (g) maintain domestic law such that Article IX of this Convention is enforceable;
 - (h) consistently and reliably comply in practice with the provisions of the Member State's domestic law referenced in this subpart (2);
 - (i) be a party to a treaty or treaties that, with respect to other Member States, provides for adequate mutual legal assistance in criminal matters; and
 - (j) consistently and reliably comply in practice with this Convention.
- (3) The Members of the Convention may decide to invite any Government prepared to assume the obligations of membership to accede to this Convention. Such decisions shall be unanimous. Accession shall take effect upon the deposit of an instrument of accession with the depositary Government.
- (4) Members of the Convention shall monitor the compliance or lack thereof of each Member with subpart (2) of this article. The Convention shall terminate the membership of any Member in the Convention that it finds is not in substantial compliance with subpart (2) of this article. Said termination shall be effective immediately upon the affirmative finding of two-thirds of the Members of the

Convention at a meeting of the Convention and the terminated Member shall have no more standing in the Convention than any other non-member state. The terminated Member may be readmitted pursuant to subpart (3) of this article.

Article VI

GOVERNANCE

- (1) Unless the Members of the Convention otherwise agree unanimously for special cases, decisions shall be taken and recommendations shall be made by mutual agreement of all the Members.
- (2) Each Member shall have one vote. If a Member abstains from voting on a decision or recommendation, such abstention shall not invalidate the decision or recommendation, which shall be applicable to the other Members but not to the abstaining Member.
- (3) No decision shall be binding on any Member until it has complied with the requirements of its own constitutional procedures. The other Members may agree that such a decision shall apply provisionally to them.
- (4) A Convention Conference, to which all the Members shall be invited to send delegates, shall be the body from which all acts of the Convention derive. Each Member State shall designate a person or persons to participate in the Conference as delegates. Each Member shall have one vote in the Convention Conference. There shall be an annual Convention Conference. Special Convention Conferences may be called upon the request of a majority of the members. Each Member shall be responsible for its own expenses. Convention Conference expenses shall be borne by the host government.
- (5) Members shall designate each year a Chairman, who shall preside at its session, and a Vice-Chairman.
- (6) Members may establish an Executive Committee and such subsidiary bodies as may be required for the achievement of the aims of the Convention.
- (7) Upon such terms and conditions as the Conference may determine, the Convention may:
 - (a) address communications to non-member States or organizations;
 - (b) address communications to individuals or private institutions;
 - (c) establish and maintain relations with non-member States or organizations;and
 - (d) invite non-member Governments or organizations to assist in activities of the Convention.
- (8) The first annual Convention Conference shall be in [***]. The time and place of subsequent Convention Conferences shall be as determined by the Members.
- (9) Each year, the Chairman of the Convention Conference shall issue a report describing and analyzing the operation of the Convention. The report may also contain recommendations of the Convention Conference. The Chairman shall make the report publicly available, provided however, that the Members may vote to not disclose a portion of the report if it determines that doing so is reasonably necessary to further the purposes of the Convention.

Article VII

GENERAL OBLIGATIONS

In order to achieve the purposes set forth in Article II, the Members of the Convention and those acting under their authority, in a manner consistent with this Convention and subject to the restrictions of this Convention, may:

- (1) obtain information,
- (2) provide information to other Member governments,
- (3) cooperate with law enforcement, intelligence and defense authorities of other Member governments,
- (4) make recommendations to other Members, and
- (5) enter into agreements with other Members, non-member States and international organizations.

In order to achieve the purposes set forth in Article II, the Members, in a manner consistent with this Convention and subject to the restrictions of this Convention, shall:

- (1) cooperate with law enforcement, intelligence and defense authorities of other Member governments,
- (2) enact and maintain domestic law to enforce Article VIII of this Convention, and
- (3) take steps to ensure that information obtained by means of the Convention and provided to other Members is safeguarded.

Article VIII

PRIVACY

- (1) No information obtained by means of the Convention shall be provided to any Member government and no Member government shall use information obtained by said Member government by means of the Convention except for the following purposes:
 - (a) for national security purposes,
 - (b) to detect, prevent or defend against terrorism and to apprehend persons who have committed acts of terrorism,
 - (c) to detect, prevent or defend against serious ordinary law crimes and to apprehend persons who have committed serious ordinary law crimes.
- (2) All Member Governments shall enact and maintain domestic law to enforce subpart (1) of this Article. Each Member shall ensure that individuals who act in contravention to subpart (1) of this Article shall be criminally liable such that said individual is (a) subject to deprivation of liberty of not less than four years, and (b) subject to dismissal if employed by the Member's government.

- (3) All Member Governments shall ensure that information obtained by means of the Convention or exchanged among the Member States by means of the Convention is not used for commercial, or political or other purposes unrelated to achieving the purposes of the Convention set forth in subparts (1), (2) and (3) of Article II.
- (4) Each Member Government shall respect the right of other Member Governments to respect and protect the privacy of citizens or other innocent persons in cases unrelated to achieving the purposes of the Convention set forth in subparts (1), (2) and (3) of Article II.
- (5) All Member Governments shall ensure that citizens of the Member States shall be secure in their persons, houses, establishments, papers and effects against unreasonable searches and seizures.
- (6) All Member Governments shall enact or maintain domestic law establishing adequate safeguards for the privacy of the citizens of the Member States. Said domestic law shall provide at least the following safeguards:
 - (a) protect individuals and private establishments from warrantless searches and seizures and require that warrants not be issued but upon a showing of probable or reasonable cause;
 - (b) prohibit the disclosure of tax information about individuals or private establishments obtained by Member States to private parties and restrict its use to national security, law enforcement, anti-terrorism or tax administration purposes;
 - (c) prohibit the disclosure of financial or personal information about individuals or private establishments that is (1) obtained by Member States by operation of law and (2) not in the public domain to private parties and restrict its use to national security, law enforcement, anti-terrorism or tax administration purposes;
 - (d) such other safeguards as the Members may provide, subject to the provisions of this Convention.

Article IX

RIGHTS OF PROTECTED PERSONS

- (1) Evidence obtained by a Member State by means of the Convention in deprivation of any rights, privileges, or immunities secured by this Convention, or other evidence obtained because of said evidence, shall not be admissible in a Court of Law of any Member State in a proceeding against a Protected Person or in an administrative proceeding of any Member State against a Protected Person.
- (2) Every person who, under color of any treaty, statute, ordinance, regulation, custom, or usage, of any Member State subjects, or causes to be subjected,

any Protected Person to the deprivation of any rights, privileges, or immunities secured by this Convention, shall be liable to the injured Protected Person in an action at law, suit in equity, or other proper proceeding for redress.

(3) To protect any rights, privileges, or immunities secured by this Convention, a Protected Person shall be entitled to injunctive relief in a Court of Law of competent jurisdiction of any Member State against:

- (a) any Member State, or
- (b) any person who under color of any treaty, statute, ordinance, regulation, custom, or usage, of any Member State,

who subjects, or causes to be subjected, said Protected Person to deprivation of any rights, privileges, or immunities secured by this Convention.

(4) Each Member State shall take such steps as are necessary under its domestic law to ensure that Protected Persons' rights under this Article are secured.

Article X

RATIFICATION

- (1) This Convention shall be ratified or accepted by the Signatories in accordance with their respective constitutional requirements.
- (2) Instruments of ratification or acceptance shall be deposited with the Government of the United States, hereby designated as depositary Government.
- (3) This Convention shall come into force on 30th September, 2003, if by that date three Signatories or more have deposited such instruments as regards those Signatories; and thereafter as regards any other Signatory upon the deposit of its instrument of ratification or acceptance.
- (4) Upon the receipt of any instrument of ratification, acceptance or accession, or of any notice of termination, the depositary Government shall give notice thereof to all the Contracting States and to the Secretary-General of the Organization.

Article XI

TERMINATION

Any Member State may terminate the application of this Convention to itself by giving three months' notice to that effect to the depositary Government.

IN WITNESS WHEREOF, the undersigned Plenipotentiaries, duly empowered, have appended their signatures to this Convention.

Task Force on Information Exchange and Financial Privacy

Appendix

This appendix contains many of the government documents referenced in this report and that constitute the basic framework of current and proposed information reporting and exchange networks in the United States and abroad. Either because they were quite lengthy documents or because they were only available for sale, a number of important documents were not included in this appendix.

The 1998 OECD report entitled “Harmful Tax Competition: An Emerging Global Issue” is available for purchase (\$16.00) and immediate download at:

<http://www.oecd.org/.../scripts/publications/bookshop/redirect.asp?231998041E>

Additional information about the U.S. qualified intermediary rules (including country specific attachments), U.S. know your customer (KYC) rules and U.S. income tax treaties is available at:

http://www.irs.gov/prod/bus_info/qi/index.html

The 131 page text of the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism (USA PATRIOT ACT) Act of 2001 (which includes the *International Money Laundering Abatement and Financial Anti-Terrorism Act of 2001*, the *First Responders Assistance Act*, the *Crimes Against Charitable Americans Act of 2001*, and the *Critical Infrastructures Protection Act of 2001*) (H.R. 3162; Public Law No: 107-56) is available at:

http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=107_cong_bills&docid=f:h3162enr.txt.pdf

The 90 page 2001 National Money Laundering Strategy, released jointly by Treasury and Justice Departments is available at:

<http://www.treas.gov/press/releases/docs/ml2001.pdf>

The Financial Crimes Enforcement Network, U.S. Department of Treasury, Strategic Plan 2000-2005 is available at:

<http://www.ustreas.gov/fincen/finstrategicplan2000.pdf>

The SAR Activity Review (October 2001) is available at:

<http://www.ustreas.gov/fincen/sarreviewissue3.pdf>