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Bryan S. Arce

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TAKEN TO THE CLEANERS: PANAMA'S FINANCIAL SECRECY LAWS FACILITATE THE LAUNDERING OF EVADED U.S. TAXES

It is estimated that as much as \$1.5 trillion may be “laundered” every year worldwide, or about two to five percent of the global domestic product.¹ Of this amount, \$500 billion can be attributed to hiding the proceeds of tax evasion.² Tax evasion and money laundering, although separate and distinct crimes, are intertwined in that all illegal proceeds, when laundered, effectively evade taxes, and all legitimate money that evades taxes becomes illegal and subsequently needs to be “laundered.”³

Money laundering can have substantial negative economic consequences for a country on an international scale.⁴ Money laundering can disrupt a country's financial integrity or even alter its economic policy.⁵

1. Linda McGlasson, *Revisions to Bank Secrecy Act: Anti-Money Laundering Exam Manual a “Positive Step,”* Aug. 31, 2007, <http://www.bankinfosecurity.com/articles.552>. See also Internal Revenue Service, Overview: Money Laundering, <http://www.irs.gov/compliance/enforcement/article/0,,id=112999,00.html> [hereinafter IRS Overview: Money Laundering] (last visited Feb. 13, 2009) (defining “money laundering” as “the means by which criminals evade paying taxes on illegal income by concealing the source and the amount of profit”)

2. Lucy Komisar, *Closing Down the Tax Haven Racket*, June 8, 2007, <http://the.komisarscoop.com/2007/06/closing-down-the-tax-haven-racket>.

3. Steven A. Dean, *Philosopher Kings and International Tax: A New Approach to Tax Havens, Tax Flight, and International Tax Cooperation*, 58 HASTINGS L.J. 911, 931 n.90 (2007). See also U.S. CONG., OFFICE OF TECH. ASSESSMENT, INFORMATION TECHNOLOGIES FOR CONTROL OF MONEY LAUNDERING 2 (1995) (“Hiding legitimately acquired money to avoid taxation also qualifies as money laundering.”).

4. John McDowell & Gary Novis, *The Consequences of Money Laundering and Financial Crime*, ECON. PERSPS. (May 2001).

5. *Id.* (“Money laundering can also adversely affect currencies and interest rates, as launderers reinvest funds where their schemes are less likely to be detected, rather than where rates of return are higher. And money laundering can increase the threat of monetary instability due to the misallocation of resources from artificial distortions in asset and commodity prices. . . . There are [also] significant social costs and risks associated with money laundering. Money laundering is a process vital to making crime worthwhile. It allows drug traffickers, smugglers, and other criminals to expand their operations. This drives up the cost of government due to the need for increased law enforcement and health care expenditures (for example, for treatment of drug addicts) to combat the serious consequences that result. . . . [Financial] criminal activity has been associated with a number of bank failures around the globe”). See also Julia Layton, *How Money Laundering Works*, <http://money.howstuffworks.com/money-laundering3.htm> (last visited Dec. 12, 2008) (“Other major issues facing the world's economies include errors in economic policy resulting from artificially inflated financial sectors. Massive influxes of dirty cash into particular areas of the economy that are desirable to money launderers

It corrupts government and banking officials, creates volatile international exchange rates, and produces unpredictable capital movements.⁶ Furthermore, money laundering helps fund terrorism and terrorist organizations, and undermines the national security of a country.⁷ But the effects of money laundering can also be felt on a local level. Loss of tax revenue is arguably one of the more significant socio-economic effects of money laundering.⁸ A government's inability to raise money through the collection of taxes may restrict investments in social services.⁹ Basic social programs such as health, housing, and education may not be properly funded, or may even be discontinued, because the tax revenue required to subsidize such programs has evaded government collection through the money laundering process.¹⁰ All citizens feel the effects of tax evasion and money laundering, in that the loss of tax revenue forces the government to place the burden on honest taxpayers to cover such costs through higher tax rates.¹¹

One of the most common and increasingly used methods to evade taxes and to launder money is to place assets in a "tax haven country."¹² In general, a "tax haven" is simply a country that imposes few or no taxes.¹³ However, some tax havens provide financial mechanisms, such as confidential bank accounts and shell companies, the only purposes of which are to hide the identities of the true owners from tax authorities and law enforcement of other countries.¹⁴ These countries also tend to have strict financial secrecy laws that severely limit, if not prevent, the

create false demand, and officials act on this new demand by adjusting economic policy.").

6. Sam Vaknin, *Money Laundering in a Changed World*, May 21, 2005, <http://www.globalpolitician.com/2746-money-laundering>.

7. International Monetary Fund, Factsheet: The IMF and the Fight Against Money Laundering and the Financing of Terrorism, Apr. 2007, <http://www.imf.org/external/np/exr/facts/aml.htm> [hereinafter IMF Factsheet]. See also Juan Zarate, Assistant Sec'y for Terrorist Fin. & Fin. Crimes, Prepared Remarks to the Florida Bankers Ass'n. (Feb. 9, 2005) [hereinafter Zarate Remarks to the Florida Bankers Ass'n] (on file with the Treasury Dep't. Office of Public Affairs).

8. See McDowell & Novis, *supra* note 4. See also Layton, *supra* note 5.

9. Annan Boodram, *The Many Faces of Money Laundering*, <http://www.caribvoice.org/Business/moneylaund.html> (last visited Dec. 12, 2008).

10. Komisar, *supra* note 2.

11. McDowell & Novis, *supra* note 4.

12. David Johnston, *Tax Cheats Called Out of Control*, N.Y. TIMES, Aug. 1, 2006. See also Komisar, *supra* note 2.

13. BLACK'S LAW DICTIONARY 695 (2d Pocket ed. 2001).

14. Komisar, *supra* note 2.

exchange of tax-related information between governments,¹⁵ obstructing a government's ability to find and prosecute tax cheats. The U.N. Office on Drugs and Crime states that such "financial havens and bank secrecy are a 'tool kit' for money launderers."¹⁶ Furthermore, in the United States, \$40 to \$70 billion of tax revenue are believed to be hidden from the Internal Revenue Service ("IRS") each year through the use of the tax haven system.¹⁷

In February 2007, as part of the proposed Stop Tax Haven Abuse Act, Panama was listed as a "probable location for U.S. tax evasion."¹⁸ In addition, the U.S. State Department currently considers Panama a "major money laundering country"¹⁹ for its allowance of financial transactions involving significant amounts of proceeds from serious crimes.²⁰ Both tax evaders and money launderers are drawn to Panama because it has, arguably, the strictest financial secrecy laws in the world and has even been nicknamed the "New Switzerland."²¹ This may be why Panama is second in the world, behind Hong Kong, in the number of foreign companies incorporated in its jurisdiction, companies believed to be used for the purpose of circumventing their local taxes.²² Moreover, the 2007 National Money Laundering Strategy²³ has identified Panama as the backdrop for a wide range of money laundering schemes.²⁴

15. David Spencer, *Exchange of Tax Information*, in 5 ACCOUNTANCY BUSINESS AND THE PUBLIC INTEREST 89 (2006).

16. U.N. Office on Drugs & Crime [UNODC], *Report on Financial Havens, Bank Secrecy and Money-Laundering*, U.N. Doc. UNIS/NAR/641 (June 8, 1998) [hereinafter UNODC, *Report*].

17. Mike Godfrey, *Senate "Offshore" Hearing Called "One-Sided,"* Aug. 3, 2006, http://www.tax-news.com/archive/story/Senate_Offshore_Hearing_Called_OneSided_xx24430.html (last visited Jan. 4, 2009).

18. Senate Newsroom Release, Summary of Levin-Coleman-Obama Stop Tax Haven Abuse Act (Feb. 17, 2007) [hereinafter Tax Haven Abuse Act Summary].

19. DEP'T OF ST. BUREAU FOR INT'L NARCOTICS & LAW ENFORCEMENT AFFAIRS, 1 INTERNATIONAL NARCOTICS CONTROL STRATEGY REPORT 5-6 (2007) [hereinafter INCSR vol. 1].

20. DEP'T OF ST. BUREAU FOR INT'L NARCOTICS & LAW ENFORCEMENT AFFAIRS, 2 INTERNATIONAL NARCOTICS CONTROL STRATEGY REPORT 53 (2007) [hereinafter INCSR vol. 2].

21. See OffshoreLegal.org, *Panama Asset Protection vs. Swiss Asset Protection*, <http://www.offshorelegal.org/asset-protection/panama-offshore-asset-protection/swiss-asset-protection-vs-panama-asset-protection.html> (last visited Dec. 12, 2008) ("Switzerland was once the offshore asset protection capital of the world.").

22. Peter Riggs, *Why Are We Negotiating a Free Trade Agreement with Tax Haven Panama?*, June 30, 2007, http://www.taxjustice-usa.org/index.php?option=com_content&task=view&id=119&Itemid=47.

23. See Fin. Inst. Letter from Fed. Deposit Ins. Corp., Bank Secrecy Act, 2007 National Money Laundering Strategy (May 23, 2007) (noting that the 2007 National Money

This is not to say that Panama necessarily condones or supports money laundering. In fact, the country has very strict anti-money laundering regulations.²⁵ The problem, however, is that Panama only recognizes the crime of money laundering when it is directly related to a specified illegal activity such as drug trafficking, kidnapping, or extortion.²⁶ Because the Panamanian Government does not rely on income taxes as an essential part of the tax revenue it collects, the evasion of income tax is not considered a crime.²⁷ Therefore, tax evasion cannot be used as a predicate offense in prosecuting a money laundering violation in Panama.²⁸ Furthermore, Panama's legal structure follows the "dual criminality" principle, meaning that an offense must be a recognized crime in both Panama and the requesting country for Panama to comply with any financial information requests.²⁹ Consequently, petitions by the United States for financial information in purely tax-related matters will generally not be honored.³⁰

The dual criminality principle provides a safeguard against abuses by foreign jurisdictions attempting to discount the privacy rights afforded by Panama's borders.³¹ A basic principle of international law is that one country generally does not enforce the tax laws of another.³² Thus, the

Laundering Strategy was an interagency report released in May 2007 that incorporates information accumulated from the 2005 U.S. Money Laundering Threat Assessment, which identified various risks to the U.S. financial sector posed by money laundering).

24. See NATIONAL MONEY LAUNDERING STRATEGY 27, 43, 51, 58 (2007). [hereinafter NMLS 2007]

25. See Sec. Comm'n Res. No. 1-2004, Feb. 9, 2004. (Pan.); Law No. 42 (2000) (Pan.); Law No. 41 (2000) (Pan.); Law No. 147 (1966) (Pan.).

26. Law No. 41, art. 389 (defining the crime of money laundering as the receipt, negotiation, conversion, or transfer of moneys, titles, securities, assets, and other financial resources with knowledge that they are the product of activities related to drug trafficking, qualified embezzlement, traffic of human beings, traffic of illegal weapons, kidnapping, extortion, embezzlement, corruption of civil servants, robbery, international vehicle contraband, and acts of terrorism).

27. Ronojit Banerjee, *Money Laundering in the EU*, <http://www.people.ex.ac.uk/watupman/undergrad/ron/tax20evasion.htm> (last visited Dec. 12, 2008). See Taxation: Income Tax, 2008 PANAMA L. DIG. §§ 21.01, 21.09 (describing incomes not subject to taxation under the Panama Fiscal Code of 1956).

28. Banjeree, *supra* note 27.

29. INT'L MONETARY FUND, WORKING TOGETHER: IMPROVING REGULATORY COOPERATION AND INFORMATION EXCHANGE (2007).

30. Martin A. Sullivan, *Economic Analysis: Ah, Panama*, 47 TAX NOTES INT'L 11 (2007), available at http://www.panamaallinone.com/doc/Economic_Analysis_Panama.pdf.

31. Panamalaw.org, Tax Information Exchange Agreements (TIEA), http://www.panamalaw.org/tax_information_exchange_agreements.html (last visited Dec. 28, 2008).

32. *Pasquantino v. United States*, 544 U.S. 349, 352 (2005); *Banco Nacional de Cuba v. Sabbatino*, 376 U.S. 398, 448 (1964). See also Banerjee, *supra* note 27.

United States must work within the parameters of a country's legal system to ensure that U.S. taxes are not evaded.

However, the obstacles to the U.S. prosecution of criminals, namely financial secrecy and dual criminality, could be circumvented very easily with a tax treaty between the United States and Panama. More specifically, a Tax Information Exchange Agreement ("TIEA")³³ would allow for the free exchange of financial tax information irrespective of differences in either country's requirement or definition of a predicate crime to money laundering.

Tax treaties are valuable mechanisms enabling U.S. federal law enforcement agencies to track down tax evaders as well as other criminals.³⁴ The advantage of tax information is that, even if the United States is unable to prosecute criminals for major money producing crimes, it can still prosecute them for the accompanying offense of tax evasion. For example, when the U.S. government could not convict Al Capone on any of his suspected crimes, the IRS was able to convict him of tax evasion.³⁵ Bruno Richard Hauptmann, the man famed for kidnapping the Lindbergh baby, was initially arrested because of his failure to "launder the ransom money successfully."³⁶

On an international level, tax treaties have led to the effective prosecution of those who have attempted to hide their assets from U.S. tax authorities. For example, an American taxpayer was recently convicted for tax evasion after he tried to hide his assets in off-shore tax havens such as Bermuda, the British Virgin Islands, and Panama.³⁷ The fact that the IRS and the Department of Justice gathered enough evidence to prosecute this case through their TIEA with Bermuda³⁸ demonstrates the im-

33. Panamalaw.org, *supra* note 31 ("This is an agreement whereby one country can request all financial investment information regarding [its] citizens and corporations. This most definitely includes bank account information and stock brokerage type investments. There is no probable cause requirement to get this information. There is no criminality or dual criminality required. There is not even a tax violation required. The terms used in these treaties run along the lines of the country requesting the information claiming that [it] believe[s] the information to be relevant to [its] tax investigation.").

34. Press Release, John Harrington, Acting Int'l Tax Counsel, Testimony Before the Senate Finance Committee on Offshore Tax Evasion (May 3, 2007) [hereinafter Harrington] (on file with Treasury Dep't).

35. F.B.I History, Famous Cases: Alphonse Capone, aka Al, Scarface, <http://www.fbi.gov/libref/historic/famcases/capone/capone.htm> (last visited Dec. 28, 2008). *See also* IRS Overview: Money Laundering, *supra* note 1.

36. Paul Bauer & Rhoda Ullmann, *Understanding the Wash Cycle*, ECON. PERSPS. 2 (2001).

37. Harrington, *supra* note 34.

38. *Id.* ("[I]n 2004, Almon Glenn Braswell was sentenced to eighteen months in prison and ordered to pay over \$10 million in back taxes, interest and penalties. Mr. Bras-

portance of such a tax treaty. Had the taxpayer hidden all of his money in Panama alone, the outcome would have been very different.

The key to prosecuting money laundering is simply to "follow the money trail."³⁹ The ability to recover tax and financial information is the most effective way to secure the evidence required to reach a conviction for money laundering.⁴⁰ IRS investigations of illegal income are critical elements in assuring a money laundering conviction,⁴¹ and the agency values that "[t]he long hours of tracking and documenting financial leads allow an investigation to go right to the door of the money launderers and eventually to the leader of the illegal enterprise."⁴² The laundering of money accomplishes two important purposes for the criminal. First, it covers the trail of evidence leading back to the crime that produced the illicit funds.⁴³ Secondly, it conceals the money itself from forfeiture.⁴⁴ For these reasons, obtaining tax information and implementing a tax treaty are of paramount importance. The United States has to be able to trace funds back to their original crime as well as recover lost tax revenue.

This Note argues that a TIEA with Panama would allow the United States to circumvent the strict financial secrecy laws that shield American tax evaders and money launderers from prosecution. Part I of this Note describes the mechanics and interrelation of money laundering, tax evasion, and Panamanian financial secrecy laws. Part II addresses the measures the United States has implemented to combat the money laundering problem and their ineffectiveness in dealing with tax evasion. Part III proposes how the United States could implement a TIEA with Panama to address the U.S. need for tax information, while at the same time, respecting Panama's commitment to protecting its financial secrecy regime.

I. MONEY LAUNDERING AND TAX EVASION IN PANAMA

First, it must be understood that money laundering and tax evasion are separate and distinct offenses. In fact, the two processes actually have opposite effects on money. Money laundering is an attempt to hide the origin of illicit proceeds in order to make them appear legitimate, basi-

well's use of a Bermuda corporation and bank account as part of his tax evasion scheme was uncovered through requests made under our TIEA with Bermuda.").

39. Australian Instit. of Crim., *Anti-Money Laundering Symposium* (2002), <http://www.aic.gov.au/conferences/2002-ml/index.html>.

40. *Id.*; IRS Overview: Money Laundering, *supra* note 1.

41. IRS Overview: Money Laundering, *supra* note 1.

42. *Id.*

43. UNODC, *Report*, *supra* note 16.

44. *Id.*

cally turning “dirty” money into “clean” money,⁴⁵ whereas tax evasion involves hiding the profits from initially legal transactions, turning “clean” money “dirty.”⁴⁶ Yet there is a distinct similarity between the methods used for money laundering and the commission of tax offenses.⁴⁷ Both require dishonesty and concealment, and when money from illegal activity is shielded from tax officials, there is a direct overlap between the two.⁴⁸ Once money evades taxes, it needs to be laundered before it can be used again.⁴⁹ In the IRS’s view, “[m]oney laundering is in effect tax evasion in progress.”⁵⁰ As a result, almost all laundered money has evaded taxes and is therefore unlawful, irrespective of its legal or illegal origin.⁵¹

The money laundering process has three separate phases: placement, layering, and integration, also known as “wash, dry and fold.”⁵² The first stage, placement, occurs when illicit funds are introduced into banking and financial systems, the primary goal of which is to remove the illicit funds from direct association with the precedent criminal activity.⁵³ Oth-

45. For a statutory definition of “money laundering,” see 18 U.S.C.A. § 1956(a)(1)(B)(i) (West 2008).

46. Dean, *supra* note 3.

47. Organisation for Economic Co-operation and Development, Money Laundering and Tax Crimes, http://www.oecd.org/document/48/0,3343,en_2649_33751_2499879_1_1_1_1,00.html (last visited Dec. 28, 2008).

48. Donato Masciandaro & Julian Alworth, *Tax Evasion, Tax Competition, Lax Financial Regulation and Money Laundering: Is There An Overlap?* (Univ. of Bocconi Soc. Sci. Research Network, Sept. 2003), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=444540#PaperDownload.

49. For example, if a person receives \$1000 for work and is liable to pay a forty percent marginal rate of income tax on it and fails to declare the income, then \$400 is considered as being stolen from the Treasury. Therefore, he does not launder the \$1000, he launders the \$400, i.e., the tax-evaded money is laundered. The complication that makes this difficult to understand is that in order to retain the \$400, he puts the whole amount of \$1000 through the laundering process. He has to show that he received \$1000 legitimately in order to evade a payment of \$400. Banerjee, *supra* note 27 (for purposes of this Note, £ has been substituted by USD).

50. IRS Overview: Money Laundering, *supra* note 1.

51. Vaknin, *supra* note 6.

52. Karen Dearn, *Cracking Down on Cash Cleaners*, June 26, 2007, <http://www.australianit.news.com.au/story/0,24897,21952515-24169,00.html>. For an example of the three-stage process in the Panamanian context, see Layton, *supra* note 5 (recounting the story of Harvard-educated economist Franklin Jurado, who went to prison in 1996 for cleaning \$36 million for Colombian drug lord Jose Santacruz-Londono).

53. UNODC, Money Laundering—Process, http://www.unodc.un.or.th/money_laundering/ [hereinafter UNODC, Laundering Process] (last visited Jan. 22, 2009). See also NMLS 2007, *supra* note 24, at intro., v. (describing various known money laundering

erwise, criminals would not be able to use the money because it would connect them to the initial crime.⁵⁴ The second stage, layering, is more complex and attempts to further remove the connection between the funds and the original illegal activity.⁵⁵ It usually involves multiple transactions among various financial institutions, accounts, and jurisdictions.⁵⁶ The purpose is to leave a trail that is almost impossible to trace back to its origin, and if successful, the criminal evades pursuit.⁵⁷ The final stage is integration. At this point in the process, the originally illicit funds are reintroduced or assimilated into the economy as seemingly legitimate funds or investments.⁵⁸

The banking system remains an attractive location for money launderers, because the system is susceptible to manipulation.⁵⁹ Furthermore, because of the confidential financial instruments and strict bank secrecy regimes present in most offshore tax havens, including Panama, banks in those jurisdictions are involved in most money laundering schemes.⁶⁰ Moreover, as Panama functions under a U.S. dollar economy, U.S. tax evaders and money launderers are drawn to the jurisdiction because capital can easily flow into the country without currency-exchange controls or restrictions.⁶¹ Once illegal money is successfully placed, or deposited,

methods such as trade-based money laundering, bulk cash smuggling, and the Black Market Peso exchange).

54. Layton, *supra* note 5.

55. UNODC, *Laundering Process*, *supra* note 53.

56. *See* Komisar, *supra* note 2 (“Often someone will use a shell company in one jurisdiction that owns a shell in another jurisdiction that owns a bank account in a third. That [is] called layering. No one can follow the paper trail.”); Layton, *supra* note 5 (“Layering may consist of several bank-to-bank transfers, wire transfers between different accounts in different names in different countries, making deposits and withdrawals to continually vary the amount of money in the accounts, changing the money’s currency, and purchasing high-value items . . . to change the form of the money. This is the most complex step in any laundering scheme, and it [is] all about making the original dirty money as hard to trace as possible.”). *See also* UNODC, *Laundering Process*, *supra* note 53 (stating that the layering stage “is the most international in nature”).

57. U.N. OFFICE ON DRUGS & CRIME, ANNUAL REPORT 80 (2005), *available at* http://www.unodc.org/pdf/annual_report_2005/keyactivities.pdf.

58. UNODC, *Laundering Process*, *supra* note 53.

59. NMLS 2007, *supra* note 24, at v. (stating that this was a key finding of the U.S. Money Laundering Assessment).

60. UNODC, *Report*, *supra* note 16. *See also* IRS, A Look Behind IRS Anti-Money Laundering Programs, <http://www.irs.gov/compliance/enforcement/article/0,,id=124069,00.html> (last visited Dec. 28, 2008) (“Each year billions of untaxed dollars are laundered through banks . . . in an effort to make the money appear legitimate *or to evade taxes.*”) (emphasis added).

61. U.S. CONG., OFFICE OF TECH. ASSESSMENT, *supra* note 3, at 10; INCSR vol. 2, *supra* note 20, at 317.

in an offshore haven bank account, it is easily “layered” through various financial transactions and other tax haven jurisdictions.⁶² The combination of anonymity and secrecy provides a “tool kit” for money launderers⁶³ and gives transactions in those jurisdictions a “cloak of confidentiality.”⁶⁴ Once dirty money has been effectively “cleaned” offshore, banks provide the primary gateway for the money to re-enter the United States.⁶⁵

Panama remains one of the best jurisdictions for financial anonymity.⁶⁶ The U.S. State Department has listed Panama as a “country of primary concern” for money laundering because of the confidentiality and information protection it provides.⁶⁷ Anonymity can be accomplished by several means with varying degrees of secrecy and complexity, from the simple use of a Panamanian debit or credit card account,⁶⁸ to the opera-

62. NMLS 2007, *supra* note 24, at 27. See also John L. Evans, *International Money Laundering: Enforcement Challenges and Opportunities*, 3 SW. J. L. & TRADE AM. 1 (1996) (“Once the proceeds of crime are successfully deposited in the financial system many laundering operators take the precaution of moving money, not just offshore, but through more than one tax haven and through a maze of shell companies and respectable nominees.”).

63. UNODC, *Report*, *supra* note 16.

64. Spencer, *supra* note 15, at 89.

65. NMLS 2007, *supra* note 24, at v. (stating this was a key finding of the U.S. Money Laundering Assessment). See also Vaknin, *supra* note 6 (“It is important to realize that money laundering takes place within the banking system. Big amounts of cash are spread among numerous accounts, (sometimes in free economic zones, financial off shore centers, and tax havens), converted to bearer financial instruments (money orders, bonds), or placed with trusts and charities. The money is then transferred to other locations, sometimes as bogus payments for ‘goods and services’ against fake or inflated invoices issued by holding companies owned by lawyers or accountants on behalf of unnamed beneficiaries. The transferred funds are re-assembled in their destination and often ‘shipped’ back to the point of origin under a new identity. The laundered funds are then invested in the legitimate economy. It is a simple procedure—yet an effective one. It results in either no paper trail—or too much of it. The accounts are invariably liquidated and all traces erased.”)

66. Complete Offshore Privacy and Anonymity in Panama, <http://www.offshorelegal.org/asset-protection/panama-offshore-asset-protection/complete-offshore-privacy-and-anonymity-in-panama.html> [hereinafter Complete Offshore Privacy] (last visited Feb. 3, 2009).

67. For a complete index of “vulnerability factors” used to list countries, see INCSR vol. 2, *supra* note 20, at 41.

68. See Robert L. Sommers, *Tax Amnesty for Offshore Accounts: The Program and Results*, May 2003, http://www.taxprophet.com/hot_topic/May03.shtml (“Typically, taxpayers deposit funds in foreign ‘tax-haven’ banks and then access their funds with debit or credit cards issued by the banks. The taxpayer’s identity is protected under secrecy laws in the tax haven jurisdiction, so the IRS cannot compel the offshore banks to divulge this information.”). See also Complete Offshore Privacy, *supra* note 66 (describing how a

tion of bearer shares and shell corporations in conjunction with nominee directors.⁶⁹ Both individuals and corporations may use these financial tools,⁷⁰ and the more complex the financial arrangements are, the more secret (hidden) the information becomes.⁷¹ The origin of any illicit money, becomes even more difficult to identify once the money is placed in a Panamanian bank account and “layered” through subsequent bank transfers and commingled with legitimate money.⁷² The laundered funds are then generally reintroduced to the U.S. market through bank wire transfers using “correspondent” and “payable through” accounts, which can further protect against detection.⁷³

taxpayer can purchase anonymous prepaid cards that cannot be traced because they are purchased with cash).

69. Int'l Ctr. for Political Violence and Terrorism Research, *Old Laundering Methods Hold Fast*, Mar. 2007, at 3, [http://pvtr.org/pdf/Financial-Response/BulkCash-Trade\(ICP VTR\).pdf](http://pvtr.org/pdf/Financial-Response/BulkCash-Trade(ICP VTR).pdf). See also NMLS 2007, *supra* note 24, at 63 (describing “Bearer Shares” as a financial device that permits ownership to be attributed to the person in *possession* of the shares, rather than the true beneficial owner of the corporation and provides for a “high level of anonymity”) (emphasis added); IRS, Abusive Offshore Tax Avoidance Schemes—Glossary of Offshore Terms, <http://www.irs.gov/businesses/small/article/0,,id=106572,00.html> [hereinafter IRS Glossary of Offshore Terms] (A “beneficial owner” is defined as “the true owner of an entity, asset, or transaction as opposed to any stated ownership provided in documents or oral representations. The beneficial owner is the one that receives or has the right to receive proceeds or other advantages as a result of the ownership.”); NMLS 2007, *supra* note 24, at 63 (“Shell Corporations generally have no employees or physical assets and are nothing more than a mailing address.”). See also Elizabeth MacDonald, *Shell Games: With No Federal Oversight, the States are Helping to Shelter Crooks, Money Launderers and, Possibly, Terrorists*, FORBES.COM, Feb. 12, 2007, <http://www.forbes.com/forbes/2007/0212/096.html> (noting that generally, shell corporations are being increasingly associated with criminal activity); IRS Glossary of Offshore Terms, *supra* (Furthermore, to preserve the anonymity of true beneficial owners of such corporations, “nominee directors” are employed to “provide a veil of secrecy as to the beneficial owner’s involvement.”).

70. Focus Publications, S.A., *Focus Panama*, <http://www.focuspublicationsint.com/focuspanama/en/company-law.htm> (last visited Dec. 30, 2008).

71. IRS Glossary of Offshore Terms, *supra* note 69.

72. U.S. CONG., OFFICE OF TECH. ASSESSMENT, *supra* note 3, at 9.

73. USA PATRIOT Act, H.R. 3162, 107th Cong. § 312 (2001) [hereinafter USA PATRIOT Act] (defining a “correspondent account” as “any account established for a foreign financial institution to receive deposits from, or to make payments or other disbursements on behalf of, the foreign financial institution [in the United States]”). See also *id.*; NMLS 2007, *supra* note 24, at 21–22, app. A; (An example of a “payable through” account is one where a foreign bank maintains a checking account at a U.S. bank. “The foreign bank could then issue checks to its customers, allowing them to write checks on the U.S. account. A foreign bank may have several hundred customers writing checks on one ‘payable through account’”); Buchanan, Ingersoll & Rooney P.C., *Potential Tax Implications of the Enhanced Money Laundering Provision of H.R. 3162*, 2001, <http://www.buchananingersoll.com/news.php?NewsID=1251> (“The term ‘payable-

Yet, Panama's most important asset protection mechanism remains its financial privacy laws; more specifically, its bank secrecy laws.⁷⁴ Although the financial instruments for hiding identities, origins of money, and bank transactions can be effective in evading the scrutiny of tax or law enforcement officials, they do not alone grant absolute anonymity or secrecy.⁷⁵ Regardless of subsequent attempts to layer, or hide, the origin of funds, in order to make use of Panama's banking system, one must initially provide his or her identification to the bank he or she wishes to use.⁷⁶ Generally, U.S. tax officials have the expertise to trace illicit money to its source, even if the "trail" is complicated and purposely confused.⁷⁷ However, what Panama's secrecy laws provide is, in effect, a barrier to U.S. tax officials following the financial trail back into Panama.⁷⁸

Under Panamanian Decree-Law No.9 of February 26, 1998, Panama established the "Superintendency of Banks" in order to "oversee the preservation of the soundness and efficiency of the banking system" and "[t]o punish violations."⁷⁹ The Superintendent of Banks can inquire, retrieve, and record any financial information he or she deems important in upholding the integrity of the Panamanian banking system.⁸⁰ Further-

through' account is defined as an account through which a foreign financial institution permits its customers to engage, either directly or through a sub-account, in usual banking business activities. A 'correspondent' account is defined as an account established to receive deposits from, make payments on behalf of, or permit financial transactions to be executed with respect to a foreign financial institution.").

74. Mark Nestmann, *Where Your Financial Secrets Remain Secret*, Apr. 6, 2007, <http://www.sovereignsociety.com/offshore2081.html>. See also OffshoreLegal.org, *Panama Offshore Legal Services*, <http://www.offshorelegal.org/panama-bank-secrecy-laws.html> (last visited Jan. 3, 2009); Panamalaw.org, *Panama Bank Secrecy Laws*, http://www.panamalaw.org/panama_bank_secrecy.html (last visited Jan. 3, 2009).

75. Ronald Edwards, *Panama Anonymous Bearer Share Corporations*, Nov. 13, 2006, <http://www.goinglegal.com/article9864986.html> ("A bank anywhere in the civilized world will require a beneficial owner for any bank account and will also require identity documents for that person so the bearer share corporation may not be able to conduct banking matters completely anonymously.").

76. See ANTI-MONEY LAUNDERING: INTERNATIONAL LAW AND PRACTICE 146, 147 (Wouter H. Muller, Christian H. Kälin & John G. Goldsworth eds., 2007) (describing Panama Agreement No. 9-2000 of the Superintendency of Banks of October 23, 2000 [Prevention of Unlawful Use of Banking Services]).

77. IRS Overview: Money Laundering, *supra* note 1.

78. See MacDonald, *supra* note 69. ("[W]ithout such [private corporate ownership and bank account] information the police come to a dead end.").

79. See Law No. 9 (1998) (Pan.), art. 5 (Functions of the Superintendency of Banks); *id.* art. 84 (Information Regarding Bank's Clients) (Superintendencia de Bancos trans.).

80. *Id.*

more, all banks are obligated to maintain due diligence⁸¹ and care in dealing with clients or potential clients,⁸² and must release any information requested by the superintendent to that office.⁸³ However, the secrecy laws currently in place act as “blocking statutes” and create a legal regime against the disclosure of that financial information to any authorities outside the country.⁸⁴

The term “bank secrecy” does not address the privacy of a bank’s own activities, but rather those of the bank’s patrons.⁸⁵ A duty of discretion regarding disclosure of patrons’ information binds all bank employees, representatives of the bank, and government officials who are in any way involved with banking.⁸⁶ Panama’s bank secrecy laws are predominantly regulated by Articles 84, 85, and 86 of the Banking Act of 1998.⁸⁷ Article 84 of the statute prohibits the Superintendency of Banks to reveal to a third party, such as a U.S. tax official, any information obtained from bank records, acquired through any inquiry or investigation.⁸⁸ The requirement for confidentiality extends to any staff members, external auditors, or experts who may be employed or utilized by the superintendent’s office.⁸⁹ Article 85 forbids Panamanian banks from disclosing

81. BLACK’S LAW DICTIONARY, *supra* note 14, at 203 (defining “due diligence” as “such a measure of prudence, activity or assiduity, as is properly to be expected from, and ordinarily exercised by, a reasonable and prudent man”).

82. Law No. 42 (2000) (Pan.) (The law provides in pertinent part, “The persons, natural or juridical, here mentioned, are under the following obligation: to adequately identify their clients. To that effect they shall require from their customers all due references or recommendations, as well as the corresponding certifications that attest the incorporation and effectiveness of societies, and also the identification of officials, directors, proxies and legal representatives of those societies, in a manner that enables them to adequately document and determine the real owner or direct or indirect beneficiary.”).

83. *Id.* art. 2.

84. RESTATEMENT (THIRD) OF FOREIGN RELATIONS LAW OF THE UNITED STATES § 442 rpts. n.4 (1987) (“Blocking statutes are designed to take advantage of the foreign government compulsion defense, § 441, by prohibiting the disclosure, copying, inspection, or removal of documents located in the territory of the enacting state in compliance with orders of foreign authorities. Some statutes cover all documents, some only certain categories. . . . All blocking statutes appear to carry some penal sanction.”).

85. Rolf H. Weber, *Swiss Banking Secrecy in Evolution*, 18 BANKING & FIN. L. REV. 317, 318 (2003).

86. *Id.*

87. Shirley & Associates, *Panama Bank Secrecy*, <http://www.shirleylaw.com/en/re-sources/bank-secrecy.htm> (last visited Jan 3, 2009).

88. Law No. 9 (1998) (Pan.), art. 84 (Information Regarding Bank’s Clients, reaffirmed in Pan. G.R. S.B. No. 02-2002 (Norms That Impose Restrictions on the Use of Available Information)).

89. *Id.* art. 84.

their client's identity or transactions, absent the client's consent,⁹⁰ while Article 86 proscribes penalties of up to \$100,000, in addition to any other "civil or criminal sanctions that may apply" for violating the provisions of the statute.⁹¹ Additional penalties can include imprisonment of up to six months for certain violations.⁹²

In addition, the attorney-client privilege supplies a final layer of security.⁹³ By law, the use of a licensed Panamanian attorney is required to establish a corporation, and the attorney is bound to maintain his or her client's confidentiality.⁹⁴ The attorney-client privilege bars the release of all information relating to the client's personal affairs, as well as any financial dealings or transactions.⁹⁵ Therefore, because it is a lawyer who initiates a corporation, and in many circumstances, sets up its bank account and provides the required nominee directors, a tax evader using such an arrangement is practically shielded from all tax scrutiny.⁹⁶

As if these formidable obstacles to a foreign government's intrusion were not sufficient, recently, Panama sought to further fortify its privacy protection by proposing amendments to Articles 187 and 188-A of its Criminal Code.⁹⁷ The amendments include imprisonment for simply publishing information regarding a third party without that party's express permission, or for even inquiring into a third party's personal affairs without official state authorization.⁹⁸ Although these laws were initially implemented to protect the privacy of public officials from the media,

90. *Id.* art. 85 (Confidentiality of Banks).

91. *Id.* art. 86 (Penalties).

92. *Foundations and Trusts*, 2008 PANAMA L. DIG. § 2.06 (stating that under Panama Law No. 25 of June 12, 1995, art. 35, violations of the secrecy and confidentiality provisions of this law "shall be punished with imprisonment for six months and [a] fine of U.S. \$50,000").

93. Sullivan, *supra* note 30.

94. *Corporations: Incorporation*, 2008 PANAMA L. DIG. § 2.03 [hereinafter LAW DIGEST, *Corporations*] (Under Panama Decree 147 of May, 1966, art. 1, a Panamanian corporation's registered agent must be an attorney admitted to practice in Panama, and such agents are under a duty to know their clients and maintain proper information about their clients. However, such information is only disclosed upon petition filed by the Public Prosecutor or member of a judicial organ, relating to narcotics trafficking or "of money laundering arising therefrom.").

95. Ronald Edwards, *Why Use a Law Firm?*, Nov. 17, 2006, http://www.goinglegal.com/article_97775_86.html.

96. Sullivan, *supra* note 30.

97. Press Release, Article 19, Panama: Proposed Criminal Code Severely Restricts Freedom of Expression and Information (Feb. 22, 2007) ("Article 19 is an independent human rights organization that works globally to protect and promote the right to freedom of expression.").

98. *Id.*

anyone wishing to protect his or her privacy can hide behind this legislation.⁹⁹

Nevertheless, the constraints on disclosure are not unrestricted. There remain limited situations where privileged information can and is turned over to Panamanian authorities.¹⁰⁰ Panama's main bank secrecy laws have provisions that allow for the disclosure of information to third parties if requested "within the course of criminal proceedings,"¹⁰¹ and this exception extends to the attorney-client privilege as well.¹⁰² However, information the Superintendency of Banks receives or records is not authorized to be disclosed to U.S. authorities, unless that information can be proven to be specifically related to laundering proceeds from the drug trade or other serious crimes.¹⁰³ Tax-related misconduct is only a civil matter in Panama, and therefore does not rise to the level of an exception to the restriction on disclosure of information to third parties.¹⁰⁴ For an American tax evader whose only illegal act is to have hidden his or her profits from U.S. tax officials, this legal system provides maximum protection with little cause for fear of prosecution.

In addition, the Panamanian tax code allows for certain foreign investors to be exempt from paying any income taxes at all.¹⁰⁵ These exempt foreign investors tend to be those who implement the types of financial mechanisms mentioned earlier in order to execute the types of transactions required for tax exemption status.¹⁰⁶ Therefore, because these taxpayers are not required to pay taxes to Panama, they cannot be guilty of any Panamanian tax offense, irrespective of whether such violations are treated as civil or criminal matters. There can be no crime of money laundering if the funds allegedly laundered are legal on all levels in Panama.

The dual criminality principle¹⁰⁷ is a significant restriction to U.S. tax officials seeking to prosecute tax cheats for money laundering or tax eva-

99. *Id.*

100. Law No. 9 (1998) (Pan.), arts. 84–85.

101. *Id.*

102. LAW DIGEST, *Corporations*, *supra* note 94.

103. Law No. 41 (2000) (Pan.), art. 389 (Capital Laundering).

104. Panamalaw.org, *supra* note 31. *See also* Banerjee, *supra* note 27.

105. Fiscal Code (1956) (Pan.) (Taxation).

106. Offshorelegal.com, *Tax Implications of Banking in Panama*, <http://www.offshorelegal.org/offshore-banking/panama-offshore-banking/tax-implications-of-banking-in-panama.html> (last visited Jan. 3, 2009). *See also* AssetProtectionCorp.com, *Panamanian Trusts*, <http://www.assetprotectioncorp.com/panamatrusts.html> (last visited Jan. 3, 2009).

107. For a discussion on dual criminality, see *supra* Intro.

sion.¹⁰⁸ Because Panama adheres to the dual criminality principle, without a tax treaty in place to compel the government to release requested financial information, tax officials must pursue the information via the long and cumbersome process compelling disclosure through the judicial process.¹⁰⁹ A U.S. agency must either secure a federal court order, or a “letter rogatory,”¹¹⁰ to compel a foreign jurisdiction to provide requested information. Although foreign courts generally honor such inquiries,¹¹¹ because a request of judicial assistance is based on the principle of “comity”¹¹² between countries, Panama is not obligated to comply with such requests.¹¹³ In fact, compliance with a letter rogatory for information in purely financial matters is a rare event in Panama.¹¹⁴ Even putting the issue of comity aside, the slow process of compelling information from a foreign government can hinder a U.S. agency’s investigation of suspected tax evasion.¹¹⁵ While the process drags on, tax evaders can continue to layer and hide their money, making it very difficult for authorities to detect the funds once, or if, a request is honored.¹¹⁶ The U.S. State Department has acknowledged the deficiency; because “letters rogatory are a time consuming cumbersome process,” it recommends that they only be used as a last resort, when “there are no other options availa-

108. For an example of how a lack of dual criminality would require a country to acquiesce to demands for information from another country, see *Daily E-Mail Alert No. 1,425*, Aug. 4, 2006, TECH L.J., <http://www.techlawjournal.com/alert/2006/08/04.asp>.

109. Dep’t of St., Bureau of Consumer Affairs, *Preparation of Letters Rogatory*, http://travel.state.gov/law/info/judicial/judicial_683.html [hereinafter DOSBCA, *Letters Rogatory*] (last visited Jan. 3, 2009).

110. *Id.* (“A letter rogatory is a formal request from a court in one country to ‘the appropriate judicial authorities’ in another country requesting compulsion of testimony or documentary or other evidence. . . . In some countries which do not permit the taking of depositions of willing witnesses, letters rogatory are the only method of obtaining evidence.”).

111. Edward Ord, *The Internal Revenue Service Abroad*, in SUMMARY OF THE CANNES MEETING: MAY 26–27, 1988 (Milton Grundy prep., 1988).

112. RESTATEMENT (THIRD) OF FOREIGN RELATIONS LAW OF THE UNITED STATES, § 101 cmt. e (quoting *Hilton v. Guyot*, 159 U.S. 113, 163–64 (1895)) (“Comity, in the legal sense, is neither a matter of absolute obligation, on the one hand, nor of mere courtesy and good will, upon the other. But it is the recognition which one nation allows within its territory to the legislative, executive or judicial acts of another nation, having due regard both to international duty and convenience and to the rights of its own citizens or of other persons who are under the protection of its laws.”).

113. JODY R. WESTBY, INTERNATIONAL GUIDE TO COMBATING CYBERCRIME 45 (2003).

114. Sullivan, *supra* note 30.

115. UNODC, *Report*, *supra* note 16. See also Edmund L. Andrews, *I.R.S. Curtails Many Audits in Tax Havens*, N.Y. TIMES, May 3, 2007.

116. UNDOC, *Report*, *supra* note 16.

ble.”¹¹⁷ Without a current TIEA, this burdensome process is the method that must be used to investigate tax evasion. This being the case, IRS officials are abandoning audits of off-shore accounts, and in some cases, not even starting an investigation.¹¹⁸

It is clear that “significant restrictions on access to bank information for tax purposes remain in . . . Panama.”¹¹⁹ The Organization for Economic Cooperation and Development (“OECD”) states that a “[l]ack of transparency and a failure to co-operate internationally create conditions [in Panama] that can be exploited by dishonest taxpayers to evade their tax obligations.”¹²⁰ Unless tax officials can “tease the information they need out of bank records,” their law enforcement efforts “come to a dead end.”¹²¹ To demonstrate the importance of being able to follow the money trail back to Panama, both Saddam Hussein and Osama bin Laden used money laundering schemes that implemented Panamanian shell corporations and bank accounts to help fund their respective Iraqi and al-Qaeda military operations.¹²²

II. U.S. MEASURES TO COMBAT MONEY LAUNDERING AND THEIR INEFFECTIVENESS IN DEALING WITH TAX EVASION

In 1970, the U.S. Congress enacted the Bank Secrecy Act (“BSA”), acknowledging that U.S. banks were being used to hide money from criminal activity and tax evasion.¹²³ The Bank Secrecy Act does not shield or hide financial information. Rather, its regulations create a financial transparency in the banking industry that allows law enforcement and other agencies to track the laundering of evaded taxes and other criminal activities.¹²⁴ Although the BSA itself does not criminalize mon-

117. DOSBCA, *Letters Rogatory*, *supra* note 110.

118. Andrews, *supra* note 115.

119. OECD, *OECD Reports Progress in Fighting Offshore Tax Evasion, But Says More Efforts Are Needed*, Oct. 10, 2007, http://www.oecd.org/document/48/0,3343,en_2649_201185_39482288_1_1_1_1,00.html.

120. *Id.*

121. MacDonald, *supra* note 69.

122. Lucy Komisar, *Saddam's Secret Money-Laundering Trail*, June 2, 2004, <http://the.komisarscoop.com/2004/06/02/saddams-secret-money-laundering-trail/>.

123. Federal Deposit Insurance Corporation, *Bank Secrecy Act and Anti-Money Laundering: Combating Money Laundering*, http://www.fdic.gov/regulations/examinations/bsa/bsa_2.html (last visited Jan. 3, 2009). For a statutory definition of tax evasion, see 26 I.R.C. §§ 7201, 7206 (2000).

124. James H. Freis, Jr., Financial Crimes Enforcement Network Dir., Remarks to the PAN-Am. Congress on Asset Laundering and Fin. Terrorism Prevention and Control (July 27, 2007) [hereinafter Freis, Jr., FinCEN Dir. Remarks]. See Cynthia A. Glassman, SEC Comm’r, Opening Remarks Before the Symposium on Enhancing Fin. Transparency

ey laundering, it requires financial institutions to maintain records for certain transactions, effectively creating a “paper trail” that is used to prosecute such cases.¹²⁵ Money laundering was not criminalized in the United States until the 1986 enactment of the Money Laundering Control Act,¹²⁶ which recognizes tax evasion as a predicate offense.¹²⁷ Yet, the BSA remains the essential anti-money laundering regulatory system for U.S. law enforcement agencies¹²⁸ and is administered by the Financial Crimes Enforcement Network (“FinCEN”), the Financial Intelligence Division of the U.S. Treasury Department.¹²⁹

FinCEN has also acknowledged that financial crimes extend beyond U.S. borders and broadened its intelligence network to include international anti-money laundering support.¹³⁰ FinCEN now assists other countries in improving their efforts to combat financial crimes,¹³¹ with the agency’s Office of International Programs being its second largest department behind the domestic component.¹³² International law enforcement agencies rely on information obtained through the BSA’s reporting requirements to detect global money laundering schemes.¹³³ FinCEN freely shares this information with the goal of using international efforts to ultimately protect the U.S. financial system from such financial crimes.¹³⁴

After the September 11th attacks on the World Trade Center and the Pentagon in 2001, Congress passed the “Uniting and Strengthening

(June 4, 2002) (defining “financial transparency” as “timely, meaningful and reliable disclosures about a company’s financial performance”).

125. Bauer & Ullmann, *supra* note 36. *See also* Cook & Company, Bank Secrecy Act of 1970 (BSA), http://www.cookco.us/financial/bank_secrets_act.htm (last visited Jan. 14, 2009) (requiring all financial institutions to submit five currency and monetary instrument reports: the Currency Transaction Report, Currency and Monetary Instrument Reports, Foreign Bank Account Records, Suspicious Activity Reporting System, and FinCEN Form 110).

126. Money Laundering Control Act, 18 U.S.C.A. § 1956(a)(1)(A)(ii) (West 2008).

127. *Id.*

128. Freis, Jr., FinCEN Dir. Remarks, *supra* note 125.

129. INCSR vol. 2, *supra* note 20, at 15.

130. Press Release, James E. Johnson, Treas. Assistant Sec’y, Office of Pub. Affairs, House Banking & Fin. Serv. Subcomm. on Gen. Oversight & Investigations (Apr. 1, 1998) [hereinafter Johnson Treas. Assistant Sec’y Press Release].

131. INCSR vol. 2, *supra* note 20, at 15.

132. Norman J. Rabkin, Dir., Admin. of Justice Issues, Statements Before the Subcomm. on Gen. Oversight & Investigations, Comm. on Banking & Fin. Services, House of Representatives (Apr. 1, 1998).

133. IRS, Bank Secrecy Act, <http://www.irs.gov/businesses/small/article/0,,id=152532,00.html> (last visited Jan. 3, 2009).

134. Freis, Jr. FinCEN Dir. Remarks, *supra* note 125.

America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001,” the Patriot Act.¹³⁵ Title III of the Act specifically addresses money laundering¹³⁶ and presents amendments to the Bank Secrecy Act.¹³⁷ The amendments generally increase the level of specificity required of financial institutions in the gathering and reporting of their information.¹³⁸ The most recent amendment is FinCEN’s final rule for § 312 of the Patriot Act, which went into effect September 10, 2007, and increases the level of due diligence required by U.S. banks when transacting with certain foreign accounts.¹³⁹

However, what both the BSA’s and the Patriot Act’s requirements for self-regulation have done is essentially transform civilian bank employees into law enforcement agents with the responsibility of monitoring and maintaining specific financial information.¹⁴⁰ Complications can arise when individuals in the private sector do not have the same level of interest in meticulously maintaining the due diligence that the statutes require or that law enforcement intended.¹⁴¹ The effectiveness of the statutes in producing an essential “money trail” for the prosecution of tax evasion and other financial crimes can be undermined by those in the industry whose primary interest is financial performance, not prosecutorial assistance.¹⁴² Although the BSA is considered an integral part of protecting the American financial system from the movement of illicit funds, and a majority of the private sector have complied with its requisites in good faith, clear failures to conform, and even straightforward decisions not to comply, with the statute demonstrate the pitfalls of pri-

135. USA PATRIOT Act, *supra* note 73.

136. *Id.*

137. See 31 C.F.R. § 103 (providing updated regulations relating to money and finance).

138. U.S. Commodities Futures Trad. Comm., Anti-Money Laundering and Terrorist Financing, <http://www.cftc.gov/industryoversight/antimoneylaundering/index.htm> (last visited Jan. 3, 2009).

139. FDIC, Fin. Inst. Letter, USA Patriot Act, Final Regulation Implementing Section 312—Special Due Diligence Programs for Certain Foreign Accounts (Dec. 21, 2007). See 31 U.S.C.A. 5318(i)(2)(A)(i)–(ii) (West 2008) (describing three specific types of foreign bank accounts to which the rules apply, more specifically, those banks operating under an offshore banking license, a license issued by a country designated as being non-cooperative with international anti-money laundering principles, or a license issued by a country designated by the Secretary of the Treasury as warranting special measures due to money laundering concerns).

140. Vaknin, *supra* note 6.

141. Mark Pieth, *Multi-Stakeholder Initiatives to Combat Money Laundering and Bribery*, in LAW AND LEGALIZATION IN TRANSNATIONAL RELATIONS 95 (Christian Brüttsch & Dirk Lehmkuhl eds., 2007).

142. *Id.*

vate self-regulation.¹⁴³ Two current examples are Bank of America being fined \$3 million in January 2007 for “fail[ure] to comply with anti-money laundering rules relating to ‘high risk’ accounts,”¹⁴⁴ and American Express agreeing to pay \$65 million for similar BSA violations.¹⁴⁵

These lapses fundamentally defeat the purpose of any anti-money laundering legislation and demonstrate a weakness in the system. However, “the continued safeguarding of the [U.S.] banking system” from the threat of money laundering remains the U.S. government’s primary goal.¹⁴⁶ The 2007 National Money Laundering Strategy identifies areas vulnerable to money laundering for the purpose of adjusting and strengthening current federal laws in the area.¹⁴⁷ Yet, even with full and proper compliance with current or improved statutory regulations on the part of all participants in the banking industry, the requirements for the collection of information do not extend into Panama. FinCEN’s increased international effort to combat money laundering and the heightened reporting conditions put in place after September 11th do not overcome the BSA’s limitations in appropriating information from Panamanian financial institutions or officials. As discussed above, although Panamanian officials collect financial information as per their anti-money laundering regulations, this information cannot be exchanged with U.S. officials unless the United States can demonstrate that such information is directly related to a criminal investigation.¹⁴⁸ Notwithstanding the U.S. government’s increased ability under the Patriot Act to requisition documents from foreign banks,¹⁴⁹ Panama’s dual criminality requirement effectively

143. Zarate Remarks to the Florida Bankers Ass’n, *supra* note 7. For further commentary on the subject of self-regulation, see Christian Brüttsch & Dirk Lehmkuhl, *Introduction*, in *LAW AND LEGALIZATION IN TRANSNATIONAL RELATIONS*, *supra* note 141, at 1, 1–8.

144. Jonathan Stempel, *Bank of America Unit Fined over Money Laundering*, MONEYNEWS.COM, Jan. 29, 2007, <http://archive.moneynews.com/money/archives/articles/2007/1/29/114547.cfm>.

145. John Poirier, *American Express Fined \$65 Million over Money Laundering*, REUTERS, Aug. 7, 2007, <http://www.reuters.com/article/businessNews/idUSN0644580020070807>.

146. McGlasson, *supra* note 1.

147. FDIC, Fin. Inst. Letter, Bank Secrecy Act: 2007 National Money Laundering Strategy (May 23, 2007).

148. See discussion *supra* Part I.

149. See 31 U.S.C.A. § 5318(k)(3)(A)(i) (West 2008) (“In general, the Secretary of the Treasury or the Attorney General may issue a summons or subpoena to any foreign bank that maintains a correspondent account in the United States and request records related to such correspondent account, including records maintained outside of the United States relating to the deposit of funds into the foreign bank.”).

negates any legislatively expanded authority and allows evaded taxes to be shielded from U.S. agency inquiries.

Internationally, the United States combats money laundering through the Financial Action Task Force ("FATF"), a thirty-three member organization established in 1989 by the G-7 Summit in Paris, whose primary focus is on promoting anti-money laundering policies.¹⁵⁰ The United States, through FinCEN, was an essential part in the FATF's development and aided the agency in its initial policy considerations.¹⁵¹ Although Panama is not one of the FATF's thirty-three members, it is a member of the Caribbean Financial Action Task Force ("CFATF").¹⁵² The CFATF was established in 1992 and is one of many "FATF-style regional bodies, which, in conjunction with the FATF, constitute an affiliated global network to combat money laundering and the financing of terrorism."¹⁵³ These task forces were implemented as a way to get around the burdensome process of using letters rogatory to compel foreign jurisdictions to provide information.¹⁵⁴

To facilitate the exchange of information, two of the FATF's most significant recommendations were that countries criminalize money laundering beyond drug-related offenses and that banks report suspicious transactions to domestic authorities.¹⁵⁵ Although Panama has complied with both proposals, it has not extended its list of predicate offenses to include tax-evasion¹⁵⁶ or made any specific references to tax matters in its Suspicious Activity Reporting Agreement.¹⁵⁷ Therefore, Panama's dual criminality constraint hinders the FATF's power to obtain informa-

150. IMF Factsheet, *supra* note 7.

151. Johnson Treas. Assistant Sec'y Press Release, *supra* note 130.

152. INCSR vol. 2, *supra* note 20, at 33.

153. *Id.*

154. Pieth, *supra* note 142, at 81 ("[T]he traditional instruments of international law are frequently considered too cumbersome and slow. Increasingly, international law is created by unconventional means: 'task forces' prove to be far more expedient . . .").

155. U.S. CONG., OFFICE OF TECH. ASSESSMENT, *supra* note 3, at 113. For a complete list and description of the FATF's Forty Recommendations, see also the Financial Action Task Force, <http://www.fatf-gafi.org> (then follow "40 Recommendations" hyperlink) (providing "a complete set of counter-measures against money laundering").

156. See Law No. 41 (2000) (Pan.), art. 389 (amending the Penal code to expand the predicate offenses for money laundering beyond narcotics trafficking to include "qualified embezzlement, illegal weapons traffic, human traffic, kidnapping, extortion, embezzlement, corruption of civil servants, terrorism, robbery or international vehicle contraband established in the Panamanian Law") (Superintendencia de Bancos trans.).

157. INT'L MONETARY FUND, PANAMA: DETAILED ASSESSMENTS OF OBSERVANCE OF STANDARDS AND CODES FOR BANKING SUPERVISION, INSURANCE SUPERVISION, AND SECURITIES REGULATION 172 (2007). See *id.* at 176 (describing a proposed amendment to include tax-related matters in the Suspicious Activity Reporting Agreement).

tion through the CFATF relating purely to tax evasion. In addition, Panama's secrecy laws prohibit the *Unidad de Analisis Financiero*, the country's financial intelligence unit, from disclosing such tax-related information to its foreign counterparts.¹⁵⁸ This lack of transparency is why Panama is perpetually labeled by the U.S. Department of State a "jurisdiction of primary concern" as a "major money laundering country."¹⁵⁹

Furthermore, the exclusion of tax-related violations as a predicate offense for money laundering in Panama's legal system even impedes U.S. agencies' ability to acquire financial documents directly through the U.S. Mutual Legal Assistance Treaty ("MLAT")¹⁶⁰ with Panama.¹⁶¹ This is because "the MLAT is used primarily to fight narcotics trafficking, related money laundering, and other serious crimes. 'Pure tax' matters are not covered."¹⁶² Therefore, the ability to request information through the MLAT, relating to a money laundering probe, may not necessarily be used in a tax investigation scenario.¹⁶³ Panama's classification of tax evasion as only a civil violation seriously impedes the United States' ability to find and prosecute American tax evaders.

The Stop Tax Haven Abuse Act,¹⁶⁴ introduced to the Senate in February 2007, has attempted to narrow the scope of legislation to target tax evasion specifically through alleged tax haven countries. If adopted, the bill would put in place presumptions of tax evasion for certain transactions completed through specified off-shore jurisdictions, such as Panama.¹⁶⁵ The summary of the bill explains that the need for such presump-

158. FinCen Advisory, Advisory Issue 23, *Transactions Involving Panama*, (July 2000), http://www.fincen.gov/news_room/rp/advisory/html/advis23.html.

159. DEP'T OF ST. BUREAU FOR INT'L NARCOTICS & LAW ENFORCEMENT AFFAIRS, MAJOR MONEY LAUNDERING COUNTRIES 2005 (2006), <http://www.state.gov/p/inl/rls/nrcrpt/2006/vol2/html/62131.htm>.

160. INCSR vol. 2, *supra* note 20, at 31 (MLATs, "which are negotiated by the Department of State in cooperation with the Department of Justice[,] . . . allow generally for the exchange of evidence and information in criminal and ancillary matters. In money laundering [and asset forfeiture] cases, they can be extremely useful as a means of exchanging banking and other financial records with treaty partners.").

161. INT'L MONETARY FUND, UNITED STATES: REPORT ON THE OBSERVANCE OF STANDARDS AND CODES 14 (2006).

162. Sullivan, *supra* note 30.

163. ORG. FOR ECON. COOPERATION & DEV., ACCESS FOR TAX AUTHORITIES TO INFORMATION GATHERED BY ANTI-MONEY LAUNDERING AUTHORITIES: COUNTRY PRACTICES (2002), available at <http://www.oecd.org/dataoecd/16/5/2389989.pdf>.

164. Stop Tax Haven Abuse Act, S. 681, 110th Cong. (2007) [hereinafter Stop Tax Haven Abuse Act] (Title I: Deterring the Use of Tax Havens for Tax Evasion).

165. *Id.* § 101 (establishing presumptions for entities and transactions in offshore secrecy jurisdictions).

tions stems from the tax and secrecy laws of these jurisdictions, which effectively prevent U.S. authorities from accessing the necessary information.¹⁶⁶ Section 205 clarifies that U.S. investigators may access Suspicious Activity Reports gathered in tax haven territories for civil tax matters, and not strictly for criminal proceedings.¹⁶⁷ Yet, the most significant provision of the proposed Act attempts to circumvent the dual-criminality provision by expanding the Treasury Secretary's authority under § 311 of the Bank Secrecy Act, allowing him to impose financial penalties on jurisdictions and financial institutions determined to be "impeding U.S. tax enforcement."¹⁶⁸ The Treasury Secretary would also have the power to limit such institutions' abilities to operate and conduct business within the United States.¹⁶⁹ The bill essentially requires that a jurisdiction have a tax treaty, or similar agreement, in place to provide for timely and mandatory exchanges of tax information.¹⁷⁰ However, the bill is not yet law, and while there is some congressional support for its underlying challenges to the fundamental structure of tax haven jurisdictions,¹⁷¹ there are those who believe the Stop Tax Haven Abuse Act has little chance of becoming legislation.¹⁷² In fact, even those who support the bill recognize that congressional backing is weak.¹⁷³ Therefore, until Congress decides the fate of the bill, the United States remains in its current position of relative ineffectiveness in appropriating information from Panama relating to the evasion of U.S. taxes and possible underlying illegal activity.

III. A PROPOSAL TO IMPLEMENT A TAX INFORMATION EXCHANGE AGREEMENT

Every country has the right to implement and enforce both tax and legal systems that best suit its needs and promote competition for

166. Tax Haven Abuse Act Summary, *supra* note 18.

167. Stop Tax Haven Abuse Act, *supra* note 164, § 205 (calling for improved "Enforcement of Foreign Financial Account reporting").

168. *Id.* § 102 (authorizing "Special Measures against Foreign Jurisdictions, Financial Institutions, and Others That Impede United States Tax Enforcement").

169. *Id.*

170. *Id.* § 7492(b)(F)(D)(i) ("[A] treaty or other information exchange agreement with the United States that provides for the prompt, obligatory, and automatic exchange of such information as is foreseeably relevant for carrying out the provisions of the treaty or agreement or the administration or enforcement of this title.").

171. Komisar, *supra* note 2.

172. Robert E. Bauman, *The Anti-Tax Haven Jihad*, SOVEREIGN SOC'Y LTD., Feb. 22, 2007, http://baumanblog.Sovereignsociety.com/2007/02/the_antitax_hav.html (describing the possible challenges to the constitutionality of the Stop Tax Haven Abuse Act).

173. Komisar, *supra* note 2.

investment.¹⁷⁴ Countries often create tax regimes that will assure a certain amount of revenue for the government, while rarely accounting for the laws of other jurisdictions or the potentially harmful impact they may have on surrounding regions.¹⁷⁵ As the current situation illustrates, conflicts can emerge when a country must access information that may be protected by a foreign legal system, in order to enforce its own laws.¹⁷⁶ A government's inability to investigate potential tax violations that transcend its borders facilitates the evasion of domestic taxes by encouraging taxpayers to transfer assets to foreign jurisdictions.¹⁷⁷ There is a traditional rule that one nation will not assist another nation in enforcing its tax collection procedures.¹⁷⁸ This causes a tension between the sovereign power of one nation to "enforce its laws and protect its borders," and the sovereign power of another jurisdiction to enforce its secrecy laws and keep private any information within its territorial boundaries.¹⁷⁹ Yet, these types of conflicts have generally been resolved through the execution of collaborative tax treaties.¹⁸⁰

This Note argues that the best approach for the United States to reconcile its need for tax information with Panama's right to its tax and bank secrecy systems is to negotiate a TIEA with Panama. The government of Panama has demonstrated in recent years that it is not unconditionally opposed to the exchange of tax information.¹⁸¹ Although Panama has not

174. Rafael E. Berrocal R., *If It Agrees to OECD's Changes, Panama Could Lose Its Financial Privacy*, Feb. 13, 2001, <http://www.freedomandprosperity.org/Articles/epa02-13-01/epa02-13-01.shtml>.

175. Dean, *supra* note 3, at 924.

176. Sullivan, *supra* note 30.

177. Dean, *supra* note 3, at 925.

178. *Pasquantino v. United States*, 544 U.S. 349, 351 (2005). *See also* Spencer, *supra* note 16, at 88.

179. U.S. CONG., OFFICE OF TECH. ASSESSMENT, *supra* note 3, at 117. *See also* BLACK'S LAW DICTIONARY, *supra* note 14, at 654-55 (defining "Sovereignty" as "the supreme political authority of an independent state," and "Sovereign Power" as "the power to make and enforce laws").

180. Dean, *supra* note 3, at 924.

181. *See* Letter by Norberto Delgado Duran, Minister of Econ. & Fin. for the Rep. of Pan., to the Sec'y Gen. of the OECD (Apr. 15, 2002) [hereinafter Letter by Minister of Econ. & Fin. for the Rep. of Pan.]. *See* OECD, http://www.oecd.org/pages/0,3417,en_36734052_36734103_1_1_1_1_1,00.html (last visited Feb. 13, 2009) (describing the organization as an intergovernmental body that "monitors trends, analyses and forecasts economic developments and researches social changes or evolving patterns in trade, environment, agriculture, technology, taxation and more. [The OECD] provides a setting where governments compare policy experiences, seek answers to common problems, identify good practice and coordinate domestic and international policies.").

signed any such treaty with another country,¹⁸² and has refused to approach the issue with the United States,¹⁸³ a treaty better tailored to accommodate Panamanian concerns may be able to overcome this hurdle.

In April 2002, Panama sent a commitment letter to the OECD, agreeing to respect the Organization's principles of "effective exchange of tax information."¹⁸⁴ The government expressly agreed to exchange bank and financial information with other countries investigating tax matters that may only rise to the level of civil offenses in Panama, and would normally be barred from disclosure.¹⁸⁵ However, in December of that year, Panama's government expressed concern to the OECD about the organization's lack of "non-discriminatory treatment."¹⁸⁶ The government believed that the OECD was not committed to creating a "level playing field" and favored certain European OECD members by exempting them from the same exchange obligations as were imposed on Panama.¹⁸⁷ Concerned by the OECD's double standard and inaction to ameliorate the disparity, Panama withdrew from its earlier commitment.¹⁸⁸ The OECD's policy was viewed as a threat to Panama's sovereignty¹⁸⁹ by trying to impose restrictions, unfairly and inequitably, on its ability to compete in the financial services market.¹⁹⁰

Nevertheless, by negotiating a TIEA solely with Panama, where information exchange commitments would be equal between both countries, the United States could resolve the "level playing field" issue. A narrow jurisdictional scope with equally binding terms would indicate a dedication to fairness and a respect for Panama's sovereignty. Panama has a legitimate concern that it may lose its competitive edge in the region if it relaxes its secrecy laws.¹⁹¹ Due to the fact that other notorious

182. Panamalaw.org, *supra* note 31.

183. Robert E. Bauman, *Where Are They Now? The World's Top Asset Havens . . . Still On Top*, 6 ESCAPE FROM AM. E-ZINE (July 2004) http://www.escapeartist.com/efam/60/Best_Banking_offshore.html.

184. Letter by Minister of Econ. & Fin. for the Rep. of Pan., *supra* note 181.

185. *Id.*

186. Press Release, Gov't of the Rep. of Pan., Panama Reiterates to the OECD the Need for Equitable and Non-Discriminatory Treatment (Dec. 10, 2002).

187. *Id.*

188. Daniel J. Mitchell, Strategic Memorandum from the Ctr. for Freedom & Prosperity (Jan. 6, 2003), <http://www.freedomandprosperity.org/memos/m01-06-03/m01-06-03.shtml>.

189. See Dean, *supra* note 3, at 935 (Panama, as a recognized tax haven jurisdiction, would perceive the OECD initiative as a threat to its sovereignty).

190. Daniel J. Mitchell, *The OECD's Dishonest Campaign Against Tax Competition: A Regress Report*, Prosperitas: A Policy Analysis from the Ctr. for Freedom & Prosperity Found., vol. IV, iss. I, 1-2 (June 2004).

191. Dean, *supra* note 3, at 958.

“tax havens” such as the Bahamas and the Cayman Islands have signed TIEAs,¹⁹² the value to Panama in maintaining its secrecy laws and not entering into a similar agreement increases.¹⁹³ Yet, through diligent negotiations, both countries could circumvent this concern by narrowly tailoring the conditions that would trigger the requirement to exchange information, and restricting the categories of data that would have to be transferred.

Conceivably, both countries would be able to define specific circumstances that would elicit the exchange of information, but that do not infringe on Panama’s general assurance of secrecy. For example, by limiting a situation to defined asset amounts transferred through specific types of financial instruments or transactions that originate from U.S. banks, U.S. investigators could gain access to information customized to tax evasion, while Panama could retain its overall international commitment to secrecy. Although such a limited scope may exclude many instances of tax evasion and money laundering from scrutiny, it would at least be a step in the right direction. Collaboration on a small scale would allow authorities in both nations to familiarize themselves with an increased volume of information exchanges, without getting overwhelmed by a flood of requests that may accompany a broader treaty. As the process becomes more customary, it may be easier to slowly expand the treaty’s reach.

In addition, a narrow scope would mean that only very specific transactions, those purposely instigated to evade U.S. taxes, would be deterred from going through Panama. Therefore, the country could retain its lucrative bank secrecy regime with little financial loss from legitimate business. Additionally, the United States could offset any minimal loss to Panama by implementing an asset sharing program. The countries could share not only the revenue from recovered taxes, but also any punitive damages U.S. authorities impose for tax violations.¹⁹⁴ Regardless of the specific provisions of a U.S.-Panamanian TIEA, a treaty would require a careful balancing of both countries’ right to administer their respective laws. This will only be possible through diligent diplomacy and the willingness of each government to accommodate and respect the other’s necessities.

192. Sullivan, *supra* note 30.

193. Dean, *supra* note 3, at 958.

194. See 26 I.R.C. § 7431(c) (2000) (authorizing the imposition of punitive damages for convictions of tax evasion).

CONCLUSION

The loss of tax revenue to the U.S. Treasury is a significant side effect of money laundering with a substantial impact on the U.S. economy. Evaded taxes are typically funneled through tax haven countries because of the anonymity and strict secrecy laws those jurisdictions provide. The lack of economic transparency in these offshore havens permits the origin of illicit funds to remain hidden from U.S. investigators, and aides the money's re-entry into the U.S. banking system as seemingly legal money. Although tax evasion and money laundering are inherently similar, they are separate and distinct violations. While both can be criminal matters in the United States, the evasion of taxes is not a criminal issue in Panama unless the tax evasion directly implicates a more serious crime usually relating to drugs. Only in those situations do Panama's secrecy laws authorize disclosure of tax and financial information. Therefore, requests for information in purely U.S. tax evasion investigations will generally not be honored. This creates a safe haven for tax cheats to hide their money and subsequently launder it back to the United States.

The U.S. government has made a cogent effort to strengthen its domestic laws regarding money laundering and financial crimes. However, reinforced domestic legislation can neither overcome the principle of dual criminality, nor compel Panama to breach its own secrecy regime. Furthermore, international financial task forces, put in place to combat money laundering, have also not been able to reach purely economic matters such as tax evasion. Consequently, evaded taxes remain protected in Panama.

Nevertheless, the signing of a TIEA could circumvent the barriers established by secrecy laws. Although Panama does not currently have such an agreement in place, it may be possible through diplomatic channels to tailor an agreement that would accommodate both the United States' need for access to financial information and Panama's insistence that its secrecy laws not be compromised. However, until such a TIEA is effectuated, Panama's bank secrecy laws will continue to facilitate the laundering of evaded U.S. taxes.

*Bryan S. Arce**

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