

# IRS Targeting of Offshore Promoters

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In the business news and legal publications, we read about the US Justice Department filing an ex parte petition for leave to serve “John Doe” summonses on the Swiss banking giant, UBS and its subsidiaries. The Justice Department is seeking the names of US persons who have not filed required tax returns, tax reports, a Form W-9, other qualified intermediary forms, and have not paid taxes. These filings by the Justice Department are made on behalf of the Internal Revenue Service (IRS), which will likely include both the civil division and the criminal division. Some years ago, the IRS referred to itself as the “friendly IRS.” One can see that these actions by the IRS are not friendly. But the IRS has been unfriendly for some time in its pursuit of promoters who have recommended entities or structures that the IRS deems to constitute tax evasion and/or tax fraud by US persons.

A practitioner engages in providing advice regarding offshore structures that apparently avoids US income taxes for American clients. Life is good, and the money is coming in. The practitioner receives continuous referrals and is adept at implementing structures, which have become routine for him, his partners/associates and his staff. The implemented planning apparently provides the deferral/avoidance of US income taxes. Then everything changes for the practitioner when he receives a Notice that he is targeted as an offshore tax-shelter promoter (promoter) under a civil investigation pursuant to Internal Revenue Code (IRC) Sections 6700 and 6701. The practitioner has no understanding of the changes he is about to experience. His professional life and personal life have been altered dramatically. As the years go by, the actions and particularly the inactions of the IRS will wreak havoc over his life.

IRC Section 6700 is titled “Promoting abusive tax-shelters, etc.” and IRC Section 6701 is titled “Penalties for aiding and abetting understatement of tax liability.” Both IRC Sections 6700(c) and 6701(f) state: “The penalty imposed by this section shall be in addition to any other penalty provided by law.” Thus, the IRS is not limited to these provisions in its civil investigation of the promoter.

For the purposes of this article, reference to a targeted offshore tax-shelter promoter shall mean an alleged offshore tax-shelter promoter because this is an investigation and no court of law has classified the targeted individual as a promoter. Note that the word “investigation” is used with respect to civil matters, where in the past the word “investigation” denoted a criminal or civil fraud matter.

## Intentions of the IRS

One cannot look into the minds of the managers in charge of the IRC Sections 6700 and 6701 offshore tax-shelter promoter investigations, nor are the agents conducting such investigations, but observations are available with respect to the implications and results of these investigations. The IRS may not be seeking tax-shelter promoter tax penalties and interest from targeted promoters but instead is generally seeking five things: (1) the financial destruction of the promoter; (2) the destruction of the promoter’s business; (3) the emotional destruction of the promoter; (4) the potential injunction against the promoter for engaging in recommending and implementing certain transactions that the IRS have targeted with respect to the promoter; and (5) the potential indictment of the promoter.

## IDRs

The promoter will begin receiving what is the beginning of one of his worst nightmares: the dreaded “Information Document Request” (IDR), Department of the Treasury Form 4564. A study of the defined words and terms in the IDR shows the serious and encompassing requests for information the IRS is seeking from the promoter.

Form 4564 —

Department of the Treasury

Internal Revenue Service

Information Document Request (IDR)

Sec. 6700/6701 Promoter Investigation

Description of Documents Requested:

PLEASE PROVIDE THE FOLLOWING REQUESTED INFORMATION BY THE DATE BELOW.

The following protocols apply to this Information Document Request.

The term “document” is used in a comprehensive, singular and plural sense, and refers to any means of preserving thought or expression.

The term “document” means, without limitation, any written, typed, photocopied, photograph recorded, mechanical, or electronic reproduction of communications or representations, whether comprised of letters, words, numbers, pictures, sounds, symbols, computer data, or any combination thereof. Where any of the foregoing items contains any marking not appearing on the original, then such item shall be considered to be a separate original document. The term “document” also includes the following, without limitation and for purposes of illustration only:

(a) Contracts, agreements, plans, term sheets, summaries, opinions, studies, reports, schedules, work papers, computations, appointment calendars, telegrams, communication memoranda, minutes, notes, comments, messages, telexes, telegrams, teletypes, cables, facsimiles, or other written notes or communications, books, graphs, printed matter,

outlines of oral representations, and all financial records, and any other writings, bulletins, announcements, press releases, brochures, notices of the meetings, agendas, attendance lists, manuals, and journal et al entries, and alterations or modifications of the foregoing;

(b) Items designated as internal, confidential, private, or not to be disclosed;

(c) All electronic mail (e-mail), whether in a computer disk and/or any other system or device which saves historical e-mails, attachments; and  
 (d) Video and/or audio tapes, cassettes, films, microfilm, computer files in any format, computer disks, and computer and software programmes.

Included in the IDR is a Description of Documents Requested with respect to specific clients or others that the promoter has represented or worked with, including partners, associates, employees and professionals outside the firm of the targeted promoter.

The IDR, with the above definitions, covers all records, financial or otherwise, as well as a list of clients. This request includes all bank records of the promoter and his firm. The promoter quickly sees this daunting task and further sees that most or all of his personnel will be engaged in helping obtain this information. The initial IDR is only one of a series of IDRs that will follow. The promoter will see each IDR becoming more specific with requests. For example, the IDRs will begin including requests for information about specific clients and specific parties that the promoter has dealt with, such as service providers, trust companies, lawyers, CPAs, etc.

### Interviews by IRS

In addition to peppering the promoter with IDRs, the IRS will request an interview with the promoter. It is highly recommended that the promoter's lawyer be present at this interview. It is also recommended that a criminal tax practitioner/lawyer be present at the interview. Although the civil investigation is separate from any potential criminal indictment investigation, it may be necessary for a criminal tax practitioner to be present in order to ensure that the promoter makes no comments that can incriminate him in a criminal indictment investigation. The promoter will learn that the IRS agent is speaking with clients of the promoter and some of these clients are speaking with the IRS agent without their counsel present. The IRS interviews clients of the promoter to determine what advice was given to the clients by the promoter, as well as the structures and entities that were implemented by the client. Having a loyalty to their clients, some promoters want to help and protect their clients because the promoters know that these interviews will likely lead to audits. Often, the promoters cannot understand that the interests of the clients and the promoter are now adverse, and the promoter is in no position to help his clients.

The promoter discovers that the IRS is interviewing former partners, if any, former associates and former employees of his firm. And the promoter will then learn that the IRS wants to interview current partners, associates and employees. The mere contact by the IRS with the various parties causes fear and anxiety. An IRS interview with the client, even if counsel is present, brings the promoter to new levels of stress and angst. Furthermore, if the client is represented by counsel, that lawyer may not have been involved in the planning that was implemented through the promoter. Counsel for these clients may find the interests of the promoter are adverse to their clients' interests. For example, counsel may take the position that the clients did not understand the planning transactions and that the promoter should be held responsible as a practitioner holding himself out as an expert in international tax laws and the tax compliance/reporting requirements.

Tension and anxiety are developing between the promoter; his current and past employees, current and past partners/associates, and especially among the promoter and his clients. These IRS interviews will likely take years. The mere fact that years are going by and no assessment is being made with respect to the promoter's penalty or other tax that is allegedly due, leaving the

hapless promoter with no way to discharge any tax liability and stop the investigation, results in the consequences stated previously: (1) the financial destruction of the promoter; (2) the destruction of the promoter's business; (3) the emotional destruction of the promoter; (4) the potential injunction against the promoter for engaging in recommending and implementing certain transactions that the IRS have targeted with respect to the promoter; and (5) the potential indictment of the promoter.

If the promoter has partners, and the Notice of a civil investigation under IRC Sections 6700 and 6701 is sent to one or more of these partners, additional tension, frustration and adverse interest develops between these parties. First, they do not know if one or more of the partners will be promoters that the IRS is ultimately seeking as the "promoter." In the meantime, the promoter is paying legal fees and potentially other fees (such as accounting fees), and the revenue of his business is dramatically dropping each month. Lawsuits or threats of lawsuits from clients and current or former partners and employees may develop.

### Potential Criminal Indictment Investigation

In addition to the civil investigation, something dreadful occurs. The promoter calls his lawyer stating that he has two unannounced visitors in his home – Criminal Investigation (CI) agents. The CI agents advise the promoter that they are conducting a criminal indictment investigation and want to know if they can ask the promoter some questions. Note that the CI agents do not state that they are conducting a criminal indictment investigation of the promoter, but that they are conducting a criminal indictment investigation. As time goes by, the promoter and his partners will not know whether the investigation will conclude in one or more of the promoters being indicted. And it likely will take years for this determination to be made.

The promoter is well-advised to provide no information and answer no questions asked by the CI agents. When the lawyer (preferably a tax lawyer) receives the phone call from the promoter that the CI agents are at his home or place of business, the lawyer must advise the promoter to decline to speak with the CI agents. And this is when the promoter must immediately retain criminal tax counsel.

### Civil Investigation Suspended during Criminal Investigation

A civil investigation under IRC Sections 6700 and 6701 is suspended during the criminal indictment investigation by the CI agents. All parties involved are aware that the civil investigation is still looming but not even the lawyer for the promoter can get an IRS agent handling the civil investigation to respond. The civil investigation is shut down for the time being.

The promoter will naturally want to stop the bleeding by ending the investigation and attempting to negotiate the amount of tax-shelter penalties. As stated, no assessment of tax-shelter penalties is made, and the civil investigation is simply suspended during the criminal investigation. The promoter begins to wonder if this process of destruction will ever come to an end.

When an individual receives a notice from the IRS that he is under a civil investigation as a promoter of alleged offshore tax-shelters, he can expect an unfriendly IRS to issue numerous IDRs and ask questions of numerous individuals, whether directly or indirectly involved, or related to his planning recommendations and implementations. Because the investigation by the IRS drags on and on, it takes a serious toll on the life of the promoter.

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Please see page 6 for Richard Duke's new regular feature, *Dubai Digest*, which launches in this issue.

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