

IN THE UNITED STATES DISTRICT COURT FOR THE
SOUTHERN DISTRICT OF FLORIDA
MIAMI DIVISION

CASE NO. 1:09-MC-20423-GOLD/MCALILEY

UNITED STATES OF AMERICA,

Petitioner,

vs.

UBS AG,

Respondent.

**BACKGROUND INFORMATION FOR THE COURT'S
CONSIDERATION PRIOR TO THE SCHEDULED STATUS CONFERENCE**

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Yesterday, the Internal Revenue Service (“IRS”) began a process pursuant to which it seeks to have this Court order Swiss-based employees of Respondent UBS AG (“UBS”) to violate Swiss criminal law in Switzerland. Such violations would expose these employees to substantial prison terms, as well as fines, penalties and other sanctions. The IRS similarly believes that this Court should require UBS, a Swiss bank and one of the largest banks in the world, to violate Swiss law in a manner that will expose it to penalties, civil liability and the possible revocation of its banking license. The IRS makes this request notwithstanding that it has a contract with UBS that expressly permits UBS to comply with Swiss law by keeping confidential the very information that the IRS now demands.

Notwithstanding the extraordinary importance, consequences and international implications of these issues, the IRS submitted to this Court a proposed order to show cause that provides for a limited, expedited briefing schedule and a truncated procedure for this matter. Indeed, after waiting seven months to file its petition, the IRS proposes that the Court order that UBS be given only eleven days after service of the Court’s order to respond to the IRS’s petition. There is simply no reason to have, nor equity in having, such an expedited process here. UBS respectfully requests that, rather than entering the proposed order to show cause submitted by the IRS, the Court use the status conference now scheduled for February 23, 2009 to give the parties the opportunity to address a possible briefing schedule, discovery, the nature of the hearing that might take place in this matter, and the role of the governments of both Switzerland and the United States in these proceedings.

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On July 1, 2008, this Court authorized the IRS to issue the “John Doe” summons to UBS. See In the Matter of the Tax Liabilities of John Does, 08-21864-MC-LENARD (S.D.

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Fla.), Docket Entry No. 5. The summons seeks account information for a class of unidentified U.S. taxpayers who have accounts with UBS in Switzerland. See Declaration of Daniel Reeves (“Reeves Dec.”) ¶¶ 5-6 & Ex. 1. The IRS issued the summons knowing full well that UBS and its employees could not provide information responsive to the summons that was located in Switzerland without violating Swiss law. Indeed, in full and fair recognition of the incompatibility between the John Doe summons and Swiss law, the IRS initially agreed to limit the scope of UBS’s obligations in response to the summons to the production of documents or information located in the United States.

Since being served with the summons in July of 2008, UBS has cooperated fully, working diligently and in good faith to provide the IRS with information responsive to the summons that UBS could provide without violating Swiss law. Indeed, over the past seven months, UBS has provided the IRS with information located in the United States relating to more than three hundred accounts targeted by the John Doe summons. See Reeves Dec. ¶ 18.

The U.S. government has now also been provided with responsive account information that was located in Switzerland. On February 18, 2009, this Court approved a deferred prosecution agreement between UBS and the U.S. Department of Justice. See United States v. UBS AG, 09-60033-CR-COHN (S.D. Fla.), Docket Entry No. 19. As part of the deferred prosecution agreement, the U.S. government was provided with documentation located in Switzerland for certain additional accounts that are targeted by the John Doe summons. This production was made pursuant to an order issued by the Swiss Financial Market Supervisory Authority (“FINMA”) based on evidence available in UBS’s files that supported a reasonable suspicion that the holders of these accounts engaged in conduct that constituted “tax fraud or the like,” as that term is used in the Convention between the United States of America and the Swiss

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Confederation for the Avoidance of Double Taxation with Respect to Taxes on Income (the “Double Taxation Treaty”), and that therefore the account information could be provided to the U.S. government consistent with the Double Taxation Treaty and Swiss law.

In a very public move giving little or no credit to UBS’s productions and its commitments in the deferred prosecution agreement — including UBS’s agreement to exit the relevant U.S. cross-border business — the IRS now asks this Court to place UBS and its employees into an untenable position, stuck between the enforcement power of this Court and the criminal law of their sovereign home country. The petition filed by the IRS will thus force the Court to consider a series of important issues:

First, the IRS’s petition raises significant issues of international comity and conflicts of law. The IRS has a legitimate interest in making sure that U.S. taxpayers pay taxes on their income. UBS does not dispute that. However, in the absence of the express authorization of the Swiss authorities granted pursuant to fully negotiated standards set forth by the two governments in U.S.-Swiss treaties, Swiss law strictly prohibits UBS and its employees from disclosing to the IRS the account information located in Switzerland that the IRS seeks through its summons. The IRS’s petition does not acknowledge these restrictions and instead simply ignores the existence of Swiss law and sovereignty.

Second, while the IRS attempts to downplay them, the treaties between the United States and Switzerland provide administrative procedures pursuant to which the IRS has the ability to seek information relating to tax fraud or the like that is located in Switzerland. See Double Taxation Treaty art. 26(1); Double Taxation Treaty Protocol § 10; Treaty Between the United States of America and the Swiss Confederation on Mutual Assistance in Criminal Matters arts. 1(1), (4). It is true that the IRS may not be able to obtain information as quickly or as

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broadly through these treaty mechanisms as the IRS might be able to in the United States, but these treaty mechanisms reflect a carefully negotiated, mutually accepted agreement balancing the interests of the U.S. and Swiss governments. With yesterday's filing, the IRS asks this Court to rewrite the relevant treaties between two sovereign nations, the United States and Switzerland. To the extent that the IRS is not satisfied with treaties that the U.S. government has negotiated, that concern should be remedied through diplomacy, not an enforcement action such as the one the IRS has commenced here.

Third, the IRS entered into an agreement known as a "Qualified Intermediary Agreement" with UBS (and many other banks). That agreement sets forth, among other things, the manner in which UBS, in its capacity as a "Qualified Intermediary," is to conduct information reporting and tax withholding for U.S. clients with accounts in Switzerland. Most relevant for the present proceeding, the Qualified Intermediary Agreement contains specific procedures addressing the treatment of accounts held by U.S. taxpayers. Subject to special rules limiting investments by U.S. taxpayers in U.S. securities, these procedures expressly recognize that UBS — like any other Qualified Intermediary that is prohibited by law from disclosing account holder information — may maintain accounts for U.S. taxpayers who choose not to submit an IRS Form W-9 to UBS and that UBS is not required to disclose the identities of such account holders to the IRS. And that is what took place. In this action, the IRS seeks to repudiate its own contract and demands the production of the very account information that the IRS agreed would remain confidential.

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The IRS issued the summons in July 2008. Now, seven months later, the IRS seeks to commence an enforcement proceeding on an expedited schedule and with a truncated

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process. In light of the complex issues and international implications raised by the IRS's petition, rather than entering the proposed order to show cause submitted by the IRS, we respectfully request that this Court use the scheduled status conference to address how this matter should proceed.

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Dated: February 20, 2009

Respectfully submitted,

s/ Eugene E. Stearns

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CERTIFICATE OF SERVICE

I hereby certify that on February 20, 2009, I electronically filed the foregoing document with the Clerk of Court using CM/ECF. I also certify that the foregoing document is being served this day on all counsel of record identified on the attached Service List via transmission of Notices of Electronic Filing generated by CM/ECF or other approved means.

s/ Gordon M. Mead, Jr.
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SERVICE LIST

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