U.S.-Mexico Information Exchange Agreement

by Mike McIntyre

Some years ago, a U.S. tax shelter promoter ran an advertisement in a U.S. medical journal that offered doctors the opportunity to earn tax-free interest income at high rates. The scheme involved the deposit of U.S. dollars through an allegedly foreign trust in Mexican banks. A friend working in a Mexican bank told me that the advertisement generated a huge volume of deposits from U.S. doctors. The scheme, however, did not work, at least from my reading of U.S. tax laws. It was indeed too good to be true, like many of the glittering tax shelter schemes of the 1980s and late 1970s.

The use of Mexican banks by U.S. tax evaders is probably far less common than the use of American banks for that purpose by their Mexican counterparts. I have no good idea of the extent to which Mexican residents are evading Mexican taxes by putting their deposits in American banks. The nervous public reaction of some Texas bankers to the recent U.S.-Mexico exchange of information agreement suggests that they believe that the volume of deposits moving north has been considerable. Certainly the United States has done nothing to discourage such deposits, having provided a full exemption from U.S. taxes for interest on bank deposits held by foreign residents.

Now comes the U.S.-Mexico information exchange agreement. It went into effect on January 18, 1990, and, by its terms, it should provide the tax authorities in both countries with an effective tool for controlling cross-border tax evasion. (For a story on the agreement, see Tax Notes Int’l 5 (January 1990).) But tax officials on both sides of the U.S.-Mexico border seem intent on assuring Mexican and American tax evaders that the new tool will not be used for that purpose, at least on a routine basis. There seems to be an official consensus that any serious effort at curtailing tax evasion by depositors and other typical investors will simply cause individuals willing to commit tax fraud to take their deposits and other investments somewhere else.

There will be, I suppose, some capital flight resulting from the new agreement. Tax evaders are not a trusting lot. Recall what happened after the repeal of the German withholding tax last April. (For a story on the repeal, which was effective on July 1, 1989, see 1 Tax Notes Int’l 3 (July 1989).) Many depositors had removed their deposits from German banks when the German withholding tax on interest went into effect. According to press reports, they have not repatriated those deposits after the repeal of the withholding tax for fear that they will be targeted for a tax audit. Assurances by the German tax authorities that they fully believe in the honesty of those depositors has not had the desired effect. I suppose that the depositors do not want to take the chance that the tax authorities are either that naive or that cynical. I suspect that Mexican and American depositors engaging in tax evasion will be similarly risk averse.

Despite the apparent short-term limitations on the effective scope of the U.S.-Mexico exchange agreement, I am optimistic that the agreement will eventually become an important
instrument for limiting capital flight from Mexico. I hope that it can become a prototype for exchange agreements between other developed and developing countries. I realize that enforcement measures can only be a part of any viable solution to the problem of capital flight from the developing world. But they are, in my view, an essential part, and they deserve the full support of the international tax community.

Index for TNI

This month we publish a supplemental issue containing a cumulative table of contents and a set of indexes for volume 1 of TAX NOTES INTERNATIONAL. We hope that readers will find these research tools useful. Future issues of TNI will also be indexed. All subscribers to TNI will receive the index supplements for free—that is, without any additional charge.

We have been having some extended discussions at TNI about the new indexes, and I expect those discussions to continue. One issue is how the subject index should be organized and another is how often the index should be published. Readers are invited and encouraged to give their input. To have any impact on the design of the indexes for volume 2, we will need your comments right away. The most valuable comments are likely to be those based on the extended experience of our readers with the indexes. Such comments are most welcome, and we will take them into account in designing the indexes for volume 3.

A special feature our index supplement is a crossword puzzle, based primarily on words used in volume 1 of TNI. We will give a prize for the first correct solution received, so warm up your fax machine. You must submit a copy of the puzzle -- to prevent abuse of library copies, we will not accept an original. If you cannot make or otherwise obtain a copy of the puzzle for any reason, write to us and we will send you one. The winner will receive a copy of [*231] The UNITARY TAX CONTROVERSY: ARTICLES AND COMMENTS, edited by Charles Davenport. (Please note the corrections to the puzzle on p. 235.)

Poetry Contest Winners

In the tradition of Dante Alighieri (“Onorate l’altissimo poeta”), we give honor this month to Bruce McCrae. Mr. McCrae is the winner of the TNI poetry contest for his evocative ditty “Back to Back.” And congratulations to Carl Shoup, our runner-up. (See p. 235 for the winning entries.) We give a warm thank you to them and to everyone else who participated in the contest.

A stunning reproduction, suitable for framing, of “Ode to Corporate Tax” is being sent to the first-place winner. We are delighted to announce that arrangements have been made for other readers to obtain their own collectors’ copy of that poem for $1,036 plus $4 for shipping, handling, and insurance. The charge is modest, given the inflation that the art market has been experiencing of late, and the proceeds go to a good cause, the Treasury Historical Association, a charitable foundation formed in 1973 to preserve the U.S. Treasury Building.