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# "White Money Strategy" in Switzerland

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Combating abuses in the areas of money laundering and taxation is the major objective of the current Swiss financial market policy. This strategic orientation in terms of "financial integrity" was announced by the Swiss government (the Federal Council) on 28 February 2010 and 22 February 2012[1] before being detailed in a report issued on 19 December 2012[2], soon after the adoption of the revised Financial Action Task Force Recommendations (the "**FATF Recommendations 2012**")[3]. The main reforms aimed to i) facilitate international exchange of information; ii) extend duties of care in relation with untaxed assets and iii) regard all serious offences, including tax offences, as predicate offences to money laundering.

The purpose of this paper is to provide an overview of the options proposed by the Federal Council in order to implement the standard set by the FATF Recommendations 2012 into the national law and to fulfill Switzerland's international engagements. Two independent draft bills, the first on combating money laundering and terrorist financing, the second on enhancing due diligence requirements in the area of taxation, were submitted for consultation to the Swiss political and economic actors on 27 February 2013[4]. The progress that has been made since then is summarized below.

## In the Area of Money Laundering

The measures proposed in February 2013 aimed at introducing serious tax offences (in the area of both direct and indirect taxation) in the list of the predicate offences to money laundering, as well as provisions to ensure transparency of legal entities and rules for the identification of beneficial owners and politically exposed persons ("**PEPs**").

On 13 December 2013, the Federal Council adopted the dispatch on the new Federal Act for Implementing the Revised Financial Action Task Force Recommendations (the "**Bill**")[5]. The key points provided for in the Bill are discussed hereafter.

### I. Introduction of a New Predicate Offence to Money Laundering

The Federal Council initially proposed to introduce a new criminal offence in the Federal Act on Direct Federal Taxation (**LIFD**; RS 642.11) and the Federal Act on the Harmonization of Direct Taxation

1 - For more information see http://www.sif.admin.ch/dokumentation/00513/00772/index.html?lang=en&msg-id=43511.
2 - The Federal Council's report on Switzerland's financial market policy of 19 December 2012 (see http://www.sif.admin.ch/dokumentation/00513/00772/index.html?lang=en&msg-id=47291).
3 - The FATF Recommendations 2012 were adopted on 16 February 2012. Switzerland actively contributed to the elaboration of this new international standard that aims at accommodating new developments in international financial crime (see http://www.fatf-gafi.org/topics/fatfrecommendations/documents/internationalstandardsoncombatingmoneylaunderingandthefinancingofterrorismproliferation-thefatfrecommendations.html).
4 - See http://www.sif.admin.ch/dokumentation/00513/00772/index.html?lang=en&msg-id=47934.
5 - The Bill and the Federal Council's Message can be found at http://www.admin.ch/ch/f/gg/pc/ind2013.html.

at Cantonal and Communal Levels (**LHID**; RS 642.14). By doing so, it intended, first, to extend the criteria characterizing tax fraud to include any behavior considered as fraudulent and, second, to characterize serious tax frauds, i.e. where tax factors of CHF 600'000 or more had been concealed from the tax authorities, as felonies punishable as predicate offences to money laundering[6].

Under the current regime, only felonies [i.e., offences punishable by more than 3 years imprisonment in the sense of Art. 10 al. 2 of the Swiss Criminal Code (**SCC**; RS 311.0)] constitute predicate offences to money laundering in Switzerland. Article 305bis SCC indeed defines money laundering as "*an act that is aimed at frustrating the identification of the origin, the tracing or the forfeiture of assets which […] originate from a felony*".

However, as of today, tax offences are not legally regarded as felonies, with the exception of Art. 14 al. 4 ACL, which punishes an aggravated tax fraud committed in relation with duties appearing in a case of cross-border movement of goods[7]. Evasion of direct taxes for instance – whether committed wilfully or negligently and irrespective of the amount of tax evaded – currently constitutes a mere contravention (i.e., an offence only subject to a fine)[8]. Similarly, tax fraud, defined as a combination of forgery of documents and use of false certifications in order to avoid direct taxes, only counts as a misdemeanor, punishable by imprisonment up to three years[9].

The results of the consultation procedure however decided the Federal Council to drop its initial proposal to introduce a new criminal offence in the tax legislations. It rather suggested in the Bill that Art. 305bis SCC should be amended in a way that not only felonies but also tax frauds in accordance with Art. 186 LIFD or Art. 59 LHID would constitute predicate offences to money laundering, provided the amount of tax evaded exceeded CHF 200'000 per tax period.

Concerning indirect taxation, it proposed to extend the scope of Art. 14 al. 4 ACL beyond the cross-border movement of goods in order include other taxes levied by the Confederation, such as VAT on transactions on Swiss territory and services. No amendment to Art. 305bis SCC is necessary for indirect taxation as Art. 14 al. 4 ACL already punishes a felony.

## II. Increase in the Transparency of Legal Entities

The FATF Recommendations 2012 require countries to implement measures to identify the beneficial owners of legal entities and enhance the transparency of unlisted companies issuing bearer shares. Indeed, in the eyes of the FATF, banking secrecy is not the only problem to combat financial abuses. This problematic also encompasses anonymous participation in all kind of legal entities/ trusts.

The legislative solution proposed by the Federal Council allows companies with bearer shares to choose between (i) the disclosure to the company of the shareholders' identity and the identity of the beneficial owners of the shares if the shareholder has a stake of 25% or more in the voting rights or share capital at the time of acquisition of the shares (in addition, the company shall keep the record)[10]; (ii) as a variation, the disclosure of the shareholders' identity to a financial intermediary which will keep such a record (the company decides to delegate this duty to an authorized third party)[11] or (iii) a simplified conversion of the bearer shares into registered shares or (iv) the issuance of bearer shares in the form of uncertificated securities credited to a securities account by a custodian[12].

6 - In parallel, the Federal Council also launched in May 2013 a consultation for the revision of the criminal administrative law. Amendments to the Federal Act on Administrative Criminal Law (**ACL**; RS 313.0) were suggested for the investigation and prosecution of tax offences. According to the Federal Council's proposal, tax authorities should be entrusted with reinforced powers to investigate any kind of tax offences, also by obtaining bank records. This proposal is highly criticized as Swiss law on privacy, which includes Swiss banking secrecy, is a fundamental cornerstone of the Swiss legal regime. The results of the consultation procedure are expected soon (see for more information http://www.admin.ch/ch/f/gg/pc/ind2013.html).

7 - To be exhaustive, it should be mentioned that the Swiss Federal Tribunal considers that fraud committed by misuse of a fiscal instrument (VAT carrousel fraud) falls under the definition of a criminal fraud in the sense of Art. 146 SCC and could be considered as a predicate offence to money laundering (ATF 110 IV 24, consid. 2e; TF, 1C_171/2010 of 6 April 2010 and the references quoted by Ursula CASSANI in: *L'infraction fiscale comme crime sous-jacent au blanchiment d'argent: considerations de lege ferenda*, RSDA 1/2013, p. 1ss). According to the same author, a tax fraud committed by a criminal organization could also fall under Art. 260ter SCC, which is also a felony.

8 - See Art. 175 LIFD and Art. 56 LHID.

9 - See Art. 14 al. 2 ACL; Art. 186 LIFD; Art. 59 LHID.

10 - Proposed Art. 697i and 697j of the Swiss Code of Obligations (**SCO**; RS 220).

11 - Proposed Art. 697k SCO.

12 - Issuance according to Art. 6 of the Federal Intermediated Securities Act (**FISA**; RS 957.1).

The obligation to disclose the identity of the beneficial owners as soon as a shareholding of 25% is reached also applies in the case of registered shares of unlisted companies and partners in limited liability companies, although not retroactively (duty limited to new acquisitions)[13].

The Bill introduces various sanctions to punish non-compliant shareholders, from the suspension of their voting and economic rights[14] to criminal sanctions[15].

## III. Identification of Beneficial Owners

During Switzerland's last evaluation, the FATF identified some unresolved deficiencies that needed to be remedied in domestic law. The identification of the beneficial owners is one of them. The Bill therefore seeks to amend Art. 4 of the Swiss Anti-Money Laundering Act (**AMLA**; RS 955.0) by formally including an obligation to identify the beneficial owners of all unlisted companies as well as to progressively introduce due diligence obligations concerning the identification of the beneficial owners of all legal entities (in the sense of the physical persons controlling the legal entities), even for operating companies[16].

## IV. Identification of Domestic PEPs

The FAFT Recommendations 2012 extended the obligation to identify domestic PEPs and persons exercising (or having exercised) an important function at or on behalf of an international organization for due diligence purpose, in addition to foreign PEPs.

The Bill therefore adds to the AMLA a formal definition of national PEPs[17]. By so doing, all financial intermediaries should equally apply the PEPs regulations in terms of risk-assessment. Relatives of PEPs are similarly concerned by these regulations.

## V. Regulations on Cash Payments for Purchase of Both Movable and Immovable Property

The Bill proposes to introduce a new rule in the AMLA requiring all payments in excess of CHF 100'000 for property purchases or sales of movable property to be arranged through a financial intermediary subject to the AMLA.

During its last evaluation of Switzerland, the FATF indeed identified deficiencies in the anti-money laundering requirements for professions outside the financial sector. The suggested amendment to the AMLA will introduce a new category of persons to whom the anti-money laundering regulations will apply[18]. As of today, the AMLA is indeed exclusively applicable to financial intermediaries. As a consequence, cash payments at auctions will, in the future, only be possible up to a sum of CHF 100'000[19].

## VI. Extension of the Powers and Responsibilities of the MROS

The Money Laundering Reporting Office of Switzerland ("**MROS**") already has the power, since 1 November 2013[20], to exchange financial information (including the name of a financial intermediary, the name of the account holder, the account number, the sum of deposited assets, the identity of the beneficial owners and information relating to transactions) with its counterparts abroad, subject to certain conditions[21].

The Bill dated 13 December 2013 proposes to enlarge this power and allow the MROS, upon request, to obtain all the information it deems necessary for its analysis of suspicious activities from other federal, cantonal and communal authorities.

It also suggests to report the obligation of freezing the assets imposed on the financial intermediary

13 - Proposed Art. 790a and 837 SCO.
14 - Proposed Art. 697m SCO.
15 - Proposed Art. 327a SCC.
16 - As of today, Art. 4 AMLA only imposes the identification of the beneficial owner when the customer is not the beneficial owner; when the customer is a domiciliary company or when a cash transaction of considerable financial value is being carried out.
17 - Proposed Art. 2a AMLA.
18 - Proposed Art. 2b and 2c AMLA.
19 - Also for auctions regulated by the Debt Collection and Bankruptcy Act (RS 281.1).
20 - Amendment of the AMLA of 21 June 2013; FF 2012 6449.
21 - For example, no original documents are transmitted abroad. The information is sent in the form of a report and is coupled with a disclaimer of liability reminding foreign partners of their obligation to respect the principles of administrative cooperation.

(bank), in the event of a suspicious activity report ("**SAR**"), to improve the effectiveness of the reporting system[22]. As of today, the financial intermediary must freeze the assets relating to its SAR until it receives a decision from the MROS or the criminal authorities, which can take up to maximum 5 days. During that time, the financial intermediary is prohibited from informing the client of the SAR and of the freezing of the account[23].

Under the Bill, the freezing will only take place when the MROS communicates the suspicions to the competent criminal authority. A maximum deadline of 30 days will be set to the MROS for its analyses in order to limit the burden of the financial intermediary. If, during the time of the MROS' analysis, the financial intermediary suspects that contaminated funds could leave Switzerland (upon the client's instructions), it should alert the MROS and delay the execution of the transaction for five working days. If the MROS agrees with the transaction or does not reply within 5 days, and only in this case, the financial intermediary could execute the transaction.

### VII. Adoption of the Bill

The Bill now has to be validated by both chambers of the Swiss Parliament. It is likely that the Act will be adopted without too many amendments to avoid Switzerland's inclusion on the OECD gray list, which stigmatizes uncooperative jurisdictions in the drive for transparency of tax affairs and effective exchange of information. The entry into force of the Bill is expected for January 2016.

## In the Area of Taxation

### I. Enhanced Due Diligence Requirements

The second legislative consultation launched by the Federal Council on 27 February 2013 enshrined in the AMLA new due diligence requirements for financial intermediaries when accepting assets. They aimed at preventing the inflow of untaxed assets in the Swiss financial center[24].

The Federal Council did not want to impose on the financial intermediaries a general obligation to obtain self-declarations from the clients[25]. It rather proposed a risk-based approach, where financial intermediaries should use pre-defined risk indicators to make an assessment of the tax situation of the clients[26]. The procedure would be analogue to the due diligence requirements already imposed on financial intermediaries under the anti-money laundering rules. Besides, like the risk indicators for money laundering, the risk indicators for tax non-compliance would also be defined in the AMLA.

Concretely, where a financial intermediary would come to the conclusion that the assets of the client are undeclared, it should refuse the assets deposit. It should also verify that the assets already under custody are tax-compliant by, if need be, asking the client to straighten them within a reasonable timeframe. If the client refuses, the financial intermediary should terminate the business relationship. The duty to send a SAR to the MROS would be limited to cases where the assets are suspected to derive from predicate offences to money laundering.

During the consultation period, wide-spread criticism was expressed towards the draft from the part of all Swiss political parties and economic actors. In reaction, the Federal Council announced in November 2013 that it would review its policy and propose to apply the new due diligence requirements in the area of taxation only to those states with which no agreement on the automatic exchange of information ("**AEI**") would exist in a foreseeable future[27]. It indeed reckoned that such an international AEI standard will soon exist[28], which would enable Switzerland to conclude the necessary implementation agreements with its

22 - Proposed Art. 10 AMLA.
23 - Current Art. 10 and 10a AMLA.
24 - http://www.sif.admin.ch/dokumentation/00513/00772/index.html?lang=en&msg-id=47934.
25 - Swiss banks have already started requesting those tax compliance declarations from their clients (see http://www.tdg.ch/economie/UBS-exige-desormais-la-conformite-fiscale-/story/28019341; http://www.lemonde.fr/economie/article/2013/09/16/des-banques-suisses-veulent-des-clients-francais-fiscalement-en-regle_3478021_3234.html for their French clients).
26 - Increased risk would consist for instance of investments to be carried out in complex structures without justification or a client's wish for greater discretion. Whereas lower risk would arise where there is an international double taxation agreement between the client's country of domicile and Switzerland.
27 - For more information on the results of the consultation cf. http://www.admin.ch/aktuell/00089/index.html?lang=en&msg-id=51189.
28 - See OECD proposal to elaborate an AEI international standard by February 2014 presented to the G20 on 20 July 2013 (http://www.oecd.org/newsroom/oecd-calls-on-g20-finance-ministers-to-support-next-steps-in-clampdown-on-tax-avoidance.htm); see G20's approval of the implementation procedure among the G20 members by the end of 2015 (https://www.g20.org/sites/default/files/g20_resources/library/Saint_Petersburg_Declaration_ENG.pdf).

principal partner states. The Federal Department of Finance has therefore been instructed to submit a new proposal on the structure of the due diligence requirements, which will apply only to those clients domiciled in other states. The new requirements will be established on the basis of material interfaces already existing in the area of money laundering as foreseen.

## II. Automatic Exchange of Information

With its main partner states (i.e. members of the OECD, the G20 and the European Union), Switzerland should be able to conclude the necessary agreements for implementation of the AEI within two to four years. It already signed, on 15 October 2013, the OECD/Council of Europe Convention on Mutual Administrative Assistance in Tax Matters[29].

The European Commission as well as the OECD/G20 strongly support the AEI and want to implement it between national tax authorities as from 2015[30].

Within the European Union, only Austria and Luxembourg have resisted to the AEI by levying a retention tax in order to guarantee the privacy of their bank clients. The withholding tax solution was also favored by Switzerland[31].

However, the coexistence model that existed in respect of interest income in the EU Savings Tax Directive will disappear by 2015. Put under considerable pressure, Austria and Luxembourg indeed both announced in 2013 that they would apply the AEI to the EU citizens.

Under these circumstances, the Federal Council published in June 2013 its intention to cooperate actively, within the scope of the OECD, on the development of a global standard for the AEI in order to ensure the tax compliance of foreign asset management clients[32]. Such a standard should apply to all financial centers and incorporate rules to determine the beneficial owners of all legal entities, including trusts in Anglo-Saxon countries.

Recent developments in international tax law have therefore caused Switzerland to adapt its conservative approach regarding the exchange of information in tax matters and implement quickly a great number of reforms.

Another example is the enactment, following the adoption of the OECD minimum standard for administrative assistance set out in Art. 26 of the OECD Model Tax Convention in March 2009, of the Tax Administrative Assistance Act (RS 672.5), which enables the exchange of information with partner states upon receipt of group requests that do not name individual clients and regardless of whether or not there was a tax offence (which means also in assessment procedures)[33]. Switzerland also revised a number of its double taxation treaties to adapt the corresponding administrative assistance provisions to the OECD international standards[34].

## Conclusion

Swiss political authorities, together with the protagonists of the financial sector, consider that effectively preventing financial sector abuses is a prerequisite for a successful financial center. The Federal Council therefore attaches great importance to preserving the integrity of its financial institutions by continually expanding its anti-money laundering regulations and enhancing the due diligence requirements of the financial actors. Despite some adjustments still needed to enable a full implementation of the FATF Recommendations 2012, Swiss mechanisms in this area are already largely compatible with the international standards.

29 - The Swiss Parliament still has to ratify it. The project might also be subject to a referendum.
30 - The international standard should be inspired by the US Foreign Account Tax Compliance Act (**FATCA**), which should be implemented in Switzerland as from 1 July 2014. FATCA essentially requires foreign financial institutions to conclude an agreement with the US tax authorities, in which the institutions undertake to report information on US accounts. If the client does not agree, any sums paid to them from the US will be subject to a penalty tax of 30%.
31 - See the withholding tax agreements signed with the United Kingdom and Austria.
32 - http://www.efd.admin.ch/dokumentation/medieninformationen/00467/index.html?lang=en&msg-id=49287.
33 - This Act entered into force in February 2013. New proposed amendments to the Tax Administrative Assistance Act have to be approved by the Swiss Parliament (see http://www.efd.admin.ch/dokumentation/medieninformationen/00467/index.html?lang=en&print_style=yes&msg-id=50606).
34 - At the end of 2012, 44 double taxation agreements have been revised.

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