The Impact of the Swiss-EU Relationships on the Swiss Banking Secrecy

MASTER THESIS

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“The only obstacles that can not be bypassed and can not be avoided, indeed, are death and taxes.“

Nicolas G. Hayek

Swiss Entrepreneur

Abstract

Switzerland and the European Union share common values and have peaceful and well functioning economic and political agreements. Nevertheless, the Swiss banking secrecy is definitely a thorn in the EU's flesh, especially because of tax fraud or money laundering. Since the existence of the Swiss banking secrecy it has been associated with holocaust money, tax evasion, potentates' money etc. and also has been confronted with espionage attacks by foreign authorities and various other disputes. Recent global events have shed light on the Swiss banking secrecy's wider international agenda. A newly debate about the Swiss banking secrecy started with the global economic crisis and the Euro crisis. Finally, not a day goes by where there is no report or article in the media regarding the banking secrecy, the Swiss banks and its issues concerning the European Union or the United States. This writing focuses on the relationship between Switzerland and the European Union which is affected by Swiss banking secrecy: By explaining the history and importance of the Switzerland as a financial centre, its banking secrecy and the differences to other systems, possible issues and conflicts can be outlined. This thesis covers existing issues with EU member states. What regulations and restrictions were enforced by the Swiss government under pressure from international institutions or the European Union towards the Swiss banking secrecy or Swiss law due to international conflicts, issues and recommendations will be analysed.

Keywords: *Swiss Banking Secrecy; Swiss Banks; Bank Client Confidentiality; Tax Fraud; Tax Evasion; Switzerland; European Union; Bilateral Agreements*

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Abbreviations

AMLO FINMA	Anti-Money Laundering Ordinance of the Swiss Financial Markets Supervisory Authority
AMLA	Swiss Anti-Money Laundering Act
CDB	Swiss bank's code of conduct with regard to the exercise of due diligence
CHF	Swiss Franc
CS	Credit Suisse
DTA	Double Taxation Agreements
EU	European Union
FATF	Federal Task Force
FDFA	Federal Department of Foreign Affairs
FINMA	Financial Market Supervisory Authority
FTA	Swiss Federal Tax Administration
IRS	Internal Revenue Service
OECD	Organisation for Economic Co-operation and Development
PEP	Politically Exposed Persons
QI	Qualified Intermediary
SBA	Swiss Bankers Association
SFBC	Swiss Federal Banking Commission
SPC	Swiss Penal Code
SNB	Swiss National Bank

1. Introduction

The Swiss financial sector is highly important for the Swiss economy. Approximately one third of worldwide privately invested foreign assets are being managed or administered in Switzerland. Therefore it goes without saying that Switzerland has to be aware that its financial centre is not being abused for criminal activities such as money laundry or tax fraud. Despite the fact that since the 1990s regulations and law enforcement has been improved against money laundering, corruption and any other international criminality in connection with private assets, Swiss banks and therefore the government are being repeatedly accused of facilitating criminal activity. Switzerland and the European Union always have had an special relationship: Switzerland a democratic country known for its rural areas, cheese, chocolate, watches and its banks – situated in the heart of Europe, connecting the South with the North. With its four official languages German, French, Italian and Rhaeto-Romanic, it boasts a culturally and ethnically diverse demographic. Its relationship to the EU can be interpreted from well-functioning to contradictory. Switzerland‘s economy is one of the most competitive and stable on a global level. After the United States of America and People‘s Republic of China it is the third biggest trading partner of the European Union. Switzerland and the EU have a free trade agreement, insurance agreement and a so called “Bilateral I agreements“ and “Bilateral II agreements“. The most relevant aspects of those two agreements are the free movement of people, that the technical barriers to trade have been removed and the entrance to the Shengen/Dublin area.

Although Switzerland and the European Union share common values and have peaceful and well functioning economic agreements, the Swiss banking secrecy is definitely a highly disputed and considerably unwanted policy from the EU‘s point of view: International debates about the policies of the banking secrecy have existed since before the First World War. When economic crisis‘ occurred, the Swiss banks were targeted to give out sensitive information about their clients. The never-ending debate about the banking secrecy relaunched with the global economic crisis in 2008. when U.S. investment bank Lehmann Brothers collapsed and the economic crisis hit the United States of America badly. At that time, Switzerland‘s biggest bank, the UBS was enveloped in a tax fraud scandal. U.S. authorities accused the investment bank and wealth management departments of the UBS of helping U.S. clients to transfer their assets to Switzerland, hence giving them the opportunity to hide assets from the concerned authorities. In particular employees of the UBS helped, even encouraged South American and American citizens to put their assets into Swiss bank accounts to avoid taxation in their home countries. The authorities postulated that the Swiss government and the UBS give out the financial information of its various clients from

the United States and South America. U.S. authorities pressured Switzerland‘s government into the giving out of previously unobtainable financial information. So the UBS investment bank was forced to give out economic information of approximately 4‘500 bank accounts. The U.S. authorities claimed for more than 24‘000 accounts. The UBS paid the United States 780 million U.S. Dollars and agreed on the disclosure of a smaller number of account details. In Switzerland this case caused big debate that firstly the Swiss government is not sovereign enough and lost credibility, secondly it was argued that the Swiss banking secrecy was no longer secure and therefore guaranteed. This issue brought the debate of the Swiss banking secrecy also to the agenda of the European Union. Furthermore the alleged sale of a CD-Rom containing data implicating German nationals having undeclared bank accounts in Switzerland and so avoiding taxes in Germany increased pressure on the banking secrecy. According to the media the CD was sold from a former Swiss bank employee to the German authorities, which caused a wave of financial declarations across Germany. Whether the CD existed or not is not entirely clear as its existence has never been confirmed nor denied by German government or authorities.

In virtue of the economic crisis in the EU, Switzerland was considered as a scapegoat and also as a reason for the EU‘s bad economy because of the banking secrecy which arguably enables EU citizens to avoid paying taxes by putting their assets in Swiss bank accounts. One of the main activists against the Swiss Banking Secrecy was former Finance Minister of Germany Peer Steinbrück. He wanted to break the Swiss banking secrecy. He claimed that Switzerland has to be forced to adapt to EU regulations and cooperate in the fight against money laundering and tax fraud. He referred to the Swiss as Indians who should be put on the OECD black list. Switzerland‘s banking policy and therefore its banking secrecy became increasingly pressurised which caused many, especially foreigners to fear consequences from their governments for having money on Swiss bank accounts. It led to a money outflow from Swiss Banks – people literally preferred having their money under their pillows than in a Swiss bank account. At first the global and then the European debate regarding Swiss bank secrecy caused a loss of reputation and trust in the financial sector of Switzerland and its Banks. The international conflicts caused the government to change regulations and improve its legal measures. Despite the fact that the Swiss banking centre underwent a reputation crisis and major banks had to face lawsuits against international authorities, the Swiss financial sector and therefore its banks performed well under the given circumstances in comparison with other financial centres and remains as one of the most secure and stable.

2. Interest of research

The Swiss financial sector has been highly attractive not only for national, but also for international clients over the decades. One arguable factor is the Swiss banking secrecy and the client confidentiality. However, it has come under national and international criticism over the decades; Swiss banks and authorities have often been blamed to facilitate money laundering, tax fraud and other criminal actions because of the banking secrecy or simply they are given a competitive and economic advantage over their European counterparts. This thesis shows the reasons to why the banking secrecy to become such a disputed issue. It describes its origins, development and implementation into the Swiss constitutional law. The motivation and factors of creating a national regulation for banking secrecy will also be discussed. The Swiss-EU relations, its bilateral agreements and recent events or conflicts with the United States and EU Member States concerning the Swiss banking secrecy will be analysed. The main focus of the research is to show how the future idea of the Swiss banking secrecy differs within Europe, namely Switzerland and the European Union; how the banking secrecy has been affected by the European Union and vice versa. Additionally, the discussion as to whether future agreements or consensus can be achieved will be outlined.

2.1 Structure

The Swiss financial sector has been highly attractive not only for national, but also for international clients over the decades. One arguable factor is the Swiss banking secrecy and the client confidentiality. However, it has come under national and international criticism over the decades; Swiss banks and authorities have often been blamed to facilitate money laundering, tax fraud and other criminal actions because of the banking secrecy or simply they are given a competitive and economic advantage over their European counterparts. This thesis shows the reasons to why the banking secrecy to become such a disputed issue. It describes its origins, development and implementation into the Swiss constitutional law. The motivation and factors of creating a national regulation for banking secrecy will also be discussed. The Swiss-EU relations, its agreements, recent events and conflicts with the EU and the United States concerning the Swiss banking secrecy will be analysed. The main focus of the research is to show how the future idea of the Swiss banking secrecy differs within Europe, namely Switzerland and the European Union; how the banking secrecy has been affected by the European Union and vice versa. Additionally, the discussion as to whether future agreements or consensus can be achieved will be outlined.

2.2 Hypotheses & Approach

The goal of this thesis is to show how the conception of future banking and the idea of the Swiss banking secrecy differs between the European Union and Switzerland, and how this affects the Swiss-EU relationship. The general idea of the questioning and the hypotheses come from a clear position and support of the Swiss banking secrecy. The hypotheses state that the concept of the Swiss banking secrecy is often misinterpreted and associated in the wrong context. It can be seen as a tradition, a piece of Swiss culture which has been implemented into constitutional law. This piece of Swiss culture is simply not being respected by the European Union or the United States. In addition to that do European Law or the regulations of the member states indirectly favour the bank client confidentiality and therefore the Swiss economy. Finally, the European Union and in particular certain member states which repeatedly try to break or weaken the banking secrecy, violate Swiss sovereignty. In addition to that, its attempts do not achieve longterm results but even have the opposite effects.

The methodology of the thesis relies on qualitative approaches; since the issue of the Swiss Banking Secrecy can be hardly measured by quantitative means. Numbers and figures for instance of eligible undeclared assets or information of bank accounts are not accessible and protected by the bank client confidentiality hence it is highly difficult and simply illogical to work with quantitative methods. It does not mean that charts, figures and statistics will not be used to find significant results to the questioning. Qualitative methods such as a qualitative interview, or an expert interview are significant for the result of this writing. Additionally chronological analyses of different events and happenings will be taken into account, to clarify the issue objectively. In this way the constructed hypotheses can be verified or falsified. To summarise, the review of the world literature is the basis for the construction of the hypotheses and will finally be tested by the connection of expertise knowledge, statistics et cetera.

3. Chronological Analysis of the Swiss Banking Secrecy

3.1 Before the Second World War

From 1910 to 1913, as well as during the First World War, the Swiss financial centre was in deep crisis and banks were failing. Within a three year period from 1910 till 1913, 45 district or regional banks bemoaned losses of 112 million Swiss Francs which was at the value of the Swiss state budget in 1912. Other 28 banks merged either with a cantonal bank or with a major bank because of the economic situation. From 1906 to 1915 85 banking institutions were deregistered. The crisis in the period

before and during World War I which got banks into serious difficulties, caused the legislation and implementation of modern banking laws (cf. Vogler 2005: 11). The U.S. stock market crash 1929 and shortly after, the banking crisis in 1931, demanded further regulations of the banks. From 1926 Swiss banks went through a boom phase but on an international comparison with the big financial centres such as New York or London, as well as Paris, Frankfurt, Vienna or Amsterdam by that time, Switzerland was an insignificant player. Individual British, German and French banks achieved approximately the same balance sheet total as more than half of all Swiss banks together. The German banking crisis from 1931 affected the major Swiss Banks, which were involved in foreign business, negatively. Between 1930 and 1935, the eight major banks balance sheet total decreased more than 50% to a total of 4,2 billion Swiss Francs. One factor of this negative balance was the so called “bank moratorium“ in Germany, where more than 1 billion Swiss Francs were blocked and could not have been transferred due to the circumstances of the foreign exchange. Struggling major banks, “Bank Leu“ or “Die Schweizerische Bankgesellschaft“ were saved thanks to direct financial aid from the state or its shareholders. Nevertheless, banks which were highly involved in the German market had to undergo serious financial difficulties. With the fiscal- and foreign exchange policies of the National Socialists in Germany, these dire straits increased and were not possible to overcome- The “Basler Handelsbank“ as well as the “Eidgenössische Bank“ were taken over. In total, 60 banks were liquidated or taken over between 1930 and 1939 (cf. Vogler 2005: 12). These difficulties which the Swiss banks had to undergo led to the formulation and implementation of modern banking laws. The political discussion whether to create and manifest modern banking laws became more disputed. Talking of the banking secrecy, it is important to note that the banks and its employees already had a so called requirement of discretion concerning their clients and their accounts, that predated 1915. This kind of secrecy can be seen as an early form of banking secrecy which has not been implemented by any law but in fact has been regarded by the bank employees as something natural and given.

In 1922 the the formulation of banking laws were requested by Swiss farmers. After the First World War they demanded the implementation of modern banking laws. Their principal argument was that the outflow of capital from the major Swiss banks to foreign banks would increase the interest rates what would endanger their existence. The social democratic party on the other hand, suggested in their initiative of capital levy that the war debts could be lowered by a unique conscription of wealth. Therefore, all legal entities were obligated to inform the revenue authorities about their assets. In other words all monetary institutes had to undergo control measures by the

authorities which would have meant the opening of the banking secrecy. The initiative caused a capital outflow from Switzerland before the actual vote in 1922. The results showed a clear rejection of the initiative. The defeat of the social democratic party‘s initiative had a major impact for the future discussion about abandoning the banking secrecy – it vanished from the political agenda (cf. Vogler 2005: 17-18). The idea of the afore mentioned initiative was actually implemented in various European countries after World War I. A tax was introduced which would reduce the debts caused by all the expenses of war. Therefore officials were hired to spy and observe citizens of their countries. The main goal was to find out whether people had moved their assets to foreign countries to avoid the war tax. Swiss bank clerks were offered bribes to make them give out internal bank information about relevant clients. Even before the National Socialists were in power in Germany, there were various events between 1931 and 1932 where German officials tried to obtain possession of information over German clients, assets and deposits; Arthur Pfau, to name an example, in 1931 exposed bank clients of the “Schweizerischen Bankgesellschaft“. Pfau was reported to the police and deported by the foreign police. When the National Socialist took over the government in Germany, they introduced a law in June 1933 that Germans had to declare all their foreign assets and eventually face a minimum of three years imprisonment if they did not. The introduction of the law to collect the assets of enemies of the people and enemies of the state was fundamental to confiscating capital from Jewish people and politically oppositional citizens (cf. Vogler 2005: 20). The Swiss National Bank as well as the Office of the Attorney General of Switzerland considered those laws and attempts of espionage as serious violations of the Swiss sovereignty (cf. Ladd 2011: 541). Not only disputes with Germany over client information occurred but also with France. When in October 1932, two employees of the “Basler Handelsbank“ were arrested in Paris while meeting potential French clients, they were accused of helping them to avoid the coupon tax. The authorities confiscated a list with more than thousand names of French clients. The list included prominent names and caused a major domestic debate in France. It was followed by a cash outflow from Swiss banks by their French clients for a short period of time. With the change of government in 1936 there was a reflux of capital. Nevertheless, the incident in Paris barely affected the creation of a banking secrecy law and banking law, more the fact that again a major bank – the “Basler Handelsbank“ had gotten into serious difficulties. Apart from the “Basler Handelsbank“ another major Swiss bank got into a smiliar crisis. The “Schweizerische Volksbank“ was as well a victim of the German banking crisis in 1931. It resulted in an involvement of the state in the bank‘s cooperative capital to the amount of 100 million Swiss Francs. The state involvement

and thus the Swiss taxpayer stakes in the banks meant that the banking system had to be under visible and public control. Neither the right-wing or bourgeois parties nor banking representatives could longer be in favour of no banking control measures (cf. Vogler 2005: 27). In 1934 on the 8th November, the Swiss parliament voted in favour of the Federal Banking Act. The two chambers, Council of States as well as the National Council agreed on passing the law with one dissenting vote by a count of 119:1. Interesting fact is that the banking secrecy is only codified in Article 47 and was neither a disputed issue by the commission of experts nor by the parliament. Even the social democratic party did not request the elimination of the banking secrecy because they did not intend to endanger the complete banking legislation in virtue of one article. The whole political spectrum was in agreement about the necessity of a banking control authority. Therefore, the crisis of the mentioned Swiss banks gave the final push of the political and economic parties involved to agree and pass the Federal Banking Act, which came into force on the 1st of March in 1935 (cf. Vogler 2005: 25-27). The Swiss banking secrecy has very rationalistic origins with Jean-Marie Musy, who was Swiss Federal Council and Finance Minister from 1920 to 1934, a political supporter and father. It is important to note that the creation and implementation of the banking secrecy can not be explained by a minimum of factors. It can not be proven that the political side of the agricultural sector had agreed on the introduction of banking secrecy laws in exchange for subsidies from banks. As well, the idea of implementing the banking secrecy because of humanitarian aspects such as protecting the Jewish respectively their assets from the National Socialist regime in Germany can not be proven and are considered urban legends. The reasons for establishing the laws include repeated bad experience due to missing banking law in economically difficult times, as well as increasing espionage attacks by foreign governments and officials, finally accelerated by the endangerment of national security because of the National Socialists in Germany (cf. Löpfe 2010: 33-35). Even before the parliament had agreed to pass the Federal Banking Act in 1934 the Banking Secrecy existed as an unwritten law, which the banks relied on for decades. The economic crisis in the financial centres in Switzerland and especially the espionage forced the banks and authorities to establish a legal framework to ensure the security of their clients and their privacy. The main goal of introducing a national banking law was to protect the Swiss banks and the Swiss clients against further harm. As mentioned before, the Swiss banking secrecy or the bank client confidentiality was formulated in only one Article (Article 47) which protects the interests of the client and not the interest of the bank. Article 47 had not been further discussed or considered critical while passing the law. The Swiss banking secrecy as

we know it today was a beside article and was implemented as a law of privacy. Political disputes because of the banking secrecy existed already before World War II and thus the establishment can not be explained by Nazi atrocities; it can be explained by the wide political consent of the political parties, authorities or the government to regulate and protect the banks on a national level; the banking secrecy itself was a considerably small and undisputed aspect of the Federal Banking Act in 1934 and codified only in Article 47 1934 (cf. Vogler 2005: 30).

3.2 After Second World War

The Federal Banking Act and thus the banking secrecy came into force in 1935. Meaning that by the end of World War II the law had been active for ten years from which approximately half fell in the war period. This means that the banking secrecy barely could have plaid a significant factor for the attractiveness of the Swiss financial- and banking sector, especially at that time. Nevertheless Switzerland and its financial centres have been often associated with holocaust money, money laundering, tax fraud, tax evasion, etc. and that arguably because of the infamous Swiss banking secrecy. The independent Swiss Experts Commission of World War II concluded that European citizens transferred their liquid assets to Swiss banks already in the 1920s respectively 1930s. Europeans feared inflation, expropriation, political insecurities, war etc. Switzerland was a reasonable choice to transfer the assets: The country had never been involved in any severe international conflict or war; it has always maintained its traditional neutral political position; its geographical position is in the heart of Europe and thus the international image of the financial sector was considered positive. Since World War II Switzerland kept those positions up to now and for a long period of time a process of trust building and finally a credence relationship between the Swiss banks and its clients could have been implemented. To build such a trustful relationship Vogler differs between primary and secondary factors which caused the success of the financial sector and its banks in Switzerland (cf. Vogler 2005: 32).

Primary factors:

- political stability and legal security
- stability of the economy as well the currency
- stability of the banking system
- free convertibility of the currency

Secondary factors:

- globalisation degree of the economy and the banks
- banking secrecy
- experience of the clients
- professionalism of the service (cf. Vogler 2005: 32)

After World War II the banking secrecy had been established for ten years. The uncertainties of war and the economic instability in Europe, especially in Germany and France caused people to move their assets to Switzerland for the before mentioned reasons. It gave the Swiss banks and its financial sector a good reputation. The banking secrecy was a factor which ensured the peoples privacy about their assets but whether it plaid a major role is arguable. The following chapter shows how the banking secrecy had been implemented into law and how it was adapted on different legal basis to this day.

4. Swiss Banking Secrecy

4.1 General Basis

It is accepted that basically all financial centres and its authorities have a banking secrecy, basic laws and regulations that protect the individual or client information from any third party. The clients data and its transactions are treated as protected private information. The significant difference between countries and their banking secrecy is the level of client confidentiality. What information is shared with whom under varying circumstances. The clauses and regulations under which sensitive information is kept or shared and which instances have the right to seek the data, e.g. tax authorities, money laundering related authorities etc differs from country to country (cf. Aggarwal et al. 2009: 2). The Swiss financial sector or the Swiss banks have the tradition of keeping the information about clients assets private. Under no circumstance, especially not state influence, can access be allowed to pecuniary circumstances of individuals, private organisations or economic enterprises. Except if there is a public interest or a higher private interest in case of alleged unlawful actions. The assets deposited at the banks, its connected transactions as well as the personal information of the clients are legally protected by the banking secrecy. On international comparison Switzerland holds a privileged position and because of that is often accused of profit mongering and dubious business deals (cf. Mueller 1998: 15). The inclusion of the banking secrecy in the banking law in 1934 signified that in addition to the existing private law professional secrecy, violation would consequence

criminal sanction. As previously mentioned was it necessary to create for the authorities, as well as the banks, a legal basis on a national level with the purpose of protection of clients despite their origins. This was due to the repeated espionage incidents towards foreign clients, the international threat and the political and economic uncertainties. The banking secrecy which actually should have been named bank client confidentiality has been mistakenly associated as preventive measure for the prosecution of the Jews. Truth is that it is connected with the implementation of the Federal Banking Act which its creation can be clearly explained by political and economic events. Many of these events already occurred before the time of National Socialist regime in Germany (cf Föllmi 2001: 12).

The banking secrecy as we know it today relies on various articles, not only from the Federal Banking Act but also Swiss Federal Law on Banks and Savings Banks and the Swiss Code of Obligations, the Swiss Civil Code and Federal Data Protection Act. The protection of the individual privacy is basis for the banking secrecy. Secondary the different laws are a public protection against violation of the banking secrecy. The following chapter shows how the banking secrecy is constructed and implemented by the different Swiss laws and regulations.

4.2 Legal Basis

4.2.1 Private Law

Touching upon the individual privacy and the banking secrecy; in all western states the protection of secrets of an individual is a basic legal aspect and guaranteed. In Switzerland this is assured by law of the Swiss Civil Code Article 27 and Article 28 (cf. Schweizerisches Zivilgesetzbuch 1907: 6-9), stating that originator of the secret, the original entitled person or the initial secret keeper are assured of protection of their secrecy. This legal basis is a legal asset for the individual. It is the judge's task to interpret from private law about content and scale of a secret. Should there be damage or a violation of the secrecy from a third party involved and with consent of the secrecy, the originator of the secret has to be compensated in virtue of Article 41 of the Swiss Code of Obligations and in addition served satisfaction according to Article 49; for auxiliaries the bank is liable, Article 101 (cf. Bundesgesetz betreffend die Ergänzung des Schweizerischen Zivilgesetzbuches (Fünfter Teil: Obligationenrecht) 1911: 27) (cf. Mueller 1998: 60-61).

4.2.2 The Federal Banking Act

The from the 8th of November 1934 Federal Banking Act is still valid in Federal law of Switzerland and called the Federal Act on Banks and Savings Banks (12.3.2012). The banking secrecy itself is codified in Article 47 and quoted in the version of the Swiss Financial Market Supervisory Authority Laws which came into force on the 1st of January 2009 (cf. Bundesgesetz über die Banken und Sparkassen 1934: 30-31):

Art. 47

1 Imprisonment of up to three years or fine will be awarded to persons who deliberately:
   a. disclose a secret that is entrusted to him in his capacity as body, employee, appointee, or liquidator of a bank, as body or employee of an audit company or that he has observed in this capacity;
   b. attempts to induce such an infraction of the professional secrecy.

2 Persons acting with negligence will be penalised with a fine of up to 250'000 francs.

3 In the case of a repeat within five years of the prior conviction, the fine will amount to 45 day rates at a minimum.

4 The violation of the professional secrecy also punishable after conclusion of the licensed or official responsibilities or the professional exercising duties is punishable.

5 The federal and cantonal provisions on the duty to provide evidence or on the duty to provide information to an authority remain reserved.

6 Prosecution and judgment of offences pursuant to these provisions are incumbent upon the cantons. The general provisions of the Swiss Penal Code are applicable (cf. Bundesgesetz über die Banken und Sparkassen 2012: 30-31)

Article 47 applies mostly in cases where the protection of private law is not sufficient. It occurs especially abroad when secret keeping instances are forced under political pressure to reveal involuntarily the secret information. Violation of the Article 47 includes bank employees, corporate and executive bodies after their professional career. Foreign banks situated in Switzerland underlie the same regulations. Therefore, the banking secrecy becomes a public duty of bank bodies to protect their professional secrecy. It is important to note that the banking secrecy can not be a barrier of higher legal interests (cf. Mueller 1998: 66)

4.2.3 Contract Law

The general conditions of the banks include explicitly the information that the banks commit to their clients to preserve the banking secrecy. It does not change the fact that the banks are obliged to keep the banking secrecy even without the explicit notation in their general conditions. The concealment by the banks of their client's information is an accessory obligation of the banks; it is based on two different articles. Firstly Article 398 (2) of Swiss Code of Obligations which obligates the mandated bank to secrecy (cf. Bundesgesetz betreffend die Ergänzung des Schweizerischen Zivilgesetzbuches (Fünfter Teil: Obligationenrecht) 1911: 153). Secondly Article 27 and 28 of the Swiss Civil Code which stand for the protection of the individual rights (cf. Schweizerisches Zivilgesetzbuch 1907: 6-7). In the sense of the relationship between the bank and its client, it means that the bank is obligated to confidentiality concerning the specifics of the relationship together with the assets which both belong to the privacy of an individual. Hence, the banking secrecy is under the purview of Article 28 of the Swiss Civil Code and included in the secondary obligations of the contract law (cf. Emmenegger et al. 2009: 203).

4.2.4 Data Privacy Act

With the data privacy act which came into force in 1993 the protection of banking secrecy reached another dimension; the data privacy act is the more general law but sustains the banking law in crucial aspects. Article 12 up to Article 15 contain rules on how private individuals have to process personal data. The term of "process" includes the procurement, retention, utilisation, processing, conversion, disclosure, archiving and destruction; every individual has a legal entitlement for protection of their personal information and data. Article 3 of the data privacy act further diversifies "highly protected personal information" such as religion, race, political activity, criminal prosecution or health (cf. Bundesgesetz über den Datenschutz 1992: 3). Not included in the type of "highly protected personal information" is data about the personal income or wealth and thus in general the financial circumstance (cf. Mueller 1998: 71). Banks are considered as private individuals in the data privacy act and hence have to process the data of clients according to the data privacy act. Article 6, 10a 12 and 13 of the data privacy act determine the publication of sensitive personal information and are germane for the protection of confidential information of banking-related data of clients. Article 6 states that personal information can not be disclosed abroad if the identity of the person concerned was seriously endangered (cf. Bundesgesetz über den Datenschutz 1992: 3-8). In addition Article 10 determines the premises of the process or transfer of personal data to a third party. Article 12 explicates that the

disclosure of “highly protected personal information“ or personality profiles to a third party would go against law if it can not be based on a permissible justification (cf. Bundesgesetz über den Datenschutz 1992). Personal data can only be transferred from a bank abroad with the explicit consent of the client. Without the consent, the bank can only transfer the personal information after rendering the data anonymous or process the data within Switzerland (cf Emmenegger et al. 2009: 204). In that sense, banks are obligated for functioning organisation dealing with data because of the banking secrecy respectively the data privacy act (cf. Mueller 1998: 73).

4.2.5 Supervisory Body

The banking supervision law includes regulatory body to oversee the banking secrecy. This aspect the Swiss banking law, in accrodance with Article 3 request that the banks have proper organisational structure from its leaders which means that management must operate faultlessly in this regard (cf. Bundesgesetz über die Banken und Sparkassen 1934: 3). The organisational risk of a violation of the banking secrecy or the implementation of these risks, belong to the area of competence of the Swiss Financial Market Supervisory Authority (FINMA). On the other hand the binding decision whether Article 47 of the Federal Banking Act is respected or fulfilled and its consequences in case of violation in an individual case, fall in the area of competence of a criminal judge. Hence, the supervisory body the FINMA, its regulations and measures are strengthening the protection of the banking secrecy. Nevertheless, it does not provide a direct legal basis for the secrecy protection. In a specific area the FINMA has regulated the dissemination of data: if a bank externalises a business branch and this consequences a transfer of client data to the external branch the bank has to follow specific regulations of the FINMA. These include the keeping of the banking secrecy and refer to Article 3 of the Federal Banking Act which state that the supervisory body can present their view of the banking secrecy and request from the bank to follow the measures of the view of supervisory body, the FINMA (cf. Bundesgesetz über die Banken und Sparkassen 1934: 3). Article 3 itself does not provide further legal basis for the protection of the banking secrecy (Emmenegger et al. 2009: 205).

4.3 Legal Measures against Criminal Activity

4.3.1 General Regulations

The Swiss banking secrecy and thus the bank client confidentiality which is a more suitable term in the way that it protects the client and not the bank, serves to protect individual privacy. In any case of criminal abuse, protection of the privacy does not

apply. Enquiries of prosecution authorities must be obeyed by the banks. With newly introduced definitions of a criminal offence, banks are obligated to disclose data; the most recent cases being insider trading in 1988 or money laundering in 1990. The Swiss banks are also obliged within the procedures of international administrative and legal assistance to provide sensitive data to foreign prosecution authorities (cf. Der schweizerische Bankensektor 2010: 68-69). The bank client confidentiality does not apply in every case, in other words if a client should be involved in any criminal activity. In other particular cases banks are obligated to provide information of clients:

- in civil action suits (e.g. inheritance or divorce),
- in debt collection or forced liquidation proceedings,
- in criminal suits (e.g. money laundering, involvement in a criminal organisation, theft, tax fraud, blackmail, etc.),
- proceedings under international administrative and legal assistance (cf. Der schweizerische Bankensektor 2010: 69)

Tax fraud is a specific case and is differentiated in the Swiss legal system. Tax evasion and tax fraud are legally two different terms, unlike in the European Union. To protect individuals the differentiation is made and relies on the concept of self-declaration (cf. Föllmi 2001: 13). Swiss Bankers Association (SBA) declares that Switzerland assumes every individual citizen having personal responsibility to follow the tax liability towards the state and not its bank. The Swiss banks are not obliged to inform the state or the tax authorities of the amount of interest which is credited to the clients bank account. This definition corresponds to the principles of self-declaration (cf. Perroulaz 2008: 127). Tax evasion are omissions and errors which occur in individual declarations of income and assets and are not considered or do not constitute a criminal act. Nonetheless tax evasion can be punished in form of a penalty. The amount of the fine is depending on the amount not being declared and will be a multiple of that. If tax declaration documents should be forged it is deemed as tax fraud and thus is a criminal act subject to criminal prosecution. This differentiation between tax fraud and tax evasion was affirmed by a public referendum which in Switzerland was a result of direct democracy. The differentiation is also ingrained in Swiss legal tradition. It is based on a mutual trust and respect between the Swiss people and the government and authorities and is considered an essential feature of Swiss comprehension of state governance (cf. Der schweizerische Bankensektor 2010: 69-70).

In cases with foreign authorities, Switzerland provides mutual legal assistance. Article 1 of the Federal Act on International Mutual Assistance states the international cooperation in criminal actions (cf. Bundesgesetz über internationale Rechtshilfe in Strafsachen 1981: 1) In the sense of mutual legal assistance in banking matters, assets may be frozen or handed over to the foreign authorities concerned, depending on the case information may be exchanged. The Swiss law bases its international mutual assistance in criminal activity on the principles of speciality, proportionality and most importantly dual criminality. The bank client confidentiality will be lifted as a coercive measure by Swiss courts, only in the case where the action of the investigation violates laws in both Switzerland and the requesting country (this stated the dual criminality rule). Secondly, the proportionality rule which serves to guarantee that discretion is exercised in case the proceedings adversely affect a third party or individuals which are not directly involved; additionally the assurance that the measures sought in conducting the request for assistance are in proportion to the crime itself. Last, the speciality rule which determines that any collected information through the mutual assistance arrangement can only put to use in criminal proceedings if mutual assistance is granted (cf. Der schweizerische Bankensektor 2010: 70)

Assets which belong to dictators or potentates are assets which were acquired illegally by politically exposed persons (PEP), defines the FINMA Anti-Money Laundering Ordinance. The money unlawfully obtained in the concerning country is often reinvested in the international financial centres. With the money taken out it creates a problem for the economic development as well as a reputation problem of the Swiss financial centre. Therefore, it is only logical that Swiss government prevents that such money is being invested in the banks. Switzerland will provide legal assistance in case unlawfully obtained money may have ended up in Swiss banks and so facilitate the process of unbureaucratic and effective restitution (cf. Der schweizerische Bankensektor 2010: 71).

The Financial Action Task Force (FATF) a key organisation in the fight against the financing terrorist activities as well as money laundering, created in cooperation with the banking industry 49 recommendations or international standards of preventative measures against the aforementioned issues. The FATF and the Organisation for Economic Co-operation and Development (OECD) are the most important international co-ordination departments in the realm of money laundering. Switzerland respects and obeys these international standards, is a member of the FATF since 1989 and bases their preventative measures on them (cf. Perroulaz 2008: 129-130). Switzerland itself passed with the Swiss Anti-Money Laundering Act (AMLA), giving it its own

regulations on combating money laundering and terrorist financing in the financial sector on the 10th of October 1997. It relies on the FATF standards, where Article 1 respectively Article 2 state that financial intermediaries are obliged to identify assets of potentially criminal origin and report such assets to the anti-money laundering agency (cf. Bundesgesetz über die Bekämpfung der Geldwäscherei und der Terrorismusfinanzierung im Finanzsektor: 1997: 1-3). A crucial method for international legal assistance is the restitution of potentates‘ assets. Mutual legal assistance is an important instrument for combating potentates’ assets. For over 20 years Switzerland has addressed the issue of restitution and is the only country which has done so. In that period of time, approximately 1.7 billion Swiss Francs (CHF) of frozen, blocked assets have been returned to the countries concerned. Nevertheless, there have been various cases where legal assistance has become ineffective, especially when the governments concerned are not willing or unable to cooperate. The blocked assets of Mobutu Sese Seko former president of the Republic of Congo were unblocked by the Federal court in July 2009 because of the lapse of time. In December 2008 the Swiss Federal Council authorised the Federal Department of Foreign Affairs (FDFA) to constitute a bill which should prevent such cases such as the Mobutu‘s. The bill should cover the issues of confiscating, collecting and restoring unlawfully obtained assets. The law should finally ensure that the assets will be restored and be addressed and in the end benefit the people of the countries concerned. The bill‘s consultation closed in spring 2010 (cf. Der schweizerische Bankensektor 2010: 69-71). Switzerland committed on an international level for the fight against corruption and embezzlement and the restitution of public assets. Switzerland and its government has organised international government meetings since 2001 which take place in Lausanne. In the meeting key representatives of major financial centres would come together with representatives of Eastern and Southern countries to find solutions and regulations to enforce restitution of illegal assets. Further cooperations with various institutions such as the United Nations Office on Drugs and Crime (UNODC), the World Bank since 2007 and the International Center for Asset Recovery (ICAR) from 2006 on concludes the list (cf. schweizerische Bankensektor 2010: 69-71).

4.3.2 International Agreements on Tax Regulations

In 2007 the Swiss Parliament passed treaties with Mexico and Brazil in order to cooperate in case of criminal actions. Other treaties with Latin American countries are either already ratified or being discussed. The government stated that it has not planned to extend special agreements to other countries which are in particular agreements with the European Union or the United States (cf. Perroulaz 2008: 128).

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Touching upon the cooperation with the European Union, Switzerland signed two Bilateral agreements with the EU. Bilateral I agreements in 1999 and the more recently Bilateral II agreements on the 26th of October 2004. The first set of agreements covers important political domains such as asylum, culture, environment and security. The scope of these domains is extended by Bilateral II agreements and includes further economic interests regarding the financial sector, tourism and mutual legal assistance. Agreements on combating fraud, capital income taxation as well as the Schengen/ Dublin Agreement are of significant importance to the Swiss financial centre. For Switzerland it was the highest priority to keep the bank client confidentiality safeguarded under all agreements. The agreement on the taxation of savings income between Switzerland and the EU came into force on 1st July 2005. An introduction of a system which secures taxes for the EU member states, an automatic exchange of information has been implemented by the Swiss government. This system does not affect the bank client confidentiality (cf. schweizerische Bankensektor 2010: 72). The system of securing taxes involves the voluntary declaration of interest payments and tax retention. It means that Switzerland provides an effective taxation guarantee for the EU; by respecting all savings interest payments made via paying agents in Switzerland to individuals liable to pay tax in the EU. The system is also applicable to debtors outside the EU and their interest payments. However, it excludes the interest payments which have its source in Switzerland and are contingent on Swiss withholding tax (cf. schweizerische Bankensektor 2010: 72). The agreement on taxation of savings income in 2005 also includes an incremental tax rate. It started with a rate of 15% which was increased in 2008 until June 2011 to 20%, thereafter to 35%.If authorised by the beneficiary of the interest payments, in lieu of tax retention in Switzerland they can be reported to the tax authorities at the beneficiary's country of residence. (cf. Der schweizerische Bankensektor 2010: 72). The agreement with the EU on the taxation of savings income forced the Swiss banks to make great efforts and caused them substantial costs in order to fulfil the requirements and implement all necessary adjustments by a given time. The amount of gross revenue from Swiss withholding tax on savings income of individuals which are taxable in the EU was CHF 738.4 million in 2008. 25% of this revenue was retained by Switzerland to cover the expenses. The majority and thus 75% is directly going to the EU and is paid to the EU member states. In 2008, approximately 43'000 savings income declarations were voluntarily made. With the goal to close certain loopholes the EU is currently revising the regulations and guidelines on savings income taxation. The target is to revise the field of life insurance and structured products, investment funds and the taxation of securities-like claims, which so far have not been considered in taxation. The usage of

a legal entity as an intermediary as well should no longer be possible for private individuals. On the other hand, during renegotiations between Switzerland and the EU will the Swiss Bankers Association demand a reduction of the current maximum tax rate of 35% (cf. Der schweizerische Bankensektor 2010: 72). In June 2005, the Swiss people had agreed to join the Schengen/Dublin area. The agreements included a reduction of border control and the continuing and closer cooperation in asylum legislation and police work. For the banking sector the agreements are only relevant in legal assistance in criminal cases. Since the Schengen/Dublin is a dynamic agreement, Switzerland has maintained an opt out clause in case of an extension of legal assistance provisions which apply to direct taxation. It means that Switzerland does not have to follow newly implemented provisions concerning direct taxation and still remain a party of the agreement. A part of the Bilateral II agreement is the agreement on combating fraud. It has been implemented in Switzerland since April 2008 although not all EU member states have adopted it. The agreement serves the further administrative and legal assistance in indirect taxation matters, such as tax fraud or serious tax evasion. Switzerland has granted the EU authorities the same instruments as in domestic proceedings. Those measures (hearing of witnesses, inspection of bank accounts, house searches) apply not only for tax fraud but also for tax evasion. In order for a premise to be searched a judicial search warrant is needed. In addition to that, the amount of the offence must be larger than 25‘000 Euros. This only applies for indirect taxation. The principle of speciality remains that in direct taxation proceedings, the information gathered because of the legal assistance arrangement can not be used (cf. Der schweizerische Bankensektor 2010: 73). The Swiss government has recently signed an agreement with Germany, Great Britain and Austria on the revision and the renewal of their tax agreements. Other revised agreements with Italy or France can be expected in the near future. The concept of the revised tax agreement was approved by the Economic Commission of the Council of States of Switzerland on the 15th of May 2012. Also approved were the international regulation on withholding tax, which regulate the enforcement and implementation of the agreements within Switzerland. However, the Commission explicitly postulated that foreign authorities are not entitled to do any examination or investigations, which was decided unanimously. The agreements and the law have to be approved by the chambers of the Swiss parliament as well as the parliaments of the respective countries. The Swiss Federal Council sees the agreements as alternative to an automatic exchange of information of client information. With the agreements, the foreign tax authorities would receive the amount of tax they are entitled to, without the bank client confidentiality being affected. If all, the domestic and foreign parliaments

approve the agreements, undeclared assets and future income from capital investments of British, Austrian and German clients will be taxed at a flat-rate. These lump sum amounts will be anonymously transferred to the foreign authorities. The agreements propose different tax rates for the three countries according the respective taxation systems, for Great Britain and Germany 21-41%, for Austria 15-38%. Taxation rate for future income from capital investments amounts for Austria 25%, Germany 26,375% and ranges for Great Britain from 27 to 48%. The agreements go into effect on the 1st of January 2013 (cf. Tax Agreements I 2012).

Another agreement which Switzerland is having with 73 countries, including all major industrialised states, is the double taxation agreements (DTA). This is to prevent double taxation, meaning that income and assets are not being taxed in two different countries. This principle applies for private individuals with different domiciles in different countries or companies which are situated in more than one country (cf. Der schweizerische Bankensektor 2010: 73). With Switzerland being a founding member of the OECD it follows the international standards and participates in the agenda of the OECD covering financial markets, economic policies, structural policy, health and tax. In tax matters, the OECD sets the worldwide standards, guidelines and regulations. The OECD proposes to its 30 member states a model for double taxation agreements. The model should neither be applicable law nor effective law, it is simply a template which different countries can base their international agreements on. The template contains 31 Articles which regulate certain taxation issues (cf. Perroulaz 2008: 130-132). Article 26 of the Model Tax Convention on Income and on Capital discusses the regulation of mutual assistance in exchanging information between the tax authorities of the concerned contracting states (OECD 2010). The Federal Council decided on May 13th 2009 to adapt the Article 26 of the OECD model and its regulation on mutual administrative assistance in tax matters. Mutual assistance in tax matters was from then on guaranteed by the Swiss authorities, not only in tax fraud but also in tax evasion cases. To implement the Federal Council‘s decision, the DTA have been adjusted to the certain standards. With the introduction of Article 26 there was no change for the bank client confidentiality hence was not affected. The DTA with countries which have been adjusted to the OECD standard respectively with Article 26, Switzerland provides an exchange of information only upon request and not automatically. Administrative assistance is only provided if certain conditions are fulfilled (cf. schweizerische Bankensektor 2010: 74):

the foreign tax authority has to submit a request in writing, stating an adequately reasonable suspicion;

the request must include a specific reference to the identity of the person liable to tax;
the facts of the tax evasion case have to be adequately described;
the bank or branch concerned has to be specified (cf. Der schweizerische Bankensektor 2010: 74).

Should the individual liable to tax, disagree with the decision to provide administrative assistance, there is the possibility to file a complaint to the Federal Administrative Court (cf. Der schweizerische Bankensektor 2010: 74).

4.3.3 Combating Money Laundering

Over the past years, Swiss authorities have implemented different preventive measures to fight money laundering and organised crime. On one side the government has implemented regulations and institutions, the Federal Act on the Prevention of Money Laundering in the Financial Sector which came into force on the 1st April 1998. Second the Anti-Money Laundering Ordinance of the Swiss Financial Markets Supervisory Authority (AMLO FINMA) and last Swiss Penal Code (SPC). On the other side are the banking institutions; it is in the banks own interest to ensure their services not being abused or misused. The Agreement on the Swiss bank‘s code of conduct with regard to the exercise of due diligence (CDB) discusses the banks‘ self-regulation and plays significant part in the fight against money laundering. The Anti-Money Laundering Act (AMLA) is relevant to all financial intermediaries who accept assets from a third party for instance banks, insurance companies, attorneys, wealth managers, fund managers, property managers, securities traders et cetera. The AMLA is based on the former Swiss Federal Banking Commission (SFBC) Anti-Money Laundering Ordinance and the CDB; its implementation is founded on self-regulation and direct public supervision by the AMLO FINMA. It obligates all financial intermediaries to register every case of justified suspicion of money laundering to a federal control authority. Money brokers, trustees, finance companies and wealth managers so far have not been publicly supervised thus have united themselves to self-regulatory associations. Comparably with the CDB for banks these associations had to create regulations which could meet the legal requirements (cf. Der schweizerische Bankensektor 2010: 75). In 2003 the Anti-Money Laundering Ordinance of the SFBC came into force which is today known as FINMA. The ordinance was revised in 2008 to meet not only the standards the FATF, but also the 9 special recommendations against financing of terrorist activities. Guidelines against assets belonging to politically exposed persons and money laundering have been tightened and extended with the area of financing of terrorist activities. A systematic

and electronic global monitoring of high-risk business relationships is demanded by the Anti-Money Laundering Ordinance of the SFBC and the FINMA (cf. Der schweizerische Bankensektor 2010: 75). Under the terms of Article 305bis of the SPC, “punitive measures for any action designed to obstruct investigations into the origin or location, or prevent the confiscation of assets, if such assets are known or must be assumed to be proceeds from a crime“ (cf. Schweizerisches Strafgesetzbuch 1937: 120). “Professional financial intermediaries are statutorily obliged to apply the “know-your-customer” principle. Insufficient identity verification of a contracting partner or beneficial owner is deemed an offence“ and “financial institutions are allowed to report to authorities any observations leading to the conclusion that assets originate from a crime. Such reporting does not constitute a violation of bank client confidentiality“ states Article 305ter (cf. Schweizerisches Strafgesetzbuch 1937: 121). Articles 322ter up to 322octies name the penal provisions for corruption. Strictly punished is the act of active or passive bribery among Swiss officials as well as the preferential treatment because of offering or accepting a bribe from foreign or domestic officials (cf. Schweizerisches Strafgesetzbuch 1937: 128-139).

Talking of the self-regulation of banks, the agreement on the code of conduct regarding the exercise of due diligence (CDB) plays an important role combating money laundering. The CDB came into force in 1977, long before the AMLA and before the inclusion of relevant provisions in the SPC. In five-year intervals the CDB is revised, last in 2008. The CDB‘s core elements are the duty of financial intermediaries to verify the identity of their contracting partner or the beneficial owner. The details of the CDB determine how to proceed the identification and what documents have to be examined. Other core elements of the CBD are the prohibition to assist or help in the flight of assets from countries where it is restricted to place cross-border investments and the prohibition of banks to assist actively in tax evasion or similar actions by issuing incomplete statements. The FINMA, as well as the banks mandate statutory bank auditors to control the compliance with the CDB. Possible violations against the CDB are being judged by the independent CDB supervisory body as well as designated inspectors. Fines up to a maximum of CHF 10 million can be imposed. The fines cover the expenses. The remaining amount is donated to Red Cross (cf. Der schweizerische Bankensektor 2010: 76). Non-Governmental Organisations often accuse Switzerland and its banks of allegedly manage large amounts of illegal flight capital from developing countries. There have been cases where Swiss banks have been beneficiary of flight capital but in those cases, there has always been the effort to return the money to the concerned countries. In addition to that those accusations are often based on non-existing or unreliable statistics (cf. Chaikin 2005: 106).

Last but not least the significant role of the Financial Action Task Force (FATF). The FATF includes 35 nations from which Switzerland is one of its founding members since 1989. At that time the FATF was created to give an overview of international anti-money laundering cooperation forms and work on measures against the issue of money laundering. The main goal of the FATF today is to combat money laundering by establishing international standards and guidelines to prevent money laundering and financing of terrorist activities. Therefore, the FATF monitors its member states at regular intervals whether they meet 40 recommendations and 9 special recommendations or the status of implementation of the recommendations. The 40 recommendations have been revised in 2003 in order to cover new forms of crime in the areas of financing terrorism and money laundering. The catalogue of measures has been repeatedly expanded in the area of financial and stock exchange offences that may predicate money laundering. In April 2005 Switzerland has been reviewed for the third time after 2001 and 2004. The review resulted positively. The FATF has acknowledged Switzerland‘s leading role in the fight against money laundering. It is important to note that first FATF‘s recommendations were based on the CDB. After their revision in 2003 the Swiss Federal Council announced to adapt Swiss legislation to fulfil the FATF‘s recommendations. In 2005 the draft of the Federal Council expanded the range of predicative crimes to money laundering and extended the group of entities that are subject to the AMLA. In addition should the need for exchange of data among authorities that are involved in fighting money be addressed in the AMLA. Further the draft proposed to holders of bearer shares to disclose their shares to the respective companies. The proposal was criticised by the Swiss Bankers Association and generally by the financial centre as a whole. As a result a more moderated version of the AMLA detailed which came into force on the 1st of February 2009. The revised version of the AMLA has been approved by the FATF although certain aspects regarding the transparency with regard to bearer shares and the implementation of international standards for blocking assets generated through terrorist activities and the effectiveness of the reporting system for suspicious activities have been criticised. Since the review in 2005 by FATF the international supervision of Switzerland has terminated because of reaching the 3rd cycle of the worldwide evaluation process. It means for the future that Switzerland is one of the first countries which is being evaluated in a two year interval in a simplified procedure along with Italy, Great Britain and Norway (cf. schweizerische Bankensektor 2010: 77).

4.4 Ethical Aspects of the Banking Secrecy / International Conflicts

It is clear that the Swiss banking secrecy creates various moral and ethical grey areas. Generally speaking, the most relevant cases are regarding tax fraud or tax evasion, money laundering, managing of potentates‘ assets et cetera. To repeat Swiss law differentiates tax fraud and tax evasion and thus does not assist in every request of information exchange by foreign authorities. It is argued that more than a third (30-40%) of all offshore invested assets are being managed in Switzerland which is estimated CHF 4000 billion. Statistical projections claim that approximately 70-90% of those assets are not declared in their domestic countries and hence not taxed (cf. VBG Institut 2006: 3). For retaining of dormant assets, in case of Holocaust Money or the theft and administration of state capital or potentates‘ money of developing countries, Swiss authorities and banking institutes have often been blamed. In the previous chapters certain issues have been outlined (see Chapter 4.1, 4.2, 4.3). This subchapter will focus on ethical grey areas by presenting different facts and positions which occurred during international conflicts between Swiss banks, authorities and other jurisdictions, namely the European Union, the United States, developing countries or victims of the Holocaust. Ethical grey areas occurred on micro, meso as well as on macro level. The end of this chapter gives an overview of moral and ethical aspects of the Swiss banking secrecy and its polemics.

4.4.1 United States vs. UBS

The homo economicus, the concept of rational, self-interested and selfish individuals which base their decisions on maximising economic benefits for themselves applies in the following case on the micro level. (cf. Gaus 2008: 19). There is moral conflict of bank employees; bank employees often get a percentage of the clients‘ assets they acquire. So it occurred in the United States in 2008 that employees of the largest bank in Switzerland the UBS, not only encouraged and also helped U.S. clients to transfer their assets to offshore bank accounts of the UBS in Switzerland to bypass the status of a Qualified Intermediary (QI) which is a direct agreement between the U.S. and the banks to exchange and report information of the clients to the U.S. Internal Revenue Service (IRS). So basically, the UBS helped American citizens in tax evasion matters (cf. Missbach 2009: 116). The UBS tax fraud case started in 2007, when Igor Olenicoff was found guilty of criminal tax fraud in connection with offshore bank accounts managed by a UBS private banker. The information which was obtained by Bradley Birkenfeld, the former UBS private banker, the IRS started to build a case. After various arrests and hearings of UBS executives in the United States, the IRS filed a claim directly to the UBS to disclose all information of approximately 52‘000 American

citizens with undeclared assets in Switzerland (cf. Bondi 2010: 7-9). The UBS refused to comply. They argued that according to the DTA the U.S. authorities had to address their request of information exchange directly to the Swiss Federal Tax Administration (FTA). Since the information was within Switzerland‘s sovereign territory, authorisation and assistance had to be granted by Swiss officials. After one year of diplomatic and legal disputes the Swiss government signed in 2009 a Revised Tax Treaty with the United States. In September 2009, Switzerland and the United States agreed on the Double Taxation Amendment. Since the DTA, at that time, did not necessarily include or limit the exchange of information in the terms of tax fraud or tax evasion, the Double Taxation Amendment states that the tax authorities from both United States and Switzerland may exchange such relevant information in order to enforce and administer domestic laws of the two parties. Therefore, the types of cases which are eligible for mutual assistance in sharing information from the competent governmental authorities have been broadened to include tax fraud and tax evasion (cf. Victorson 2011: 833). If the U.S. should request information from the Swiss authorities to enforce American tax laws following premises must be fulfilled according to Article 4 of Double Taxation Amendment:

- “information such as a name, address, account number or similar identifying information of the person allegedly violating the U.S. tax laws (i);
- the period of time for which the information is requested (ii);
- a statement of the information sought including its nature and the form in which the
- requesting State wishes to receive the information from the requested State (iii);
- the tax purpose for which the information is sought; and (iv);
- the name and, to the extent known, the address of any person believed to be in possession of the requested information (v).“ (cf Protokoll zur Änderung des Abkommens zwischen der Schweizerischen Eidgenossenschaft und den Vereinigten Staaten von Amerika zur Vermeidung der Doppelbesteuerung auf dem Gebiet der Steuern vom Einkommen 2009: 5).

“The purpose of referring to information that may be relevant is intended to provide for exchange of information in tax matters to the widest possible extent without allowing the Contracting States to engage in “fishing expeditions” or to request information that is unlikely to be relevant to the tax affairs of a given taxpayer“ (cf. (cf Protokoll zur Änderung des Abkommens zwischen der Schweizerischen Eidgenossenschaft und

den Vereinigten Staaten von Amerika zur Vermeidung der Doppelbesteuerung auf dem Gebiet der Steuern vom Einkommen 2009: 6).

The UBS on the other hand admitted to have helped U.S. clients to avoid taxation and agreed on paying a fine of 780 million U.S. Dollars, disclose the information of 4‘450 account holders and cease its offshore banking activities in the United States (cf. Victorson 2011: 832-833). The example UBS vs. the United States shows various aspects which are morally reprehensible. On a micro level, employees encouraged American citizens to break the lawin their domestic country for the eomployees own benefit. They did not only put their clients to danger but also caused major reputation loss to their bank, the UBS and the Swiss financial centre. So there is also the ethical conflict for financial intermediaries. Generally speaking, individuals use the banking secrecy to either promote offshore banking or for their own benefits or either hide their assets to avoid paying taxes, so basically dishonest and greedy bankers as well as clients (cf. Chaikin 2005: 103). On a meso and corporate leve,l the bank itself chose the strategy to blame the individual bank employees for the damage they caused to the IRS and the UBS. Last on a macro level where the Swiss government who had their own financial interests, evident in the allowence the data transfer. Since the UBS underwent a major crisis; the Swiss government bought 9% of shares in order to prevent the bank‘s collapse. So it was in the governments interest to find a fast as possible agreement with U.S. authorities so that the stock price of the UBS would stabilise. After the settlement the government sold the shares for a profit (cf. Bondi 2010: 12).

4.4.2 European Union, Tax Fraud & Tax Evasion

Another important case is the relationship between Switzerland and the EU or its member states. Over the past years accusations have been made against the Swiss banks and the banking secrecy by EU member states. The bank client confidentiality implemented in Austria, Liechtenstein or Switzerland give the possibility to EU clients to avoid paying taxes in their domestic countries which obviously favours the rich. With tax evasion in Switzerland, primarily the neighbouring countries are negatively affected, since Switzerland is situated in the heart of Europe. In 2001 the French parliamentary delegation estimated the percentage of illegal assets in Switzerland to 90% (cf. Assemblée National, 2001: 32). The “Deutsche Bank“ assumes 70% (cf. Missbach 2009: 103). The following charts show the percentage which the KPMG have estimated.

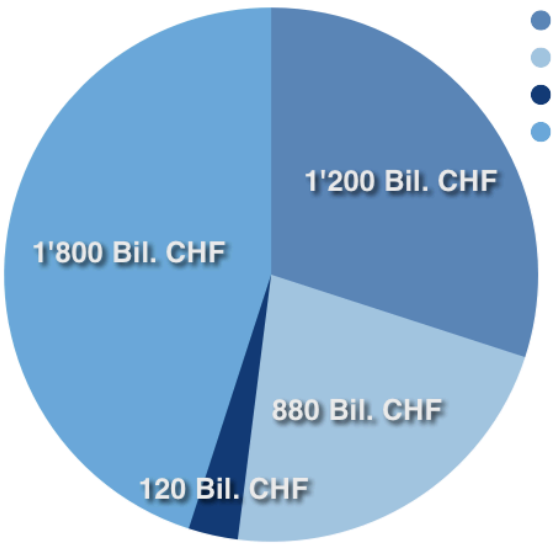


Chart 1: Source: KPMG/Helvea (2010)

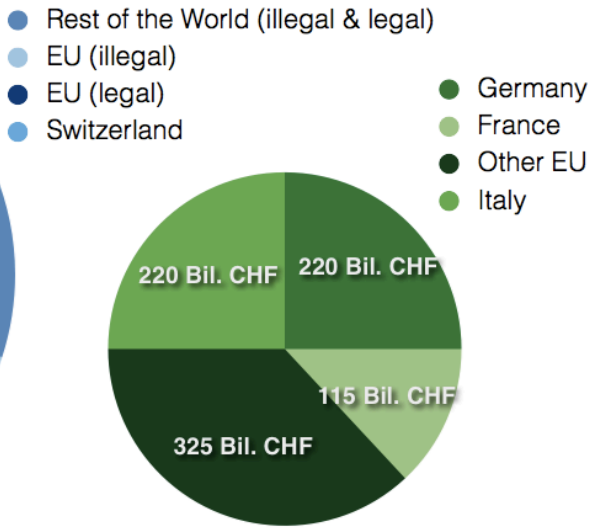


Chart 2: Source: KPMG/Helvea (2010)

Chart 1 shows that approximately 880 billion Swiss Francs from EU clients is alleged to be illegally in Switzerland. In Chart 2 the estimations display that out of those CHF 880 billion, German, Italian and French clients have allegedly the largest undeclared amounts of assets in Switzerland. The “Banca d‘Italia“ figures that illegally foreign invested money by Italians is amounted to 500 billion Euros. In 2009 Italy launched a tax amnesty programme which allowed Italian citizens to legally declare their assets from abroad for a compensation tax fee of 5%. The tax amnesty caused an inflow of 70 billion Euros. Nearly 45% (25-30 billion Euros) was administered on Swiss bank accounts. Total tax revenue for Italian tax authorities in virtue of the tax amnesty programme amounted 5 billion Euros (cf. Victorson 2011: 846-847). One could argue that according to the statistics of the tax amnesty, 45% of the estimated amount which has not been repatriated may be administered by Swiss banks also. It would mean that approximately other 230 billion Euros are placed on Swiss bank accounts. The German Federal Ministry of Finance recently claimed that more than 500 billion Euros of illegal German assets are put in banks either in Switzerland, Liechtenstein or Luxembourg. The EU Commission stated in 2006 that because of tax fraud, the EU annually misses out tax revenues amounting to 200-250 billion Euros (cf. Missbach 2009: 104). The different amounts of the estimations made by various authorities or instances show clearly those numbers are simply assumptions and financial projections, certainly not empirical data. Nonetheless, there is no doubt that there are foreign clients which have placed their assets in Swiss banks to avoid taxes.

In the cases of tax fraud and tax evasion Switzerland has signed various agreements and made different efforts to cooperate with international authorities. Still, the Swiss

fiscal policy can be criticised for ethical reasons, especially for its tax practices with foreign assets. Switzerland does not tolerate autonomous interfering or structuring of the respective foreign countries with these assets, therefore attracts tax evaders. It is clear that the use of banking secrecy practices is severely criticised by foreign officials which is based on ideological and moral aspects, for that reason opinions on the banking secrecy are rather subjective. Additionally, there is simply no instance which can prohibit those practices. It means that all the dialogue and dispute about the banking secrecy is highly affected by crisis‘. Crisis which leads people to rethink and creates conflict potential between countries because of different policies. It is important to note that in Europe the individual state is autonomous and thus want to demonstrate its sovereignty, especially in crisis (cf. World Justice Forum Foundation (WJF) 2009: 21). The reason for the conflict between Switzerland and the EU, especially with the neighbouring countries Germany, France and Italy is the subject of taxation. It is a violation of law when EU citizen avoids paying taxes in their respective country. It is violation of Swiss law to actively or passively help in tax evasion as a financial intermediary. The question arises whether it is the duty of the Swiss banks or the Swiss tax authorities to monitor their foreign clients in tax matters. Swiss banks claim that it does not fall in their area of competence, which does not mean that the banks or the authorities would not cooperate with foreign authorities (see Chapters 4.2 / 4.3). Referring to the Swiss Banking Association (SBA) about the self-declaration principle where every individual citizen has personal responsibility to follow their own tax liability towards the state and not its bank. The Swiss banks are not obliged to inform the state or the tax authorities about the amount of the interest which is credited to the clients bank account (cf. Perroulaz 2008: 127). So the banks and authorities escape the duty while putting the legal and moral responsibility on the individual itself. The cases of taxation between Switzerland and the EU have been intensively discussed. Foreign authorities have not hesitated to make use of any kind of option which could have damaged the reputation of the banking secrecy and thus the Swiss financial centre, such as not respecting Swiss sovereignty and banking secrecy laws by purchasing CDs with sensitive information (cf. Wittrock 2010). To evolve the situation Switzerland has recently agreed to revise or renew the tax agreements with Germany, Great Britain, Austria and is negotiating with Italy and France (see Chapter 4.3.2). On the 15th of March 2012, over the negation period between Switzerland and Germany arrest warrants were issued by the public prosecutor‘s office of Switzerland against three tax officials in North Rhine-Westphalia which were involved in the purchase of a CD from the Swiss bank Credit Suisse containing sensitive information of German clients and their undeclared assets. The Swiss prosecution office stated

that the act of purchasing a CD with sensitive data is illegal since the CD itself violated banking secrecy laws. The German tax officials were accused of economic espionage against the bank Credit Suisse (cf. Tax Agreements II 2012). The dispute between Germany and other EU member states with Switzerland seems to be endless. Both parties are not willing to tolerate the banking secrecy laws or abandon the banking secrecy. It is questionable whether the campaign of the opposition of the banking secrecy actually wants to address tax issues or uses it as competition tool. With further tax agreements, which should come into force in January 2013, the situation among the two parties could be relieved for a given period.

4.4.3 Holocaust Victim Assets Litigation

Another case which reflects badly on the Swiss banking sector and bank honesty is the one concerning victims of the Holocaust and their assets. In 1996 and 1997 numerous class action suits were filed in several United States federal courts against certain Swiss banks and other Swiss entities. The class action suits were filed by Holocaust survivors and descendants of the Holocaust victims. A judge of the United States District Court for the Eastern District of New York, Edward R. Korman consolidated all cases. The allegations stated that Swiss financial institution knowingly collaborated and aided the Nazi Regime by accepting illegally obtained assets allegedly of slave labour and retained or concealed assets of Holocaust victims. Swiss bankers had manipulated the banking secrecy to hide Nazi deposits of gold which was illegally obtained from the Holocaust victims. The allegations were a huge shock for the the Swiss government and Swiss banking sector, since it was viewed with huge respect. The Holocaust survivors were represented by various attorneys led by Burt Neuborne. The defendants were mainly financial institutions and the Swiss banks. The Swiss government was not included (cf. Holocaust Victim Assets Litigation 2012). The combination of the American legal suits and the threat of sanctions against Swiss financial institutions, led Switzerland to take legislative and compensatory action in dealing with the Holocaust victims as never before. During the litigation and settlement discussions the Swiss Parliament passed a law on the 13th of December 1996 to establish an Independent Commission of Experts – the Bergier Commission. The Commission‘s mandate was to investigate the amount, the way and origin of money and assets that found their way into Switzerland in connection with Nazi politics. Covering the period immediately after, during and prior to Second World War (cf. Holocaust Victim Assets Litigation 2012). In order to examine the issue all banks, insurance companies and other private entities had to disclose all their relevant information to the Bergier Commission. It signified that banking secrecy, the official

secrecy of the Swiss government and its courts and the professional secrecy of lawyers were suspended in order to successfully investigate for inactive bank accounts or dormant assets for the period of World War II (cf. Chaikin 2005: 103-104). The second formed Commission was The Volcker Committee, an independent Committee formed by a Memorandum of Understanding between the World Jewish Restitution Organisation, The World Jewish congress and the SBA in 1996. The Volcker Committee presented the final reports in the end of 1999. During the relevant period of 1933 till 1945, 6.8 million Swiss bank accounts were opened. Further, the Committee audited more than 300‘000 accounts. 53‘886 accounts had a possible or probable relationship to victims of Nazi prosecution. The Committee ranged the amount of mainly dormant assets with a possible connection to victims of Nazi prosecution from 643 million U.S. Dollars to 1.36 billion U.S Dollars (cf. Holocaust Victim Assets Litigation 2012). After all, the Committee could not find any clear evidence that Swiss financial institutes were active or connected in anyway of laundering or looting of assets. The Bergier Commission produced various reports. Main findings brought no evidence of looting or laundering. What the Commission was able to prove was that the Swiss National Bank (SNB) plaid a significant role in the handling of gold of the Reichsbank, contrary to commercial banks. Despite the fact that no evidence was found that the SNB was aware that the gold may have been looted from Nazi victims, the Commission criticised the SNB not acting in good faith. The parties reached an agreement to settle the lawsuits in August 1998. The agreement was signed on the 26th of January 1999 and concluded Swiss banks to pay 1.25 billion U.S. Dollar as a global settlement. The Swiss banks, the Swiss government and other entities on the other side were released and forever discharged from all claims relating World War II, Nazi Regime, Holocaust et cetera. Nevertheless, it caused a huge damage to the reputation of the banking sector and the prejudice of Swiss financial institutes being associated with Holocaust victims‘ assets remained (cf. Chaikin 2005: 105).

4.4.4 Emerging Nations & Developing Countries / Final Recommendations

A major problem in developing and transition countries is the fact that their governments are corrupted and the countries are governed undemocratically. Hence, the theft of public assets is a serious and huge problem. In developing and transition countries between 20-40 billion U.S. Dollars is associated with bribes received by public officials. Corrupt leaders illegally obtain money from their countries which usually is due to this capital not being reinvested into their own economy, further increasing these countries developmental status. It affects negatively public

institutions, especially those involved in the public financial sector, it destroys the private investment climate, it weakens public health and education programmes and thus has the biggest impact on the poor. Those illegally obtained assets are often hidden in the world's financial centres (cf. World Justice Forum Foundation (WJF) 2009: 9-11).

Political leader	Country	Stolen assets ($billion)	Average annual GDP ($billion)	Annual theft as percent of average nominal GDP	
				Lower bound	Upper bound
Mohamed Suharto (1967-98)	Indonesia	15 to 35	86.6	0.6	1.3
Ferdinand Marcos (1972-86)	Philippines	5 to 10	23.9	1.5	4.5
Mobutu Sese Seko (1965-97)	Zaire	5	8.8	1.8	1.8
Sani Abacha (1993-98)	Nigeria	2 to 5	27.1	1.5	3.7
Slobodan Milosevic (1989-2000)	Serbia/Yugoslavia	1	12.7	0.7	0.7
Jean-Claude Duvalier (1971-86)	Haiti	0.3 to 0.8	1.2	1.7	4.5
Alberto Fujimori (1990-2000)	Peru	0.6	44.5	0.1	0.1
Pavlo Lazarenko (1996-97)	Ukraine	0.114 to 0.2	46.7	0.2	0.4
Arnoldo Alemán (1997-2002)	Nicaragua	0.1	3.4	0.6	0.6
Joseph Estrada (1998-2001)	Philippines	0.07 to 0.08	77.6	0.04	0.04
			Average % of GDP	**0.9**	**1.8**

Table 1: Source: World Justice Forum Foundation (WJF) (2009)

- Table 1 shows various political leaders and their amount of illegal assets. Some of those assets have been administered in Switzerland. In particular, money from Ferdinand Marcos, Sani Abacha or Jean-Claude Duvalier. The FINMA Anti-Money Laundering Ordinance allows business relationships with politically exposed persons (PEP). Problems arise if political events cause the PEP to become a personae non grata, in the eyes of the Swiss government of international authorities and organisations (cf. Swiss Bankers Association, Dictators' assets 2012). It occurred numerous times that the Swiss government froze the assets of PEP's, the most recent cases with the Arab Spring movement. Assets of from the former Egypt and Libyan regime as well as the Syrian regime have been frozen. Switzerland has frozen CHF 1.217 billion potentates' money in total in the year 2011. CHF 650 million concerning the regime of Muammar al-Gaddafi. 410 Million Swiss francs come from the regime of the ceded, Egyptian President Hosni Mubarak and 60 million from the environment of the fallen, Tunisian President Ben Ali (cf. Dictators' assets

II 2012). It is then the task of Swiss authorities to restitute the frozen assets to the governments concerned (see Chapter 4.3.1).

- Touching upon the moral aspect it is ethically highly questionable to manage such assets under the afore mentioned circumstances. The SBA claims that it is in the interest of the banks and the financial centre not being associated with potentates‘ money and thus not administer such assets in the first place. They add that the measures used to block these assets are globally accredited. At the same time it is argued that Switzerland is a haven for dictators’ assets cf. Swiss Bankers Association, Dictators’ assets 2012).
- To finalise the ethical and moral aspects of the banking secrecy with its international disputes it can be stated that the list of ethical questions in the previously formulated conflicts are hard to be answered. Following points give a brief overview of the Swiss banking secrecy‘s moral grey areas or ethical aspects. Hence, the formulation of recommendations which may resolve ethical and moral aspects of the banking secrecy and its connected practices:

- It is the duty of every individual taxpayer to declare his income and assets in private area as well in business area;
- The individual countries and governments have to respect each other’s laws and regulations, as well as traditions in order to successfully cooperate
- The distinction between tax evasion and tax fraud can be seen as an artificial border. It encourages passive tax evasion, is discriminatory and is therefore highly problematic from an ethical point of view;
- It is ethically questionable if regulations and measures to reduce money laundering are used as in order to favour the image of the Swiss financial centre;
- On the other hand it is necessary to critically question whether the Swiss banking secrecy is used as a competition measure or as a pretext to harm the Swiss financial centre;
- It is not in the sense of the Swiss banking secrecy to use its practices for economic benefits such as profit maximisation or to the disadvantage of minorities or the less fortunate;
- Administration of assets of PEPs should be well considered and examined;
- Evaluation whether the existing self-regulation effectively is combating money laundering. If necessary, other instruments have to be implemented;

- Protective measures against money laundering would be to accept only assets, which previously have been taxed. Hence, an elimination of the distinction between tax evasion and tax fraud;
- Important step with the EU would be extending the existing tax agreements. A next step could be the exchange of information between the legitimate authorities, so that tax justice and a fair tax competition can be achieved (cf. VBG Institut 2006: 16-17).

5. The Swiss Financial Centre

5.1 Facts & Figures

The Swiss financial centre is one of the most prestigious and among the leaders of the global market. The banking sector belongs to the world's best and makes a significant contribution to gross value added in Switzerland and hence to the wealth of the whole Swiss population. The Swiss banks are financial institutions with a long tradition and history and are of high importance to the Swiss economy. The banks offer a wide range of qualified jobs. The tax contribution by the banks covers a significant part of the public expenses. In Switzerland, there are more than a third of all worldwide offshore assets are being administered. This figure is a proof for the international importance of the financial centre of Switzerland in the field of private banking. In the sector of wealth management Switzerland stands among the leaders. In a ranking of the worldwide largest wealth managers three Swiss banks are represented in the top ten. More than anywhere else in the world, banks are specialised in wealth management. (cf. Der Finanzplatz Schweiz und seine Bedeutung 2011: 1).

Assets under management in Switzerland (2010)

	Assets under management (CHF bn)	Share in %
Domestic clients	2,650	48%
Foreign clients	2.850	52%
Total	**5,500**	**100%**

Table 2: Source: Calculations SBA, Swiss National Bank (2010)

Table 2 shows official statistics of the SNB and the SBA that in total CHF 5.5 billion are under Swiss management. With a market share of 27% in 2011, Swiss banks are in the leading position in the market of cross-border private banking. A value added of approximately CHF 8 billion is generated by 29,000 employees who work in the segment of wealth management for foreign clients. Wealth management is the core

business of Swiss banks. It is important to note that a distinction between "Swiss banks" which can be also subsidiaries in other countries and "banks in Switzerland" which are actually geographically located in Switzerland must be made. According to the FINMA the term of "assets" includes fiduciary deposits, securities held in client portfolios, amounts due to clients in savings and investment accounts and other amounts due to clients from time deposits. (cf. Der Finanzplatz Schweiz und seine Bedeutung 2011: 2-3).

Number of employees (2010)

	Financial sector	Banking sector
Employees working in Switzerland	195,045	141,900
Employees working abroad	177,000	104,000*
Total employees	**342,045**	**245,900**

Table 3: Source: Swiss National Bank, Federal Statistical Office (2010)

5.7% of the whole Swiss work force is employed by the financial sector. 108'000 work either for security dealers or banks; other 33'900 are employed by other financial services. Insurance companies employ 53,145 and 104'000 work for Swiss banks abroad in branches or subsidiaries. In total 320 banks are active in Switzerland which have 3'726 branches. From those 284 branches are abroad. Table 4 shows that 10.7% of value added, meaning CHF 58.6 billion is accounted by the financial sector in Switzerland. If indirect effects are included the added value of the whole financial increases to an approximate of CHF 90 billion which is nearly one fifth of Switzerland's GDP. 6.7% of the Swiss GDP contributes the banking sector itself, the insurance sector 4%, CHF 21.9 billion. Employees of the financial sector account CHF 260'000 each of value added in Switzerland which is twice Swiss average (cf. Der Finanzplatz Schweiz und seine Bedeutung 2011: 1).

Value added of the financial sector (2010)

	Absolute (in CHF bn)	Contribution to overall value added
Total value added banking sector	36.7	6.7%
Retail banking	13.7	2.5%
Wealth management	15.5	2.9%
Asset management	4.5	0.8%
Investment banking	3.0	0.5%
Total value added insurance sector	21.9	4.0%
Total value added financial sector	**58.6**	**10.7%**

Table 4: Source: Calculations SBA, State Secretariat for Economic Affairs SECO (2010)

The statistics and figures give a brief overview about the volumes of the financial centre in Switzerland and show the significance of the banks for the state and its economic wealth. The upcoming subchapter names factors for Switzerland becoming such an important and successful player on the global financial markets. The significance of the banking secrecy is highly disputed and has been displayed in this paper. The following focuses on other aspects and indicators, despite the arguable factor of the Swiss bank client confidentiality. Therefore studies will be taken into account.

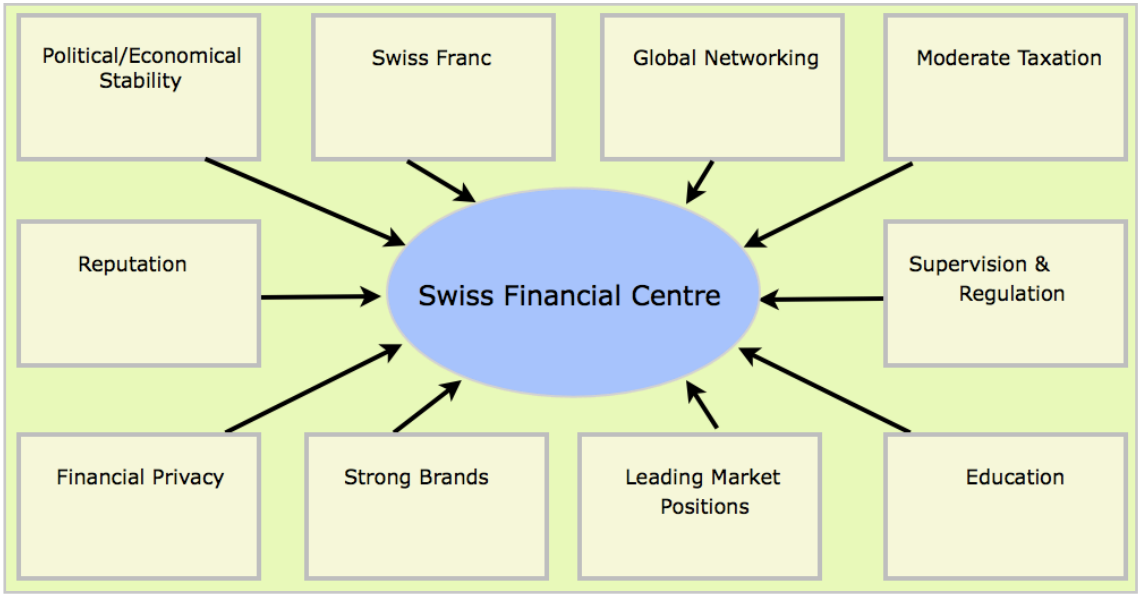
5.2 Significance of the Swiss Financial Centre

Without a doubt is the intensive protection of the individual privacy by the banking secrecy a significant element for the success story of the Swiss banking centre. It is logical that the question arises whether the existence of the banking secrecy has been essential for the positive development of Switzerland becoming an international financial centre of high importance, especially for the success of the wealth management (cf. Vogler 2005: 55).

The study of Vogler (2005) analyses exactly the issue of the extent of the banking secrecy having a significant impact in the positive development of the Swiss financial centre. Therefore, he compares the different financial centres; he analyses the development of European financial centres and the United States, in particular the banking secrecies, international significance, banking laws and regulations, characteristics etc. Alphabetically ordered Belgium, Germany, France, Great Britain, Italy, Luxembourg, the Netherlands, Austria, Hungary, Sweden, Switzerland, at that time Czechoslovakia and the United States are included in Vogler‘s research (cf. Vogler 55-59). His findings state that firstly, that “there is no universal model for the mechanism by which banking law, company law, etc., or banking secrecy can function as the foundation of a country’s development into a significant financial centre with a strong asset management sector“, secondly that “there is no evidence that banking secrecy is a fundamental or indispensable tool in the creation of a successful asset management business; traditional asset management for private individuals is a business that cannot be built on banking secrecy alone. Other elements have to provide the motivating force“ (cf. Vogler 2005: 55) (see Chapter 3.2).

Switzerland has been a traditional country exporting capital. This because till the 18th century the domestic demand for credit was small. As a result of international crisis‘, inflation, political instability, wars and monetary decay in foreign countries, Switzerland had a huge inflow of flight capital. The savings surplus and inflow of capital was at that time a bad basis for the international banking business as well as for the wealth

management. Switzerland did not have the intention nor the instruments to become a major financial centre. The Swiss economy was simply too small. With the recurrent political and economic problems in foreign countries people would invest in the Swiss Franc. It caused the Swiss Franc to become a strong and stable currency benefiting the financial centre and the Swiss economy. In the 20th century, the financial centre profited the most because of World War I, World War II, revolutions and inflation which most importantly occurred abroad. Switzerland was so politically stable that one could predict economic trends and conditions. Investors never had to fear unpleasant surprises. Additionally, Switzerland had the lowest inflation that assets in Swiss Francs would maintain their value. The Swiss Franc could always be converted, also for foreigners. With the transition to flexible exchange rates the Swiss Franc had appreciated strongly which made the currency even more popular and benefited the economy (cf. Schiltknecht 2008: 2-4). The economic and political crisis in Europe, generally the bad circumstances, especially in the neighbouring countries of Switzerland plaid a major role in the development of the Swiss financial centre in the 20th century. Foreign non-existent factors which existed in Switzerland led to the increasing importance, reputation and trust in the Swiss financial institutions to this day.



Graph 1: Source: EFV / Die Volkswirtschaft (2006)

As graph 1 shows is the success of the financial centre today dependent on various interconnected factors:

- The political and macroeconomic stability is a prerequisite for the confidence and trust of the clients; the Swiss Franc impacts positively on the

macroeconomic stability, since it is a strong international reserve- and diversification currency;

- The efficient financial infrastructure and strong global networking allow the market players to profitably manage their assets and risks to diversify them internationally;
- The Swiss financial centre enjoys foreign trust and has a high reputation hence is attractive for international clients and as business location. Despite the strong brands in the banking and insurance sector, high educational standards, multilingualism, service quality, a multicultural environment etc., the government regulation and supervisory bodies contribute to the success of the financial centre with strong measures combating terrorist financing or money laundering;
- in the matter of taxation, Switzerland is highly attractive in the international tax environment in virtue of the qualified and mobile workforce as well as the competitive taxation, the effective income tax rates between 16% and 25% (cf. Gerber et a. 2006: 4-5)

Because of the named factors the Swiss financial centre and its banking and insurance sector is ranked among the best in the world. Z/Yen Group published a study "The Global Financial Centres Index" in March 2011 analysing the profiles of 75 financial centres. With a representative survey of financial centre assessments, they defined different areas which are most significant for the competitiveness of a financial centre. These factors would be subject to the index itself. To those factors of competitiveness they separately analysed the criteria of reputation and stability.

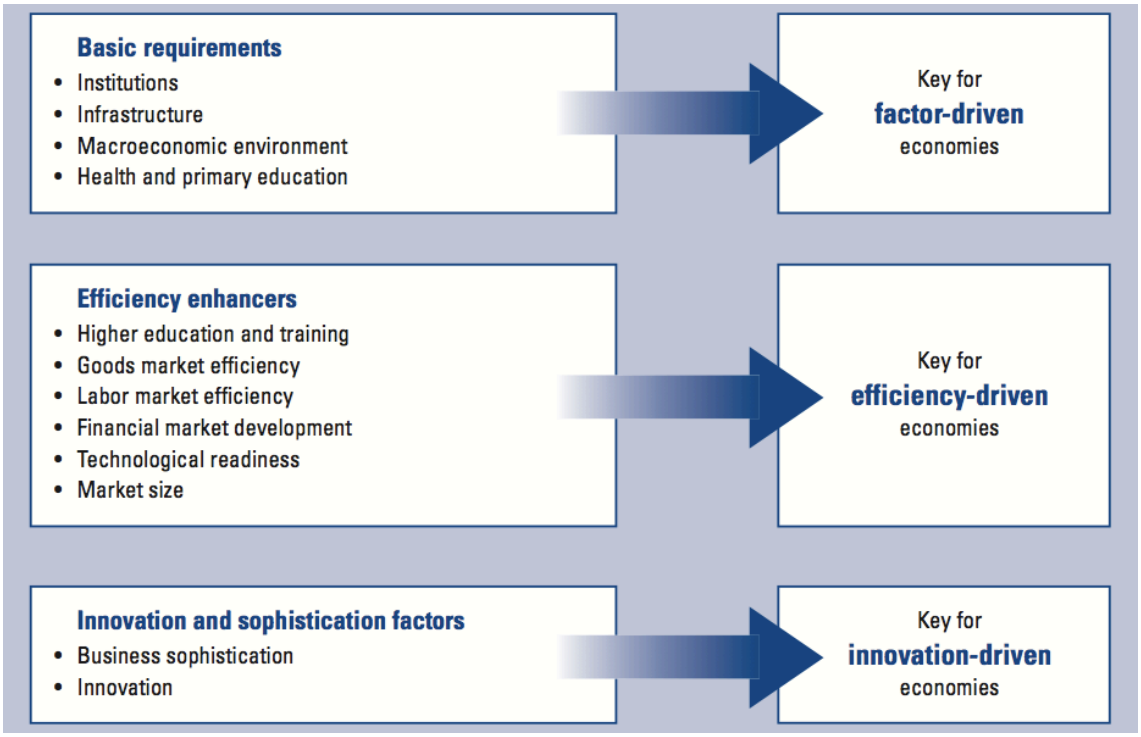
Switzerland and its financial centres Zurich (8) respectively Geneva (9) ranked among the top ten on an international level. Looking at European financial centres Zurich was ranked second, Geneva third behind London (cf. The Global Financial Centres Index 9 2011: 4-5) In the cases of stability and reputation both Geneva and Zurich were among the top fifteen financial centres in the world. Along with Singapore, Hong Kong, New York, London and Frankfurt the Swiss financial centres Geneva and Zurich were found most stable. In the case of reputation, Zurich ranked 8th while Geneva was ranked 11th (cf. The Global Financial Centres Index 9

Competitiveness Factors	Rank
The availability of skilled personnel	1
The regulatory environment	2
Access to international financial markets	3
The availability of business infrastructure	4
Access to customers	5
A fair and just business environment	6
Government responsiveness	7
The corporate tax regime	8
Operational costs	9
Access to suppliers of professional services	10
Quality of life	11
Culture & language	12
Quality / availability of commercial property	13
The personal tax regime	14

Table 5: Source: Z/Yen Group (2011)

2011: 29-30). The study concluded that the Swiss financial centre is the most balanced in Europe and remains attractive for foreign clients not only because of high reputation but also because of stable and sensible regulations (cf. The Global Financial Centres Index 9 2011: 15).

The World Economic Forum publishes every year the Global Competitiveness Report. Their department called "Centre for Global Competitiveness and Performance" evaluates every year in cooperation with prestigious institutes all around the world, the competitiveness of the different economies in the world. The report divides the term "competitiveness" into 12 pillars. These pillars are examined and finally brought together to be summarised in the index of competitiveness. Institutions, infrastructure, macroeconomic environment, higher education and training, health and primary education, goods market efficiency, labour market efficiency, financial market development, technological readiness, market size, business sophistication and innovation form the basis for the analysis (Graph 2).



Graph 2: Source: World Economic Forum (2010)

Further the report puts the countries into five separate stages of development. The results of the report ranks Switzerland on the first place and thus considered most competitive. It characterises Switzerland for its very sophisticated business culture, excellent capacity for innovation, world-leading scientific research institutions, macroeconomic environment, independent judiciary, excellent infrastructure, highly developed financial and labour market strong, rule of law, and a highly accountable public sector. (cf. The Global Competitiveness Report 2010-2011 2010: 14-15).

International studies show that the Swiss financial centre and the Swiss economy are among the best and most important in the world and will continue to perform well. The reasons have been named. Nevertheless, the Swiss financial centre which is used to success, underwent various reputation crisis‘ for different reasons and was not able to escape the global economic crisis either (see Chapter 4.4). The bank client confidentiality in most cases has been the main issue, also in recent disputes with EU member states. The past has shown that the Swiss economy has highly benefited from the globalisation and opening of markets. As it is expected that Switzerland will be able benefit from it in the future, the Swiss government has to continue to revise regulations which protect the financial centre (cf. Roth 2008: 13). Regarding the tax issues and the banking secrecy the Swiss banks and the SBA stated not to acquire untaxed assets in the future, so called “strategies for legitimate money“. Results of the strategy would be the tax agreements with Germany, Great Britain and other EU member states. (cf. insight 1.12 2012: 6). In that way the issue of taxation with neighbouring countries as well as the EU body could be resolved without affecting the banking secrecy and fair competition guaranteed.

6. Switzerland and the EU: Chronological Overview

- 22.07.1972: Signing of free trade agreement between the Switzerland and the EU;
- 02.05.1992: Signing of the EEA Agreement by the then 12 EU States and seven EFTA States;
- 26.05.1992: Switzerland sends a request to Brussels in order to enter the European Economic Area;
- 06.12.1992: The Swiss people reject to enter EEA Switzerland with a majority vote of 50.3 %;
- 21.06.1999: Signing of the Bilateral I agreements;
- 21.05.2000: The Swiss people accept the Bilateral I agreements (67.2 %);
- 01.06.2002: Bilateral I agreements come into force;
- 26.10.2004: Signing of the Bilateral II agreements;
- 05.06.2005: The Swiss people accept the agreement to participate in Schengen/ Dublin with 56 %;
- 01.07.2005: The agreement on the taxation of savings income come into force
- 25.09.2005: The Swiss people accept the extension of the free movement of persons concerning the 10 new EU Member States (54 %);
- 01.03.2008: The Schengen/Dublin agreement come into force
- 12.12.2008: Start of operational implementation of Switzerland in the Schengen area (removal of checks on persons at the land borders);

- 08.02.2009: The Swiss people accept the continuation of the free movement of persons (Bulgaria and Romania with 59.6 %);
- 29.03.2009: Removal of controls of people at airports within the framework of the Schengen/Dublin agreement (cf. Chronological Overview: Switzerland - EU: 2012)
- 18.04.2012: Agreement on the Free Movement of Persons Switzerland – EU: Invocation of the Safeguard Clause with respect to the EU-8 States (Safeguard Clause 2012)
- 15.05.2012: Concept of the revised tax agreement approved by the Economic Commission of the Council of States of Switzerland, important step for resolving tax issues (cf. Tax Agreements I 2012)

The relationship between the EU and Switzerland is considered a positive one. The major conflicts mostly occur among Switzerland and its neighbouring countries Germany, France and Italy. The main issue is taxation. Switzerland has shown various efforts to resolve the issue and has implemented different measures in order to cooperate with foreign authorities (See Chapter 4.3.2). Nevertheless Switzerland has remained the position not to abandon the banking secrecy and the bank client confidentiality (see Chapter 4.4.2). The question whether Switzerland should enter the European Union will not be answered in the near future. There is a strong force, basically the majority force in Switzerland which wants to remain as neutral country. Despite that, the recent Euro crisis and political instability of various European member states are factors which do not favour the possible decision of Switzerland entering the EU and the Eurozone. Although Switzerland is not a member of the European Union, it contributes to the European cohesion by supporting the different European fonds.

7. Hypotheses

- As mentioned in the beginning of this writing does the thesis follow a general questioning. However, four hypotheses can be outlined. The Hypotheses favour the banking secrecy. The construction of the hypotheses is based on the review of world literature as well as recent political and economic events in the environment of the Swiss financial centre and the Swiss banking secrecy.

- H1: The concept of Swiss bank client confidentiality is misinterpreted and observed in the wrong context – it is a Swiss tradition, a piece of Swiss culture.

- H2: The banking secrecy is not respected by foreign authorities and their attempts to weaken it are violations of Swiss sovereignty.

- H3: The weakening of the Swiss banking secrecy by foreign authorities have had only short-term success, in the long term, the contrary dominates – the Swiss population, Swiss banks, as well as the government want to maintain and restrengthen the banking secrecy because of these attacks.

- H4: The banking secrecy is often used as a pretext – among other conditions, laws and regulations of the EU countries indirectly favour the Swiss financial centre.

8. Methodology

The previous chapters have touched upon the questioning of this thesis and have outlined different aspects from either the opposition of the Swiss banking secrecy or the parties in favour of the banking secrecy. It has been displayed what the main issues concerning the bank client confidentiality are and how the banking secrecy itself has been justified historically, politically and economicaly. In order to give a further input to the issue and test the hypotheses, an expert interview will be taken into account. The interview was held on the 28th of January 2012 at the World Economic Forum in Davos with an expert of the Swiss financial centre. The person who preferred not to be fully named, has great experience in the world of finances. After working in Zurich, Geneva, Hong Kong and Japan he was in the Executive Board of the Bank Leu, Credit Suisse, member of the Board of Directions in different companies and now CEO of a financial management company of which he is majority shareholder. The company is specialised in management, investment and consulting of assets of domestic and foreign clients in the European market. Along with the core statements of the interview, representative surveys contribute to the findings of the thesis are being used to test the hypotheses. It is concluded in Chapter 8.2 respectively in the conclusions.

8.2 Discussion of the Results

- H1: The concept of Swiss bank client confidentiality is misinterpreted and observed in the wrong context – it is a Swiss tradition, a piece of Swiss culture.

Regarding H1 the interviewee states that the banking secrecy was never created with the intention to enable tax evasion, tax fraud or any other criminal activities. It was created to protect the privacy of the individual, the ideal of freedom; its protection is firmly anchored in the Swiss thinking and Swiss values. It is important to state that the Anti-Money Laundering Ordinance is one of the best in the world as well as the supervisory body FINMA. Additionally, the interviewee recollects the events of 9/11 when Swiss specialists were asked for assistance by U.S. authorities to monitor cash flows of the al-Qaeda. The Swiss Attorney General concluded that in terms of monitoring money laundering the Swiss authorities are among the best where the U.S. still need a lot of development. The United States may have improved but there is no such thing as self-regulation measures, as known in Switzerland, which also explains the mortgage crisis. The procedure of opening an account in Switzerland is the same for more than 20 years. When a foreigner wants to open a Swiss account he has to declare the origin of his assets, he must be able to prove it with documents. The clients economic background is being questioned and his documents are then stored by the bank. The client has to sign a document that ensures that the claims made are truthful. PEPs have to answer further questions and provide extra documents. All clients have to sign a document that they are entitled to the assets or have to name the person which is entitled to the money. The expert adds that he is sure that Swiss banks have to follow most statutory obligations worldwide. Regarding taxes he states that it is Swiss thinking everyone being responsible for himself to pay taxes and thus it is not the task of Swiss authorities to act as “tax police“ for foreign country, the Swiss ideal of freedom is that above all. It is further interesting that Switzerland has high tax honesty; the country has low tax rates and high quality of life – a normal human being would not come up with the idea to evade taxes in such an environment (cf. Interview regarding the Swiss Banking Secrecy 2012).

It can be argued that the Swiss banking secrecy and its projection in the movies and the media is often in connection with criminal activity. Therefore, it can be doubted that general public, as well as policy makers of the opposition of the banking secrecy have a broad knowledge about the creation and implementation of the Swiss banking secrecy. The bank client confidentiality existed long ago before the actual implementation into Swiss law. The bank client confidentiality how it actually should be named, is a professional secrecy known also from other professions, such as doctors or lawyers. The reasons for its implementation were certainly not to enable tax evasion or other criminal activities. The banking secrecy itself was only one article (Article 47) of the Federal Banking Act which was implemented in virtue of the crisis which affected badly the Swiss financial centre. The banking secrecy as we know it today is

a construct of different laws to protect the individual and its privacy and has been a Swiss cultural tradition and trademark over more than a century (see Chapters 3, 4.2).

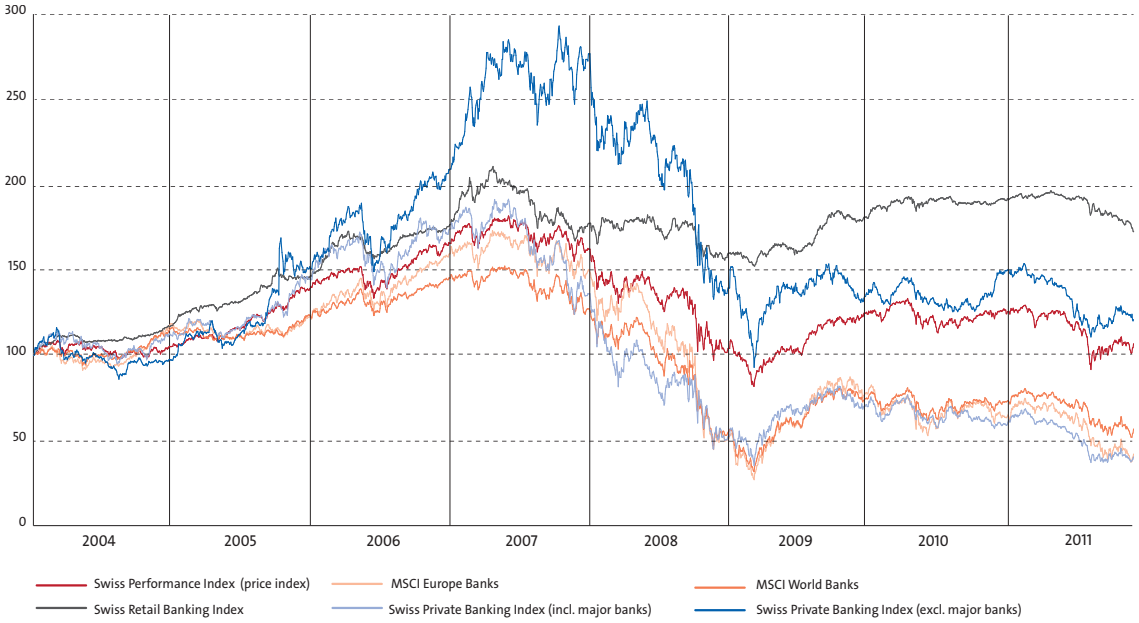
- H2: The banking secrecy is not respected by foreign authorities and their attempts to weaken it are violations of Swiss sovereignty.

It is most certain that the banking secrecy laws are not compatible with EU regulations, especially not with policies of Switzerland‘s neighbouring countries Germany, France and Italy. Nevertheless, those laws are implemented in Swiss legislation. Switzerland is a neutral and sovereign state and thus from a legal perspective, the banking secrecy laws have to be seen as absolute by the EU and its member states. The attempts from EU member state Germany to buy CDs with sensitive information violates Swiss law. The expert claims in the interview that the actions of the EU, especially of Germany are highly questionable and can not be tolerated. In his personal opinion it is a criminal act. Talking of the weakening of the banking secrecy, he affirms that the banking secrecy has been weakened and will become less important in the matter of taxation. However, domestic and foreign media barely reports about the assistance Swiss authorities have provided over the past years in cases of tax fraud and even tax evasion. Concerning data privacy the banking secrecy will remain and automatic exchange of information is not expected. (cf. Interview regarding the Swiss Banking Secrecy 2012). German tax law expert Moris Lehner explains that it is questionable whether a democratic state is allowed to buy such information which was illegally purchased in the first place. On the one hand it is important for the state to collect the taxes which it deserves on the other hand should the state no use instruments which go on a criminal level themselves. So with a purchase of such a CD Germany would encourage the act of denunciation. Lehner adds that in his opinion German courts will allow to use such CDs as evidence. Generally, it would cast a very dark shadow over the German state (Lehner 2010: 2-3). Switzerland see such attempts as a violation of their law, which resulted in the issuing of arrest warrants against German officials which were accused to buy such CDs with sensitive information (see Chapter. 4.4.2). Legally speaking, the attempts violate Swiss law and thus can not be tolerated, since Switzerland is a sovereign state and has various agreements with the EU and thus Germany. On the other side it can be argued that German authorities use all possible means to collect taxes which they deserve from German citizens who are breaking the law in the first place. Various agreements have been implemented already for mutual assistance in tax matters, further agreements are expected. Hence, H2 can neither be falsified nor confirmed.

- H3: The weakening of the Swiss banking secrecy by foreign authorities have had only short-term success, in the long term, the contrary dominates – the Swiss population, Swiss banks, as well as the government want to maintain and restrengthen the banking secrecy because of these attacks.

The interviewee clearly indicates that there is a strong political force (the majority of Swiss political parties) which wants to protect and keep the banking secrecy from being broken. The conservative forces in favour of the banking secrecy become more popular in virtue of the attacks. As well as the Swiss banks and SBA want to keep the banking secrecy. Touching upon the effects, it can be said that the Swiss financial centre will become less important. The attacks are direct attempts to harm the Swiss financial centre. The Swiss financial centre is a direct competitor of New York, London and Frankfurt and the respective states are concerned with serious debt problems either in their own country or in the EU. So it is also a tool to create a competitive advantage. It can be seen that foreign clients are uncertain, but the expert is sure that if legal security maintains and the decision makers communicate in clear ways, the future will bring an inflow of declared assets (cf. Interview regarding the Swiss Banking Secrecy 2012). So from an economic perspective the attacks had negative effects, referring to the UBS case and the Euro crisis (see Chapter 4.4.1). Politically as mentioned it can be said that banking commissions and associations along with the government do not see abandoning the Swiss banking secrecy as an option. The Swiss financial centre was not created from one day to another – it was a long process and in the world of finance there are certain factors which are of highest importance such as trust, legal and economic security, political stability, professionalism etc. (see Chapter 5.2). Switzerland‘s financial sector, its financial institutions and the country itself possessed those characteristics over decades and thus positive reputation was created. This reputation is the centre piece of the Swiss financial centre, once reputation is lost it is hard to regain it. That is why Swiss authorities and banks want to restrengthen and keep the banking secrecy, since it is an intrinsic part of Swiss culture. The public opinion affirms that. The representative study of the SBA in 2011 evaluated the public opinion of Swiss people concerning the Swiss banking secrecy. The representative survey shows that Swiss people have the opinion almost without exception that the financial privacy must be guaranteed and preserved from third parties (91%, in comparison to 2010: 89%) Only 7% are support the opposite. Concerning the bank client confidentiality 73% want to keep it, while 22 % want to abolish it (cf. Aktuelle Bankenfragen 2011 Meinungen und Vorstellungen der

Schweizer Bürger 2011: 37-41). Looking at the performance of the banks it can be seen in Chart 3 that because of the global economic crisis the performance of the the Swiss Private Banking Index lost significant points. As well looking at the UBS affair it can be seen that the curve stagnates. Nevertheless, in comparison with the other indexes Swiss banks respectively the Swiss Private Bank Index which includes the major banks UBS and Credit Suisse did not under perform. The curves of the MSCI Europe Banks as well as the MSCI World Banks the curves run similar to each other. Thus from an economic point of view it can be argued that the Swiss banks were not significantly affected, by the attacks of foreign authorities (cf. Birchler et al. 2011: 41-43). The hypotheses therefore can be confirmed.



Graph 2: Source: Bloomberg / Datastream (2011)

- H4: The banking secrecy is often used as a pretext – among other conditions, laws and regulations of the EU countries indirectly favour the Swiss financial centre.

The expert claims that it is definitely true that neighbouring countries of Switzerland follow a tax policy which favour tax evasion. Talking of Germany which has an income tax rate of 50%. Switzerland is among the countries in Europe with the lowest tax rates. It is the understanding in Switzerland that the states provides certain regulations which contribute to the quality of life. The taxation policy is such a regulation, better said policy which attracts foreigners. With signing the Schengen/Dublin agreements, free movement of labour and people was possible. Hence, foreigners wanted to profit from the Swiss regulations, high wages, political and economic stability. Despite that, it is true that the competition on the global market has become tougher. The individual market players use questionable measures to create competitive advantage, since the

Swiss financial centre is a direct competitor of the European financial centres. So there are certain policy makers and lobbyists which try to damage the reputation of the Swiss financial centre, especially the media does often not portray the objectively. Certainly, tax evasion was facilitated by the Swiss banking secrecy but this also means that its policies were misused. From a historical point of view, European countries suffered from political uncertainties over the decades. Due to the First World war as well as due to the Second World War European citizens had lost all their savings and assets. This fear somehow remained. The expert states that from personal experience with his clients from Germany, Italy or France he senses the fear that they would lose their savings once more in virtue of the Euro crisis, which is unlikely (cf. Interview regarding the Swiss Banking Secrecy 2012). To summarise, there is no doubt that due to economical crisis‘ the competition among the financial centres becomes more intense. Therefore all kinds of instruments are used in order to acquire clients or damage the reputation of competitors. Chapters 4.3.2 and 4.4.2 explain the contradictory and complex sides of H4, hence the hypotheses can neither be confirmed nor falsified.

9. Conclusions

The Swiss banking secrecy and the bank client confidentiality have been existing for more than a hundred years. It has been under criticism since its existence and implementation into constitutional law in 1935. Various myths and falsehoods exist about the Swiss banking secrecy. History shows why the Swiss financial sector has become one of the most competitive and prestigious in the world. The Swiss financial centre was able to remain its position among the best, despite undergoing economic crisis‘, being repeatedly attacked by foreign authorities and suffering loss of reputation. Various factors such as, trust, professionalism, political stability, legal security were improved over the decades, thus have raised the overall reputation of the Swiss financial sector. The most controversial factor for its success is without a doubt the banking secrecy. The banking secrecy is often misinterpret plus the knowledge about the reasons of its creation and implementation is often lacking. Due to movies and the media as well as international accusations, the Swiss banking secrecy and thus the Swiss financial centre are often facing prejudices. Switzerland is often portrayed as a rogue country. The Swiss banking secrecy has been considered a tool for criminal activity and tax evasion. The EU, especially Switzerland‘s neighbouring countries Italy, Germany and France want the Swiss government to abandon the Swiss banking secrecy laws and therefore attempted to harm it with more or less success. Concerning the questioning of the thesis about the future of Swiss

banking, the impact of the relationship between the EU and Switzerland on the banking secrecy, the conclusions can be made from an interconnected political and economic point of view. Talking of political aspects, it can be stated that Switzerland will remain its position and keep its policies concerning the banking secrecy. Due to cooperation and signing of agreements with the European Union, Switzerland guarantees mutual assistance in criminal matters. Nevertheless, no agreements so far had an actual affect on the Swiss banking secrecy. Switzerland does not see the automatic exchange of sensitive information as an option. This because of the Swiss thinking of protecting the individual privacy – the banking secrecy represents Swiss culture – the idea of freedom. Switzerland does not tolerate criminal actions such as money laundering or tax fraud and thus will continue to provide mutual assistance in exchanging information with foreign authorities. This only if the claims are well documented and indicate criminal action. Otherwise it is of high importance to avoid, better said not tolerate “fishing expeditions“. If the recent agreements revising the existing tax agreements pass through the different parliaments the issue of tax evasion can be resolved and the bank client confidentiality would remain and not be affected. Various EU member states see the Swiss banking secrecy as a competitive advantage and portray it as a harm to their own financial centres and the state itself. To summarise the political aspects; the issue of the Swiss banking secrecy can be resolved with the revised tax agreements, at least for a given time. The intentions of the banking secrecy, claim the Swiss, are only positive and benefit the individual freedom and privacy. The EU authorities remain in the position against the Swiss banking secrecy. Touching upon the economic aspects, it can be stated that there is no doubt that the Swiss banking secrecy has favoured tax evasion and thus given the Swiss financial sector an immense economic boost over the years. The attempts to weaken the banking secrecy have been successful and therefore major Swiss banks had to disclose sensitive information and pay fines to foreign authorities. Swiss banks and the Swiss Bankers Association have just recently stated that they will follow a strategy for legitimate money. The future will show whether the Swiss financial sector, its financial institutions, banks and insurances will be able to remain among the world leaders – a time of change has come to the Swiss financial centre and the Swiss banking sector.

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11. Personal Interview

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12. Appendix

Graph 1:

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