The End of Secret Swiss Accounts?: The Impact of the U.S. Foreign Account Tax Compliance Act (FATCA) on Switzerland's Status as a Haven for Offshore Accounts

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The End of Secret Swiss Accounts?: The Impact of the U.S. Foreign Account Tax Compliance Act (FATCA) on Switzerland’s Status as a Haven for Offshore Accounts

Jane G. Song*

Abstract: The closing of Switzerland’s oldest bank Wegelin in early 2013 was a symbolic moment for the Swiss banking industry. Add to Wegelin fourteen other Swiss banks under fire by the U.S. Department of Justice for aiding tax evasion, and Swiss banks no longer seem to be shrouded in a cloak of mystery. While Switzerland is still the top destination for offshore wealth, U.S.’s Foreign Account Tax Compliance Act (FATCA) began implementation in 2014. This Comment will argue that FATCA will fundamentally alter Switzerland’s status as a safe haven for secret offshore accounts, as Swiss banks promise to automatically provide the U.S. government with account information, and cooperate with other international transparency measures picking up momentum alongside FATCA. This Comment will also analyze FATCA’s impact on Switzerland’s banking policies regarding the transparency of offshore accounts used for foreign tax evasion and conclude by posing questions about the future of Swiss banking industry.

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INTRODUCTION

In the film *The World Is Not Enough*, James Bond asks, “If you can’t trust a Swiss banker, what’s the world come to?” We may have taken for granted that few, if any, illicit transactions that Bond dashed after would have existed without the help of Swiss bankers shuttling money around in secret accounts. But the question that has recently come up is exactly that: what if you can no longer trust a Swiss banker? The closing of Switzerland’s oldest bank Wegelin in early 2013 was a symbolic moment for the Swiss banking industry. A famed institution with 270 years of history shuttered its doors within one year after being indicted by the U.S. government for helping U.S. citizens avoid $1.2 billion in taxes through offshore accounts. Add to Wegelin fourteen other Swiss banks under fire by U.S. Department of Justice for aiding tax evasion, and Swiss banks no longer seem to be shrouded in a cloak of mystery.

Yet the real dagger aimed for the heart of Swiss secret banking has just been thrown. Although Switzerland is still the top destination for $8.5 trillion of offshore wealth, managing $2.2 trillion in 2012, U.S.’s Foreign Account Tax Compliance Act (FATCA) began implementation in 2014. In this Comment, I will argue that FATCA will fundamentally alter Switzerland’s status as a safe haven for secret offshore accounts, as Swiss banks promise to automatically provide the U.S. government with account information, and cooperate with other international transparency measures picking up momentum alongside FATCA.

This Comment will analyze FATCA’s impact on Switzerland’s banking policies regarding the transparency of offshore accounts used for foreign tax evasion. Part II will give the background on history of Swiss banking secrecy, U.S.-Swiss policies on secret banking, and major events that led up to the enactment of FATCA. Part III will explain the key provisions of FATCA, the two types of FATCA Intergovernmental

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1 *THE WORLD IS NOT ENOUGH* (MGM Studios 1999).
Agreements, and the mechanics of the 2013 U.S.-Switzerland Implementation Agreement (U.S.-Swiss Agreement). Part IV will illustrate how the current semi-automatic information exchange provision in the U.S.-Swiss Agreement is a huge shift from previous Swiss information exchange policies, and discuss how it will fundamentally change the Swiss banking landscape. I will show that Switzerland is significantly affected by its proactive efforts to comply with FATCA, which in turn challenges the economics of the Swiss banking industry, in particular the nature of Switzerland’s private banking business. Part V will then further assess how FATCA’s impact on Switzerland is in line with recent international trends for greater cross-border financial transparency. I will conclude by posing questions about the future of Swiss banking industry.

I. SWISS SECRET BANKING POLICIES AND EVENTS LEADING UP TO FATCA

Over the past century, Switzerland has developed a reputation for a secret banking system that affords the ultimate privacy and protection for its clients. Switzerland has become the ideal destination for tax evaders as a depository of more than 25% of the world’s offshore wealth in 2012. Meanwhile, it has been estimated that individual tax evasion has cost the U.S. government as much as $100 billion. In this section, I will describe how Switzerland’s secret banking business, U.S. policies against secret banking, various U.S.-Switzerland tax agreements, and the 2008 UBS tax evasion scandal have set the stage for the passage of FATCA and U.S.’s crackdown on tax evasion through secret Swiss accounts.

A. Swiss Banking Secrecy

Switzerland developed its financial and banking industry by responding to Europe’s market needs after the World Wars. When many countries experienced hyperinflation and exchange controls after World War I, wealthy Europeans began investing their assets in more stable countries including Switzerland. Swiss banks captured the market share of individuals who wanted to hide their assets from government investigation and feared the loss of their savings due to the instability in their home

7 See Urs Martin Lauchli, Swiss Bank Secrecy with Comparative Aspects to the American Approach, 42 ST. LOUIS L.J. 865, 866 (1998); W. BLACKMAN, SWISS BANKING IN AN INTERNATIONAL CONTEXT 18 (1989).
8 BOSTON CONSULTING GROUP, supra note 5, at 11.
10 BLACKMAN, supra note 7, at 16–17.
countries. By the end of Second World War, Switzerland had replaced Brussels in its status as a leading banking hub.

Yet it was the Swiss Banking Act that took Switzerland’s banking reputation to the next level. Despite their early twentieth century success, Swiss banks had to face the regulations of the Nazi government, which enacted legislation in 1933 requiring citizens of the Nazi regime to declare all of their foreign assets. So the Swiss Parliament in 1934 passed the Federal Act on Banks and Savings Banks (Swiss Banking Act), Article 47 of which established a code of secrecy for banking and account information. It created the concept of banker-client privilege, akin to lawyer-client privilege, that provided the utmost privacy to bank clients. The Swiss Banking Act sought to protect Switzerland’s economic sovereignty in its banking system, and prevent individuals and other entities from divulging financial information to foreign governments.

Under the current Swiss law, banking secrecy is protected under both civil and criminal codes. Civil law on bank secrecy exists in the Swiss Civil Code and the Code of Obligation. Article 28(1) of the Swiss Civil Code provides that a customer can petition a judge to bar a bank from releasing private information. Article 27 of the Swiss Code of Obligation gives a customer a cause of action against a bank for damages for violation of secrecy and disclosure of private information. The Swiss Penal Code complements the civil law by providing that bankers face criminal

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13 See Chambost, supra note 11, at 5.


15 See id. art. 47 (providing that any person who in his capacity as a body, employee, appointee or liquidator of a bank, or employee of an auditing firm, attempts to induce an infraction of the professional secrecy, is subject to imprisonment or fine).

16 See Campbell, supra note 11, at 664. Under Nazi laws, failure to report foreign holdings carried the death penalty. See Bernhard F. Meyer, Swiss Banking Secrecy and Its Legal Implications in the U.S., 14 New Eng. L. Rev. 18, 26 (1979). Thus Switzerland felt an economic as well as political impetus to enact banking law to protect itself from a serious threat to privacy. Id.


19 See Schweizerisches Obligationenrecht [OR] [Code of Obligations] Mar. 30, 1911, SR 220, art. 27 (Switz.) [hereinafter Swiss Code of Obligations]. These policies for banking secrecy are derived from contractual and agency principles. See Campbell, supra note 11, at 664.
prosecution if they divulge confidential information about their customers. Swiss Penal Code Article 271 prohibits financial institutions from acting on behalf of a foreign government, and Article 273 makes it a crime for a person to divulge secret business information to a foreign government authority. Thus, this multi-layered legal protection of banking secrecy fostered an environment for Switzerland to attract customers and flourish as the most competitive wealth management center in the world. Unsurprisingly, Switzerland also became an attractive destination for U.S. persons seeking to benefit from Swiss bank secrecy laws.

B. U.S.-Swiss Policies on Secret Banking and Tax Avoidance Prior to FATCA

While Swiss banks have faced no domestic civil or criminal liability when assisting international clients shelter assets in Switzerland, they have been subject to risk of liability and scrutiny by foreign governments, including the U.S. Thus over the past fifty years, U.S. and Switzerland entered into a number of agreements regarding bank secrecy and tax avoidance.

To begin, the U.S. legal system generally views foreign bank secrecy laws as promoting and facilitating illegal activity, and prosecutors have attempted to enforce its national laws regardless of their possible effect on foreign laws. While U.S. law recognizes that bankers owe a duty to not disclose customer information to a third party, it does not recognize that


21 See SWISS PENAL CODE


23 See, e.g., infra text accompanying note 69.


25 See Lauchli, supra note 7, at 878–79.
privilege when it comes to government inquiries. In 1970, in response to findings that secret bank accounts have been utilized by Americans to evade income taxes and conceal assets, Congress passed the Bank Secrecy Act (BSA) to provide the IRS with access to bank records and facilitate criminal and tax investigations for money laundering.

Since then, the U.S. has engaged in a number of tax agreements with Switzerland, principally to avoid international double taxation and prevent tax avoidance and evasion. Like the U.S., Switzerland enters into tax treaties with other nations to eliminate barriers against cross-border economic transactions. Tax agreements are critical because the U.S. is a key economic partner for Switzerland. The next paragraphs provide an overview of the U.S.-Swiss tax agreements that were signed prior to FATCA.

U.S. and Switzerland first entered into a tax treaty in 1951 (now replaced by the 1996 Treaty), focused on administrative assistance for eliminating double taxation of income. The treaty lacked any real bite on tax avoidance; Switzerland agreed to exchange information only in criminal cases involving “tax fraud,” a criminal offense narrowly defined under Swiss law. Also, the Swiss authorities were not required to provide the

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26 See id. at 877.
31 For a discussion of the importance of the U.S. market to Switzerland, particularly in context of Swiss banks, see infra notes 153–158.
33 See STAFF OF J. COMM. ON INTERNAL REVENUE TAXATION, 87TH CONG., LEGISLATIVE HISTORY OF UNITED STATES TAX CONVENTIONS 2388 (Comm. Print 1962). The 1951 Treaty did not target tax avoidance; it sought to eliminate double taxation by exemption in one of the countries or by applying credit. Id. U.S. already had similar conventions in force with Canada, Denmark, France, the Netherlands, Sweden, and the U.K. Id.
34 See 1951 Convention, supra note 32, art. XVI(1).
35 See BUNDESGESetz ÜBER DAS VERWALTUNGSTRAFRECHT [VSTRFB] [CRIMINAL ADMINISTRATIVE LAW] March 22, 1974, SR 313.0, art. 14(2) (Switz.). According to a long line of Swiss Supreme Court cases, tax fraud refers to tax avoidance of a significant amount when the taxpayer uses forged or fortified documents or adopts fraudulent conduct to deceive the tax administration. XAVIER
United States with the proof of the fraud for further U.S. proceedings.  

Thus, the first major U.S.-Swiss cooperation effort took place in 1973, when the two countries agreed to a Mutual Legal Assistance Treaty (Swiss MLAT) to combat organized crime. But because the Swiss MLAT was ineffective for tax-related matters, the two countries signed the Memorandum of Understanding (Swiss MOU) in 1982 for cooperation on insider trading investigations. Switzerland pledged assistance by outlining specific procedures for collecting and transmitting information to the United States.

The 1951 Treaty has been updated a number of times since its inception, to varied results. In 1996, the United States and Switzerland replaced the 1951 Treaty by improving the tax information exchange provisions and broadening the definition of “tax fraud,” but the treaty gave more attention to the limitation of its benefits to specific applicable parties, rather than to an exchange of information. So the 1996 Treaty was updated with a mutual agreement in 2003 to give way to “exchange information necessary to properly implement the provisions of the convention or to prevent tax fraud . . . .” In the 2003 Agreement, Swiss authorities agreed to turn over account information if the United States

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36 OBERSON & HULL, supra note 35, at 281. The Switzerland Supreme Court judgment on May 16, 1975, ATF 101 Ib 160, found that the Swiss authorities do not have to provide proof in accordance with U.S. implementing legislation. Id.


38 The Swiss MLAT generally excludes “violations with respect to taxes.” Id. art. 2.


40 See id. at 7–11. In 1981, Switzerland also enacted into law the International Mutual Assistance in Criminal Matters, which allowed the United States and any other country to obtain legal assistance from Switzerland if the offense was considered a crime in Switzerland, see BUNDESGESETZ ÜBER INTERNATIONALE RECHTSHILFE IN STRAFSACHEN [IRSG] [FEDERAL ACT ON INTERNATIONAL MUTUAL ASSISTANCE IN CRIMINAL MATTERS] Mar. 20, 1981, SR 351.1 (Switz.), http://www.admin.ch/opc/en/classified-compilation/19810037/201301010000/351.1.pdf.


42 Compare id. art. 22 (Limitation of Benefits), with id. art. 26 (Exchange of Information). In particular, The Memorandum of Understanding for the 1996 Treaty provides detailed explanation and examples for Article 22 (Limitation of Benefits). See id.

suspected that an individual was committing a “tax fraud” such as tax evasion using offshore accounts.\textsuperscript{44} Thus, the 2003 Agreement broadened the definition of “tax fraud” under the 1996 Treaty. However, it did not elaborate on the implementation of the “exchange of information.”\textsuperscript{45}

Finally, an amendment of the 1996 Treaty was proposed in 2011 to inch towards “a more robust exchange of information” between the United States and Swiss tax authorities.\textsuperscript{46} The Amendment based on a 2009 Protocol with Switzerland would change the standard for when Switzerland has to produce tax-related information, moving from the highly restrictive “tax fraud” standard to the less restrictive “may be relevant” standard.\textsuperscript{47} However, the United States has not been able to take advantage of such information exchange system because the Amendment is still pending ratification in the Senate.\textsuperscript{48} Therefore, while the United States has had a number of agreements with Switzerland regarding tax evasion, it has not been able to actually effectuate a successful information exchange mechanism. This would change with FATCA.

C. The UBS Scandal and the Lead-up to FATCA

A major impetus to the enactment of FATCA was the UBS scandal in 2008. The UBS scandal first pointed out problems with the existing qualified intermediary system for foreign financial institutions to report U.S.-source income to the IRS and withhold taxes on that income. Then, Switzerland’s compliant response to the UBS scandal set the stage to

\textsuperscript{44} See id. appendix (outlining 14 examples of tax evasion abuses considered “tax fraud,” each involving tax evasion using offshore accounts).

\textsuperscript{45} See id. (lacking explanation of what “exchange of information” entails).

\textsuperscript{46} Message to the Senate Transmitting the Protocol Amending the Swiss Confederation-United States, 2011 DAILY COMP. PRES. DOC. 52, at III (Jan. 26, 2011). The proposed 2011 Amendment seeks to enter into law a Protocol signed between the United States and Switzerland on September 23, 2009, as corrected by an exchange of notes effected on November 16, 2010, together with a related agreement effected by an exchange of notes on the same day. Id. The Protocol would give IRS greater access to Swiss banking records, and improve tax information exchange in a number of ways. See S. PERMANENT SUBCOMM. ON INVESTIGATIONS, 113TH CONG., OFFSHORE TAX EVASION: THE EFFORT TO COLLECT UNPAID TAXES ON BILLIONS IN HIDDEN OFFSHORE ACCOUNTS 35-37 (2014) [hereinafter OFFSHORE TAX EVASION REPORT]. The Protocol was signed into law in Switzerland in 2012, but has not yet been ratified by the Senate. Id. at 37. During the February 26, 2014 Senate Hearing, Credit Suisse pointed to the Senate’s failure to ratify the Protocol as the reason that the bank could not provide names of U.S. customers. See Joel Schectman, \textit{Credit Suisse: Senate Forcing Banks to Keep Secrets}, WALL ST. J. (Feb. 27, 2014, 11:03 AM), http://blogs.wsj.com/riskandcompliance/2014/02/27/credit-suisse-senate-forcing-swiss-banks-to-keep-secrets/.

\textsuperscript{47} EXPLANATION OF 2009 PROTOCOL, supra note 29, at 18. The Amendment follows the U.S. Model Income Tax Convention and the OECD standards for exchange of tax information. See Message to the Senate Transmitting the Protocol Amending the Swiss Confederation-United States, supra note 46, at III.

implement a more robust information exchange program—FATCA.

1. The UBS Scandal and Its Illumination of Problems with the Qualified Intermediary System

The Swiss and U.S. perspectives on banking secrecy came to a head-on collision with the UBS scandal. The U.S. Department of Justice’s investigation into UBS AG, a titan in Swiss private banking,\(^{49}\) revealed that the bank’s clients used undeclared Swiss Bank accounts to avoid reporting $20 billion of income to the IRS.\(^{50}\) This information came to light in 2007 with the confessions by Bradley Birkenfeld, a former UBS private banker who provided the IRS detailed accounts of how he helped U.S. taxpayers evade paying millions in U.S. taxes.\(^{51}\) The Department of Justice responded by filing a petition in the U.S. District Court for the Southern District of Florida requesting for leave to serve IRS administrative summons (John Doe Summons) with UBS, asking to disclose the names of all U.S. clients for whom the bank had not filed forms with the IRS disclosing their Swiss accounts.\(^{52}\)

In response to the UBS scandal, the Senate Permanent Subcommittee on Investigations (PSI) in July 2008 held publicized hearings on offshore accounts.\(^{53}\) The hearings addressed shortcomings with the current IRS program to pursue offshore accounts, the Qualified Intermediary (QI) system that has been effective since 2001.\(^{54}\) The QI system requires foreign banks to enter into Qualified Intermediary Agreements with the IRS, to identify and document any customers who hold U.S. investments or have received U.S.-source income into their offshore accounts, and withhold


\(^{52}\) See Memorandum in Support of Ex Parte Petition for Leave to Serve “John Doe” Summons at 6, In the Matter of the Tax Liabilities of John Does, No. 08-21864 (S.D. Fla. 2008).


income tax from payments of U.S.-source income received by foreigners.55

The hearings illuminated flaws in the design of the QI system. The most obvious issue is that a low percentage of U.S. income flows in through QIs.56 The QI system also only requires reporting on U.S.-source income and not foreign-source income,57 and does not require a look-through of foreign shell entities to determine the actual beneficial owner of the income.58 And while QIs have in place an auditing regime with external auditors, the auditors are not required to follow up on indications of fraud or illegal acts by the QI.59

The PSI hearings prompted a policy action. The hearings revealed that UBS helped its U.S. clients structure their foreign accounts to avoid QI reporting to the IRS.60 In response, then-IRS Commissioner Doug Shulman testified that the IRS was “taking a number of steps to enhance the QI program.”61 This mobilized the conversation for a stronger reporting regime for offshore accounts.62 In October 2009, the House and the Senate introduced the Foreign Account Tax Compliance Act (FATCA),63 seeking to address gaps in the QI system with a penalty withholding tax feature to increase compliance.64

FATCA was ushered into law on March 18, 2010, as part of the Hiring Incentives to Restore Employment Act.65 For foreign companies, key

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56 See GAO REPORT, supra note 55, at 14. For example, in 2003, about 88% of U.S.-source income reported to IRS were not reported by QIs. Id.

57 I.R.C. § 1441(a) (2013); see TAX HAVEN BANKS REPORT, supra note 54, at 22.

58 See GAO REPORT, supra note 55, at 22. IRS regulations allow withholding agents (domestic and QIs) to accept documentation declaring corporations’ ownership of income at face value, unless they have “a reason to know” that it is invalid. Rev. Proc. 2008-12, § 5.10.

59 TAX HAVEN BANKS REPORT, supra note 54, at 24; GAO REPORT, supra note 55, at 27.

60 TAX HAVEN BANKS REPORT, supra note 54, at 16.

61 Tax Haven Banks Hearings, supra note 53, at 60 (statement of I.R.S. Comm’r Doug Shulman).


FATCA provisions require foreign financial institutions (FFIs) to enter into an agreement with the IRS (FFI Agreement).\(^{66}\) They then must undertake certain identification and due diligence measures regarding their accountholders, report annually to the IRS on their U.S. accountholders, and in certain situations withhold and pay to the IRS 30% of any payments of U.S.-source income.\(^ {67}\) Thus, FATCA sought to create a “powerful incentive for foreign financial institutions to provide the IRS with the information it needs to identify persons seeking to evade U.S. tax.”\(^ {68}\)

2. Swiss Compliance with IRS Requests

After FATCA was enacted, there still lingered a big question whether Switzerland, a country with a large number of secret U.S. accounts,\(^ {69}\) would actively participate in the new information-reporting program. Switzerland signaled its answer to this question by acquiescing to U.S. requests for account information in the aftermath of the UBS scandal.

To settle the criminal charges from John Doe summons, UBS agreed to pay a $780 million penalty and pass on financial data of certain U.S. clients.\(^ {70}\) However, UBS initially did not comply with U.S. government standards, only releasing the names of about 300 individuals who had committed the narrow Swiss Penal Code definition of “tax fraud” of “affirmative acts of fraud or deception.”\(^ {71}\) So in February 2009, the Department of Justice filed another civil lawsuit against UBS to seek the identities of 52,000 more Americans suspected of hiding total of $15 billion at the bank.\(^ {72}\) UBS argued that Swiss law prevented them from providing information about their clients, and the Swiss government forbid its compliance.\(^ {73}\) However, under a final three-party agreement between UBS,

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\(^{66}\) I.R.C. § 1471(b) (2012).


\(^{68}\) Foreign Bank Account Reporting Hearings, supra note 64, at 10 (statement of Stephen E. Shay, Deputy Assistant Sec’y of the Treasury).

\(^{69}\) For example, Credit Suisse, as of 2006, “had over 22,000 U.S. customers with Swiss accounts whose assets, at their peak, exceeded 12 billion (CHF)” (about $13 billion). OFFSHORE TAX EVASION REPORT, supra note 46, at 3. Most of these accounts were undeclared. Id.


\(^{71}\) See Declaration of Barry B. Shott at 6, U.S. v. UBS AG, No. 09-20423 (S.D. Fla. Feb. 6, 2009), 2009 WL 3061580. For the Swiss definition of tax fraud, see supra note 35.

\(^{72}\) See Petition to Enforce John Doe Summons at 1, U.S. v. UBS AG, No. 09-20423 (S.D. Fla. Feb. 19, 2009), 2009 WL 864716.

\(^{73}\) Brief of UBS AG in Opposition to the Petition to Enforce the John Doe Summons at 40, United States v. UBS AG, No. 09-20423 (S.D. Fla. Apr. 30, 2009), 2009 WL 1612393.
the Swiss government, and the United States on August 19, 2009, UBS agreed to disclose the names of 4,450 U.S. account holders suspected by the IRS of evading taxes.74

The UBS settlement created the foundation for Swiss compliance with IRS requests.75 Since the UBS scandal, Swiss attitude towards the U.S. crackdown on tax evasion can be described of as one of appeasing compliance. Fourteen additional major Swiss banks, including Credit Suisse, came under criminal investigation by prosecutors across the country for aiding tax evasion.76 Wegelin, the oldest Swiss bank, was indicted, pled guilty, and then filed for bankruptcy in 2013.77 To prevent other banks from suffering the same fate as Wegelin, Switzerland negotiated a non-prosecution agreement with the United States in August 2013 that requires Swiss banks to voluntarily come forward, disclose undeclared American assets on their books, and pay related penalties.78 By January 2014, 106 of

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77 See Raymond & Browning, supra note 2.

78 See Joint Statement Between the U.S. Department of Justice and the Swiss Federal Department of Finance, U.S.-Switz., Aug. 29, 2013, available at http://www.justice.gov/iso/opa/resources/7532013829164464664074.pdf [hereinafter 2013 Joint Statement]. The banks that take part in the non-prosecution program are required to provide details on American accounts, “inform on banks that transferred money into secret accounts or that accepted money when secret accounts were closed,” and “reveal all cross-border activities and close accounts of Americans evading taxes...” Robert W. Wood, Swiss Bank Frey To Close Over IRS Investigation, FORBES (Oct. 17, 2013, 11:09 PM), http://www.forbes.com/sites/robertwood/2013/10/17/swiss-bank-frey-to-close-over-irs-investigation/. “The fines for banks are set in tiers based on time.” For example, “banks that held accounts as of August
some 300 Swiss banks signed onto the program, the goal of which was to “enable every Swiss bank that is not already under criminal investigation to find a path to resolution.” This series of events set up an environment for Swiss compliance with FATCA.

In addition to its dealings with the United States, Switzerland also made attempts to comply with international transparency standards by signing twelve bilateral tax cooperation agreements with OECD members. In 2013, Switzerland signed the OECD Tax Convention to become the 58th country to join the OECD’s convention on sharing tax information with foreign tax authorities. As Switzerland responds to pressure from the United States to help fight tax evasion, its actions signal how Swiss political support for bank secrecy may have diminished in the recent years.

II. FATCA AND ITS IMPLEMENTATION IN SWITZERLAND

Since its 2010 enactment, FATCA has been at the center of both revelation and criticism as the world geared up for its official rollout in

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1, 2008, must pay a fine equal to 20% of the top dollar value of all non-disclosed accounts.” Id. However, fourteen banks already under investigation by the U.S. government are excluded from the agreement. See 2013 Joint Statement, supra note 78, at § I.A.


81 Note that Swiss banks are generally uneasy about the non-prosecution program: most of the banks surveyed by EY have “somewhat negative” or “negative” view of the effect of the disclosure program on Switzerland as a financial center. ERNST & YOUNG, EY BANKING BAROMETERS 2014: NEW REALITIES IN SWISS BANKING 18 (2014).

82 See Mathieu van Berchem, Switzerland Passes OECD Grey List Hurdle, SWISSINFO.CH (June 1, 2011, 10:41 PM), http://www.swissinfo.ch/eng/Specials/Rebuilding_the_financial_sector/News_results_regulations/Switzerland_passes_OECD_grey_list_hurdle.html?cid=3037085. As result of the UBS scandal, Switzerland was added to OECD’s “Grey List” of tax havens in 2009, and had to sign bilateral agreements to get off the list. Id.


84 Switzerland’s current Finance Minister Eveline Widmer-Schlumpf has pushed for a more administrative assistance and disclosure to fight international tax evasion. Switzerland’s Parliament and Federal Council have taken legislative actions in this effort. See Swiss Edge Further Away from Bank Secrecy with New Tax Steps, REUTERS (Oct. 9, 2013, 8:54 AM), http://www.reuters.com/article/2013/10/09/us-swiss-tax-idUSBRE99OIGW20131009 (describing that Switzerland is bowing under pressure from the United States and the EU to end bank secrecy); Catherine Bosley, Swiss Bankers Stripped of Secrecy as Data Swap Embraced, BLOOMBERG (June 18, 2013, 5:01 PM), http://www.bloomberg.com/news/2013-06-17/swiss-bankers-stripped-of-secrecy-as-minister-embraces-data-swap.html (reporting that Switzerland’s interactions with the United States signal “cleaning-up of the legacies,” and that the country is heading toward automatic exchange of information).
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2014. The United States has successfully negotiated a number of intergovernmental agreements, including with Switzerland, to facilitate FATCA’s implementation around the world. In this section, I will first highlight the key features of FATCA. Next, I will describe the two types of FATCA model intergovernmental agreements. This will then segue into an explanation of the U.S.-Swiss Agreement.

A. Mechanics of FATCA

FATCA was designed to strengthen U.S. law in tax withholding procedures and weak information arrangement between countries. It boils down to a two-prong approach: first, disclosure requirements for U.S. taxpayers with foreign accounts, and second, more controversial requirements for “foreign financial institutions” (FFIs). This section will focus on the requirements for FFIs.

In a nutshell, FFIs have to sign an agreement with the IRS (FFI Agreement) to identify the residency status of their clients, and provide the IRS with U.S. account information. FFIs are broadly defined: in addition to banks, non-U.S. entities such as broker/dealers, insurance companies, hedge funds, securitization vehicles, and private equity funds are considered

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86 Foreign Bank Account Reporting Hearings, supra note 64, at 9–10. Note that there have been bills proposed to update or amend parts of the FATCA to heighten the stringency of FATCA enforcement. See, e.g., Stop Tax Haven Abuse Act, S. 174, 114th Cong. (2015); Cut Unjustified Tax Loopholes Act, S. 268, 113th Cong. (2013).

87 See I.R.C. § 6038D(a) (2012). Individual U.S. taxpayers with foreign accounts and assets exceeding $50,000 on the last day of the tax year have to report them on an information return. Id.

88 See I.R.C. § 1471.

89 See id.

90 FFIs include any foreign entity that accepts deposits, holds financial assets for others as a substantial portion of its business, or engages in the business of investing, reinvesting, or trading in securities, partnership interests, or commodities. See id. 1471(d)(2); Treas. Reg. § 1.1471-5(b)(3) (2013).
FFIs.\textsuperscript{91}

FFIs have to sign up with the IRS and comply with a number of reporting requirements. FFIs must obtain information for each account holder to determine whether the account is a “U.S. account”—an account of a U.S. person or foreign entity with substantial U.S. ownership.\textsuperscript{92} Under Final Treasury Regulations for FATCA, FFIs have to conduct a stringent due diligence and verification process to identify, document, and classify existing client relationships.\textsuperscript{93} FFIs then have to report information on U.S. account holders to the IRS.\textsuperscript{94} Required information includes account balance or value of each U.S. account,\textsuperscript{95} as well as amount of dividends, interest, other income, and gross proceeds from the sale of property credited to a U.S. account.\textsuperscript{96}

While FATCA is theoretically “voluntary,” FFIs that do not sign an agreement with the IRS are subject to a 30% withholding tax on U.S.-derived income including interest, dividends, gross proceeds from disposition of U.S. securities, and pass-through payments.\textsuperscript{97} Also, U.S. account holders that do not provide requested information to FFIs in order to comply with FFI Agreements will be considered “recalcitrant account holders”\textsuperscript{98} and FFIs must withhold a 30% tax on the U.S.-source payments it makes to those account holders.\textsuperscript{99}

B. FATCA Intergovernmental Agreements

The IRS has recognized that the international reach of FATCA could be at odds with local laws, and that foreign government cooperation will be necessary to enforce FATCA around the globe.\textsuperscript{100} With that in mind, the


\textsuperscript{92} See I.R.C. § 1471(d)(1).

\textsuperscript{93} DEPT OF THE TREASURY & INTERNAL REVENUE SERVICE, REGULATIONS RELATING TO INFORMATION REPORTING BY FOREIGN FINANCIAL INSTITUTIONS AND WITHHOLDING ON CERTAIN PAYMENTS TO FOREIGN FINANCIAL INSTITUTIONS AND OTHER FOREIGN ENTITIES 38, 39 (2013); Treas. Reg. § 1.1471-4(c).

\textsuperscript{94} See I.R.C. § 1471(c); Treas. Reg. § 1.1471-4(d)(3).

\textsuperscript{95} See I.R.C. § 1471(c); Treas. Reg. § 1.1471-5.

\textsuperscript{96} See I.R.C. § 1471(b).

\textsuperscript{97} See id. § 1471(d)(6).

\textsuperscript{98} See id. § 1471(b)(1)(D)(i).

\textsuperscript{99} See id. § 1471(b)(1)(D)(ii).

Treasury developed Intergovernmental Agreements (IGAs), beginning with the U.K. in 2012. Since then, the United States has signed bilateral IGAs with more than fifty-five countries, and has reached agreements in substance with fifty-seven additional jurisdictions.

To facilitate IGAs, FATCA Model Agreement I (Model I) created a framework that allows foreign institutions to report the necessary information regarding U.S. accounts to their respective governments rather than to IRS directly, while still avoiding FATCA withholding. Thus, Model I provides for an automatic exchange of information between IRS and the foreign tax authority. As defined by the OECD, automatic exchange of information “involves the systematic and periodic transmission of ‘bulk’ taxpayer information by the source country of income to the country of residence of the taxpayer concerning various categories of income.” The automatically exchanged information is collected by the tax authorities in the source country and systematically sent to the tax authorities in the residence country. Commentators favor this automatic exchange of information for reasons including timeliness, early fraud detection, deterrent effects that increase voluntary compliance, and ease of administrability.

With respect to Switzerland, the United States’ parallel joint statements with Japan and Switzerland in June 2012 revealed an alternative model agreement (Model II) for FATCA implementation. Under Model statement, the six governments agreed to explore a common approach to FATCA implementation through domestic reporting and reciprocal automatic exchange, based on six existing bilateral treaties. Id.


102 See FATCA Resource Center, supra note 85.


106 See id. at 3–4.


108 See Press Release, U.S. Dep’t of Treasury, Joint Statement from the United States and
II, the financial institutions themselves have to send the names and data of their customers directly to the IRS after obtaining consent from their customers. Thus, the exchange of information is not between governments as in Model I, but rather between the FFIs and the IRS. The joint statements with Japan and Switzerland created a launch pad for the agreement between the United States and Switzerland for implementation of FATCA (the U.S.-Swiss Agreement), which was signed on February 14, 2013.

C. The U.S.-Swiss Agreement

The U.S.-Swiss Agreement, based on Model II, requires Switzerland to direct all reporting Swiss financial institutions to register with the IRS by January 1, 2014, and to comply with FATCA due diligence, reporting, and withholding requirements. Switzerland agreed to instruct reporting Swiss financial institutions to request certain information from preexisting account holders and report it to the IRS, and to obtain consent from new account holders to report this information as a condition for opening the account. The U.S.-Swiss Agreement guarantees Swiss financial institutions that they will not be prosecuted in Switzerland if they report bank information to the IRS. Otherwise, Swiss financial institutions

See Joint Statement with Switzerland, supra note 109.


See id. art. 3.

See id. (FFIs have to collect information such as the name, address, and Tax Identification Number of the U.S. account holder, the account number, the account balance or value, and payments made with respect to the account holder); see also Treas. Reg. § 1.1471–4(d)(3).

See U.S.-Swiss Agreement, supra note 109, art. 4.
would have to make the difficult decision to either comply with FATCA or face disclosure liability under the Swiss Penal Code. The Swiss government has essentially lifted the veil of banking secrecy with respect to U.S. customer information within the parameters of FATCA.

The mechanics of U.S.-Swiss Agreement operates as follows. In order to service U.S. customers, a Swiss financial institution has to enter into a FFI agreement with the IRS to comply with IRS reporting requirements according to Final FATCA Regulations. Entering into a FFI agreement eliminates the FFI’s 30% penalty tax on all payments of U.S.-source income. After entering into a FFI agreement, the financial institution has to receive consent from a U.S. person or U.S.-owned foreign entity in order to supply their information to the IRS. If the account holder declines consent, the financial institution cannot deliver individual information to the IRS without violating Swiss banking secrecy rules still in effect.

However, Swiss financial institutions will be required to annually report “aggregate information” on non-consenting accountholders to the IRS. The U.S. Competent Authority (the Secretary of Treasury) may then use the aggregate information received as the basis for submitting a “group request” for specific information. Upon receiving a group request, the Swiss Federal Tax Administration (Swiss FTA) has to follow specific procedures to provide the information to the U.S. Competent Authority. Swiss financial institutions are not required to withhold tax or close non-consenting accounts unless a group request has been received and the Swiss financial institution is unable to provide the Swiss FTA with information to be exchanged with the IRS within eight months.

In sum, the U.S.-Swiss Agreement is more cooperative than any of the prior agreements with the United States regarding offshore tax evasion or tax collection.

III. THE IMPACT OF FATCA ON THE SWISS BANKING INDUSTRY

Since its introduction, FATCA has had and will continue to have a significant impact on the Swiss banking industry. FATCA turned the Swiss banks’ long-held tradition of secrecy upside down, and the banking industry
is witnessing the micro and macro-level economic impacts of its implementation. In this section, I will first show that the semi-automatic nature of information exchange in the U.S.-Swiss Agreement creates a new standard for banking transparency in Switzerland, in sharp contrast to Switzerland’s previous information exchange policies. Then I will explain Switzerland’s incentives to proactively comply with FATCA, and the additional measures it introduced to facilitate its compliance. Finally, I will describe how Switzerland’s compliance with FATCA is reshaping the look and character of the Swiss banking industry and affecting the competitiveness of Swiss banks in the world stage.

A. A Semi-Automatic Exchange of Information: A Huge Shift for Switzerland

The current U.S.-Swiss Agreement provides for a Model II “semi-automatic exchange of information,” a level of disclosure that represents a huge step toward transparency for Switzerland. In the context of Switzerland’s legal construct for secret banking, where bankers are subject to criminal penalties if they do not protect the identities of their clients, the U.S.-Swiss Agreement’s provision for systematic exchange of account information presents a stark juxtaposition.

Although the U.S.-Swiss Agreement does not provide for a completely automatic exchange of information as defined by the OECD, and there is no reciprocity requirement in law for U.S. institutions to disclose the information of U.S. residents in noncompliant countries, the U.S.-Swiss Agreement’s provision for systematic exchange of account information presents a stark juxtaposition.

125 See supra Part III.A.
126 According to the OECD, automatic exchange of information “involves the systematic and periodic transmission of ‘bulk’ taxpayer information by the source country of income to the country of residence of the taxpayer concerning various categories of income.” See supra notes 105–107 and accompanying text.
127 FATCA was written as a unilateral system for foreign financial institutions to provide information, but the Treasury has negotiated a number of IGAs with promises of reciprocity on United States’ part. See, e.g. Agreement Between the Department of Treasury of the United States of America and the Ministry of Finance and Public Credit of the United Mexican States to Improve International Tax Compliance Including with Respect to FATCA, U.S.-Mex., art. 6(1), Apr. 17, 2014, U.S. DEP’T OF TREASURY, available at http://www.treasury.gov/resource-center/tax-policy/treaties/Documents/FATCA-Agreement-Mexico-4-17-2014.pdf. To move towards reciprocity, the Treasury has promulgated regulations to require U.S. banks and credit unions to report information on interest paid to nonresident aliens. 26 C.F.R §§ 1.6049-4(b)(5)-8. Additionally, Treasury’s Financial Crimes Enforcement Network (FinCEN) issued a notice of proposed rulemaking to facilitate reporting and tax compliance investigation in order to advance international commitments made through FATCA reciprocal IGAs. Press Release, U.S. Dep’t of Treasury, Treasury Issues Proposed Rules to Enhance Financial Transparency (July 30, 2014), http://www.treasury.gov/press-center/press-releases/Pages/jl2595.aspx; Jay R. Nanavati, United States: Treasury’s FinCEN Proposes Rules Forcing U.S. Financial Institutions To Collect Data For FATCA Reciprocity, NASDAQ, Aug. 5, 2014,
same information to Swiss authorities, the Agreement has many of the features that an automatic exchange of information system aims for. The U.S.-Swiss Agreement is a two-step information exchange: while the main exchange is between the financial institution and the IRS, the Swiss FTA steps in upon a group request and delivers information to the U.S. authorities when there is hindrance from non-consenting account holders. Thus, there is a “systemic and periodic transmission of ‘bulk’ taxpayer information by the source country of income to the country of residence of the taxpayer” as is the case for a completely automatic system.

Moreover, the U.S.-Swiss Agreement is even more remarkable when compared to other multilateral tax agreements that Switzerland has recently engaged in. In the few years prior to FATCA, Switzerland entered into “Rubik Agreements” with key trading partners Austria, Germany and the U.K. that focused on anonymous tax withholding as a substitute for automatic information exchange for non-Swiss residents holding Swiss accounts. For example, the Swiss-Austria agreement requires Swiss banks to levy a 25% withholding tax on future investment income and capital gains of Austrian tax residents equal to the Austrian capital yields tax. The Swiss banks then transfer the proceeds of the withholding tax to the Austrian Ministry of Finance. Once the Swiss banks impose the withholding tax, the tax resident’s Austrian tax obligation is fulfilled.


128 See U.S.-Swiss Agreement, supra note 109, art. 5 ¶ 3.
129 See OECD, AUTOMATIC EXCHANGE OF INFORMATION: THE NEXT STEP, supra note 106, at 3.
130 The “Rubik” model (like the name of the famous puzzle) was created by the Swiss Association of Foreign Banks to separate income from wealth and send tax at source to third countries, while maintaining the Swiss bank account holder’s anonymity. See British Receive Initial Funds From Tax Deal, SWISSINFO.CH, Jan. 30, 2013, http://www.swissinfo.ch/eng/british-receive-initial-funds-from-tax-deal/34867206; see also infra notes 131-142 and accompanying text.
133 See id. at 4.
134 See id. at 3. Alternatively, Austrian taxpayers can authorize their Swiss bank to report their future
Further, Switzerland reports to the partner country names of ten jurisdictions to which the partner country residents who close their Swiss accounts transfer the largest volume of assets, as well as the number of partner country residents who moved funds out of Switzerland to those jurisdictions. However, Switzerland does not have to disclose the actual identity of those individuals. These arrangements are intended to maintain client anonymity through anonymous withholding. The end result encourages Switzerland’s partner country to pressure the jurisdictions where the partner country’s residents move their money to create additional Rubik Agreements with the partner country, further perpetuating Rubik Agreements as the standard.

In effect, the Rubik Agreements allow Swiss financial institutions to opt for in-country tax withholding instead of bulk transmission of account information back to the resident country. While there are a number of significant administrative issues raised by this method, the anonymous withholding method has been justified by Switzerland “as a means of protect[ing] the financial privacy of account holders.” But from the partner countries’ perspective, automatic exchange of information is superior to anonymous withholding for reasons such as reaching untaxed principle, maintaining a sense of fairness, and providing a multilateral solution. Practically speaking, these anonymous withholding agreements have hampered the emergence of automatic cross-border information reporting system. Their endorsement by Switzerland, a major offshore asset management center, has diminished Switzerland’s opportunity to lead other

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135 See Grinberg, supra note 108, at 342.
136 See id.
137 See id.
138 See id.
139 See id.
140 Swiss banks themselves have to compute and withhold the tax amounts for each customer after figuring out their individual tax residency and assets in possession. Then the proceeds are remitted anonymously to the partner country. See id. at 340–41.
141 See id. at 339. These anonymous withholding agreements assert that they achieve a level of cooperation that would be “equivalent” to an automatic exchange of information. Id. at 342–43 (citing Swiss-Austria Cooperation Agreement, supra note 133, art. 1; Swiss-U.K. Cooperation Agreement, supra note 133, art. 1; Swiss-Ger. Cooperation Agreement, supra note 133, art. 1). Thus, Switzerland’s ratification of these agreements with key financial centers would achieve a political goal of Swiss policy, the acceptance of the idea that anonymous withholding is equivalent to automatic exchange of information. Id. at 343.
financial centers towards a more open exchange system.\textsuperscript{143}

Thus, by agreeing to an exchange of information and supplying detailed account information to the U.S. government instead of withholding anonymously, the U.S.-Swiss FATCA Agreement represents a fundamental shift from Switzerland’s previous information disclosure policies. More remarkably, Switzerland has recently indicated an intention to negotiate a reciprocal Model I IGA to replace its Model II IGA.\textsuperscript{144} This is a big step for Switzerland — among other changes, going from Model II to Model I will place a greater administrative burden for Switzerland because the Swiss tax authority will act as an intermediary between FFIs and the IRS.\textsuperscript{145} On the other hand, Model I’s automatic exchange of information between governments reduces compliance costs for FFIs.\textsuperscript{146} Model I is the OECD’s “preferred route for the implementation of FATCA,” and also serves as the template for the common international model for automatic exchange of information.\textsuperscript{147} Thus, the anticipated change will perpetuate the “Swiss commitment to automatic exchange of information at the [g]lobal [f]orum.”\textsuperscript{148}

B. Changes in the Swiss Banking Landscape Due to FATCA

The Swiss banking landscape has already been shaped, and will continue to be shaped by FATCA. This is because Switzerland is economically incentivized to actively comply with FATCA despite its high costs. Also, recent events in Switzerland continue to demonstrate the country’s willingness to cooperate with the U.S. on tax related matters. In turn, FATCA will have a significant impact on the nature of the Swiss banking industry.

\begin{itemize}
\item \textsuperscript{143} See Grinberg, supra note 108, at 340.
\item \textsuperscript{145} See id. For a discussion of differences between IGA Models I and II, see supra notes 103–111 and accompanying text.
\item \textsuperscript{148} Swiss Automatic Exchange of Information Press Release, supra note 146.
\end{itemize}
1. Switzerland’s Proactive Compliance Efforts

It is evident that Switzerland is making proactive efforts to comply with FATCA requirements. Swiss banks cannot escape FATCA because not only is the U.S. an important market, but the 30% penalty for FFIs is triggered on their payments of U.S.-source income. Also, recent judicial and parliamentary decisions in Switzerland indicate the country’s willingness to comply with FATCA requirements.

To begin, while FATCA presents significant administrative burdens, Swiss banks will make an effort to comply because of the importance of the U.S. market for Swiss banks. Some of the criticisms of FATCA point to reports that Swiss banks are denying accounts to U.S. citizens in order to evade FATCA compliance.\(^{149}\) There also seems to be evidence that U.S. citizens are renouncing their citizenship to avoid U.S. taxation;\(^{150}\) the number of people renouncing their U.S. citizenship set a new record in 2015, and a recent survey revealed that 76% of Americans abroad feel incentivized to give up their U.S. passports.\(^{151}\) However, it is not feasible for Swiss institutions to simply deny accounts to all U.S. individuals and entities.\(^{152}\) The size of U.S. wealth still remains attractive for Swiss banks—North America occupied 36% of global millionaire wealth in 2008, and its share is expected to hover around 34% in 2016.\(^{153}\) As the CEO of private Swiss bank Vontobel put it, “the U.S. is simply too big, too wealthy[,] and too important.”\(^{154}\)

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\(^{149}\) See Foreign Bank Account Reporting Hearings, supra note 64, at 70 (noting that U.K., Swiss, Dutch, and Spanish banks are refusing as clients U.S. citizens living in their countries).

\(^{150}\) Laura Saunders, Overseas Americans: Time to Say ‘Bye’ to Uncle Sam?: Chased by the U.S. Government, Thousands Are Severing Ties With America. Here’s What You Need to Know, WALL ST. J., Aug. 16, 2013, http://online.wsj.com/article/SB100014241278873323455104579014772169287210.html. But note that renunciation of citizenship requires individuals to file back taxes, pay any penalties owed, and also face exit tax on individuals with annual income of $150,000 or have a net worth of at least $2 million. I.R.C. § 877(a)(2) (2006).


\(^{154}\) U.S. Wealth Market Still Attractive for Swiss Banks – Vontobel CEO, REUTERS, Sep. 12, 2013, http://www.reuters.com/article/2013/09/12/vontobel-unitedstates-ceo-idUSL5N0H831J20130912. The CEO commented that the profit margins in emerging markets “are less attractive than in the U.S.” Id.
Additionally, refusing to accept U.S. account holders will not relieve a FFI from being subject to FATCA because the 30% withholding tax for FFIs that do not sign a FFI Agreement is triggered on their U.S.-source income.\footnote{See I.R.C. § 1471; Treas. Reg. § 1.1471-2.} Switzerland is among the top investors in the U.S.: Swiss cumulative investment was estimated at $212 billion in 2013, and U.S. represented 19.8% of Switzerland’s direct investment abroad in 2011.\footnote{See B.J. Henderson et al., World Markets for Raising New Capital, 82 J. FIN. ECON. 63, 73–75 (2006) (finding that U.S. has the largest capital market in the world, and is home to 66% of the total global cross-border equity issues). See also Stavros Peristiani, Evaluating the Relative Strength of the U.S. Capital Markets, CURRENT ISSUES ECON. & FIN. (Fed. Reserve Bank of N.Y., New York, N.Y.), July 2007, at 1 available at http://www.newyorkfed.org/research/current_issues/ci13-6.pdf (noting that New York City is a leading site for conducting business because the effective performance of U.S. capital markets).} Also, Swiss finance and insurance affiliates are estimated to hold more than $1.4 trillion in U.S. assets.\footnote{See Robert Wood, Swiss Banks Reveal Americans, U.K. Deal Sputters, And Germany Embraces FATCA, FORBES, Jul. 9, 2013, http://www.forbes.com/sites/robertwood/2013/07/09/swiss-banks-reveal-americans-u-k-deal-sputters-and-germany-embraces-fatca/. This was a follow-up to 2011, when Swiss tax authorities gave the go-ahead to temporarily circumvent Switzerland’s vaunted bank secrecy laws. For a discussion of the 2011 Amendment, see supra notes 46–48.} So in order for FFIs to avoid 30% tax on investments earned in the U.S., they have to comply with FATCA reporting regulations. While FATCA may lead to Swiss institutions discouraging U.S. investments, Swiss financial institutions ultimately will not be able to overlook the significance of the U.S. capital market.\footnote{During the March 2014 Senate Hearing on offshore tax evasion, Credit Suisse urged the Senate to pass the 2011 Amendment, which would “allow for much more information to be provided on U.S. client accounts to U.S. authorities.” CREDIT SUISSE, LEGACY U.S.-SWISS TAX ISSUES: STATEMENT OF CREDIT SUISSE, FOR UNITED STATES SENATE PERMANENT SUBCOMMITTEE ON INVESTIGATIONS COMMITTEE ON HOMELAND SECURITY AND GOVERNMENTAL AFFAIRS 5 (2014). For more on the 2011 Amendment, see supra notes 31–34.}

Further, recent events in Switzerland reaffirm the country’s willingness to cooperate with U.S. on tax evasion matters under specified parameters. On July 5, 2013, the Federal Supreme Court of Switzerland ruled that IRS’s “group requests” under the 1996 Treaty is permissible if the requests include enough detail to establish grounds for suspicion of fraud.\footnote{See Press Release, Swiss Federal Supreme Court, Exchange of Information in Tax Matters with the United States – The Federal Supreme Court Rejects a First Appeal, at 1 (Jul. 5, 2013), http://www.bger.ch/fr/press-news-2c_269_2013-eng-t.pdf.} Thus, the Court upheld the lower court’s decision that Credit Suisse can reveal client data to U.S. authorities.\footnote{On January 6, 2014, the Federal Administrative Court in St. Gallen rejected the appeal against the Federal Supreme Court’s decision (see supra note 158).} Switzerland is trying to ascertain the boundaries of this decision.\footnote{On January 6, 2014, the Federal Administrative Court in St. Gallen rejected the appeal against the Federal Supreme Court’s decision (see supra note 158).}
Gallen blocked Julius Baer’s transfer of account information to the IRS because the IRS’s request did not meet the “level of detail which is required for which administrative assistance can be granted.” Nevertheless, while the federal court delayed Julius Baer’s release of information given the circumstances, the decision does not necessarily threaten the core of the Supreme Court’s July 2013 ruling permitting banks to respond to IRS’s group requests within sufficient parameters.  

Finally, in September 2013, the Swiss parliament voted in favor of a Swiss law that requires Swiss banks to report the holdings of U.S. clients to U.S. tax authorities, essentially enacting FATCA as law. The Swiss House of Representatives and the Senate both approved the law, after the lower house initially rejected the bill twice and fueled speculation that Switzerland would not comply with FATCA. Thus, Swiss Banking Association’s “welcoming of the signing of the [U.S.-Swiss Agreement]” for reducing the “complexity and costs arising from the unilateral FATCA legislation” seems to have symbolized the country’s willingness to cooperate with U.S. authorities regarding FATCA.

2. Impact on the Swiss Banking Industry

The burden of implementing FATCA is substantially impacting the economic health of the individual Swiss banks as their costs rise and...
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margins fall. FATCA is perpetuating the consolidation of Swiss banks that began during the recession. The consolidation, in conjunction with international pressure for transparency, is reshaping the look and character of the Swiss private banking industry.

To start, FATCA is costly for Swiss banks. The Swiss Banking Association has estimated the implementation costs for FATCA to be around CHF 200-300 million.\(^{169}\) This is on top of the hefty settlement cost many banks are enduring for U.S. criminal investigations for facilitating tax evasion. At the same time, declined margins have now become the norm for Swiss banks since the recession.\(^{170}\) The decline is attributed to relatively flat new money, low performance of assets under management, and elevated competitive and regulatory pressures.\(^{171}\) According to a September 2014 study of Swiss private banks, KPMG found that one-third of Swiss private banks in its study were in continuing decline, while two-thirds of these banks posted negative returns in 2013.\(^{172}\) The number of these banks reporting losses increased more than 50% from 2012 to 2013.\(^{173}\) Further, the banks in the study that paid for U.S. tax evasion fines and related costs saw their return on investment decline by negative 8.2 percentage points in 2013.\(^{174}\) These changes undoubtedly impact the Swiss economy, where the banking sector alone accounts for CHF 35 billion of added value, or 6% of the overall economy.\(^{175}\)

As a result, bank consolidation has become a real phenomenon in Switzerland.\(^{176}\) KPMG found that January to July 2014 saw M&A activity


\(^{171}\) Id. at 5.

\(^{172}\) Id. at 6, 12.

\(^{173}\) Id. at 8 (finding that 23 banks reported losses in 2012, and 34 banks in 2013).

\(^{174}\) Id. at 41 (noting that these banks represented only one-fifth of all Swiss private banks, so many more are likely exposed in the coming years). See also supra note 80 and accompanying text (stating that more than 106 Swiss banks have voluntarily come forward as of January 2014).


\(^{176}\) Swiss private banking business has been going through a fundamental change and facing a number of challenges, namely increased regulation, consolidation, and declining margins. See DELOITE WEALTH MANAGEMENT CENTER RANKING 2013, supra note 22; PwC, THE END OF A GOLDEN AGE? PWC PRIVATE BANKING STUDY (2013), available at http://www.pwc.ch/user_content/editor/files/publi_adv/pwc_private_banking_study_2013_e.pdf [hereinafter PWC PRIVATE BANKING STUDY]; SWISS
involving almost 10% of the Swiss private banks in its study, involving around CHF 125 billion in assets under management. Smaller Swiss banks that are more pessimistic about future outlook have been particularly affected by cross-border regulatory developments and decline in profitability, and thus driven into consolidation. So while small and medium-sized banks have suffered outflows of assets under management (at the end of 2013, small banks represented 61.7% of KPMG’s sample but only 7.8% of total assets under management), large banks have won market share (from 59% in 2008 to 78% in 2013). This is in line with the number of banks in Switzerland dropping from 338 in 2005 to 283 in 2013, a 16% decline.

Since the enactment of FATCA, the pressure for transparency has impacted the prominent market niche that Switzerland occupied in secret private banking. Most private Swiss banks direct their core efforts on private banking, exclusively courting high net-worth individuals and focusing on asset management. They do not solicit funds from the public, and do not make loans and investments. Private banking is the most important revenue source for Swiss banks, managing CHF 3.1 billion in assets and generating gross revenue of 26.5 billion in 2013. Since 2007, Swiss banks have seen a marked downturn in revenue due to a decline in client assets and increased competition from service providers in clients’ countries of origin, since previous untaxed offshore assets are now

177 PERFORMANCE OF SWISS PRIVATE BANKS, supra note 170 at 19.
179 PERFORMANCE OF SWISS PRIVATE BANKS, supra note 172, at 31.
181 Swiss banks believe that tax transparency places a huge burden on the Swiss financial industry. See ERNST & YOUNG, supra note 81, at 11. With FATCA and other automatic exchange of information systems on the rise, the euphoria of 2010 when the financial industry proposed anonymous withholding tax has “evaporated.” Id. For a comparison of anonymous withholding versus automatic exchange of information, see supra Part IV.A. For a discussion on automatic exchange of information as a new global trend, see infra Part V.
182 See KPMG SWITZ. & UNIV. OF ST. GALLEN, supra note 49, at 6, 7.
183 2014 BANKING BAROMETER, supra note 182, at 6.
185 SWISS BANKERS ASSOCIATION & BOSTON CONSULTING GROUP, supra note 149, at 19.
regulated.\textsuperscript{186} Singapore and Hong Kong are likely to benefit from the increasing transparency in Switzerland, and they are quickly catching up to Switzerland’s status as the top center for wealth management.\textsuperscript{187} Because of the competition,\textsuperscript{188} Swiss banks have been evaluating new business opportunities, adjusting their footprint in the global banking industry, and leveraging potential that have not been exhausted.\textsuperscript{189}

As a result of regulatory developments and increased competition, private banking in Switzerland is experiencing a change in customer base with a rise in assets from emerging markets. Foreign clients are important for Swiss banks: as of end of 2013, 51.3\% of the CHF 6.1 trillion (about $3.1 trillion) assets managed in Switzerland were from foreign clients.\textsuperscript{190} While almost half of the foreign assets under management in 2010 were from Western Europe and North America, about 55\% of foreign assets were from emerging countries in 2013.\textsuperscript{191} Thus, growth regions such as the Middle East, Latin America, and Asia are increasingly important for Swiss private banking.\textsuperscript{192} On the other hand, assets from Western Europe and the U.S. declined due to FATCA and the resulting taxation of assets; Swiss banks’ business with the most affluent customers was most impacted by this change.\textsuperscript{193} The transformation in customer base goes hand in hand with decrease in profitability, even though the reduction in affluent customers is partly compensated with inflow of new customers with lower margins.\textsuperscript{194}

In sum, the burden of FATCA has not only affected the economics of the Swiss banking industry, but it is also altering the look and character of Swiss private banking.

IV. FATCA’S IMPACT ON SWITZERLAND IN CONTEXT OF RECENT INTERNATIONAL TRENDS

As a final point, this section will highlight how FATCA’s impact on

\textsuperscript{186} See PWC PRIVATE BANKING STUDY, supra note 178, at 6. Additionally, price competition has intensified in the Swiss private banking industry, which further pressurizes margins. \textit{Id.} As a result, the banks’ average income per employee reduced by 40\%, from CHF 656,000 in 2007 to CHF 395,000 in 2011, \textit{Id.}

\textsuperscript{187} DELOITTE WEALTH MANAGEMENT CENTER RANKING 2013, supra note 22, at 24; see also 2014 BANKING BAROMETER, supra note 182, at 21.

\textsuperscript{188} Survey shows that Swiss banks believe that private banking is a business area where the competition is especially fierce. ERNST & YOUNG, supra note 81, at 21.


\textsuperscript{190} SWISS BANKERS ASSOCIATION & BOSTON CONSULTING GROUP, supra note 149, at 20.

\textsuperscript{191} \textit{Id.}

\textsuperscript{192} \textit{Id.}

\textsuperscript{193} \textit{Id.} Further decline in assets from developed countries is expected for future years. \textit{Id.} at 22.

\textsuperscript{194} \textit{Id.} at 22–23.
Switzerland is further bolstered by recent international trends moving toward greater cross-border financial transparency. Automatic exchange of information has become the standard around the world, and various international regimes based on IGA Model I are being set up to this effect. So while FATCA is not an end-all legislation for combating tax avoidance,195 it certainly drives the current global movement for automatic exchange of information, and complements a number of international initiatives that crack down on tax evasion.

First, automatic exchange of information has become the global norm.196 During the 2013 G20 Summit in St. Petersburg, world leaders endorsed automatic exchange of information as the new global tax standard.197 The G20 Leaders’ Declaration announced a plan to begin to exchange information automatically on tax matters among G20 members by the end of 2015.198 Consequently, the OECD in July 2014 announced the Standard for Automatic Exchange of Financial Information in Tax Matters (the Standard), a single global standard for an automatic exchange of information between authorities worldwide.199 The Standard contains a Model Competent Authority Agreement (Model CAA) and the Common Reporting Due Diligence Standard (CRS), which are similar to and were built off IGA Model I.200

Following the release of the Standard, the European Commission in October 2014 agreed on a draft directive to implement the new Standard in the EU beginning 2017.201 Also in October 2014, 51 jurisdictions signed the

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195 One of the biggest issues that commentators have with FATCA is that it is largely unilateral in U.S. banks’ favor and only adversely affects non-U.S. financial institutions. See also supra note 85.
196 Indeed, a recent survey even revealed that Swiss banks have also accepted the automatic exchange of information as the new global standard. ERNST & YOUNG, supra note 81, at 19 (finding that about half of the banks surveyed believe that automatic exchange of information will become the new international standard by 2020).
198 See TAX ANNEX, supra note 199, at 3.
first Multilateral Competent Authority Agreement on Automatic Exchange of Financial Information to automatically exchange information under the Standard, with Switzerland joining in a month later. The competent authority agreement lays out details of what information will be exchanged at what time. Further, the Global Forum on Transparency and Exchange of Information for Tax Purposes, which includes more than 120 countries and jurisdictions, has received commitments from over 80 of its members to implement the new Standard within specific timeframes.

Finally, implementation of FATCA aligns with the current international mood against tax avoidance. OECD’s Action Plan on Base Erosion and Profit Shifting (BEPS), endorsed by G20 leaders in July 2013, has been hailed as the ultimate constructive move to reform international taxation policies for multinational enterprises. The BEPS report recommends 15 specific actions to prevent international tax avoidance by multinational companies with aggressive tax positions and lays out a timeline for swift implementation of its policies. Further, Switzerland’s neighbors are also coming down on tax avoidance. For example, U.K.’s General Anti-Abuse Rule (GAAR) came into effect in July 2013 to better define abusive tax arrangements. Luxembourg, another country notoriously known as a safe haven for secret accounts, revealed that it will begin an automatic exchange of tax data with almost all of EU

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203 See Multilateral Competent Authority Agreement, supra note 204.


205 See Tax Annex, supra note 199, at 3.


member nations beginning on January 1, 2015. To conclude, various international agreements and plans in the pipeline indicate a general movement toward greater taxing transparency, particularly in regards to automatic exchange of information. This will further cement the lasting impact that FATCA has on the Swiss banking industry.

CONCLUSION

With FATCA enforcement beginning in 2014 against a backdrop of greater international scrutiny for transparency, one can expect to see great changes in the Swiss banking industry. Switzerland’s participation in U.S. and international regimes for greater exchange of information has lead way to an unprecedented amount of disclosure, assistance, and cooperation by Swiss banks. Throughout this process, there has been a full-fledged debate in Switzerland: is moving toward transparency a betrayal of Swiss values as a disinterested Alpine nation, or is Switzerland ready for a fundamental shift in its belief in privacy? The answer to this debate seems to lean on the latter, but moving forward, the debate will certainly shape Switzerland’s historical and cultural identification with neutrality, privacy, and independence. Swiss banks are hopefully optimistic through the tough conditions — in the short term, Switzerland is still expected to remain as the largest single offshore center, with about 25% of total offshore wealth by the end of 2017. Yet, in this new era of tax and banking transparency, how Switzerland’s reputation will change in the long term remains to be seen.


209 See Emma Thomasson, Special Report: the Battle for the Swiss Soul, REUTERS, Apr. 18, 2013, http://www.reuters.com/article/2013/04/18/us-swiss-banks-specialreport-idUSBRE93H07620130418. While Conservative politician Christoph Darbellay publicly called Wegelin executives “traitors” that dragged Swiss finance through the dirt, Josef Ackermann, the chairman of Zurich Insurance, called on Switzerland to resist international attacks. Id.

210 See Ernst & Young, supra note 81, at 11.

211 See ERNST & YOUNG, supra note 81, at 11.

212 BOSTON CONSULTING GROUP, supra note 5, at 12.