

1973

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Recommended Citation

Walter Meier, *Banking Secrecy in Swiss and International Taxation*, 7 INT'L L. 16 (1973)
<https://scholar.smu.edu/til/vol7/iss1/3>

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Banking Secrecy in Swiss and International Taxation

I. Introduction

Protection of privacy in money affairs, tracing as far back as to ancient Rome, proves to be not only a long living, but also a much debated, axiom of law. At present more than twenty per cent of all nations provide secrecy in banking matters at degrees that keep accounts basically secret from foreign—and in some cases even from domestic—investigations. Disputes on the legitimacy of banking secrecy and on conflicts of interest arising therefrom are inevitable.

The increasing worldwide interpenetration of men and capital and other developments that pay less and less attention to national boundaries, apparently aggravate the issue. Some connect tax evasion and capital flight directly to the existence of banking secrecy, or blame it even as their very root. Others take a more balanced view and regard shortcomings in the international tax morality and capital movements as having much broader aspects. Most critical publicity focuses traditionally on Switzerland. The questions involved are domestically, as well as in their global context, more complex than many critics may be aware. And there are valid points on both sides.

The objective of this study is to review the tax problems connected with Swiss banking secrecy. To understand the issue, it is indispensably necessary to know what banking secrecy means in terms of the Swiss legal and fiscal system. The close affinity between tax information and banking secrecy makes it also necessary to scrutinize the exchange of information rules in international tax treaties and to throw a glance at treaties on mutual assistance in criminal matters. Since protection of privacy in banking matters has come under particularly vigorous attack from the United

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The opinions voiced in this article are those of the author and do not necessarily reflect the views of the Swiss tax authorities.

States, emphasis will be laid on the Swiss–United States tax relationships. However, the underlying problems and the assessment of the situation refer – *mutatis mutandis* – to other countries as well.

II. Banking Secrecy in Switzerland

A. Survey

Swiss law assigns a high priority to the sanctity of the individual and his personal rights. The sphere of privacy (*Geheimsphäre*) is recognized as an integral part of the personal rights of each individual. It includes his intellectual existence (*geistiges Sein*), health, family life and financial affairs.¹ Privacy is an enforceable right by virtue of Article 28 of the *Civil Code* and Articles 41 and 49 of the *Code of Obligations*.

A person wrongfully injured in his personal privacy may sue for injunction and, in certain cases, for damages. In the field of banking, the banker's obligation to observe the client's privacy, by keeping secret his financial status and money transactions, is in addition being regarded as an essential *contractual element* (duty of loyalty) under the law of agency² the violation of which may make the agent liable.³ *These time-honored principles of private law are the fundamentals of Swiss banking secrecy.*

The broad scope of personal rights—normally extended also to aliens residing in Switzerland—merits particular legal protection in a country whose geographical position, tradition of neutrality and political stability made it for centuries a refugium for politically, religiously and racially persecuted people. It is not so long ago when Nazi agents on their ruthless drive to seize private assets of German Jews, attempted by all means to gain access to the identity of Jewish depositors in Swiss banks and thereby grossly violated the public order and sovereignty of Switzerland. The Swiss government deemed it necessary to curb such illegal activities of foreign powers, by supplementing the civil law liability for violating banking secrecy with the criminal offense under provisions of the public law. The intelligence game of foreign agents spying for banking information thus became a little more risky.⁴

¹See Egger, *Kommentar zum Schweizerischen Zivilgesetzbuch*, 2d ed., Zurich, 1930, art. 26. The sphere of privacy is also extended to the 'economic personality'. For an outline in English see Meyer, *The Banking Secret and Economic Espionage*, 23 GEO. WASH. L. REV. 287 (1955).

²Art. 394 *et seq.* of the Code of Obligations.

³*Id.* art. 97.

⁴That the penal protection of privacy in banking affairs has not become obsolete, is shown in a recent case in which a diplomat of the British Embassy in Switzerland and a senior officer of the British Treasury, successfully bribed two employees of a Geneva bank to disclose names and other data as to allegedly British depositors. See *Neue Zürcher Zeitung* (*Fernaussage*), March 12, 1972, at 20.

B. Swiss Banking Law

Current legislation on monetary and banking is based on the Constitution of the Swiss Confederation.⁵ The *Federal Law relating to Banks and Savings Banks of November 8, 1934*, as amended (hereinafter cited as "Banking Law"),⁶ is one of the most important legislative acts in this area. It is the expression of a liberal economic policy, contains traditional principles of banking operations and binds all banks, private bankers, savings banks and financial institutions who publicly solicit deposits. Supervision of banks is exercised by the Federal Banking Commission whose members are appointed by the Swiss Federal Council.⁷

The main objective of the Banking Law is the *protection of the depositor and other bank creditors*. An essential part of the safeguards is found in Article 47 in that it makes violations of the confidential relations between the banker and his clientele punishable.

C. Scope of Article 47 of the Banking Law

Article 47 was amended in 1970⁸ and deals now exclusively with the violation of banking secrecy. The provision reads as follows:⁹

1. Whosoever discloses a secrecy that has been entrusted to him or of which he has received knowledge in his capacity as official, employee, agent, liquidator or commissioner of a bank, as observer of the banking commission, as official or employee of a recognized auditing firm, or whosoever attempts to induce somebody else to commit such a violation of the professional secrecy, shall be punished with imprisonment up to 6 months or with a fine up to 50,000 francs.

2. If the act has been committed by negligence, the penalty shall be a fine up to 30,000 francs.

3. The violation of professional secrecy remains punishable beyond the termination of the official or professional relationship, or the exercise of the profession.

4. Excepted are Federal and cantonal provisions concerning the duty to testify and the duty to present information to an official.

Violation of banking secrecy is an *ex officio* offense (*Offizialdelikt*), which means that the injured party does not have to file a request for prosecution, thus emphasizing the public interest in the punishment of such offenders or, in other words, the assurance of the government in protecting

⁵Art. 31 quater, 38 and 39.

⁶*Amtliche Sammlung der Bundesgesetze und Verordnungen* (Official Collection of Federal Laws and Regulations (hereinafter cited as "AS")) 1971, at 808. For an unofficial English translation of the Banking Law (as in force in 1968) see "Swiss Federal Banking Law," published by the Union Bank of Switzerland, Zurich, 1968.

⁷The Federal Council (*Bundesrat*) is the highest executive authority in Switzerland.

⁸AS 1971, at 808.

⁹Translated by the author.

the individual's privacy. The negligent disclosing of banking information is, in line with that policy, also punishable. A further significant feature is subjection to the punishment of even an unsuccessful attempt to induce somebody else to disclose secret data—a device designed to protect bank officials from third person's attempts and pressures to supply information.¹⁰

The 1970 amendment extends the personal scope of Article 47 to some additional persons, whereby members and officials of the Banking Commission are now subjected to the more severe penalties of the *Penal Code*.¹¹ The new paragraph 3 now makes it clear that violation of banking secrecy remains punishable beyond the date on which the offender terminates his official position or resigns from the exercise of his professional activity. Article 47 was finally supplemented by a clause determining that banking secrecy is subject to Federal or cantonal provisions relating to the duty to testify by a witness, and the duty to supply information to an official.

That clarification may be regarded as a legislative effort to do away with the widespread legend that banking secrecy enjoys an absolute legal protection. Swiss legal doctrine¹² and practice¹³ have always maintained the view that in certain cases other legal provisions take precedence over banking secrecy. Violations of Article 47 are investigated by the cantonal criminal prosecution authorities, and punished by the ordinary cantonal courts.¹⁴

In this context it is necessary to recall also Article 273 of the *Penal Code* on economic espionage (*Wirtschaftlicher Nachrichtendienst*) making punishable a person who discloses information considered a business secret to a foreign source.¹⁵ The Federal Court has repeatedly confirmed that this provision includes the offence of directing information to foreign fiscal or currency authorities.¹⁶ Finally, Article 162 of the *Penal Code* is to be

¹⁰The successful attempt is punishable in connection with art. 24(1) of the Penal Code.

¹¹Art. 320.

¹²See, among many authors, Maurice Aubert, *Berufsgeheimnis des Bankiers*, *Separatdruck aus Schweizerische Juristische Kartothek*, 1970, with an index of other literature on the topic.

¹³*Entscheidungen des Schweizerischen Bundesgerichtes* (Decisions of the Swiss Federal Court (hereinafter cited as "BGE")) 95 (1969) I 444.

¹⁴Most other offenses against the Banking Law are dealt with administratively by the Federal Department of Finance and Customs. See art. 51 bis.

¹⁵Art. 273 reads as follows:

A person who, through searching, secures a manufacturing or business secret, in order to make it accessible to a foreign official agency, or to a foreign organization, or to a private business enterprise, or to their agents, a person who makes accessible a manufacturing or business secret to a foreign official agency, or to a foreign organization, or to a private business enterprise, or to their agents, shall be punished by imprisonment, in serious cases in the penitentiary. In addition a fine may be imposed. (Translation according to Meyer, *supra* n. 1, at 302).

¹⁶BGE 74 (1948) IV 102.

mentioned, dealing with—only upon complaint (*Antragsdelikt*)—the offence of revealing a business secret which had to be guarded under a legal or contractual obligation.¹⁷

To sum up, Article 47 of the Banking Law does not determine the substantive scope of banking secrecy. The obligation to observe secrecy existed in Swiss law long before the enactment of that widely cited provision.¹⁸ Nor does Article 47 indicate when secrecy will be superseded by overriding rules. The answer on this essential question can only be derived from various Federal and cantonal laws.¹⁹ The following section reviews briefly some significant areas in which banking secrecy might be overruled by other legal provisions. The position of banking secrecy in the Swiss tax system will, however, be analyzed more thoroughly in the following chapter.

D. Limitations on Banking Secrecy

Contrary to a widespread belief numerous cases exist where *Federal and cantonal laws take precedence* over the Federal rule on banking secrecy. Such limitations are based on various procedural provisions on both legislative levels as well as on Federal substantive laws.

To testify in trial proceedings is a public duty and can for this reason not be avoided by referring to a contractual agreement to secrecy. Only provisions of the public law can provide exceptions therefrom. The *Federal*

¹⁷Art. 162 (*Verletzung des Fabrikations—oder Geschaeftsgeheimnisses*) reads as follows:

A person who reveals a manufacturing or business secret with regard to which he was under a duty to observe secrecy because of a duty imposed by law or assumed by contract, a person who takes advantage of such a disclosure, shall be punished by imprisonment or fine in case complaint has been made by the injured party. (Translation according to Meyer, *supra* n. 1, at 303 n.68).

¹⁸It is therefore inaccurate to speak of so-called Swiss "secrecy laws," a term frequently used in Anglo-American countries to designate mysterious (and actually non-existing) laws on banking secrecy. The confidentiality between the banker and his client is based—as various other confidential relationships—on provisions of private law as discussed above. With art. 47 a rule of public law merely reinforced the already existing protection.

¹⁹How much easier is it to interpret an 'untraditional' law on banking secrecy as introduced in various countries in the last decade! Thus the Lebanese Banking Secrecy Law of September 3, 1956, leaves no doubt on its quasi-absolute scope:

Managers and employees of the banking establishments referred to in the first article as well as persons who are acquainted through their quality or their function, by one means or another, with bank books, operations and banking correspondence, are bound to absolute secrecy, in favour of the bank's clients, and cannot disclose to anyone whatsoever, private individual or an administrative, military or judicial authority, clients' names, their assets and facts of which they are aware, except with the client's written authorization of his heirs' or his legatees,' or in case he should be declared bankrupt, or in the event of a dispute between the client and the bank resulting from banking relations.

*Code of Criminal Procedure*²⁰ does not extend to the banker the right to refuse to testify or produce documents in criminal investigations or proceedings as it does with regard to clergymen, attorneys, notaries, physicians, pharmacists, midwives and their professional assistants.²¹ The banker therefore cannot refuse to comply with such procedural provisions in cases where facts covered by banking secrecy come into play.

Similarly the *Federal Code of Civil Procedure*²² authorizes only persons enumerated in Article 321 of the *Penal Code* to refuse to testify, and these only to the extent that facts to be disclosed are professional secrets within the meaning of that provision.²³ The banker does not belong to those privileged persons. However, the judge may waive the obligation to disclose a professional secret if the interests of an involved person for not disclosing it outweigh other interests.

At variance from the two Federal judicial procedural codes the *Federal Law on Administrative Procedure*,²⁴ as applied in administrative procedures, grants to the holder of a professional or business secret the right to deny testimony to the extent that an obligation to testify is not expressly imposed on him by another Federal Law.²⁵ Such a duty may for instance, for bankers, be established in some fiscal proceedings which are conducted under the rules of the Federal Code of Criminal Procedure. But in most administrative procedures the banker will be exempted from testifying by virtue of his capacity as holder of a professional secret.

Of more practical importance are the *cantonal procedural laws* under which the overwhelming majority of criminal and civil trials are held.²⁶ The hierarchy of the different levels of law provides the maxim of the overriding force of Federal law over inconsistent cantonal law.²⁷ However, the Federal Constitution reserves to the cantons the right to legislate on court procedures.²⁸ Legal doctrine and practice in Switzerland generally recognize that Article 47 of the Banking Law was *not* intended to impose any restrictions, on the power of the cantons to promulgate their civil and

²⁰*Bundesgesetz ueber die Bundesstrafrechtspflege vom 15. Juni, 1934* (BS 3, at 303). — THE FEDERAL CODES OF CRIMINAL AND CIVIL PROCEDURE determine the procedures before the Federal Court (which is comparable to the United States Supreme Court). This Court exercises mainly appellate jurisdiction over decisions of cantonal tribunals.

²¹Art. 77.

²²*Bundesgesetz ueber den Bundeszivilprozess vom 4. Dezember, 1947* (AS 1948, at 485).

²³Art. 42.

²⁴*Bundesgesetz ueber das Verwaltungsverfahren* (AS 1969, at 737).

²⁵Art. 16.

²⁶There exist twenty-five cantonal jurisdictions. Each canton has its own criminal and civil procedural laws.

²⁷Art. 2 of the Interim Regulations of the Federal Constitution.

²⁸Arts. 64 and 64 bis.

criminal procedural codes. To this extent, cantonal procedural laws take precedence over banking secrecy.²⁹

Like the Federal Code, the majority of the cantonal codes of criminal procedure do not exempt the banker from the obligation to testify, or to comply with other procedural measures such as opening books to inspection. Only two cantons have provided that the holder of a professional secret may refuse testimony in criminal matters.³⁰ The cantonal codes of civil procedure are less uniform with respect to the obligation of testimony. Most cantons, however, include in the group of persons entitled to refuse testifying on the ground of professional secrecy, only clergymen, lawyers and physicians. Bankers would principally be obliged to testify in those cantons.

Some of the procedural codes contain special provisions concerning business secrets, with the effect of leaving it to the discretion of the court to exempt someone from giving evidence.³¹ Other cantons fix a general right to refuse to testify with respect to professional secrets without listing the privileged persons. Bankers probably do not have to testify in those jurisdictions. In addition to the outlined procedural limitations, there are various instances in the *substantive law* in which banking secrecy is superseded by other norms.³²

With regard to inheritance laws the principle of direct succession (*Universalsukzession*) prevails, which means that all rights of the deceased person pass to the heirs. A bank must therefore disclose information with respect to the estate to the heirs, the agent representing the estate, the executor and the official administrator winding up the estate.³³ Essential limitations on banking secrecy are further imposed in proceedings for the enforcement of debts. A debtor cannot hide his assets in bank accounts under the veil of secrecy.³⁴

One area, however, remains controversial. Swiss law allows, under certain conditions, the securing of a debt by means of an attachment (*arrest*) even in cases where the creditor cannot specify the debtor's assets. There are strong arguments against a duty to disclose banking secrecy in such cases, since that device—easily available—could be abused for the purpose of merely obtaining knowledge of another person's assets, and thus to circumvent banking secrecy.

²⁹BGE 95 (1969) I 439.

³⁰Cantons of Vaud and Neuchâtel.

³¹For instance, Zuerich Code of Civil Procedure, para. 188.

³²For a survey see Aubert, *supra* note 12; Meyer, *supra* note 1, at 293; Mueller, *The Swiss Banking Secret*, 18 INT'L & COMP. L.Q. 360 (1969).

³³BGE 89 (1963) II 93.

³⁴BGE 86 (1960) III 114.

E. Numbered Accounts

Widespread misconceptions prevail with reference to so-called "secret accounts" or "numbered accounts" in Swiss banks.³⁵ It must be reemphasized that there is no legal difference between ordinary and numbered bank accounts. The numbered account, labelled by a code number instead of by the name of the holder, is simply an internal device of the banker to provide a more efficient protection of confidentiality with regard to infringements by subordinated employees. The identity of such accounts remains restricted to a few senior bank officials.³⁶ Both types of accounts enjoy the same legal secrecy protection (there exists no legal "superdiscretion"), and both of them are subject to the very same limitations of law. Tax and criminal prosecution authorities deal with numbered and ordinary accounts in exactly the same way.

III. Swiss Tax System and Banking Secrecy

A. Tax Assessment and Availability of Information

The multitude of Federal and cantonal tax laws have one common feature: the Swiss tax authorities must primarily rely on the assessment data provided by the taxpayer himself. This approach is based on the sound assumption that the taxpayer knows his financial status best. By filing the tax return he sets in motion the process of determining his tax liability. If the assessment seems to be insufficient or understated, the revenue service may request him to appear for a personal interrogation or to submit evidence such as banking documents, contracts, salary certificates.

A legal obligation of third parties to supply information in assessment proceedings does generally not exist except in a few cases where it is regarded as an absolute necessity and only to the extent that the tax law provides it explicitly.³⁷ The assessment of taxes constitutes an administrative procedure, for which no general obligation of a citizen to give testimony exists, nor need he make a statement or produce a document or article of evidence as it prevails under judicial procedural rules.

³⁵The establishment of numbered accounts is by no means a privilege of Swiss banks. The Government of Singapore, for instance, also introduced the system of numbered accounts when revising its banking regulations in 1970. *See The Straits Times*, August 1, 1970.

³⁶According to one estimate, numbered accounts make up only about 3 to 4 per cent of all accounts and the amounts involved are less than 10 percent of total deposits. *U.S. NEWS AND WORLD REPORT*, Feb. 21, 1972, at 61.

³⁷For instance, with respect to partnerships to determine the income of each partner, or employers to issue salary certificates, or a debtor to certify the amount of indebtedness. For Federal income tax see Federal Defense Tax Act (*Wehrsteuerbeschluss*), art. 90.

As a corollary the tax authorities have a wide range of discretionary powers. They evaluate submitted information and evidence freely. Even where tax laws require the cooperation of third parties, it is usually up to the taxpayer to collect the information. The Swiss legislators thus emphasize the system of self-assessment, by being very reluctant to concede to the tax authorities, the competence to apply directly to the source of information.

Under that concept it is obvious that the tax authorities have *no basis to obtain assessment data directly from banks*. If a client authorizes his bank to provide the revenue service with the demanded information, then a bank may not refuse to supply it, since secrecy is a right only of the client and not of the bank.³⁸ The principle of non-availability of tax information from third parties, extends also to proceedings in which the bank itself is taxpayer. Knowledge of a person's financial status obtained when auditing the books of a bank may not be used for the assessment of that person. The Federal Anticipatory Tax Law provides explicitly that banking secrecy has to be observed in such cases.³⁹

These assessment rules apply basically also on proceedings of tax appeals. This is of particular significance when a judicial authority is dealing with an appeal. The court then relies generally on the administrative rules as set forth in the tax law—at variance from non-tax trials at which the citizen's general duty to give testimony prevails.⁴⁰ However, any tax system requires some efficient weapons to make unwilling taxpayers comply.

The Swiss tax authorities can put pressure on a taxpayer suspected of underreporting his revenues by means of an *official estimate* of his tax liability (*Ermessenstaxation*). It means a careful ex officio determination of income and property under due consideration of all circumstances. The official estimate device may in certain causes be combined with the withdrawal of the right to appeal and with a penalty for tax evasion.⁴¹

Experience shows that the Swiss system of self-assessment with its effective means of determining the tax liability of non-complying persons works satisfactorily. Of course, like any system, it cannot completely

³⁸BGE 74 (1948) I 492.

³⁹Art. 40(5). For a case on the cantonal level see BGE 64 (1938) I 187.

⁴⁰See Ernst Blumenstein, *System des Steuerrechts*, 3d ed., Zurich, 1971, at 419 *et seq.* However, the judicial procedure provisions are applicable in criminal tax fraud trials.

⁴¹There exist some additional safeguards to prevent abuses of this liberal assessment system. A considerable degree of control may be exercised by using data obtained from tax returns of other taxpayers (except banks), and a cooperation to that end between the various tax authorities on all levels. Further, capital income, such as dividends and interest (derived from Swiss sources), are burdened with a relatively high withholding tax of thirty percent (equalling roughly the highest tax brackets), refundable only upon reporting the income item.

eliminate tax evasion. But it leaves the citizens' privacy in financial matters to a fair extent untouched, and makes it unnecessary to burden third parties with informative obligations which would widely be regarded as not appropriate.

B. Tax Offenses and Banking Secrecy

Swiss tax authorities have no direct access to bank information in the assessment procedure. The crucial answer whether banking secrecy must be lifted in investigations for tax offenses is a very complex issue and cannot be immediately derived from the tax laws.

Federal and cantonal tax laws are not uniform with respect to the terminology of tax offenses. They use various terms for violations of tax provisions. The patterns of proceedings to investigate and punish tax offenses also vary greatly. But most tax laws draw a distinction roughly between mere evasion of taxes by non-reporting of income or property, and more severe cases in which the means to evade taxes have distinctive fraudulent characteristics, be it through deceiving the tax authorities by deliberately using incorrect, falsified or untrue balance sheets, financial statements, inventories and other documents of evidentiary value, or be it through concealing documents containing tax-relevant evidence or by using other fraudulent means.⁴²

The line between the two groups varies from canton to canton and there is also no uniformity in the Federal tax laws.⁴³ For purposes of this study the offense of mere non-reporting will be referred to as *tax evasion* (*Steuerhinterziehung*) and the qualified form with fraudulent traits as *tax fraud* (*Steuerbetrug*).

The offense of tax evasion is regularly subjected to fines only, often determined as a multiple of the tax deficiency. Persons convicted of tax fraud are under most tax laws punishable either by fines or by imprisonment, or both. The rationale for this differentiated penal treatment for the two kinds of tax offenses must evidently be sought in an attitude considering tax fraud—that has close similarities to the severely punishable common crime of fraud—as having a much higher degree of moral turpitude and social harm than mere tax evasion.⁴⁴

⁴²*Compare* Decision of the Federal Court of March 16, 1951, published in *Archiv fuer Schweizerisches Abgaberecht*, vol. 20, at 91.

⁴³The Federal Defense Tax Act uses only the term "tax evasion," which also includes the forms of fraudulent violations (Art. 129). The Federal Anticipatory Tax Law clearly differentiates between the terms "tax evasion" and "tax fraud" (Art. 61).

⁴⁴Notwithstanding an inner relationship between common fraud and tax fraud the latter is not punishable under the Penal Code because of the autonomous position of the tax laws within the Swiss legal system (*compare* arts. 333 and 335(2) of the Penal Code).

The distinction between tax evasion and tax fraud may become the *decisive factor for the availability of bank information*. Tax evasion, not considered as a crime in terms of the *Penal Code*, is dealt with in an administrative procedure by the tax authorities. In line with the assessment rules, bankers as well as other third persons may then not be required to furnish information.

Tax fraud, on the other hand, may be prosecuted by two different procedures, depending on the pattern of the applicable tax law. Under one group it remains an administrative procedure identical to that applicable on tax evasion. Third-party (including bank) information is then not obtainable. This group includes the Federal income tax (Defense Tax), assessed and collected by the cantons under supervision of the Confederation⁴⁵ and, among others, the income and net wealth tax in the Canton of Berne (therefore often referred to as "Berne group"). A second group of tax laws goes a wholly different way and transfers the investigation of tax fraud cases to the ordinary prosecution authorities and the punishment to the criminal courts (this group is sometimes referred to as "Zurich group").⁴⁶

This pattern of prosecuting tax fraud is much more severe in that the proceedings are no more conducted under the provisions of the tax law but under the rules of the criminal procedure code. As already pointed out, most procedural codes do not exempt the banker from the duty of furnishing information, to give testimony or to produce documents. Hence *banking secrecy may in such cases be superseded by procedural duty*. The tougher approach fits into the widely held view that puts tax fraud at an equal adverse standing as other criminal delicts, warranting the application of the same rigid procedural rules.⁴⁷

IV. International Treaties and Banking Secrecy

A. Tax Treaties

1. OECD DRAFT CONVENTION

The application of a tax treaty implies an appropriate cooperation between the tax administration of the contracting countries. Facts on which the domestic tax laws and treaty rules are to be applied must in many cases be ascertained bilaterally. The OECD Draft Convention of 1963 includes

⁴⁵Federal Defense Tax Act, art. 129.

⁴⁶That group includes, among others, the cantons with the major banking centers: Zurich, Basel-City and Geneva.

⁴⁷See P. Lavanchy, *Das Bankgeheimnis in der Schweizerischen Gesetzgebung mit besonderer Beruecksichtigung des Steuerrechts*, Thesis, Zurich 1935, at 23. Compare also BGE 96 (1970) I 737.

in Article 26 a provision pertaining to the exchange of information.⁴⁸ Information necessary for the carrying out of the treaty, and of the domestic laws (to the extent that the taxes concerned are covered by the treaty) is exchangeable. Apart from the furnishing of routine information, assistance will be requested in cases where the information obtained from the regularly available sources, is not sufficient or is in need of confirmation.

However, the OECD formula is subject to some essential limitations.⁴⁹ One stipulates that the requested country is not bound to carry out administrative measures going beyond its own domestic laws. Obviously, tax secrecy may not constitute an obstacle for the exchange of information. Supplied information must be treated as secret and not be disclosed. The information clause may, on the other hand, not be construed to oblige supplying particulars which are not available under the laws, or in the normal course of the administration of the requested country. Thus, data already in the files of the tax authorities, or available in the normal procedure of assessment, are obtainable.

There exists no obligation to undertake investigations of the taxpayer's or other persons' books. A last restriction pertains to the disclosure of certain secret data. Information which would disclose any trade, business, industrial, commercial or professional or trade process secrecy as well as those which would be contrary to public policy are excluded. The OECD commentary mentions further dispensations—for example "information protected by provisions on banker's discretion."⁵⁰ This approach does not substantially vary from the Swiss policy in this field.

B. SWISS TAX TREATIES

Switzerland has traditionally observed a prudent reluctance in the area of international exchange of fiscal information. This attitude reflects basically the information pattern prevailing in the domestic tax system with its primary reliance on the taxpayer as source for assessment data. It might further have to be linked with attempts of some governments to abuse fiscal information for non-tax purposes, such as supervision of international capital movements or currency control.⁵¹ However, Switzerland has not

⁴⁸See commentary on art. 26, OECD document C(63)87.

⁴⁹Para. 2 of art. 26.

⁵⁰Commentary on art. 26, No. 13. This interpretation is confirmed by criticism of some members of the Ad Hoc Group of Experts on Tax Treaties between Developed and Developing Countries expressed on art. 26 at its 1970 Geneva meeting. They suggested extension of the scope of the information clause in order to eliminate "avenues of tax avoidance due to the secrecy of bank-accounts." See U.N. publication E/4936, ST/ECA/137, at 19.

⁵¹See Locher, *Handbuch und Praxis der schweizerisch-amerikanischen Doppelbesteuerungsabkommen, Einkommens- und Erbschafts-steuern* (Handbook and Practice of the Swiss-American Conventions for the Avoidance of Double Taxation, Income and Estates and Inheritance Taxes) (hereinafter cited as "Locher"), vol. I, No. 185.

been sitting back, but curtailed unilaterally tax-free evasion schemes through the use of Swiss banking accounts.⁵²

Among the tax treaties concluded by Switzerland, only four of them include an information provision.⁵³ The clause in the treaties with the United Kingdom, France and Germany are nearly identical, with the exception that the treaty with the United Kingdom does not explicitly list the banking secrecy as nonexchangeable information.⁵⁴ But the omission does not have any practical significance since business and professional secrecy also covers banking data. The information provision in the Swiss-United States Treaty provides in addition for the exchange of information "for the prevention of fraud." The scope of this formula and its particular impact on banking secrecy calls for a particular analysis.⁵⁵

But it is important to point out within this context, that even without an exchange of information clause Switzerland provides all treaty partners routinely or, in particular cases, upon request, with any information that is necessary for the correct treaty application and for the prevention of abuses of treaty benefits.⁵⁶ It considers the provisions on the mutual agreement procedure and on the reduction of taxes withheld at the source or similar clauses as an appropriate basis for the exchange of information.⁵⁷

⁵²The withholding tax of thirty percent on capital income (dividends, interest, etc.) from Swiss sources is a final tax burden to non-residents, unless relief is granted in a tax treaty with the payee's country, and only to the extent that such income is reported to the revenue service of the residence country. With respect to income for non-Swiss sources it is clear that benefits from tax treaties between Switzerland and third countries may not be claimed by persons, who are not residing in Switzerland and not reporting the respective income item.

⁵³United States of America (1951), art. XVI; United Kingdom (1954/1966), art. XX; France (1966), art. 28; Germany (1971), art. 27.

⁵⁴Art. 28 of the Swiss-French Tax Treaty reads as follows:

1. The competent authorities of the Contracting States may exchange on application such information (being information which is available under their respective taxation laws in the normal course of administration) as is necessary for the carrying out of this Convention. Any information so exchanged shall be treated as secret and shall not be disclosed to any person other than those concerned with the assessment or collection of the taxes which are the subject of this Convention. No information shall be exchanged which would disclose any trade, banking, industrial or professional secret or any trade process.

2. In no case shall the provisions of this Article be construed so as to impose on one of the Contracting States the obligation to carry out administrative measures at variance with its regulations and practice or which would be contrary to the sovereignty, security, public policy or general interest of its own State or to supply particulars which are not procurable under the legislation of its own State or the State making such application.

⁵⁵See *infra*, ch. 5.

⁵⁶A case decided under the 1948 Swiss-Swedish Tax Treaty (with no provision on exchange of information), evidences that Switzerland gives a fairly wide interpretation to the (*in casu*) unwritten obligation to prevent abuses of treaty benefits by means of furnishing information upon request to the treaty partner. See 72 *Schweizerisches Zentralblatt fuer Staats- und Gemeindeverwaltung*, 178 (1971).

⁵⁷Switzerland entered out of these considerations a reservation on art. 26 of the OECD Draft Convention. See commentary on art. 26, No. 14.

The inclusion of an explicit clause in the treaties with the three mentioned countries may, therefore, be regarded as little more than a declaratory and psychological concession taking into consideration bargaining aspects and peculiarities in the tax relationships with those treaty partners. However, information protected by banking secrecy is—in line with the OECD Draft Convention provisions—in either case for the reasons already explained not obtainable.

B. Treaties on Mutual Assistance

Switzerland concluded treaties on mutual assistance in civil and criminal matters⁵⁸ with a number of countries. It also ratified the *European Convention on Mutual Assistance in Criminal Matters* of April 20, 1959.⁵⁹ None of those treaties rule on particulars with respect to procedural matters. A Federal law on mutual assistance does not exist,⁶⁰ and the *Federal Law of Extradition* of 1892⁶¹ is silent on the matter. The providing of judicial assistance remains therefore within the realm of the cantonal legislation. Hence, cantonal procedural provisions determine the availability and the extent of assistance and information. The same applies to the duty to disclose information shielded by banking secrecy.⁶²

All treaties on mutual assistance in criminal matters concluded so far by Switzerland, exclude investigations or proceedings concerning violations with respect to *fiscal laws*. The Federal Law on Extradition also provides for an exclusion clause.⁶³ The non-availability of mutual assistance in fiscal matters pertains also to violations of tax laws which are prosecuted like criminal acts under applicable cantonal procedural law such as tax fraud.⁶⁴ Banking information is therefore internationally not obtainable in criminal cases to the extent that they relate to tax offenses.⁶⁵

This policy is by no means confined to mutual assistance treaties to which Switzerland is a treaty party, but it reflects a still prevailing international standard. The European Convention on Mutual Assistance in Criminal Matters of 1957 similarly includes a provision, by which assist-

⁵⁸For the publication of the treaties see *Bereinigte Sammlung der Bundesgesetze und Verordnungen*, 1848–1947 (Revised Collection of Federal Laws and Regulations 1848–1947), (hereinafter cited as “BS”) 12, at 59 *et seq.*

⁵⁹AS 1967, at 831.

⁶⁰A Federal law on mutual assistance in criminal matters is in the stage of preparation and may be enacted in the future.

⁶¹BS 12, at 267.

⁶²For a case of international mutual assistance in criminal matters, between Switzerland and Austria, in which information covered by banking secrecy was disclosed, see *Blaetter fuer Zuercherische Rechtsprechung*, vol. 36, No. 108. For a summary of that decision in English see Meyer, *supra* note 1, at 327 n. 125.

⁶³Art. 11. See also BGE 74 (1948) IV 104.

⁶⁴See *supra*, ch. 3.

⁶⁵For an exception from this rule under the Swiss-U.S. tax treaty see *infra*, ch. 5.

ance may be refused in a case of a fiscal offense.⁶⁶ It remains obviously a matter of fact that most countries remain sensitive in this area and are not willing to afford other nations substantial support and cooperation in enforcing foreign tax laws and fiscal claims.

Though not falling strictly within the terms of mutual assistance, another approach available to foreign countries to get access to confidential information in non-fiscal cases is worth mentioning here for the sake of comprehensiveness of this survey. If a country is civilly injured by an illegal act which was committed against it which also constitutes a crime under Swiss law, the foreign country might be accorded the *status of an "injured party"*—not as a public body but as a quasi private person—within the meaning of the applicable cantonal procedural code. The party rights under the code are then similarly extended to the injured foreign country, however, subject to certain conditions. Banking secrecy will then be superseded by the cantonal procedural rules unless they privilege a banker.⁶⁷

The Federal Court recently confirmed the availability of the injured party status to a foreign state.⁶⁸ Two American citizens defrauded the U.S. Government on contracts to supply war material by issuing fictitious invoices for several million dollars, and by depositing the embezzled funds in a Swiss Bank. Upon application of the United States the Zurich District Prosecutor granted the United States the status of an injured party and therewith the right to inspect files including bank documents, but only after submitting a formal declaration, that the information so obtained would not be used for fiscal purposes in the United States.

Significant in this context is the argument of the Court that there is "no reason to treat a public body otherwise and worse than a private person, if, as a result of transactions under civil law the community has been directly injured by a criminal act."⁶⁹ Foreign countries may by nature have relatively few opportunities to obtain the injured party status. Nevertheless, this approach is entirely consistent with established Swiss legal rules, and the decision in no way constitutes a 'landmark case.'⁷⁰

⁶⁶Art. 2(a). Also the European Convention on Extradition is applicable on fiscal offenses only "if the Contracting Parties have so decided in respect of any such offense or category of offense" (Art. 5).

⁶⁷See *supra*, ch. 3.

⁶⁸BGE 95 (1969) I 439 and 451. A slightly divergent version of one of the decisions was published in English in 9 *INTERNATIONAL LEGAL MATERIALS* 567 (1970). However, under the misleading title "Swiss Court Decision Concerning Obligation of Banks to Furnish Information in Tax Fraud Proceedings." For comments on the decision in the U.S. see: *L.A.R., Swiss Banks and the Avoidance of American Tax and Securities Laws—An Assessment Based on Proposed Legislation*, 3 N.Y. U. JOURNAL OF INT'L L. & POL. 94 (1970); von Tuerk, *Banking Secrecy*, 12 HARV. INT'L L. J. 579 (1971).

⁶⁹9 *INTERNATIONAL LEGAL MATERIALS* 574 (1970).

⁷⁰Wall Street Journal, March 2, 1970, at 9.

V. Swiss—United States Tax Treaty and Banking Secrecy

A. Tax Treaty Information Clause

1. SCOPE OF ARTICLE XVI

The Swiss–United States Tax Treaty contains an information clause, with a scope covering not only information necessary for carrying out treaty provisions, but also for the prevention of tax fraud. It follows the standard pattern of most United States tax treaties.⁷¹ Since the wide reach of the information provision is not consistent with the long-standing Swiss policy in this treaty area, it must be assumed that the United States regarded it as a *conditio sine qua non* for the conclusion of the agreement.⁷² The painstaking interpretative history of the “fraud” clause with the still prevailing difficulty of fitting it into two different tax and legal systems, raises serious doubts whether its draftsmen had grasped the complexities of the formula.

Article XVI(1) and (3) provide:

1. The competent authorities of the contracting States shall exchange such information (being information available under the respective taxation laws of the contracting States) as is necessary for carrying out the provisions of the present convention, or for the prevention of fraud or the like in relation to the taxes which are the subject of the present Convention. Any information so exchanged shall be treated as secret and shall not be disclosed to any person other than those concerned with the assessment and collection of the taxes which are the subject of the present Convention. No information shall be exchanged which would disclose any trade, business, industrial or professional secret or any trade process.

2. . . .

3. In no case shall the provisions of this Article be construed so as to impose upon either of the contracting States the obligation to carry out administrative measures at variance with the regulations and practice of either contracting State or which would be contrary to its sovereignty security or public policy or to supply particulars which are not procurable under its own legislation or that of the State making application.

The application of that part pertaining to the exchange of information “necessary for carrying out the provisions” of the Treaty did not pose particular problems. Its main purpose is to give to the other country information on taxpayers claiming an exemption or deduction from taxes under the Treaty in order to prevent the abuse of treaty provisions and to secure the taxation of treaty-favored income.⁷³ The question of disclosing

⁷¹For an outline on information clauses in U.S. tax treaties, see Mitchell B. Carroll, *Evolution of U.S. Treaties to Avoid Double Taxation of Income*, pt. II, 3 INT'L LAW. 163 (1968).

⁷²Locher, vol. 2, art. XVI, No. 9.

⁷³Locher, vol. 1, No. 190.

information under banking secrecy does not arise here because treaty advantages benefit the taxpayer only to the extent that he supplies the demanded data with respect to his capital investments in stocks, bonds, bank deposits, etc.⁷⁴

Very few precedents deal with the interpretation of the crucial "prevention of fraud" clause.⁷⁵ Until the recent, hereinafter discussed decision of the Federal Court no Swiss judicial authority has ever knowingly ruled on that area of Article XVI. Some conclusions could, however, be drawn from some related Treaty provisions, and a few published rulings of administrative authorities.

The obligation to furnish information pertains only to offenses with regard to taxes covered by the Treaty,⁷⁶ and the term "fraud" must be interpreted under the law of the requested country.⁷⁷ Notwithstanding the restrictive wording, it appears to be obvious that the "fraud" clause applies not only to preventive, but also to repressive measures. It is difficult to mark a borderline between prevention and suppression in the field of taxation, and the provision would otherwise become meaningless to a large extent, for the tax authorities are often not in a position to prevent tax fraud.⁷⁸

The two requirements need not be fulfilled cumulatively; in other words, information to prevent or suppress fraud need not also be related to a case of double taxation. Further it is not required that the person on whom information is demanded be taxable in both countries or that he be suspected of an illegal tax offense.⁷⁹ Not available is information which would disclose any trade, business, industrial or professional secret, or any trade process. However, in a decision of 1956 the Federal Department of Finance and Customs ruled that facts relating exclusively to tax offense (and

⁷⁴See, for instance, form R 82 for the refund of Swiss tax withheld at source on dividends and interest derived from Swiss sources, and form R US 1 for refund of, or credit for, additional withholdings of tax on U.S. dividends or bond interest.

⁷⁵It is noteworthy that comprehensive analyses on tax treaties between the U.S. and other countries than Switzerland, with similar "prevention of fraud" clauses, are practically silent on the interpretation of this queer "appendix" to a convention for the avoidance of double taxation. Compare, for instance, Chrétien, 39 *Revue de Science et de Législation Financières*, 415 (1947) on the 1939 and 1946 Treaties with France; Lazerow, 39 *FORDHAM L. REV.* 649 (1971) on the 1967 Treaty with France; Hermon Manning Wells, *U.S. Policies in International Double Taxation of Income*, Thesis, Geneva 1950, at 206 *et seq.*, and Carroll, *supra* note 71, at 163.

⁷⁶Art. I(1)(a).

⁷⁷Art. II(2).

⁷⁸See Locher, vol. 2, art. XVI, No. 9. A circular issued by the Swiss Federal Council in 1951, deals with information "for the prevention and discovery of tax fraud cases." *Kreisschreiben* No. 2 of November 30, 1951, § III(3), *Bundesblatt* (Federal Gazette) 1951 III, at 995.

⁷⁹The IRS could hence, in a fraud case, require information from Swiss tax authorities with respect to a person not subject to U.S. taxation. See Locher, vol. 2, art. XVI, No. 7.

not to a genuine secret), the non-disclosure of which would serve only to escape prosecution, cannot be regarded as worthy of protection, and to take precedence over the Treaty obligation to release such information.

Under a more lenient interpretation, any illegal act could be qualified as a professional secret and make the application of Article XVI in tax fraud cases ineffective.⁸⁰ With respect to the cardinal question of whether, and to what extent, *banking secrecy* could bar the exchange of information in fraud cases, very little official authority is available. In 1955 the Swiss Federal Tax Administration (hereinafter cited as "FTA") specified in a letter to the IRS, that it cannot supply information referring to bank affairs, because such an investigation is not possible under Swiss law.⁸¹ The FTA suggested to the IRS that it secure the necessary certificates or information directly from the taxpayer.⁸²

Two years later the Federal Council rejected an appeal of a corporation, against the decision of the FTA to furnish information to the IRS in a tax fraud case.⁸³ The object of the IRS request was an inquiry into the control of a Swiss corporation, and its transactions with a United States company and the shareholders thereof. The FTA investigated the case and reported to the IRS the relevant facts, refusing however some information considered to be protected by banking secrecy. It cannot be derived from the decision whether the furnished information was nevertheless regarded as meeting the IRS needs.

2. RULING OF THE SWISS FEDERAL COURT OF 1970

On December 23, 1970 the Federal Court handed down a decision with respect to Article XVI, which should shed some more light on its interpretation.⁸⁴ The Court ruled basically that the FTA was by virtue of the "fraud" clause entitled to supply the IRS with information consisting of bank data on allegedly questionable dealings between a Swiss Bank and a United States citizen. The importance of the decision requires that it be closely examined.

The object of the judgment was an appeal by the U.S. citizen against an order of the FTA to transmit to the IRS upon its request, a report summarizing the result of the investigation that also contained data from books and records of the bank involved. The appeal was primarily founded

⁸⁰Partly published in Locher, vol. 2, art. XVI, No. 8.

⁸¹Published in Locher, vol. 2, art. XVI, No. 4.

⁸²This suggestion makes sense under a tax law that threatens a non-complying taxpayer with a presumptive assessment if he does not supply sufficient evidence.

⁸³Published in Locher, vol. 2, art. XVI, No. 14.

⁸⁴BGE 96 (1970) I 737. Unofficial translations of the decision are published in CCH, U.S. TAX CASES, 1971, No. 9435, and in 10 INT'L LEGAL MATERIALS 1029 (1971).

on the contention that there was no basis under Swiss domestic law for the investigation made at the bank, since no Swiss taxes were at stake and that, in addition, banking secrecy would bar the furnishing of the intended information.

The Court first reaffirmed the doctrine that under Swiss tax law third parties—and that includes banks—may not be required to give information on a taxpayer in assessment proceedings, and it pointed out that this rule applies equally to international administrative assistance in tax matters.⁸⁵

However, the issue at bar was not the investigation of an assessment measure, but a proceeding for tax fraud with respect to United States taxes. Therefore the examination of the requirement for obtaining information in a proceeding of tax fraud affecting the United States Federal income tax was necessary. The Court held that neither the text of the clause nor the spirit and purpose of the Treaty, indicates intentions of the two countries to limit the availability of information to cases where taxes were simultaneously evaded in both countries. Hence, Switzerland would not have to consider whether Swiss tax laws have been violated as criterion for supplying information to the United States.⁸⁶

Of great importance then is the conclusion that available information under the “fraud” clause, must be interpreted as meaning all information that could be procured from banks under Swiss law, if the taxpayer had defrauded Swiss tax authorities with respect to its income tax or, in more general terms, each party to the Treaty must furnish some *information* that it could obtain under domestic law if the situation were reversed.⁸⁷

The decisive factor for applying the “fraud” clause is thus whether or not a bank must, if the fraud had been committed under Swiss law, furnish information to shed light on acts allegedly committed by a bank customer. Since the Federal law does not contain any provisions on this subject, and the cantonal tax laws give entirely different answers, the question arises—and this is another basic issue—whether Switzerland has undertaken a treaty obligation to exchange under the “fraud” clause, only that information which could be obtained from banks under the applicable cantonal law—if the situation were transposed accordingly—or whether this country has agreed to establish an obligation under Federal law on the part of the banks to supply information in certain cases. If Article XVI has to be interpreted accordingly, this obligation would take priority over divergent cantonal law, by the fact that a tax treaty becomes Swiss domes-

⁸⁵BGE 96 (1970) I 746.

⁸⁶*Loc. cit.*, at 746.

⁸⁷*Loc. cit.*, at 746/747.

tic law after its approval by the Federal Parliament and its ratification by the Federal Council.⁸⁸

The text of the Treaty or its legislative history does not answer this question and the Court tried to find its way by looking to the purpose of the Treaty for its interpretation. It logically argued that if cantonal law were used as a basis, the result would be that identical information would be available or not available in Switzerland, depending on the applicable cantonal law, and pointed to the possibility, in case of predominance of cantonal rules, to shift fraudulent manipulations to banks located in "favorable" cantons. The Court then assumed that on the question of bank information the attention of the United States must have been primarily directed at the three important international banking centers: Zurich, Basel and Geneva.⁸⁹

In those cantons tax fraud is considered to be a criminal offense, and is prosecuted in accordance with the provisions of the codes of criminal procedure, which usually do not authorize the banker to refuse giving evidence. Notwithstanding the fact that these procedural obligations are directly based on the procedural law, the Court held that their actual basis is nevertheless cantonal tax legislation, and the reference to the provisions of the procedural codes constitutes merely a simplification from the viewpoint of legal technique.⁹⁰

The Court proceeded then to its crucial and most arguable step of interpretation, by assuming that the uniform pattern of rules in the three major banking centers on the question of bank information in cases of tax fraud, could have been *interpreted by the United States Treaty negotiators as an expression of the prevailing Swiss legal concept* ("*als Ausdruck der herrschenden schweizerischen Rechtsauffassung*"), and that they could have, under given circumstances *in good faith assumed that Switzerland had agreed to include bank information in the "fraud" clause*.⁹¹

It would be contrary to the meaning and purpose of the Treaty if Switzerland would now insist on basing the criterion on the availability of information on cantonal law. The Court thus established a competence under Federal law to carry out investigations at banks in order to fulfill the Treaty obligations in tax fraud cases.⁹² The ruling also explicitly confirmed that banking secrecy is professional secrecy.

⁸⁸Transitional Provisions of the Federal Constitution, art. 2.

⁸⁹BGE 96 (1970) I 748.

⁹⁰The availability of the information "under the respective *taxation* laws of the contracting States" is required by art. XVI(1) of the Treaty (emphasis added).

⁹¹BGE 96 (1970) I 750.

⁹²The Court left the question open as to whether facts determined with respect to such investigations under the Treaty, rule could be used for domestic tax purposes.

But with regard to the last sentence on Article XVI(1) according to which information disclosing any trade, business, industrial or professional secret or any trade process cannot be exchanged it held—again a bold interpretation—that no independent importance can be attached to it for the reasons already set forth.⁹³ The Court did not omit to emphasize, however, that the Swiss banking secrecy is not abolished by virtue of Article XVI, but can merely be lifted under very specific conditions. The Swiss tax authorities are therefore required to examine carefully, the allegation in a request for information in a tax fraud case before starting inquiries at a bank.⁹⁴

The scope and possible future effects of the decision are difficult to evaluate.⁹⁵ The ruling fully covers the willingness of the FTA to provide the IRS, in an apparently serious fraud case, with bank information and thus sanctions, for the first time, a limitation on Swiss banking secrecy in international tax relationships. But can it be interpreted as holding that banking secrecy may always be lifted when a United States taxpayer defrauded United States taxes, even, for instance, if the Swiss bank did not take part in the fraud as happened in the case at bar? It is doubtful that Switzerland intended the Treaty to provide such far-reaching assistance obligations.

A close examination of the decision raises at least as many questions as it answers, and leaves serious doubts as to whether the issue on the fraud clause is settled. One of the points to be questioned is the judicial assumption that the uniform availability of bank information in criminal proceedings at three main banking centers could have been interpreted by the United States Treaty negotiators as prevailing Swiss legal opinion. Such reasoning sounds artificial and not convincing. Swiss federalism in the area of taxation and legislation is so notorious, that it can be expected to be known to tax treaty experts as a nation with unlimited sources of intelligence, and even if not, such knowledge would have been easily obtainable.

The argument that shady transactions could otherwise be shifted to cantons where banks are not required to furnish information, is an objection equally valid for Swiss domestic transactions and is nothing more than

⁹³BGE 96 (1970) I 752.

⁹⁴The request for assistance must credibly justify the necessity of an investigation for tax fraud ("glaubhaft die Notwendigkeit einer Untersuchung auf Steuerbetrug begründen"), *loc. cit.*, at 751.

⁹⁵For comments in the United States (with an unmistakable tendency to give the effect of the ruling an "overshooting" importance) see *Swiss Bank Accounts Not Immune From IRS*, 34 J. OF TAXATION, 293 (1971); Steptoe, *The "Secret" Swiss Account: End of An Era*, 38 BROOKLYN L. REV. 383 (1971).

one of the prices to be paid for a federalistic system.⁹⁶ The interpretation given in the ruling puts the IRS with respect to the availability of tax information in fraud cases in a better position than many cantonal tax authorities—an absurd result, that could never have been intended by Switzerland when negotiating the Treaty.

Another unsolved main issue is the question of the usefulness of bank information to the United States as supplied by virtue of a tax treaty. Tax information exchanged between the revenue services of two countries are usually furnished in the form of a confidential official report (*Amtsbericht*). Such reports merely serve informative purposes, and are hence not documented with original records or other items of evidence. This area of international administrative assistance, as provided in tax treaties, must be clearly distinguished from international judicial assistance as applied in treaties on mutual assistance in criminal matters.

An agreement on judicial assistance requires numerous detailed procedural provisions, dealing with questions as to giving testimony, availability of documents, execution of letters rogatory, personal appearance, etc. A treaty for the avoidance of double taxation has a completely different objective and cannot be a suitable tool to cover this complex field of international assistance.⁹⁷ But if tax information as supplied by a treaty partner cannot be effectively used in court proceedings in the United States, with its rigid rules for due process, the usefulness of a “fraud” provision becomes fairly limited, and its effectiveness questionable.

B. Unilateral Measures of the United States

Because of the virtual impossibility of efficiently curbing the use of foreign bank facilities for tax evasion, and other illegal purposes at the

⁹⁶The pros and cons of Swiss federalism (a term applied in Switzerland to emphasize a tendency to preserve the individuality of political subdivisions, hence, with an exactly opposite meaning from that used in the United States) should, of course, not be evaluated only under the narrow viewpoint of taxation. The federal structure, historically grown during centuries, is—with all its bearable shortcomings—still widely held as the very “lifeblood” of a lively democracy, and as a keystone for good relations between, and protection of, different linguistic and cultural population groups. It is clear that the postulate of an “ideal” tax system has to be subordinated to the more vital socio-political aspects of the country’s structure. The United States position with respect to the Swiss way of handling tax offenses at the H.R. 1969/1970 Hearings (see *infra* note 107, at 81), that these “policies may have been necessary 100 years ago or 50 years ago, but now Switzerland is in the modern era” appears for these (and other) reasons rather out of place.

⁹⁷That no judicial assistance can be read into art. XVI may also be concluded from its text. Whereas most U.S. tax treaties contain the standard formula that exchanged information may be disclosed only “to persons (including a court or administrative body) concerned with assessment, collection, enforcement, or prosecution with respect to taxes,” the Swiss–U.S. Tax Treaty is much more restrictive by prohibiting the disclosure of information “to any person other than those concerned with the assessment and collection of taxes.” It cannot be assumed that the prosecuting and judicial bodies have not been deliberately omitted as recipients of tax information.

international level, the United States has launched a unilateral program for obtaining more information on foreign accounts and transactions in various areas.

A first measure deals with the disclosure of foreign bank accounts. Each United States taxpayer is, with respect to taxable years beginning on or after January 1970, required to disclose his interest at any time during the taxable year in foreign bank, brokerage, and similar accounts on his tax return.⁹⁸ The question appears to be based on the general authorization of the IRS, to require information from all persons subject to United States tax.⁹⁹ An affirmative answer requires the filing of an additional form, specifying the type of interest and other relevant details, with the return.

This approach of obtaining bank information directly from the taxpayer, looks like a variation on the Swiss approach, but differs in its method of applying pressure on non-complying taxpayers. The Swiss tax authorities usually require in suspicious cases the production of bank records or, if refused, the payment of taxes on the basis of an assumed income; the United States system puts the deterrent effect on penal and forfeiture sanctions.

Another area of counter-measures is covered by "*The Currency and Foreign Transactions Reporting Act*" (also known as the "Secret Foreign Bank Accounts Act"), as enacted on October 26, 1970.¹⁰⁰ This legislation aims at "frustrating organized and white collar criminal elements who use secret foreign accounts" in connection with tax evasion and drug, gambling, securities and currency violations,¹⁰¹ and provides for certain reporting or record keeping "where such reports or records have a high degree of usefulness in criminal, tax, or regulatory investigations or proceedings."¹⁰²

Obtaining records by established discovery procedures from banks and other institutions, in connection with the examination of a particular taxpayer's returns, apparently does not infringe his right of privacy under United States legal concepts. To proceed a step further, and survey such records regularly, would certainly open immense possibilities to the IRS, in tracking foreign dealings and would provide leads to tax evasion cases. It is

⁹⁸The question on form 1040 reads: "Did you, at any time during the taxable year, have any interest in or signature or other authority over a bank, securities, or other financial account in a foreign country (except in a U.S. military banking facility operated by a U.S. financial institution)?"

⁹⁹IRC, § 6011(a). See also 37 Fed. Reg. 6913 (1972) § 103.24.

¹⁰⁰Pub. L. 91-508 (84 Stat. 1114 *et seq.*) (hereinafter cited as "1970 Act"). For comments on the 1970 Act see, Thomason, *Secret Foreign Bank Accounts*, 6 TEXAS INT'L L. FORUM 105 (1970); *Secret Swiss Bank Accounts: Uses, Abuses, and Attempts at Control*, 39 FORDHAM L. REV. 500 (1970-1971); Steptoe, *supra* note 95, at 303; Seltzer, *New rules*, 34 J. OF TAXATION 292 (1971).

¹⁰¹Statement of Samuel R. Pierce, Jr., Treasury General Counsel, Wall Street Journal, March 31, 1972, at 3.

¹⁰²1970 Act, § 202.

questionable, however, whether the advantages of such broad authority would outweigh possible adverse effects on legitimate business transactions.¹⁰³

The regulations implementing the provisions of titles I and II of the 1970 Act¹⁰⁴ basically require *individuals* who physically take more than \$5,000 in cash, foreign currency, travelers' checks, money orders or bearer-form negotiable securities out of the country or arrive in the United States with such a sum to report it to the customs officer on the spot. If the monetary instrument is mailed or otherwise transported separately, the report must be filed by mail with the Commissioner of Customs.

Further, each person having financial interests in a foreign bank account is required to keep records of all tax-relevant aspects of the account for five years. *Banks and financial institutions* have to report currency transactions—domestic or foreign—of more than \$10,000 each (except in a few specified cases), and must keep records of all transfers of more than \$10,000 into or out of the United States. They must retain such records for two years (in some cases for five years) so that the authorities may reconstruct the transactions in such account. Unreported transactions may result in civil or criminal penalties and confiscation of the currency moved in violation of the reporting provisions.

The enforcement of such rules naturally poses problems, but there is no doubt that the measures will have a certain deterrent effect on illegal money transfers. The approach chosen by the United States also saves the legislator from having to single out specific nations whose banking system appears to be particularly attractive to United States persons. Thus, the risk of substituting one country's financial facilities for those of many others available to prospective tax evaders is reduced. The 1970 Act might serve as a model for other countries facing similar problems.

VI. Proposed Treaty Between Switzerland and the United States on Mutual Assistance in Criminal Matters

The beginning of the Swiss–United States cooperation in the field of mutual assistance in criminal matters goes back as far as the last century.

¹⁰³It is interesting to note that in the United States new voices claim that one of the "problems inherent in this type of legislation, is that it jeopardizes banking 'privacy' which also exists in the United States," and that any investigation under the 1970 Act therefore be restricted to the bank records of those suspected of a crime. See *L.A.R.*, *supra* note 68, at 103.

¹⁰⁴The application of the rules has been delayed by objections raised with respect to a first set of regulations, set forth in tentative form by the U.S. Department of Treasury on June 10, 1971 (36 Fed. Reg. 11208 (1971)). U.S. banks are apparently not enthusiastic about the rules; see *New York Times*, Aug. 16, 1971, at 37. The somewhat eased final version of the regulations becomes effective July 1, 1972. 37 Fed. Reg. 6912 (1972).

In 1900 a Treaty for the Extradition of Criminals was concluded.¹⁰⁵ This bilateral relationship was supplemented by cooperation on an ad hoc basis and accession by both countries to a number of multilateral agreements designed to combat typical international crimes.

The main reason that no bilateral treaty on judicial assistance came into existence for so many decades, must certainly be linked to the great difficulties of reconciling particulars of the Anglo-American procedural law with the Continental European pattern of criminal proceedings. It appears that the conclusion of the European Convention on Mutual Assistance in Criminal Matters in 1959¹⁰⁶ has initiated a change in the United States attitude toward considering a treaty concept, that would also fit into the European procedural system. Another impetus to approach Switzerland for the conclusion of an assistance treaty is probably linked with the problems arising in the United States with regard to the shifting of illegally acquired moneys to foreign countries. The public discussion on this topic culminated at the Hearings before the Committees on Banking and Currency of the Senate and the House of Representatives in 1968 to 1970.¹⁰⁷

The confidential course of the negotiations has hitherto prevented the release of substantive information on the scope of the prospective agreement. There is no doubt that the reconciling of fundamental differences in the fiscal and legal concepts of the two countries, poses major obstacles for a speedy preparation of a draft. With a view to the non-availability of banking information to the Swiss tax authorities themselves, it can safely be predicted that the treaty will, on principle, not be applicable to investigations or proceedings concerning violations of tax laws. Tax offenses would also have to be excluded on the ground that the exchange of information and granting of assistance in tax fraud cases is exhaustively regulated by the Tax Treaty.

But this principle will presumably suffer one significant exception. Unofficial reports indicate that judicial assistance might, under specified circumstances, be extended to *tax offenses of persons who belong to organized crime*.¹⁰⁸ It is reported that assistance would be granted only on

¹⁰⁵BS 12, at 267; T.S. No. 354.

¹⁰⁶472 U.N.T.S. 186.

¹⁰⁷*Hearings before the Subcommittee on Financial Institutions of the Committee on Banking and Currency, U.S. Senate, 91st Cong. 2d Sess., on S. 3678 and H.R. 15073, Washington, 1970; Hearings before the Committee on Banking and Currency, House of Representatives, 90th Cong. 2d Sess., on Legal and Economic Impact of Foreign Banking Procedures on the United States, Washington, 1968; Hearings before the Committee on Banking and Currency, House of Representatives, 91st Cong. 1st and 2d Sess., on H.R. 15073, Washington, 1970 (hereinafter cited as "H.R. 1969/1970 Hearings").*

¹⁰⁸*Compare New York Times, Aug. 18, 1970, at 1 and 8; Tax News Service, Aug. 31, 1970, pt. 11, at 53; European Taxation, Sept. 1970, pt. 11, at 128; Secret Swiss Bank Accounts: Uses, Abuses, and Attempts at Control, 39 FORDHAM L. REV. 508 (1970-1971); U.S. NEWS & WORLD REPORT, Feb. 12, 1972, at 61.*

grounds of reasonable suspicion that the alleged crime has been committed by upper echelon members of a criminal group of persons (other than mere gangs) who were actively engaged in obtaining significant influence in commerce or politics for a substantial period of time and, in addition, if it can be concluded reasonably that the requested assistance would result in the imprisonment of such persons for a longer period of time.¹⁰⁹ Such a proceeding would obviously supersede banking secrecy. If the final draft of the proposed treaty takes that direction, the United States may claim to have reached one of its main policy aims in its campaign against Swiss banking secrecy.

The United States characterizes organized crime as "a totalitarian and closed society operating within an open and democratic one," and as a threat that cannot be ignored or tolerated any longer.¹¹⁰ Some go even further, and claim that its impact has become a worldwide problem.¹¹¹ Unique features of organized crime are its dedication to illegality as a *continuing* enterprise, its reach of all profitable areas of criminality and a great flexibility on changes of economic or legal conditions.¹¹² The social and political dangers of organized criminality are certainly eminent.

Particularly demoralizing is the fact that responsible leaders, not directly involved in the committing of common crimes, apparently very often succeed in escaping criminal prosecution. Loopholes in the laws, shortcomings in law enforcement, and a wide net of corruption are regularly cited as reasons for this degree of immunity from legal accountability.¹¹³

Thus the only way to punish top people of criminal groups is often prosecution for tax offenses. There is no doubt that the upper echelon of organized crime also takes advantage of international finance transactions to harbor the fruits of their crimes outside the United States. International assistance to locate such funds would be one among the various desirable weapons for the difficult fight against this devastating form of lawlessness.

The inclusion of provisions concerning organized crime in a judicial assistance treaty poses very difficult definitional problems, particularly in view of the fact that not even United States domestic law allows the truly

¹⁰⁹*Neue Zuercher Zeitung*, Aug. 23, 1970, at 17.

¹¹⁰MESSAGE FROM THE PRESIDENT OF THE UNITED STATES RELATIVE TO THE FIGHT AGAINST ORGANIZED CRIME, April 23, 1969, H.R. Doc. No. 91-105, at 2.

¹¹¹H.R. 1969/1970 Hearings, at 15.

¹¹²Compare Wilson, *The Threat of Organized Crime: Highlighting the Challenging New Frontiers in Criminal Law*, 46 NOTRE DAME LAW. 41 (1970).

¹¹³See particularly the shocking report of Senator McClellan, *The Organized Crime Act* (S.30) or its Critics: Which Threatens Civil Liberties? 46 NOTRE DAME LAW. 55 (1970). See also Presidential Message, *supra* note 110. The statement at the H.R. 1969/1970 Hearings "that the tax evasion problem is the most serious aspect of these hearings, even more than the use of these secret foreign accounts by the organized underworld" (at 56) is in view of the described realities uncomprehensible.

responsible to be brought to trial. Besides this specific area many other thorny questions arising from the different legal concepts of the two countries must be solved. Serious problems include the extreme formalism and the rigid exclusionary rules of the United States procedural law. The rules for due process, finding its ultimate rationale in the system of trial by jury, do not easily fit into a bilateral agreement with a civil law country where judges have a far wider discretion in evaluating facts and evidence.¹¹⁴

Such discrepancies take particularly vexing dimensions if they become interrelated with other conflicting legal approaches of the two countries. Thus Swiss law protects the individual's privacy to a much greater extent than United States legislation. Also on the procedural side various restrictions exist.¹¹⁵ It is obvious that such rights may not be basically curtailed in international assistance proceedings. A particularly careful weighing of interests will be necessary in cases in which the disclosure of facts affects persons who are not connected in any way to the offense which is the basis for an assistance request.¹¹⁶

Another 'pièce de résistance' for mutual assistance might be the so-called doctrine of limitation on use of obtained information (*Prinzip der Spezialitaet*) as applied under Swiss law.¹¹⁷ This rule means that information may not be used in any proceeding relating to an offense other than that for which assistance has been granted. Conflicts could then emerge when the crime for which assistance is obtained also involves a violation of tax laws (the falsification of a document may, for instance, be connected with tax evasion). Obtained assistance may not be used for the prosecution of a fiscal offense.

Conversely, information supplied under a tax treaty must not be brought into an investigation in proceedings for common crimes.¹¹⁸ This doctrine is hardly compatible with the United States procedural concept under which any item of evidence is considered as a matter of public record. Other procedural questions to be cast into the framework of the two legal con-

¹¹⁴Thus both the rule against opinion, inference or inclusion, and the rule against hearsay would require in assistance proceedings, that original records or documents be presented to the U.S. authorities. An official report with all the necessary information furnished by the authorities of the requested country, would apparently be of little value in a U.S. trial.

¹¹⁵See Meyer, *Obtaining Evidence in Switzerland for Use in Foreign Courts*, 3 AM. J. COMP. L. 412 (1954); Miller, *International Cooperation in Litigation Between the United States and Switzerland: Unilateral Procedural Accommodation in a Test Tube*, 49 MINN. L. REV. 1069 (1965).

¹¹⁶If the proposed treaty should provide for the furnishing of documentary evidence to the requesting country, this delicate question would particularly arise when imparting banking information in form of ledger sheets.

¹¹⁷*Verwaltungsentscheide der Bundesbehoeden* (Administrative Decisions of Federal Authorities) 1957, No. 3.

¹¹⁸The doctrine is also embodied in the OECD Draft Convention, art. 26(1).

cepts, concern rules on personal appearance for testimony in the requesting country, the interviewing of persons in the requested country by representatives of the requesting side, the authentication of documents and many related items of assistance proceedings.¹¹⁹

If the prospective treaty comes into effect with provisions on the availability of fiscal and banking information in cases concerning organized crime, it may certainly be regarded as a significant step forward in the international combat against dangerous forms of crime.¹²⁰ But the exception with respect to organized crime could hardly be interpreted as a departure from the traditional Swiss approach in the area of tax and banking information. Assistance would only be granted for the purpose of bringing leaders of criminal groups to trial, and the roundabout over tax offenses has to be regarded as a mere tactical device.

There should also not arise the illusion that Switzerland's share to that end, will become a decisive factor in curbing the organized underworld. '*La Cosa Nostra*' commits much more abominable crimes than tax evasion, and other escape routes to shelter moneys are available. Again, it should be taken into consideration that the main attack can only be mounted on legal loopholes and other shortcomings within the nation where such demoralizing operations can be run without seriously risking having to account legally for them.

VII. Concluding Observations

This study does not attempt to pass judgment on values and demerits of banking secrecy, or to make futile guesses on its real impact on international tax morale. The area is very comprehensive and has manifold economic, legal and political implications. Existence of secrecy in banking affairs is, in Switzerland and in numerous other countries, to varying degrees, a matter of fact,¹²¹ and must be faced in some way. A few summarizing remarks focus on some crucial points and should recall some aspects that are often neglected when outlining one or the other sector of the problem.

¹¹⁹The necessity of agreeing on a large set of partly complex procedural rules, may be regarded as another conclusive argument that a brief information clause in a tax treaty such as art. XVI of the Swiss - U.S. Tax Treaty, cannot be interpreted as an obligation to provide judicial assistance. Exchange of information under a tax treaty is confined to purely administrative assistance, and thus excludes the servicing of evidentiary items such as original documents.

¹²⁰The discussed agreement would knowingly be the first comprehensive mutual assistance treaty in criminal matters, between the United States and a civil law country.

¹²¹In 1970, banking accounts could be kept secret from foreign investigations in 27 countries, 163 N.Y. L.J. 41 at 1 (1970).

Under domestic taxation, Swiss banking secrecy clearly does not offer a refuge to tax evaders or persons involved in crime. A well-balanced approach, not artificially imposed but grown through a long legislative history, allows the maintenance of privacy in money matters to a reasonable extent without providing tax escape routes. The approach provided by Swiss law (in particular in the tax area), to keep banking secrecy within its legitimate purposes, cannot be simply overlooked when considering its broader implications and possible remedies.

Internationally, banking secrecy poses obviously more onerous problems. Not too long ago, widely applauded as a virtue, change of times and a pragmatic approach now cause many to condemn the extensive legal protection of the bank depositor against unveiling data in favor of foreign governments as a vice of Switzerland's legal system. Even leaving out of consideration the basic concepts of Swiss banking secrecy, deeply imbedded in the country's legal system and "*tout imprégnée de juridisme et de moralisme*",¹²² it cannot be reasonably expected that a country furnishes confidential information to foreign revenue services, which is not obtainable to its own tax authorities.

Neither is it conceivable to abandon by a stroke of the pen, a tax system, integrated into a federalistic structure, that relies basically on information given by the taxpayer. As is well known, in Switzerland changes in the law need the consensus of the electorate, and public opinion would hardly be prepared to give the green light to such a drastic step. Currently, it is highly questionable whether the curtailing of Switzerland's banking secrecy, would bring any sensible relief to problems of tax evasion of other countries. Exchange-of-information clauses in tax treaties still have, even without secrecy in banking affairs, a very limited scope.

The numerous nations maintaining secrecy—some of them with a much tighter veil¹²³—would willingly substitute for the one loophole allegedly already plugged. A worldwide harmonization of the secrecy concept, probably belongs for the foreseeable future, to the realm of wishful thinking. And it is a sad truth to remember that even without banking secrecy, our imperfect world would still offer a wide field to sophisticated tax evaders.

The present survey also shows that Switzerland does not flatly refuse international cooperation in the area under discussion, where the law-enforcement problems really outgrow a country's possibilities, and where the degree of lawlessness emerges as a danger of international

¹²²Vasseur, in the preface to Raymond Farhat, *Le Secret Bancaire, Étude de Droit Comparé* (France, Suisse, Liban), Paris 1970, at III.

¹²³The assumption that the use of such banking accounts has not—or not yet—outmatched that of Swiss banks must probably be linked, besides the latter's reputation, with the belief, right or wrong, that Switzerland's political and economic stability remains eternally unshakable.

concern such as organized crime. Unilaterally, in the 1970 amendment to the Banking Law, Switzerland strengthened the requirements with respect to the establishment of new banks (there is some belief that foreign-controlled banks have been less hesitant in engaging in questionable transactions).

Further, a sound self-interest should induce banks to observe a defensible standard of banking ethics,¹²⁴ and to exercise an alert self-restraint vis-à-vis investors with assets of doubtful origin. The prosperity of the Swiss banks does not depend on dubious dealings which, in the long run, would not only damage their reputation, but could also generate adverse effects on the nation as a whole. The large majority of Swiss bankers are doubtlessly aware of their great responsibility in this area.

A realistic analysis of the underlying problems and facts should suggest that tax evasion and money-related crime, must primarily be combatted in the affected country itself. No nation modifies its law and tax system on the grounds of mere convenience to a foreign government, even with full awareness of today's international interdependence in economic, political and social affairs. The "*do ut des*" plays in no other area of international law a more significant role, than in international fiscal relationships—the treasures still belong to the best defended national fortresses.

Even if the possibility should not be ruled out that multilateral agreements might ease the problem of international tax evasion at some future date, the practical and doctrinal obstacles to bring all nations in this area under one umbrella can hardly be over-estimated. And not all countries have hitherto seriously attempted to do their homework in dealing with tax evasion and related problems.

The claim for international assistance and for compliance of other nations with one's own requests loses much of its credibility, if domestic measures in this field lack the necessary vigor or are handicapped by factors that are in no way related to banking secrecy.¹²⁵ The hardly disputable argument that the issue is, with regard to the United States, "essentially an American problem which should, in the last analysis, be solved by Americans,"¹²⁶ has therefore, to some extent at least, global validity.

¹²⁴The Swiss Bankers' Association issued guidelines in 1968 to that end, with particular emphasis to observe U.S. regulations.

¹²⁵Thus, in view of the long-existing penetration of organized crime in American life (as referred to in the Presidential Message of 1969), it is difficult for an outsider to understand why the relevant U.S. laws, and the law enforcement machinery, have not been adapted to the situation in a way that would have dealt a striking blow to organized crime conspiracy, thus making cumbersome international efforts to locate illegally acquired funds abroad less compelling.

¹²⁶*L.A.R.*, *supra* note 68, at 106. See also *Swiss Bank Accounts*, *supra* note 100, at 500.