



The end of banking secrecy

In the wake of the collapse of Switzerland's oldest private bank, following threats of prosecution by the United States government, global risk specialists mi2g consider what lies ahead for Swiss banks and banking privacy in general

Established 270 years ago, Wegelin and Co bank had managed to survive every threat posed to them across three centuries: revolution, financial disaster and war, including being invaded by Napoleon, the Sonderbund civil war and then Hitler. Thus they weathered every storm but one: the assault by the United States government. The attack on Swiss banking secrecy by the US has sought to reclaim the funds lost through tax evasion schemes sold to its citizens.

Remarkably, Wegelin neither had offices nor employees in the United States. They were 100 per cent Swiss and violated no Swiss law. However, US authorities believed that a handful of Wegelin's US clients were hiding assets and not paying taxes. The fact that the bank wasn't subject to US law and had zero legal responsibility in ensuring

their customers filed tax forms became irrelevant. The US government ultimately crushed Wegelin by threatening the bank with lawsuits, investigations, Internal Revenue Service (IRS) penalties and criminal charges levied personally against the bank's directors.

The US Department of Justice (DoJ) has been steadily closing a net around Swiss banks ever since the UBS admission of assisting tax evasion by US citizens in 2009. That year, UBS avoided US prosecution by paying \$780 million (£491) and handing over confidential data. Ever since the DoJ and the US tax authority – the Internal Revenue Service (IRS) – have been building cases against other Swiss banks that are alleged to have either opened secret accounts from scratch or poached UBS clients who wanted to dodge the tax-evasion crackdown such as Wegelin.

At the end of last year, it was revealed that 11 Swiss banks had been given an ultimatum to hand over thousands of client names and pay billions in fines to avoid tax evasion prosecution in the US. The Swiss banks were under pressure to provide all correspondence with offshore clients over the past 11 years – with deadlines set for the end of January 2012. Some of the banks in question were very close to caving in and delivering the data directly – until the Swiss government intervened and persuaded them to encrypt the data for the time being.

As a result, the documents that have been handed over to date are encrypted to protect the names of individuals and client advisors. The key to decoding the information will only be provided on assurances from the US government that no further action against Switzerland's remaining 300 banks will be taken. Switzerland wants these assurances to be enshrined in a new treaty with Washington, DC.

There are signs, however, that Switzerland may be mistaken in believing that a global solution is in the offing. The American side is unlikely to be interested in such a solution at this stage, because it would give them less opportunity to exert pressure by making examples of banks of the Wegelin-type and impose hefty billion dollar fines. Many Europeans believe that the US will only come forward to make a deal when the fruit has been squeezed totally dry.

Since the precedent set by the United States government's settlement in 2009 with UBS, US authorities have offered eleven financial institutions in Switzerland (and Israel) a settlement agreement in which the US government's investigations in those financial institutions – for aiding tax evasion – and potential prosecution would be dropped.

The terms of the US government agreement would be similar to the UBS settlement in 2009 and would require each of the 11 Swiss and Israeli financial institutions to share client data regarding US citizens and, most likely, pay a hefty fine. Further assertions were made by Swiss officials at the time that offshore tax evasion would not be tolerated under the cloak of Swiss banking secrecy rules.

Two months ago, the IRS reported that eight Swiss banks, including Credit Suisse, Julius Baer, and Basler Kantonalbank, turned over US client data on taxpayers suspected of tax evasion on 30 January 2012. Not that this puts an end to the negotiations between the US and Swiss governments; three more banks are still expected to turn over client data and a total of 11 banks are expected to pay heavy fines.

Past Swiss guarantees of statutory bank secrecy dating back to 1934 are now gone, surrendered under pressure from threatened and existing US indictments of multiple Swiss bankers. The IRS and the US DoJ tax division have made it clear that they are intent on taking the secret out of secret bank accounts and will prosecute anyone involved: tax payer, banker or professional advisor such as a legal attorney. The consequences for failure to comply with the proper disclosure and filing requirements may lead to audits, severe financial penalties, and in some cases, criminal prosecution.

To add to Wegelin-type Swiss banking woes, there is the new American FATCA legislation: the Foreign Account Tax Compliance Act. The law effectively requires every bank in the world to make a choice: To either accept Americans as customers, but agree to share information with the US

government, or to close the door to all US citizens and residents forever.

Wegelin and Co may be the first standalone Swiss bank to fire-sell its operations in Switzerland as a result of tax evasion pressure from the US, but it's unlikely to be the last.

The twin-track civil and criminal approach seems to be working for the American authorities and the Wegelin case suggests the battles are far from over. In fact, the action taken by the US vis-à-vis Swiss private banks may be a prelude to further action by European and Asian sovereign nations looking to recover their own taxes.

Wegelin's fire sale is likely to be followed by more consolidation in Switzerland's embattled financial services industry as the old, low-cost model of booking secret money comes under relentless assault from major governments around the world following the lead of the US government. The reality is that the service and pricing model of the past no longer works as Swiss banking secrecy erodes and private wealth management goes increasingly on-shore. ■

THE MAN BEHIND MI2G

DK Matai is an engineer turned entrepreneur and philanthropist who founded mi2g, the global risk specialists, in 1995 while developing simulations for his PhD at Imperial College. DK helped found ATCA – The Asymmetric Threats Contingency Alliance – in 2001.

Explain the objectives of mi2g?

mi2g is a Queen's award winning super-computing organisation focussed on global risk management for banks, insurance and reinsurance companies particularly in the area of black swans and low probability high impact events. mi2g's real time intelligence is deployed worldwide for contingency capability, executive decision making and strategic threat assessment.

How does the organisation hope to achieve these objectives?

Using super computing technology the mi2g intelligence unit visualises complex risk from real time data. mi2g's bespoke security architecture, digital risk management and D2-banking rely on an innovative family of underlying tools to deliver scalable infrastructure that brings together people, processes and technology.

What is the Asymmetric Threats Contingency Alliance?

ATCA 5000 is a global collective of strategic intelligence for chairmen, chief executives and parliamentarians at the highest level. ATCA was founded in 2001 to resolve complex global challenges through collective Socratic dialogue and joint executive action to build a wisdom based global economy. Present membership of ATCA is by invitation only and has over 5,000 distinguished members.

How can a business or individual hope to benefit from membership to the ATCA?

Intelligence exchange amongst a distinguished peer-group leads to greater preparedness for asymmetric threats and opportunities arising from climate chaos and the environment, radical poverty and microfinance, geo-politics and energy, organised crime and extremism, as well as demographic skews and resource shortages.