



The future of banking secrecy

Christoph Kerres and Florian Proell on recent developments in banking secrecy in Switzerland and Austria

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Banking secrecy is currently going through a time of change. In light of the financial crisis and the related decreased tax revenues, calls for the uncovering of tax evaders are growing louder. Countries with legal regimes that prevent access to fiscally relevant banking details of foreign customers have therefore come under criticism. Exchange of information is an important tool in fighting non-compliance with tax laws in an increasingly borderless world. The ongoing political pressure by the OECD has forced countries with banking secrecy to make drastic allowances. Using the example of banking secrecy in Austria and Switzerland, this article considers recent developments and the future of banking secrecy in more detail.

Compliance with OECD standards

On 13 March 2009, countries with banking secrecy, such as Austria, Switzerland and Liechtenstein, decided to ease the fiscal exchange of information bilaterally and abandoned their current reservation to Article 26 of the OECD Model Tax Convention. As a consequence of these political commitments, many countries are presently signing bilateral agreements for the exchange of information for tax purposes. Countries must have 12 such agreements in order to be considered to have substantially implemented the internationally agreed OECD standards.

The acceptance of the OECD standards is particularly significant for Switzerland

and Liechtenstein, as these countries differ from others in their treatment of tax evasion and criminal tax offences. In Switzerland and Liechtenstein, dishonestly misreporting income in a tax return is not necessarily considered a crime. Such matters are dealt with in administrative courts and not in criminal courts, regardless of the evaded tax amount. Fraudulent tax conduct only leads to criminal investigations if they are based on a deliberate falsification of records. Cases of dishonest misreporting have not been subject to legal assistance in Switzerland so far. The legal framework in Liechtenstein concerning the exchange of fiscally relevant information was even more restrictive.

In contrast to Switzerland and Liechtenstein, Austria recognises no difference between 'dishonest misreporting' and 'deliberate falsification' of tax returns, but its banking secrecy laws require the instigation of administrative or judicial proceedings. The person accused of evading taxes, for reasons of constitutional legality, must be informed about the imminent suspension of banking secrecy. Moreover, it depends on the severity of punishment – the higher the evaded amount, the higher the degree of punishment – as to whether the evasion is considered to be an administrative or criminal offence. Austria is presently elaborating on a new *Administrative Assistance Act*, which will harmonise Austrian banking secrecy with OECD standards.

Withholding tax

Within the European Union the automatic exchange of fiscal information is based on the European Council Regulation 2003/48/EC on the taxation of savings income. The aim of the directive is to enable the taxation of savings income, in the form of interest payments made in one member state to individual residents in another member state

for tax purposes. Belgium, Luxembourg and Austria will introduce a system of information reporting at the end of a transitional period during which they levy a withholding tax at a rate of 15 per cent for the first three years, 20 per cent for the following three years, and 35 per cent as of 2011. This transitional period ends if and when the EC enters into an agreement, following a unanimous decision of the Council, with Switzerland, Liechtenstein, San Marino, Monaco and Andorra to exchange information upon request as defined in the OECD Model Agreement and if and when the Council agrees by unanimity that the United States is committed to exchange of information upon request as defined in the OECD Model Agreement. As Switzerland and Liechtenstein are presently concluding OECD-conforming double-tax agreements with other OECD member states bilaterally, it is very unlikely that Austria and Luxembourg will have to apply the automatic exchange on the basis of the directive on taxation of savings income as of 2011. However, only recently the European Commission has affirmed its ambitions to introduce an efficient cooperation and recovery system in the field of taxation and drafted two proposals for a council directive (COM(2009) 28 and 29) concerning administrative cooperation in the field of taxation and mutual assistance for the recovery of claims relating to taxes, duties and other measures. These EC-proposals will prevent member states from declining to supply information concerning a person resident for tax purposes in the member state of the requesting authority solely because this information is held by a bank or any other financial institution. Beyond that, information communicated shall be provided by electronic means using a common communication network.



Limits to banking secrecy

In addition to the client-banking relationship, which is based on contract law, Austria, Switzerland and Liechtenstein provide for strict banking secrecy. Several law provisions allow for banking secrecy to be breached under certain circumstances. In international matters, international judicial assistance in criminal matters is the most important. In general, a bank cannot refuse to give evidence and is obligated to hand over documents and objects relating to criminal cases and evasion of taxes. In Austria, banking secrecy can only be suspended if the tax evader deliberately commits a fiscal crime. As previously mentioned, legal proceedings have to be instigated, as only a judge may suspend banking secrecy. The court order has to include a summary of evidence, the name of the tax evader and of the bank and a statement concerning compliance with the principle of proportionality in regard to suspension. After receipt of the court order, the bank has the ability to appeal against the decision of the judge within 14 days. Concerning tax fraud, which is to be considered an administrative offence due to the severity of punishment, a formal notification has to be issued by the tax authority. Therefore, the disclosure of banking data is only permitted if it will be used as evidence against the tax evader and is only needed to substantiate the suspicion. In Austria and Switzerland, suspicion alone is not sufficient to secure access to banking data.

Legal assistance in fiscal matters

As a general rule, Austria and Switzerland do not provide legal assistance to countries beyond bilateral treaties and EU legislation. So far, foreign requests for fiscal exchange of information have only been dealt with if



the request complied with the domestic banking secrecy standards and the double criminality of the act related therewith could be verified. On the basis of these general rules, Austria, in many cases, refused to provide legal assistance in fiscal matters to Germany because of the lack of an officially instituted legal proceeding. Switzerland, on a similar but more controversial basis, refused to provide foreign fiscal authorities with bank details of their foreign costumers as it held the view that dishonestly misreporting income in a tax return is not necessarily considered a crime. In future, Austria and Switzerland, by accepting the OECD standards, will have to differentiate between their citizens and foreign citizens. New procedural rules have to be implemented, which, on the one hand, shall guarantee unchanged banking secrecy for their citizens, while on the other, will ease banking secrecy for foreigners from OECD member states.

Alongside the international measures from the OECD, Germany is presently elaborating on a new draft law on the suppression of tax evasion, which will come into force in summer 2009. This *Tax Evasion Act* will provide for a domestic type of a

'black list' of reluctant tax havens, including Austria, Switzerland and the Principality of Liechtenstein, and shall ensure that German entrepreneurs investing in countries deemed to be non-cooperative tax havens will face drastic fiscal disadvantages if they fail to cooperate with the German tax authorities. According to the provisions of the new draft law, German tax authorities are free to assess overdue taxes, the regulations concerning the withholding tax shall not apply and, moreover, the deduction of income-related expenses can be denied. In any case, the present version of the new draft law on tax evasion provides for an obligation to cooperate that is far beyond the OECD standards, as an automatic exchange of information will be required.

Repatriation of assets

In view of the international erosion of banking secrecy, the question arises as to whether there are legal risks associated with undeclared investments in savings of income in Austria, Switzerland and Liechtenstein. With the adoption of the OECD standard on administrative assistance in tax matters these countries will exchange information with other governments in individual cases where 'a specific and justified request has been made' for any form of tax offence. Currently, these countries are renegotiating existing bilateral treaties, and requests from other governments made according to the standard will be honoured once new treaties come into effect. At present, it is unclear whether Swiss or Austrian banks will have to provide administrative assistance in fiscal matters retrospectively. Besides the possibility of making a corrected return that may lead to immunity, savers in exceptional cases are well advised to repatriate their foreign investments. ■