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Since its inception, the FATF has operated under a fixed lifespan, requiring a specific decision by its ministers to continue. The current mandate of the FATF (2012-2020) was adopted at a ministerial meeting in April 2012.

The FATF currently comprises 34 Member jurisdictions and two regional organisations, representing most major financial centres in all parts of the globe.

The objectives of the FATF are to set standards and promote effective implementation of legal, regulatory and operational measures for combating money laundering, terrorist financing and other related threats to the integrity of the international financial system. The FATF is therefore a policy-making body, which works to generate the necessary political will to bring about national legislative and regulatory reforms in these areas.

In addition, the FATF has developed a series of recommendations that are recognised as the international standard for combating of money laundering and the financing of terrorism and proliferation of weapons of mass destruction. They form the basis for a coordinated response to these threats to the integrity of the financial system and help ensure a level playing field. First issued in 1990, the FATF Recommendations were revised in 1996, 2001, 2003 and most recently, in 2012 to ensure that they remain up to date and relevant, and are intended to be of universal application; this revision is intended to strengthen global safeguards and further protect the integrity of the financial system by providing governments with stronger tools to take action against financial crime. They have been expanded to deal with new threats, such as the financing of proliferation of weapons of mass destruction and to be clearer on transparency and tougher on corruption.

The FATF also monitors the progress of its members in implementing necessary measures, reviews money laundering and terrorist financing techniques and counter-measures, and promotes the adoption and implementation of appropriate measures globally. In collaboration with other international stakeholders, the FATF works to identify national-level vulnerabilities with the aim of protecting the international financial system from misuse.

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Joint statement on the tax dispute between Switzerland and the United States: better to make a painful break than to draw out the agony

Background

In August last year, Switzerland and the United States signed a joint statement to settle a long-lasting dispute between the Swiss banks and US authorities. The dispute can be traced back to 2008 when UBS and other Swiss banks' offshore businesses were accused of assisting US clients to avoid taxes. UBS entered into a deferred prosecution agreement (DPA) with the United States Department of Justice Tax Division (DOJ) and the United States Attorney's Office for the Southern District of Florida. Under this agreement, UBS was, inter alia, forced to pay a fine for the total amount of $780m and to restructure its cross-border business. At the same time, the Swiss Financial Market Supervisory Authority (FINMA) permitted the transfer of client data to the US Internal Revenue Service (IRS) by applying emergency law.

Unfortunately, the Swiss government has not been able to settle the dispute quickly on the alleged conspiracy to defraud the IRS on behalf of all Swiss banks because of Swiss banking secrecy.

The Swiss Banking Act renders a breach of bank confidentiality a crime ('Swiss Banking Secrecy') and, inter alia, states: 'whoever discloses a secret entrusted to him in his capacity as officer, employee, agent, liquidator or commissioner of the bank, as representative of FINMA, officer or employee of a recognized auditor, or who has become aware of such secret in this capacity, and whoever tries to induce others to violate professional secrecy, shall be punished by a prison term not to exceed three years or by a fine'.

Swiss Banking Secrecy, in essence, reinforces privacy and contractual confidentiality obligations of the bank vis-à-vis its customer. Accordingly, Swiss Banking Secrecy encompasses information provided to the bank either by a prospective customer, customer and former customer. The Swiss Banking Act expressly reserves federal and cantonal provisions on the duty to testify or disclose information to public authorities in connection with civil, administrative and criminal proceedings. For all these proceedings, federal and cantonal laws have developed relatively complex and detailed standards as to if and what a bank is held to disclose. Most importantly, Swiss Banking Secrecy does not hinder the Swiss authorities from producing bank documents for the requesting foreign authorities provided that the preconditions to grant mutual judicial assistance are fulfilled. Should a Swiss bank deliver client data to foreign tax authorities outside of a mutual judicial assistance proceeding, it would breach Swiss Banking Secrecy and therefore, the bank would commit a criminal offence.

The joint statement

The joint statement signed by the Swiss and US authorities on 29 August 2013 now provides for a programme (the 'Programme') under which each Swiss bank may individually settle the tax dispute with the US authorities. The Programme classifies Swiss banks into four categories:

Category 1

Swiss banks already subject to criminal investigations as of the date of the Programme: about 12 Swiss banks. It is intended that these banks will enter into a DPA similar to the one entered into by UBS. As a consequence, these banks will have to deliver certain information, excluding client names, and pay a fine to the US authorities. As the first of these banks, Credit Suisse has entered into an agreement with the United Stated District Court for the Eastern District of Virginia, under which Credit Suisse pleaded guilty to aiding tax avoidance and agreed to pay a penalty in the amount of $2.8bn.

Category 2

Swiss banks against which the DOJ has not yet initiated criminal investigations but have reasons to believe that they have infringed US tax law while dealing with US clients. Each Category 2 bank will enter into a non-prosecution agreement (NPA) with the DOJ and will have to describe its cross-border business and provide data on clients having left the bank after August 2008. In addition, these banks will have to pay a penalty, as described in more detail below. At this stage we cannot exclude the possibility that the DOJ will request Category 2 banks to plead guilty in the NPA as well.

Category 3

Swiss banks in this category have no reason to believe that they have violated US tax law while dealing with US clients. These banks will also have to deliver certain client data, again, on anonymised bases, but are not subject to a fine.

Category 4

Swiss Banks in this category execute local business only, and only have to certify their local status. These banks are not subject to a fine either.

Most Swiss banks, which are not already subject to criminal investigations of the DOJ are assumed to belong to Category 2 and have requested the DOJ to enter into a NPA prior to 31 December 2013 which is the deadline set under the Programme. Category 2 banks will not be subject to criminal investigations, but will be subject to a penalty proportional to assets credited to US related accounts held by the bank during a certain time period. The amount of the penalty is not related to

the misbehaviour or guilt of the bank. For instance, a bank that has accepted a new client after February 2009 will be subject to a penalty of 50 per cent of the maximum amount of assets credited to the account between the opening date of the account and the date of entering into the NPA. The determination of the maximum amount of the aggregated US related accounts may be reduced by the value of each account to which the Swiss bank can demonstrate that such an account was not an undeclared account, was disclosed by the Swiss bank to the IRS or was disclosed to the IRS through a voluntary disclosure program or initiative following notification by the Swiss bank of such a program or initiative and prior to the execution of the NPA.

Extensive investigations by each Swiss bank

Each Category 2 bank has to apply the indicia under the US Foreign Account Tax Compliance Act (FATCA) to determine whether an account qualifies as a US related account under the Programme. Each bank requesting an NPA has to provide the DOJ with information, inter alia, on the structure of its cross-border business for US related accounts, in addition to the names and functions of individuals who structured, operated or supervised the cross-border business. We understand that this information will have been submitted to the DOJ at the end of June 2014 at the latest, provided that the respective bank has applied for an extension under the Programme. Upon execution of an NPA, the respective Swiss bank will have to provide detailed information on US related accounts that were closed after 1 August 2008, known as the leaver list. It is noteworthy, that the leaver list will not include the names of the account holders. The production of information under the leaver list shall be compliant with Swiss Banking Secrecy as described above.

Obviously, the internal investigations of the Category 2 banks and the production of information are extremely time-consuming and tie up extensive internal and external manpower.

From a Swiss tax law perspective, it is disputed whether the penalty applicable on Category 2 banks will be a justified business expense and therefore, be deductible.

Penalty to be deductible under Swiss tax law

According to general principles of Swiss tax law, justified business expenses are deductible for corporate income tax purposes. The penalty under the Programme is directly linked to the bank's business as it reflects the core purpose of a bank to accept and manage client's assets. Swiss banks do not participate in the Programme voluntarily but have been requested by both the Swiss government and FINMA to do so in order to settle the long-lasting tax dispute with the US for the benefit of the entire Swiss financial centre. As mentioned above, the amount of the penalty applicable for Category 2 banks will be calculated based on the assets credited to US related accounts. The penalty does not depend on any negligence or guilt of a bank.

Therefore, there is no doubt that the penalty to be paid by each Category 2 bank under the Programme qualifies as a justified business expense of each bank. It is not upon the tax authorities to judge whether any expense would be immoral or not. Swiss tax law is neutral in disregard. Consequently it is our understanding that the tax authorities may not distinguish between (deductible) moral business expenses and (non-deductible) immoral business expenses.

As an exemption to the above-mentioned rule, the Swiss Federal Act on Direct Taxes and the Swiss Federal Act on the Harmonisation of Cantonal and Municipal Direct Taxes both state that tax penalties (*Steuerbussen*), in addition to bribery money, are not deductible as business expenses for corporate income tax purposes. As a consequence, it crucial whether the penalty paid under the Programme qualifies as a *tax penalty* or not.

In our opinion, a payment may only qualify as a tax penalty if the amount of the penalty or fine relates to the misconduct and guilt of the person or entity subject to the respective tax. Therefore, this would, in principle, not be true for a penalty of a Category 2 bank as these banks will be subject to a penalty regardless of any fault or guilt. The Programme rather sanctions the refusal to provide full information on US related accounts by the Swiss banks due to Swiss Banking Secrecy. Swiss banks are obliged to comply with Swiss Banking Secrecy and may only deliver client names provided that the procedures and conditions under the judicial assistance are complied with.