

Administrative Assistance in Tax Matters – Present and Future Challenges for Switzerland

BY SIMONE NADELHOFER | NATER DALLAFIOR

On August 19, 2009, Swiss bank UBS and the Internal Revenue Service (IRS) signed a settlement agreement regarding the pending IRS/UBS case, thus putting an end to one of the biggest cross-border tax disputes in history. According to a parallel agreement between the US and Switzerland, the IRS will submit a request for administrative assistance based on the existing US-Swiss Double Taxation Treaty, seeking information relating to certain UBS accounts of US persons. It is expected that approximately 4,450 accounts will be provided to the IRS in response to this request.

This contribution describes the main features of administrative assistance proceedings based on tax treaties from a Swiss perspective.

Legal Instruments for the International Exchange of Information in case of Tax Offences

In its international relations, Switzerland has two ways of exchanging information in case of tax offences.

The information exchange can take place between justice authorities within the framework of mutual legal assistance proceedings in criminal matters. Or information can be exchanged between tax authorities by way of mutual administrative assistance on the basis of bilateral double taxation treaties (DTT), as will be the case in the UBS/IRS deal.

For the foreign state, a request based on a DTT has a clear advantage over mutual legal assistance in criminal matters: due to the so-called principle of specialty, information on tax offences transmitted via mutual legal assistance may only be used for criminal tax proceedings. As opposed thereto, information obtained through mutual administrative assistance may also be used by the foreign tax authorities for the administrative taxation procedure giving rise to the criminal tax proceedings.

Principle of Double Criminality

Most of the DTTs signed by Switzerland are based on the OECD Model Tax Convention on Income and on Capital, which provides for the exchange of information between contracting States in its article 26. Years ago, Switzerland made a strict reservation on this provision. However, the reservation was relaxed in 2005, such as to allow for the exchange of information in cases of tax fraud subject to imprisonment as defined by both contracting States. This is what we call the principle of double criminality.

This rule has important consequences in the framework of tax offences under Swiss law, since a distinction is made between tax evasion and tax/duty fraud. Traditionally, Switzerland grants assistance in tax matters only when the foreign procedure involves elements of an offence tantamount to tax/duty fraud in Switzerland. Pursuant to Swiss law, duty and tax fraud are misdemeanors and involve the use of willful deceit for the purpose of evading taxation (duty fraud) or the use of false or falsified documents or documents with untrue content such as account books, balance sheets, profit and loss statements, or wage statements and other certifications by third parties (tax fraud). It is important to note that a tax return is not itself considered a “document”.

As opposed thereto and in light of the lesser gravity of tax evasion from a Swiss point a least, all forms of mutual legal and administrative assistance are excluded in case of tax evasion. This corresponds to the fact that under

domestic law, tax evasion is prosecuted by the cantonal administrative authorities without application of coercive measures and without lifting of bank secrecy. Tax evasion occurs when a taxpayer willfully or negligently fails to submit a tax return or submits an incomplete tax return, so that an assessment is improperly omitted or a final assessment is incomplete.

Exception: Serious Tax Offences are also Covered in Case of DTT Requests from the US

According to the DTT in force between the US and Switzerland, the term “tax fraud or the like” is not restricted to conventional forms of fraud involving falsified documents or schemes of lies. Information may also be obtained with regard to serious tax offences, specifically the continued evasion of large sums of tax. Under the applicable DTT between the two states and in light of the latest practice of the Swiss Federal Administrative Court in relation with UBS accounts held by offshore corporations controlled by US-persons, account information may also be released even if the IRS does not yet know the name of the bank client concerned when it submits its request (fishing expedition).

Procedure to be followed in case of DTT requests

Mutual administrative assistance in tax matters is the responsibility of the Swiss Federal Tax Administration (SFTA). Based on a request from a foreign tax authority pursuant to a DTT, the SFTA will make a preliminary review of the request. If sufficient probable cause has been shown for the suspicion of tax or duty fraud or, in the case of the US, of serious tax offences, the SFTA gathers the necessary information to be transmitted to the foreign state. It may order coercive measures such as seizure of records by the police. Bank secrecy is lifted in such cases.

The affected party has the possibility of contesting the decree issued by the FTA concerning the information to be transmitted to the foreign authority by filing an appeal with the Swiss Federal Administrative Court. The Court renders a final decision on the permissibility and scope of the information to be transmitted. The decision may not be appealed to the Federal Supreme Court.

Administrative Assistance in Tax Matters in the Future

On 13 March 2009, the Swiss Government offered to adopt the OECD standard on administrative assistance in tax matters (article 26 OECD Model Tax Convention) within the framework of DTTs. The decision followed pressure on Switzerland from other OECD member countries to ease its strict banking secrecy laws. According thereto, the distinction between tax evasion and tax fraud will be abolished in cases of assistance sought under a DTT. In return, Switzerland will seek to enforce stricter requirements to avoid fishing expeditions, e.g., the requirement to identify the name of the taxpayer will certainly be one of the key requirements.

However, the distinction between tax fraud and tax evasion will remain so long as the existing treaties have not been renegotiated, and notwithstanding, it will cover only facts occurring after the revised DTT enters into force.

Up to now Switzerland has signed 11 amended DTT (Denmark, Luxembourg, France, Norway, Austria, Britain, Mexico, Finland, Faeroe Islands, Spain and USA) and negotiated new treaties with other countries.

Simone Nadelhofer is an Attorney at Law in Zurich.



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