ATTORNEYS AT LAW

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# Newsletter


**Authors:**
Peter Burckhardt
Andreas Hösli

WHITE-COLLAR CRIME AND COMPLIANCE

## Exposure to new risks of criminal liability due to the implementation of the FATF Recommendations

The Federal Act on the Implementation of the Revised FATF Recommendations will enter into force in two stages on 1 July 2015 and 1 January 2016. The new rules substantially tighten the Swiss framework for combatting money laundering, and extend beyond the financial services industry. This exposes financial intermediaries and dealers to new risks of criminal liability.

### 1 INTRODUCTION

The implementation of the 2012 Recommendations of the *Financial Action Task Force* (**FATF**) entails extensive changes to several federal acts, in particular the Anti Money Laundering Act (**AMLA**), the Criminal Code (**CC**) and the Code of Obligations (**CO**). This newsletter offers an overview over the most relevant developments from a money laundering perspective, shows some practical approaches for implementation and points out the major risks of criminal liability.

### 2 THE FATF RECOMMENDATIONS

#### 2.1 BACKGROUND

The **FATF** is an intergovernmental organization that was founded in 1989 by the G7 states. It is seated at the OECD in Paris. Besides Switzerland, which is a founding member, 33 more states – including the most important financial hubs – as well as two regional organizations are members of the FATF.

The objectives of the FATF consist in defending the integrity of the financial system and in unifying the different national rules. To this end, the FATF adopted **40 Recommendations** in 1990, which have since been acknowledged as the international standard in the fight against money laundering and financing of terrorism. After several changes, the Recommendations were last revised in 2012.

#### 2.2 IMPLEMENTATION BY SWITZERLAND

The FATF regularly monitors the implementation of its Recommendations in member countries by conducting **mutual evaluations**. Following its last evaluation in 2005,

Switzerland will be evaluated again in the spring of 2016. As a global financial hub, Switzerland is under significant pressure to adapt its legal framework to the FATF Recommendations. After a long and difficult political process, the Swiss Federal Assembly (parliament) adopted the Federal Act on the Implementation of the Revised FATF Recommendations on 12 December 2014.

Changes will ensue in the following **seven areas**: (1) improvement of transparency regarding legal entities, in particular with respect to bearer shares, (2) tightening of duties of financial intermediaries with regard to the identification of the beneficial owner of legal entities, (3) broadening of the definition of politically exposed persons (PEP) to include domestic PEP as well as PEP of intergovernmental agencies, (4) qualification of serious tax crimes as predicate offences to money laundering, (5) duties of care in connection with cash payments in sales transactions, (6) increase of the effectiveness of the system of suspicious activity reporting of the Money Laundering Reporting Office (MROS) as well as (7) implementation of the FATF Recommendations regarding sanctions in the area of financing of terrorism.

The Swiss Federal Council (government) has opted to **enact** the relevant measures in **two stages**. Changes to the CO, the Collective Investment Schemes Act (CISA) and the Federal Intermediated Securities Act (FISA) will come into effect on **1 July 2015**. The remainder of the changes, in particular the changes to the CC regarding the laundering of proceeds from serious tax crimes as well as changes to the AMLA, will enter into force on **1 January 2016**. With effect from the same date, the revised FINMA Anti Money Laundering Ordinance (**AMLO-FINMA**) and the revised Agreement on the Swiss Bank's Code of Conduct (**CDB**) are expected to enter into force.

## 3 MORE COMPREHENSIVE DUTIES OF CARE FOR FINANCIAL INTERMEDIARIES

### 3.1 NEW FRAMEWORK

The new legal framework imposes a general **obligation** for financial intermediaries **to identify the beneficial owner** (art. 4 AMLA). This duty is no longer limited to cases in which there is doubt that the latter is identical with the contracting party.

The term of **financial intermediary** is defined broadly, to include, *inter alia*, banks, fiduciaries as well as investment advisors and asset managers (cf. art. 2 para. 2 and 3 AMLA).

A new and significant result of the application of the new framework is that the duty to establish the identity of the beneficial owner now extends to **active business entities** (art. 4 para. 2(b) AMLA). The revised Act defines the beneficial owner of an active business entity as the individual who, directly or indirectly, controls the entity, either by holding, alone or in concert with third parties, **25 percent** of the capital or voting rights in the entity, or by other means (art. 2a para. 3 AMLA). As of 1 July 2015, **companies** must prepare a **register** of the beneficial owners reported to them (art. 679l CO).

These duties to establish beneficial ownership are not applicable to **listed companies** and to subsidiaries majority-owned by such companies (art. 4 para. 1 AMLA).

### 3.2 PRACTICAL IMPLEMENTATION

According to the explanatory notes accompanying the Implementation Act, financial intermediaries are free to use **Form A** in all business relations; however, this is not mandated by the new framework. If the financial intermediary is certain that the contracting party is identical with the beneficial owner, it can confine itself to **document** this, for example in the account-opening documents (art. 4 para. 2(a) and art. 7 AMLA).

> "Beneficial ownership must now be established even when dealing with active business entities."

## 4 SERIOUS TAX OFFENCES AS PREDICATE OFFENCES TO MONEY LAUNDERING

### 4.1 NEW CONCEPT OF THE LEGISLATOR

In the 2012 revision of its Recommendations, the FATF determined that **serious tax crimes** related to direct as well as indirect taxes should be considered predicate offences to money laundering. Thus, in Switzerland, as of 1 January 2016, not only felonies (*i.e.* offences carrying a custodial sentence of more than three years), but also **"qualified tax offences"** will qualify as predicate offences to money laundering (art. 305$^{bis}$ para. 1 CC).

The term "qualified tax offences" includes **tax fraud** committed against the Confederation as well as Cantons and municipalities with regard to direct taxes according to art. 186 of the Federal Income Taxation Act (FITA) or art. 59 para. 1 first lemma of the Communal and Cantonal Income Tax Harmonization Act (CCITHA), if the amount of tax evaded exceeds **CHF 300,000** per tax period (art. 305$^{bis}$ para. 1$^{bis}$ CC). This includes, in particular, offences in the areas of income and wealth tax for individuals, profit and capital tax for legal entities as well as real property gains tax, while excluding cantonal estate and gift taxes.

Whoever, for the purpose of tax evasion and with fraudulent intent, submits forged, falsified or substantially incorrect **documents** with augmented evidentiary value (such as business records, balance sheets or salary certificates; art. 186 para. 1 FITA, art. 59 para. 1 CCITHA), is considered to commit tax fraud.

In the area of **indirect taxes** (such as VAT, tax on tobacco or customs duties), art. 14 para. 4 Criminal Administrative Law Act (CALA), which has been a felony and a predicate offence to money laundering since 1 February 2009, has been slightly amended and is now no longer limited to customs contraband.

### 4.2 CRIMINAL LIABILITY EXTENDING TO TAX OFFENCES COMMITTED ABROAD

The person who commits a qualified tax offence **abroad** shall be punished in Switzerland if the offence committed is punishable abroad according to the principle of double incrimination (art. 305$^{bis}$ para. 3 CC). In particular, this means that tax offences committed to the detriment of **foreign tax authorities** also qualify as predicate offences to money laundering in Switzerland if (in the case of evasion of direct taxes) the tax evaded exceeds CHF 300,000 per tax period and if the act is also punishable in the foreign state where the offence was committed. In order for the requirement of

double incrimination to be met, the relevant tax offence needs to qualify as tax fraud from a Swiss point of view (which should not be construed too strictly) and "mere" tax evasion needs to be considered a criminal offence abroad.

"Serious tax crimes committed abroad may constitute predicate offences to money laundering."

### 4.3 PRACTICAL IMPLEMENTATION

In the future, financial intermediaries will need to review their clients' tax compliance with regard to the assets managed, in addition to complying with existing duties of clarification under the AMLA. The review to be undertaken is dictated by a **risk-based analysis** of certain relevant indicators.

For example, the use of complex offshore structures that are difficult to comprehend or a lack of identity between the account holder and the beneficial owner which cannot be plausibly explained would be indicative of **increased risk**. On the other hand, certain factors, such as self-declaration by the client or the fact that there is an information exchange treaty in place between the client's state of residence or incorporation and Switzerland, may indicate lower risk. If there is cause to suspect a lack of tax compliance, **further investigative measures** must be taken.

In its explanatory notes, the Swiss Federal Council details that the laundering of proceeds from serious tax crimes does not lead to the contamination of a taxpayer's entire assets. Contamination is only assumed in the **amount of the tax actually evaded** in the individual case. However, this amount will often be an abstract pecuniary advantage which cannot be allocated to a particular account of the client for lack of a paper trail. In practice, this will often beg the question of which assets should be reported to MROS and finally blocked. In light of this, a certain link between the tax savings in question and the contaminated assets should be made a requirement.

### 4.4 NO RETROACTIVITY

According to the relevant transitional provision, the new framework outlined above does not **apply retroactively**. This means that serious tax offences committed before 1 January 2016 do not qualify as predicate offences to money laundering.

However, acts committed before 1 January 2016 may be punishable abroad. Foreign law may, in particular, declare punishable acts of aiding and abetting taxpayers in committing tax crimes.

## 5 CASH PAYMENTS EXCEEDING CHF 100,000

The issue of cash payments was one that evoked an **extremely controversial debate** in parliament, which could only reach agreement after several rounds of debates and a conciliation conference. This debate is to be seen against the backdrop of today's tendency to view large cash payments in sales transactions as unusual and, from a money laundering point of view, as potentially suspicious.

Parliament refused the original proposition of a total ban on cash payments exceeding CHF 100,000. Instead, it opted to implement new duties of care for **dealers** taking receipt of more than CHF 100,000 in cash. These duties involve identifying the contracting party as well as the beneficial owner and drawing up appropriate documentation (art. 8a para. 1 AMLA). Moreover, the background and goal of a transaction must be identified if the transaction seems unusual or if there is reason to believe that the assets involved may stem from a felony or qualified tax offence or be at the disposal of a criminal organization (art. 8a para. 2 AMLA).

This new rule does not explicitly subject whole industries to the money laundering framework, but instead focuses on the legal transaction. The Act defines dealers as individuals or legal entities who deal professionally in goods and in the course of these activities receive cash payments (art. 2 para. 1(b) AMLA). Professions the legislator had in mind when drafting this provision included **real estate agents, art dealers, luxury car dealers** or **jewelers**.

"Internal compliance procedures must be adapted to minimize the risk of incurring criminal liability."

Dealers may free themselves of these duties of care by using a **financial intermediary** for payments exceeding CHF 100,000 (art. 8a para. 4 AMLA).

## 6 RISK OF CRIMINAL LIABILITY

If the financial intermediary (for example, the bank employee responsible or the bank itself due to a lack of organization according to art. 102 para. 2 CC) or the dealer has cause to suspect that means of cash payment derive from a felony or a qualified tax offence, this must be **reported** to MROS immediately (art. 9 AMLA). If it fails to do so, the financial intermediary or dealer may, in addition to a fine according to art. 37 AMLA, incur criminal liability pursuant to art. 305$^{bis}$ CC.

Under the revised money laundering framework, the financial intermediary (or dealer) is **not** always obliged to **immediately** block assets connected to transactions reported to MROS. Instead, as a general rule, blocking ensues only after MROS informs the intermediary that it will process the report on to the competent criminal prosecution authorities (art. 10 AMLA).

Financial intermediaries and dealers who do not sufficiently comply with their duties under AMLA risk incurring criminal liability pursuant to art. 305$^{bis}$ CC, which also entails a risk of confiscation of the contaminated assets (art. 70 CC).

Financial intermediaries may additionally be exposed to regulatory sanctions as well as prosecution for insufficient diligence in financial transactions pursuant to art. 305$^{ter}$ CC (the latter likely applies to dealers as well).

## 7 CONCLUSION

The (partial) subjection to AMLA is entirely new to **dealers**. Barring a willingness to completely dispense with cash transactions exceeding CHF 100,000 in the future, they must comply with requirements that were, to date, imposed only on financial intermediaries. **Financial intermediaries in a traditional sense**, in turn, must adapt their internal

compliance procedures to comply with new, more comprehensive duties of care, if they wish to minimize risks of criminal liability. In particular, the introduction of serious tax crimes as predicate offences to money laundering constitutes a shift in paradigm. The challenging task of implementing compliance with the new duties of care is not made easier by the fact that there is still substantial uncertainty and controversy on a number of pivotal issues. Therefore, financial intermediaries are well advised to err on the side of caution until these questions have been decided by the courts.

## Contacts

The content of this Newsletter does not constitute legal or tax advice and may not be relied upon as such. Should you seek advice with regard to your specific circumstances, please contact your Schellenberg Wittmer liaison or any of the following persons:


In Zurich:

Peter Burckhardt

Partner
peter.burckhardt@swlegal.ch

Andreas Hösli

Rechtsanwalt
andreas.hoesli@swlegal.ch

In Geneva:

Paul Gully-Hart

Partner
paul.gully-hart@swlegal.ch

Benjamin Borsodi

Partner
benjamin.borsodi@swlegal.ch



**SCHELLENBERG WITTMER LTD / Attorneys at Law**

ZURICH / Löwenstrasse 19 / P. O. Box 1876 / 8021 Zurich / Switzerland / T +41 44 215 5252

GENEVA / 15bis, rue des Alpes / P. O. Box 2088 / 1211 Geneva 1 / Switzerland / T +41 22 707 8000

SINGAPORE / Schellenberg Wittmer Pte Ltd / 6 Battery Road, #37-02 / Singapore 049909 / www.swlegal.sg

www.swlegal.ch


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