Tax crimes and money laundering ï a new focal point for FATF

by Lorenzo CROCE

Having already been significantly threatened by the inclusion of article 26 OECD Model Tax Convention in the new Double Imposition Conventions negotiated by Switzerland and the disclosure of 4000 UBS client names to the American Internal Revenue, Swiss banking secrecy is at risk of becoming eternally dead and buried in the next few months following a staggering new proposition from the Financial Action Task Force (FATF).

The FATF has just established a preliminary-draft in order to qualify tax crimes as predicate offences for money laundering. In short, if such a proposition should come about, this would mean that any person who has accepted a deposit, helped to transfer or manage funds in the knowledge or on the presumption that these funds were the result of tax offences, risks being prosecuted for money laundering in accordance with article 305 of the Swiss Penal Code. As for the financial intermediaries, they will be obligated to systematically declare suspected tax offences to the Money Laundering Reporting Office Switzerland (MROS).

Even though a formal decision has not yet been made, there is every reason to believe that this proposition will be adopted at the FATF plenary assembly at the end of 2011 within the scope of a partial revision of its standards. In light of the financial crisis, there is mounting international pressure, notably from the G20 countries. However, it must be stressed that this proposition is not aimed at combating organised crime. It is nothing other than a simple pretext. Under the pretext of fighting against money laundering, the true aim is a recovery of state funds by transforming the banks and other financial intermediaries into foreign tax officers. Therefore, no more need to pay out millions to buy CDs of stolen data!

However, this criminalisation of the economic world is neither desirable nor justified. One could admit that the channels worked for laundering capital are consistently the same as those used to try to conceal money from Inland Revenue, but the similarities between tax offences and money laundering stop there.

Money laundering involves reintroducing criminal money into the economic cycle through processes which aim to cover the source of the money.

Yet, as regards concealed funds from the Inland Revenue, these clearly have legal origins (revenue, wealth, succession, donation etc.). It is not a question of concealing illegal patrimonial values by imparting an apparent legal justification upon them, but rather avoiding the control by tax authorities of funds which have a legal source. It therefore appears doubtful that money resulting from tax offences could then be laundered.

Furthermore, in Switzerland only crimes, that is offences punishable with a prison sentence of more than three years, are likely to constitute predicate offences for money laundering. As a result, if the proposition made by FATF does indeed materialise, it would be necessary to establish tax offences in crime. Yet the seriousness of these offences, particularly tax evasion, is not comparable to that of other crimes connected to laundering. It is disproportionate to place money laundering resulting from tax offences on the same footing as laundering resulting from drug trafficking, terrorism or prostitution.

Whatever it may be, the implementation of this proposition runs the risk of creating significant difficulties.

First of all, it will be necessary to determine what is included under the term "tax offences". In this respect, FATF has voluntarily refrained from elaborating on this notion - aside from the fact that it targets both direct and indirect taxes - leaving each country to decide for themselves what is to be understood by this term in relation to their domestic law. So what will Switzerland decide? Will it establish limited amounts or will it enact a catalogue of crimes? Will tax evasion be part of this and if necessary, where will the line be drawn between tax planning, legal practice and evasion? According to the Ambassador Alexandre Karrer, who is in charge of the Swiss case within FATF, "tax crimes must implicitly be reserved to significant offences such as a falsification of accounts or the embezzlement of money". However, it remains doubtful that Switzerland will resist international pressure and it is possible that tax evasion will be considered as a predicate offence for money laundering.

The adoption of the new regulation will also pose problems in terms of investigations. In a practical sense, how can financial intermediaries ensure that the funds received from their client have been declared to the Inland Revenue? Will it be necessary for the client to sign a standard form or will they have to

request a declaration certificate from the foreign tax authorities knowing that tax declarations are generally not granted until several years after the acquisition of revenue? Similarly, how can financial intermediaries lead the necessary investigation on funds which have been transferred from generation to generation?

There are so many questions which remain unanswered.

On an organisational plan, it will be, under all circumstances, necessary to hire and train a significant number of collaborators both at the level of the authorities and the financial intermediaries. This measure will lead to considerable supplementary costs which will be directly passed onto the client. This in turn runs the risk of eroding the competitive Swiss financial position as, unlike certain countries, Switzerland wants to be seen as performing well and there is no doubt whatsoever, that it will rigorously implement this new regulation.

We have seen that it is neither justified nor desirable to subject tax offences to articles 305^{bis} and 305^{ter} of the Swiss Penal Code as well as to the Swiss Federal Law concerning the fight against money laundering and terrorist financing in the financial sector. The new FATF proposition is solely aimed at allowing the acquisition of funds by the foreign tax authorities and not the fight against organised crime. What is even worse is the significant risk of weakening the system because of the tidal wave of communications to MROS which will probably happen. Furthermore, beyond the generated costs, this proposition is extremely complicated to implement, particularly for the financial intermediaries who solely have access to limited investigative means to exert their due diligence.

Ultimately, there are other effective solutions to actively fight against tax fraud. Indeed, Switzerland has already undertaken such measures by providing assistance, not only in cases of fraud but also in cases of tax evasion. Furthermore, the setting up of a discharge tax at the outset ("Rubik" project) is currently under discussion with Germany and England and would allow a definitive resolution of the problem while safeguarding the Swiss banking secrecy. It is therefore necessary to take advantage of this approach rather than abusively using the system of fighting against money laundering and the financing of terrorism.