

# Exchange of Information in Tax Matters between Switzerland and India or 'Do the Tax Authorities Hold the Key to Swiss Bank Accounts'?

India and Switzerland recently signed a protocol to the existing double tax treaty that allows for the exchange of information on tax evaders between the two countries, considered a must for obtaining details on unaccounted funds kept by Indians in Swiss banks. The present contribution aims at providing an overview of the new rules and the conditions to be met for an exchange of information from a Swiss perspective.

**'Banking** secrecy remains intact.' These were the often quoted words of the Swiss Finance Minister in the spring of 2009 following the handover of the names and account information of hundreds of US taxpayers holding secret accounts with UBS in Switzerland. Since then, the Swiss banking secrecy system has been under steady and increasing international pressure to soften its standards for the exchange of information in tax matters. At the same time, court proceedings have been filed abroad against holders of Swiss accounts based on data stolen by former employees of Swiss banks. The tax probes started by the Indian Government to track undisclosed overseas accounts allegedly held by almost 700 Indian citizens with the Swiss branch of HSBC are a well-known example. The Indian Government received such information, which included account numbers, names and addresses as given in the passports of the account holders, from the French Government which in turn received it from a former HSBC employee.

These recent developments have reshaped the Swiss banking secrecy system and given rise to several legislative changes, implementing Switzerland's new policy towards exchange of information in tax matters.

In March 2009, Switzerland adopted the OECD standard on the exchange of information, as set out in the OECD Model Tax Convention, and withdrew its reservation to Article 26. The OECD Model Tax Convention provides, inter alia, for a system of administrative assistance among tax authorities of the signatory countries. It does not apply to individual cases but is merely a model text that can be used as a basis for double tax agreements ('DTA') as negotiated and signed by the relevant countries.

Since March 2009, Switzerland (re-)negotiated more than 40 DTAs with administrative assistance clauses in accordance with internationally applicable standards. It is in this context that Switzerland and India on August 30th, 2010 signed a protocol to amend their existing DTA ('CH-IN DTA').

Indian News Agencies commented widely on this development, highlighting new possibilities for obtaining information on bank accounts of Indian citizens or corporations in Switzerland. The development came at a time when the Indian Government was under increasing pressure from opposition parties and the Indian Supreme Court to reveal the names of individuals with black money overseas. Data from the Swiss National Bank

shows that the total deposits of Indian individuals and companies in Swiss banks stood at about USD 2.5 billion at the end of 2010.

The present contribution aims at providing an overview of the main changes shaping administrative assistance proceedings triggered by a request for information from Indian tax authorities in Switzerland under the new rules.

### Background Information

The amended CH-IN DTA came into force on 7 October 2011. Based on the new rules, Switzerland shall not only provide information to India in cases of serious crimes (such as fraud, money laundering, corruption, etc.) in the course of mutual legal assistance proceedings in criminal matters, but also in cases of simple tax evasion under the CH-IN DTA. This includes, e.g., cases where taxpayers merely omit to declare funds ultimately held on a Swiss bank account or where the exchange of information is foreseeably relevant for taxation in India. The former requirement that the offender had used false documents or particular structures aiming at hiding the real beneficial owner is no longer valid.

### Administrative Assistance Procedure

#### Letter of Request

Switzerland does not automatically disclose information about Swiss accounts but will only consider a request if the Swiss Federal Tax Administration (the 'SFTA') receives a letter of request from the 'Central Government in the Department of Revenue' in India, which is the Ministry of Finance of India (the 'MFI').

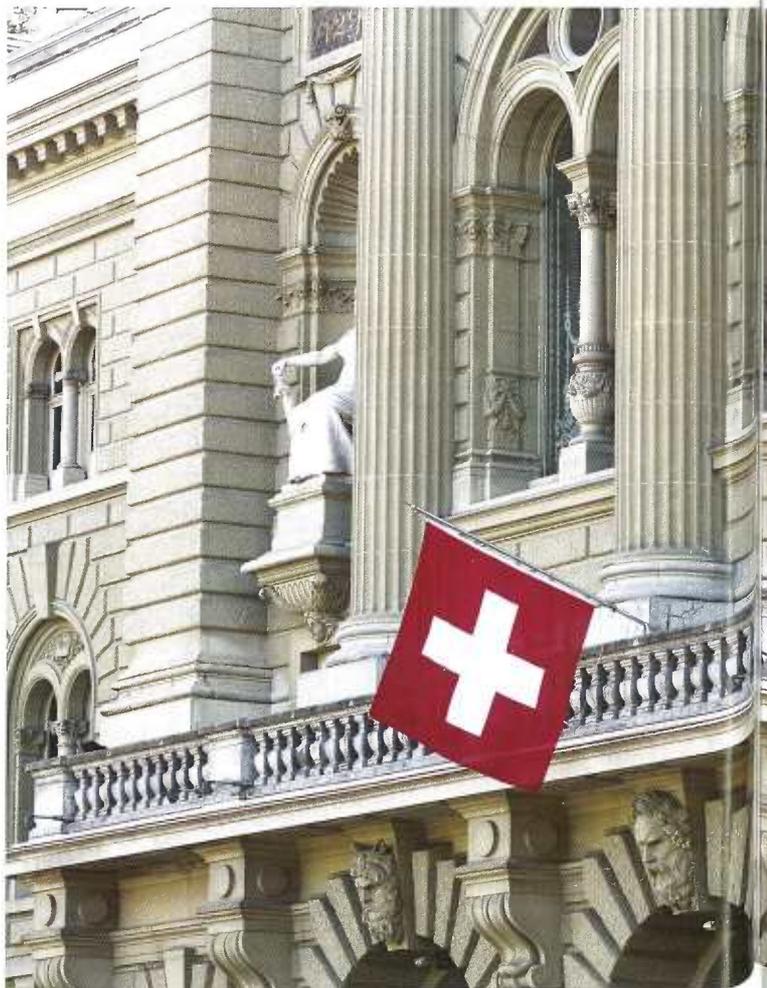
For the request to be admitted, the following conditions must be met:

1. The person/entity targeted by the request must be identified; such identification may be provided by other means than by indicating the name and address of the person concerned, e.g., by indicating an account number. Furthermore, since recently and under certain conditions, 'group requests' are admissible (see the Group Requests section below).
2. The information holder, i.e., any person believed to be in possession of the requested information (e.g., banks, trustees, fiduciaries, company directors etc.), is to be identified in the request to the extent possible.
3. Tax investigations must be under way in India and the requested information must be sought for the purpose of such tax investigation.

4. The investigation must concern the Indian income tax (including any surcharge thereon) according to article 2 of the DTA. No information may be requested by India from Switzerland in relation to other taxes, e.g., the Indian wealth tax or VAT. By contrast, capital gains tax is deemed to be income tax, and, hence, is covered by the DTA.
5. The requested information must be 'foreseeably relevant' to the Indian tax administration and the recovery of income tax. Whether the information, once provided, actually proves to be relevant is of no importance.

#### No Protection For Banking Secrecy

The CH-IN DTA explicitly states that the requested state may not decline to supply information solely because the information is held by a bank, any other financial institution, nominee or person acting in an agency or a fiduciary capacity or because it relates to beneficial ownership interests. In other words, the request for information may be addressed both to a Swiss bank and to Swiss trustees or company directors. In all these cases, the affected taxpayer is no longer protected by Swiss banking secrecy.



By contrast, Switzerland may decline to disclose information relating to trade secrets, confidential communications between attorneys, solicitors or other admitted legal representatives acting in such capacity and their clients to the extent that the communications are protected from disclosure under domestic law. Switzerland has very stringent rules regarding attorney-client privilege. Swiss authorities will therefore not order a lawyer to disclose information related to him in the course of his representation of the client.

**No Retroactivity?**

As a rule, according to Swiss practice regarding international treaties, new clauses relating to the exchange of information have no retroactive effect or application. Accordingly, requests for information filed after the entry into force of the new rules can only relate to information regarding tax periods after the date of entry into force of the revised treaty text.

As to the CH-IN DTA, its amended article 26 provides for the exchange of information between the Swiss Authorities and the Government of India with respect to information that relates to any fiscal year beginning on or after the 1st day of January 2011.

According to section 3 of the Indian Income Tax Act 1961, the term 'fiscal year' (which is also referred to as 'previous year') means the financial year immediately preceding the assessment year. 'Assessment year' means the period of twelve months commencing on the 1st day of April every year (Indian Income Tax Act section 2). Therefore, under Indian tax laws the first fiscal year after 1 January 2011 is 1 April 2011 to 31 March 2012, the first relevant assessment year for the CH-IN DTA being the year 2012-13. Hence, any income earned/deposited on a bank account opened and closed on or before 31 March 2011 cannot be taxed in the fiscal year 2011-12 (i.e., 1 April 2011 to 31 March 2012) or any subsequent year but can only be taxed by way of re-opening and re-assessing the past assessment years, subject to applicable time limitations. Accordingly, the newly amended DTA should not be applicable on accounts or information pertaining to the period prior to 31 March 2011, as the same cannot be taxed as income of the previous/financial year 2011-12 or any subsequent year. However, this question has not yet been decided by Swiss courts and their interpretation of article 26 of the CH-IN DTA remains to be seen.

**Group Requests**

Switzerland interprets the DTA so that identification of the person under investigation may be provided by means other than by indicating the name and address of the person concerned, which again opens the door to so-called 'group requests'.

In practical terms, it is possible that in the future the SFTA will have to search for bank accounts opened by that person in all Swiss banks, a practice constantly refused in the past by Switzerland.

As an alternative, if the name of the information holder, e.g., a bank, is known to the Indian tax authorities, the latter may ask for information regarding certain Indian tax payers identified on the basis of a 'pattern of behaviour'. The description of the 'pattern of behaviour' of a person should give rise to the assumption that taxpayers whose behaviour corresponds to this pattern have not complied with their statutory obligations. However, it must be shown that the information holder (e.g., a bank) has significantly contributed to such taxpayers' behaviour, which must be non-compliant with Indian tax legislation.

By way of an example, and with reference to a decision of the Swiss Federal Administrative Court (the 'SFAC') of 5 April 2012 (A-737/2012), the United States IRS described



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the 'pattern of behaviour' of US taxpayers – without indicating any individual names – who presumably held bank accounts with Credit Swiss in Switzerland, in terms of a failure by the beneficial owners of the accounts stated on the bank documents (such as Form 'A') to declare their bank accounts to the United States IRS, or where there was a discrepancy between the beneficial owner named on Form 'A' and on the form 'W-8BEN'.

### Offshore Structures

A crucial issue is whether the Indian tax authorities will gain access to information on direct or indirect ownership kept in bank records, particularly the so-called Bank Form 'A' (stating the 'beneficial owner').

The exchange of information pursuant to double taxation treaties is a relatively new area in Switzerland where there is still little case law. However, there has been litigation in the context of requests filed by the US tax authorities against certain US clients of UBS and there are numerous precedents of the SFAC which is the only and last instance of appeal against decisions of the SFTA to disclose information based on a DTA. Although specific rules were applicable in the UBS matter, these decisions show the trend in the treatment of offshore structures such as Liechtenstein foundations or trusts when examining a request for information on the beneficial owners of such structures by foreign tax authorities.

For the purposes of a request for information, offshore structures will be assessed by Swiss authorities on the basis of the economic reality ('substance over form'), i.e., the decisive factor is whether and to what extent the person under investigation was able to continue to control and have a power of disposition over the account assets and revenue.

Swiss courts may be more favourable towards alleged 'beneficial owners' of discretionary trusts, i.e., without any entitlement to fixed income or capital of a trust, than to beneficial owners with a fixed interest under a trust document, e.g., a right to receive annual income from the trust assets.

Based on the information received from the information holder, the SFTA will decide on the eligibility for administrative assistance. In the case of eligibility for administrative assistance, the SFTA will rule in a final decision against the account holder that the information shall be disclosed.

### Illegally Obtained Data

At present, Switzerland does not admit requests for assistance if the information on which the request is based was 'stolen'. The new Swiss statute on the provision of administrative assistance which entered into force on 1 February 2013 explicitly states that a request will not be entertained if based on information that was obtained by acts that are punishable under Swiss law, such as the illegal acquisition of data ('fruit of the poisonous tree' doctrine).

Notably, in 2009 a former employee of HSBC Geneva stole client data that was handed over to French authorities and further passed on to the Indian Government. Also, stolen Swiss bank data that was contained in several CDs purchased by German authorities was passed on to other countries. Based on such experiences, the Swiss legislator has excluded the exchange of information in cases where the foreign request is based on information obtained from stolen bank data.

Therefore, for the time being, Switzerland will not admit a request for information from Indian tax authorities relating to information on HSBC accounts obtained through the stolen data. However, and not least because of pressure from India, the Swiss Government recently announced Switzerland's willingness in the future to cooperate with foreign tax authorities seeking administrative assistance on Swiss account holders identified using data obtained passively through other governments, while maintaining the policy of non-cooperation in circumstances where the stolen bank data in question had been purchased by the government issuing the request. The Swiss Government's proposal still needs to be approved by Parliament.

### Examination of Request By SFTA/Rights of the Concerned Person

If, after preliminary examination, the request from the Indian authorities is considered admissible by Switzerland, the SFTA will issue an order to disclose the requested information ('disclosure order') requesting the information holder, typically a bank or wealth manager, to submit the information/account documentation to the SFTA. The information holder will have no right to appeal against this order and will have to provide the information requested.

The bank or other information holder must inform the relevant account holder, the beneficial owner and

possibly also any authorised representative of the account (a 'concerned person') of the administrative assistance procedure. If the account holder or the beneficial owner is domiciled outside Switzerland, he/she may appoint an agent, e.g., a lawyer admitted in Switzerland, to receive notifications in Switzerland, concerning the request filed by the requesting state to Switzerland and inform the SFTA of the appointment of his/her agent. If the concerned person cannot be contacted or fails to appoint an agent in Switzerland, the SFTA may notify the concerned person through publication in the Swiss Federal Gazette or through other appropriate means.

The concerned person is entitled to examine the files sent to the SFTA by the information holder and to participate in the procedure by making objections in writing (supported by evidence) to the SFTA already at the stage of the disclosure order. However, the deadline to make such objections is relatively short (not exceeding 30 days) and may not be extended. Switzerland is considering a change to its legislation such that in the future, the taxpayer will no longer be heard in the case of an exchange of information (no tipping off).

On the basis of the file received from the information holder and the possible objections lodged by the concerned person, the SFTA will decide whether the information and supporting documentary evidence (such as account documents) shall be transmitted to the requesting state and to what extent.

### Appeal

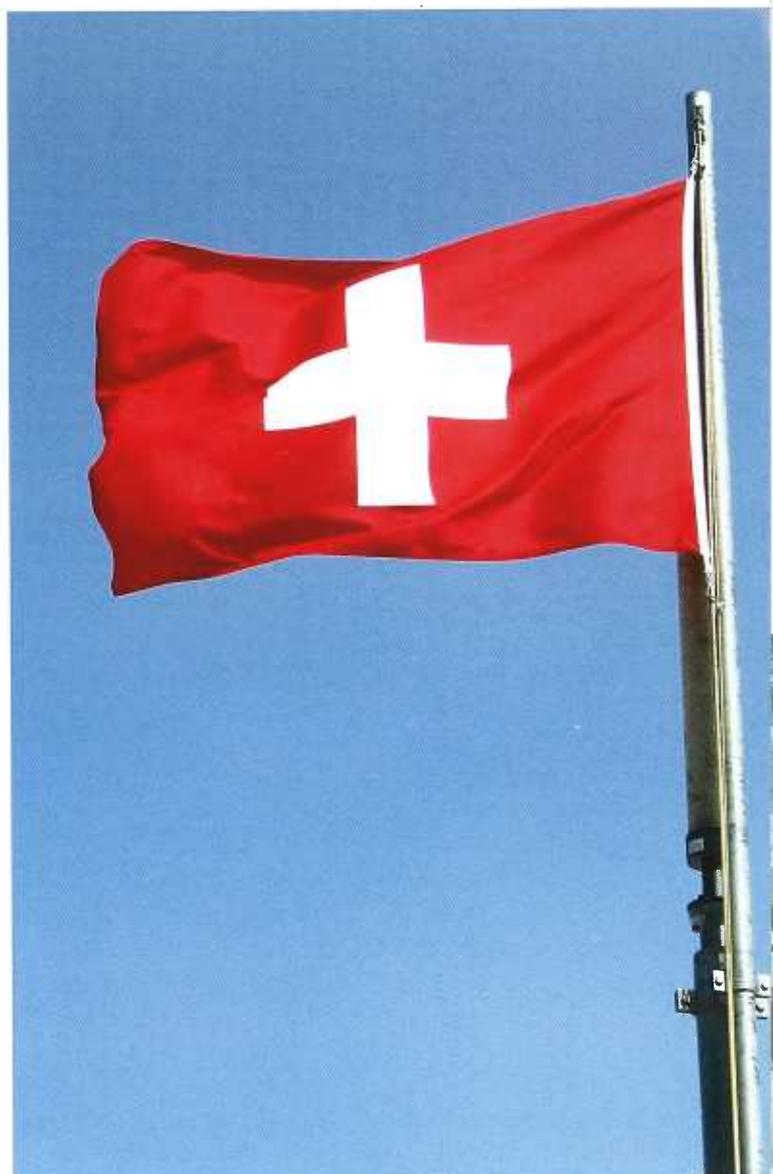
An appeal may be lodged with the SFAC against the decision of the SFTA within 30 days (non-extendable) after its receipt by the relevant person. Again, Switzerland is considering a change to its legislation for such appeal to be abolished.

In the case of an appeal, the SFAC will render a final decision as to whether the information is to be transmitted at all and to what extent, as the case may be. A further appeal against the decision of the SFAC may be lodged before the Federal Supreme Court in limited cases only.

As a rule, the appeal has a suspensive effect, meaning that no information will be handed over to the requesting state before the final decision comes into force.

In the appeal, various arguments can be used, including:

- the information requested is not foreseeably relevant for the tax investigation in India of the person concerned;
- the information requested falls outside the scope of the DTA (e.g., the tax investigation concerns taxes other than income tax);
- the information is requested for a tax period prior to the entry into effect of the DTA and is therefore contrary to the principle of non-retroactivity;
- the person under investigation is not the effective 'beneficial owner' of the funds of the structure;
- the request is not sufficiently specified but rather a fishing expedition;
- the request contains obvious errors, contradictions or omissions;





- the decision of the SFTA is granting more information than actually sought by the requesting state;
- information on third parties who are manifestly not involved in the subject matter is at stake; and
- the request is based on illegally obtained data.

**Transmission**

Once the final decision or the decision of the SFAC on appeal has entered into force, the information will be transmitted to the requesting state.

As a rule, the information transmitted under a DTA may be used by the foreign tax authorities not only for the taxation procedure but also for other purposes (for example in criminal tax proceedings), subject to consent by the requested state.

**Conclusion**

Switzerland pursues a 'white money' policy, i.e., a policy of welcoming only tax declared assets and income. The Swiss Federal Government aims to prevent banks and other financial intermediaries from harbouring and managing assets not disclosed to tax authorities having jurisdiction over the relevant foreign client by making financial institutions introduce enhanced due diligence requirements. It is envisaged that financial intermediaries must request a self-declaration from clients on the fulfilment of their tax obligations. The Swiss Federal Government has instructed the Federal Department of

Finance to submit a corresponding consultation draft in the course of 2013.

These developments will enhance legal certainty and should strengthen the reputation of Switzerland as a financial centre. Yet, numerous uncertainties remain which will call for judicial decisions. The best option available to each taxpayer will essentially depend on each individual's circumstances, having particular regard to the period during which the bank account has been open, the origin of the funds and the fluctuation of the funds since their deposit. Legal guidance will be crucial to navigate in such uncharted waters.



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