Bank fraud: recent developments in Switzerland

Friday 28 April 2023

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Switzerland is widely recognised as a global leader in asset management, with assets under management totalling CHF 8.8 trillion at the end of 2021.[1] Key factors such as its long-standing political neutrality and stability, a strong legal system, a highly-skilled workforce and a rigorous regulatory framework overseen by the Swiss Financial Market Supervisory Authority (FINMA) have given it a reputation for dependability, security and innovation, attracting clients from all over the world.[2]

This success has created a unique environment that has, nonetheless, been marred by some of the largest banking fraud cases in recent years. These include the Credit Suisse fraud case, involving a former wealth manager who, in 2015, was convicted of embezzling over CHF 100 million from his clients' accounts.[3] And, more recently, a case involving allegations of large-scale fraud against a senior executive at Hyposwiss Private Bank in Geneva, Switzerland.[4]

A series of scandals can occur which tarnish the bank's reputation and cause a loss of trust from both clients and markets. For example, in 2016, BSI AG was involved in several scandals surrounding the Malaysian sovereign wealth fund 1MDB and the Petrobras case, leading to its downfall and acquisition by EFG Bank AG. Credit Suisse AG also suffered a similar fate, after its involvement in multiple scandals (including Archegos and Greensill), and was bought out by UBS AG in a controversial transaction that may itself lead to further litigation.[5] Below, we highlight significant recent developments in case law related to **bank fraud and bank liability** and outline **what to expect when internal fraud is discovered**. We also discuss selected related **practical considerations**.

Recent case law developments in bank liability

In cases of fraud, the client (the victim of the fraud), may take legal action against both the fraudster and the bank. The rogue banker may not have the financial means to fully compensate the victim, so taking legal action against the bank becomes the more viable option. Although there may be reluctance to take legal action against Swiss banks, there has been an increase in such cases, with progressively developing case law.

Over the past year, there have been two noteworthy cases relating to fraud and bank liability.

In the first case, the Swiss Supreme Court clarified the type of contractual claim that a bank client can make against its bank, depending on the nature of the fraud involved.[6] According to its ruling, in cases of internal fraud, where the fraud is committed by an employee of the bank, the client has a claim for damages against the bank. However, in cases of external fraud, where the fraud is committed by a third party, the client is entitled to a claim for performance, which means that it can claim for the restitution of its assets held with the bank.[7] Its rationale is that faulty identification of powers of disposition are part of the risks inherent in banking activities, and the bank should bear this risk if it committed gross negligence in conducting its checks.[8] This argument was not well received by the practitioners, as there should be no differentiation between internal and external fraud.[9]

On the one hand, claims for damages may seem advantageous, as the claimant may ask for loss of profit in addition to the restitution of its assets held with the bank. However, and as highlighted by the Court, the claimant must prove the damage it suffered by providing factual and evidentiary support.[10] In complex matters, the claimant must be diligent in detailing the damages it has incurred.[11]

On the other hand, claims for performance may be considered favourable to the client, as the bank cannot invoke concomitant fault on the client's part (Art. 44 of the Swiss Code of Obligations ('CO')). However, the question of concomitant fault is indirectly taken into consideration when assessing whether the bank can counterclaim for damages due to breach of contractual obligations by the client, on the basis of Article 97 CO.[12] The examination of potential contractual breaches by the client includes an assessment of its possible fault.

In the second noteworthy case, the Swiss Supreme Court provided clarifications on tort claims based on Art. 41 CO, in conjunction with a breach of Art. 305bis of the Swiss Criminal Code ('SCC'), which prohibits money laundering.[13] It has now been established that money laundering offences may constitute an unlawful act under Art. 41 CO, giving rise to a tort claim.[14] In this context, in the recent decision, the Court stressed the need to examine the intentional conduct of particular bank employee(s), rather than the bank's overall conduct. These employees must fall within the limited circle of individuals listed in Art. 29 SCC, i.e., typically employees with a supervisory position and decision-making authority.[15] The challenge is therefore to identify such employee(s) and prove that they committed an act of money laundering wilfully, or at least recklessly, in violation of anti-money laundering laws and regulations.[16]

What can be expected when internal fraud is discovered?

In a bank, the most common instances of fraud usually involve the relationship manager conducting unauthorised payments or trading. These transactions may include unauthorised Lombard loans and/or cross pledges between clients' accounts, as well as falsified bank statements and contracts.

There are several ways in which banks can detect fraud:

a) They use IT surveillance systems to identify suspicious activities, such as unusual transactions or high-amount money transfers.
b) Market downturns and unexpected losses may prompt close examination of risky investments or imprudent lending practices that could be linked to fraudulent activities.
c) Fraud detection may also arise from direct reporting by clients, employees, or auditors.

Upon uncovering internal bank fraud, the bank usually initiates an internal investigation to assess the scope of the fraud and identify the individuals implicated and clients affected. If the investigation confirms the occurrence of fraud, the bank will consider filing a criminal complaint against its employee(s) and claiming plaintiff status. Where a bank discovers internal fraud, it must report it to FINMA, which may appoint an investigating agent and open enforcement proceedings to investigate suspected breaches of regulatory and anti-money laundering laws.**[17]**

In this initial phase, clients will often face difficulties when attempting to obtain an explanation from the bank of the detail of the fraudulent activities that took place in their account. In some instances, banks indemnify their clients without any discussion, but this is rare. In the vast majority of cases, the bank argues that it is the victim of its own employee, contending that the client's lack of diligence allowed the rogue banker to continue to perpetrate its fraud, thereby breaching the causation link between the bank's violation of its obligations and the resulting damage, or constituting a concomitant fault, which could lead to a partial or total reduction of the compensation for the damage.

In this situation, clients should act swiftly to challenge the transactions/operations on their accounts, as the general terms and conditions typically stipulate a short time period to do so. If the fraud was perpetrated over a long period of time, it may also be urgent to interrupt the statute of limitation.

Practical considerations

Once these urgent actions have been taken, the client's counsel should establish a strategy to build up the case and obtain compensation for the damage incurred. Some practical considerations identified in large cases of fraud include the following:

Gathering information

The extent to which the bank co-operates in disclosing relevant information and documentation pertaining to the fraud may differ. It largely depends on whether the bank itself is being targeted and the degree to which it intends to defend its fraudulent employee (or not). For instance, the bank may seek to establish plaintiff status against the employee, while in other instances, such as money laundering cases, the bank may be directly targeted and intervene in the proceedings as a defendant alongside the employee. Clients have a range of alternatives for obtaining information and documents and are usually able to directly obtain some relevant documents from the bank on the basis of contractual law. Criminal proceedings, with the assistance of a public prosecutor, may also enable clients to obtain information and documents concerning the fraud by accessing the criminal file, though not all relevant documents for a civil claim may be obtained this way.

Benefitting from enforcement proceedings

Financial institutions that fall under FINMA's supervision are legally required to promptly report any event of substantial importance from a regulatory point of view (Art. 29(2) of the Federal Act on the Swiss Financial Market Supervisory Authority). In this context, FINMA usually opens enforcement proceedings to investigate possible breaches of regulatory laws (including anti-money laundering laws and regulations).

The enforcement proceedings can be highly useful in establishing certain critical aspects or facts that are decisive for the bank's civil or criminal liability. For instance, FINMA's analysis may reveal repeated deficiencies illustrated by the bank's lack of critical thinking and inadequate monitoring, which may demonstrate the bank's gross negligence or inadequate organisation.

As an example, in a case involving Credit Suisse AG, FINMA produced a 270-page report highlighting repeated warning signs that the bank received but chose to ignore without justification.**[18]**

Claiming damages

The victim of the fraud can file civil claims against the bank in the criminal proceedings to seek compensation for its damage resulting from the fraud. In some cases, the criminal proceedings against the bank may be sufficient, particularly when the victim has 'only' suffered unauthorised payments. However, in more complex instances of fraud (e.g., unauthorised trading requiring an expert report on the damages calculation), criminal courts typically rule on the criminal offences and refer the client to the civil court for its damages claim.

Leverage recovery chances by working with lawyers from other jurisdictions

When it comes to large fraud cases, multiple jurisdictions are often involved (because of the use of offshore companies, trusts, foreign life insurance, payments wired in foreign countries, etc.), making it crucial for lawyers from each jurisdiction to collaborate and establish a global strategy, to maximise the chances of recovering losses, by analysing thoroughly the advantages of each jurisdiction for the claimant and moving the bank out of its comfort zone.

For further questions or comments about this topic, please contact the authors.

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[12] Swiss Supreme Court Decision 146 III 121.
[13] Swiss Supreme Court Decision 4A_603/2020 of 16 November 2022.
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