

Agreement between Switzerland and Germany to resolve bilateral tax issues

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1 Background and history

At 6.7% of gross domestic product, the Swiss banking sector makes an important contribution to prosperity in Switzerland. Almost 10% of the country's tax revenues come from the Swiss banks, which provide around 142,000 skilled jobs in Switzerland. The legitimate protection of clients' privacy in financial matters is an important factor in this success. Switzerland has therefore made strong efforts to prevent abuse at the international level by means of international administrative and judicial assistance processes and cooperation based on multilateral and bilateral agreements, such as the recent adoption of the OECD 26 standard. The Swiss banks have consistently supported Switzerland in these efforts and implemented the corresponding measures.

A variety of problems and issues have arisen in the cross-border banking business in recent years that jeopardise important political and economic bilateral relations. In response to these developments, the Swiss Bankers Association has promoted the *2015 Financial Centre Strategy* since 2009. This strategy forms part of the sector's future orientation and was unveiled by the Swiss government at the end of 2009. It is based on the following four pillars:

- **Retain and strengthen trust through regularisation**

The regularisation of untaxed assets in Switzerland is at the heart of any future solution with other countries. The trust that foreign clients have in Switzerland's legal system and the fiduciary responsibility exercised by Swiss bankers, both of which have been developed carefully over many years, require no less.

- **Focus on taxed assets**

Swiss banks will in future focus on the acquisition and management of taxed assets. The adoption of the global standard of Article 26 of the OECD Model Double Taxation Agreement supports this approach. The standard provides for administrative assistance on a case-by-case basis for all tax offences where there is legitimate suspicion. This eliminates the distinction between tax evasion and tax fraud for other countries.

- **Protection of privacy remains key**

The financial market strategy retains the protection of client privacy as a central aspect of the Swiss legal approach, while making it possible for action to be taken to combat or prevent all tax offences. The SBA firmly rejects the automatic exchange of information and has developed a comprehensive flat rate tax model as an equivalent solution. The model allows all taxable income from assets and capital gains to be recorded in accordance with

the tax law of the treaty state concerned, and the tax payable on them to be withheld and transferred to the responsible tax authorities anonymously.

- **Growth and market access**

A strong financial centre is of the greatest importance for the Swiss economy. The prerequisite for this is growth, which can only be achieved by continuously improving competitiveness. The banks themselves are primarily responsible for this. Each day, Swiss banks can and must demonstrate the benefits they offer their clients in all areas, thereby distinguishing Switzerland from other financial centres. At the international level, other countries must respond in kind to the flat rate tax model by improving market access for financial services from Switzerland and reducing existing bilateral discrimination.

In the interests of preserving foreign clients' trust in Swiss banks, which has been painstakingly built up over the years, and regulating outstanding bilateral issues relating to taxation, the Swiss government has been holding talks and negotiations with various countries including Germany since 2010. On 10 August 2011, the two countries initialled an agreement that resolves the pending taxation issues in the interests of both countries and the clients affected by the agreement.

2 Key aspects of the agreement

Regularisation of the past

- Bank clients have two options to regularise untaxed assets held by banks in Switzerland:
 - Payment of a flat rate one-off sum;
 - Voluntary disclosure to the German authorities without penalty.
- Regularisation will be effected by means of an anonymous one-off payment.
- This means that bank clients will have fulfilled their tax obligations in Germany.
- A maximum tax rate of 34% of the assets will apply for the one-off payment. The effective tax rate for bank clients is likely to be between 20% and 25% of total assets.

Advance payment by the Swiss banks

- The Swiss banks have committed to making an advance payment of CHF 2 billion. This demonstrates the willingness of the Swiss banks to ensure the practical implementation of the letter and spirit of the agreement. This payment is due after the agreement comes into effect and will thereafter be offset against the tax payments made by clients.

Final withholding tax for the future

- The banks will deduct an amount annually on an anonymous basis from income from assets equivalent to German income tax.
- The deduction of this withholding tax will also have the effect of satisfying any tax liability.
- The tax rate is 26.375%.

System control measures

- The German tax authorities are entitled to monitor the correct implementation of the German final withholding tax by Switzerland through random queries. Should the German authority wish for further information with regards to the reported bank accounts, a normal request for administrative assistance pursuant to OECD 26 must be submitted.

Simplification of cross-border business/easier market access

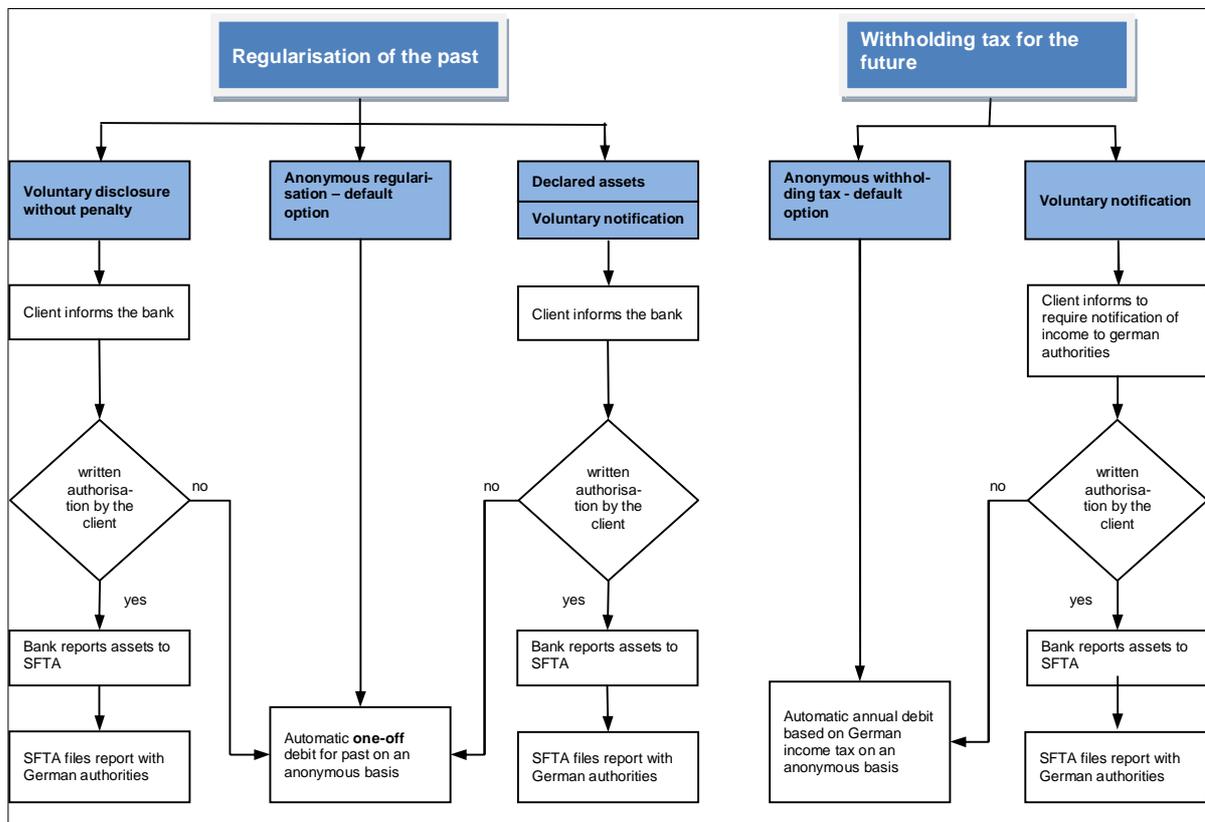
- Swiss banks can operate in the German market under easier conditions.

Decriminalisation of banks, bank employees and bank clients

- Regularisation means that clients, banks and their employees will be protected from any criminal prosecution.

No future exploitation of stolen data

- Germany has committed not to use information from purchased data carriers containing stolen data in future for legal proceedings against Swiss banks or their employees.



3 Position of the Swiss Bankers Association

- The SBA welcomes the initialling of the bilateral treaty covering tax issues between Germany and Switzerland.

- The bilateral treaty is a milestone in the implementation of the 2015 Financial Centre Strategy:
 - It is a well-negotiated compromise and must be evaluated in its totality. The Swiss banks will have new growth opportunities due to improved bilateral market access.
 - Clients of banks in Switzerland who are taxable in Germany will receive a means to tax compliance while maintaining their privacy at the same time.
 - Germany will obtain tax revenues quickly and unbureaucratically.
- The solution sends out a strong signal and could therefore act as an international benchmark for other countries in tax cooperation.
- The SBA acknowledges the significant efforts by the Swiss government and, in particular, the State Secretariat for International Financial Matters (SIF) in the negotiation of the bilateral treaty.
- The SBA remains committed to seeing that the banks achieve the technical implementation cost efficiently and compliant with the bilateral treaty by 2013.

4 Questions & Answers

4.1 General/Significance for clients

Which clients will be affected by the flat rate tax?

The agreement only applies to natural persons domiciled in Germany. The agreement also applies to natural persons domiciled in Germany who hold indirect assets in Switzerland – for example through a foundation or other domiciliary company in which they have a beneficial interest.

Which assets will be regularised under the agreement?

The agreement covers assets in bank accounts and securities portfolios held by the above-mentioned clients in Switzerland.

Are assets at Postfinance also affected?

The agreement covers all assets (bank accounts and securities portfolios) held by the above-mentioned clients at banks, brokers, Postfinance and asset managers.

What can clients do now?

At this stage, clients are not required to take any immediate action in terms of the provisions of the agreement. The treaty will have to be signed and then ratified by the parliaments of both countries, after which it enters into force. Once the agreement has entered into force (provisionally on 1 January 2013), all clients will have five months to choose one of the following options:

- Regularisation of the past:
 - Anonymous regularisation by way of a one-off flat rate tax.
 - Voluntary disclosure to the German tax authorities without penalty and voluntary notification to the Swiss Federal Tax Administration (SFTA).
 - For bank clients who were already tax compliant: voluntary notification to the Swiss Federal Tax Administration (SFTA).

- Final withholding tax for the future:
 - Anonymous annual withholding tax to satisfy tax liability (flat rate tax)
 - or, voluntary notification to the Swiss Federal Tax Administration (SFTA).

If clients do not select any of the above options, they will automatically be subject to the flat rate tax.

If clients decide not to take advantage of this beneficial solution, they must withdraw their assets from Switzerland by 31 May 2013. However, the Swiss banks will not actively support clients in this regard.

If bank clients use the flat rate tax option, will the Swiss bank-client confidentiality not be affected?

Quite the opposite, in fact. The bank will debit clients with the flat rate tax due and transfer the money to the Swiss Federal Tax Administration (SFTA), which will in turn transfer the money to the German tax authorities. The process will be monitored exclusively by the SFTA; foreign authorities will not be involved in the process at all. The legitimate protection of privacy in financial matters is preserved, and the solution safeguards it for the long term, thereby strengthening it.

In which currency will the levied taxes be calculated for clients?

The tax will be calculated in EUR to minimise currency fluctuations.

Can clients still be held liable for tax offences despite regularisation?

Regularisation means that clients and Swiss banks and their employees can no longer be criminally prosecuted or held financially liable for tax offences, unless there was already evidence that might result in criminal proceedings before the signing of the agreement.

In the event of tax queries, how can bank clients prove that they have regularised their assets in Switzerland?

Bank clients will receive certification from their bank showing the tax deducted. This certification can be used as proof in any tax enquiry and will be recognised by the German tax authorities.

4.2 One-off flat rate tax for the past

Bank clients can regularise their previously untaxed assets as follows:

4.2.1 Anonymous regularisation

How does anonymous regularisation work?

The regularisation of previously untaxed assets will be effected by way of a one-off payment. The amount will be calculated by the bank using a flat rate method and deducted from the client's assets.

How will clients know how much they have to pay?

The maximum nominal tax rate has been negotiated between Germany and Switzerland and is 34% of assets. However, this is different to the effective tax rate that clients will pay. Because of the calculation methodology (that considers factors such as statutory limitation), the rate for the majority of clients will probably be between 20% and 25% of total assets.

The amount that has to be paid to regularise the existing assets will be calculated for each client according to the tax rates defined in the agreement. Clients will receive more detailed information from their client advisors at a later stage.

Do clients have to do anything right now if they wish to make use of this option?

Anonymous regularisation is expected to be the default option so for the moment there is no action required from bank clients as a result of the agreement. Banks will contact clients to advise them of the next steps within a period of two months after the agreement enters into force. In all cases, clients remain responsible for their own tax affairs.

When exactly will the flat rate payment for the past be deducted?

Banks will deduct the amount owed from client accounts five months after the agreement enters into force (provisionally on 31 May 2013) and will provide clients with certification of the deduction. Clients will be able to appeal the certification.

Will clients receive confirmation giving details about the payment of the one-off flat rate tax?

Yes. This certification can be used as proof in any tax enquiry by the German tax authorities and will be recognised by the German authorities.

What happens if there is insufficient cash in the account at the time the tax is deducted?

If clients opt for the anonymous one-off flat rate tax, they must ensure that there is sufficient cash available at the time the tax is deducted. If there is insufficient cash for the full deduction of the tax, the bank will inform clients that their balance is insufficient and set a specific deadline by which to have the funds available. At the same time, the bank will advise clients of the consequences of not having sufficient cash available by this deadline. If the necessary balance is not available in the account upon expiry of the deadline, the bank will switch to the voluntary notification process and provide the required information to the SFTA.

4.2.2 Voluntary self-disclosure without penalty and voluntary notification

What is voluntary self-disclosure without penalty?

As an alternative to anonymous regularisation, bank clients have the option of voluntary disclosure to the German tax authorities without penalty. This option requires bank clients to make a late declaration in Germany of untaxed assets.

What must bank clients do if they wish to choose this option?

To cover Swiss formalities, bank clients must inform the bank of their intention to make use of the voluntary disclosure without penalty option in Germany. In addition, clients must authorise the bank in writing to notify the Swiss Federal Tax Administration (SFTA) of the assets under management at the bank. The SFTA will then forward this information to the German tax authorities.

If clients fail to provide the bank with this authorisation, the bank has to follow the one-off flat rate tax procedure, i.e. the bank will deduct the tax amount owed for the past and forward this to the SFTA.

What data will be forwarded by the SFTA to the responsible German tax authorities?

Following written authorisation from the client, the bank will provide the SFTA with the name and date of birth of the client, domicile, name of the bank, account number/IBAN code and the amount of assets at the end of the year for each year within the statutory limitation period.

Will clients receive a copy of the notification that the bank gives to the SFTA?

Clients will receive certification from the bank showing the information provided to the SFTA (name and date of birth of the client, domicile, name of the bank, account number/IBAN code and the amount of assets at the end of the year for each year within the statutory limitation period).

4.2.3 Voluntary notification

What is voluntary notification?

This option is open to bank clients who have previously fulfilled their German tax obligations.

What must bank clients do if they wish to choose this option?

Bank clients must inform the bank that they wish to notify the responsible German authorities. Clients must authorise the bank in writing to notify the SFTA of the assets under management at the bank. The SFTA will then forward this information to the German tax authorities.

4.3 Final anonymous withholding tax for the future

How does the final anonymous withholding tax for the future work?

The final withholding tax for the future will see income from assets (interest income, dividends, other income and capital gains) taxed anonymously by a deduction equivalent to German income tax.

How will clients know how much they have to pay?

The current tax rates applicable in Germany for German income tax will apply. The tax rate is 26.375% in total. The tax will be deducted on an anonymous basis.

Bank clients can pay tax on their future income from assets as follows:

4.3.1 Final anonymous withholding tax (flat rate tax)

How does the anonymous withholding tax work?

Based on its client data, the bank deducts the tax due and forwards the entire amount to the SFTA without any information that may identify individual clients. The SFTA will then forward the amounts to the responsible German tax authorities.

What must bank clients do if they wish to choose this option?

The anonymous withholding tax is expected to be the default option and will be calculated and deducted by the bank automatically so for the moment there is no action required from bank clients. The bank will contact clients to advise them of the next steps within two months after the agreement enters into force.

Will clients receive a statement in future giving details about the final tax paid?

Yes, clients will receive certification annually giving details about the final withholding tax paid for each tax year. This certification is valid for tax purposes and will be accepted by the German authorities.

4.3.2 Voluntary notification

Bank clients can authorise the bank to notify the SFTA of the income from assets from their assets under management in Switzerland. The SFTA will then forward this information to the responsible German authorities.

What must bank clients do if they wish to choose this option?

Bank clients must inform the bank of their intention to notify income to the responsible German authorities. Clients must authorise the bank in writing to provide the SFTA with the information required (name and date of birth of the client, domicile, name of the bank, account number/IBAN code, the applicable tax year and the total amount of investment income). The SFTA will then forward this information to the German tax authorities.

If clients fail to provide the bank with this authorisation, the bank has to follow the withholding tax procedure, i.e. the bank will deduct the tax amount owed and forward this to the SFTA.

Will clients receive a statement in future giving details about the data provided?

Yes, clients will receive certification annually for their information giving details about the amounts notified.

Can clients offset losses carried forward from one account against profits in another account, as is possible in Germany?

As under German law, clients can offset losses carried forward from one account against profits in another account. If the accounts are held at the same bank, the bank can do the offset calculation directly. If the accounts are at different banks, the client must approach the German tax authorities and request an ordinary tax assessment in order to apply for the offset. The bank will provide the client with a confirmation of the loss for this purpose.

Will a bank in Switzerland accept a certificate that no tax is normally due ("Nichtveranlagungsbescheinigung") and waive the final withholding tax?

Tax will not be deducted only if the client authorises notification to the German tax authorities. Without such authorisation, the bank will automatically deduct the withholding tax.

Will foreign withholding tax on dividends and interest be offset against the final withholding tax?

Non-reclaimable foreign withholding tax will be taken into consideration when deducting the final withholding tax pursuant to the applicable double taxation agreements between other countries and Germany. As a result, non-reclaimable tax already withheld will only be deducted where this exceeds the withholding tax due.

4.4 General questions about the agreement

Haven't the banks breached their duty of fiduciary responsibility towards their clients with this agreement?

Settlement of tax affairs has always been and will remain the sole responsibility of clients, and not of their bank. By introducing the one-off flat rate tax Switzerland is offering existing bank clients a simpler way than in the past to regularise their affairs while simultaneously preserving privacy. Future final withholding tax on income from assets will be deducted automatically by the bank on an anonymous basis. This means that the client's privacy can be safeguarded and the tax paid without any effort by the client.

How will compliance with the agreement be monitored?

As with the EU taxation of interest income, the SFTA will monitor compliance with the agreement by the banks using control measures.

What are the system control measures that can be undertaken by the German tax authorities?

The German tax authorities are entitled to monitor the correct implementation of the final withholding tax by Swiss banks through random queries. These system control measures must be viewed in the context of the entire package of measures that offers bank clients the opportunity to regularise their past in an anonymous manner and also to enjoy the protection of their privacy in future while complying with their tax obligations.

On average, the German authorities can make about 500 queries per year; the queries must contain the name of the client and a justified suspicion of tax irregularities. This rules out the possibility of "fishing expeditions". By contrast, the name of the bank does not have to be included in the query. The query process can only be used for the future, i.e. for new assets brought into Switzerland. Private assets that have been regularised by a one-off payment are not subject to the query process. If these conditions for the query are met, the Swiss authorities will search for and report only accounts held, without releasing any additional details such as the account balance, etc. Bank clients have recourse to the German courts.

If the German authorities require additional information on accounts reported they will have to submit a normal request for administrative assistance under the double taxation agreement, while bank clients will have recourse to all Swiss courts. Any request for administrative assistance must conform to the standard under Article 26 of the OECD.

What is the advance payment?

The Swiss banks have committed to an advance payment of CHF 2 billion. This demonstrates the willingness of the Swiss banks to ensure the practical implementation of the letter and spirit of the agreement. The advance payment is due after the agreement comes into effect and can thereafter be offset against the one-off tax payments made by clients.

How will the banks divide up the advance payment?

The banks have agreed amongst themselves which banks will contribute what share to the advance payment. The individual allocation is based on the size of the business with affected clients as per 31 December 2010.

Each bank will decide itself on how to fund the advance payment.

What happens now? What is the timetable?

The parliamentary process will begin once the agreement has been initialled and signed. In Switzerland, the decision by parliament will be subject to an optional referendum. The SBA is very eager to see the entire process brought to a rapid conclusion. If ratified, the agreement will enter into force at the start of 2013.

Can the agreement be terminated at a later date?

Each party can terminate the agreement whilst respecting a two-year notice period. Given that the agreements have been entered into in the interests of both countries, we assume that they will have a long period of applicability. In addition, Germany has explicitly recognised that the agreement is an equivalent alternative to the automatic exchange of information under the EU Savings Tax Directive.

What will happen if Germany changes the tax rate in future?

The agreement stipulates the current tax rates that apply in Germany. If these rates change under German law, Switzerland will adopt the adjusted rates simultaneously.

How does the introduction of the final withholding tax relate to the EU taxation of interest income?

The EU taxation of interest income will continue to be applied with a tax rate of 35%. However, clients will be taxed with a factual rate of 26.375% due to the agreement which foresees a carry back. This tax deduction will also satisfy tax liability.

Der Zinssatz der EU-Zinsbesteuerung beträgt unverändert 35%. De facto beträgt die Endbelastung für den Kunden für alle Zinsen nur 26,375% aufgrund der Verrechnung gemäss dem Abkommen. Diesem Steuerabzug kommt ebenfalls die abgeltende Wirkung zu.

4.5 Questions about the impact on the Swiss financial centre and the banks

What does the agreement mean for Switzerland as a financial centre?

We are confident that the agreement sends out a strong signal. It gives Switzerland the chance to implement its forward strategy for the financial centre. The parties to the agreement have also clearly acknowledged for the long term that the flat rate tax model is equivalent to the automatic exchange of information.

The solution for Switzerland could therefore act as an international benchmark for other countries in tax cooperation.

Will the competitiveness of the financial centre be hurt by this arrangement?

On the contrary, the financial centre will be able to reorient itself and grow from a position of strength. International reach, capital market expertise and quality of service, coupled with the stability offered by Switzerland, are continuing to gain in significance for Swiss banking.

Is there still a future for offshore banking?

The Swiss financial centre continues to be very attractive. Its core values of stability, universality, responsibility and excellence are the pillars of sustainable success. The agreement will mean that the clients in question will enjoy even greater legal certainty and – where this is not yet the case – be able to invest their assets in Switzerland in compliance with tax law.

How much money will be regularised?

We are not able to say. The amount depends on the extent of undeclared figures, which is currently unknown, and the willingness of clients to regularise.

How many clients will choose anonymous regularisation and how many will choose voluntary disclosure without penalty?

We are unable to give an estimate. Clients are free to make their own decision.

Do you expect to see assets moved out of the country?

It is difficult to predict. We assume that the terms of the agreement and the advantages of the Swiss financial centre will reduce asset outflows.

How much will the implementation of the agreement cost Switzerland's banks?

We think the figure will be at least in the mid-three-digit millions of Swiss francs.

Once all the parameters of the flat rate tax model are known, the technical implementation of the tax can be drawn up. The Swiss banking landscape is very heterogeneous as to size of banks, business areas, number of clients from Germany etc., so the costs will probably vary significantly between the banks. However, optional services that are currently being developed by SIX Group in close cooperation with the SBA will be able to reduce the outlay for the banks.

The SBA aims to find practical solutions that can be applied across the sector and is actively working on developing such solutions. It is clear that the costs resulting from the implementation must remain within reason, especially for small and medium-sized banks.

Do you anticipate consolidation in the Swiss banking sector?

It is difficult to forecast the impact of the agreement. We believe that the terms of the agreement and the advantages of the Swiss financial centre such as increased legal certainty and easier market access will strengthen the attractiveness of the Swiss banking sector.

What does easier market access in Germany mean?

Foreign banks that wish to provide financial services in Germany require written authorisation under German law. Furthermore, if foreign banks wish to provide financial services to private clients, client contact must be made via a German bank.

The agreement will facilitate access to the German market for Swiss banks that wish to offer their financial services in Germany:

- Simplified and accelerated exemption procedure for Swiss banks in Germany.
- Client contact will no longer have to be made via a German bank as a matter of principle.
- Certain products such as securities funds that meet the regulatory requirements in Switzerland can also be sold in Germany.

How much additional business do you expect thanks to the improved market access?

It is not possible to answer that question at present. However, improved market access does present Swiss banks with new business areas and therefore attractive growth opportunities.

Does the improvement in market access mean that a financial services agreement with the EU is finally off the agenda?

The proposed bilateral treaty only creates easier market access at the bilateral level. It does not affect EU law because it is a package of national measures.

Switzerland is an open economy and as such will continue to work at all levels towards non-discriminatory market access for its goods and services.

The EU is pushing for automatic exchange of information. How do you expect it to react?

EU member states are free to enter into bilateral agreements with non-member countries provided that they do not breach EU law. We expect that countries that enter into such an agreement with Switzerland will work within the EU to have the flat rate tax model recognised for the long term as an equivalent measure to the automatic exchange of information.

Can Germany introduce an automatic exchange of information at a later date?

In the agreement final withholding tax is recognised as equivalent to the exchange of information for the long term. The legitimate protection of privacy in financial matters is preserved, and the solution safeguards it for the long term, thereby strengthening it.

Will Switzerland negotiate similar solutions with other countries?

We would welcome it if an equivalent solution could be agreed with other European countries. Further countries have already indicated an interest in this type of solution.
