Report on international financial and tax matters 2012
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2011 was the year of the debt crisis. The debt burden of many industrialised nations has now increased to the point where their ability to finance themselves over the long term is open to question. Confidence in government bonds as a secure investment has been shaken. The consequences for the real economy are unmistakable: huge pressure to make savings and vital structural reforms to regain competitiveness are leading to widespread job losses and reductions in social benefits, which in turn represent a threat to social and political stability.

With its open economy and major financial centre, Switzerland too is affected by these developments. On the one hand, the increased flight of investors to the Swiss franc has seen the currency appreciate dramatically, which poses a clear threat to the competitiveness of Swiss exporters. On the other, given Switzerland’s healthy financial situation, there is growing political pressure not only to show solidarity and help tackle the latest financial crisis, but also to push ahead with long sought-after adjustments in the field of finance and tax.

Switzerland has recognised the need to take the initiative itself. For example, the debt brake concept is an exemplary model that is likely to be increasingly adopted elsewhere. In February 2010, the Federal Council fleshed out its financial market strategy, which together with reforms in the field of finance and tax will establish the ideal parameters for the further development of an economic sector that is important for Switzerland. A number of important steps towards implementation followed in 2011. In keeping with its strategy of financial integrity, Switzerland signed withholding tax agreements with Germany and the United Kingdom, and is prepared to sign further such agreements with other states. Clarification in the tax sphere is also being sought with the United States and the EU. Thanks to the rapid passing of the “too big to fail” bill, systemic risks that became apparent during the financial crisis have been reduced.

2012 will bring with it particular challenges. As a result of its own efforts, Switzerland is in pretty good shape relative to many other countries, but for precisely this reason expectation is growing among our international partners that we will play our part in tackling the latest deep-rooted crisis. And Switzerland will indeed contribute – by continuing to keep our own financial house in order, by applying generally respected tax rules, by further reducing our systemic risks, and by contributing on the international stage with constructive proposals and commitment. When the economic environment becomes more hostile, it is important to strengthen international collaboration and preserve the competitiveness of the financial centre – and therefore ultimately also the Swiss economy as a whole. This is a responsibility shared between the government and the private sector.

I invite you to read this report – which is now appearing for the second time – as it will give you an idea of the many different current and future issues at stake in the area of international financial and tax matters.

I hope that it makes for interesting reading.

Bern, January 2012

Eveline Widmer-Schlumpf
Head of the Federal Department of Finance
Overview

By setting the course for a new financial market strategy at the end of 2009 and in early 2010, the Federal Council signalled a new beginning. The aim is for Switzerland to have a competitive and secure financial centre and business location with optimum, internationally accepted framework conditions. This is the only way to ensure that the financial centre’s contribution to Switzerland’s prosperity remains substantial and sustainable. The benefits and credibility of the new financial strategy essentially depend on the extent to which it is applied and to which actions follow words. The Federal Council is taking various steps in this regard at the national and international level. The integrity of the financial market should be consolidated with a strategy of financial integrity. Switzerland does not want to attract untaxed or criminal money. The stability of the financial sector will be improved with an ambitious yet moderate regulatory framework. Switzerland’s competitiveness as a financial centre and business location will be promoted through fiscally attractive yet non-discriminatory framework conditions and the sensible implementation of international regulatory standards. Finally, international integration will be improved through Switzerland’s active participation in international financial bodies, which will safeguard its strong position within the international financial system.

In 2011, important milestones were achieved in the implementation of the financial market strategy:
– At the end of September, parliament approved the legislative proposals designed to strengthen financial sector stability (too big to fail, TBTF). The package of measures is intended to prevent the difficulties of a major bank from endangering the entire national economy and also prevent the government from having to bail out such a bank with tax money. The core points of the proposal are more capital, stricter liquidity requirements, better risk management, and organisational precautions for an emergency (see section 2.2.3). The stringent requirements imposed by the Financial Stability Board (FSB) on systemically important financial institutions and adopted by the G20 Heads of State and Government in November corroborate the approach chosen by Switzerland.
– In autumn, Switzerland signed an agreement with both Germany and the United Kingdom on cooperation in tax matters (withholding tax agreement; see section 3.2.3). These agreements reconcile two concerns: the states’ justified concern regarding taxation of their citizens, and the equally justified concern of bank clients regarding protection of their privacy.
– The Federal Council’s dispatch on the new Tax Administrative Assistance Act aims to provide a legal basis for implementing the new administrative assistance policy. This legislation replaces the ordinance enacted in 2010 and governs the specific application of administrative assistance as negotiated in accordance with the OECD standard in the more than 40 double taxation agreements revised in the meantime (see sections 3.2.1 and 3.2.2).
– In March, parliament approved an increase in the IMF’s financial safety net (New Arrangements to Borrow) and a new loan to the IMF’s Poverty Reduction and Growth Trust. Switzerland will provide the IMF with a total of up to approximately CHF 23 billion. Through its contributions to the IMF, Switzerland also supports the countries affected by the euro crisis and thus makes a key contribution to international financial stability, a major concern for Switzerland as an exporting country (see section 4.2).
– Switzerland also engages in financial and tax-related exchanges with countries other than the United States and those in Europe. In 2011, Switzerland signed memoranda with Russia and India on an institutionalised financial dialogue (see section 2.5).
– Switzerland has been closely involved in the revision of the FATF standards against money laundering, terrorist financing and proliferation financing, which are expected to be adopted at the beginning of 2012 (see section 2.4.1).

Much work still remains to be done. Despite all the relief and austerity programmes, the international debt crisis is unlikely to be defused in the near future. The pressure is mounting for Switzerland too, not only for the countries most severely affected. Under these circumstances, it is important for Switzerland to continue to push ahead with the implementation of its new financial market strategy.
Important steps lie ahead in 2012 and beyond:

– The withholding tax agreements with Germany and the United Kingdom must be secured by parliament. Negotiations with additional countries on similar tax agreements are to be sought.

– The tax-related problems from the past with the United States (tax crimes committed by US clients of Swiss banks) must be resolved on the basis of the applicable legislation and incorporated within a global solution.

– Switzerland must play an active role in the further development of the OECD standard on administrative assistance in tax matters.

– With regard to the future framework for company taxation, a solution must be sought that accommodates Switzerland’s competitiveness as a business location, the budgetary interests of the Confederation and the cantons, and international acceptance.

– With respect to financial dialogues, existing partnerships should be consolidated and new dialogues entered into with additional countries (Australia, Brazil, China and India).

– Switzerland must ratify the IMF quota reform and Switzerland’s IMF constituency must be strengthened.

– The interests of Switzerland as seat of the FSB and non-member of the G20 must be actively represented in the planned institutional strengthening of the FSB.

– The bill to strengthen financial sector stability approved by parliament must be implemented as efficiently as possible and without compromising the competitiveness of the institutions concerned.

– Within the scope of examining further regulatory reforms in the wake of the 2008 financial crisis, the extent to which international trends are to be taken into account (e.g. for hedge funds or OTC derivatives trading) must be carefully determined.

– Switzerland must contribute to endeavours to establish and implement new international FATF standards to combat money laundering, terrorist financing and proliferation financing in such a way that detailed provisions do not divert its focus from the goal at hand.

Thanks to its financial market strategy, Switzerland can approach the numerous financial and tax-related challenges in a targeted and coherent manner.

Review and outlook

2010

25 February: Federal Council fleshes out new financial market strategy from end of 2009: consistently oriented towards managing taxed assets; improved market access abroad

1 March: State Secretariat for International Financial Matters (SIF) commences work: implementation of financial market strategy

30 September: Commission of Experts submits “too big to fail” final report to Federal Council

1 October: Administrative Assistance Ordinance on implementation of double taxation agreements (DTAs) in accordance with OECD standard enters into force

2011

18 March: Parliament authorises increase in Switzerland’s participation in IMF’s safety net (New Arrangements to Borrow) to around CHF 16 billion and granting of a loan worth slightly over CHF 700 million to IMF’s Poverty Reduction and Growth Trust

20 April: Federal Council presents dispatch on strengthening financial sector stability (too big to fail)

18 May: IMF Country Report gives Switzerland good marks for regulatory reform of financial sector as well as for budgetary, monetary and financial sector policy

1 June: OECD peer review: Switzerland allowed to progress to second phase subject to reservation

17 June: Parliament approves ten revised DTAs in accordance with OECD standard

6 July: Federal Council presents dispatch on Tax Administrative Assistance Act

31 August: Federal Council adopts dispatch on amending Stock Exchange Act (stock exchange offences and market abuse)

7 September: Federal Council adopts dispatch on total revision of Insurance Policies Act

21 September: Switzerland and Germany sign withholding tax agreement

25 September: Switzerland and Russia sign memorandum on financial dialogue and revised DTA

30 September: Parliament approves too big to fail bill
2011
3 October: Switzerland and India sign memorandum on financial dialogue
6 October: Switzerland and UK sign withholding tax agreement
26 October: Switzerland submits follow-up report on combating financial crime to FATF

2012
- Parliamentary deliberations on withholding tax agreements with Germany and UK, negotiations with other countries
- Resolution of administrative assistance issues with United States
- Clarification of company taxation issues with EU
- Parliamentary deliberations on IMF quota reform
- Resolution of Swiss IMF seat issue
- Institutional strengthening of FSB with headquarters in Basel
- Implementation of too big to fail bill
- Cooperation on further development of tax-related OECD administrative assistance standard
- Clarification of need for regulation of over-the-counter (OTC) trading in derivatives, etc.
- Implementation of FATF standards on money laundering, terrorist financing and proliferation financing
- IMF assessment program, peer reviews: Global Forum second phase, FSB peer review report
- Continuation of existing financial dialogue and preparation of further financial dialogue
International developments

Outlook

At around 3%, global economic growth is likely to continue to be modest in 2012. The International Monetary Fund is anticipating growth of around 5% for the emerging markets, and around 1% for the industrialised nations. The euro zone in particular is unlikely to post any growth. It is unlikely that sovereign debt burdens will be scaled down rapidly even in 2012. In Switzerland too, economic growth can be expected to slow further, while the consolidation trend in the financial centre is likely to persist.

Global economic growth slowed in 2011, with the International Monetary Fund (IMF) expecting a final global growth rate figure of around 4% (2010: 5.1%). Significant risks exist for the financial sector in the current economic environment, given the backdrop of heavily indebted nations and households.

In regional terms, there were considerable disparities. In the industrialised nations, the IMF is expecting the increase in gross domestic product (GDP) to fall well short of 2% (2010: 3.1%), in contrast to emerging and developing nations, which are expected to post a growth rate in excess of 6% (2010: 7.3%). In addition to negative events such as the natural catastrophe in Japan, the growth of the industrialised nations has been held back above all by the debt crisis in Europe and the lacklustre economic recovery in the United States. In 2011, the central banks of the largest industrialised nations once again pursued an exceptionally expansive monetary policy. Timely normalisation of monetary policy will be essential if inflationary risks and renewed asset price bubbles are to be avoided without curbing the economic recovery.

The precarious state of government finances, particularly in the affected members of the euro zone, cast a shadow over a number of financial institutions in 2011 in the form of actual and threatened losses in the values of their government bond holdings. At the same time, however, many of these institutions possess at least implicit state guarantees from the country in which they are domiciled. The vicious debt circle that this implies is a major problem for financial stability, as it means a build-up of significant risks in financial sectors even outside these countries due to the interconnectedness of the international financial system. Uncertainty over potential future losses also made it difficult for many financial institutions to refinance themselves in the market in 2011, with the European Central Bank having to make extensive amounts of liquidity available, for example.

The international community faces a major challenge, as dramatic consolidation of national budgets is necessary in many countries against a backdrop of a fragile global economic recovery. At the same time, the reforms of financial market regulation need to be implemented so as to strengthen global financial stability.

For an economy with a pronounced international orientation such as Switzerland’s, the difficult global economic situation also poses major challenges. The environment of subdued financial activity is likely to see the balance sheets of banks remain under pressure for a prolonged period, as well as trigger a process of consolidation. Against such a backdrop, the establishment of positive parameters for the financial sector becomes all the more important.

The precarious financial situation of a number of countries deteriorated further in 2011. In the euro zone, Portugal became the third country (after Greece and Ireland) to seek official assistance, while an agreement had to be reached on a restructuring of Greek debt (a “haircut”). In Italy and Spain too, developments took a further negative turn. The creditworthiness of the United States likewise came under pressure, as a political dispute over an increase to the debt ceiling brought the country within a whisker of default. In addition to the euro zone and the United States, Japan too is grappling with unresolved debt problems.

Public debt in % of GDP

Source: IMF
Financial market regulation

Outlook
One feature of 2012 will be global implementation of new financial market regulations. The FSB regulations for systemically important financial institutions which were approved by the G20 in November 2011 should be written into national law. This process is already far advanced in Switzerland. The revision of the Banking Act designed to strengthen financial sector stability (“too big to fail”) will enter into force in 2012, and will be fleshed out with ordinances. Politicians will have to decide whether – and to what extent – Switzerland should replicate the EU regulations in order to meet the third-country regime requirement, as well as how the issue of over-the-counter trading in derivatives should be regulated. Decisions are currently being reached by the FATF on the degree to which serious tax crimes should be considered money-laundering predicate offences which have to be reported. Furthermore, Switzerland is keen to agree a formal financial dialogue with China and other countries.

2.1 Overview
Switzerland’s financial centre makes a significant, albeit slightly declining, contribution to gross value added, employment and tax revenue (see Figure 2). In 2010, for example, financial intermediaries in the credit and insurance industry delivered value added of some CHF 58 billion. This equates to a 10.6% share of GDP, a slightly higher figure than in other major financial centres such as the United Kingdom (8.9%) and the United States (8.4%), but much lower than in Luxembourg (28.3%), for example. Studies show that the finance industry has been the key growth driver of the Swiss economy over the past 20 years, accounting for around a third of overall GDP growth. From a headcount perspective, some 212,000 people (expressed in full-time equivalents) were active in the Swiss financial sector at the end of 2010. This sector therefore accounts for 6.2% of overall employment.

The banks are key players in the financial markets, playing an intermediary role between the supply and demand side where capital is concerned. Switzerland had a total of 320 banking institutions in 2010, of which almost a half were foreign banks. Both companies and private households are reliant on a sufficient supply of credit funding, for which the financial centre acts as either supplier or intermediary. In mid-2011, the outstanding credit volume – i.e. the amount of credit from banks actually being used – amounted to more than CHF 1,000 billion. Three quarters of this amount related to domestic mortgage receivables. Strong competition between the many providers in the Swiss market results in low financing costs in the form of low interest rates and interest rate margins. A considerable degree of uncertainty exists in the real estate market, however, with respect to both future property price development and the level of risk assumed by the banks.

The restructuring and consolidation which is currently apparent in the banking sector could well accelerate in the future, not least as a result of various realignments within the industry. In addition to banks, insurers and pension funds also form part of the financial sector. In 2010, there were 248 insurance companies under regulatory supervision in Switzerland, and half of these were active in the property and casualty business (i.e. non-life). The capital investments of Swiss insurers amounted to some CHF 500 billion at the end of 2010. Almost half of this sum was invested in fixed-income securities. More than 2,300 pension funds are likewise important...
players in the Swiss financial centre. At the end of 2009, their invested capital amounted to just under CHF 600 billion, of which over a third was invested in bonds.

2.2 Competitiveness and ability to withstand crises

2.2.1 Ensuring and improving international competitiveness

The Swiss financial centre must remain competitive, and it is for the state to create favourable parameters accordingly. In addition to playing an active role in international bodies and institutions, the state continually monitors developments in other financial centres, and improves local parameters in Switzerland where necessary.

As part of this remit, the Federal Council wants to strengthen the international competitiveness of the Swiss financial centre sustainably by means of targeted measures to improve the general, regulatory and tax environment. In the regulatory area, particular focus is on adopting the dispatch on the total revision of the Insurance Policies Act, which dates back to 2 April 1908. The key objectives of this total revision are an alignment of insurance policies law with the changed parameters and requirements, and the need to ensure both a reasonable and feasible degree of protection for insured persons. The bill seeks to achieve a balance between the obligations of policyholders on the one hand and those of insurance companies on the other. The dispatch was adopted by the Federal Council on 7 September 2011.

In addition, the Federal Council also adjusted the Ordinance of 2 December 1996 on Stock Exchanges and Securities Trading as of 1 August 2011. Non-supervised foreign proprietary traders – i.e. securities dealers – who undertake short-term trades in securities in a professional capacity exclusively for their own account, will now also be admitted as members of a Swiss stock exchange subject to certain prerequisites being met. Thanks to this change, a competitive disadvantage of the Swiss financial centre was eliminated.

In the tax area, a longer-term optimisation of the Swiss tax system is being strived for, with the additional aim of eliminating (or at least minimising) market-distorting effects. To this end, the Federal Tax Administration (FTA) – as instructed by the Federal Council – has evaluated possible ways of financing the gradual abolition of stamp duty over a prolonged period of time. The FTA published its findings in a study in mid-2011. This study evaluates the impact of individual categories of stamp duty (issue tax, transfer tax and insurance tax) with respect to both their efficiency and their influence on the appeal of the Swiss financial centre. Viewed from this perspective, issue tax came off worse than transfer tax. The former should therefore be abolished first if there is the political will to do so.

As part of its work on the bill designed to strengthen financial sector stability (“too big to fail”, TBTF) in the autumn session of 2011, parliament set the initial course and resolved to abolish the issue tax on bonds and money market securities, and to exempt participation rights from the issue tax wherever these originate from the conversion of hybrid capital. Furthermore, at the end of August 2011, the Federal Council adopted a dispatch aimed at invigorating the Swiss capital market. This envisages changes to withholding tax with the aim of facilitating the issue of bonds under competitive conditions in Switzerland. These changes will also apply for the newly created CoCos (see section 2.2.3). As a result, CoCos (contingent convertible bonds) are bonds that are con-
the overall parameters for the Swiss capital market will be improved. Parliamentary treatment of this issue should be completed in 2012.

2.2.2 Early recognition of international developments

A mechanism for the early recognition of international developments is an important factor in the stability of the Swiss financial centre and its ability to remain competitive. In 2011, SIF initiated the development of an early recognition system in order to improve knowledge of other major international financial centres and thus enable Switzerland to follow international regulatory initiatives in the financial market area and their potential repercussions. The early recognition system is being developed in collaboration with other government departments (FDFA, embassies, FINMA, SECO, SNB) and the industry associations of the banks, insurance companies and investment funds. It consists of three pillars:

- Analysis of the structures, functions and developments of key competing financial centres in order to identify international developments and enable detailed consideration of the positioning of the Swiss financial centre.
- Mapping and monitoring of changes in international financial market regulations (Früherkennung Finanzmarktregelierung Ausland – FFA) with a view to identifying regulatory developments abroad at an early stage, as well as facilitating analysis and the elaboration of opinions by the Swiss authorities.
- Analysis and monitoring of international market indicators with potential repercussions for the Swiss financial market and financial centre as the key factors in anticipating crises and increasing the stability of the financial centre.

2.2.3 Reduction of systemic risks (“too big to fail”)

Systemically important financial institutions make a key economic contribution but represent a stability risk at the same time, as their collapse would entail unacceptable risks for the economy in question. This “too big to fail” problem is particularly pronounced in Switzerland, as the two big banks Credit Suisse and UBS have a dominant position in important business areas. What’s more, their total assets amount to many times Switzerland’s GDP, which means that the losses of either of these two systemically important banks could exceed the country’s financial capabilities. Hence there is the additional risk of “too big to be rescued”.

Back in the autumn of 2008, the Swiss Financial Market Supervisory Authority (FINMA) laid down capital requirements for the two big banks that significantly surpassed international standards, and introduced a leverage ratio\(^2\) In June 2010, a new liquidity regime was also agreed with these banks. On 20 April 2011, on the basis of proposals drawn up by a commission of experts, the Federal Council adopted the dispatch on the legislative proposal designed to strengthen financial sector stability. This was approved by parliament on 30 September 2011, which means it could enter into force at the beginning of March 2012.

The approved measures require a higher level of capital and contain rules for liquidity, risk diversification and organisational measures at the big banks. The basis for this is the Basel III supervisory standard of the international Basel Committee on Banking Supervision (see section 2.2.4). The measures in Switzerland go further, however. Depending on their size, market share and risk profile, the requirements for the two big banks – based on

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* In accordance with FSB proposal for SIFIs, see also Figure 5
figures at the end of 2009 – are for 19% of risk-weighted assets to be held in the form of equity in the narrowest sense (of which at least 10% common equity) and convertible capital to be held with strict requirements regarding capital quality and legal security (see Figure 4).

Organisational measures ensure the maintenance of systemically important functions (e.g. payment transactions, or the deposit and lending business) in the event of the insolvency of a systemically important bank. The combined impact of capital and organisational measures has a key role to play. If a systemically important bank’s capital ratio falls below a certain level, the emergency plan is generally triggered, i.e. the systemically important functions are ensured by transferring them rapidly to a new legal entity, for instance. To support this process, two new regulatory capital instruments have been created: reserve capital and convertible capital (CoCos). The purpose of CoCos is to ensure that the emergency plan can be implemented with a sufficient capital base.

Finally, a provision on the regulation of remuneration has been enshrined in legislation. If a systemically important bank becomes reliant on federal funding despite all the measures taken, the Federal Council will impose measures on their remuneration systems.

On the one hand, this comprehensive package has a preventive effect. It attempts to prevent insolvency by ensuring greater capital and liquidity cushions as well as better risk management. On the other, the emergency plan should ensure the continuation of systemically important functions in the event that insolvency nonetheless occurs. As a result, the bankruptcy of a systemically important bank should not drag down the entire economy. The distorting effect of a de facto state guarantee is greatly reduced as a result. This prevents a situation whereby the state (and therefore the taxpayer) would have to assume major financial risks in the future in order to bail out a systemically important bank.

2.2.4 Bank regulation in accordance with Basel III

On the basis of its findings following the recent financial market crisis, the international Basel Committee on Banking Supervision undertook a comprehensive revision of the existing Basel II standard. The new international standard requires banks to hold significantly more and higher-quality capital in order to absorb losses. Thanks to the revision of the Capital Adequacy Ordinance and the corresponding FINMA implementing regulations, this new standard is to be adopted by Switzerland and enhanced with transparent capital buffers that are specifically tailored to Swiss circumstances. The new requirements, which were elaborated by the authorities, the affected institutions and industry associations, will be more rigorous overall but also more transparent and more straightforward, and will allow for better risk controlling. The Swiss implementation of the new capital guidelines include the requirements drawn up under international mechanisms (“Basel pur”). On top of these come additional capital requirements as laid down by FINMA according to the size of the bank in question (Swiss supplements).

Most of the more than 300 banks operating in Switzerland already possess capital of sufficiently high quality to fulfil the more rigorous future guidelines. The greatest impact will be on Switzerland’s big banks, as the recent “too big to fail” legislation provides for more rigorous provisions for these institutions (see section 2.2.3).

In accordance with the transitional periods that apply to international standards, the Swiss Basel III guidelines are to enter into force on 1 January 2013. This will not complete implementation of the Basel III standard in Switzerland, however. In the future, banks will have to hold additional capital in the form of a variable anti-cyclical buffer, the size of which will change in line with the economic cycle. Within the scope of a hearing, the banks were able to put forward their views on this issue as well as on the implementation of the mortgage-related measures passed by the Federal Council on 17 August 2011 (stronger risk weighting for residential property). The implications of the introduction of the unweighted leverage ratio and the new minimum standards regarding liquidity risks are to be analysed in detail during initial observation periods. This should allow the identification and correction of any unintended consequences that may arise. The relevant draft revisions for Swiss banks will follow starting in 2012.
### International developments in the supervision of systemically important banks

At an international level and in significant financial centres, efforts are currently underway to regulate systemically important financial institutions (SIFIs). These developments are based on the new regulatory standard Basel III, which, among other things, imposes more stringent qualitative and quantitative requirements for the capital that must underpin risk-weighted assets (RWA). It is currently assumed that this standard will be adopted by all major financial centres. However, additional requirements will be needed for SIFIs in order to limit the risks they pose to financial stability.

<table>
<thead>
<tr>
<th>CH: Strengthening of financial sector stability</th>
<th>Additional capital requirement</th>
<th>CH: too big to fail</th>
<th>Additional organisational requirements</th>
<th>Regulation status</th>
</tr>
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<tbody>
<tr>
<td>The passing of the bill on the regulation of systemically important banks by parliament on 30 September 2011 made Switzerland a pioneer in addressing the “too big to fail” problem.</td>
<td>19% of RWA*, of which at least 10% to be held as common equity and the remainder in the form of CoCos.</td>
<td>- Emergency plan to ensure the continuation of systemically important functions in the event of a crisis.</td>
<td>Approved by parliament. Entry into force probable 01.03.2012.</td>
<td></td>
</tr>
</tbody>
</table>

| FSB: New standards for financial institutions | - In addition to Basel III, common equity of between 1% and 3.5% of RWA. | Basel III / FSB: | - Setting out international standards for national legal frameworks to safeguard the recovery and resolution of financial institutions. Requirements for the drawing up of emergency plans in a cross-border context. Regular review of resolvability by supervisory authorities. | Approved by the G20 on 04.11.2011. To be incorporated into national regulations. |

| USA: “Dodd-Frank Act” – restrictions for large commercial banks | Expected to adopt the FSB standards: additional common equity amounting to between 1% and 3.5% of RWA. | - Organisational requirements for commercial banks regarding the separation of proprietary trading and particularly high-risk business (“Volcker Rule”). | Entry into force on 21.07.2010. |

* Dependent upon the systemic importance of banks (calibration, as at end of 2009)
<table>
<thead>
<tr>
<th>EU: Alignment with FSB proposals and emergency measures</th>
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<tr>
<td>In its proposal of 20 July 2011 regarding the implementation of Basel III in the Capital Requirement Directive IV (“CRD IV”), the EU Commission purposely did not cover the SIFI regulation in view of the outstanding G20 decision in Cannes at the beginning of November. Within the EU, there is fundamental agreement that specific SIFI requirements are necessary. Moreover, 70 big European banks are obliged to build up a higher minimum cushion of pure equity by mid-2012. It is likely that CoCos will also be acceptable in this respect.</td>
</tr>
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</table>

| FSB: |
| – Expected to adopt the regulation of an additional 1% to 3.5% of RWA. |

| EU: |
| – Emergency measure to combat the debt crisis: 9% of RWA in the form of pure equity capital by mid-2012. |

| FSB: |
| – Likely alignment with proposals. |

| Regulation status |
| Proposal of a SIFI regulation which is similar to the FSB approach expected from the Commission soon. |

| GB: Ringfencing in accordance with the Independent Commission on Banking (ICB) |
| The United Kingdom will adopt the EU-wide SIFI regulations, which are still being drawn up. In addition, the ICB has presented its final report on the improvement of system stability and competition in the banking sector. The focus is on the organisational and legal separation of national retail business from investment banking. |

| EU: |
| – Implementation of regulation. |

| ICB: |
| – 17% to 20% of RWA at group level and at least 10% of RWA at retail bank level, partly as convertible capital. |
| – Leverage ratio of between 3% and 4.06%. |

| ICB: |
| – Ringfencing of retail area: the national (probably EMU-wide) retail business must be transferred to a subsidiary company. These units are subject to a ban on wider banking functions (proprietary trading, global retail business, etc.). |

| EU: |
| – Implementation of regulation. |

| D: Introduction of a bank levy |
| Germany too will adopt the planned EU-wide SIFI regulations. Furthermore, German has introduced a bank levy (as part of the restructuring law passed on 9 December 2010), whereby the basis for calculating the levy is the degree of systemic risk posed by the banks and their total assets. The corresponding revenue is to be channelled into a restructuring fund that can be used to wind up banks in emergencies. |

| EU: |
| – Implementation of regulation. |

| D: |
| – Bank levy to fund an ex ante fund to finance restructuring. |

| D: |
| – In an emergency, partial or complete transfer of bank functions to a “bridge bank” financed by the restructuring fund, with the possibility of re-transfer at a later stage. |

| EU: |
| – Implementation of EU regulation. |

| D: |
2.3 Market access

2.3.1 Regulation projects
The strengthening of the EU single market in the area of financial services continually presents new challenges with respect to market access for the Swiss financial centre and Swiss financial intermediaries. For example, in the area of collective capital investments, the Federal Council launched a standardised simplified prospectus (Key Information Document/KID) in mid-July 2011 in line with the UCITS IV Directive of 13 July 2009 (relating to collective investment in transferable securities), by adjusting the Ordinance on Collective Investment Schemes of 22 November 2006.

In addition, in view of the EU’s Directive on Alternative Investment Fund Managers (AIFMD), which entered into force on 22 July 2011, the Federal Council submitted a partial revision of the Federal Act of 23 June 2006 on Collective Capital Investment Schemes for consultation on 1 July 2011. The goals of this legislative adjustment are on the one hand to strengthen investor protection and the quality and competitiveness of the Swiss financial market, and on the other to ensure access to foreign markets for Swiss financial market players. To this end, the supervisory regime should be extended to all asset managers of Swiss and foreign collective capital investments. At the same time, the requirements for the management, custody and distribution of collective capital investments are to be aligned with the provisions of the AIFMD.

There are a number of other challenges facing Switzerland in the area of market access. In the aftermath of the recent financial crisis, both the United States (see also section 3.2.4) and the EU Commission have initiated a comprehensive reform of financial market regulation. The aim of the EU regulation initiative is to increase transparency and stability in EU financial markets when implementing the decisions of the G20. At the same time, the harmonisation and integration of the European single market for financial services is to be driven forward. EU financial market regulation is to be tightened, widened in scope, and adjusted in line with developments in the financial markets.

The regulation initiative comprises more than 25 individual regulations. Although there have been a number of projects delays relative to the announced timetable, all EU institutions are striving to implement the individual regulations by 2014 – with a transitional period allowed for national implementation.

Two regulation initiatives are of major importance for the further development of the EU financial market, and indirectly for Switzerland too. The revision of the MiFID (Markets in Financial Instruments Directive)\(^3\) one of the cornerstones of EU financial market regulation, is leading to adjustments to the principles and rules of conduct for the provision of financial services within the EU. The EU is also looking to improve transparency and financial stability in trading in over-the-counter (OTC, or non-exchange-traded) derivatives through the proposed European Market Infrastructure Regulation (EMIR). Among other things, the draft envisages the compulsory clearing of these instruments via central counterparties and the introduction of mandatory reporting.

The general increase in the level of regulatory rigour and the introduction of EU third-country rules are having an impact on Switzerland and its financial centre too. Switzerland is following these regulation initiatives carefully with a view to preserving its competitiveness, as the affected Swiss financial intermediaries will be able to access the EU financial market in the future only if they meet the prerequisites of the third-country regime under the EMIR and the revised MiFID. As the equivalence of Swiss law is a key condition for market access, the need for adjustment here should be investigated.

2.3.2 Bilateral agreements
Important components of the bilateral tax agreements signed with Germany and the United Kingdom in the autumn of 2011 (see section 3.2.3) are a protocol and a memorandum on market access and cross-border financial services. As a result, Switzerland was able to reduce the regulatory and administrative hurdles for market

\(^3\) The proposal of the EU Commission on 20 October 2011 for a revision of the MIFID involves on the one hand the overhauling of the MIFID itself, and on the other a new ordinance entitled «MiFIR» (Markets in Financial Instruments Regulation).
access in Germany and eliminate certain ambiguities surrounding market access in the United Kingdom for Swiss financial institutions. However, it was possible to address certain country-specific regulatory hurdles. Responsibility for general market access regulations lies with the EU Commission.

In the case of Germany, the existing mandatory requirement for a client relationship to be initiated via a local bank or bank branch will now lapse. The largest obstacle to market access has thereby been eliminated. In order to facilitate the cross-border sale of financial products, Germany and Switzerland have recognised the UCITS conformity of German and Swiss securities firms in a corresponding protocol. This recognition should facilitate approval for the distribution of German investment products in Switzerland, and vice versa. The necessary technical aspects are due to be regulated through an implementation agreement between the supervisory authorities of both countries.

In the case of the United Kingdom, a memorandum has been drawn up which sets out the relevant modalities for the opening of new accounts, the acquisition of new clients, and the management of existing clients. This creates the necessary legal transparency for Swiss banks to establish and maintain an active presence in the British market.

2.4 Financial market integrity

2.4.1 FATF
Switzerland is at the very forefront of international efforts to tackle cross-border financial crime, and has effective mechanisms at its disposal for combating money laundering and terrorist financing. As a founding member of the Financial Action Task Force (FATF), Switzerland is committed to ensuring effective and practicable international standards in the 34 member countries.

The FATF has been working on revising its international recommendations since the end of 2009. This revision, which is nearly complete, involves more than half of the 49 current recommendations, which are also to be restructured. As Switzerland is co-chair of the working group tasked with coordinating the revision, it was well able to preserve its interests. Within the scope of the revision, preventive measures were dealt with. Switzerland managed to prevent the abolishment of bearer shares and establish a level playing field concerning the transparency of legal persons and legal structures such as trusts. The revision will have an impact on the exchange of financial information between the Money Laundering Reporting Office Switzerland (MROS) and its foreign counterparts.

Serious tax crimes are now also to be considered predicate offences for money laundering. Accordingly, financial intermediaries would have a mandatory duty to report any suspicious cases to the authorities. However, member states have a certain freedom of manoeuvre when it comes to implementation in national legislation. Every country can essentially arrive at its own definition of a serious “tax crime”. In the interests of efficient implementation of the FATF rulings, Switzerland is opting for a narrow definition of serious tax crime. The main objective from the Swiss perspective is not the criminalisation of as many tax offenders as possible, but the efficient combating of money laundering.

The results of these endeavours, which also involved consultation with the private sector, are expected to be passed as an overall package by the Plenary Meeting (the decision-making body of the FATF) in February 2012 and implemented by 2013. Subsequently, in the course of conceptual work on assessing the effectiveness of anti-money laundering systems, a detailed evaluation methodology will be prepared.

The FATF continued its member state evaluations as part of its third evaluation cycle. This round was completed in 2011. A fourth evaluation cycle should commence at the end of 2013. Switzerland is actively campaigning for peer reviews of evaluations and for subsequent post-evaluation controlling in order to ensure equal treatment and a level playing field.

Effective since 2008, the FATF is also tasked with examining measures to counter the financing of the proliferation of weapons of mass destruction. Switzerland is campaigning for more effec-
tive export controlling systems as the key instrument in the fight against proliferation financing. At the start of 2012, the FATF will adopt a new standard on proliferation financing with a view to specifying the corresponding financial sanctions as adopted by the UN Security Council.

The FATF is preparing a renewal of its current mandate (2004–2012). The new mandate (2012–2020) is expected to be adopted during a ministerial meeting in April 2012. Switzerland is committed to rationalised governance of the body. It advocates having the new mandate focus on the implementation and consolidation of the standards already adopted rather than on the development of new standards. This should ensure that the processes for verifying implementation of the standards continue to guarantee transparency and equal treatment.

2.4.2 Other organisations in the area of combating money laundering and terrorist financing

Numerous international institutions conduct peer reviews among their members. In the context of the fight against corruption, these include the OECD, the European Council and the UN. An important player in the area of the exchange of information in tax matters is the Global Forum on Transparency and Exchange of Information for Tax Purposes (see section 3.4.2), while the Financial Stability Board (FSB) should also be mentioned in the area of financial stability (see section 4.3). Consequently, the concept of “communicating vessels” has emerged, whereby the results of different evaluations are taken into account in the analyses of the FATF, and vice versa.

Switzerland participates actively in specialised international discussions on terrorist financing. For example, it contributed in 2011 to the initiative launched by the UN Security Council’s Counter-Terrorism Committee Executive Directorate (CTED) aimed at globally strengthening national policies designed to prevent abuse of the charitable sector for the purposes of terrorist financing. Finally, Switzerland is working to deliver improvements to global sets of anti-money laundering measures by making a substantial contribution to financing the IMF’s trust fund for combating money laundering.

Switzerland also contributes to the effective deployment of available resources through its involvement in the Steering Committee.

**World Bank report: How corrupt assets are hidden**

A report prepared by the World Bank examined 150 cases of corruption in a selected number of countries worldwide. As part of these cases, over 800 corporate vehicles were used to conceal corrupt assets. The highest number of such corporate vehicles was found in the United States (102), while seven were based in Switzerland (see table). The report also shows that 76 of the corporate vehicles had a bank account in Switzerland, while 107 had one in the United States.

The report also addressed how easy it is to set up such a corporate vehicle without naming the beneficial owner. 41 of just over a hundred trust and company service providers failed to undertake sufficient due diligence. For example, only 3 of the 27 US service providers reviewed asked for clear identity documentation. In the remaining sampled OECD countries, the figure was 9 out of 20 respondents.

<table>
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<th>Number of corporate vehicles per country</th>
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<tr>
<td>United States</td>
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<td>British Virgin Islands</td>
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<td>Panama</td>
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<td>Cayman Islands</td>
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2.4.3 Amendment of the Stock Exchange Act (stock market offences and market abuse)

On 31 August 2011, the Federal Council approved the dispatch on amending the Stock Exchange Act (stock market offences and market abuse). As a result of the amendment, norms will be created in the area of both criminal law and supervisory law that sanction market abuse efficiently and take account of international regulations. This should strengthen the integrity and competitiveness of Switzerland’s financial centre.

At the criminal law level, the constituent elements of insider trading in particular will be extended and stated more precisely. Those of price
manipulation will largely be maintained. Both offences will be transferred from the Criminal Code and written into the Stock Exchange Act. In compliance with the FATF Recommendations, the criminal acts of insider trading and price manipulation will be considered as crimes in serious cases.

In addition, insider trading and market manipulation will now be prohibited under supervisory law for all market participants. In order to enforce the aforementioned bans and the provisions on the disclosure of holdings, the Swiss Financial Market Supervisory Authority (FINMA) will now be able to apply certain supervisory instruments to all market participants. Furthermore, the enforceability of the provisions on the disclosure of holdings will be improved, and the possibility of paying a control premium will be abolished.

2.5 Cooperation

Financial dialogues

For a number of years now, the FDF has been conducting financial dialogues with selected countries such as Japan, Germany and France. The aim of these dialogues is to forge close contacts with the relevant authorities of the partner state in question. These in turn help to identify and implement shared interests, for example in the area of financial market policy or financial market regulation, and facilitate mutual coordination in international financial forums (e.g. the IMF, FSB). The improved information situation regarding future national and international developments also helps to sensitize partner states to issues of concern to Switzerland and improve early-warning mechanisms. Furthermore, the financial dialogues offer a framework for starting negotiations with the partner state in question on market access for the financial sector (see section 2.3.2) or on tax issues, for example. On the basis of its positive experiences to date, the FDF is continuing to pursue existing financial dialogues, and is also initiating financial dialogues with new partner countries – particularly with emerging market countries, as their international relevance and interconnectedness with the Swiss economy are very much on the rise. Within the scope of the financial dialogues initiated with Russia and India, an appropriate framework for structured and ongoing dialogues was established in 2011 with the signing of a corresponding agreement (Memorandum of Understanding, MoU) in each case.

There has also been a lively exchange of ideas between Switzerland and China with a view to establishing a formal bilateral financial dialogue. On 9 November 2011, the Federal Council approved an MoU for a financial dialogue between Switzerland and China. The first contacts with Australia and Brazil were likewise forged in 2011. These financial dialogues are managed by the FDF. SIF coordinates Switzerland’s positioning in financial issues together with other federal departments.

Industry bodies and authorities

The recent financial crisis showed the importance of smoothly-functioning cooperation between authorities. In January 2011, the FDF, the Swiss National Bank (SNB) and FINMA signed a joint MoU on cooperation. The MoU covers the exchange of information on financial stability and financial market regulation issues, as well as collaboration in the event of a crisis unfolding which could potentially threaten the stability of the financial system. The corresponding responsibilities and powers of the three authorities are enshrined in legislation, and are not changed by this MoU.

In addition, cooperation between the individual authorities was also improved through the “Financial Market Policy” interdepartmental working group. This working group is chaired by SIF’s State Secretary. In addition to the FDF, the FDFA, DEA, FDJP, SNB and FINMA are also represented in this group. Finally, the cooperation between the Swiss financial centre, the authorities and the regulators initiated in 2008 with a view to improving the parameters and increasing the competitiveness of the Swiss financial centre was successfully continued. Authorities and industry representatives meet regularly to hold talks. This institutionalised dialogue with the finance industry (“Financial Centre Forum”) is likewise chaired by the State Secretary of SIF.
3
International tax matters

Outlook:
Implementation of financial integrity strategy
International pressure on Switzerland to cooperate more closely in the fight against tax offences has increased further. Switzerland has no desire to oppose initiatives in this sphere, and is continuing to implement the OECD standard for provision of administrative assistance. Switzerland’s existing framework for providing administrative assistance will probably be reviewed at the end of 2012 as part of the second phase of the peer review of the Global Forum on Transparency and Exchange of Information for Tax Purposes (Global Forum). A resolution to the tax problems of the past is also being worked out with the United States. Furthermore, in its efforts to ensure fair tax mechanisms, Switzerland has put forward a credible and efficient alternative to the automatic exchange of information in tax matters. The withholding tax agreements signed with Germany and the United Kingdom are due to be ratified and should enter into force in 2013; similar agreements are likely to be concluded with other nations.

3.1 Overview
With the signing of withholding tax agreements with Germany and the United Kingdom, a solution was reached which respects the privacy of bank clients on the one hand while ensuring that the legitimate tax claims of Switzerland’s partner countries are met on the other. The signing of these two agreements also represents a firm step in the implementation of the Federal Council’s strategy for the Swiss financial centre. Switzerland is prepared to sign agreements of this kind with other countries too. Moreover, Switzerland has made significant progress in terms of recognizing and adopting the international standard for the provision of administrative assistance in tax matters. Where company taxation is concerned, the emphasis is on ensuring the ongoing appeal of Switzerland as a business location with a competitive tax burden, taking into account the financing requirements of the Confederation and the cantons, as well as international acceptance.

3.2 Bilateral cooperation

3.2.1 Double taxation agreements in line with OECD standard
The OECD has drawn up an international standard for tax cooperation to which its member states are expected to adhere (see section 3.4.1). In March 2009, the Federal Council decided to extend administrative assistance in tax matters and to include the corresponding Article 26 of the OECD Model Convention when negotiating new double taxation agreements (DTAs), as well as to revise existing DTAs accordingly. Since then, such an administrative assistance provision has been initialled in a DTA by more than 40 countries (as at 31 December 2011). At the same time, numerous agreement provisions have been improved (e.g. the reduction of withholding tax rates for dividends, interest and royalty payments), certain discriminatory provisions have been removed, and arbitration clauses have been negotiated.

By the end of 2011, parliament had approved more than 20 agreements with administrative assistance provisions in accordance with the new standard. Most of these have already entered into force. Switzerland is prepared in principle to adopt a standard-compliant administrative assistance provision in all its existing double taxation agreements, as well as include such a provision in any future agreements. Overall, Switzerland has DTAs with approximately 80 states.
**DTAs with administrative assistance in accordance with new standard**

**Agreements in force (20)**
Austria Luxembourg
Canada Mexico
Denmark Netherlands
Faroe Islands Norway
Finland Poland
France Qatar
Germany Spain
Greece United Kingdom
India Uruguay
Japan Chinese Taipei (Taiwan)

**DTAs approved by parliament (3)**
Kazakhstan Turkey United States

**Signed DTAs (9)**
Hong Kong Slovakia
Malta South Korea
Romania Sweden
Russia United Arab Emirates
Singapore

**Initialled DTAs (10)**
Australia Ireland Slovenia
Bulgaria Oman Turkmenistan
Colombia Peru
Czech Republic Portugal
(As at 31.12.2011)

3.2.2 International tax administrative assistance – implementation in domestic law

The administrative assistance clauses of the individual double taxation agreements (see section 3.2.1) form the legal foundation for the exchange of information between Switzerland and the relevant contracting state. The way in which administrative assistance will be organisationally executed is to be covered by the Federal Act on International Administrative Assistance in Tax Matters (Tax Administrative Assistance Act). The Federal Council adopted the corresponding dispatch on 6 July 2011. The Tax Administrative Assistance Act should replace the Federal Council Ordinance on the Provision of Administrative Assistance in Accordance with DTAs which came into force in October 2010. It governs the provision of administrative assistance under DTAs and other agreements for the exchange of information in tax matters with respect to both foreign and Swiss requests for administrative assistance. Like the Administrative Assistance Ordinance, the Tax Administrative Assistance Act sets out how and from whom the requested information is to be procured, the form in which the transfer of information is to take place, the parties to be informed about requests for administrative assistance, and to whom rights of participation and appeal will be assigned.

3.2.3 International withholding tax

As part of the implementation of the Federal Council’s strategy to regularise untaxed foreign assets held in Switzerland, while at the same time preserving the privacy of bank clients, joint declarations were signed with both Germany and the United Kingdom at the end of October 2010, in both cases announcing the intention to

### Figure 7

#### Regularisation of the past

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<th>Written authorisation</th>
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<td>Bank levies tax at source</td>
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| Bank reports account information to FTA |
| Bank transfers tax amount to FTA |

| FTA reports account information to partner state Regularisation |
| FTA transfers tax amount to partner state Regularisation |

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<th>Withdrawal to third country</th>
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<td>No regularisation</td>
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### Figure 8

- **Voluntary reporting**
- **Anonymous payment of tax**
- **Close account**
- **Written authorisation**
- **Bank levies tax at source**
- **Bank reports account information to FTA**
- **Bank transfers tax amount to FTA**
- **FTA reports account information to partner state Regularisation**
- **FTA transfers tax amount to partner state Regularisation**
- **Withdrawal to third country**
- **No regularisation**
conduct negotiations on outstanding financial and tax matters. Negotiations on a final withholding tax commenced with both partner countries at the start of 2011, leading to the formal signing of agreements with Germany (on 21 September 2011 in Berlin) and the United Kingdom (on 6 October 2011 in London). This represents a solution that respects the privacy of bank clients on the one hand, while ensuring that the legitimate tax claims of the partner states are fully met on the other. In order to take account of individual objections from the EU Commission with respect to the compatibility of these withholding tax agreements with the Swiss-EU agreement on the taxation of savings income, Switzerland is still clarifying various aspects together with Germany and the United Kingdom.

Under the agreements, persons resident in Germany or the United Kingdom can retrospectively have their existing bank relationships in Switzerland taxed either by making a one-off tax payment or by disclosing their accounts. In order to ensure that a minimum sum is raised through this regularisation of the past, while at the same time underlining their firm intention to implement the agreements, Swiss paying agents have committed to an advance payment to the two partner countries in question. This sum will be netted off against payments from bank clients to regularise the past, thereby reimbursing the Swiss paying agents.

Once the agreements enter into force, any future capital gains and capital income relating to the assets of persons domiciled in Germany or the United Kingdom will also be subject to a final withholding tax. The proceeds of this tax will be forwarded by Switzerland to the relevant authorities in the partner country.

The rates for this tax will be based on the relevant tax rates applicable in Germany and the United Kingdom respectively, in order to avoid the distorting effect of tax competition.

To ensure that each agreement meets its objectives, Switzerland has agreed with the two partner countries a clause for providing information on request. This will allow German and British authorities to submit a request for administrative assistance to Switzerland in which the name of the client is stated, but not necessarily the name of the bank. The number of requests for assistance will be subject to an annual limit. In all cases, applications for assistance must be backed by reasonable grounds. So-called “fishing expeditions” are not permissible.

In addition, the problem of potential purchases of tax-relevant data and the criminal prosecution of bank employees has been resolved. Accordingly, the partner countries no longer see any reason for the purchase of illegally acquired bank client data. Furthermore, they will typically refrain from launching criminal proceedings against bank employees for participating in tax offences, and have declared that the criminal prosecution of bank employees for participating in such offences relating to the past is extremely
improbable. Finally, the agreements state that the agreed system will have a long-term impact which is equivalent to the automatic exchange of information in the area of capital income.

In addition, it has been agreed with both partner countries that the cross-border provision of financial services should be simplified (see section 2.3.2). Both agreements require approval by the respective parliaments of the countries involved, and are expected to enter into force at the start of 2013. The ratification process is currently underway in the contracting states. A particular topic of discussion during this process is the issue of compatibility with areas of EU responsibility. Switzerland is prepared to discuss this model with other interested countries too. Negotiations with Greece are expected to commence soon, for example.

3.2.4 United States
Switzerland has been holding talks with the United States on unresolved tax issues for more than a year. These talks relate to the US investigations into alleged infringements of US tax legislation by Swiss banks and the potential handover of client data. Under Swiss law, client data may be handed over as part of an administrative assistance procedure at federal level, but not directly by a bank. The objective of the negotiations with the US authorities is to find a solution that is compatible with Switzerland’s current legal framework.

The cases of the directly affected banks are to be dealt with through requests for administrative assistance: in the case of tax fraud in accordance with the existing double taxation agreement (DTA) of 1996, and in the case of both tax fraud and tax evasion in accordance with the new – but not yet ratified – DTA of 2009. Under the existing DTA, requests for assistance are possible even without the provision of specific names or personal details, as long as an alternative form of identification is supplied. Applications on the basis of specific patterns of behaviour should also be possible under the new DTA without the provision of specific names or personal details. However a decision has yet to be made by Swiss parliament in this respect.

At the same time, a global solution is being sought that will apply to the entire Swiss financial centre and thereby put the past to rest. Another development geared to the future is the US “Foreign Account Tax Compliance Act” (FATCA), which was passed by Congress in March 2010. This legislation is designed to ensure comprehensive worldwide reporting on US taxpayers who hold bank accounts and assets with financial services providers outside the United States. The US authorities have set out a staggered time-frame for the implementation of this Act (expected to apply from 1 January 2014 onward). Given its significant international activity, particularly with the United States, Switzerland will be greatly affected by this legislation.

FATCA envisages the imposition of a withholding tax of 30% on all payments of dividends, interest, sales proceeds, etc. from the United States to a foreign financial institution, irrespective of whether the financial institution in question is accepting payment on behalf of a US taxpayer, another client or indeed itself. To avoid payment of this withholding tax, a financial institution must sign an agreement with the US tax authority (the IRS) in which it accepts comprehensive reporting obligations with respect to all clients who are liable to pay US taxes. This will involve a substantial amount of administrative work. After the Federal Council instructed the FDF to initiate discussions, SIF made it clear to the US authorities during a number of different meetings that the implementation of FATCA had to take account of the concerns of the financial institutions that would be affected. Modalities for a simplified implementation of FATCA will be sounded out within the scope of talks on general financial issues.

3.3 European Union
3.3.1 Company taxation
Company taxation is an important component of international competition among business locations. The receipts from the profit taxes of legal entities make an important contribution of the financing of the Confederation’s and cantons’ government expenditure. However, the attractiveness of Switzerland’s company taxation is also causing its international acceptance to be jeopardised. The EU takes exception to the inequality in the tax treatment of domestic and foreign revenues in certain cantons. Switzerland,
for its part, is firmly committed to open tax competition. However, it is prepared to enter into discussions with the EU on certain company taxation issues. Back in 2007, the EU Commission criticised certain cantonal tax practices as constituting “illegal state aid”, arguing that such practices distort free competition and breach the Free Trade Agreement which dates back to 1972. The Federal Council has always rejected this interpretation. A compromise solution proposed in 2009 fell through following resistance from certain EU member states.

In June 2010, the EU put forward a proposal to Switzerland to cultivate a dialogue on the so-called “Code of Conduct” on company taxation. This Code of Conduct obliges EU member states to campaign on a political level against damaging competition in the area of company taxation. The focus is on tax provisions and tax practices that in certain situations lead to significantly lower effective taxation than is customary in the relevant member state.

In August 2010, the Federal Council instructed the FDF to enter into exploratory talks with the EU Commission on a potential dialogue regarding this Code of Conduct. Together with the other departments concerned, SIF has entered into preliminary discussions with the Taxation and Customs Union Directorate-General (TAXUD), a process that has also involved the individual cantons. The aim is to set out the relevant prerequisites for any dialogue and to clarify the relationship with the dialogue conducted so far on certain cantonal tax practices. Such a dialogue will focus on so-called “ring-fencing”, i.e. the unequal treatment of domestic and foreign revenues. At the end of October 2011, convergence was achieved with the EU on key framework conditions for the actual dialogue. A definitive agreement on its initiation is foreseeable. The cantons will be consulted on this issue before the Federal Council makes a decision.

In November 2011, the OECD Forum on Harmful Tax Practices, which is part of the OECD Committee on Fiscal Affairs, also made another attempt to examine special rules for company taxation. An initial selection of 27 regimes was chosen for further investigation based on reports from member states. The selection includes several Swiss tax regimes, some of which have been criticised previously by the EU Commission. Within the scope of its activities, the forum takes care to coordinate its work with that of the EU and the Global Forum (see section 3.4.2).

3.3.2 Other EU tax issues
The EU is currently working on eliminating the loopholes in the applicable Savings Tax Directive. On the one hand, further financial instruments (e.g. security-like debt claims, certain life insurance products and structured products) should be taxed. On the other, circumvention of the directive by using legal entities as intermediaries should be prevented. Switzerland is prepared, under certain conditions, to adapt the bilateral agreement on the taxation of savings income with the EU when the EU has completed its revision of the Savings Tax Directive. For Switzerland, the automatic exchange of information is still not up for discussion.

In addition, the EU is considering concluding agreements with a number of third-party countries – including Switzerland – on administrative assistance in tax matters in accordance with the OECD standard (see section 3.4.1). The corresponding negotiation mandate has yet to be issued, however. Switzerland is at a very advanced stage in the implementation of the OECD administrative assistance standard as part of double taxation agreements (see section 3.2.1). It has agreed the corresponding administrative assistance clauses with numerous EU member states. An administrative assistance agreement with the EU therefore appears unnecessary from the Swiss standpoint.

3.4 Multilateral cooperation

3.4.1 OECD

OECD Tax and Development
In January 2011, the OECD launched a three-year programme designed to help developing countries mobilise their resources to ensure the proper and reasonable levying of taxes. As a central platform, the Informal Task Force on Tax and Development was established with the involvement of OECD tax and development experts as well as
representatives from developing countries, the business sector, NGOs and international organisations. Switzerland is a member of the task force and is committed to ensuring that the needs of developing countries are taken into account within the scope of the programme’s four focal topics. Switzerland will also make a voluntary contribution to such endeavours. Education and the establishment of a viable administration are Switzerland’s priorities. Also important for Switzerland, however, is ensuring that the rules to be applied to developing countries can be implemented. Switzerland advocates a simplification of transfer pricing in relation to developing countries, but without abandoning the key principles of the OECD. In the area of reporting requirements for companies operating internationally, Switzerland is promoting purpose-oriented transparency in a way that accommodates the interests of both the tax authorities and companies.

OECD administrative assistance standard and the OECD/European Council’s multilateral convention on administrative assistance

The OECD has drawn up an international standard for administrative assistance in tax matters to which both member and non-member states are expected to adhere. This standard, set out in Article 26 of the OECD Model Convention and in the model Tax Information Exchange Agreement (TIEA), stipulates that countries must, on request, exchange tax information of any kind and description that is required to enforce the domestic laws of the requesting country. This international standard does not, however, constitute an obligation to provide administrative assistance on an automatic or spontaneous basis. “Fishing expeditions” are not permissible. The OECD is currently revising the commentary to Article 26 of its Model Convention so that group requests should also be permitted in addition to individual requests. For group requests, unlike individual requests, taxpayers are identified in the request by a description of certain patterns of behaviour, and not by name or similar identification criteria. By contrast, “fishing expeditions”, i.e. random requests unrelated to an ongoing tax investigation are still impermissible. The new commentary is expected to enter into force in mid-2012.

The Convention on Mutual Administrative Assistance in Tax Matters of 25 January 1988 (multilateral convention), which OECD and European Council member states may join, goes beyond the international standard in some areas. The convention obliges participating states to provide administrative assistance on a spontaneous basis. Moreover, it also contains provisions on the automatic exchange of information, timetables for tax audits, participation in tax audits abroad and assistance in enforcement, although reservations are possible in these areas. The convention was amended by a protocol on 27 May 2010, and now provides for mandatory retroactivity in cases of tax fraud. Switzerland has not signed the convention. The OECD and the Global Forum recommend joining the multilateral convention, which is likely to represent the international standard in the medium term. At the G20 summit in November 2011, the G20 states signed the convention or announced their intention to do so.

3.4.2 Global Forum on Transparency and Exchange of Information for Tax Purposes

The Global Forum is responsible for reviewing compliance with the OECD standard in the area of transparency and the exchange of information for tax purposes by means of so-called “peer reviews”. The Global Forum encompasses the G20 countries, all OECD countries, as well as all other countries that have committed to the OECD standard in the area of administrative assistance. Consisting of more than 100 member states, the Global Forum may also review the jurisdictions of non-member countries. Switzerland is actively involved in the various bodies of the Global Forum.

The peer review is broken down into two phases. The first phase focuses on whether tax-relevant information exists and is available to the national authorities. Another aspect of this phase involves establishing whether the necessary legislative basis exists for the cross-border exchange of such information between the relevant national authorities. The second phase focuses above all on reviewing the effectiveness and efficiency of the information exchange process in practice.
The Global Forum approved the first phase of the peer review report on Switzerland on 1 June 2011. The report certifies that Switzerland has made “important changes” regarding administrative assistance. Just like many other countries, Switzerland does not fully meet all the criteria stipulated. In particular, the report concludes that the identity of holders of bearer shares cannot be determined in all cases under Swiss legislation, and that the requirements for identifying the relevant taxpaying individuals and information holders (e.g. banks) remain too restrictive in requests for information. With respect to the Global Forum’s recommendation regarding the identification of the affected taxpayers and information holders, Switzerland has already made the necessary adjustments in order to comply fully with the standard.

The second phase of the peer review report on Switzerland is envisaged for the end of 2012, as long as a significant number of agreements that meet the international standard have been approved by then. In addition, in keeping with the terms of the review procedure, Switzerland must present a status report on the measures it intends to take to improve the unfulfilled criteria within six months of the report being approved by the Global Forum, with a more detailed written report to follow within 12 months. In both cases a re-evaluation may take place after the Global Forum has reviewed and assessed the measures taken by Switzerland.

3.4.3 UN

One of the tasks entrusted to the 25-member UN Committee of Experts on International Co-operation in Tax Matters is the alignment of the UN Model Convention on double taxation with recent developments. Another is to coordinate dialogue on the strengthening of international cooperation in tax matters, above all between countries in the developing world and those of the industrialised world. The revised Model Convention and its commentary are expected to be published in 2012. At last year’s meeting, the UN Committee of Experts continued its revision of the commentary to the Model Convention, focusing in particular on the following topics: unwarranted recourse to the convention, attribution of profits to permanent establishments, the meaning of the term “beneficial owner” for the purposes of the convention and the tax treatment of services.
International financial system

4.1 Overview

The current state of the global economy and the financial markets presents the IMF and the FSB with a number of exceptional challenges. Switzerland is making an active contribution to the key discussions of the IMF’s Executive Board and the FSB.

There were changes at the top of both institutions during 2011. In the case of the IMF, the former French Finance Minister Christine Lagarde was appointed Managing Director. At the FSB, the incumbent Governor of the Canadian National Bank, Mark Carney, was appointed the new Chairman.

The G20 played a rather less prominent role in 2011 than in the previous two years. At a political level, there were no changes in Switzerland’s relationship with the G20. At a bilateral and technical level, by contrast, there were important contacts: Switzerland was invited to a host of high-ranking G20 events, such as the conference on the reform of the international monetary system in Nanjing (March 2011) and the conference on commodities and derivatives trading in Istanbul (September 2011).

When it comes to international financial and monetary issues, as well as the monitoring of the financial system, Switzerland is heavily involved in key discussions through its position in the IMF and the FSB. In order to underpin this commitment through the bilateral route, working papers with proposals were drawn up for the issues which were of most importance to Switzerland (international monetary system, strengthening of the ministerial committee of the IMF, combating corruption, commodity trading) for the period of the French G20 presidency, with discussions with both G20 and non-G20 nations.

4.2 International financial and monetary issues

The IMF must ensure that financial and monetary developments are carefully monitored, in individual member states and the financial and monetary system as a whole. At the same time, the IMF is the key body for evaluating the implementation of lending programmes in countries such as Greece, Ireland and Portugal. Finally, it makes important contributions to ensuring macroeconomic stability in the emerging markets and in low-income countries. In all these areas, Switzerland works to ensure that the IMF has an appropriate toolkit and the appropriate institutional setup.

4.2.1 IMF reforms

In December 2010, the IMF members passed a resolution to reform the IMF quotas and governance. As part of this reform, the regular resources of the IMF – which are provided through the quotas of individual member states – are to be doubled. At the same time, there will be a shift of approximately 6% of the overall quota to dynamic emerging market and developing countries (EMDCs). The quota increase will take effect as soon as it is ratified by a qualified majority of IMF members. This is expected to be the case at the end of 2012 at the earliest. A corresponding bill was submitted to the Swiss parliament at the end of November 2011.
Another development to emerge from the reform of IMF quotas and governance is the reallocation of two Executive Board seats currently held by advanced European countries to the EMDCs. The specific details of this redistribution have yet to be determined. Switzerland is of the opinion that adequate representation in the IMF Executive Board is justified on the basis of the size and significance of its economic and financial centre, the importance of the Swiss franc, and the role of Switzerland as a financial contributor to the IMF and as a “bridge” between Europe and Central Asia/ the Caucasus. Switzerland is seeking to strengthen collaboration in the constituency and expand the group where possible.

During the Annual Meetings of the IMF in September 2011, IMF Managing Director Christine Lagarde put forward an action plan containing proposals to adjust the toolkit of the IMF so as to improve support to member countries and strengthen the international financial and monetary system. The underlying objective is to ensure that the lessons learnt from the recent financial and economic crisis are taken into account to a greater extent.

The surveillance work of the IMF was scrutinised more closely in 2011 in the “triennial surveillance review”. Switzerland considers a strengthening of the IMF’s surveillance work to be crucially important. Given the exceptional
challenges posed by the crisis, the IMF should play a key advisory role vis-à-vis its members. At the same time, it should be ensured that the IMF acts as the principal body in the discussion of systemically important issues.

In 2011, the IMF dedicated considerable time to the question of how far it might take on a greater insurance role in order to protect countries from “contagion” through the international financial system. Switzerland takes a rather sceptical stance with respect to the further expansion of the IMF’s insurance role. The main reason for this stance is the fact that insurance lines (and in particular the FCL, or Flexible Credit Lines) already tie up significant IMF resources which are supposed to be available to combat extraordinary emergencies.

4.2.2 Lending by the IMF
Loan commitments under current IMF programmes reached a peak of around USD 250 billion in 2011. This reflects the current situation in the financial markets and the global economy, with substantial risks of a growth slump in the United States and a further intensification of the debt crisis in the euro zone.

Some 26 countries pursued loan programmes with the IMF in 2011. The main loan programmes were those involving Greece, Ireland, Portugal, Romania and the Ukraine. The programme with Iceland was successfully completed in 2011. The IMF’s flexible credit lines (FCLs) agreed with Mexico, Poland and Colombia were once again extended by a year as well as increased in 2011. Low-income countries also experienced a significantly higher need for financing as a result of the financial crisis. In 2011, almost 30 countries pursued programmes with the IMF through the “Poverty Reduction and Growth Trust” (PRGT). This entailed credit commitments amounting to some USD 4 billion, with an interest rate remaining at 0% until the end of 2011.

4.2.3 IMF funding
The IMF’s regular resources are provided by its members via the so-called quota system. These quotas can be called on by the IMF as needed. They earn interest at the prevailing market rate and are typically provided by countries’ central banks.

In recent decades, the regular resources of the IMF have grown much less strongly than the volume of global financial flows. Apart from an increase of just under 10% in the wake of the 2008 reform, the regular funds of the IMF have remained unchanged since 1998.

Following a depletion of the IMF’s available funding due to commitments resulting from the ongoing financial and economic crisis, a multi-phase augmentation of the IMF’s resources was decided on in the spring of 2009. At the end of 2010, a doubling of total quotas was agreed as part of the reform of the IMF’s quotas and governance. This will be submitted to the Swiss parliament for ratification in 2012. In 2011, the revision and augmentation of the safety net of the IMF (which was likewise initiated in 2009) was ratified by the IMF’s members, including Switzerland. Shortly after entering into force, these so-called “New Arrangements to Borrow” (NAB) were fully activated by NAB members in April 2011.
Under the NAB, the 40 participating countries provide the IMF with resources totalling 370 billion special drawing rights (SDRs), i.e. approximately CHF 540 billion, to finance its support measures whenever its regular funds are exhausted. Switzerland participates in the NAB with a contribution of some CHF 16 billion (SDR 10.9 billion). The SNB makes the corresponding credit lines available to the IMF. Interest is paid on drawn credit at the prevailing market rate, and the credit is not guaranteed by the Confederation. According to the resolution to reform the quotas and governance, the upcoming doubling of quotas will be offset by a reduction in overall NAB funds. For Switzerland, this will mean an overall decline in the maximum commitment to the IMF.

The IMF helps low-income countries to implement sustainable macroeconomic policies through its Poverty Reduction and Growth Trust (PRGT).

The funds provided for this trust, which do not form part of the IMF’s regular resources, were increased by a total of USD 14 billion in 2011, primarily through bilateral contributions by donor countries.

A new loan provided by the SNB for SDR 500 million, for which a guarantee by the Confederation was approved, is expected to be drawn on from 2012 onwards. This is the third contribution of this type by Switzerland following the granting of two loans by the SNB with a federal guarantee in 1995 and 2001, with interest payable at the prevailing market rate in each case. The interest costs for the loans are additionally subsidised through the PRGT. This means that the poorest countries paid no interest up to the end of 2011. From 2011 onwards, Switzerland will contribute CHF 16 million to these interest subsidies in four annual payments.

Switzerland provided no monetary assistance based on the Monetary Assistance Act (MAA) in 2011. A standing credit facility amounting to CHF 2.5 billion is available for any potential assistance measures required to prevent or remedy serious disruptions to the international monetary system or to support countries which cooperate particularly closely with Switzerland in the sphere of monetary and economic policy.

Switzerland maintains a close partnership with the IMF in a number of areas of technical collaboration, both bilaterally and together with other countries. This includes providing technical assistance to strengthen the financial sectors of emerging and developing countries, strengthen tax administrations, manage natural resources, and combat money laundering and the financing of terrorism.

### 4.2.4 Switzerland’s country report

On 14 May 2011 the Executive Board of the IMF approved the report on Switzerland’s annual policy consultation. IMF staff and IMF Executive Directors welcomed the Swiss authorities’ proactive conduct in the wake of the crisis, and considered this conduct to have contributed to the country’s swift and broad-based economic recovery. According to the IMF, Switzerland exhibits robust economic growth, although this is expected to slow in 2012. While domestic demand is expected to remain strong, the delayed

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4 Original NAB participants: Australia, Belgium, Central Bank of Chile, Danish National Bank, German Bundesbank, Finland, France, Italy, Japan, Canada, Republic of Korea, Kuwait, Luxembourg, Malaysia, Netherlands, Norway, Austria, Saudi Arabia, Swedish Riksbank, Swiss National Bank, Singapore, Spain, Thailand, United Kingdom, United States, Hong Kong Monetary Authority.

New NAB participants since 2011: Brazil, China, Greece, India, Ireland, Bank of Israel, Bank of Mexico, New Zealand, Philippines, Poland, Portugal, Russia, South Africa, Cyprus.
impact of the strong franc and a weak global economic environment should lead to a slowdown in Switzerland’s export activity and a narrowing of its trade surplus. Inflation is likely to remain moderate. In the medium term, further reforms in the area of financial market regulation will prove necessary. One aspect which requires clarification according to the IMF is the role of the supervisory authorities (FINMA) and the SNB in the area of macroprudential oversight. Finally, the measures taken by Switzerland in connection with the “too big to fail” problem (see section 2.2.3) were assessed positively by the IMF.

4.3 Financial stability

The stability of the financial system is of critical importance to the Swiss economy and its financial centre. For this reason, Switzerland is heavily involved in the work of the Financial Stability Board (FSB), which has emerged as the key international body in the area of financial stability. Switzerland has two seats on the FSB, which are occupied by the FDF and the SNB respectively.

The FSB pushed ahead with a number of important projects in 2011. Particular emphasis was laid on containing the risks posed by systemically important financial institutions (“SIFIs”). In November 2011, the G20 approved the new standards of the FSB for the resolution (or winding-down) of SIFIs. These set out the prerequisites that a country’s national legal framework should have in place in order to facilitate the successful restructuring or resolution of SIFIs both in a national and a cross-border context. In the case of global systemically important financial institutions (so-called “G-SIFIs”), the FSB calls for the elaboration and regular review of recovery and resolution plans in a cross-border context. It was also agreed that additional capital requirements should apply to global systemically important banks – which include UBS and Credit Suisse – based on a sliding-scale system to reflect the degree of an institution’s systemic importance (see Figure 5: Overview of additional requirements for big banks). As a pioneer in this area, Switzerland has made a substantial contribution to the SIFI discussions.

The tighter regulation of financial institutions brings with it the danger of a transference of business activities to the “shadow banking system”. Accordingly, the FSB is to draw up proposals for the regulation and oversight of the shadow banking system in 2012.

The FSB also emphasises the improvement of transparency in the over-the-counter (OTC) trading of derivatives. The international dimension of this business area presents great challenges, however, since existing regulation is geared around national jurisdictions. The FSB is supporting the work of individual jurisdictions by helping to coordinate national regulation measures and monitoring the implementation of reforms. Switzerland too is reviewing the need for action in the area of OTC derivatives trading.

Another area of activity for the FSB is the monitoring of implementation of financial market reforms. This is also the objective of the thematic and country-specific “peer reviews” of the FSB, which provide supervisory authorities with feedback on the quality of regulation. In 2011, the remuneration systems of financial institutions were evaluated, and overall progress – including in Switzerland – was considered satisfactory. In a parallel development, an evaluation of deposit insurance systems was also initiated in 2011. Switzerland’s country-specific peer review, which got underway in 2011, shows that the measures of the TBTF bill are viewed as positive overall. In other areas of financial oversight too, Switzerland’s ongoing reforms are being welcomed. The FSB’s final report will be published at the beginning of 2012.

**Swiss credit obligations vis-à-vis the IMF (as at November 2011)**

<table>
<thead>
<tr>
<th>In CHF mn, rounded</th>
<th>Utilised</th>
<th>Still undrawn</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Quota</td>
<td>1988.3</td>
<td>2946.6</td>
<td>4934.9</td>
</tr>
<tr>
<td>Gen./New Arrangements to Borrow</td>
<td>887.0</td>
<td>14673.8</td>
<td>15560.8</td>
</tr>
<tr>
<td>Purchase/sale of SDRs</td>
<td>-122.0</td>
<td>2467.8</td>
<td>2345.8</td>
</tr>
<tr>
<td>Poverty Reduction and Growth Trust</td>
<td>298.5</td>
<td>713.4</td>
<td>1011.9</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>3051.8</strong></td>
<td><strong>20801.7</strong></td>
<td><strong>23853.5</strong></td>
</tr>
</tbody>
</table>

Source: SNB

Figure 13
In view of the expanding remit of the FSB, the question of how to strengthen this Basel-based institution will also be on the agenda for 2012. At the same time, Switzerland will be advocating improvements to the organisation’s transparency and efficiency.

4.4 International activities in the area of customs

International financial matters also concern the customs area.

The agreement with the EU on the simplification of customs formalities and on customs security measures approved by the Federal Assembly on 18 June 2010 was implemented in 2011. Amendments to Annex I to the agreement, concerning entry and exit summary declarations, had already been discussed with the EU Commission, and new amendments to the same Annex are planned for 2012.

Due to the fact that Norway is not a member of the EU, goods traffic with this country has in principle been subject to the advance notification requirement since 1 January 2011. However, Norway has negotiated an agreement with the EU similar to the one with Switzerland on the simplification of customs formalities and on customs security measures, and thereby meets the European security standards. The Federal Customs Administration (FCA) is currently negotiating with Norway on an agreement that would recognise the equivalence of the two countries’ security standards and risk analysis. Once the negotiations with Norway are complete, the FCA will commence negotiations on the mutual recognition of the status of authorised economic operator (AEO) with other countries, namely the USA, Japan and China.

At the request of Russia, Switzerland intends to initiate negotiations with it on an agreement in the customs area. The negotiations with the United States on an agreement on administrative assistance in the customs area have not yet been completed.
5

Further information

Federal Department of Finance (FDF):
wwwefd.admin.ch

State Secretariat for International Financial Matters
(SIF):
www.sif.admin.ch

Federal Tax Administration (FTA):
www.estv.admin.ch

Federal Customs Administration (FCA):
www.ezv.admin.ch

Swiss Financial Market Supervisory Authority (FINMA):
www.finma.ch

Swiss National Bank (SNB):
www.snb.ch

Organisation for Economic Co-operation and Development
(OECD):
www.oecd.org

Financial Stability Board (FSB):
www.financialstabilityboard.org

International Monetary Fund (IMF):
www.imf.org

Financial Action Task Force (FATF):
www.fatf-gafi.org