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International Banking Secrecy: Developments in Europe Prompt New Approaches

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ABSTRACT

The frequent connection between banking secrecy and various corrupt political and business practices has drawn considerable attention from non-secrecy states. In Europe, the issue presently is ripe because of the European Community's plans for a unified economy in 1992. This Note begins with a moral and historical examination of banking secrecy. Then, the author reveals the banking practices and legal structures through which banking secrecy is exploited. The author next sets forth the substantive banking secrecy laws of four European states and attempts to surmise the direction of their policies regarding banking secrecy. Next, the author describes past attempts, both unilateral and bilateral, to resolve the issue. Finally, the author proposes that, although a worldwide solution hardly is imminent, the increasing economic interdependence of small groups of states, such as the European Community, mandates serious consideration of multilateral approaches to resolve the international banking secrecy issue.

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I. INTRODUCTION

Banking secrecy has surfaced in the news alongside some of the past decade's most notorious social enemies, including exiled tyrants, insider traders, drug lords, and tax evaders.[1] Recently, a major Luxembourg-based financial institution pleaded guilty to money laundering charges in a United States District Court drug case connected with Manuel Noriega.[2] Nicolae Ceausescu, the recently executed Romanian dictator,

1. Insider traders, drug lords and tax evaders use banking secrecy to conceal illegal gains. Tyrants of politically volatile third-world countries stash funds away in banking secrecy jurisdictions in case they are overthrown. *See* I. WALTER, THE SECRET MONEY MARKET 71-76 (1990).

2. *See* Barrett & Schmitt, *Noriega-Linked Bank Admits Laundering*, Wall St. J., Jan. 17, 1990, at 4 col. 4. Under the plea agreement, the Bank of Credit and Commerce International agreed to a record forfeiture of $14.8 million to the United States government. *Id.*

also had substantial holdings in a foreign secrecy jurisdiction.[3] Besides foreign exiled tyrants, controversial political figures in the United States, such as those involved in the Iran-Contra scandal, have concealed their illegal activities through banking secrecy jurisdictions.[4] Dennis Levine is an example of an infamous insider trader who had an account in a secrecy jurisdiction.[5] Similarly, Marc Rich, a commodities broker, used Swiss bank accounts to evade paying forty-eight million dollars in taxes.[6]

The above facts illustrate why banking secrecy has become controversial, implicating transnational tax, criminal law, and political issues. Although many countries, like the United States, view banking secrecy as an impediment to criminal and tax prosecution and as a tool for the political tyrant and drug trafficker, banking secrecy states arguably have an interest both in the sovereignty of their legal systems and the stability of their economies. Moreover, several recent political events have intensified the debate over banking secrecy. During the past ten years, for instance, the United States, in its efforts to crackdown on international drug trafficking and insider trading of securities, has broadened its attempts to penetrate foreign banking secrecy laws beyond the traditional realm of prosecuting tax evasion.[7] In Europe, declining confidence in Swiss banking secrecy during the past decade has prompted many investors to transfer funds to banking institutions in other secrecy jurisdictions.[8] In addition, the European Community (the Community) seeks to establish a unified banking system throughout its member countries as part of its plans for multinational unification in 1992.[9] Furthermore, the recent political and economic reforms in Eastern Europe suggest a possible continuation of economic unification in Europe that may extend far beyond the Community's current plans for 1992.

With these recent events in mind, this Note will first examine banking secrecy as a moral issue and trace its historical development. Then, this

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3. Cody, *The Days May be Numbered for Some Secret Swiss Accounts*, Wash. Post, Feb. 5-11, 1990 (Nat'l Weekly Ed.), at 20, col. 1.

4. *See* Shenon, *Swiss Bank Records in Iran-Contra Case Are Released to U.S.*, N.Y. Times, Nov. 4, 1987, at A1, col. 1.

5. *See* Putka, *Those Famed Swiss Bank Accounts Aren't Quite as Impenetrable as They Used to Be*, Wall St. J., June 20, 1986, at 21, col. 4.

6. *See* Mufson, *Switzerland Enters Marc Rich Case to Halt U.S. from Obtaining Subpoenaed Papers*, Wall St. J., Aug. 5, 1983, at 3, col. 2; Bock, *Swiss Secrecy: Don't Bank on It*, TIME, Dec. 7, 1987, at 49.

7. *See* Note, *Swiss Bank Secrecy and United States Efforts to Obtain Information from Swiss Banks*, 21 VAND. J. TRANSNAT'L L. 63, 105-06 (1988).

8. *See generally id.*

9. *See infra* Part VI.

Note will set forth the general legal and financial structures that allow the exploitation of banking secrecy. Next, this Note will examine the laws and policies of the major European banking secrecy markets. This Note will then consider the methods through which individual governments and international organizations have chosen either to combat banking secrecy or to resolve the legal conflicts that emerge from the practice. Finally, this Note will examine the legal and political alternatives for resolving this issue both in the immediate context of a Europe headed toward greater unification and in the context of the increasing interdependence of global economies and political structures.

II. BACKGROUND

A. *Moral Arguments*

Despite its undeniable connection with illegal activities, banking secrecy poses difficult legal and moral problems because it is more of a facilitator of illegal or immoral activities than immoral itself.[10] Indeed, some individuals in international banking and legal circles righteously support banking secrecy. Some defenders of banking secrecy, for example, contend that its critics too often presumptively equate banking secrecy with illegality.[11] They argue that banking secrecy is a right of "financial privacy" that should be treated like those physical privacy rights that the United States Supreme Court has recognized as fundamental.[12]

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10. *See* I. WALTER, *supra* note 1, at 205. Though one might attempt to equate the role of a facilitator to that of an aider and abetter, the crime of aiding and abetting requires an element of intent which is usually absent in a bank's facilitation of its clients' immoral or illegal activities. On the other hand, one must ask at what point does "looking the other way" become morally reprehensible when so much is known about the exploitation of banking secrecy.

11. *See* de Capitani, *Banking Secrecy Today*, 10 U. PA. J. INT'L BUS. L. 57, 58 (1988); *see also* N. DEAK & J. CELUSAK, INTERNATIONAL BANKING 232 (1984). The appeal of banks in secrecy jurisdictions also may be attributable to the fact that such jurisdictions frequently offer a wider range of services, because they have less burdensome regulatory systems. *Id.* Other defenders of banking secrecy point out that bankers in secrecy jurisdictions abhor criminals and in practice will refuse to accept deposits from suspicious sources. *See* E. CHAMBOST, BANK ACCOUNTS: A WORLD GUIDE TO CONFIDENTIALITY 24 (P. Walton & M. Thompson trans. 1983). *But see* Karzon, *International Tax Evasion: Spawned in the United States and Nurtured by Secrecy Havens*, 16 VAND. J. TRANSNAT'L L. 757, 817-19 (1983).

12. Perhaps these proponents view financial privacy as an undeniable aspect of individual sovereignty akin to the right to choose to have an abortion. *See* Roe v. Wade, 410 U.S. 113 (1973).

Nineteenth century German law viewed banking secrecy as a constitutionally guaranteed human right. *See* Palmer, The Austrian Banking System Under the 1979 Statute

Others perceive banking secrecy as a professional secrecy that deserves the same legal protection as the attorney-client privilege or the secrecy between a patient and a doctor.[13] Additional arguments for banking secrecy include that it is a reasonable response to the unfairness of particular types of tax systems,[14] that it is an undeniable aspect of human nature,[15] and that it is a cherished individual liberty essential to a free and democratic society.[16] Still another argument is that states should not sacrifice the social utility of banking secrecy as an indirect remedy for the social problems that it incidentally facilitates.[17]

On the other hand, moral arguments exist in opposition to banking secrecy. One is that a semantic problem emerges when the terms "financial privacy" and "banking secrecy" are used interchangeably. Opponents of banking secrecy point to the fact that "secrecy" may concern

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46, n.130 (July 1980) (available in the University of Michigan Law School Library and the Library of Congress); *see also infra* note 27 and accompanying text.

13. Edmond Israel, the Chairman of the Luxembourg stock exchange, has said, "[w]e believe that banking secrecy is just as important as for example the secrecy in the medical field." *Despite EC Tax Threat, Banking is Booming in Luxembourg*, Reuters, Mar. 30, 1989 (Nexis).

14. *See* I. WALTER, *supra* note 1, at 3 (suggesting that certain individuals seek banking secrecy to avoid the unfairness of progressive tax rates); E. CHAMBOST, *supra* note 11, at xi (characterizing certain tax regimes as "systematic, organized plundering which should be prevented").

15. *See* I. WALTER, *supra* note 1, at 2 (observing that even family members often keep financial matters secret from one another).

16. Commenting on the Swiss abstention from an Organization for Economic Cooperation and Development (OECD) report recommending the abolition of banking secrecy, the Swiss Ambassador to the OECD remarked that banking secrecy is "indivisible from the democratic system and the strict respect for individual liberties in effect in my country." *Swiss Thwart OECD Move to Loosen Bank Secrecy*, Reuters (N. Eur. Serv.), July 3, 1985 (Nexis).

Proponents of the argument that banking secrecy is an integral part of a free and democratic society support the argument by citing to the development of banking secrecy in Switzerland as a response to Hitler's attempts to confiscate Jewish property. *See infra* note 28 and accompanying text.

17. One author discusses several situations that possibly justify the social utility of banking secrecy. These include: (1) an international spy whose anonymity is essential to the security of the country for which the spy works; (2) an individual in a politically volatile state who wishes to protect his money from seizure in case a revolution occurs; or (3) a dissident in a totalitarian country who uses a secret account to deposit his illegal publishing royalties. *See* M. SKOUSEN, THE COMPLETE GUIDE TO FINANCIAL PRIVACY 78 (4th ed. 1983).

Other legitimate reasons for placing funds in foreign secrecy jurisdictions include frustrating and deterring the claims of either distant relatives in probate or alleged tort victims with unjustified claims. *See* I. WALTER, *supra* note 1, at 2.

matters that are not private, but which an individual simply wishes to keep from third parties.[18] Moreover, opponents assert that no special legal or professional considerations justify special restrictions on the exchange of banking information.[19] One commentator concludes that professional secrecy, in general, serves a useful social purpose only to the extent that the value of the client's confidence in professional secrecy outweighs the increase in the social welfare if the information were disclosed.[20]

The laws in banking secrecy jurisdictions, however, frequently overvalue professional confidence in situations, such as those involving tax evaders, insider traders, drug-traffickers, and political tyrants, where disclosure would have a greater utility to society as a whole. In response to those who support banking secrecy as a reasonable reaction to aggressive tax regimes, critics note that all honest taxpayers suffer when dishonest taxpayers evade taxes.[21] Furthermore, banking secrecy opponents contend that although protected rights and liberties are cherished and necessary in a free and democratic society, in certain circumstances, society's need for orderly governance outweighs even the most well-protected liberties.[22]

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18. S. BOK, SECRETS 119 (1985). *See id.* at 116-35 for a general philosophical discussion of professional secrecy. According to another author, just because criminal or civil liability has been attached to the disclosure of certain information does not render that information "private" in the sense of pertaining to an individual's sphere of privacy. S. STROMHOLM, RIGHT OF PRIVACY AND RIGHTS OF THE PERSONALITY 67 (1967). These observations undermine the argument that financial privacy is worthy of protection similar to that of a fundamental right as recognized by the United States Supreme Court. *See supra* note 12 and accompanying text.

19. ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT, TAXATION AND THE ABUSE OF BANK SECRECY 3-4 (1985) [hereinafter OECD, TAXATION].

20. S. BOK, *supra* note 18, at 122. The attorney-client privilege, an example of professional secrecy under United States law, exists because of its usefulness in the United States adversarial trial system. Also, in the absence of secrecy between doctor and patient, a disease might prove more damaging to those patients who are ashamed that they are infected. In both the legal and medical situations, the value of the professional secrecy generally outweighs the social utility of disclosure. *See id.*

21. It is also important to note that banking secrecy facilitates capital flight whether it is caused by oppressive taxation, a dismal economic outlook, or political volatility. All citizens of a state pay for capital flight, because it increases the national debt. This has been a severe problem in Latin America. *See* I. WALTER, *supra* note 1, at 53-67.

22. *See generally* G. GUNTHER, CONSTITUTIONAL LAW, Pt. III (11th ed. 1985) (discussing individual rights under United States constitutional law).

B. *History*

Although banking secrecy appears to have begun early in human history, it is thinly documented. One author suggests that banking secrecy might have originated four thousand years ago with the Hammourabi Code in ancient Babylon.[23] Romans may have practiced banking secrecy, and subsequent barbarian tribes may have recognized banking secrecy in their form of common law.[24] In Austria, banking secrecy has existed in customary law and tradition since the sixteenth century.[25] Between the seventeenth and nineteenth centuries, German and Italian banking rules and articles of association included banking secrecy provisions and penalties for non-compliance.[26] During the nineteenth century, banking secrecy in Germany developed both as an incident to the contractual relationship between the banker and the client and as a constitutionally guaranteed human right.[27] In the twentieth century, the Swiss Civil Code crystallized traditional banking secrecy customs in response to Nazi attempts to force German citizens to declare and return to Germany all foreign assets.[28]

Today, nearly every country legally recognizes some form of banking secrecy.[29] The range of exceptions to banking secrecy in a country's codes and common law determines whether a jurisdiction has adopted "banking secrecy."[30] The exceptions to banking secrecy under United

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23. *See* E. CHAMBOST, *supra* note 11, at 3. Chambost concedes that the Hammourabi Code does not contain any express provision on banking secrecy, but he infers the existence of banking secrecy from a provision which allows a banker to make public the records of a client only under certain circumstances. *Id.* Presumably, this exception would be necessary only if banking secrecy was the understood norm.

24. *Id.* at 3-4.

25. Palmer, *supra* note 12, at 46.

26. *See* de Capitani, *supra* note 11, at 58 (referring to the rules of the Banco Ambrosiano Milano of 1593 and the Hamburger Bank of 1619).

27. Palmer, *supra* note 12, at 46 & n.130.

28. *See* E. CHAMBOST, *supra* note 11, at 6. The Nazi government of Germany promulgated regulations requiring declaration of foreign assets in 1933. *Id.* at 5. The following year, the Swiss codified their banking secrecy customs by providing criminal sanctions for a breach of such secrecy. *Id.* at 6. Before this codification, the Swiss had enhanced secrecy through the custom of numbered accounts and accounts with false names. *Id.*

29. *See generally id.* at 91-259. Chambost surveys the varying degrees of legally protected banking secrecy in over thirty countries and sets forth his dichotomy of banking "havens" and banking "infernos." Banking "infernos" are those jurisdictions which are hostile to the practice of banking secrecy. *Id.* at 92.

30. For example, the famous case of Tournier v. National Provincial & Union Bank of England, [1924] 1 K.B. 461 (C.A. 1923), established the law of banking secrecy in the

States law are so numerous that some have quipped that the title of the "Banking Secrecy Act of 1970"[31] is a misnomer.[32]

In recent decades, many third world countries have adopted strict banking secrecy laws in order to subsidize their banking industries and economies.[33] Although these third world countries generally have no historical tradition of banking secrecy, they share several common characteristics with European banking secrecy jurisdictions, such as geographic isolation, narrow export economies, and vulnerability to adverse conditions in international trade.[34] In many third world secrecy jurisdictions, the banking and tourism industries constitute the source of nearly all of the country's foreign cash.[35] Banking secrecy laws, therefore, are an essential ingredient in the development of these countries' economies.

United Kingdom. The court enunciated four exceptions to the law of banking secrecy. There will be no banking secrecy if: (1) ordered by law; (2) necessitated by a duty to the public; (3) necessary to protect the bank's interests; or (4) the client expressly or implicitly grants permission. *Id.* at 473. *But see infra* note 196 (Under the Greek Banking Secrecy Act, even the depositor cannot waive banking secrecy.).

31. *See infra* Part V.A.1.

32. M. SKOUSEN, *supra* note 17, at 24. Actually, the Banking Secrecy Act does not protect banking secrecy in the United States; instead it is aimed at combating the exploitation of banking secrecy abroad. *See infra* Part V.A.1. The United States, however, does not lack legal protection of banking secrecy entirely; theories of contract, agency, and tort law recognize and protect financial privacy to a limited extent. *See Tournier*, [1924] 1 K.B. at 421 (contract theory in Anglo-Saxon law); Graney Dev. Corp. v. Taksen, 92 Misc. 2d 764, 768, 400 N.Y.S.2d 717, 720 (N.Y. Sup. Ct.), *aff'd*, 66 A.D.2d 1008, 411 N.Y.S.2d 756 (N.Y. App. Div. 1978) (agency theory); L. FISCHER, THE LAW OF FINANCIAL PRIVACY: A COMPLIANCE GUIDE ¶5.04 (1983 & Supp. 1989). The Financial Institutions Regulatory and Interest Rate Control (Right to Financial Privacy) Act, Pub. L. No. 95-630, § 1100, 92 Stat. 3541, 3697-3710 (1978), also protects financial records from undue interference by the government.

33. Many countries in the Caribbean and South Atlantic, such as Antigua, the Bahamas, Bermuda, the Cayman Islands, Montserrat, the Netherlands Antilles, and Panama now have strict banking secrecy laws. Their geographical proximity to unstable Latin American governments and drug producing countries makes them desirable havens for capital flight and drug profits. *See* I. WALTER, *supra* note 1, at 210-221. For an analysis of the history and development of financial havens, see R. BLUM, OFFSHORE HAVEN BANKS, TRUSTS, AND COMPANIES 1-28 (1984).

34. I. WALTER, *supra* note 1, at 35.

35. *Id.* at 108.

III. LEGAL STRUCTURES THROUGH WHICH BANKING SECRECY IS EXPLOITED

This section gives a basic description of the legal structures used to exploit banking secrecy.[36] The varying laws of different banking secrecy jurisdictions are described only in general terms. The larger purpose of this section is to bring to light the workings of these structures in order to weigh their usefulness against their potential for abuse.

A. *Direct Protection: The Account and the Banker-Client Relationship*

In the typical banking secrecy jurisdiction, the most basic level of financial confidentiality begins with current accounts and deposit accounts (checking and savings accounts, respectively). At this level, three types of accounts provide various degrees of secrecy. In the "classic named account," the depositor signs an agreement, by which the financial institution will maintain a current or deposit account, and a signature card, which enables the depositor to perform over-the-counter transactions.[37] The particular secrecy laws of the jurisdiction apply both to all information concerning this account and to all levels of bank employees.[38] Although banking secrecy laws generally secure information concerning a

36. "The ways in which foreign secret bank accounts are used to avoid income taxes are almost as numerous as the ways of earning money." *Legal and Economic Impact of Foreign Banking Procedures on the United States: Hearings Before the House Comm. on Banking and Currency*, 90th Cong., 2d. Sess. 14 (1968) (statement of Robert M. Morgenthau, United States Attorney for the Southern District of New York). *See* Meyer, *Swiss Banking Secrecy and Its Legal Implications in the United States*, 14 NEW ENG. L. REV. 18, 43 (1978). Concrete examples of how these banking secrecy structures are exploited include: (1) skimming cash receipts by failing to report all income made outside the United States and placing such income in a foreign bank account; (2) declaring inflated purchase prices on items purchased abroad for resale in the United States to reduce domestic profit and having the seller put the difference between the actual prices and the inflated prices in a foreign bank account; and (3) declaring lower than actual sales prices on items sold abroad and placing the difference in a protected foreign account. *Id.* at 43-44. Certain loan arrangements involve "captive banks" owned by the borrower and chartered in the secrecy jurisdiction. These banks offer the allure of concealed profits as well as tax deductions. *Id.*; *see also* I. WALTER, *supra* note 1, at 43-44. Additionally, an individual can take advantage of the fact that banks in most banking secrecy jurisdictions are allowed to buy and sell securities on exchanges on behalf of their depositors. The securities transactions are made in the bank's name, and thus, banking secrecy allows the depositor to evade taxes on any gains. *See* Meyer, *supra* at 45-46.

37. *See* I. WALTER, *supra* note 1, at 39.

38. For an example of a law that applies to all levels of bank employees, see *infra* notes 77-97 and accompanying text.

"classic named account" with both civil and criminal liability, the danger of disclosure from this arrangement lies in the large number of bank employees, from teller to director, who are privy to the information.[39]

To enhance the secrecy of an account, many banking secrecy jurisdictions permit banks to open and maintain numbered accounts.[40] Although similar in many ways to the "classic named account," this arrangement offers added protection against the violation of banking secrecy. For example, in addition to the deposit agreement, the depositor also signs an agreement that prohibits over-the-counter cash withdrawals by the depositor.[41] Instead, the bank assigns the depositor an account manager who is empowered to make the necessary current and management transactions.[42] Through this arrangement, the bank restricts the depositor's contacts with the bank to the account manager and the bank director. At the same time, the depositor's identity remains unknown to subordinate employees, because the transaction documents only refer to an account number.[43]

Secrecy is enhanced further by various internal measures that restrict the account manager's access to records concerning the numbered account.[44] Moreover, when corresponding with the holder of a numbered account, banks use unmarked envelopes that bear only the account holder's name and address in handwriting.[45] Also, when another party wishes to transfer funds to an individual who holds a numbered account, the bank does not admit immediately that the transferee holds an account at the bank. Instead, the bank conditionally accepts the money subject to further investigation.[46] The bank then will establish that it holds an account for the transferee and that the transferee is willing to accept the

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39. *See* I. WALTER, *supra* note 1, at 39-40. Banking secrecy protection under local law and banking secrecy in practice may mean two different things if a bank employee earning a minimum salary decides to make a side business of blackmailing customers who cherish the protection of banking secrecy. *See also* R. BLUM, *supra* note 33, at 256.

40. *See* I. WALTER, *supra* note 1, at 39-40.

41. *See id.* at 39; *see also* E. CHAMBOST, *supra* note 11, at 51.

42. *See* I. WALTER, *supra* note 1, at 39; *see generally* E. CHAMBOST, *supra* note 11, at 47-48.

43. *See* I. WALTER, *supra* note 1, at 40; *see also* E. CHAMBOST, *supra* note 11, at 47.

44. *See* I. WALTER, *supra* note 1, at 40; *see also* E. CHAMBOST, *supra* note 11, at 48.

45. *See* I. WALTER, *supra* note 1, at 40; *see also* E. CHAMBOST, *supra* note 11, at 50.

46. *See* I. WALTER, *supra* note 1, at 40; *see also* E. CHAMBOST, *supra* note 11, at 48.

transfer.[47] After verifying this information internally, the bank accepts the funds for the transferee, and only by doing so, implicitly acknowledges that it holds an account for the transferee.[48]

To further confuse investigators, some banking secrecy jurisdictions permit customers to open accounts under false names.[49] The statements of such accounts appear on their face to belong to individuals other than the holders.[50] So long as the holders do not divulge their secrets, the banks are bound by the applicable secrecy laws not to disclose the identities of the depositors.

B. *Multiple Layers of Secrecy Protection Through the Structuring of Entities*

Many banking secrecy jurisdictions have liberal laws and customs that allow settlors or promoters of legal intermediary entities, similar to trusts, foundations, and corporations in Anglo-Saxon law, to be hidden beneficiaries of such entities.[51] The private nature of such arrangements and the professional secrecy of bankers and lawyers provide the beneficial owner with a double layer of secrecy protection.[52] Although legal rules defining such trust-type arrangements vary among jurisdictions, the basic trust arrangement involves one party (the settlor) who entrusts another party (the trustee) with property for the benefit of a third party (the beneficiary).[53] Any of the three parties may consist of single or multiple individuals or legal entities.[54]

Two frequent variations on this arrangement include the "discretionary" trust and the "disguised" trust. Under the discretionary trust, the

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47. *See* I. WALTER, *supra* note 1, at 40; *see also* E. CHAMBOST, *supra* note 11, at 48.

48. *See* I. WALTER, *supra* note 1, at 40; *see also* E. CHAMBOST, *supra* note 11, at 48.

49. *See* I. WALTER, *supra* note 1, at 40; *see also* E. CHAMBOST, *supra* note 11, at 54.

50. *See* I. WALTER, *supra* note 1, at 40; *see also* E. CHAMBOST, *supra* note 11, at 54.

51. *See* I. WALTER, *supra* note 1, at 41-42; *see also* E. CHAMBOST, *supra* note 11, at 58. One of the most well-known and extensively used such jurisdictions is Liechtenstein. *See Swiss Banks and Secrecy Laws: Hearings Before the House Comm. on Banking and Currency on H.R. 15073*, 91st Cong., 1st and 2nd Sess. 364-369 (1969-70). Similar entities also may be found in Panama and other Caribbean jurisdictions. *See* Meyer, *supra* note 36, at 45.

52. *See* E. CHAMBOST, *supra* note 11, at 58.

53. *See* I. WALTER, *supra* note 1, at 42; *see also* E. CHAMBOST, *supra* note 11, at 61.

54. *See* I. WALTER, *supra* note 1, at 42.

trustee determines which of several potential beneficiaries will receive the trust property.[55] In a disguised trust, the settlor, sometimes known as the owner beneficiary, is or may be a beneficiary of the trust.[56]

Another method of maintaining secrecy through structured entities utilizes "shell," "dummy," or "paper" corporations.[57] Under one scheme, a shell corporation issues shares in bearer form that require no guarantees from the local administrators.[58] Because the administrators consent to turn over executive powers to whomever places their name on the stock certificates, only the lawyer who established the corporation knows the true identity of the owner of the corporation.[59] The true owner may further protect his identity by placing another party's name on the stock certificates and signing a fiduciary agreement with that person.[60] Another type of "dummy" or "paper" corporation requires significant initial capitalization, but once the corporation is formed, the capital can be returned immediately to the owners.[61] This type of corporation issues no stock and requires no disclosure of the owner or owners, even though it is listed in the public register.[62]

C. *How Secrecy Users Avoid Disclosure from the Regulation of International Currency Transfers*

Although no strict exchange control system exists in the United States,[63]the Banking Secrecy Act[64] requires financial institutions to re-

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55. E. CHAMBOST, *supra* note 11, at 62; *see* I. WALTER, *supra* note 1, at 42.

56. E. CHAMBOST, *supra* note 11, at 62; *see* I. WALTER, *supra* note 1, at 42. Individuals who exploit banking secrecy often devise complex trust schemes with multiple trustees, beneficiaries, and private agreements to conceal the fact that the settlor is also the beneficiary of the trust. *See generally* E. CHAMBOST, *supra* note 11, at 62-64.

57. Liechtenstein law offers several variations on the "shell" corporation, namely, the *Aktiengesellschaft*, the *Stiftung*, and the popular *Anstalt*. These entities are based on the Company Law, which was enacted in 1926. *See* I. WALTER, *supra* note 1, at 197.

58. *See id.* at 43; E. CHAMBOST, *supra* note 11, at 66.

59. *See* I. WALTER, *supra* note 1, at 43; *see generally* E. CHAMBOST, *supra* note 11, at 67.

60. *See* I. WALTER, *supra* note 1, at 43.

61. *See id.* at 197 (describing the *Anstalt*, which is available in Liechtenstein).

62. *Id.*

63. Exchange controls are legislation through which a country prevents the free exchange of its currency on the international market. In countries that have such legislation, compliance with the exchange control regulations impedes the use of banking secrecy jurisdictions. For an introduction to this problem and a discussion of how banking secrecy users avoid it, see generally E. CHAMBOST, *supra* note 11, at 16-24. While the United States does not have exchange controls, it does regulate international money transfers. These regulations present problems of their own for the banking secrecy user.

port certain transactions. Moreover, for accounting and bureaucratic purposes, United States financial institutions employ their own record keeping practices. Obviously, the usefulness of an account in a secrecy jurisdiction is diminished when the account holder's home country records the transactions that transmit funds to and from the account abroad. These reporting and record keeping practices in countries like the United States present the secrecy user with the difficult task of concealing his or her identity while transferring or receiving money across national borders.

An examination of the various methods of transferring money abroad under the United States Banking Secrecy Act reveals both attractive and unattractive options for the would-be user.[65] Personal checks, for example, offer virtually no confidentiality. Under the Banking Secrecy Act, banks must keep special records of checks written for amounts in excess of ten thousand dollars.[66] Many banks, however, will retain, for up to five years, photocopies of checks written for less than ten thousand dollars.[67]

An individual also may engage in various international financial transactions that require less involvement from financial institutions and place the burden of reporting the transactions on the individual. The most familiar of these transactions involves smuggling funds across a border either personally or by courier. If the individual is carrying more than ten thousand dollars, the individual must report this fact.[68] An individual who sends cash abroad by mail must report such transaction only if the value exceeds ten thousand dollars.[69] However, an individual who does not desire to smuggle cash may remain anonymous by using other monetary instruments. An individual may purchase a money order, designate a foreign bank as payee, and leave the payor space blank. Thus, the use of money orders avoids any record of the purchaser.[70] Also, an individual may send funds abroad confidentially by paying cash for cashier's checks that are signed by the bank manager rather than the

64. Pub. L. No. 91-508, 84 Stat. 1114 (1970) (codified at scattered sections of 12 U.S.C. (1988)). *See infra* notes 155-71 and accompanying text.

65. *See generally* M. SKOUSEN, *supra* note 17, at 89-95; *see also* L. FISCHER, *supra* note 32. Congress recently has made illegal the act of structuring transactions to avoid reporting requirements. *See infra* notes 161-62 and accompanying text.

66. M. SKOUSEN, *supra* note 17, at 89.

67. *Id.*

68. *Id.* at 93.

69. *Id.* at 90. An individual also may send up to $5,000 in municipal bonds without reporting the transaction to the customs service. *See generally id.* at 89-93.

70. *Id.* at 90.

individual.[71]

Through the use of commodities, an individual can transfer funds to secrecy jurisdictions and completely avoid the Banking Secrecy Act. Individuals can purchase rare coins, diamonds, or other highly marketable commodities in the United States and then resell them abroad. The transferor is not required to report this type of transaction.[72] The methods of retrieving money and delivering it from secrecy jurisdictions are similar.[73]

IV. Law and Policy in the Major Banking Secrecy Powers in Europe Besides Switzerland

This Note will not directly discuss banking secrecy law and policy in Switzerland because the subject is already well documented.[74] This section seeks to describe foreign laws and policies on banking secrecy in other jurisdictions to aid in weighing the interests of banking secrecy jurisdictions in situations such as judicial proceedings[75] and treaty negotiations.[76]

A. *Austria*

1. Banking Secrecy Law in Austria

Sections 23 and 34 of the Austrian Banking Statute of 1979[77] (the Banking Statute of 1979) codified the professional tradition and common law of banking secrecy in Austria and are the basis for the protection of Austrian banking secrecy today.[78] Section 23 sets forth the duty of banking secrecy, the persons bound by it, and exceptions from the duty.[79]

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71. *Id.*

72. *Id.* at 92. Gold and silver may be subject to declaration at customs. *See id.* at 94.

73. *See id.* at 93.

74. *See* Note, *supra* note 7, at 66-67 n.18.

75. *See infra* note 186.

76. *See infra* Part V.C.

77. Banking Statute of 1979, §§ 23, 34 (Aus.), *translated in* Palmer, *supra* note 12, at 94-95.

78. The concept of Austrian banking secrecy grew out of German and Swiss doctrines and case law. Under the common law, the violation of banking secrecy gave rise to a civil action for damages. Banking secrecy was a valid excuse to avoid testifying in civil, but not criminal, proceedings. Banking secrecy, however, did not protect information from being examined by the tax authorities. *See* Palmer, *supra* note 12, at 46-47.

79. Section 23 of the Banking Statute of 1979 has been translated as follows:

> (1) Credit institutions, their associates and members of instrumentalities, as well as the persons working at them may not disclose or use secrets entrusted or made accessible to them exclusively as a result of the business relationship with the cli-

Section 34 provides for criminal sanctions for the violation of section 23.[80] The Civil Code concerning delictual liability, rather than the Banking Statute of 1979, treats civil liability for violation of banking secrecy.[81]

All persons who work at banking institutions, as well as government authorities who have obtained knowledge of the facts subject to banking secrecy, are bound by section 23.[82] Moreover, the Banking Statute of 1979 only governs officially licensed banks.[83] Although the Banking Statute of 1979 does not define the term "banking secret," the government draft of the statute characterizes a "banking secret" as "facts known only to a limited number of persons, the disclosure of which would be detrimental to the client."[84]

Exceptions to the duty of banking secrecy arise in criminal, tax administration, and inheritance proceedings,[85] as well as when a client expressly waives the privilege.[86] According to article 23, banking secrets are not privileged information "in connection with criminal court proceedings . . ., and in connection with criminal proceedings for intentional

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ent (banking secret). If instrumentalities of government authorities, while carrying out their official activities, obtain knowledge of facts subject to banking secrecy, they shall maintain official secrecy from which they may be released only in the instances of para. 2. The obligation arising from a banking secret shall prevail without any time limits.

(2) The obligation to keep banking secrets shall not exist:

1. in connection with criminal court proceedings in relation to the criminal courts, and in connection with criminal proceedings for intentional fiscal offenses, except for fiscal contraventions, in relation to the authorities that adjudicate fiscal crimes, or

2. in the case of an inheritance proceeding in relation to the inheritance court . . ., or

3. if the client expressly consents to the disclosure of the secret in writing, or

4. for generally worded information on the economic situation of an entrepreneur, as is customary in banking practice, if he does not object to the giving of the information.

(3) A credit institution may not plead banking secret to the extent that the disclosure of the secret is required to determine its own tax liability.

Palmer, *supra* note 12, at 94-95.

80. Palmer, *supra* note 12, at 49.

81. *Id.*

82. Banking Statute of 1979, § 23(1). *See supra* note 79.

83. Palmer, *supra* note 12, at 50.

84. *Id.* at 50-51. Further, "facts otherwise worthy of protection are not protected if knowledge of them is obtained outside the bank-client relationship." *Id.* at 51.

85. Banking Statute of 1979, §§ 23(2)1-2. *See supra* note 79.

86. *Id.* § 23(2)3. *See supra* note 79.

fiscal offenses [such as tax administration] . . ., or . . . in the case of an inheritance proceeding. . . ."[87] According to Austrian commentators, the wording of these exceptions fails to address directly certain issues.[88] For example, the language "in connection with . . . proceedings" may permit the disclosure of banking secrets of persons other than the accused.[89] Furthermore, critics fear that tax authorities will initiate criminal proceedings without proper cause because of the inclusion of "criminal proceedings" in the same phrase as "fiscal offenses."[90] Furthermore, by punishing the "use" of banking secrets, the Banking Statute of 1979 may have created a method for prosecuting insider trading.[91]

Some observers assert that Austrian banking secrecy is more secure than that of Switzerland because of the wide range of punishment outlined in the criminal provisions of section 34 of the Banking Statute of 1979.[92] This assertion, however, has been disputed because of two flaws not found in Swiss law.[93] To be punished for the use or disclosure of bank secrets an individual must have the specific intent to inflict harm or obtain a benefit[94] and the victim must complain to the authorities.[95]

Further shortcomings of the Banking Statute of 1979 arise from its application to foreign parties. The statute, for example, fails to address the question whether foreign courts will be assisted in proceedings that fall within the statute's exceptions.[96] Since only the client and not a central agency can enforce a breach of secrecy, a bank may disclose the secrets of a client if a foreign court pressures the client not to prosecute the disclosing bank official.[97]

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87. *Id.* §§ 23(2)1, 2. *See supra* note 79.

88. *See* Palmer, *supra* note 12, at 51.

89. *Id.*

90. *Id.*

91. *Id.* at 54. The prosecution of insider trading is a relatively undeveloped area of Austrian law. *Id.*

92. *Id.* at 52-53. Under section 34 of the Banking Statute of 1979, the use or disclosure of banking secrets is punishable by fine, imprisonment of up to one year, or both. *Id.*

93. *Id.* at 53.

94. *Id.* In the original government draft, specific intent was not required, but if found, it increased the punishment from six months to one year. *Id.* at 53-54.

95. *Id.* at 53.

96. *Id.* at 52.

97. *Id.* at 54-55. For a discussion of "compelled consent" in the United States, see *infra* note 187.

2. Banking Secrecy Policy in Austria

Investors have not taken advantage of banking secrecy in Austria to the degree they have in other secrecy jurisdictions.[98] One historical reason is that Austria has not enjoyed great prosperity since World War II.[99] As a result, the Austrian private banking industry failed to develop the sophistication and diversity of financial services necessary to attract foreign investors.[100] Another factor may be that Austria, unlike Switzerland, did little to market its banking secrecy prior to the enactment of the Banking Statute of 1979. Immediately after the Austrian legislature enacted the Banking Statute of 1979, however, Austrian banks began to advertise the country's banking secrecy custom and law both at home and abroad.[101] Still, critics caution that Austria should avoid attaining a reputation as a haven for illicit monies.[102]

Recently, interest in Austria by foreign investors has expanded because of Austria's increasingly sophisticated banking services and capital markets.[103] Moreover, as the crumbling of the Iron Curtain creates new investment opportunities for western concerns, Austria's historical, cultural, and business ties with Eastern Europe will add to the appeal of Austria's banking industry.[104]

B. *Liechtenstein*

1. Banking Secrecy Law in Liechtenstein

One commentator notes that the banking secrecy statutes in Liechtenstein are vague because of particularly unclear language.[105] Bankers in Liechtenstein strictly adhere to banking secrecy, however, due to the se-

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98. *See* Evans, *East & West Battle for Austria's Banks*, EUROMONEY, Jan. 1989, at 90.

99. Evans, *Sometimes Eccentric, Always Profitable*, EUROMONEY, Nov. 1987, at 30.

100. *See* Evans, *East & West*, *supra* note 98, at 90.

101. *See* Palmer, *supra* note 12, at 45-46 & n.129.

102. *Id.* at 46 n.129. The Austrian Parliament recently has been preparing legislation which would curb banking secrecy in cases of suspected money laundering. *See European Finance and Investment—Offshore Centre 2; European Banking Secrecy and Disclosure— Requirements; the Record*, Fin. Times, Survey (Mar. 29, 1990) (Nexis) [hereinafter *European Finance and Investment*].

103. *See generally* Evans, *Sometimes Eccentric*, *supra* note 99, at 30.

104. *See* Evans, *East & West*, *supra* note 98, at 91.

105. *See* E. CHAMBOST, *supra* note 11, at 217 (one such clause, *handeln nach Tren und Glauben*, translates to "act according to allegiance and the law"). Banking secrecy in Liechtenstein evolved from both the common law and the customs of the banks. *See generally id.* at 216-17.

verity of the sanctions for violating the law.[106] In addition to providing stiff penalties,[107] the code of Liechtenstein also proscribes both negligent and knowing disclosure.[108] An individual who assists or induces another to violate banking secrecy also will incur criminal liability.[109]

The law in Liechtenstein always has held bankers to a high standard of conduct when they accept deposits or take on new clients.[110] Recent legislation has altered that standard by requiring bankers to identify depositors, customers, and the individuals whom they may represent.[111] In cases of money laundering or insider trading, the courts now may re-

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106. The penal clause for banking secrecy in Liechtenstein, article 47, states:

1) Whoever knowingly

. . . .

b) as part, civil servant, or employee of the bank, as accountant or accountant's assistant, as member of a bank commission, civil servant or employee of the secretary, violates his duty to maintain secrecy or professional secrecy, [or] who induces or attempts to induce [such a violation],

will be punished for this violation with a penalty of up to 20,000 francs or with imprisonment up to 6 months. Both penalties may be combined.

2) In case a perpetrator acts negligently, he will be punished for this violation with a penalty up to 10,000 francs.

LANDES-GESETZBLATT [LG] art. 47 (Liechtenstein), Jahrgang 1961, Nr. 3, v. 27.1.61, *Auszug aus dem "Gesetz über die Banken und Sparkassen" v. 21.12.60.*

107. *Id.* §§ 1(b), 2. *See supra* note 106.

108. *Id.* § 2. Note that penalties for knowing disclosure are more severe than the penalties for negligent disclosure. *See supra* note 106.

109. *Id.* § 1(b). *See supra* note 106.

110. The commitment to secrecy commences upon the banker's first contact with the client. It continues even after the bank employee has been terminated, although the equivalent of a three year statute of limitation applies to violations of banking secrecy.

As in most banking secrecy jurisdictions, exceptions to banking secrecy exist in Liechtenstein. An individual charged with banking secrecy may assert the following defenses: client's consent, self-defense, emergency, and protection of a legitimate interest. In inheritance and bankruptcy proceedings, administrators will be privy to banking secrets. Additionally, criminal cases warrant an exception to banking secrecy. Similar to other European countries, Liechtenstein fails to view simple tax evasion as a criminal matter. Courts will only lift banking secrecy in cases of criminal tax fraud which involve the willful use of forged documents and records.

In civil cases, when a witness refuses to testify by pleading banking secrecy, the court will determine whether banking secrecy applies. If the court determines that banking secrecy should not apply, or if the client waives banking secrecy, then the witness must testify. *See* Memorandum of Law provided by Dr. Walter Meier, LL.M., an attorney in Zurich, Switzerland (on file at Vanderbilt Law Library).

111. The government also is preparing legislation to expand bank supervision and to provide legal assistance in international criminal investigations. *See Liechtenstein Takes Steps to Protect Banks' Image*, Reuters, Oct. 10, 1989 (Nexis).

quire that banks divulge information about the suspected individual's accounts.[112]

2. Banking Secrecy Policy in Liechtenstein

In light of its economic and cultural ties to Switzerland, it is not surprising that Liechtenstein has a long tradition of banking secrecy.[113] Unlike Switzerland, however, Liechtenstein has not focused its economic policy on developing the country into an international banking center.[114] As a result, Liechtenstein is less vulnerable to political pressure from opponents of banking secrecy.

In the past, Liechtenstein vigorously defended its banking secrecy despite pressures from foreign countries.[115] As Swiss attitudes toward the practice have changed during the past decade, however, so too have Liechtenstein's. Both the government and banking industry of Liechtenstein now are following the Swiss lead by liberalizing their banking secrecy laws.[116] Moreover, a "political will" currently exists in Liechtenstein to avoid the negative labels associated with banking secrecy.[117] Liechtenstein manifests this attitude through its unwillingness to take advantage of the opportunities presented by an eroding Swiss secrecy law.[118] To this end, Liechtenstein prefers to emphasize the strength of its professional asset management services rather than its banking secrecy and low tax rates.[119]

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112. *See Neue Sorgfaltspflichtvereinbarung in Liechtenstein, Wirtschaft*, Somstag/Sonntag, 2./3. Dezember, 1989, at 41, col. 1.

113. Liechtenstein and Switzerland share a unified currency. *See* E. CHAMBOST, *supra* note 11, at 216.

114. *See Switzerland and Liechtenstein*, ABECOR/Dresdner Bank AG, (May 3, 1988) (Nexis).

115. Hans Adam, the colorful monarch of Liechtenstein, stated, in effect, that the United States had no viable economic pressures that could compel Liechtenstein to relax its banking secrecy laws. Berss, *The Prince that Roared*, FORBES, Apr. 29, 1985, at 151. At other times, Hans Adam has been quoted as defending banking secrecy. "We give legal assistance in cases of criminal abuse. It would be impossible, even if we had a police state, to prevent all misuses of our system. Even in communist countries, there are economic scandals." Studer, *A New Prince Takes the Reins in Liechtenstein*, Christian Sci. Monitor, June 13, 1984, at 1.

116. *See Liechtenstein Takes Steps to Protect Banks' Image*, Reuters Oct. 10, 1989 (Nexis) (referring to the money laundering and insider trading legislation discussed *supra* at notes 111-12 and accompanying text).

117. *Id.*

118. *See id.*

119. Templeman & Glasgall, *A Mouse That's Roaring Into Money Management*, BUS. WEEK, Feb. 1, 1988, at 72.

C. *Luxembourg*

1. Banking Secrecy Law in Luxembourg

Under article 458 of the Luxembourg Penal Code, professionals, in general, have an obligation not to reveal secrets obtained in the course of their relationships with their clients.[120] Although article 458 does not mention bankers specifically, legislation passed in 1981 expressly extended the protection of article 458 to relationships between bankers and their clients.[121] The 1981 legislation, however, did not change Luxembourg banking secrecy law. Rather, it codified a protection that professional custom and the legal system had recognized since before World War II.[122]

The language of article 458 appears to allow professionals to disclose secrets of their clients when they are called to testify before a court and when a statute compels disclosure.[123] With respect to banking secrecy, the allowance for disclosure is not as broad. As the exception to absolute secrecy, courts may obtain banking secrets in domestic civil matters such as bankruptcy, seizure, and inheritance proceedings as well as in domestic criminal matters.[124] In international matters, courts in foreign coun-

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120. A Senate Report on banking secrecy provides a translation of article 458 of the Luxembourg Penal Code.

> Physicians, surgeons . . . and all other persons to whom, by reason of their position or profession, secrets have been confided, and who reveal such secrets in cases other than those in which they are called to testify in court and in those in which the law compels their disclosure, shall be punishable by imprisonment from eight days to six months and a fine from 100 to 500 francs.

LUX. PENAL CODE, art. 458, *translated in* CRIME AND SECRECY: THE USE OF OFFSHORE BANKS AND COMPANIES, S. REP. NO. 99-130, 99th Cong., 1st Sess. 94 n.200 (1985).

121. Article 16 of the law of April 23, 1981 states:

> as an extension to article 458 of the Criminal Code [relating to medical secrets] which will prohibit the administrators, members of supervisory and management boards, management and other employees of entities defined in article 19 of this law [*i.e.*, Luxembourg banking concerns] from revealing secrets which they have learned in their professional capacity.

E. CHAMBOST, *supra* note 11, at 177.

122. Kauffman, *Le secret bancaire en droit Luxembourgeois*, 16 DROIT ET PRACTIQUE DU COMMERCE INTERNATIONAL [D.E.P.D.C.I.] 73, 76 (1990). Although the Germans passed legislation which abolished banking secrecy during the occupation, Luxembourg bankers ignored the legislation, and maintained banking secrecy in practice. Eventually, the custom developed into a "gentleman's agreement" between the banker and the client. *Id.* at 77-78.

123. LUX. PENAL CODE, art. 458. *See supra* note 120.

124. A. Schmitt, *Luxembourg*, in BANKS ABROAD 243, 252 & n.16 (F. Schwank &

tries may pierce banking secrecy if the principle of "double incrimination" applies.[125] According to this principle, disclosure will be permitted only when the crime at issue is punishable in both the foreign country seeking disclosure and Luxembourg.[126] This means that a foreign action for tax evasion, which is not punishable in Luxembourg, will not require disclosure.[127] On the other hand, tax fraud involving the falsification of documents will be sufficient cause to lift banking secrecy, because tax fraud is a punishable crime in Luxembourg.[128] The procedures for lifting banking secrecy will vary depending on the particular state seeking assistance, but it usually will involve letters rogatory and the applicable mutual judicial assistance treaty.[129]

Unlike many banking secrecy jurisdictions, Luxembourg does not view the client as the ultimate master of the banking secret. The client's power to waive the protection of banking secrecy may be limited if the bank determines that such waiver is not in the best interest of the client,[130] or if the public interest in maintaining secrecy outweighs the client's private interests.[131]

Criminal and civil sanctions exist for cases in which banking secrecy has been violated.[132] Civil sanctions stem from the idea that banking secrecy is implied in the contractual obligations between a banker and client.[133] To impose criminal sanctions, either the Minister of the Interior or the individual whose right to banking secrecy has been violated may initiate proceedings.[134] The available criminal sanctions in Luxembourg are less severe than those in Austria and are similar in severity to those of Liechtenstein.[135]

F. Ryder, eds. 1986). Notably, Luxembourg recently made money laundering a crime. *See* Kauffman, *supra* note 122, at 102.

125. Kauffman, *supra* note 122, at 102.

126. *Id.*

127. *Id.* at 100-01.

128. *Id.* at 101.

129. *See id.* at 83 (listing the mutual assistance treaties to which Luxembourg is a party).

130. *Id.* at 93-94.

131. *Id.* at 93.

132. *Id.* at 99.

133. *Id.* at 99-100.

134. *Id.* at 99.

135. If an individual is found guilty of violating banking secrecy, the court may sentence the individual for a period ranging from eight days to six months, impose a fine between 100 and 500 francs, or impose both a fine and prison sentence. LUX. PENAL CODE, art. 458. *See supra* note 120. Compare these penalties with the range of penalties in Austria, where the court may sentence the individual to imprisonment for up to one

2. Banking Secrecy Policy in Luxembourg

Luxembourg bankers boldly parade their banking secrecy laws before private banking customers.[136] According to Luxembourg banking lore, Belgian dentists travel to the Grand Duchy on holidays to deposit their profits and gain the favorable treatment of Luxembourg tax laws and banking secrecy.[137] Belgians and other foreigners have a long history of exploiting tax and secrecy laws in Luxembourg, and Luxembourg banks have earned a reputation for sophisticated and adept portfolio management.[138]

Not only is Luxembourg a member of the European Community, but also of the Organization for Cooperation and Development (OECD). Its membership in these organizations provides advantages when marketing its banking products and services.[139] Since the Community plans to unify its economy in 1992, however, many foreign depositors are concerned that Luxembourg will eliminate its banking secrecy laws as a result of pressure from the other member countries.[140] Luxembourg bankers realize that elimination of banking secrecy laws could reduce the attractiveness of Luxembourg banks to foreigners, but emphasize that the industry should take steps to improve the country's already reputable banking services.[141]

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year and impose any fine amount the court deems appropriate, *see supra* note 92, and in Liechsteinstein, where imprisonment ranges from zero to six months and fines range up to 20,000 francs, *see supra* note 106.

136. *See Feather-Footed Shuffle in the Grand Duchy*, EUROMONEY, July 1, 1988, at 91 (comments of Jean-Luc Amez, Managing Director, AMRO Bank (Luxembourg)).

137. Evans, *Sometimes Eccentric*, *supra* note 99, at 32.

138. *See id.* Although the three largest Luxembourg banks have a long history as portfolio managers, many Luxembourg branches of foreign banks have begun managing portfolios only within the past several years. *Id.*

139. *Feather-Footed Shuffle in the Grand Duchy*, *supra* note 136, at 92.

140. *See infra* note 250; *see also* Evans, *Private Change is Client-Driven*, EUROMONEY, Nov. 1988, at 96. Though Luxembourg appears resilient to Community pressures, it is concerned about its image after the embarrassment of the Bank of Credit and Commerce International scandal. Dickson, *European Finance and Investment—Offshore Centre 3; Luxembourg Stays Resilient*, Fin. Times, Survey (Mar. 29, 1990) (Nexis). *See also supra* note 2 and accompanying text. In response to Community pressure, Luxembourg recently reconfirmed the legal basis of its banking secrecy by passing a law that closed loopholes to banking secrecy which have existed in provisions of its tax laws. *See* Kauffman, *supra* note 122, at 79; *see also Règlement grand-ducal du 24 mars 1989 précisent le secret bancire en matièère fiscale et délimitant le droit d'investigation des administrations fiscales*, MEMORIAL JOURNAL OFFICIEL DU GRAND-DUCHÈ DE LUXEMBOURG, RECUEIL DE LEGISLATION 181 (28 mars 1989).

141. *See* Evans, *Private Change*, *supra* note 140, at 96. Damien Wigny, Executive Director, Kreditbank Luxembourgeoise, has stated, "[w]e will have to work hard and

D. *Hungary*

1. Banking Secrecy Law in Hungary

The Hungarian legislature passed a law codifying banking secrecy in 1977.[142] This law may allow Hungary to capitalize on the marketing advantages of banking secrecy. Under the law, a bank may disclose deposit account information only when the depositor or his legal representative agrees prior to disclosure,[143] when a Hungarian court pronounces a confiscation,[144] when a Hungarian court pronounces a judgment in which the depositor must pay damages to the State,[145] or during the settlement of a deceased depositor's estate.[146] Though no penal provisions exist for a breach of these disclosure restrictions, the bank is financially responsible for any losses so caused.[147]

Although Hungary's express consent and probate exceptions are typical of banking secrecy provisions in other countries,[148] the exceptions based on judicial decisions are notably more limited. These provisions permit disclosure only after a judgment in a Hungarian court proceeding and likely preclude disclosure during either foreign or domestic litigation. Absent either the customer's consent or a probate proceeding, ongoing judicial proceedings are inadequate, and a bank cannot disclose information without a final Hungarian judicial judgment.

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offer an excellent service." *Id.*

142. CIV. CODE [C. CIV.], arts. 534, 535 (Hung.) *translated in* E. CHAMBOST, *supra* note 11, at 210-11. The pertinent provisions of article 534 are as follows:

> Savings accounts are secret. No information concerning the details of these accounts can be given without the prior agreement of the depositor or his legal representative . . . .
>
> . . . .
>
> The bank is nevertheless obliged to inform the courts (or notaries) on their demand in the case of a judgment pronouncing confiscation, or establishing an obligation to compensate for damage in favour of the State, or in case of litigation in respect of the deceased holder of the savings account.
>
> . . . .
>
> With regard to monetary deposits made by private persons within the framework of a bank account agreement, the regulations governing savings accounts are applicable.

Id.

143. CODE CIVIL [C. CIV.] art. 534, para. 1 (Hung.). *See supra* note 142.

144. *Id.* art. 534, para. 2. *See supra* note 142.

145. *Id. See supra* note 142.

146. *Id. See supra* note 142.

147. *See* E. CHAMBOST, *supra* note 11, at 212.

148. *See, e.g., supra* note 79.

2. Banking Secrecy Policy in Hungary

Hungarian bankers hasten to enumerate the advantages of banking secrecy for foreign depositors.[149] At this early stage, however, Hungarian banking secrecy policy has no direction; although a review of the current status of the major banking secrecy powers might shed light on how Hungary might proceed. First, as mentioned previously, depositors are seeking alternative banking secrecy jurisdictions because of the recent erosion of Swiss secrecy laws. Second, Liechtenstein appears to be following Switzerland in relaxing its banking secrecy laws and policy.[150] Third, the future of Luxembourg's banking secrecy is uncertain considering pressures that the Community may place upon it.[151] Finally, Austrian secrecy arguably is not as absolute as Hungary's.[152] These considerations render Hungary an attractive alternative to customers who desire banking secrecy, particularly since many anticipate expanded east-west trade and investment after the fall of the Iron Curtain.

V. ATTEMPTS TO COMBAT BANKING SECRECY: THE UNILATERAL APPROACH TAKEN BY THE UNITED STATES

Since World War II, the United States has promoted the elimination of banking secrecy.[153] In recent decades, all three branches of the United States government have taken measures to frustrate the use of banking secrecy jurisdictions with various degrees of success. The predominantly unilateral nature of the United States measures, however, has been criticized abroad.[154] This section examines several means employed by the different branches of the United States government to thwart the use of banking secrecy jurisdictions, explores the reasons for the mixed success of United States efforts, and inquires into the controversy that surrounds the United States efforts.

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149. Evans, *Private Change*, *supra* note 140, at 96.

150. *See supra* Part IV.B.

151. Evans, *Private Change*, *supra* note 140, at 96.

152. *See supra* Part IV.A.

153. *See* Kelly, *United States Foreign Policy: Efforts to Penetrate Bank Secrecy in Switzerland from 1940 to 1975*, 6 CAL. W. INT'L L.J. 211, 215-17 (1976).

154. *See generally* RESTATEMENT (REVISED) OF FOREIGN RELATIONS LAW OF THE UNITED STATES § 420 reporter's note 1 (Tent. Draft No. 3, 1982). For a detailed analysis of this legislation, see J. VILLA, BANKING CRIMES: FRAUD, MONEY LAUNDERING, AND EMBEZZLEMENT, chs. 6, 8 & 9 (1989).

A. *Legislative Means: The Banking Secrecy Act and Its Progeny*

1. The Banking Secrecy Act of 1970

In 1970, the United States Congress enacted the Currency and Foreign Transactions Reporting Act, commonly known as the Banking Secrecy Act, as Title II of the Bank Records and Foreign Transactions Act.[155] The Banking Secrecy Act and its regulations[156] impose various reporting requirements on individuals and assorted "financial institutions" for certain financial transactions.[157] Chapter 2 of the Banking Secrecy Act, for example, requires financial institutions to file reports with the Internal Revenue Service for all deposits, withdrawals, exchange payments, or transfers that exceed ten thousand dollars involving a United States financial institution.[158] Under Chapter 3, if an individual exports from, imports into, or receives within the United States currency or other monetary instruments in excess of ten thousand dollars, that individual must file a report with the customs office.[159] Furthermore, Chapter 4 requires any citizen, resident, or person doing business in the United States to report on his or her tax return a financial interest in, or authority over, a foreign financial account.[160]

With the Money Laundering Control Act of 1986, Congress amended the Banking Secrecy Act to promote its enforcement.[161] One purpose of the amendments was to overrule a line of cases that allowed persons to escape liability when they structured their transactions to evade the reporting requirements.[162] The amendments also brought within the scope

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155. Pub. L. No. 91-508, § 291, 84 Stat. 1114, 1118 (1970) (codified in scattered sections of 12 U.S.C., including §§ 1730d, 1829b and 1951-59 (1988)).

156. *See* 12 U.S.C. § 1730d (1988) (empowering the Secretary of the Treasury to prescribe regulations concerning record keeping).

157. *See id.* § 1953; *see also* 31 C.F.R. § 103.22 (1990). The term "financial institutions" includes a broad range of businesses such as banks, pawnbrokers, and travel agents. 12 U.S.C. § 1953(b).

158. *See* 12 U.S.C. § 1829b (referring to 31 U.S.C. § 5313 (1988) which mandates reports on domestic currency transactions); *see also* 31 C.F.R. § 103.22 (1990).

159. *See* 12 U.S.C. § 1829b (referring to 31 U.S.C. § 5316 (1988) which mandates reports on exporting and importing monetary instruments); *see also* 31 C.F.R. § 103.23 (1990).

160. *See* 12 U.S.C. § 1829b (referring to 31 U.S.C. § 5314 (1988) which mandates recording and reporting foreign financial agency transactions); *see also* 31 C.F.R. § 103.24 (1990).

161. Pub. L. No. 99-570, 100 Stat. 3207 (1986) (codified in scattered sections of 18 U.S.C. and 31 U.S.C. (1988)). *See also infra* notes 172-185 and accompanying text.

162. *See* Plombeck, *Confidentiality and Disclosure: The Money Laudering Control Act of 1986 and Banking Secrecy*, 22 INT'L LAW. 69, 84-85 (1988).

of the Banking Secrecy Act individuals either who prevent or attempt to prevent a domestic financial institution from filing a required report[163] or who cause such an institution to file a report that contains either a material omission or a misstatement of fact.[164] The amendments also provide for potential liability for persons who structure, attempt to structure, assist in structuring, or attempt to assist in structuring transactions with the intent to evade reporting requirements.[165] In addition, the amendments make it more difficult for certain institutions to obtain exemptions from the reporting requirements.[166]

The amended Banking Secrecy Act expressly permits the Secretary of the Treasury to define the term "at one time" as a "cumulation of closely related events" in the case of reporting requirements for all imports and exports of currency and monetary instruments in excess of ten thousand dollars.[167] By requiring a report when an individual "is about to transport"[168] money, rather than when an individual "attempts to transport" money, the new amendments provide for earlier apprehension of offenders of the import-export clause. Furthermore, the amendments increase both the severity of criminal penalties against and the supervisory power of federal agencies over financial institutions.[169]

Although the theory behind the Banking Secrecy Act, and its subsequent amendments, was to hinder persons who illegally take advantage of foreign banking secrecy accounts, in practice the legislation falls short of this goal. The Banking Secrecy Act is too voluminous to direct policy effectively, and it has assisted prosecutors in only a few isolated cases. The effect of these shortcomings is that the Banking Secrecy Act does little to deter the abuse of secret bank accounts abroad.[170] Most commentators agree that the Banking Secrecy Act is inefficient in combating the use of secret bank accounts.[171]

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163. 31 U.S.C. § 5324(1) (1988).

164. *Id.* § 5324(2).

165. *Id.* § 5324(3).

166. *See* Plombeck, *supra* note 162, at 86.

167. *Id.* at 86-87. *See* 31 U.S.C. § 5316(d).

168. 31 U.S.C. § 5316(a)(1).

169. *See* Plombeck, *supra* note 162, at 91-93; *see also* 31 U.S.C. § 5322 (penalties for violation).

170. *See* I. WALTER, *supra* note 1, at 245.

171. *See, e.g.*, Note, *supra* note 7, at 95-96; Comment, *Swiss Banks and their American Clients: A Fading Romance*, 3 CAL. W. INT'L L.J. 37, 56-57 (1972).

2. The Money Laundering Control Act of 1986

In 1986, Congress passed the Money Laundering Control Act[172] as part of a battery of legislation designed to combat the national drug problem. Persons are liable under the Money Laundering Control Act if they willfully perform financial transactions for the purpose of promoting other crimes. Under the Money Laundering Control Act, there are two new federal crimes: the "Money Laundering Crime" and the "Monetary Transactions Crime."[173]

The Money Laundering Crime prohibits any person from engaging in financial transactions or transporting monetary instruments with the intent to promote "specified unlawful activity;" with the intent to commit tax evasion or fraud; or with the knowledge that the transaction or transportation is designed either to conceal or disguise the nature, location, source, ownership, or control of the proceeds of a "specified unlawful activity" or to avoid a transaction reporting requirement under state or federal law.[174] The term "specified unlawful activity" includes federal offenses such as criminal enterprise offenses,[175] Racketeer Influenced and Corrupt Organizations Act (RICO) offenses,[176] controlled substances offenses,[177] and various financial misconduct offenses.[178] Given the broad *actus reus* requirements of transacting and transporting, the statute understandably requires a high degree of scienter.[179]

The Monetary Transactions Crime makes illegal an even broader range of specified financial transactions. For example, this provision applies to any person who engages or attempts to engage in a monetary transaction in "criminally derived property" that is both valued at more than ten thousand dollars and derived from "specified unlawful activity."[180] Like the Money Laundering Crime, the Monetary Transactions Crime also has a high scienter requirement of knowledge of the illegality of the activity.[181] To be found liable for the Monetary Transactions

172. *See supra* note 161 and accompanying text.

173. Plombeck, *supra* note 162, at 71.

174. 18 U.S.C. § 1956(a) (1988). *See* Plombeck, *supra* note 162, at 71-82 (detailed discussion of the scienter requirements and the prohibited acts).

175. 18 U.S.C. § 1956(c)(7)(C).

176. *Id.* § 1956(c)(7)(A).

177. *Id.* § 1956(c)(7)(B).

178. *Id.* § 1956(c)(7)(D) (including crimes such as bribery, embezzlement, and illegal arms sales).

179. *See* Plombeck, *supra* note 162, at 71-74 (discussing the refinements of the scienter requirement in the legislative history).

180. 18 U.S.C. § 1957(a).

181. *Id.*

Crime, the defendant only must know that the activity from which the property was derived was a felony and not that it was a "specified unlawful activity."[182]

The penalties for both the Money Laundering Crime and the Monetary Transactions Crime are severe. Under the Money Laundering Control Act, these offenses are subject both to civil and criminal fines and to the possibility of imprisonment.[183] Under certain circumstances, the Money Laundering Control Act compels perpetrators of the Monetary Transactions Crime to forfeit the gross receipts of money laundering.[184]

The Money Laundering Control Act represents a necessary improvement to the Banking Secrecy Act in which the United States Congress indirectly attempted to prohibit the use of foreign secret bank accounts in the furtherance of illegal activities.[185] Nevertheless, even after the Money Laundering Control Act, it is likely United States authorities only will have sufficient resources to make examples out of the most conspicuous offenders. Because the Money Laundering Control Act has only a minimal deterrence effect on the abusers of banking secrecy, this unilateral effort by the United States Congress is likely to escape significant criticism from banking secrecy promoters abroad.

B. *Judicial Means: Extraterritorial Assertion of Jurisdiction in Foreign Bank Account Cases*

Concerns of international comity[186] arise when the courts of one state attempt to subpoena bank records located in a foreign banking secrecy jurisdiction.[187] This is particularly true when both the state holding the

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182. Plombeck, *supra* note 162, at 73-74.

183. *See* 18 U.S.C. §§ 1956(a)(1)-(2), 1957(b).

184. *See* Plombeck, *supra* note 162, at 81-82; *see also* 18 U.S.C. § 1957(b).

185. Probably because it was a part of anti-drug legislation, the Money Laundering Control Act does not include insider trading as one of the specified illegal activities. For a discussion of how holders of secret bank accounts likely will evade detection, see *supra* Part III.C.

186. Under international comity, one nation will allow another to prescribe law within the former's borders, not out of any obligation under international law, but out of deference and mutual respect. *See* Hilton v. Guyot, 159 U.S. 113 (1895).

187. *See generally* Annotation, *Discovery of, or Compelled Access to, Records of Foreign Bank Accounts, in Federal Criminal Proceeding or Investigation*, 87 A.L.R. FED. 676 (1988).

Besides the extraterritorial exercise of jurisdiction, another unilateral judicial method to pierce foreign banking secrecy laws involves a court compelling the consent of the account holder to waive the secrecy protection. *See generally* Silets & Brenner, *"Compelled Consent": An Oxymoron with Sinister Consequences for Citizens who Patronize Foreign Banking Institutions*, 20 CASE W. RES. J. INT'L L. 435 (1988). When the

judicial proceeding and the state where the bank account is located have concurrent jurisdiction and rules of law that require inconsistent conduct. For example, one state may require an individual to disclose bank records while another state will protect the account information. A United States court, when weighing comity concerns, is in the precarious position of deciding impartially whether its interests in issuing the subpoena outweigh the other state's interests in protecting the bank account. More often than not, the United States courts enforce the subpoena, finding that their interests are paramount to those of the banking secrecy jurisdiction.

In *In re Grand Jury Proceedings Bank of Nova Scotia*,[188] the United States Court of Appeals for the Eleventh Circuit applied a balancing test derived from the Restatement of Foreign Relations Law[189] (the Restatement) and held that the United States interests in investigating persons who may have violated United States narcotics laws outweighed the interests of the Cayman Islands in adhering to its banking secrecy laws.[190] The court emphasized that the Cayman Islands banking secrecy laws were not absolute, since they contained exceptions for both criminal cases and when a depositor has waived the right to secrecy.[191] The court also found that the bank, by availing itself of the benefits of doing business in the United States, was subject to the authority of the United States courts.[192] The court's analysis and holding are representative of the majority of decisions that uphold extraterritorial assertion of jurisdiction in countries with banking secrecy laws.[193]

Supreme Court held that such compelled consent did not violate the self-incrimination provision of the fifth amendment, some heralded the doctrine as a cure-all to bank secrecy. Abrams, *Doe v. United States: Has the Veil of Foreign Bank Secrecy Been Lifted?*, 67 Taxes: The Tax Magazine (CCH) 238 (Apr. 1989). Still, the question remains whether the foreign banks will recognize "compelled consent" as actual consent. *Id.* at 241. Furthermore, the "compelled consent" doctrine would appear not to apply in jurisdictions that do not provide for the customer's waiver of secrecy protection. *See infra* note 196.

188. 740 F.2d 817 (11th Cir. 1984), *cert. denied*, 469 U.S. 1106 (1985).

189. RESTATEMENT (SECOND) OF FOREIGN RELATIONS LAW OF THE UNITED STATES § 40 (1965). Since *Bank of Nova Scotia*, the Restatement has been revised. *See* RESTATEMENT (THIRD) OF FOREIGN RELATIONS LAW OF THE UNITED STATES § 403 (1987) for the revised version of section 40.

190. *Bank of Nova Scotia*, 740 F.2d at 827-828.

191. *Id.* at 827 & n.15

192. *Id.* at 828.

193. *See, e.g.*, United States v. Davis, 767 F.2d 1025 (2d Cir. 1985); *In re* Grand Jury Proceedings, 691 F.2d 1384 (11th Cir. 1982), *cert. denied*, 462 U.S. 1119 (1983); United States v. First Nat'l City Bank, 396 F.2d 897 (2d Cir. 1968); Garpeg, Ltd. v.

By contrast, the United States Court of Appeals for the Seventh Circuit, in *United States v. First National Bank of Chicago*,[194] applied the Restatement's balancing test, but reached the opposite result. In *First National Bank of Chicago*, the defendant, the subject of an Internal Revenue Service administrative summons, argued that the Greek Bank Secrecy Act precluded its disclosure of bank records located in Greece.[195] Agreeing with the defendant, the court noted that, even with the depositor's consent, the Greek Bank Secrecy Act[196] punished disclosure of bank secrets.[197]

Moreover, the court distinguished decisions which upheld extraterritorial assertion of jurisdiction on two further grounds. First, the defendant in *First National Bank of Chicago* made a good faith effort to comply

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United States, 583 F. Supp. 789 (S.D.N.Y. 1984); United States v. Chase Manhattan Bank, 584 F. Supp. 1080 (S.D.N.Y. 1984).

194. 699 F.2d 341, 345-46 (7th Cir. 1983); *accord In re* Sealed Case, 825 F.2d 494 (D.C. Cir.), *cert. denied sub nom.*, Roe v. United States, 484 U.S. 963 (1987); Application of Chase Manhattan Bank, 297 F.2d 611 (2d Cir. 1962).

195. *First Nat'l Bank of Chicago*, 699 F.2d at 343.

196. The court included a translation of the extraordinary language of the Greek law, which reads as follows:

> Article 1: Deposits in Greek banks are regarded as secret.
>
> Article 2:
>
> 1. Governors, members of the board, [members of] other collective bodies, or employees of a bank who, in the course of their duties acquire knowledge of deposits, convey any information in any manner are punished with a minimum of 6 months' imprisonment.
>
> *The consent or approval of the depositor who has the right to secrecy does not change the punishable nature of the act.*
>
> 2. Upon conviction for the offense mentioned in the above paragraph, the court cannot order suspension of the penalty nor can it change a conviction to a fine.
>
> 3. The persons mentioned in paragraph 1, called upon as witnesses at a civil or criminal trial, cannot be questioned on the secret deposits, even though the depositor consents.
>
> Article 3: As an exception, information is allowed on secret bank deposits only by virtue of a specially justified decision of a domestic court, to the extent that the information is regarded as absolutely necessary for searching and punishing offenses which are regarded as felonies committed in Greece.

Id. at 344 n.2 (emphasis added). It should be noted that since *First Nat'l Bank*, Greece reportedly has passed new legislation on banking secrecy which lifts confidentiality in cases of criminal investigations. *See* Hope, *Greece 3; Interest Rates Soar-Banking*, Fin. Times, Survey (Feb. 27, 1990) (Nexis).

197. *First Nat'l Bank of Chicago*, 699 F.2d at 347. One author suggests that the court's allocation of special treatment to a law with strict language, such as the Greek law, will prompt other countries to rewrite their banking secrecy laws with stricter language. *See* Karzon, *supra* note 11, at 822-23.

with the subpoena. Second, *First National Bank of Chicago* exclusively involved the collection of taxes, whereas the other cases pertained to the enforcement of United States criminal laws and the protection of the grand jury process.[198]

Although the United States government has been successful in reaching bank records located in secrecy jurisdictions through the judiciary's extraterritorial assertion of jurisdiction, these judicial means are an inefficient way to combat the illegal use of secret bank accounts. One author has commented that the courts' actions rarely are successful and "cannot form the basis for a routine, orderly, cost-efficient enforcement procedure of the United States tax system considering the enormous volume of financial transactions occurring in secrecy havens."[199] Another problem with such cases is that foreign states perceive the United States assertion of extraterritorial jurisdiction as an unjustified imposition of its moral and legal standards on conduct within other countries.[200]

C. *Political and Diplomatic Means: The Swiss Saga and the Transformation from Unilateral Politics to Bilateral Diplomacy*

During World War II, Switzerland's decision to remain neutral resulted in friction between the United States and Switzerland. The United States government was suspicious of Switzerland because of their unwillingness to oppose the Nazi party[201] and because of their lack of antitrust laws, their liberal holding company laws, and their banking secrecy laws.[202] In particular, the United States and its Allies were concerned that the leaders of the Axis powers, upon losing the war, would hide flight capital and looted property behind the veil of Swiss banking secrecy.[203] Hence, the United States unilaterally froze 1.2 billion dollars of Swiss assets in the United States in an effort to cripple the Swiss economy.[204] The United States also initiated the Safehaven Program, which was designed to frustrate German attempts to hide funds in neutral countries.[205]

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198. *First Nat'l Bank of Chicago*, 699 F.2d at 346-47.

199. Karzon, *supra* note 11, at 819.

200. *See* R. BLUM, *supra* note 33, at 234-37.

201. Though the Swiss government officially took a neutral posture during World War II, public opinion seemed to oppose the Nazis. *See* Note, *supra* note 7, at 84 n.145.

202. *Id.* at 83.

203. *Id.* at 82.

204. *Id.*

205. *Id.* at 82-83. At the urging of the United States, the United Nations endorsed the Safehaven Program at the 1944 Monetary and Financial Conference at Bretton Woods, New Hampshire. *Id.* at 83.

After several unsuccessful attempts to uncover German assets in Swiss accounts,[206] President Roosevelt resolved to negotiate with the Swiss.[207] These negotiations gave rise to the Bern Decree in which Switzerland agreed to disclose information on German holdings in Switzerland.[208] Even after the Bern Decree, however, Allied investigators and Swiss authorities disputed the magnitude of German assets hidden in Swiss bank accounts.[209] As a result, the United States exerted further economic pressure on Switzerland by maintaining a trade freeze on all neutral countries after it had lifted the freeze from the rest of non-Allied Europe.[210]

The Allies and Switzerland eventually returned to the negotiating table and entered into an accord titled "Understanding Reached Between Allied and Swiss Governments."[211] Despite the Allies' satisfaction with the accord, certain imprecision in the wording of the agreement hindered Allied efforts to gain sufficient information regarding German held bank accounts.[212] For example, under the accord, Swiss authorities could not begin investigating German holdings until Swiss bankers reported the presence of German assets.[213] Moreover, Swiss cantonal law, rather than any bilateral agreement, determined whether an asset was designated "German" or "Swiss."[214]

The dispute between the United States and Switzerland over the issue of banking secrecy continued in the Interhandel Case,[215] a controversy that lasted nearly twenty years. During World War II, the United States seized the assets of General Aniline and Film Corporation (GAF) under the Trading with the Enemy Act,[216] because the United States believed that a German controlled Swiss holding company, Interhandel, held a

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206. As discussed above, some proponents of banking secrecy note that Switzerland codified its customs and common law of banking secrecy in response to Nazi attempts to confiscate Jewish money abroad. These proponents argue that banking secrecy is a cherished individual liberty indivisible from a free and democratic society. *See supra* note 16 and accompanying text. The Swiss reluctance to disclose information about Nazi bank accounts after the war, however, undermines this historical support for banking secrecy.

207. Note, *supra* note 7, at 83-84.

208. *Id.* at 84.

209. *Id.* at 85.

210. Kelly, *supra* note 153, at 221 n.22.

211. Understanding Reached Between Allied and Swiss Governments, *reprinted in* 14 DEP'T ST. BULL. 1121 (1946).

212. Kelly, *supra* note 153, at 224.

213. *Id.*

214. *Id.*

215. Interhandel Case (Switz. v. U.S.), 1959 I.C.J. Pleadings 15 (Mar. 21, 1959).

216. Pub. L. No. 65-91, 40 Stat. 411 (1917) (codified as amended at 50 U.S.C. app. § 1 (1988)).

controlling interest in GAF.[217] After the war, Interhandel sued to recover its seized assets, claiming that Interhandel did not fall within the scope of the Trading with the Enemy Act.[218]

The United States Attorney General requested pretrial discovery of various documents including particular Swiss banking records.[219] The Swiss refused the Attorney General's request, declaring that granting this request would violate Swiss banking secrecy laws.[220] After the lower courts dismissed Interhandel's action, the United States Supreme Court reversed and remanded the case for determinations of Interhandel's good faith attempts to comply with the discovery order, and possibly for a trial on the merits.[221] Meanwhile, the Swiss officially requested that the United States submit the dispute to arbitration or conciliation.[222] The United States rejected this request, and the Swiss brought an action in the International Court of Justice seeking either submission of the issue to arbitration or a restoration of GAF's assets. The court held in favor of the United States, because the Swiss had failed to exhaust all possible remedies in the United States.[223] Finally, in 1965, the countries settled the dispute, whereby the United States government sold the GAF stock and divided the proceeds between the United States and the Interhandel stockholders.[224]

After 1965, the United States government realized that United States citizens were using secret Swiss bank accounts to evade taxes and conceal profits from illegal activities.[225] The United States, acting unilaterally

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217. *See* Meyer, *supra* note 36, at 41; *see also* Note, *supra* note 7, at 87-88.

218. Societé Internationale Pour Participations Industrielles et Commerciales, S.A. v. McGranery, 111 F. Supp. 435, 437 (D.D.C. 1953), *modified*, 225 F.2d 532 (D.C. Cir. 1955), *cert. denied*, 350 U.S. 937 (1956).

219. 111 F. Supp. at 438.

220. *Id.* at 438-39.

221. Societé Internationale Pour Participations Industrielles et Commerciales, S.A. v. Rogers, 357 U.S. 197, 213 (1958).

222. Kelly, *supra* note 153, at 232-33. The Swiss requested arbitration under the Arbitration and Conciliation Treaty, Feb. 16, 1931, United States-Switzerland, 47 Stat. 1983, T.S. No. 844.

223. Interhandel Case (Switz. v. U.S.), 1959 I.C.J. Pleadings 6, 29-30 (Mar. 21, 1959).

224. Kelly, *supra* note 153, at 235-36. The settlement divided the 329.1 million dollar proceeds from the sale as follows: "1.5 million dollars was allocated to the expenses involved with the sale; 17.5 million dollars was allocated to the United States for back taxes; 120.9 million dollars was allocated to the Interhandel shareholders; and 189.2 million dollars was allocated to the United States for its war claims fund." *Id.*

225. Note, *supra* note 7, at 91. *See also Foreign Bank Secrecy and Bank Records: Hearings on H.R. 15073 Before the House Comm. on Banking and Currency*, 91st Cong., 1st and 2d Sess. (1969-70).

through its Congress, enacted the Banking Secrecy Act in order to combat this problem.[226]

The United States government also initiated diplomatic negotiations with Switzerland that eventually produced the bilateral Treaty for Mutual Assistance in Criminal Matters (the Mutual Assistance Treaty) in 1977.[227] The Mutual Assistance Treaty marked the first time the two countries had agreed to cooperate in the prosecution of activities considered to be criminal in both countries.[228] Under the Mutual Assistance Treaty, banks must disclose information if the offense either was punishable under the law of the "requested state," or was included in the Schedule of Offenses attached to the Mutual Assistance Treaty;[229] if the offense involves bookmaking, lotteries, or gambling;[230] or if the offender is involved in an organized criminal group.[231] From the United States perspective, however, the Mutual Assistance Treaty is deficient to the extent that it fails to address banking secrecy directly or to take into account tax evasion.[232] The Mutual Assistance Treaty provides assistance only in cases of tax fraud, which generally are deemed criminal in most Swiss cantons.[233]

In the early 1980s, the United States government, through the efforts of the Securities and Exchange Commission (SEC), continued its unilateral efforts to combat Swiss banking secrecy. The SEC brought actions in United States courts to enforce securities laws against investors alleged to have used Swiss banks to trade on insider information.[234] As a result

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226. *See supra* Part V.A.

227. Treaty for Mutual Assistance in Criminal Matters, *opened for signature* May 25, 1973, United States-Switzerland, 27 U.S.T. 2019, T.I.A.S. No. 8302 (*entered into force* 23 Jan. 1977) [hereinafter Mutual Assistance Treaty].

228. *See* Note, *supra* note 7, at 103-04.

229. Mutual Assistance Treaty, *supra* note 227, art. 4, para. 2(a).

230. *Id.* art. 4, para., 2(b).

231. *Id.* art. 6, para. 2(a). Subsequent correspondence interpreting the Treaty, however, suggests that assistance may be refused if the disclosure likely would result in prejudice to essential interests of the requested state. Letter from Shelby Cullom Davis, United States Ambassador to Switzerland, to Dr. Albert Weitnauer, Swiss Ambassador to the United States (May 25, 1973) *reprinted in* 27 U.S.T. at 2149, T.I.A.S. No. 8302 (1976).

232. *See* Note, *supra* note 7, at 104. Tax evasion was neither specified in the Schedule of Offenses nor considered criminal in Switzerland. *Id.*

233. *Id.* Another bilateral agreement that covers cooperation between the United States and Switzerland is the Convention Between the United States of America and the Swiss Confederation for the Avoidance of Double Taxation with Respect to Taxes on Income, *done* May 24, 1951, United States-Switzerland, 2 U.S.T. 1751, T.I.A.S. No. 2316. *See* Note, *supra note* 7, at 100-03 for a discussion of this treaty.

234. *See* SEC v. Banca della Svizzera Italiana, 92 F.R.D. 111 (S.D.N.Y. 1981)

of the SEC's partial success in these cases,[235] the United States and Switzerland returned to the negotiating table "to reach a more conciliatory position with regard to cooperation in insider trading investigations."[236] These negotiations resulted in the 1982 Memorandum of Understanding (the 1982 Memorandum)[237] of which Parts Two and Three are most notable.

Part Two states that a country must supply information if "the investigation relates to conduct which might be dealt with by the criminal courts" of each nation.[238] This clause, however, merely restates what already should be in force under the Mutual Assistance Treaty. Of greater significance is Part Two's declaration that "transactions effected by persons in possession of material non-public information could be an offense under articles 148 (fraud), 159 (unfaithful management), or 162 (violation of business secrets) of the Swiss Penal Code."[239] This statement indicates an effort to enlarge the general "good faith" underpinnings of Swiss business laws into something closer to insider trading law in the United States.[240] Interestingly, commentators have not branded the 1982

(holding that Swiss corporation could not hide behind Swiss bank secrecy laws so as to evade United States insider trading statutes); SEC v. Certain Unknown Purchasers of the Common Stock & Call Options for the Common Stock of Santa Fe Int'l Corp., [1981-82 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶98,323 (S.D.N.Y. Oct. 26, 1981). Unlike banks in the United States, Swiss banks are allowed to trade in securities in their own name on behalf of clients. Under this arrangement the orders to buy and sell are in the Swiss bank's name, making the tracing of the individual investor's activities nearly impossible. *See Banca della Svizzera Italiana*, 92 F.R.D. at 117; *Santa Fe Int'l Corp.*, [1981-82 Transfer Binder] Fed. Sec. L. Rep. at ¶98,323.

The SEC also sought to compel discovery of Swiss bank records under Rule 37 of the Federal Rules of Civil Procedure. Rule 37 allows courts to impose monetary sanctions on parties who refuse an order compelling discovery. FED. R. CIV. P. 37.

235. In *Banca della Svizera Italiana*, the United States District Court compelled the bank to release information. 92 F.R.D. at 113. In *Santa Fe Int'l Corp.*, the United States District Court for the Southern District of New York ordered an accounting of defendant's proceeds from allegedly illegal transactions and issued a temporary restraining order that prevented the defendants from disposing of assets related to the controversy. [1981-82 Transfer Binder] Fed. Sec. L. Rep. at ¶98,324.

236. Note, *supra* note 7, at 107.

237. Memorandum of Understanding, *done* Aug. 31, 1982, United States-Switzerland, *reprinted in* 14 Sec. Reg. & L. Rep. (BNA) 1737 (Oct. 8, 1982) [hereinafter 1982 Memorandum]. The legal force of a Memorandum should not be overestimated. It does not have the binding effect of a treaty; it merely represents an expression of intent by the governments of two nations. *See* Note, *supra* note 7, at 107 n.318.

238. 1982 Memorandum, *supra* note 237, pt. II(3)(a).

239. *Id.* pt. II(3)(b).

240. Though the United States has recognized as criminal the use of non-public information to take unfair advantage of fluctuations in securities markets since 1934, the

Memorandum as another United States effort to impose its moral and legal standards on conduct occurring outside its borders. The text of the 1982 Memorandum is important, then, not only as a prelude to the codification of Swiss insider trading laws,[241] but also as an example of how countries may reconcile seemingly conflicting laws, once they have examined the common underpinnings.

Part Three of the 1982 Memorandum, which incorporates the Bankers' Agreement,[242] states that certain activities, although not criminal under the Swiss Penal Code, may warrant disclosure under the Bankers' Agreement, because the activities suggest insider trading.[243] The Bankers' Agreement both defines insider trading for purposes of the 1982 Memorandum[244] and prescribes procedures for obtaining information through a Swiss Commission of Inquiry.[245] The Bankers' Agreement definition of insider trading protects the United States interest in prosecuting individuals who violate United States securities laws. Moreover,

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practice known as insider trading has been widespread and largely unchecked in Europe until very recently.

241. The Swiss legislature outlawed insider trading by enacting article 161 of the Swiss Penal Code in 1988. *See European Finance and Investment, supra* note 102. For background on the enactment of article 161, see Note, *supra* note 7, at 114-16.

242. *Agreement XVI of the Swiss Bankers' Association with Regard to the Handling of Requests for Information from the Securities and Exchange Commission of the United States on the Subject of Misuse of Inside Information, reprinted in* 14 Sec. L. & Reg. Rep. (BNA) 1740 (Oct. 8, 1982) [hereinafter *Bankers' Agreement*].

243. *See* 1982 Memorandum, *supra* note 237, pt. III(1).

244. An insider is defined as:

> a) a member of the board, an officer, an auditor or a mandated person of the Company or an assistant of any of them; or
>
> b) a member of public authority or a public officer who in the execution of his public duty received information about an Acquisition or a Business Combination or
>
> c) a person who on the basis of information about an Acquisition or a Business Combination received from a person described in . . . a) or b) above has been able to act for the latter or to benefit himself from inside information.

Bankers' Agreement, supra note 242, art. 5(2), at 1741.

245. The Commission of Inquiry processes requests for information only when:

> (1) the United States Department of Justice transmit[s] its written application to the Federal Office for Police Matters; (2) the inquiry include[s] documentation of evidence materially relevant to the investigation; (3) the inquiry identif[ies] specifically transactions in question; (4) the SEC establish[es] to the satisfaction of the Commission that material price or volume movements have occurred or that the transactions violated United States insider trading laws; and (5) the SEC agree[s] not to disclose the information to any person except in connection with its investigations.

Note, *supra* note 7, at 110 (footnotes omitted).

the Bankers' Agreement protects Swiss interests in maintaining the sanctity of banking secrecy, to the extent the practice does not facilitate the violation of United States securities laws, through the delineation of measures for the disclosure of information concerning bank records. Although United States courts claim to perform essentially the same balancing of interests in their application of the Restatement,[246] foreign banking secrecy jurisdictions are more likely to find such a balancing of interests palatable when achieved through diplomatic negotiations.[247]

In 1987, the United States and Switzerland negotiated a second Memorandum of Understanding (1987 Memorandum)[248] that is similar to the 1982 Memorandum and promotes the exchange of information between law enforcement officials of the United States and Switzerland during the course of investigations. The 1987 Memorandum, like its earlier counterpart, cautiously protects the interests of both the United States and Switzerland. Since the Swiss wanted to reduce United States strong-arm tactics, the two parties agreed to gather evidence through the Mutual Assistance Treaty rather than unilateral measures. Similarly, the United States wanted to reduce Swiss delays in providing information, and Switzerland committed to streamline its handling of United States requests for information.[249]

The United States and Switzerland have traveled a lengthy course to reasonable compromises on banking secrecy. At first, the Allies supported the strong-arm methods used by the United States to lift the veil of Swiss banking secrecy. However, during the Interhandel Case and the tax evasion and insider trading scandals, the United States appeared to have only its own interests in mind. As a result, commentators criticized the United States use of unilateral measures to combat banking secrecy. Eventually, the United States realized that unilateral measures were largely ineffective at combating banking secrecy. Although unilateral measures brought the Swiss to the negotiating table, the bilateral measures became welcome replacements.

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246. *See supra* note 189 and accompanying text.

247. Many banking secrecy jurisdictions are unlikely to negotiate, because they are not as vulnerable as Switzerland to the strong-arm economic and political pressures of the United States.

248. Memorandum of Understanding, *done* Nov. 10, 1987, United States-Switzerland [hereinafter 1987 Memorandum], *reprinted in* Note, *supra* note 7, at 119.

249. *See* Note, *supra* note 7, at 114; *see also* 1987 Memoranda, *supra* note 248, arts. II(2), III(3). At least one author has chronicled and praised the success of bilateral approaches to the banking secrecy issue. *See* Knapp, *Mutual Legal Assistance Treaties as a Way to Pierce Bank Secrecy*, 20 CASE W. RES. J. INT'L L. 405, 432-33 (1988).

VI. ATTEMPTS TO COMBAT BANKING SECRECY: A UNIFIED BANKING SYSTEM IN THE EUROPEAN COMMUNITY PROMPTS DISCUSSION OF MULTILATERAL APPROACHES

Up to now, the European Community has been the chief international organization to pursue seriously the resolution of the banking secrecy issue.[250] In 1977, the Community adopted the First Banking Directive.[251] The First Banking Directive maintained the status quo of banking secrecy in each country.[252] In 1989, the Council adopted the Second Banking Directive.[253] The provisions concerning banking secrecy in the

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250. In 1985, an OECD report recommended that Member States relax their banking secrecy laws, but Switzerland, Luxembourg, and Austria opposed the report. *See* OECD, TAXATION, *supra* note 19, at 5. At least two authors have suggested that the International Monetary Fund (IMF) might be the proper organization to resolve the banking secrecy issue. *See* Note, *supra* note 7, at 118; I. WALTER, *supra* note 1, at 291. Recently, Belgium has enlisted the support of the IMF to pressure Luxembourg to relax its stance on banking secrecy. *See Support for Tax Harmonisation*, World Tax Rep., Finance/Business (June, 1990) (Nexis).

The OECD met in May 1990 to discuss ways to fight money laundering. The proposals included a partial lifting of banking secrecy under certain circumstances. *Western Nations Agree to Expand Fight Against Money Laundering*, Reuters, May 30, 1990 (Nexis).

251. *First Council Directive on the Coordination of Laws, Regulations and Administrative Provisions Relating to the Taking up and Pursuit of the Business of Credit Institutions.* 20 O.J. EUR. COMM. (No. L 322) 30 (1977) [hereinafter *First Banking Directive*].

252. The pertinent text of the First Banking Directive reads:

> *Article 12*
>
> 1. Member States shall ensure that all persons now or in the past employed by the competent authorities are bound by the obligation of professional secrecy. This means that any confidential information which they may receive in the course of their duties may not be divulged to any person or authority except by virtue of provisions laid down by law.

Id. art. 12(1), at 36. At least one author, however, questioned whether the words "except by virtue of provisions laid down by law" meant only statutory law or common law as well. *See* Case & Comment, *EEC Bank Secrecy Provisions*: Hillegom Municipality v. Hillenius, 1987 LLOYD'S MAR. & COM. L.Q. 251.

The other provisions of article 12 essentially permit a bank to divulge information in summary form for the purposes of running the banking business. *See First Banking Directive*, *supra* note 251, arts. 12(2), (3), at 36.

253. *Second Council Directive of 15 December 1989 on the Coordination of Laws, Regulations and Administrative Provisions Relating to the Taking Up and Pursuit of the Business of Credit Institutions and Amending Directive 77/780/EEC*, 32 O.J. EUR. COMM. (No. L 386) 1 (1989) [hereinafter *Second Banking Directive*].

Second Banking Directive merely restate the confirmation of banking secrecy contained in the First Banking Directive.[254]

These Directives, however, fail to reflect accurately the present debate over banking secrecy among Community members. With the unification of the banking system scheduled for 1992 and the removal of restrictions on capital transfers between Member States in 1990, most Community members fear that their residents will transfer their bank deposits to Luxembourg banks because of Luxembourg's liberal banking secrecy laws and low taxes.[255] Indeed, Luxembourg's current policies enable citizens of any Member State to commit massive tax evasion by simply transferring their holdings to a Luxembourg account.[256] Not surprisingly, Community members have recommended several proposals to prevent this unpleasant occurrence.

For various reasons, however, at least one Member State has objected to each proposal. The original proposal required each Member State to adopt a minimum fifteen percent withholding tax on all investment income.[257] The minimum withholding tax would reduce Luxembourg's competitive advantage, without directly infringing upon banking secrecy, by requiring all Community banks to withhold at least fifteen percent of their aggregate investment income. However, Great Britain, West Germany, and Luxembourg have objected to this proposal.[258] As an alternative, France has proposed that each country adopt legislation requiring banks to lift secrecy in cases of legally justified suspicion of tax fraud.[259]

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254. The pertinent text of the Second Banking Directive reads as follows:

Article 16

Article 12 of Directive 77/780/EEC is hereby replaced by the following:

'*Article 12*

1. The Member States shall provide that all persons working or who have worked for the competent authorities, as well as auditors or experts acting on behalf of the competent authorities, shall be bound by the obligation of professional secrecy. This means that no confidential information which they may receive in the course of their duties may be divulged to any person or authority whatsoever, except in summary or collective form, such that individual institutions cannot be identified, without prejudice to cases covered by criminal law.'

Second Banking Directive, supra note 253, art. 16, at 8.

255. *See Luxembourg Leads Opposition to Anti-Tax Fraud Plan*, Fin. Times, Int'l Banking Rep., Jan., 1990 (Nexis).

256. *Id.*

257. *See Taxation on Savings*, Fin. Times, Fin. Reg. Rep., Feb., 1989 (Nexis). To protect the Community's competitive position, this withholding tax would not apply to account holders who are residents of countries outside the Community. *Id.*

258. *See Luxembourg Opposes Anti-Tax Fraud Plan, supra* note 255.

259. *Id.*

Only Luxembourg objects to this proposal.[260] Another French proposal involves bureaucratic obligations on the part of banks to make declarations of large cross border transfers.[261] This proposal, however, has received almost no support from any Member State.[262]

Although the Community has yet to resolve the banking secrecy issue, the relaxation of Luxembourg's banking secrecy laws seems inevitable. Ultimately, the countries are likely to reach a multilateral compromise that protects, to the greatest extent possible, the interests on both sides of the debate. In this process of compromise, countries other than the United States for the first time will have to endure the criticism that they are imposing their legal and moral standards outside their borders in order to protect domestic interests. Should the resulting compromise discredit banking secrecy, the terms of the compromise could provide an authoritative precedent for the United States in future negotiations with banking secrecy jurisdictions outside the Community.

VII. CONCLUSION

Any resolution of the banking secrecy question by the Community will not end the debate. On the contrary, non-secrecy jurisdictions will continue to confront the problem posed by banking secrecy jurisdictions outside the Community. Switzerland, which is not a member of the Community, has relaxed its banking secrecy laws primarily in a bilateral relationship with the United States. Although appearing to follow Switzerland's lead,[263] Liechtenstein is a sovereign country and may maintain its strict secrecy laws.[264] Furthermore, Austria and Hungary may cling to banking secrecy laws that could make them financial centers for the new capitalist economies of Eastern Europe.[265] Moreover, offshore banking secrecy jurisdictions near Europe, such as the Isle of Man, Jersey, and Guernsey, pose additional problems for the reformers of banking

260. *Id.*

261. *Id.*

262. *Id.* Aside from being contrary to the general goals of the Community, perhaps the Member States recognize the probable inefficiency of this proposal because of its similarity to the United States Banking Secrecy Act. *See supra* notes 155-85 and accompanying text. The recent proposal that money laundering should be made an offense throughout the Community is further evidence that the Community may be learning from the United States. *See Proposal to Make Money Laundering a Crime Throughout the EC Offered*, 54 Banking Rep. (BNA) 312 (Feb. 19, 1990).

263. *See supra* Part V.C.

264. *See supra* Part IV.B.2.

265. *See supra* Parts IV.A and IV.D.

secrecy.[266]

At the root of the traditional argument disfavoring large scale, multilateral approaches to reforming banking secrecy is the belief that the demand for secret money will always find a new supply. While this point may still be valid, the fact that the Community now sees it in their collective interest to reform banking secrecy should prompt commentators to evaluate the best methods of developing multilateral approaches.

The lesson to be learned from the recent bilateral approaches of the United States and Switzerland is fundamental to all treaty negotiations and applicable to future multilateral approaches to the banking secrecy debate. This experience shows that the interests of each country will be protected to the maximum extent possible without unduly infringing upon other countries' interests. This result requires an evaluation of whether the typical interests and their present state of protection are justifiable.

Although Switzerland and the United States have addressed a number of fundamental interests and their protection, many other interests have not been evaluated. For instance, consider whether the numbered accounts and accounts under false names legitimately protect the privacy interests of the depositor beyond the banking secrecy laws, or whether they merely add unnecessary wrinkles to an investigation. Further, it is arguable whether owner beneficiary trusts or "dummy" corporations serve any useful social purpose, or whether they merely increase the available layers of secrecy in a banking secrecy jurisdiction in order to evade prosecution under another jurisdiction's laws.

On the other hand, one might consider whether abolishing banking secrecy is worth the risk to an economy that depends on it, or whether it might serve all parties better to phase out banking secrecy slowly while planning for economic development in new industries. In addition, the historical traditions and legal bases of banking secrecy in certain jurisdictions merit a degree of respect. Although a worldwide resolution of banking secrecy hardly is imminent, these issues have ripened with the increasing globalization of economies and political structures.

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266. *See generally* E. CHAMBOST, *supra* note 11, at 168-74, 181-84 for a discussion of these countries' banking secrecy laws.

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