

The Chiasso Scandal of 1977 and the Birth of Swiss Due Diligence — overview and summary

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On 14 April 1977 the Schweizerische Kreditanstalt, known in Ticino as the Credito Svizzero and abroad as Credit Suisse, announced that irregular transactions at its branch in Chiasso had exposed the bank to a loss. Ten days later the branch director, Ernst Kuhrmeier, and two of his senior colleagues were arrested. Within weeks it became clear that the branch had for sixteen years channelled the deposits of Italian clients into a Liechtenstein establishment called Texon Finanzanstalt, which had lent them to Italian companies in wine, tourism and plastics under guarantees that the head office in Zurich had never seen. The commitments of this "bank within the bank" reached about CHF 2.2 billion, and the loss that the Kreditanstalt finally absorbed is put by the Historical Dictionary of Switzerland at about CHF 1.4 billion.¹ For a Swiss bank of the 1970s the figure was without precedent. For Lugano and Chiasso, which had grown since 1945 on the deposits of Italian clients, it was a public demonstration of what the lira economy had become.

This chapter asks how a branch of Switzerland's oldest large commercial bank could run a parallel institution for a decade and a half, why the affair broke in 1977, and how Swiss law and Swiss banking responded. Its argument is that the Chiasso scandal marks the birth of Swiss due diligence in banking. Before 1977 the identification of clients and the origin of their money were matters of discretion and custom, protected by Article 47 of the Banking Act. Seven weeks after the first announcement, the Swiss National Bank and the Swiss Bankers Association concluded an agreement that obliged every bank in Switzerland to verify the identity of its clients, to establish the beneficial owner of the assets in cases of doubt and to refrain from active assistance in capital flight and tax evasion. That agreement, revised eight times since, is today the CDB 20, whose material rules FINMA has incorporated into the federal law against money laundering.

The chapter builds on the two that precede it. Chapter D.I treats the Banking Act of 1934 and its Article 47 on banking secrecy, while Chapter D.II describes the post-war flight of Italian capital, the cash couriers known as *spalloni* and the foundation of banks and fiduciary companies in Lugano and Chiasso. Chapter D.IV continues the story with the money laundering cases of the 1980s and the introduction of Articles 305bis and 305ter of the Swiss Criminal Code in 1990. The present chapter takes the Chiasso affair from its origins to the trial of 1979, follows its political and regulatory consequences, traces the line from the agreement of 1977 to the Anti-Money Laundering Act of 1997 and the CDB 20, and ends with the due diligence obligations that a relationship manager in Lugano must apply today.

1 Conclusion

The Chiasso scandal grew out of the conditions that had made Lugano and Chiasso prosperous. Italian savers who had moved money across the border in breach of their own currency law wanted interest in a strong currency, a safe name and invisibility. Italian companies wanted credit without the questions of Italian banks. A branch director with a large personal following, working at a distance from a head office that measured his success by his results, connected the two through a Liechtenstein establishment and the guarantees of his bank. For sixteen years Texon Finanzanstalt functioned as a bank within the bank, and when the Italian recession after 1973 turned its loans into losses, its managers hid the losses by taking in more deposits. When the structure collapsed in April 1977, the Kreditanstalt assumed commitments of about CHF 2.2 billion and absorbed a net loss that the sources put between CHF 1.2 and 1.4 billion.

The consequences went far beyond the bank. The Ticino Court of Assizes sentenced the branch director and his deputy to four and a half years' imprisonment in July 1979, but the trial could address only the damage to the bank, since neither capital flight from Italy nor the evasion of Italian taxes was an offence under Swiss law. A member of the Ticino government resigned, the National Council debated the affair for a full day, and the Social Democrats launched a popular initiative against the abuse of banking secrecy that the people rejected on 20 May 1984. The lasting response was a private agreement. On 2 June 1977 the banks, the Swiss Bankers Association and the Swiss National Bank concluded the agreement on due diligence, which obliged every bank to identify its clients, to establish the beneficial owner in case of doubt and to refrain from active assistance in capital flight and tax evasion.

That agreement has proved more durable than any of the political proposals of the time. Revised in five-year cycles, purged of the Form B exception in 1992, supplemented by the criminal provisions of 1990 and integrated into the Anti-Money Laundering Act of 1997, it survives as the CDB 20, whose material provisions apply to banks as ordinance law through Article 35 AMLO-FINMA. Its forms A, K, S, T and R are the daily instruments of every relationship manager in Lugano. The questions it asks have widened from the identity of the client to the origin of the money, the tax status of the assets and the risk profile of the relationship. The core idea of 1977, that a Swiss bank must know who stands behind the money it accepts, remains the foundation of Swiss due diligence.

For the Lugano financial centre, Chiasso marked the end of an era in which the Italian client's discretion was the bank's highest value and the beginning of one in which discretion had to coexist with verification. The cases of the 1980s, described in Chapter D.IV, showed that this transition was slow and incomplete. The end of banking secrecy towards Italy after 2015, treated in Chapter E.II, completed it. A relationship manager in Lugano who knows the history of Texon understands why the forms exist and why a guarantee given outside the bank's books, a client relationship known to only one employee or an entity that belongs to nobody remain warning signs today.

2 In five sentences

From 1961 to 1977 the Chiasso branch of the Schweizerische Kreditanstalt channelled the deposits of Italian clients through Texon Finanzanstalt in Vaduz into Italian companies in tourism, wine and plastics, backed by bank guarantees that the head office in Zurich never saw. When the losses of these companies after the oil crisis could no longer be hidden, the bank announced the affair on 14 April 1977, the branch director Ernst Kuhrmeier and two colleagues were arrested on 24 April, and the bank assumed commitments of about CHF 2.2 billion with a net loss of about CHF 1.2 to 1.4 billion. The Ticino Court of Assizes sentenced Kuhrmeier and Laffranchi to four and a half years' imprisonment on 3 July 1979, a Ticino cantonal minister resigned, and the Social Democrats' banking initiative inspired by the affair was rejected by 73 per cent of voters and all cantons on 20 May 1984. The lasting response was the due diligence agreement concluded on 2 June 1977 by the banks, the Swiss Bankers Association and the Swiss National Bank, which obliged banks to identify clients, to obtain a declaration on the beneficial owner on Form A and to refrain from active assistance in capital flight and tax evasion. Revised in five-year cycles up to the CDB 20 and incorporated into federal law

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through the Anti-Money Laundering Act of 1997 and Article 35 AMLO-FINMA, that agreement remains the foundation of the know-yourcustomer practice that every bank and relationship manager in Lugano applies today.

3 Notes

1. Jan-Henning Baumann, "Schweizerische Kreditanstalt (SKA)", in Historisches Lexikon der Schweiz (HLS), version of 27 November 2012, <https://hls-dhs-dss.ch/de/articles/041821/2012-11-27/> ("Verlust von ca. 1,4 Mrd. Fr."); the figure of CHF 2.2 billion for the deficit is given in "Grandes affaires économiques suisses (26): le scandale de Chiasso, l'histoire d'une banque dans la banque", Le Temps, <https://www.letemps.ch/economie/grandes-affaires-economiques-suisse-26-scandale-chiasso-lhistoire-dune-banque-banque>. It also gives the date of the press release. ↩

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