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Analysis - Swiss tax deals preserve bank secrecy "lite"

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By Emma Thomasson

ZURICH (Reuters) - Two years ago, it looked like the foreign tax man might break into vaults which house about a third of the world's offshore wealth, tearing through the long Swiss tradition of protecting the privacy of banking clients.

But the outlines of tax deals Berne has struck with Germany and Britain, as well as the end to a U.S. probe into top bank UBS (UBSN.VX: Quote, Profile, Research), suggest there is still a healthy future for big Swiss private banks even if smaller players might struggle.

Under agreements signed with London on Monday, and expected with Berlin on Wednesday, Switzerland will help tax assets British and German citizens have stashed in secret accounts, potentially yielding billions of euros in extra revenue.

But it has managed to fend off demands to automatically exchange account information with other countries in exchange for levying a withholding tax on interest and investment income, dividends and capital gains, to be transferred annually to the tax authorities of the clients' home countries.

This, analysts say, will in part preserve the secrecy that has helped it build up a $2 trillion (1.3 trillion pounds) offshore wealth industry.

"Withholding tax set to save bank secrecy 'lite'," wrote the Swiss daily Tages-Anzeiger on Tuesday.

Switzerland has agreed to share information to stop the new tax being evaded if Britain provides the name of a suspected tax dodger, but will only do so in a limited number of cases and will not breach client privacy for "fishing expeditions."

"Given the situation that Switzerland has got into due to UBS and everything, the result is a good one as Germany and Britain have agreed to no automatic exchange of information, which would have been unthinkable," said Martin Janssen, professor of finance at the University of Zurich.

END TO STOLEN BANK DATA?

Angered by tax evasion, Germany, France and Italy -- whose citizens have some 470 billion Swiss francs (300 billion pounds) in untaxed accounts -- have all bought Swiss bank data from whistleblowers, souring relations with their Alpine neighbour.

Ties with Germany were particularly strained after Peer Steinbrueck, former Social Democrat German finance minister, said the Swiss were like Indians running from the cavalry prompting a Swiss politician to compare him to a Nazi.

But talks have been more constructive since centre-right governments came to power in both Germany and Britain and Switzerland now hopes their support for a withholding tax will set the tone for talks with other countries, scuppering a European Commission call for automatic exchange of information.

In return, Berne is demanding better market access for Swiss banks and an end to the purchase of stolen Swiss client data.

Cash-strapped governments are hoping the tax will yield billions in extra revenue, but experts have noted that similar deals in the past have only yielded limited funds and wily wealthy clients have often found ways to circumvent the rules.

"There will be some ways out, at least partially. Perhaps some of the money will move to Australia first and then come back in a couple of years if Switzerland introduces trusts like in the UK," said Janssen.

While the Swiss Bankers Association estimated that implementing the tax could cost hundreds of millions of francs, it does not expect a big flow of assets out of the country.

"Swiss expertise, innovation, discretion, international outlook and above all political, economic and social stability are still in place and represent the pillars of enduring success," it said in a statement.

UBS, which lost its crown as the world's biggest wealth manager during the financial crisis, announced on Tuesday it has stopped bleeding money for the first time since early 2008, boosted by deposits from Asians and the super-rich.

"TOO MUCH FEAR?"

Analysts at Citigroup said a withholding tax might only have an earnings impact for UBS and Credit Suisse of 1 percent, although higher for more offshore-dependent Julius Baer (BAER.VX: Quote, Profile, Research), while compliance costs could mean a hit of about 3 percent to banks' pretax margins.

"We argue that too much fear is still priced in and that a series of Swiss tax agreements could partly resolve concerns on the offshore business model," they said in a note.

Citi said UBS and CS have already done a lot to build up onshore businesses, with offshore European accounts making up "only" about 15 percent of managed assets. They are also well placed to attract the new rich in booming emerging markets.

PricewaterhouseCoopers said this trend, plus rising regulatory costs, would benefit big players.

"Large asset management institutions can cater to these new markets, but they are likely to remain closed to small banks," the accounting and advisory group said in a recent report, predicting more consolidation for the sector.

"The number of private banking institutions has fallen from 181 in 2005 to 170. This number will continue to fall."

Herbert Scheidt, the chief executive of mid-sized private bank Vontobel (VONN.S: Quote, Profile, Research), said the rate a withholding tax is set at would be critical with anything above 25 percent potentially driving assets to centres like Singapore and Hong Kong.

"It is a bitter pill to swallow but there is no other way. We thus put in place a viable solution for the future of the Swiss financial centre," he told the Handelzeitung newspaper.

(Editing by Sitaraman Shankar)