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Background Report: Commodities

Report of the interdepartemental plattform on commodities to the Federal Council

Executive Summary

Switzerland has a long tradition as one of the world's leading centres of commodities trading, whose importance has risen markedly in recent decades. Because of growing public interest in the commodities industry and the importance of the issue for both domestic and foreign policy, the FDFA, the FDF, and the EAER informed the Federal Council in the spring of 2012 of their intention to prepare – in consultation with the concerned agencies of all of the Departments – a report addressed to the Federal Council summarizing the available information relevant to the issue of commodities trading in Switzerland, together with a discussion of the challenges connected therewith and a set of recommendations.[1] Many of the subjects dealt with in the report are relevant not only to the commodities industry. The report also recalls that Switzerland, as a rule, does not pursue economic policies tailored to individual sectors, but formulates policy to create overall favourable conditions for doing business in all sectors, including the commodities industry, and for the people involved therein both at home and abroad.

The present report underscores the sizable economic and fiscal importance of the commodities industry for Switzerland. For certain commodities – such as crude oil, for example – Switzerland is the world's most important centre of trade. It is estimated that around 500 companies and some 10,000 employees are active in the commodities industry, which, in addition to trading, also comprises shipping, transaction financing, inspections services and product testing. The commodity cluster contributes some 3.5% to Switzerland's GDP.

The reasons for Switzerland's major role in global commodity trading can be traced to the country's long tradition in the industry and to the favourable conditions found here for doing business in all sectors. These include a stable and predictable political, economic, and legal environment, a competitive corporate taxation regime and a business-friendly regulatory climate. In addition to other factors that contribute to Switzerland's appeal as business location, such as the availability of well-trained personnel and a generally high standard of living, the country's sophisticated and stable financial system make it particularly attractive as a commodity trading centre. Commodity traders must be able to rely upon the availability of a highly performative financial sector for the hedging of risks and the financing of transactions. Conversely, a robust commodity trading sector offers financial service providers a welcome opportunity for diversifying their business activities.

[1] The security of Switzerland's supply with commodities is not subject of the present report. This issue has been dealt with in several reports answering Parliamentary requests.

The important place that Switzerland occupies in commodity trading brings with it a variety of challenges. As a business location, Switzerland faces intense international competition, also in the commodities industry, above all, from such places as Singapore, Dubai (United Arab Emirates), China (in particular, Hong Kong), the United States, the United Kingdom, and the Netherlands. Upcoming locations have succeeded in positioning themselves as attractive, as compared to Switzerland, particularly in the domains of taxation and regulatory costs, and actively campaign on their own behalf. There is no evidence, at present, of a general trend amongst companies to move away from Switzerland, but much will depend on whether Switzerland succeeds, also in the future, in providing a competitive legal and economic setting for conducting business. Switzerland thus faces the challenge of maintaining and strengthening the features that make it an attractive and reliable business location, including the competitiveness of its tax regime and the efficiency of its financial centres.

Switzerland has a strategic interest in supporting the sustainable development also of this industry. Commodities are strategic goods and the rising trade in commodities provides a stimulus for the job market and for tax revenues. As the industry increases in size, it brings with it additional challenges that must be taken seriously, among other, in the domain of human rights and environmental protection in resource-exporting countries, in the fight against corruption, and in connection with the phenomenon of the “resource curse” in developing countries. These challenges can also involve reputational risks for individual companies, and for Switzerland as a country, in particular, where the conduct of companies domiciled in Switzerland should run contrary to positions taken and supported by Switzerland in the domains of development policy, and the promotion of peace, human rights, and social and environmental standards.

All of these issues, and the questions tied to them – including those relating to transparency in product and finance flows, and in tax and regulatory matters – must be dealt with in a constructive and sufficiently nuanced manner, within the context of the country’s current financial, economic, foreign policy, and development policy objectives, and the solutions proposed should be presented before the appropriate international bodies. In this context, the merchanting of commodities and the extraction of resources must be treated as separate activities, even if certain international corporations operate in both sectors. The Federal Council expects of all companies operating in or out of Switzerland to conduct themselves responsibly, and with integrity, in complying with human rights, environmental, and social responsibility standards, both in Switzerland and abroad. It is especially in fragile states where governance is deficient that the population and the economy suffer as a result of non-compliance with international standards.

The present report, taking into consideration ongoing international developments, provides an overview of Switzerland’s commitments and the legal regime currently in force in Switzerland.

In the domain of financial regulation, the drafting of new statutory rules with respect to the off-exchange trade in derivatives is already underway. These reforms will increase transparency in derivative trading, including the trade in commodity derivatives, in keeping with the international standards by the G20 and the Financial Stability Board (FSB). In addition, Switzerland is today, for the most part, already in conformity with the International Organisation of Securities Commissions (IOSCO) Principles for the Regulation and Supervision of Commodity Derivatives Markets.

As concerns the fight against money-laundering, Switzerland implements the standards recommended by the Financial Action Task Force (FATF). Following the 2012 revision of the FATF recommendations, Switzerland now intends to strengthen its regime for combating money-laundering and the financing of terrorism. The consultation draft to this effect was passed by the Federal Council on 27.02.2013.

In formulating its policy on sanctions, Switzerland conforms with the resolutions of the UN Security Council. In addition, since 1998, Switzerland has also joined in sanctions enacted by the EU in practically all significant cases. Commodity sanctions are an important means of exerting pressure on countries and regimes, since they stop the flow of a significant source of revenues for the country against which the sanctions are directed.

With regard to financial flows between extractive industry companies and governments, the Federal Council welcomes greater transparency. For this reason, it actively participates in the Extractive Industries Transparency Initiative (EITI), and in this way promotes the disclosure of such payments. In addition, it follows attentively all international developments in this area, including regulatory projects in the USA (Dodd-Frank Act) and in the EU (financial reporting and transparency directives).

In international competition in respect of business location, an important consideration – even if it does not stand alone – is both the applicable rate of taxation and the structure of the tax regime. Certain of the corporate tax regimes currently in force in Switzerland have come in for criticism by the EU, because they treat domestic and foreign revenues differently. Within the framework of the Corporate Tax Reform III, currently being drafted, and the ongoing dialogue with the EU on corporate taxation, Switzerland's objective is to strenghten Switzerland's competitiveness as a business location, while seeking a solution that is adequate to the budgetary needs of the Confederation and the cantons and, at the same time, is also capable of finding a higher level of international acceptance.

Globally operative commodity groups – like other multinational enterprises – sometimes face criticism for setting up their corporate and transfer pricing structures in such a way as to shift their taxable income to countries with low rates of taxation. By means of double taxation agreements (DTAs) and tax information exchange agreements (TIEAs), Switzerland contributes to the ability of developing countries and emerging economies to take legal action against the use of abusive transfer pricing practices.

Because they often operate in fragile contexts, members of the commodity industry bear a special responsibility with regard, for example, to respect of human rights, the prevention of corruption, and protection of the environment. Although the primary responsibility for enforcing compliance with laws and standards lies, in principle, with the resource-extracting host states themselves, there is growing recognition internationally that with globalisation and the rising importance of private actors, additional solutions may be needed. Fragile and conflict-affected states often lack the capacities needed for dealing with these problems.

For this reason, Switzerland is actively involved in the development and implementation of international initiatives and standards, and supports various international instruments for the promotion of corporate social responsibility. It is expected of international corporations that, in addition to complying with statutory requirements both in Switzerland and abroad, they will also meet their duties of care and diligence as comprised in the notion of corporate social responsibility. Through its commitment to development, moreover, Switzerland contributes to the strengthening of governance in commodity-producing host countries. The central focuses of activity in this connection are, in particular, the building of democratic, legal, and tax policy capacities in the host countries, and the development of improved standards for transparency and financial reporting.

As concerns the existing legal situation with regard to the activities of multinational enterprises, it is to be noted that the right to bring action against a parent company before Swiss courts for acts committed by a subsidiary or a supplier in another country is limited, due, among other things, to the principle of territoriality. Swiss procedural law with regard to tort liability cases is based on the internationally recognised principle that jurisdiction should in all cases lie with the court that has the closest connection with the subject matter of the case and is thus in the best position to adjudicate on it.

* * *

In conclusion, it may be stated that Switzerland already does a great deal to guarantee both its competitiveness and its integrity as a centre for conducting business, including the business of commodity merchanting. Nevertheless, there do remain areas in which Switzerland's efforts can and should be reinforced. Based on the findings presented in the report, the Federal Council approved the 17 recommendations made in chapter 6.

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1. Introduction

Switzerland has a long tradition as one of the world's leading centres of commodity trading.[2] In recent years, the importance of the commodities industry in Switzerland has increased markedly. Switzerland is home to some of the world's largest, as well as numerous smaller commodity companies, all of which operate almost exclusively on the international market.

Commodity trading, which is conducted in a global market, has important consequences not only for Switzerland but also worldwide. It plays an important role in the allocation of resources, ensuring that raw materials find their way from countries where they are in oversupply to others with little or no natural resources themselves. Commodity trading conducted in an orderly, efficient and responsible manner thus contributes to sustainable global economic growth. Switzerland, with its sizeable commodities industry, makes an important contribution in this direction

Two of the main, but distinctly different, activities conducted by commodity companies, are the trading and the extraction of commodities. While some companies specialise in commodity trading, others concentrate on the production of commodities. There are, however, also companies that are involved at all stages along the value chain, from extraction and trading through processing or refining. In the Swiss commodities branch, the majority of companies are merchanting houses offering services throughout the entire supply chain. In addition, there are a large number of companies that provide services at the periphery of the commodities trading industry.

The increased importance of the commodities sector in Switzerland has been accompanied by growing public interest in the industry and has also brought with it a number of challenges. Switzerland faces international competition and strives to maintain and consolidate its competitive edge as a business location, also in the commodities sector. At the same time, the presence of large commodities companies in Switzerland can also have a bearing on foreign policy issues and the country's reputation. In addition, in recent years there have been numerous international efforts to achieve reforms in the regulation of financial markets, which also have an effect on the commodities sector. Moreover, due to the natural distribution of resources on the planet, many, though far from all, reserves of natural resources are found in countries where the rule of law is weak and the underlying economic situation is uncertain and large portions of the population live in great poverty. Particularly for companies active in the extraction of raw materials, this can create special challenges – with regard, for example, to respect for human rights or environmental standards – as there are no sufficiently detailed legal guidelines for orienting their conduct. The countries that are rich in natural resources, on the other hand, are faced with the challenge of learning to manage their natural wealth in a sustainable manner.

Because of growing interest in the commodities industry and the importance of the issue, the FDFA, the FDF, and the EAER informed the Federal Council of their intention to prepare – within the framework of the interdepartmental Working Group on Commodities and in consultation with the concerned agencies of all of the Departments – the present report, addressed to the Federal Council. The report is intended to provide an understanding of the importance of the commodities industry in Switzerland and, based on an analysis of international economic and political conditions, to outline the challenges and consequences this entails for Switzerland. These can be widely divergent, depending on whether the trading or the extraction of commodities is at issue. The economic importance of the industry in Switzerland will be dealt with in chapter 2. This will be followed in chapter 3 by a description of the current challenges (international competition in respect of business location, reputational risks, foreign policy issues, development policy issues). Chapter 4 will then address issues relating to the regulatory environment. These include aspects of financial market regulation, efforts to combat money laundering, sanctions, accounting standards, and tax matters. Chapter 5 then looks into the issues of corporate and government respon-

[2] The term commodities is used in this report generically to refer to fuel resources (e.g., petroleum or natural gas), mineral resources (e.g., copper, iron, aluminium, or gold), and agricultural products (e.g., grains, sugar, coffee or cotton).

sibility, presents instruments for responsible corporate governance, and explicates the cross-border legal situation with regard to the liability of holding companies and their subsidiaries. Chapter 6 closes the report with a set of conclusions and recommendations.

The focus of this report, therefore, will be on Switzerland's role as one of the world's most important host states with regard to commodity companies and the running of their international operations, as well as on the existing international and Swiss regulatory measures and developments within that domain. There are, without question, many other issues of interest in connection with commodities – e.g., the relationship between long-term availability of raw materials and economic growth, the continuity of industrial production even in periods of disrupted supply, or issues of resource efficiency.[3] These and other fundamental questions concerning commodities have not been addressed in the present report, the focus of which has been restricted to the issue of companies that conduct their operations in Switzerland.

It should further be emphasised that Switzerland does not pursue a policy tailored to the commodities sector. Hence, many of the subjects addressed in the present report – including such issues as corporate taxation, reforms in the domain of OTC derivatives,[4] corporate responsibility, or development policy – are far from being relevant only to the commodities industry, and must, therefore, be considered within a larger context.

2. Importance of the commodities Industry for Switzerland

2.1. Historical development

The strong growth of the commodity sector in Switzerland in recent years (see below, section 2.2) often leads to people forgetting that transit trade in this country has a long tradition.

Commodity merchanting in Switzerland goes back as far as the 18th century. Some early companies, such as cotton merchant Paul Reinhart AG, founded in the late 18th century under the name Geilinger & Blum, are still in business today. Others have, in the meantime, abandoned trading, but still profit from knowledge acquired in that branch for endeavours in other business sectors. Thus, for example, the DKHS Holding AG (DiethelmKellerSiberHegner), which was created through the merger of three mid-19th century trading companies, today specialises in providing market expansion services in Asia. Other companies, such as the Volkart Brothers or André Cie. trading houses, have become merely holding companies (Volkart Brothers), or have in the meantime gone bankrupt (André Cie.). Their business was then taken over by other trading companies in Switzerland. Also worth mentioning is the Union Trading Company (UTC), which in the 19th and 20th centuries grew to become one of Switzerland's most important trading companies, but is today no more than a small management company.

While only a small number of the traditional trading houses are today still active in commodity merchanting, since the beginning of the 20th century important companies have either been founded in or have moved to Switzerland and continue to this day to have a dominant influence on the country's commodities industry. It is notable that it was often during, or shortly after, major crises that many of the foreign commodity companies based in Switzerland chose to relocate parts of their business activities to stable and neutral Switzerland. Thus, for example, in 1915, during the First World War, the Société Générale de Surveillance (SGS) moved its headquarters to Geneva. That company is still today the largest commodity inspection and certification compa-

[3] The Federal Council has dealt with security of supply issues in detail in its 2008 Foreign Trade Strategy paper, and in its responses to various Parliamentary requests: Response to Postulate 08.3237, by Stadler: Federal Council report, "Food Crisis, Raw Material and Natural Resource Shortages"; In addition, the EAER has prepared a natural resource strategy paper on critical natural resources (2011). To complement this, the Federal Council recommended on 22 August 2012 the adoption of Postulate 12.3475 by Schneider-Schneiter, "Rare Earth Metals: Resource Strategy". The Postulate was adopted by the National Council on 28 September 2012. In addition, the FOEN publishes at regular intervals a report on the environment (http://www.bafu.admin.ch/umwelt/10822/index.html?lang=en). The 2013 Environmental Report (anticipated date of publication, June 2013) will have a special focus on the question of natural resource supplies.

[4] OTC (over-the-counter) derivatives are financial instruments not traded on a formal securities exchange.

ny in the world. After the Second World War, several US trading companies, such as Cargill, opened their European offices in Switzerland. They were followed, shortly thereafter, by cotton traders who had left Egypt due to the instability there. In the wake of the oil crisis of the 1970s, the first oil traders, including Vitol, took up domicile in Switzerland. They were joined after the end of the Cold War by other oil traders such as Trafigura or, more recently, the Russian companies Litasco and Gunvor.

The growth of Switzerland's commodities sector in recent decades has, however, not been solely a result of the relocation of large foreign trading houses that decided to open a branch office or their European or international headquarters in Switzerland. During that same period many new commodities companies were created in Switzerland and are still in the country today. Some of them have developed into global corporate groups, among other things, through acquisitions. Thus, for example, Südelektra AG, which was founded in 1926 by a group of private banks for the financing of infrastructure projects, in 1999 became the Xstrata group. In 1974, Marc Rich founded the Marc Rich + Co AG, which, following his departure in 1994, was renamed Glencore. Mercuria, founded by commodity traders in 2004, has today already become one of the largest oil trading companies in the world.

In addition to these major commodity companies, there are also very many small traders. Moreover, there is also a large number of companies that do not themselves engage in trading, but which provide essential services for commodity traders. This has given rise to a diverse hub of companies active in and around the commodities industry, comprising, in addition to the merchanting companies themselves, banks that specialise in the financing of commodity trading, companies providing inspection services, shipping companies, insurance companies, law firms, escrow agents, and consultants.

2.2. Current status

Economic Importance

Switzerland, as described in the foregoing section, has developed into one of the world's most important centres of international commodity trading. In certain areas of the country, in particular Geneva and Zug, but also in Lugano, veritable hubs of commodity traders have formed.

An approximate notion of the economic importance of this phenomenon can be garnered from the data on merchanting volume, which in Switzerland is attributable largely to commodity trading (2011: 94%).[5] Roughly three fifths of that volume are attributable to trading in energy sources (2011: 59%); one fifth to non-metallic mineral products and metals (2011: 20%), and approximately one sixth to agricultural and forestry products (2011: 15%). To record merchanting in the balance of payments, the SNB collects data from merchanting traders domiciled in Switzerland for two parameters: sales revenues abroad (gross receipts from the sale of goods abroad) and expenses abroad for purchases of goods and other expenses, such as quality control, transport, hedging costs, insurance, and salaries. The difference between these two figures is counted as net receipts, that is, as receipts from merchanting, and is recorded in the balance of payments as exports of services (see Box 1 for further details). As noted above, merchanting traders create a demand for numerous further services inside Switzerland. Because these services are paid for out of their net receipts, however, net receipts from merchanting can be construed as representing the total contribution of the commodity hub to the GDP. The sales revenues from abroad of merchanting traders in Switzerland totalled CHF 763 billion in 2011,[6] and were thus higher than Switzerland's gross domestic product of approximately CHF 580 billion. Net receipts rose from somewhat more than CHF 1 billion in the year 2000 to approximately CHF 11 billion in 2007 and CHF 20 billion in 2011 (see Figure 1). In 2010, for the first time, the share of merchanting in the

[5] Source: SNB, Swiss Balance of Payments 2011, p. 37. The remaining 6% are divided between leather, rubber, plastics and chemicals (4%) and miscellaneous (2%).
[6] Ibid., p. 37.

gross domestic product (GDP) surpassed that of tourism (2011: 2.7%)[7], on the expenditure side, and rose to as high as 3.4% in 2011. As shown in Figure 1, in 2010 merchanting also replaced receipts from the cross-border commission and services business of Switzerland's banks as the top service exports category. Receipts from the financial services of the banks have been in decline since 2007 and their share in the GDP has fallen to 2.6%.

In principle, the rise in net receipts from merchanting – and the accompanying positive impact on domestic net value added – can be seen as a result of either price or quantity effects. Given the fact that there exists, according to the SNB, a relatively high correlation between commodity prices and the net receipts of merchanting traders,[8] it is likely that the rise in commodity prices over the past decade contributed substantially to the rise in net receipts. An additional factor, however, was presumably also the fact that merchanting traders have greatly expanded their activities (quantity effect). In addition to these quantity and price effects, however, it is possible that the rise in merchanting receipts is also attributable to the fact that the base for the collection of merchanting data in Switzerland was enlarged through a rise in the number of merchanting traders. According to the SNB, after 2008, it was essentially due to the entry into the market of new merchanting companies in Switzerland that a decline in net receipts from merchanting could be avoided.[9] Without these new market entrants, a return to 2007 levels would not have been achieved until 2011.

Box 1: Merchanting

Merchanting is defined as a transaction in which a company in Switzerland purchases goods from a supplier abroad and then sells those goods on to a buyer abroad. As a rule, the goods do not cross the border into Swiss territory and are, in consequence, not subject to Swiss customs duties. The condition of the goods that are traded in merchanting transactions normally remains unchanged. Merchanting transactions must be reported at the transaction price valuation.

Example: a domestic merchanting trader purchases crude oil in Russia (expenditures) and then sells it to a buyer in Germany (receipts), without the crude oil passing Swiss customs.

Merchanting traders not only buy and sell commodities, they are also involved in organising transport in connection with the transaction, insurance against loss of or damage to the goods, storage at loading and off-loading terminals, and verification of the goods. Above all, merchanting traders must arrange for the financing of their capital-intensive commodity transactions.

In keeping with a revision of the international standards on international trade in services, merchanting transactions will no longer be considered as trade in services, after the new standards go into effect (2014), but will be counted as trade in goods.

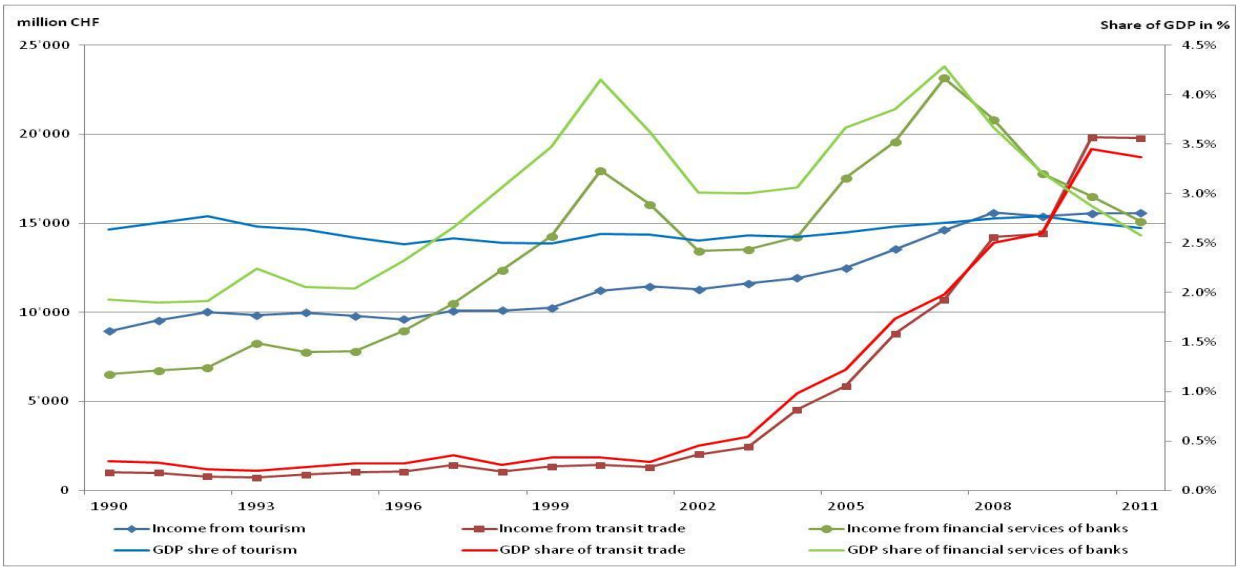
Source: SNB, Statistical collection and entry, Notes; Swiss Balance of Payments 2011; Zeier Stéphanie, Die Volkswirtschaft, 1/2 2010, "Konjunkturindikatoren: Dienstleistungshandel der Schweiz mit dem Ausland."

[7] Employment data tourism (gastronomy and tourism) for 2011: equivalent to 145,000 full-time positions (total: 217,300 employees. Source: Swiss Federal Statistical Office, FSO). In comparison thereto the (difficult) estimate with regard to employees within the commodities trading: see page 10 of this report.

[8] See the notes in the Swiss Balance of Payments 2011, p.38: The correlation between the price index for commodities and net receipts, as calculated by the SNB, was 0.56 for the period 1993 to 2008.

[9] In this study, the SNB defines "new entrant" as follows: "A company is deemed to be a new entrant in Switzerland if it was included in the statistical reporting population for the first time in 2009 or later, and was registered in the Swiss Commercial Register 2–3 years previously." (SNB Swiss Balance of Payments 2011, p. 38).

Figure 1: Receipts from tourism, merchanting, and financial services abroad by banks, in millions of Swiss francs (left scale) and share of GDP (nominal, based on expenditure metric, right scale).



Source: SNB, Monthly Statistical Bulletin, September 2012, Q1a Current account – components; SECO, Annual Aggregates of GDP, based on expenditure side data.

Although the role of imports and exports to and from Switzerland is, as a whole, negligible, special mention must be made of precious metals, which constitute an exception, and for which large physical movements are recorded. In 2011, total imports and exports of precious metals (gold, silver, platinum), as registered by the Federal Customs Administration, amounted to approximately CHF 100 billion in imports and CHF 80 million in exports. In the specific case of gold, the movements are attributable to the banks and the refineries.[10]

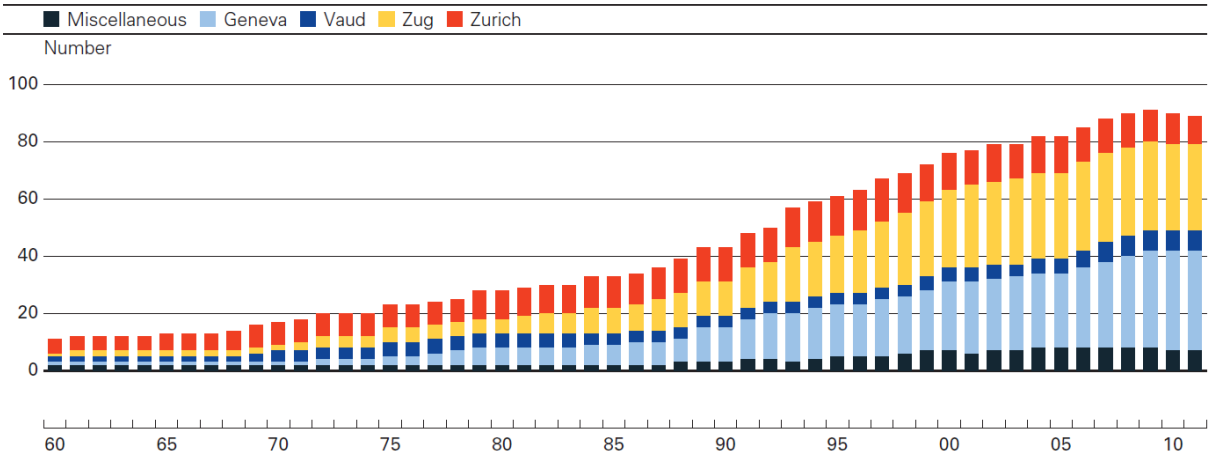
It is difficult to accurately estimate the number of companies and employees active in the industry. The 2008 census of companies published by the Federal Statistical Office (FSO) does, to be sure, contain data on the number of companies, and the number of employees and equivalent full-time positions (EFTP) broken down by sectors. However, because the General Classification of Economic Activities (NOGA [Nomenclature générale des activités économiques]) does not list commodity trading companies as a separate category – they are included both under the headings of *wholesale trade* and *holding companies* – the statistics do not make it possible to determine how many of those companies and employees belong specifically to the commodities industry.

For collecting the statistics on merchanting receipts, which are listed separately in the Balance of Payments, the SNB requests information from companies that are recorded in the Commercial Register as being primarily active in merchanting and whose transaction volume is above a certain threshold value.[11] There is, however, no duty on the part of the companies to furnish information of their own accord, but only at the request of the SNB. For this reason, it may be assumed that the number of merchanting companies listed by the SNB represents a lower limit. That number has been at roughly 90 since 2008 (see Figure 2). A listing by cantons shows, moreover, that the number of companies in the cantons of Vaud and Zurich has remained relatively constant, while the number of companies in the cantons of Geneva and Zug has risen sharply.

[10] The most important item is listed under tariff number 7108.1200, representing "*Gold, including platinated gold, in raw form, for other than monetary purposes (other than in powder form)*" (2011 imports CHF 96 billion / exports CHF 76 billion). This tariff number is not included in the published foreign trade statistics. While data is published, no breakdown by countries is provided. Source: www.ezv.admin.ch.

[11] Where sales volume exceeds 100,000 francs per quarter, companies have a duty to provide information.

Figure 2: Distribution of merchanting companies by canton



Source: Swiss merchanting companies registered in the Commercial Register, in: SNB, Swiss Balance of Payments 2011, p. 41

Other figures on the number of companies and employees in the sector are available from industry associations. According to the Geneva Trading and Shipping Association (GTSA), there are some 400 companies in the Lake Geneva region that are directly connected with commodity trading, and some 8,000 jobs that depend on the commodities industry.[12] According to the Lugano Commodity Trading Association (LCTA), the figures for the Lugano region indicate that there are roughly 70 companies and 1,000 jobs.[13] The Zug Commodity Association (ZCA) has not yet published any of its own figures in this regard. However, the Office of Economic Promotion of the Canton of Zug operates on the assumption that wholesale trading in the canton of Zug contributes roughly 25% of the canton's gross value added.[14]

A study on the future prospects for banking in Switzerland, published jointly last year by the Swiss Bankers Association and The Boston Consulting Group, estimates that there were some 520 companies operating in Switzerland in 2010 (of which, 370 in the Lake Geneva region, and 50 in Zug and Lugano) along the entire commodity value chain (trading, shipping, transaction financing, inspections, and product testing), and that those companies had some 10,500 employees (8,000 in the Lake Geneva region, 2,500 in Zug and Lugano).[15]

There are, at present, no figures available on tax revenues deriving from the commodities industry. It may be assumed, however, that tax revenues linked to commodities trading are significant and that their impact in Switzerland is felt not only at the regional level, but also nationally. Included in those tax revenues are those collected from the companies as well as those paid by their employees (capital tax, income tax, wealth tax, etc.).

Structure of the commodities industry in Switzerland

In the Handelszeitung's ranking of the largest companies in Switzerland by revenue, the commodities branch is the industry most often represented among the top 20 Swiss companies. In 2011, commodities companies occupied the three highest positions: Vitol (CHF 279.1 billion in revenues),[16] Glencore International (CHF 174.9 billion in revenues), and Trafigura (CHF 114.7 billion in revenues).[17] Companies in the industry can be divided into those that are involved at all

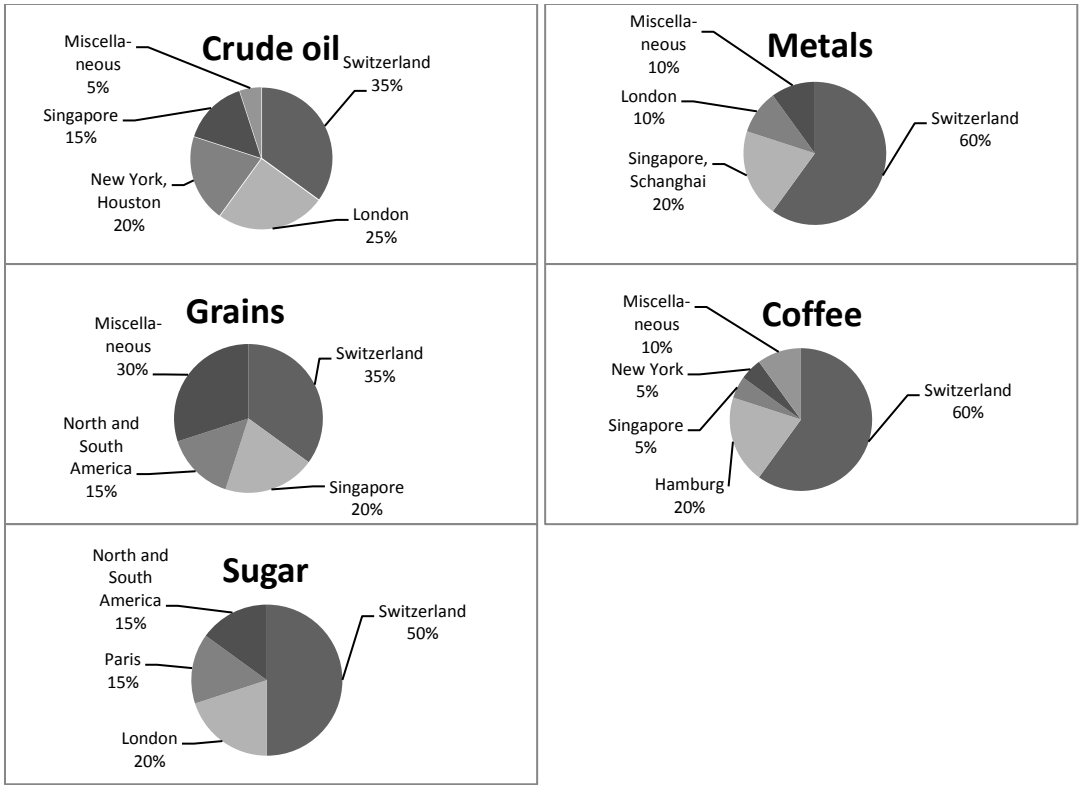
[12] Information published on the GTSA website.
[13] Information published on the LCTA website.
[14] Office of Economic Promotion, Zug, March 2011, zug: newsletter, "Finanzplatz Zug: Stark in Nischen, Gewinn aus Clusterstrukturen", No. 2. The share of commodity trading companies included in the total number of wholesalers is not specified, however.
[15] Swiss Banking and BCG, "Banking in transition – future prospects for banking in Switzerland" [in German], 2011.
[16] 2011 was the first time that Vitol published its revenue and growth figures.
[17] Handelszeitung, "Top 2012, Die grössten Unternehmen der Schweiz", 2012 edition.

stages across the value chain (vertically integrated), from extraction/production to trading, and those companies involved exclusively in commodity trading. The different sectors within the industry include energy resources (such as oil, gas, coal, and ethanol), mineral resources (such as iron, industrial metals, and precious metals), and agricultural products (such as grains, coffee, sugar, and cotton). Companies such as Vitol, Trafigura, Mercuria, Gunvor, and Litasco deal mainly in energy resources. Cargill and Louis-Dreyfus, for example, are active principally in the trading of agricultural commodities.[18] In addition to these large companies, there are also a large number of smaller companies in the industry, which are principally involved in trading and, for the most part, focus on a single category of commodity. The merger of Glencore and Xstrata[19] will lead to the creation of one of the world's largest vertically integrated commodity companies, active in all three sectors of the industry, but nevertheless focused predominantly on fuel and mineral resources. The merger is still awaiting approval by the Chinese anti-trust authorities; the EU and South African authorities have already given their green light. Overall then, it can be said that the Swiss commodities industry is dominated mainly by merchanting companies, with a few prominent exceptions.

Market share of different trading centres for the main commodity sectors

Figure 3 shows the global market share of transactions in various commodities traded through Switzerland. It should be noted, however, that the source of this information is an analysis by the industry associations, and that the figures could not be verified.

Figure 3: Market share of various trading centres based on industry figures



Source: GTSA (adapted), in: NZZ am Sonntag, 28 November 2010, and Tribune de Genève, 19 June 2012

[18] Cargill's headquarters are located in the USA; Louis-Dreyfus is based in Rotterdam. Both, however, maintain sizeable trading divisions in Switzerland.

[19] Both are publicly listed companies, Glencore on the London and Hong Kong stock exchanges, Xstrata on the London Stock Exchange.

Lake Geneva region[20]

The commodity hub Geneva is home not only to merchanting companies, but also to banks that specialise in commodity trade financing (see section 2.3), shipping companies (e.g., MSC, Riverlake), product testing companies (SGS, Cotecna), and other industry-related companies. The GTSA provides the following figures with regard to Geneva's market share in the main commodity sectors: roughly one third of the world trade in crude oil and oil products passes through Geneva. Some 75% of Russian crude oil is traded through Geneva. Among agricultural commodities, approximately one half of the global trade in coffee (with an additional 10% through Winterthur) and in sugar is conducted through the Lake Geneva region. The region is also number one worldwide in grain, oilseed and cotton trading. It is also the world leader in commodity trade financing and commodity testing, and is responsible for some 22% of the shipping of commodities worldwide.

Zug[21]

According to the Office of Economic Promotion in Zug, the two Zug-based companies Glencore and Xstrata are the world leaders in copper, coal, and zinc trading. Also at home in the Lake Zug region are the corporate headquarters of important nickel and palladium producers, as well as those of aluminium producers. Well-known companies in the oil and natural gas industries (Europe's largest natural gas pipelines are built and operated by companies from Zug, for example), and in the steelmaking and steel trading industries are also based in the canton of Zug. Commodity dealers are responsible for the majority of the demand in financial services in the region. Wholesalers and financial service providers thus have a reciprocal influence on each other with ramifications also for other service providers, such as business consulting firms.[22]

Lugano

According to the LCTA, Lugano, just behind Geneva, Zug, London, and Singapore, is an important centre for trading in steel, base metals, coal and, to some extent, agricultural commodities. Switzerland, and especially the Canton of Ticino, also plays an important role worldwide in the refining of gold.

2.3. Commodity trading and the finance industry

Commodities are traded on a global market. Physical commodity trading involves the movement of a given commodity in time and space. A trader buys physical commodities from a producer or on an exchange, which he then resells at a later point in time in a different place. Sometimes the transformation or storage of the commodities can be involved, as for example when a commodity trader purchases oil, which he then has refined before reselling it.

The ties between commodity trading and the financial industry are many and close. On the one hand, commodity traders are dependent upon the financial industry for the securing of risks. Traders, by the nature of their activities, are constantly exposed to the risk of a collapse in prices; they seek to secure themselves against price fluctuations with the help of financial derivatives. This practice, known as hedging, has a stabilising effect on prices. In the agricultural commodities sector, for example, derivatives have been used for hedging purposes for over 150 years. Potential counterpart to such transactions is normally either a buyer – e.g., an industrial manufacturer – who wishes to hedge against future price rises, or a financial investor, who deliberately takes on the risk in order to make a profit. Financial investors thus make an important contribution to the liquidity of commodity derivative markets and also assure the ability of commodity traders to find a counterparty when needed. In addition to commodity derivatives traded on formal exchanges,

[20] Source: GTSA.
[21] Office of Economic Promotion, Zug, June 2012, zug: newsletter, "Von Kupfer bis Kaffee: Die Rohstoffbranche im Kanton Zug," Nr. 2.
[22] Office of Economic Promotion, Zug, June 2012, zug: newsletter, "Von Kupfer bis Kaffee: Die Rohstoffbranche im Kanton Zug," Nr. 2.

use is also made of off-exchange traded derivatives (also referred to as over-the-counter or OTC derivatives). One of the advantages of OTC derivatives is that they are flexible and can be tailored ad hoc to the needs of the parties, while exchange-traded derivatives are, by their very nature, characterised by a higher degree of standardisation. Nevertheless, according to an industry survey,[23] in most cases, Swiss commodity dealers today prefer to use either exchange-traded commodity derivatives (53%) or centrally cleared OTC commodity derivatives (12%) for their hedging transactions. At the same time fewer than 1% of the exchange-traded commodity derivatives are traded on Swiss exchanges and only 12% of the OTC derivative contracts are concluded with a Swiss counterparty. This indicates that, in the great majority of cases, hedging transactions are of a cross-border nature.

On the other hand, banks play a central role in the financing of commodity trading. Without such debt financing through the banks, commodity traders would in many cases be unable to raise the large amounts of funding needed for the purchase of commodities. In Switzerland, roughly 70 to 80% of the financing for commodity trading is provided by the banks. This suggests that a highly developed and stable financial system is an important factor in the attractiveness of a business location (see below, section 3.1). One instrument that is often used in commodity transactions is the documentary letter of credit. This is a document issued by the bank of the buyer (i.e., the trader) to the seller, guaranteeing payment for the goods. Payment is made immediately upon presentation of the prescribed shipping documents to the buyer's bank by the seller. A letter of credit can also be used for financing purposes by issuing the documents to the order of the bank, which then becomes the de facto owner of the goods. In this way, the bank's risk is limited, since the loan is secured by a lien against the commodities. This notwithstanding, due to the large amounts involved in the financing of trades, good risk management remains essential.

In Switzerland, it is mainly French banks, such as BNP Paribas and Crédit Agricole, the two large Swiss banks, and various cantonal banks that are involved in commodity trade financing. Switzerland's position as an important commodity trading centre provides the banks with a good and welcome opportunity for diversification and for branching out from the wealth management business.

3. Challenges

3.1. International competition in respect of business location

Overall environment for business as an important factor in choosing a corporate domicile

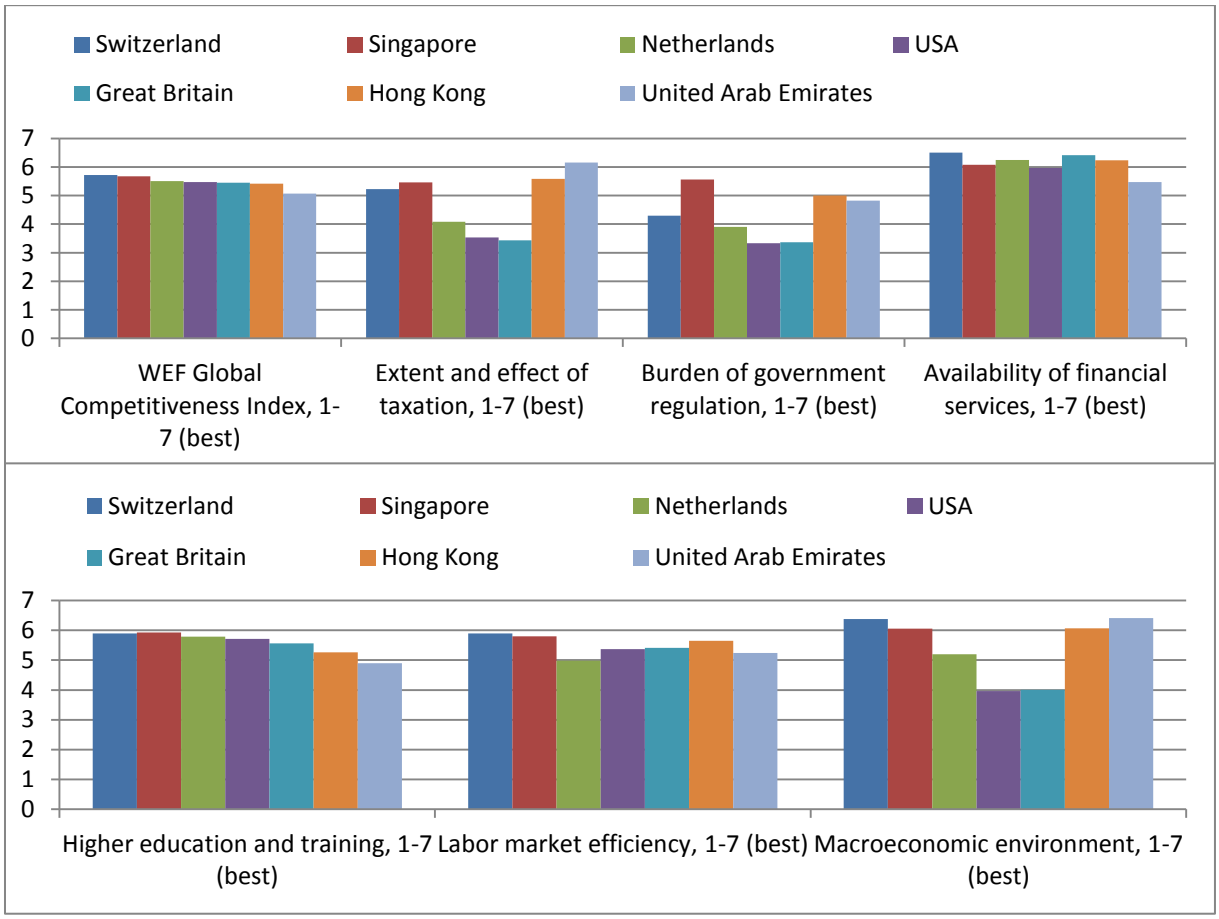
Switzerland competes internationally as a prime location for establishing a business domicile. This competition is intense, and particularly so with regard to the commodities industry. Switzerland's main competitors in this area, at the present time, are Singapore, Dubai (United Arab Emirates), the United States, the United Kingdom, and the Netherlands. Another up and coming trading centre is China and, more specifically, Hong Kong.

Figure 4 provides a comparison of the major trading centres in terms of various business location factors. The data were taken from the Global Competitiveness Report 2012-2013 published by the World Economic Forum, which describes the competitiveness of the economy overall, and not just in respect of the commodities industry. A factor of extreme importance for business locations is, in particular, a generally business-friendly environment, characterised by a stable and predictable political, economic, and legal infrastructure, competitive corporate taxation, and reasonable regulatory conditions. The presence of financial institutions specialising in commodity trading (see above, section 2.3), the availability of a highly qualified workforce, and the proximity of other providers of services essential to the commodity trading industry, are further factors of importance in the competitiveness of business locations.

[23] The survey was conducted by the FDF/SIF with the help of the GTSA, the LTCA und the ZCA, and is intended only for internal use.

The overall index shows that, in terms of general competitiveness, Switzerland ranks ahead of Singapore and the other major trading centres mentioned. The United Arab Emirates (UAE) lie somewhat further behind, whereby comparison is difficult in this case, since the trading centre Dubai is only one part of the UAE. In terms of the estimated costs engendered by government regulation and the effects of tax rates on employment and investment incentives, Switzerland is ranked below Singapore, Hong Kong, and the UAE, but ahead of the Netherlands, the USA, and the UK. In terms of the availability of financial services, the macroeconomic environment, and the efficiency of the labour market, on the other hand, Switzerland takes first place. With regard to the availability of highly qualified personnel, Switzerland ranks just behind Singapore. There is no data concerning the presence of commodity hubs.[24] However, it is reasonable to assume that Switzerland also takes the leading place in this category.

Figure 4: Global Competitiveness Index 2012-2013[25]



Source: World Economic Forum, Global Competitiveness Index 2012 – 2013 data platform.

Among the positive factors that Switzerland has to offer as a business location is also the extensive network of double taxation agreements to which it is party. At present, Switzerland is party to 86 such agreements already in effect; three further agreements have been signed, and another four have been initiated.[26] Equally important is the extensive network of investment protection agreements (IPA), through which Switzerland enhances the general conditions for doing business in the country and thus also its attractiveness as a corporate location. As a party to 116 IPAs (in effect as of 1 October 2012), Switzerland has one of the largest networks of such agreements of any country in the world.

[24] A commodities hub comprises, in addition to trading houses and banks specialised in commodity trade financing, inspections companies, shipping companies, insurance companies, law firms, escrow agents, and consultants.
[25] 1: lowest score; 7: highest score.
[26] See http://www.sif.admin.ch/themen/00502/00740/index.html?lang=en

Switzerland's central geographic location, moreover, makes it possible to conduct trades with Asia, the Middle East, and the continental US on the same day. The country's modern infrastructure, good transportation system, its liberal social order and flexible employment laws are further arguments that favour Switzerland as a centre for trading. Switzerland, especially the Lake Geneva region, is extremely well-connected, due to the presence of numerous international and multilateral institutions such as the ICRC, the UN, and the WTO. For the so-called "expat communities", "soft factors" such as the moderate climate, the varied landscape, the cultural diversity, and the personal security that the country offers, also play an important role.

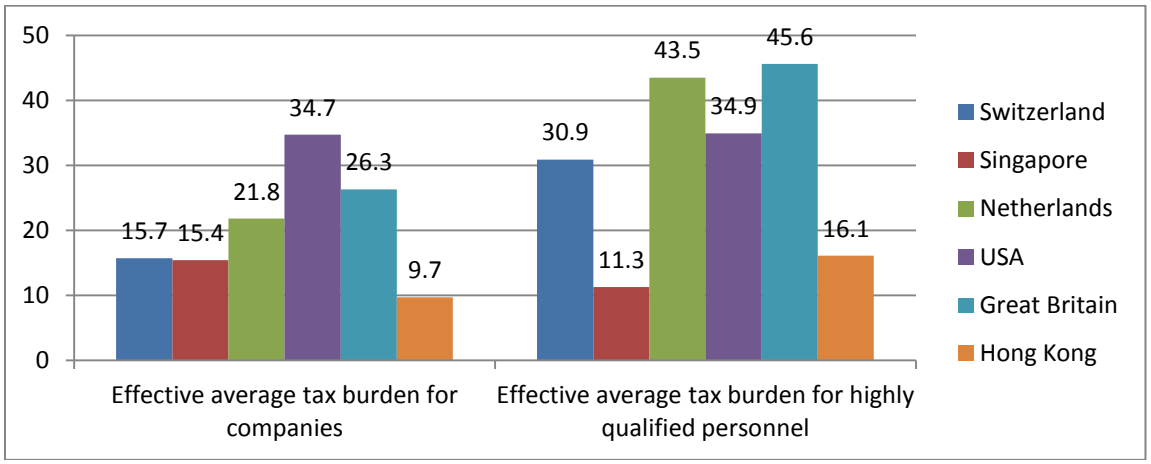
Tax considerations an important factor for companies with a high level of mobility

For internationally mobile companies, the tax environment is an important consideration. Taxes, as compensation for the public services demanded, are a cost factor, and are thus an important point of reference for businesses when deciding where to locate.

The BAK Taxation Index 2011 for companies (see Figure 5; for the complete chart see Appendix 1), complementing the tax incentive comparison presented above, shows the effective average tax rate (EATR), and can thus serve as a barometer for comparing the attractiveness of the locations considered, in terms of corporate taxes.

The effective average tax burden (EATR) for companies is lower than the Swiss average in Hong Kong and in Singapore, and higher in the Netherlands, the UK and the US. It should be noted, however, that the EATR for companies in the 17 cantons included in the BAK taxation index varies from 10.6% in Nidwalden to 21.5% in Geneva. Zug has an EATR of 13%, that of Ticino is 18.3%. This confirms the overall picture, as presented above, that the main business locations in Asia are particularly competitive insofar as the general level of taxes is concerned.

Figure 5: BAK Taxation Index 2011[27] for companies[28] and highly qualified manpower[29]



Source: ZEW/BAKBASEL, BAK Taxation Index 2011. International Benchmarking Programme (IBP). Basel: BAKBASEL.

Aside from the generally applicable tax rates, decisive for selecting the place in which to locate a business is also the applicability of tax reductions or exemptions, and thus, the fundamental issue of a company's tax status. For example, the tax burden on commodity merchanting companies in Switzerland is in the range of 10% to 15% (see also below, section 4.5). In Singapore, by con-

[27] For the United Arab Emirates/Dubai, the BAK Taxation Index does not provide any data.
[28] The figure given for Switzerland represents the (unweighted) average EATR for companies in the 17 cantons included in the survey. For other countries, the figures given are for the respective (economic) capitals of the regions taken into consideration by BAK Basel Economics: Singapore: Singapore; Hong Kong: Hong Kong; the Netherlands: The Hague; United Kingdom: London; USA: Miami (for the USA, the BAK Taxation Index provides figures on the EATR for companies only for Miami).
[29] The figure given for Switzerland represents the (unweighted) average EATR for highly qualified manpower in the 17 cantons included in the survey; the figure for the USA represents the average of the rates in Florida (31.1%), Texas (31.1%), Washington (31.1%), Delaware (38%), New York (38.1%) und California (40.1%).

trast, the effective tax rate for commodity dealers is in the attractive 5% to 10% range. This was presumably among the reasons that recently led commodity trader Trafigura to strengthen its presence in Singapore at the expense of the Geneva.[30] Dubai offers commodity trading companies so-called "Free Zones", where neither corporate nor income taxes are imposed. In Hong Kong, trading that is not conducted on Hong Kong territory is also not subject to taxation. The Netherlands also has an attractive effective tax rate for commodity merchanting companies ranging from 5% to 15%.[31]

Also important for the choice of a business domicile is the taxation of highly qualified personnel, since companies must compensate such personnel for international differences in the income taxes they are required to pay. The BAK Taxation Index 2011 for highly qualified manpower (see Figure 5) shows the effective tax burden for an unmarried employee, without dependents, who receives a net disposable income (after taxes and charges) in the amount of EUR 100,000. In this category, as well, Switzerland is more attractive than the United States, the Netherlands or the United Kingdom. The EATR for highly qualified employees in Singapore and Hong Kong, however, is markedly lower than the average in Switzerland. Of the 17 cantons included in the survey, Zug has the lowest rate, at 23.7%, while Basel-Landschaft, at 37.4%, has the highest. Geneva has an EATR of 36.4%, that of Ticino is 34.4%

All together, Switzerland thus represents a convincing alternative in terms of most business location factors. Nevertheless, in the categories of taxation and costs of government regulation, upcoming locations such as Singapore, Hong Kong, and the UAE/Dubai have succeeded in positioning themselves as particularly attractive business locations.

Switzerland's main competitors from the perspective of the Swiss commodities industry

According to an industry survey,[32] in terms of overall attractiveness as a business location, members of the Swiss commodities industry rank Singapore second, just after Switzerland. In addition to the attractive tax environment and its overall high level of competitiveness (see above), the proximity of Singapore to the Asian market presumably also plays a role. In the estimate of Swiss industry members, however, Switzerland is likely to decline somewhat in attractiveness in the coming five years, while Singapore will probably rise and thus push Switzerland back to second place. Also Dubai, currently ranked third, will probably succeed in gaining on Switzerland in the coming five years, in the opinion of the Swiss commodities industry. Great Britain, the Netherlands, and the United States are ranked behind Switzerland, Singapore, and Dubai. Their attractiveness as business locations is not likely to change markedly in the coming years, in the view of Swiss industry members. At the same time, however, it may also be assumed that those countries will be making important efforts to catch up with their competitors in the years to come.

Prospects for the coming years

At present, despite isolated reports in the media (specifically, with regard to Trafigura, see above), there is no evidence of a general trend among companies to move away from Switzerland. This is also confirmed in the results of the industry survey mentioned above. Nevertheless, other locations, such as Dubai and Singapore, actively campaign on their own behalf in Switzerland. Much will depend, therefore, on Switzerland's continued ability, also in the future, to create a competitive legal, economic, and political environment for conducting business.

3.2. Reputational risks

The sizeable economic importance of the commodities industry – both internationally and in Switzerland – has also brought with it increased public interest. Various analyses show that the commodities industry, and its presence in Switzerland, has become the focus of greater public atten-

[30] Le Temps, 23 May 2012.
[31] KPMG, Commodity trading companies – Centralizing trade as a critical success factor, October 2012.
[32] The survey was conducted by the FDF/SIF with the help of the GTSA, the LTCA und the ZCA, and is intended only for internal use.

tion both here and abroad. In recent years, this has increasingly led various NGOs, political personalities, and some of the media, to raise questions with regard, in particular, to the economic and political risks that the presence of a large number of commodity companies on its territory could entail for Switzerland.

Since the middle of 2011, Swiss NGOs have contributed to the discussion with various studies, reports, and initiatives.[33] The number of parliamentary requests on the subject has also markedly risen over the past two years. In the database of parliamentary proceedings, Curia Vista, for the period from 1 January 2002 through 31 December 2012, a total of 38 parliamentary requests[34] are found listed under the categories of "natural resources", "commodity market", "commodity agreements", "commodity prices", and "mining".[35] 30 of those were submitted in the years 2011 and 2012.

The intensification of the discussion surrounding the commodities industry in Switzerland is also reflected in the Swiss media. An analysis by Presence Switzerland on reporting in the Swiss media shows that since 2003 there has been a noticeable increase in the number of articles on the subject of "commodity trading", whereby, factual business articles clearly predominate. While the number of articles on the subjects of "corporate crime", "human rights", or "government regulation" has risen slightly overall, their percentage share has remained constant over the years at circa 12%. Articles dealing with questions of "reputation" have markedly increased in number, particularly during the last two years, and their share in all reporting on the subject of "commodities trading" reached 22% in 2012.[36]

Similar trends are discernible in the coverage of "commodity trading" in the foreign media. An analysis of reporting in 22 international newspapers of record over the last 25 years shows, on the one hand, that coverage of the subject is highly contingent on events; at the same time, however, the amount of that coverage has in fact increased over time.[37] What has also increased over the years is the proportion of references to Switzerland. While such references are found in only some 14% of reports on the subject over the entire period, there has been a disproportionate increase in the number over the last five years (to a 23% share).[38]

The criticisms raised in the public debate can be roughly broken down into five main issues: human rights violations and the financing of conflicts; environmental pollution; corruption and erosion of the rule of law (see below, section 5.1); lack of transparency; and illegal flows of money and tax avoidance (see below, section 4). The criticism, which tends to focus, in particular, on the extraction of natural resources, relates primarily to the conduct of individual companies, among which some that are domiciled in Switzerland, and the reputational risks this entails, especially for companies whose shares are listed on a stock exchange.

Criticism of Switzerland as the "country of domicile" of commodity companies, on the other hand, is much rarer; when criticism does focus on Switzerland, it usually comes from Swiss actors and the media. This notwithstanding, the conduct of companies domiciled in Switzerland, insofar as it

[33] Among others, the Bern Declaration: „Rohstoffe - Das gefährlichste Geschäft der Schweiz" or Pain pour le prochain et action de carême; „Glencore en République Démocratique du Congo: le profit au détriment des droits humains et de l'environnement." (in German, French and Italian only) [English: "Commodities – Switzerland's Most Dangerous Business"; Bread for All and the Swiss Catholic Lenten Fund, "Glencore in the Democratic Republic of the Congo: Profit before Human Rights and the Environment"], and the petition circulated by Corporate Justice: Rules for Business, Rights for People, demanding that the Federal Council and the Federal Assembly enact statutory provisions imposing on companies domiciled in Switzerland a duty to respect human rights and environmental standards worldwide. The Foreign Affairs Committee of the National Council has decided not to take up the petition; a decision by the Foreign Affairs Committee of the Council of States is still pending.
[34] Postulates, motions, interpellations, questions asked during the question time, and parliamentary initiatives.
[35] Detailed overview in Appendix 2.
[36] Based on an internal analysis of domestic media reporting on "commodity trading", by the FDFA, Presence Switzerland. For internal use only.
[37] Based on an internal analysis of domestic media reporting on "commodity trading", by the FDFA, Presence Switzerland. For internal use only.
[38] This is presumably related, not leastly, to the merger of Glencore and Xstrata.

runs contrary to standpoints expressed and supported by Swiss policy in the domains of development, peace promotion, human rights, and social and environmental rights, brings with it a heightened risk for Switzerland's overall reputation. This is particularly the case where criticism of the conduct of companies proves to be justified and no measures are taken by the government to constrain companies to act responsibly and comply with recognised standards. To date, no negative impact on Switzerland's reputation has been discernible.

An analysis of the situation by the Swiss representations abroad provides examples of various potential problematic areas:

- According to information from a large portion of Switzerland's representations abroad, multinational corporations have at their disposal extensive codes on standards relating to human rights, social responsibility, and environmental protection, which, for the most part, they also implement. Small-scale artisanal mines are particularly susceptible with regard to serious human rights violations (child labour, human trafficking, environmental risks, etc.). In countries such as the Democratic Republic of the Congo, such mines, according to various estimates, are responsible for more than one half of natural resource extraction. In this context, companies are criticised for indirectly purchasing minerals that stem from such small-scale artisanal mines. This criticism is rejected by the companies as groundless.
- The lack of transparency as to the origin of certain natural resources is also a subject of criticism. Companies – including some that are domiciled in Switzerland – are criticised for example, for buying commodities from sources that disregard human rights, finance conflicts, harm the environment, or have unlawfully acquired the resources (e.g., Nigerian oil).
- Different representations' reports draw attention to the issue of the illegal extraction of gold. Because of Switzerland's important position in the gold trade, and in the processing and refining of gold, there is a risk that gold that contributes to the financing of armed groups or of organised crime will also be imported into Switzerland. Illegal gold extraction can undermine efforts – also on the part of Switzerland – to resolve armed conflicts. Other issues that are raised in the public debate regarding illegal gold extraction are, in particular, those of environmental pollution and child labour.
- Another example, again from the Democratic Republic of the Congo, to which NGOs and the Swiss representation there draw attention, is that of the often dubious transactions behind the awarding of mining licences, which are sold at low prices to businessmen with close ties to the government. The commodities industry is exposed to a particularly high risk of corruption, due to a number of different factors (e.g., the high amounts of financial resources involved, and operations in countries where the rule of law is compromised, etc.).
- An example that was mentioned a number of times in connection with tax avoidance, relates to copper extraction in Zambia. Companies, including some that are domiciled in Switzerland, are accused of using internal accounting practices to shift profits to countries with low tax rates and, simultaneously, to transfer costs to countries with high tax rates. This enables them to regularly post losses in spite of the relatively high copper price. Critics claim that this is due, among other things, to the lack of transparency in internal financial flows within corporate groups.
- Various companies are criticised in the public debate for infringing the rights of indigenous people. One company domiciled in Switzerland, for example, has been criticised by NGOs, and in various media, for its role in civil unrest in Peru. In that particular case, other media moderated their criticism of the company and, at the same time, questioned the role played by the NGOs. In addition to raising the issue of social unrest, this case illustrates a problem that is often encountered, namely, that of obtaining reliable information as to the actual facts.

According to the information provided by the Swiss representations, Switzerland's role as a corporate domicile has, particularly in the regions where extraction is carried out, rarely been an is-

sue. At the same time, it emerges clearly that violations of human rights and environmental standards are often linked to a combination of actors, which makes the attribution of responsibility more difficult.

3.3. Foreign policy considerations

The activities of individual companies domiciled in Switzerland and engaged in commodity trading can represent a challenge in terms of Swiss foreign policy.

This is the case, specifically, for commodity companies that are owned by politically exposed persons or by governments that exhibit deficiencies in the areas of democratic or human rights.

A second issue that can potentially give rise to foreign policy challenges in connection with natural resources is that of companies domiciled in Switzerland that conduct business with countries that are subject to sanctions.

A third category of potentially sensitive commodity industry activities involves companies that have control over strategic goods or services, such as natural gas pipelines, for example. The blocking of a pipeline by a company domiciled in Switzerland, where this plays a central role in the security of another country's energy supply, could create foreign policy difficulties for Switzerland.

A further potential risk would arise if a (commodity) company controlled by a foreign government and domiciled in Switzerland were to file a suit against another foreign government in reliance upon a treaty to which Switzerland is a party. Because Switzerland, in its Investment Protection Agreements (IPA), restricts the right to initiate arbitration proceedings to investors who have a true economic connection with Switzerland, the risk to Switzerland would not be given where a company does no more than maintain a registered office, or even just a mailbox, here.

3.4. Development policy considerations

Oil production, the extraction of mineral resources, and the trade, among other things, in agricultural commodities, have far-reaching effects on the economy, government, and society of resource-rich developing countries. Pursuant to the Federal Council's Dispatch to Parliament on International Cooperation 2013-16, there are 35 countries and 7 regions that have priority in Switzerland's development cooperation strategy (SDC, SECO). At least 19 of those countries, and all 7 regions, currently possess substantial reserves of natural resources. These include, for example, Egypt, Ghana, Mozambique, South Africa, and Tanzania, in Africa; Bolivia, Colombia, and Peru, in South America; Indonesia, Mongolia, and Vietnam, in Asia; and Albania, Azerbaijan, Kyrgyzstan and Ukraine in Europe/CIS.

In these countries, large mining or vertically integrated commodity companies domiciled in Switzerland are often also active.

It is estimated that 59% of all metals and ores, 63% of all coal, and 64% of all oil originates from developing countries; 60% of all energy resources and of all mineral resources is extracted in countries where political stability is judged to be critical or extremely critical.[39] According to a UN study, in 100 (of a total of 151) developing countries, at least 50% of export revenues are derived from mineral, agricultural, and fossil resources; in one half of all African countries receipts from commodity exports actually exceed 80% of all export revenues.[40]

[39] Federal Ministry of Economy, Family and Youth of the Republic of Austria: World Mining Data – Minerals Production (http://www.en.bmwfj.gv.at/Energy/MineralRawMaterials/Seiten/default.aspx). The source uses the terminology employed in comparable UN statistics (countries of the former USSR are not counted as developing countries):
http://www.en.bmwfj.gv.at/Energy/MineralRawMaterials/Documents/World%20Mining%20Data%202012.pdf

[40] *The State of Commodity Dependence 2012* (http://unctadxiii.org/en/SessionDocument/suc2011d8_en.pdf) and the *UNCTAD Commodities and Development Report 2012* (http://unctadxiii.org/en/SessionDocument/suc2011d9_overview_en.pdf).

Academics, multilateral institutions, governments, and civil society organisations have for many years been making substantial efforts to describe and to analyse the underlying factors, socio-economic relationships, and the role of various actors involved in the extraction and trading of natural resources in developing countries.[41] The consequences of natural resource extraction and trading for sustainable development is the subject of much controversial debate. In the following, an overview of the most important opportunities and risks for developing countries will be given.

Reserves of natural resources represent, in principle, a potential source of revenues and growth for developing countries and, thus, a chance to sustainably reduce existing poverty levels. Positive examples, such as Botswana, Ghana, Malaysia, and Thailand, show that the successful utilisation of natural resource reserves can go hand-in-hand with long-term economic growth, job creation, the accumulation of currency reserves, and a rise in investments. In addition, commodity companies – in addition to the significant investments needed for the extraction of natural resources – in compliance with standards of corporate social responsibility, make contributions for the construction and maintenance of schools and hospitals and for assuring the availability of drinking water.

It must also be kept in mind, however, that the commodity business also brings with it challenges and risks that are often connected with the weak institutional capacity of developing countries, inadequate governance, international price trends, and the high dependency of exporting countries on revenues from resource extraction. In practice, problematic underlying conditions and the concomitant circumstances of the commodities trade often have a fundamentally inhibitory effect on the revenue and growth potential of developing countries, their populations, and their businesses (a phenomenon often referred to as the "natural resource curse"). In the extraction and transport of natural resources, problems arise with regard to respect for fundamental environmental and labour standards, the fair and transparent awarding of licences, the efficient and stringent oversight of extraction activities by the government, and overly optimistic forecasts concerning the number of jobs that the industry is expected to create. Endemic corruption and theft are not uncommon in the commodities industry, which undermines both the enactment and enforcement of national laws and respect for international norms and standards. Reports regularly come to light of practices injurious both to human health and to the environment, illegal mining, exploitative working conditions, and violent conflicts over access to natural resources, in which multinational corporations, publicly owned companies, or producers organised as small businesses, play a decisive role. On the one hand, it is true that businesses must keep their operations going despite often difficult circumstances. At the same time, however, their own inappropriate business practices can also contribute to a deterioration ofthe situation (the subject of corporate responsibility will be taken up again below, in section 5.1).

In addition, the revenues generated from the extraction of natural resources can give rise to other problems in the country where the resources originate. The best-known phenomenon is that of the so-called "Dutch disease". This refers to the strengthening of the local currency, resulting in a relative decrease in the competitiveness of the country's other exports, which then leads to a decline in its overall export economy and a corresponding loss of jobs. In addition, where the economy depends to a large degree on natural resource exports, the volatility of commodity prices can also create macroeconomic challenges. These can result in so-called boom-and-bust cycles, with negative structural consequences for the overall economy.

Finally, discussion has significantly increased on questions surrounding financial flows tied to the commodity business. The international flight of capital due, among other things, to tax evasion and tax avoidance, and illegal financial flows (due, in particular, to money laundering and corrup-

[41] E.g., The *United Nations Conference on Trade and Development UNCTAD*, the World Bank, the IMF, and the NGO *Revenue Watch Institute*, which focuses on natural resource issues (http://www.revenuewatch.org/about). For an overview of the academic business literature, see van der Ploeg, Frederick (2011), "Natural Resources: Curse or Blessing?", Journal of Economic Literature, 49(2): 366–420. For an extensive analysis from the perspective of international experts, see *International Study Group Report on Africa's Mineral Regimes, Minerals and Africa's Development*, ed. by the UNEC Africa and the African Union, 2011).

tion) have for some time now been seen in the international discussion (OECD, UN, etc.) as major impediments to the mobilisation of domestic resources in developing and emerging economies. These flows of money, to which financial flows connected with the commodity business are notably a part, may be presumed to constitute, in the aggregate, a fundamental obstacle to economic growth and good governance in developing countries.42 It is generally assumed that the volume of the financial flows from developing countries towards foreign financial centres exceeds by far the total of public funds spent on development assistance (2011: US$133.5 billion).[43] The actual volume can, however, at best, only be estimated, and given the state of the data and the methodology used, these figures must be used with caution. The size of the contribution to these financial flows resulting from commodity production and trading cannot accurately be estimated.

In the context of these international financial transactions, practices used to evade and avoid taxes play an important role. Such practices are often seen, also in developing countries, as being connected with a business model often used by multinational corporations, which is designed to ensure that profits become subject to taxation in places where tax rates are particularly low or non-existent (transfer pricing, on the use of which see also below, section 4.6). According to various studies, companies involved notably also in the commodities industry have a strong tendency to make use of this practice.[44]

The discussion surrounding the issue of natural resources also has an influence on the international development policy agenda. International tax issues, including the question of mobilising tax resources through the developing countries themselves, occupied a prominent place in discussions at the meetings held in Monterrey (2002) and Doha (2008). The G20 raised the issue at their September 2009 summit, and it is also a subject of discussion within the United Nations. Proposals currently under debate for developing more sustainable forms of natural resource extraction and trade range from the drafting of loose guidelines implemented via voluntary agreements with practicable monitoring mechanisms to the enactment of statutory provisions with sanction mechanisms at the national level, as found in, or sought by, the US and the EU.

Recent discussions have shown that the main areas in which policies for the promotion of more economically, socially and environmentally sustainable natural resource extraction and trade could be put into effect are the following:

- Higher standards of transparency and accountability
  - in the industrialised countries, in the domains of financial market oversight (for combating corruption and money laundering), international tax policy, and corporate accounting;
  - in developing countries, in the awarding of exploitation licenses, the setting of exploitation conditions, and in the disclosure of revenues of all kinds.
- Capacity building in the developing countries with regard to
  - taxation and the administration and use of government revenues;
  - enhancement of technical expertise in legislative drafting, law enforcement, and conduct of negotiations with multinational enterprises;
  - the reinforcement of democratic monitoring mechanisms (through parliament and the civil society, for example).

[42] The *African Economic Outlook 2012* reaches the conclusion that the Millennium Development Goal 2015 of "halving the 1990 poverty level" could have been achieved if the resources transferred abroad from Africa had been reinvested there. African Economic Outlook 2012, edited by AfDB, OECD, UNDP, and the UN-Economic Commission for Africa, 2012.
[43] OECD, Better Policies for Development, 2011, based on the estimates of Global Financial Integrity.
[44] *Draining development?: Controlling flows of illicit funds from developing countries*, edited by Peter Reuter, 2012. A study conducted by the World Bank, containing a number of analyses on the subject. The study also provides a detailed explanation of the practice of transfer pricing.

- Conduct of business by multinational enterprises:
  - Stricter implementation of existing international minimum standards, by legislative or other means, governing the business operations of multinational corporations in commodity-exporting developing countries, in particular, with regard to human rights, environmental protection, and investments (Corporate Social Responsibility).

Through participation in the international debate, through its development policy,[45] the implementation of international standards, and the adaptation of its legal regime where required, Switzerland also contributes to these efforts.

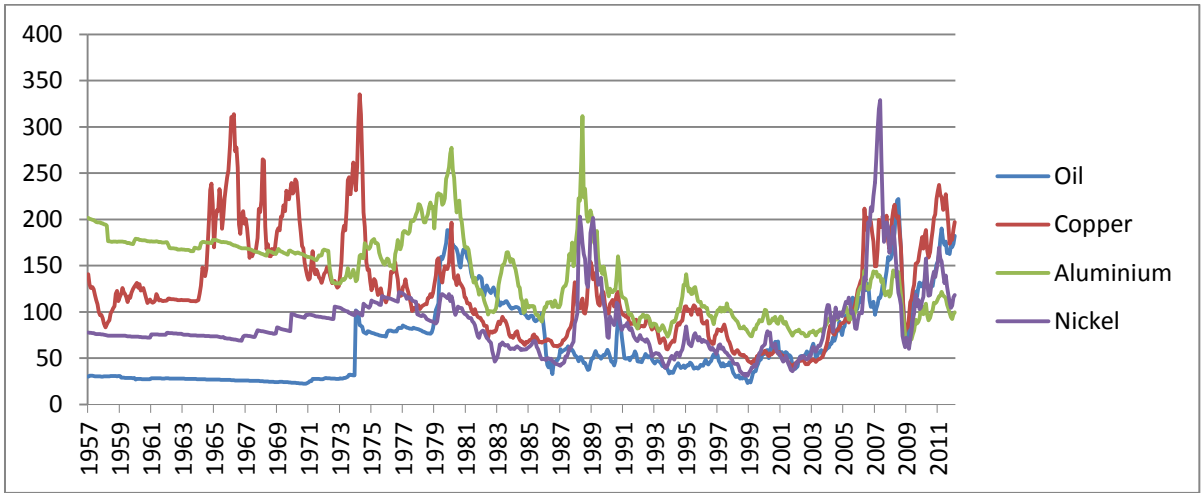
4. Regulation, oversight, and taxation

4.1. Regulatory issues: commodity trading and the financial industry

Background

Inflation-adjusted commodity prices over the past 50 years present a mixed picture. Nevertheless, since the beginning of the new millennium, prices – starting from a relative low – have undergone a substantial increase (see Figure 6). Because this rise in prices over the past 10 years occurred synchronously with an increase in the participation of financial investors on the commodity derivative markets, the role of those commodity derivative markets, and the regulation thereof, have become a focus of international debate. In this connection, attention should be drawn especially to the Principles for the Regulation and Supervision of Commodity Derivatives Markets,[46] recently drafted by the International Organisation of Securities Commissions (IOSCO)[47] under the aegis of the G20 and the Financial Stability Board (FSB).[48] Those principles are designed to ensure that the commodity derivatives markets contribute efficiently to the pricing of commodities, that they properly perform their hedging function, and that they remain free from manipulation.

Figure 6: Commodity prices in long-term comparison: high volatility is not a new phenomenon

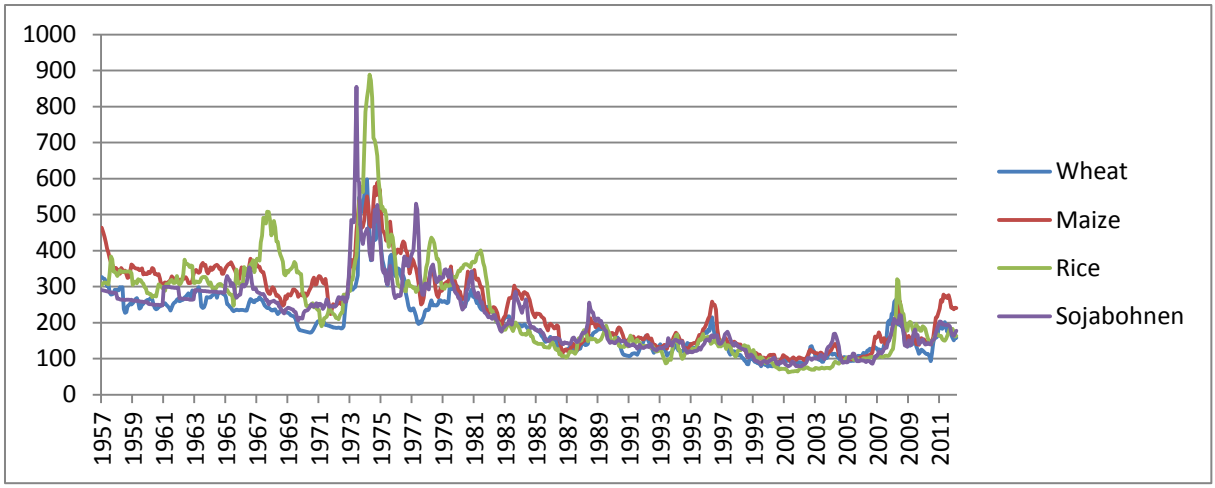


[45] Switzerland provides support, for example, for bilateral projects for the strengthening of governance and capacity building (e.g., in tax regimes) in Burkina Faso, Ghana, Mozambique, and Peru. Multilateral instruments supported by Switzerland include: the *Extractive Industries Transparency Initiative* (EITI, on which, see below, sections 4.4 and 5.1), the *IMF Managing Natural Resource Wealth Topical Trust Fund*, the *IMF Regional Technical Assistance Centers*, the *IMF Tax Policy and Administration Topical Trust Fund*, the *IMF Anti-Money-Laundering and Countering Financing of Terrorism Topical Trust Fund, and the World Bank Extractive Industries Technical Advisory Facility (EITAF).*

[46] Principles for the Regulation and Supervision of Commodity Derivatives Markets – Final Report, IOSCO, September 2011.

[47] The FINMA is a member of the IOSCO.

[48] As a member of the FSB, Switzerland has two seats, which are occupied by the Federal Department of Finance and the SNB, respectively.



Source: IMF Primary Commodity Prices, 2012. Inflation-adjusted, based on the US consumer price index. Indexed (2005 = 100).

Closely related are international efforts to regulate OTC derivatives, which are thought to have been part of the cause of the 2007 financial crisis. Standards designed to increase transparency and reduce systemic risks throughout the OTC derivative market have been developed and promoted internationally in bodies such as the G20 or the FSB. These also apply to the commodity derivatives markets. It should, however, be noted that the share of OTC commodity derivatives in the total outstanding volume of all OTC derivative classes, as of December 2011, was not more than 0.5%.[49]

A comprehensive analysis of the rise in commodity prices mentioned above is not the focus of the present report. It is nevertheless worth mentioning, however, that while financial investors can certainly contribute in the short term to the creation of financial bubbles, no convincing empirical evidence has yet been presented to show that financial investors have a lasting influence on commodity prices. Rather, according to most studies, it is real economic factors, including rising demand from emerging markets and a slow response on the supply side, that are the main causes over the middle to long term.[50] In addition, attention should also be drawn in this connection to the fact that financial investors contribute to the liquidity of derivative markets. This makes it possible for commodity dealers to find suitable hedging counterparties, which has a stabilising effect on prices (see on this, above, section 2.3).

Physical trading

A fundamental distinction must be drawn between physical trading and derivative trading (see above, section 2.3). There is no exchange for physical trading in Switzerland. Physical commodity traders are, in principle, not subject to any market oversight in Switzerland. However, those who are also active as securities traders (see below), must be licensed by the Financial Market Supervisory Authority (FINMA). The FINMA itself does not receive any information on physical trading transactions. Nevertheless, where punishable offences are involved, the criminal authorities may, under the prescribed conditions, demand information from any market participant in connection with the prosecution proceedings.

[49] BIS Quarterly Review, June 2012.
[50] See, among others, Ervin, Sanders and Merin, “Devil or Angel? The Role of Speculation in the Recent Commodity Price Boom (and Bust)”, Journal of Agricultural and Applied Economics, 41(2), 2009; Kappel, Pfeiffer and Werner, “What Became of the Food Price Crisis in 2008?”, Swiss Review of International Economic Relations, 2010; Report of the G20 Study Group on Commodities, 2011; Fattouh, Kilian and Mahadeva, “The Role of Speculation in Oil Markets: What Have We Learned So Far?”, CEPR Discussion Paper No. DP8916, 2012; FTI UK Holdings Limited, “The impact of speculative trading in commodity markets – a review of the evidence”, 2012.

Derivative trading: Exchanges

In Switzerland, commodity derivatives are traded only on Eurex, where some 40 are listed (with underlyings including agricultural commodities, gold, silver, natural gas, coal, etc.). The major exchanges for commodity derivatives are found in London, New York, and Chicago.

In the EU, exchanges on which commodity derivatives are traded are regulated via the Markets in Financial Instruments Directive (MiFID). Until now, dealers trading in physical commodities on a regulated exchange benefited from an exemption, which will, however, be subject in the future to limitations as foreseen by the MiFID II draft proposal. Those commodity dealers who do not trade in derivatives exclusively for their own account will probably no longer receive an exemption.[51] This means that companies that were until now exempted will, in the future, be subject to the MiFID II rules. Such companies will then be subject to a licensing requirement and will need to fulfil regulatory capital and organisational requirements. Depending on what the final version of the new regulation looks like in this regard, it will be necessary to review whether Swiss commodity dealers, who were not subject to the existing MiFID, or who benefited from the applicable exemptions, would now be subject to the MiFID II third country regime, as proposed by the Commission.

In addition, oversight authorities are expected to be explicitly authorised to manage positions, or introduce limits on positions, on commodity derivatives exchanges. Further, a revision of the Market Abuse Directive (MAD) is expected to extend the applicability of regulations governing insider trading and market manipulation to also include physical trading.

In the USA, commodity derivatives exchanges and their participants are subject to oversight and regulation by the Commodity Futures Trading Commission (CFTC), under the Commodity Exchange Act (CEA). Enforcement of the rules is carried out through a self-regulatory organisation, the National Futures Association (NFA). Where suspicion of market abuse arises, the CFTC is authorised to investigate not only on the commodity derivatives exchanges, but also on the physical market and the OTC market.

All Swiss exchanges are subject to supervisory oversight by the FINMA and must comply, among other things, with the rules concerning market integrity and market abuse surveillance. This is accomplished through self-regulation by the exchange itself, whose operational, administrative, and oversight structures must be approved by the FINMA (Federal Act on Stock Exchanges and Securities Trading (SESTA), art. 4). Exchanges may also set limits on positions or manage positions in order to ensure the orderly conduct of trading. In addition, all financial market participants are subject to the criminal provisions governing insider trading and market manipulation (SCC art. 161 and 161bis). In general, participants on Swiss exchanges must be securities dealers (within the meaning of SESTA art. 2 [d]), and be licensed by the FINMA (SESTA art. 10). Proprietary traders who are not primarily active in the financial industry, by contrast, do not require a licence, as they are not securities dealers. This is the case, as a rule, for commodity traders, provided that they use commodity derivatives primarily for hedging purposes. A commodity trader also requires a licence from the FINMA in order to participate on foreign exchanges. The FINMA does, however, grant exemptions, subject to clear requirements closely modelled on those of the EU's MiFID.

Derivative trading: OTC derivatives

In order to increase transparency and stability on the OTC derivative market, the FSB international standards provide that standardised OTC derivatives should be cleared through a central counterparty (CCP) and, where appropriate, traded over trading platforms. In addition all transactions should be reported to central data collection points (Trade Repositories [TR]). Further, it is recommended that non-centrally cleared transactions be made subject to higher requirements with regard to capitalisation and risk management.[52]

[51] See http://ec.europa.eu/internal_market/securities/isd/mifid_en.htm. MiFID II will not enter into effect until the middle of 2013, at the earliest, and must then be implemented by the EU Member States through their respective national laws.

[52] See the remarks of the FSB in this regard at http://www.financialstabilityboard.org/publications/r_101025.pdf;

In the EU and the US, the regulatory reforms in this area are already well advanced. In the EU, they are being implemented through the European Market Infrastructure Regulation (EMIR), supplemented by the revision of the MiFID, and in the US through the Dodd-Frank Act. In the US, and in the EU, all transactions in derivatives (OTC and non-OTC) – that is, also transactions in commodity derivatives – entered into by all market participants will, in the future, need to be reported to the appropriate TR. A final decision as to which derivative transactions are to be subject to the requirement of clearance through a CCP has not yet been reached. In any case, however, persons who purchase OTC derivatives exclusively for the purpose of hedging business risks arising from positions they physically hold, will receive an exemption.[53] Commodity traders will presumably be eligible for this exemption.

In order to assure Switzerland's continued competitiveness as a financial centre and to reinforce its financial stability, it is necessary that Switzerland implements the G20 undertakings and the FSB recommendations on trading in OTC derivatives as completely and as contemporaneously with other financial centres as possible. For this reason, on 29 August 2012, the Federal Council instructed the Federal Department of Finance to prepare by the spring of 2013 a consultation draft for new statutory regulations to govern off-exchange trading in derivatives.[54] In order to assure the competitiveness of the Swiss market participants and to maintain access to the EU market, a regulatory regime equivalent to that of the EU will be sought. In doing so, the importance of OTC commodity derivatives for price hedging must also be taken into account. The EU and the US, for example, foresee for hedging positions – as noted above – an exemption from the duty to clear transactions through CCPs. There is no need for any amendment to the existing criminal provisions on insider trading and market manipulation, as these are already applicable to trading in OTC derivatives today.

IOSCO Principles for the Regulation and Supervision of Commodity Derivatives Markets

At the end of October 2012, the IOSCO published a report on the implementation of its Principles.[55] Overall Switzerland receives good marks. Its current regulatory regime is already in compliance with the great majority of the IOSCO Principles for the Regulation and Supervision of Commodity Derivatives Markets. By implementing the OTC reforms (see above) it will presumably also be in compliance with the Principles that apply to off-exchange trading, such as, for example, with regard to access to data on OTC derivatives through central data collection points. Principles with which Switzerland is not in compliance are related to such things, for example, as the publication of aggregated positions for the different trader classes. Compliance with this principle was found, however, in almost none of the countries reviewed[56].

Financial intermediaries

As noted in section 2.3, Swiss commodity traders currently finance between 70% and 80% of their trades through banks. Banking activities, including the domain of trade financing, are subject to the supervisory authority of the FINMA, under the existing bank oversight regime. Because of the more stringent capitalisation and liquidity requirements under the new Basel III rules, it is possible that the financing of trades will become more expensive. This effect will not be limited to

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the interim rules for the capitalisation of bank exposures to central counterparties, at http://www.bis.org/publ/bcbs227.htm; and the Consultative paper on margin requirements for non-centrally-cleared derivatives, at http://www.bis.org/publ/bcbs226.htm.

[53] In the EU, for non-financial institutions that trade in derivatives not used for the hedging of physical positions, a threshold value will be fixed, above which the requirement of clearance through a CCP will apply. For commodity derivatives, the threshold value will be EUR 3 billion (gross notional value) (see the Final Report, Draft Technical Standards under the Regulation (EU) No. 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC Derivatives, CCPs and Trade Repositories).

[54] See the media release at http://www.sif.admin.ch/00488/index.html?lang=en&msg-id=45737.

[55] Survey on Implementation of the Principles for the Regulation and Supervision of Commodity Derivatives Markets – Final Report, IOSCO, October 2012.

[56] For an inclusive oversight, see the Survey on Implementation of the Principles for the Regulation and Supervision of Commodity Derivatives Markets – Final Report (IOSCO, October 2012) and Appendix A at http://www.iosco.org/library/pubdocs/pdf/IOSCOPD393.pdf

Switzerland, however, since Basel III is expected to be implemented in all major financial centres, including Singapore. As a result, it is likely that commodity dealers will increasingly take recourse to securitisation as a financing option. In the interest of maintaining the stability of the financial markets, this phenomenon would need to be followed very closely.

4.2. Combating money laundering

The recommendations of the Financial Action Task Force (FATF) constitute international norms of reference in the fight to stop money-laundering, the financing of terrorism, and the proliferation of arms of mass destruction. They were not expressly designed with the trade in natural resources in mind (other than the trade in precious metals and precious stones, cf. Recommendation 22 [c]). Nevertheless, where a country determines, based on its own national risk assessment, that certain types of institutions, activities, businesses, or professions, not covered by the FATF norms, present a money-laundering or terrorist-financing risk, it should consider applying anti-money-laundering/countering-the-financing-of-terrorism requirements there as well (Interpretive Note to Recommendation 1, para. 2). In other words, the national risk assessment is determinant with regard to the obligation to consider going beyond the FATF recommendations and making certain activities, such as commodity trading, subject to anti-money-laundering norms.

In Switzerland, commodity trading is subject to the provisions of the Anti-Money Laundering Act (AMLA; SR 955), where trades are executed for the account of a third party (cf. AMLA art. 2, para. 3 [c] in conj. with art. 5, para. 2 [b] of the Ordinance on the Professional Practice of Financial Intermediation). Proprietary commodity trading is not, as such, subject to the AMLA.[57] Nevertheless, pursuant to article 305bis of the Criminal Code, money-laundering is subject to punishment in connection with commodities trading, regardless of whether trades are executed for the account of a third party or for one's own account.

In the course of preparing the implementation of the revised FATF recommendations of 2003, and the internal study, the conclusion was made that there were no compelling grounds for making proprietary commodity trading subject to the provisions of the AMLA. Among other things, a survey of the laws of other countries had revealed that no other legal system foresaw doing so, either.[58]

The option of making proprietary trading in commodities subject to anti-money laundering rules was reviewed again recently, in connection with the implementation of the 2012 revised FATF recommendations, and was again rejected. The decision was based on the following arguments: the criterion for determining the applicability of the Anti-Money Laundering Act (AMLA) is whether an individual provides financial services in a professional capacity (financial intermediation). As a result, the interface at which the mechanisms for combating money laundering in commodity trading set in is at the point of financial intermediation. In this way, the system is able to make certain that commodity trading activities – like trading activities in other sectors – are covered. Thus, for example, where violations of human rights are committed in the extraction of resources, the applicable mechanisms under the Anti-Money Laundering Act will be set in motion as soon as the illicitly gained funds are placed in circulation by the conduct of transactions through a bank.

The 2012 revision of the FATF recommendations has brought about a reinforcement of international regulation in the fight against financial crime in a number of areas, including the transparency of legal persons and legal structures, the duty of diligence on the part of financial intermediaries (in particular, with regard to the rules for identifying politically exposed persons and beneficial owners), and international cooperation. In view thereof, Switzerland intends to introduce more stringent due diligence requirements for financial intermediaries, and will thus also be contributing

[57] See the response of the Federal Council to Motion 11.4161, "No money laundering in the proprietary trading of commodities", submitted by National Councillor Ursula Wyss.

[58] Cf. the explanatory report on the implementation of the revised recommendations of the FATF, "Mise en œuvre des Recommandations révisées du Groupe d'action financière sur la lutte contre le blanchiment de capitaux", January 2005, sect. 2.4.4, online at http://www.admin.ch/ch/f/gg/pc/documents/1237/Bericht.pdf.

to improvements in the prevention of abuses of this kind in the domain of natural resources and commodity trading.

In addition, there are today no indications to suggest that there is any widespread abuse of proprietary commodity trading for money-laundering purposes. While there does exist, in theory, a limited risk of such transactions being used for money-laundering, there is no evidence that this actually occurs in practice.

Finally, because a person trading in commodities for his own account is both his own counterparty and the beneficial owner of the goods, he would be obliged, under the terms of the AMLA, to exercise due diligence with regard to himself and to conduct an investigation into the background of his own transactions. This is difficult to imagine, even conceptually, and, given the conflicts of interest, could hardly be carried out satisfactorily in practice.[59] Where an investor executes an investment in commodities through his bank, on the other hand, that constitutes a financial transaction that is covered by the AMLA.

Even without making proprietary commodity trading subject to the provisions of the AMLA, by applying that law to trading for the account of others, the Swiss regulatory regime not only goes beyond what is called for by the FATF recommendations, but is also more stringent than required by the law of the European Union.

4.3. Sanctions

Definition, binding nature, statutory basis

The term sanction refers to measures taken by sovereign powers to compel compliance with international law. The most important, in practice, are economic sanctions or coercive economic measures. Through economic pressure, the State, companies, or persons, to whom the sanctions apply are to be constrained to alter their conduct.[60]

The UN Security Council is the only body with the authority, based on Chapter VII of the UN Charter, to impose sanctions that are legally binding on all UN Member States, and thus, also on Switzerland. In addition, coercive measures are regularly also adopted by individual countries or groups of countries (such as the EU, for example). Such measures are without universally binding effect, however.

In Switzerland, the Embargo Act (EmbA)[61] serves as the statutory basis for enforcing, through the enactment of non-military coercive measures in Switzerland, sanctions imposed by the UN, the OSCE, or Switzerland's major trading partners for the purpose of compelling compliance with international law or respect for human rights. The EmbA itself does not contain any coercive measures; these are enacted by the Federal Council in the form of a Federal ordinance.[62] It is important to emphasise that the EmbA authorises the Federal Council to effect the enforcement only of sanctions that have already been resolved upon by one of the aforementioned actors. Switzerland implements all UN Security Council sanction resolutions that are binding under international law. In addition, since 1998, Switzerland has joined in sanctions enacted by the EU in practically all significant cases. Unilateral coercive measures by Switzerland would need to be enacted in reliance upon article 184, paragraph 3, of the Federal Constitution.

[59] See the response of the Federal Council to Motion 11.4161, "No money laundering in the proprietary trading of commodities", submitted by Ursula Wyss.

[60] Sanctions can take various forms; the most important are embargoes on goods (bans on the import or export of certain goods), embargoes on services, financial sanctions (freezing of assets and bans on providing certain persons with money or other assets), travel embargoes (e.g., banning of air traffic with the State under sanction), entry and transit bans for certain persons.

[61] Federal Act of 22 March 2002 on the Implementation of International Sanctions (SR 946.231)

[62] At the present time, there are 20 Ordinances in effect imposing sanctions in conformity with the EmbA. Eleven of those Ordinances implement UN Security Council resolutions; six Ordinances are modelled on similar EU sanction resolutions; and three Ordinances comprise a combination of UN and EU coercive measures.

Commodity sanctions

The export of natural resources is for many countries and regimes an important or even vital source of revenues. The interruption of such currency flows is an effective means of exerting economic pressure. It is, therefore, not surprising that this strategically important sector of the economy is regularly the object of sanctions. In recent years the following commodities have been (or continue to be) subject to international sanctions: Petroleum and petroleum products (Iran, Iraq, Syria), lumber and lumber products (Liberia, Myanmar), charcoal (Somalia), coal, certain medals, precious stones and gemstones (Myanmar), and diamonds (Liberia, Sierra Leone, Angola, Myanmar). In addition to such sanctions, which placed a ban on the import or trade in certain commodities, there are also other measures that can indirectly interrupt or render more difficult commodity trading. Thus, for example, the sanctions against Libya in 2011 did not expressly call for an oil embargo. However, due to the ban on business dealings with the Libyan National Oil Corporation and numerous other Libyan oil companies, the de facto result was the same. Commodity sanctions, moreover, are often not limited simply to an import or trading ban, but also prohibit the providing of services, the granting of financing, the making of investments, etc., as related to the production of, or trade in, the targeted commodities.

The Kimberley Process for monitoring the worldwide trade in rough diamonds was established for the purpose of eliminating so-called "conflict diamonds" from the international market. The sale of rough diamonds played an important role in the financing of civil wars in a number of West African countries. Switzerland, which continues to play an important role in the rough diamond trade,[63] is a founding member of the Kimberley Process, which in the meantime has been extended to comprise all major production and trading countries.[64]

Consequences for Switzerland

Switzerland, because of its prominent position in all aspects of the commodities industry, including financing and transport, faces serious challenges in the implementation of coercive economic measures relating to commodities. According to the figures of the UN Independent Inquiry Committee (IIC), which in 2004-2005 investigated accusations of corruption surrounding the Iraqi "Oil for Food" program, Switzerland ranked third, behind Russia and France, among the largest purchasers of Iraqi oil. In Switzerland, 75 companies were licensed to deal in Iraqi oil. Approximately one half of the oil trade with Iraq was financed by banks domiciled in Switzerland. Hence, a significant portion of the investigations by the IIC involved companies and individuals in Switzerland.

Switzerland implements all UN Security Council sanction resolutions. Failure to adopt completely, and without hesitation, sanctions imposed by its most important commodity trading partners can easily expose Switzerland to accusations, both at home and abroad, that it is attempting to profit economically by allowing businesses to circumvent sanctions. This represents a reputational risk for the country as a whole. Moreover, discrepancies between the legal situation in Switzerland and in the countries who are its main trading partners can lead to legal uncertainty, in particular, for companies whose operations are internationally based.

For the companies themselves, breaches of international sanctions can have both criminal consequences and give rise to reputationally damaging publicity.[65]

The international interconnections between the large commodity trading companies has the effect, in part, of minimising risk. As a rule, these companies cannot afford to pursue business poli-

[63] Imports and exports of over US$2 billion per year, respectively. Practically all trading in rough diamonds is conducted through bonded warehouses.

[64] The Ordinance on the International Trade in Rough Diamonds (Diamond Ordinance, SR 946.231.11), by means of which the Kimberley Process certification system was implemented in Switzerland, also takes as its statutory basis the EmbA.

[65] Thus, for example, in 2005/2006 a Ticino gold smelter was confronted overnight with extreme financial difficulties, after having been accused (wrongly) in a UN expert report of involvement in the illegal gold trade with the Democratic Republic of the Congo. Because of the report and the negative repercussions thereof in the media, many business partners distanced themselves, jeopardising the gold smelter's continued existence.

cies that contravene sanctions imposed by the US, or the EU, for example. This correlation does not exist for small companies and micro-enterprises that have no relations whatsoever with the US or the EU and which may, therefore, be tempted to exploit loopholes in the Swiss sanctions regime in a very targeted manner. It is also the case, however, that US and EU nationals who work for Swiss companies have an obligation to comply not only with the Swiss legal order but also with sanctions imposed by their home countries.

Finally, even where Switzerland incorporates quickly and comprehensively into its own legal order commodity sanctions imposed by the UN or major trading partners, the size, diversity, lack of transparency, and mobility characteristic of the industry render the monitoring of compliance with any bans that are issued a highly challenging undertaking.[66]

4.4. Financial Reporting

International situation

The G8 governments[67] committed themselves in the Closing Statement of their Deauville Summit, in May 2011,[68] to enacting legal provisions for promoting voluntary standards that require or encourage oil, gas, and mining companies to disclose the payments they make to governments.

In the ***USA***, the Dodd-Frank Wall Street Reform and Consumer Protection Act (Section 1504), [69] which was adopted in July 2010, foresees that exchange-listed US and foreign resource extraction and export companies registered with the US Security and Exchange Commission (SEC) are required to provide information, on a country and project basis, concerning any payments in excess of US$100,000 made to governments for rights to access and extract oil, natural gas or other natural resources. Transparency is required, inter alia, with regard to taxes, royalties, licensing fees, dividends, and infrastructure spending. For each payment, disclosure must be made as to the total amount, category, currency, and financial period of payments made for each project, to each government, with an indication of the company's business segment and any other information considered by the SEC as appropriate, in the public interest and for the protection of investors. Disclosure is required – pursuant to the implementation provisions to Section 1504 – beginning in September 2013, whereby actual implementation is currently uncertain, as a coalition of industry representatives is presently pursuing litigation in the matter before a US Federal Court. The Dodd-Frank Act (section 1502)[70] further provides that any producer listed on a US exchange, and its suppliers, that work with conflict minerals originated in the Democratic Republic of the Congo or an adjoining country must, as of January 2013, report on the source of those minerals and on the measures taken to exercise due diligence with regard to the chain of their supply.[71]

In the **EU**, the European Commission, in October 2011, submitted to the Parliament and the Council of Ministers amendments to the Financial Reporting and Transparency Directives,[72] which also foresee the introduction of country-by-country disclosure requirements for exchange-listed and large[73] non-listed extractive industry companies and for forestry companies logging in

[66] Cf. Interpellation 11.4187 of 23 December 2011 by Carlo Sommaruga: Effective enforcement of the ban on the purchase and transport of Syrian oil.
[67] Germany, France, Italy, Japan, Canada, Russia, the United Kingdom, and the United States.
[68] Deauville G8 Declaration, Renewed Commitment for Freedom and Democracy, para. 62.
[69] Section 1504 adds Section 13(q) to the Securities Exchange Act of 1934.
[70] Section 1502 adds Section 13(p) to the Securities Exchange Act of 1934.
[71] The SEC voted on the implementation provisions on 22 August 2012. Further information and the final version of the rule are available at http://www.sec.gov/news/press/2012/2012-164.htmandhttp://www.sec.gov/rules/final/2012/34-67716.pdf.
[72] Directive 2004/109/EC on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market and amending Directive 2001/34/EC (Transparence Directive), the Fourth Accounting Directive (78/660/EEC) and the Seventh Accounting Directive on consolidated accounts (83/349/EEC).
[73] The revised Directives 78/660/EEC and 83/349/EEC define as large companies those that exceed two of the following criteria: balance sheet total of EUR 40 million; net turnover of EUR 20 million; 250 employees on aver-

primary forests. Disclosure is to be made of production entitlements; taxes on profits; royalties; dividends; signature, exploration and production bonuses; rental fees, entry fees and other considerations for licences and/or concessions; and other direct payments to the government concerned. Material payments are to be broken down by country and, where feasible, by project. In the on-going legislative procedure, the EU Member States have expressed a preference for limiting the requirement to country-specific reporting, without a breakdown by projects. The Council has taken the position that the requirement should be applied only for payments exceeding EUR 500,000. The EU Parliament, by contrast, continues to favour the proposal by the Commission and a lower threshold amount. Conclusion of the discussions in the Council and the Parliament is not to be expected before the spring of 2013.[74]

Accordingly, extractive industry companies domiciled in Switzerland and are exchange-listed in the US or the EU would, pursuant both to the provisions proposed by the EU Commission and to the Dodd-Frank Act, be required to disclose all payments made to governments.

In response to the developments in the US and the EU, extraction industry associations and non-governmental organisations in **Canada** signed, on 6 November 2012, a memorandum of understanding for the establishment of a framework for the obligatory disclosure, on a country-by-country and project-by-project basis, of payments made by extraction companies to governments. A draft is expected to be ready by mid-2013, which will then be submitted for implementation to the Canadian national government, the Provincial governments, and/or to stock exchange regulators.[75]

In ***Singapore***, the introduction of regulations for exchange-listed mineral, oil, and gas companies, requiring country-specific disclosure of payments, is not at present foreseen. The regulatory situation in Singapore is of some interest, inasmuch as that country could come to be seen by (commodity) companies – among other things, for tax reasons – as an alternative to Switzerland when choosing a place of domicile.

The **Global Reporting Initiative** (GRI) develops guidelines for the preparation of sustainability reports by large corporations, small and medium-sized enterprises (SMEs), governments, and NGOs. In order to fully satisfy the GRI standards ('A' rating), the Sustainability Reporting Guidelines[76] call for the country-by-country disclosure of all tax payments and, where material, other revenues, operating costs, employee compensation, interest payments and dividends.[77] For the specific reporting duties for the mining and metals industry, and the oil and gas industry, supplementary guidelines are issued.[78] Since 2012, Switzerland supports the GRI in its efforts to raise awareness for the value of sustainability reporting and to strengthen capacities in that domain in developing countries.

The ***Extractive Industries Transparency Initiative (EITI)***, founded in 2002 by governments, companies and NGOs, addresses itself to resource-rich countries to promote the disclosure in annual reports of the flows of all payments made by extractive industry companies to governments in the form of taxes, royalties, or other charges and fees. The EITI seeks to increase the transparency of payment flows as a means towards improved allocation and use of natural resource revenues. All resource-rich countries may join the EITI voluntarily; companies that extract natural resources in those countries then have an obligation to make disclosure of the payments they make to the government. Based on a review of the EITI Standards in 2011, concrete improvements were agreed upon at the last meeting of the EITI Board (October 2012), in order to

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age during the financial reporting year.

[74] For further information, see http://ec.europa.eu/prelex/detail_dossier_real.cfm?CL=en&DosId=200973.

[75] Further information and the text of the memorandum of understanding are available online at http://www.mining.ca/www/media_lib/MAC_News/2012/Transparency%20QA_Final.pdf and http://www.mining.ca/www/media_lib/MAC_News/2012/Transparency%20MoU.pdf.

[76] Available online at: https://www.globalreporting.org/reporting/latest-guidelines/g3-1-guidelines/Pages/default.aspx.

[77] Global Reporting Initiative (2006), Indicator Protocols Set: Economic Performance Indicators, pp. 4-5.

[78] So-called "Sector Supplements".

heighten the impact of the EITI. Among other things, it was decided that company-specific disclosure of payment information would be considered as required as of mid-2013, and that further discussion should be held on the disclosure of sales by state oil enterprises, and of awards of licences and contracts. 18 countries, the majority of them African, currently satisfy all EITI Compliant Standard requirements; 19 countries are currently engaged in efforts to do so. Switzerland has supported this Initiative since 2009 by accepting membership on the EITI Board, and by contributing to two trust funds administered by the World Bank Group, which provide support to countries in the implementation of the EITI, and to a trust fund administered by the IMF that assists finance ministries with the management of revenues from natural resource extraction.

The ***OECD Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High-Risk Areas*** (see also below, section 5.1), which was developed in 2011 by a wide circle of stakeholders,[79] addresses itself to extractive industry companies that operate in conflict zones. The "Guidance" assists these companies in identifying risks and in complying with their duty of diligence with regard to the supply chain, and thus in helping them avoid providing indirect support for conflicts or contributing to human rights violations through their activities. The "Guidance" is supplemented by two additional documents which deal with the specific challenges involved in the extraction and trading of gold and the metals tin, tantalum, and tungsten. The implementation of the OECD Guidance will assist producers who are subject to Section 1502 of the Dodd-Frank Act in the fulfilment both of their duty to disclose downstream suppliers and of their due diligence obligations.[80]

With regard to the ***International Financial Reporting Standards (IFRS)***, in a public consultation with stakeholders conducted in 2011 by the International Accounting Standards Board (IASB), the introduction of a country-specific disclosure requirement for extractive industry companies (including payments to governments) was assigned a low priority. In consequence, this issue, unlike the research project on possible future financial reporting standards for extractive industries,[81] is not on the IASB's current agenda.[82]

Situation in Switzerland

The new Financial Reporting Code, as amended on 23 December 2011 (nFR, i.e., amended articles 957ff. of the Code of Obligations), which entered into force on 1 January 2013, was conceived so as to be neutral with regard to the legal structure of a company, with distinctions being drawn based on the size of the company.

The nFR applies to companies that are subject to the accounting and financial reporting duty pursuant to CO art. 957. This is the case, in particular, where a company is domiciled in Switzerland and is registered in the commercial register. As long as a company does not have any outstanding bond issues and does not list its shares on a Swiss or a foreign stock exchange, it is not required to make public its annual financial statements or its consolidated financial statements (CO art. 958e).

The nFR does not draw any distinctions between different industries. It does not impose any duty to disclose payments to foreign governments or state-owned enterprises as separate items on the

[79] OECD Member States (Switzerland: State Secretariat for Economic Affairs, SECO) and other States, private sector companies, trade associations, non-governmental organisations, and academic institutions.
[80] See the remarks on the OECD Guidelines in the media release by the US Securities and Exchange Commission (SEC): http://www.sec.gov/news/press/2012/2012-163.htm.
[81] The project will deal simultaneously with financial reporting standards with regard to intangible assets, resource extraction activities, and research and development. The decision on whether to draft new IFRS standards will be made only after the research phase has been concluded.
[82] The results of the consultation and the bases for the subsequent discussion at the IASB in January 2012 are available online at http://www.ifrs.org/Current+Projects/IASB+Projects/IASB+agenda+consultation/meeting_summaries/IASB+January+2012.htm and http://www.ifrs.org/Current+Projects/IASB+Projects/IASB+agenda+consultation/meeting_summaries/IASB+May+2012.htm.

statement of earnings or in the notes to the annual financial statements (see OR art. 959b). The National Council clearly rejected the inclusion of a duty for transnational corporations to include country-specific information in the consolidated financial statements.[83] It did not, however, discuss the possibility of a limited disclosure duty applicable to payments to governments and state-owned enterprises by commodity companies. CO art. 959b, para. 5, does, nevertheless, provide that additional line items must be posted in the statement of earnings, or in the notes thereto, "insofar as this is material to an assessment of the funding situation by third parties or customary due to the nature of the company's business."

Companies whose shares are listed on a stock exchange and, if so ordered by the exchange, cooperative associations with a minimum of 2000 members, as well as foundations required by law to conduct regular audits, must also prepare an additional annual statement in keeping with a recognised accounting standard (CO art. 962, para. 1), such as the International Financial Reporting Standards (IFRS), for example. IFRS 6 ("Exploration for and Evaluation of Mineral Resources") does not foresee any duty to make specific disclosure of payments to foreign governments or state-owned enterprises. Nor do other IFRS rules prescribe the explicit disclosure of such payments. These must, however, be disclosed (indirectly) where they give rise to material additional expenses for the company and/or a need to set aside reserves. Those same companies must also prepare consolidated financial statements in keeping with a recognised accounting standard (CO art. 963b).

Where the parent company of a corporate group is an association, a foundation, or a cooperative, the duty to prepare the consolidated financial statements may be delegated to a subsidiary, provided that the latter, by means of a voting majority or by other means, controls all other companies in the group under unified management, and demonstrates that it does in fact exercise such control (CO art. 963, para. 4). The possibility of delegating the duty of preparing the consolidated financial statements, which the Swiss Parliament has included in the new Financial Reporting Code, brings with it potential for abuse, in that certain business dealings and transactions on the part of the association, foundation, or cooperative that delegates the duty will not necessarily need to be included in the consolidated statements.[84]

4.5. Corporate taxation

For companies that specialise in commodity trading, taxes are an important – though by far not the only – factor in deciding where to locate (see above, section 3.1). Different potential locations compete with each other and offer favourable tax conditions as a means of attracting companies. With regard to the commodities industry, tax competition not only with Asian countries, but also with other countries in Europe, is intense.

An important element in that international competition is not simply the rate of taxation that applies, but the structure of the tax regime. In Switzerland, companies with predominantly international activities – including commodity merchanting companies – may, as so-called "mixed companies" or as domiciled companies, be eligible to benefit from special tax regimes, subject to certain conditions at the cantonal level.[85] Some of these corporate tax regimes have come in for criticism by the EU, because they treat domestic and foreign revenues differently.

In July 2012, the Federal Council – after consultations with the appropriate Parliamentary committees and the cantons – issued a mandate for a dialogue with the EU over corporate tax regimes. The objective is to find a solution that confirms Switzerland's competitiveness as a business domicile, is adequate to the budgetary needs of the Confederation and the cantons, and is capable of finding a higher level of international acceptance.[86] Negotiations with the EU are being conducted

[83] AB 2010 N 1918ff.; see also Interpellation 11.3859, "Country-by-country financial reporting. Switzerland a regulatory oasis?" submitted by National Councillor Hans-Jürg Fehr.
[84] See AB 2011 N 882ff.; AB 2011 S 262ff.; AB 2010 N 1913ff.
[85] See on this the detailed response by the Federal Council to Question submitted by Badran (12.1119).
[86] See relevant media release at http://www.sif.admin.ch/dokumentation/00513/00772/index.html?lang=en&msg-

under the direction of the FDF, together with the FDFA and the EAER, and in consultation with the cantons. Adoption of the EU Code of Conduct by Switzerland is not being considered. The dialogue with the EU is closely tied to the ongoing Corporate Tax Reform III. In September 2012, the Federal Department of Finance and the Conference of Cantonal Finance Directors established the terms of reference for collaboration on the Corporate Tax Reform III.[87] Reform proposals are currently being drafted.

4.6. Transfer pricing and double taxation agreements

By creating corporate structures suited to the purpose in connection with the use of recognised transfer pricing structures, it is possible to concentrate earnings in locations where they are subject to a low tax burden. Globally operative commodity groups – like other multinational enterprises, as well – sometimes face criticism that through such corporate structures they contribute to a substantial reduction of the tax base in commodity-exporting countries (often developing countries).

Switzerland has not enacted any specific provisions for the review of transfer pricing practices. Nevertheless, pursuant to the Circular of 19 March 2004, issued by the Swiss Federal Tax Administration (FTA), the cantons are encouraged to apply the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations.[88] Pursuant to these internationally recognised OECD Guidelines, added value generated through commodity trading transactions is appropriately compensated where the transfer price applied between members of the same corporate group corresponds to that which is charged by independent third parties for the same performance to the same conditions.[89]

Where the transfer pricing policies of a corporate group are found to be abusive, a country whose interests have been prejudiced may, in reliance upon a double taxation agreement (DTA) that contains an applicable stipulation to that effect, make adjustments to the declared earnings of companies domiciled on its territory and tax them accordingly. The initiative in such cases must come from the country that has suffered the prejudice. Unfortunately, because the accounting know-how needed for the auditing of transfer prices is often lacking, particularly in developing countries, the transfer pricing methods used by global commodity companies are rarely subjected to review there. Cognisant of this problem, the OECD is making efforts to raise awareness for the issue, also in developing countries, as, for example, within the framework of the Global Forum on Transfer Pricing. Switzerland supports the OECD in this area and has thus far put into effect or initialled over 45 DTAs with developing countries and emerging economies.[90]

The conclusion of tax information exchange agreements (TIEA) is another means by which developing countries can be assisted in obtaining the information needed for appropriate taxation. However, according to the report by the Federal Council in response to Postulate 10.3880, "Pros and Cons of Information Exchange Agreements with Developing Countries", DTAs are, as a general rule, to be preferred, because they simultaneously make it possible to avoid double taxation.[91]

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id=44786.

[87] See the media release at http://www.efd.admin.ch/dokumentation/medieninformationen/00467/index.html?lang=en&msg-id=46084

[88] See http://www.oecd.org/ctp/transferpricing/transferpricingguidelinesformultinationalenterprisesandtaxadministrations.htm

[89] See article 9 of the Model Tax Convention on Income and Capital (http://www.oecd.org/tax/taxtreaties/oecdmtcavailableproducts.htm).

[90] See http://www.sif.admin.ch/themen/00502/00740/index.html?lang=en for an overview of Switzerland's DTAs.

[91] See also Motion 12.3796, "Conclude Tax Information Exchange Agreements with Developing Countries". The report of 4 April 2012, in fulfillment of Postulate 10.3880 may be consulted at: http://www.efd.admin.ch/dokumentation/zahlen/00578/02572/index.html?lang=de (in German).

The OECD also addresses the issue of tax avoidance by multinational enterprises in a horizontal project entitled “Basic Erosion and Profit Shifting” (BEPS). The purpose of the project is, among other things, to study the question of whether the taxable profits of multinational enterprises are allocated to locations different from those where their actual business activity takes place and, if so, to analyse the reasons for this phenomenon. Based on the study’s findings, the OECD plans to develop corrective measures within the framework of an action plan. The OECD is expected to proceed with these efforts at a brisk pace, with a view to the meeting of the Steering Committee in June 2013. As an OECD Member State, Switzerland also collaborates in these efforts. In that context, it is important that fundamental legal principles be respected and that there be a level playing field in competition in the domains of taxation and subsidies. It is anticipated that the action plan will be presented at the G20 Summit of Heads of State and Government in St Petersburg in early September 2013.

5. Corporate responsibility and government responsibility

5.1. Corporate responsibility

5.1.1. Background

The extraction of natural resources creates numerous challenges for the resource-exporting host countries, for the countries where commodity companies are domiciled, and for the companies themselves. All of the actors involved must assume a particular responsibility with regard to: the environment, conflict-zone situations, compliance with labour standards (including child labour), human rights, forced resettlement, the need for security forces for the protection of mines (value of investments and extraction products), and taxes.

A fundamental distinction must be drawn between the responsibility of companies and that of governments, both those of the host countries and those of countries in which multinational corporations are domiciled. The primary responsibility for enforcement of the applicable laws and standards lies with the host country in which natural resources are extracted or processed. There is, however, a growing recognition that with globalisation and the rising importance of private actors, new approaches are needed. Particularly in fragile states of the developing world, insufficient government capacities or ties between corrupt actors within the government, administration, and judiciary, render the task of implementing legal prescriptions more difficult.

For the multinational commodity companies that operate in such contexts there arises, therefore, a special responsibility with regard, for example, to the respect of human rights, the prevention of corruption, and protection of the environment. By voluntarily applying international codes of conduct and through similar initiatives, companies can make an important contribution to the implementation of internationally recognised standards in the host countries (see below, section 5.1.2).

Human Rights

The UN Guiding Principles on Business and Human Rights provide, for the first time, an internationally recognised frame of reference that addresses, against the backdrop of globalisation, the issue of the responsibilities of governments and the private sector to protect and respect human rights.[92] The Universal Declaration of Human Rights states, moreover, that every organ of society has an obligation to promote and recognise human rights. Accordingly, business enterprises also share in the obligation to respect and to promote respect for human rights.

[92] “Ruggie Strategy”: In order to conduct discussions on activities for the implementation of the UN Guiding Principles on Business and Human Rights also with non-governmental actors (in particular, from the business sector, the academic world, and the civil society), the Confederation has launched a multi-stakeholder dialogue. At issue are the activities of all business sectors, and not specifically those of the commodity branch. Upon adoption by the Parliament of Postulate 12.3503, submitted by von Graffenried, the Parliament instructed the Federal Council to prepare a report outlining a strategy for the implementation of the UN Guiding Principles on Business and Human Rights.

The Confederation and the Swiss representations abroad are confronted with cases in which companies under Swiss ownership, or in which Swiss nationals hold an interest, are brought into connection with violations of human rights. Among such companies are also members of the resource extraction industry, where particular risks exist in terms of human rights violations, that is, where there is a particular danger that companies may be remiss in their responsibility to respect human rights. In addition to the immediate effects that the extractive industries may have for the protection of human rights – e.g., the creation of precarious working conditions – there are also indirect consequences that may make themselves felt. Forced resettlement, for example, is normally carried out by host countries, but they do so with the intention of making possible the extraction of natural resources in the region. Forced resettlement can lead to various internationally recognised violations of human rights, including such rights as those to adequate shelter, food, water, health, education, employment, or security. In many cases, it is primarily indigenous population groups and minorities that bear the brunt of these effects. Other problem issues relate to the purchase of natural resources from dubious sources. This includes, specifically, the trade in resources from small-scale artisanal mines, where workers are, in some cases, exploited, working under extremely precarious conditions (in terms of job security, etc.), and where further risks, such as those of child labour and sexual exploitation, also exist.[93]

Environment

The exploration and extraction of natural resources inevitably has an impact on the environment. The environmental consequences of the extraction of non-renewable resources such as metals or fossil fuel sources are particularly serious: thus, for example, mining (extraction, processing and waste disposal) is often tied to erosion effects, biodiversity loss, and the contamination of soil and groundwater. Negative effects on the environment are in many cases also a result of the large amounts of material that must be processed (bedrock, fossil fuels) in order to produce a given amount of metal,[94] or of the fact that newly discovered, difficult-to-access reserves can be exploited only with high risks to the environment (e.g., deep-sea drilling for fossil fuels; hydraulic fracturing ["fracking"] of shale).

At the international level, there are no agreements that specifically address the environmental aspects of commodity production. Nevertheless, there are principles of customary international law (e.g., the duty not to cause transboundary environmental damage) and principles of formal international law (e.g., the "precautionary" and "polluter pays" principles) that do apply. In addition, there are various agreements that deal with the environmental consequences of resource extraction (biodiversity, water conservation, environmentally hazardous substances, etc.), and thus influence national environmental legislation. The environmental agreements drafted by the UN Economic Commission for Europe (UNECE) were specifically designed to prevent significant detrimental transboundary effects on the environment resulting from certain types of projects (oil refineries, mining, etc.).

There is a high degree of variation worldwide in the density of regulation and in the implementation of these agreements from region to region. While significant progress has been made through the UNECE, there is still significant room for improvement, particularly in developing countries. In addition, national courts are often hesitant in applying environmental principles and standards to corporations. Hence, it not primarily on binding standards and guidelines that efforts to ensure respect for environmental considerations in the extraction of resources are based.

Over the past 10 years, due to increased pressure on large multinational corporations, sensitivity to the environmental consequences of resource extraction has been heightened. By means of voluntary measures and initiatives, greater account is given to environmental considerations by large corporations. Thus, for example, the OECD Guidelines for Multinational Enterprises, which Switzerland supports, and the 10 principles of the UN Global Compact, include concrete de-

[93] See, e.g., "In Brief: Human rights, social development and the mining and metals industry" by the International Council on Mining & Metals, June 2012.
[94] A factor of 8 for steel, a factor of 37 for aluminium, and a factor of 348 for copper.

mands with regard to the environment (see below, section 5.1.2). In order for voluntary measures to be effective, however, it is, of course, essential that they be rigorously implemented by the companies. Conversely, such standards are often not applied by small and medium-sized companies, or where mining is conducted illegally.

Corruption

The commodities industry has not been spared from the scourge of corruption.[95] The relatively high degree to which companies in that industry are exposed to the risk of corruption can be explained by a combination of several factors.[96] First, the majority of fuel and mineral resources come from fragile states where the problem of corruption is particularly widespread. This is acerbated by the high degree of interaction between the companies concerned and the government authorities in those countries; the awarding of public contracts, the granting of licences, the payment of royalties, the creation of monopolies, and the determination of customs policies are all procedures that tend particularly to attract incitement to bribery. Finally, although the amounts at stake are quite considerable, there is little transparency in the commodities market; the complex structure of certain holding companies, and the fact that not all companies list their shares on an exchange, are conducive to the industry's relative opacity.

Also for companies domiciled in Switzerland and operating abroad, corruption can be a true problem. The pressure they face on the international markets is compounded by difficulties linked to the legal specificities, customary practices, or political situations prevailing in the countries where they operate. Upon request, the Swiss representation in the State in question provides companies with its assessment of the political or other risks posed by conditions in the country.

Regardless of the circumstances, however, such companies are subject to the entire body of Swiss legislation in the matter of preventing corruption,[97] and to the relevant laws of the States where they conduct their operations. Particularly in contexts where the rule of law is fragile, however, the enforcement of such legislation cannot be guaranteed, due to insufficient capacities, or the direct complicity, of the government, administration, and judiciary with the parties involved in corruption.[98] At the national level, Switzerland has ratified the three main international agreements dealing with the prevention of corruption, and its commitment is regularly subject to evaluation by peer review. Switzerland always receives good marks. In fighting corruption, Switzerland also draws upon voluntary initiatives for the responsible performance of due diligence by companies (see section 5.1.2), which formulate specific requirements with regard to corruption issues.[99]

International cooperation, in particular with States that do not apply the same standards, as well as the determination with which Switzerland implements the legislative instruments to which it has subscribed, are determinant factors in ensuring the effectiveness of the fight against corruption in the commodities market. Finally, the voluntary commitment of companies is of decisive importance in guaranteeing the integrity of their business dealings.

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[95] The term corruption refers to any abuse of a position of trust for the purpose of obtaining an undue advantage. Two forms of conduct are intended: that of the person who abuses his position of trust, and that of the person who, in return, grants an undue advantage. Corruption concerns both public servants and private individuals, and legal persons. See the brochure published by the SECO (2008), "Preventing corruption – Information for Swiss businesses operating abroad", p. 6.

[96] The Bribe Payers Index 2011, by Transparency International bears witness to the particularly high risk of corruption that is characteristic for the commodities industry (cf. p. 15).

[97] The bribing of public officials is a punishable offence pursuant to art. 322$^{ter\text{-}septies}$ of the Swiss Criminal Code (SCC); bribery in the private sector is proscribed by art. 4a of the Unfair Competition Act (UCA); the criminal liability of legal persons is governed by art. 102, para. 2, of the SCC.

[98] The *OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions*; the *Council of Europe's Criminal Law Convention on Corruption*; and the *UN Convention against Corruption*.

[99] Cognisant of the fact that that international commercial transactions are fertile ground for the solicitation and offering of bribes, the OECD has published, among other things, recommendations in this regard in chapter VII of its *Guidelines for Multinational Enterprises* (combating bribery, bribe solicitation, and extortion). These recommendations include, notably, the banning of corrupt practices by the enterprises themselves or via third parties; the adoption of adequate internal control mechanisms or of ethics and compliance programs or measures; the proper performance of due diligence with regard to agents engaged by the enterprise; transparency in the publicising of their efforts to combat corruption; the prohibition of illegal political contributions.

5.1.2. Instruments of corporate social responsibility

Guiding principles

Switzerland expects of all companies that operate internationally, in addition to compliance with both domestic and foreign statutory requirements, that they also exercise due diligence as a part of their corporate social responsibility (CSR).[100] This applies particularly in countries where the rule of law is not yet sufficiently well-developed, and in conflict zones. In keeping with this policy, the Confederation supports and is actively involved in the development and implementation of various international instruments and standards for the promotion of corporate social responsibility. These include, above all, the comprehensive, internationally recognised principles and guidelines: the OECD Guidelines for Multinational Enterprises101 and the 10 Principles of the UN's "UN Global Compact".[102] In addition, Switzerland also supports the thematically focused instruments of the ILO (Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy)[103] and the United Nations (Guiding Principles on Business and Human Rights).[104] Further, Switzerland is also actively involved in the drafting of the ISO 26000 Standard on Social Responsibility. These instruments serve companies in all industries as a frame of reference for the drafting and implementation of a corporate code of conduct. Through its commitment to the ILO Core Labour Conventions[105] and two declarations,[106] Switzerland also lends its support to universal rules and regulations that promote the sustainable development of world trade, also in the commodities industry. Switzerland has also assisted in the drafting of further international instruments and initiatives that deal with certain issues in a more targeted manner: (e.g., protection of minorities, the promotion of the Core Labour Conventions in ILO cooperation projects, corruption)[107] and provides active assistance in their implementation.

Specific instruments pertaining to resource extraction

In response to the challenges characteristically associated with the extractive industries, a number of voluntary initiatives and instruments have been launched since the beginning of the millennium in order to assist companies in achieving sustainable extraction of natural resources.[108] As a part of its development cooperation efforts (SECO and SDC) and under the terms of the budget allocation for promoting human security (FDFA/HSD), Switzerland supports various of these initiatives. In recent years, Switzerland has shown a particularly strong engagement for some specific initiatives, including:

- the *OECD Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High-Risk Areas*: Switzerland provides financial support for implementation and is a member of the governance group that watches over the implementation procedure (see also above, section 4.4).

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[100] On the definition and role of CSR, see the CSR concept paper published by the SECO, December 2009, at http://www.seco.admin.ch/themen/00645/04008/index.html?lang=en (in German).
[101] http://www.seco.admin.ch/themen/00513/00527/01213/index.html?lang=en
[102] http://www.unglobalcompact.org/
[103] http://www.ilo.org/empent/Publications/WCMS_094386/lang--en/index.htm.
[104] http://www.ohchr.org/documents/issues/business/A.HRC.17.31.pdf.
[105] Freedom of Association and Protection of the Right to Organise Convention, 1948 (No. 87): BBl **1974** I 1633 / SR **0.822.719.7**; Right to Organise and Collective Bargaining Convention, 1949 (No. 98): BBl **1999** I 513 / SR **0.822.719.9**; Forced Labour Convention, 1930 (No. 29): BBl **1939** I 749 / SR **0.822.713.9**; Abolition of Forced Labour Convention, 1957 (No. 105): BBl **1958** I 530 / SR **0.822.720.5**; Minimum Age Convention, 1973 (No. 138): BBl **1999** I 513 / SR **0.822.723.8**; Worst Forms of Child Labour Convention, 1999 (No. 182): BBl **2000** I 330 / SR 0**.822.728.2**; Equal Remuneration Convention, 1951 (No. 100): BBl **1971** II 1530 / SR **0.822.720.0**; Discrimination (Employment and Occupation) Convention, 1958 (No. 111): BBl **1960** I 29 / SR **0.822.721.1**.
[106] The ILO Declaration on Fundamental Principles and Rights at Work, 1998: BBl **200**0 330; ILO Declaration on Social Justice for a Fair Globalization, 2008: BBl **2012** 4209 (4257).
[107] *Good Practice Guidance on Internal Controls, Ethics and Compliance* (OECD 18 February 2010) and chapter VII of the OECD Guidelines for MNEs.
[108] These initiatives sometimes take the so-called "multi-stakeholder" approach (that is, they attempt to involve the major actors); they can, however, also be the result of efforts undertaken of their own accord by the parties concerned (e.g., industry associations).

- the *Better Gold Initiative*: in the course of the year 2013, Switzerland will be launching the Better Gold Initiative. The declared objective of this initiative is to establish, through an international private-public-partnership, a value chain for the fair and sustainable extraction and trading of gold. By this means the share of "ethical gold" in the market is to be increased. On the production side, the first step will be capacity-building for cooperatively organised micro-mines and small-scale artisanal mines in Peru, to enable them to extract gold sustainably (in keeping with the standards set by the Fair Trade and Responsible Jewellery Council). On the demand side, several actors (refineries, jewellers, and banks) have already expressed an interest. With this effort, the Better Gold Initiative represents a concrete contribution towards implementation of the *OECD Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High-Risk Areas*.
- the *Voluntary Principles on Security and Human Rights (VPSHR)*: this multi-stakeholder initiative (civil society, members of the commodities industry, Member States) has the objective of preventing human rights violations by security forces in the commodities industry. Switzerland became a full member in September 2011. Since 2012, a commodities company domiciled in Switzerland is in the process of becoming a member of the initiative. One of Switzerland's objectives is to convince further commodity companies domiciled in Switzerland to participate as well.
- the *Extractive Industries Transparency Initiative (EITI)*: Switzerland has been making efforts since 2009, along with other Donor States, to strengthen this initiative and, with it, also Switzerland's international commitment in the commodities domain. Switzerland is a member of the EITI board and finances at the multi-lateral level implementation of the initiative in certain countries together with the World Bank; at the same time, Switzerland also provides bilateral support for individual countries (Peru) (see also above, section 4.4)
- Also worthy of mention are the Swiss initiatives on private military and security companies, namely, the Montreux Document of 2008, which reiterates the relevant obligations under international law and lists recommendations to States in the matter of private military and security companies operating in armed conflicts; and the 2010 Code of Conduct for Private Security Service Providers. Security operations are an important element in daily operations along the commodity trading chain; the International Code of Conduct provides a suitable instrument for the establishment, in the future, of a certification mechanism in this domain.

In addition, Switzerland has in recent years actively taken part in multi-stakeholder procedures for the drafting and implementation of numerous voluntary private standards for promoting sustainable production and processing methods for various commodities, including coffee (*4C*), cotton (*Better Cotton Initiative*-BCI), soy beans (*Roundtable on Responsible Soy* – RTRS), biofuels (*Roundtable on Sustainable Biofuels* – RSB), and palm oil (*Roundtable on Sustainable Palm Oil* – RSPO). Switzerland is also a pioneer in the domain of *Cleaner Production*,[109] and supports this concept in numerous developing countries.

Finally, through its of a National Contact Point (NCP)[110] for the OECD Guidelines for Multinational Enterprises, Switzerland actively engages in efforts to resolve concrete problems that may arise in connection with the activities of Swiss companies abroad. The NCP makes it possible, in response to requests filed by private individuals, NGOs, or labour unions, to open a dialogue with the company concerned and to contribute to a resolution of the problem. In recent years, the NCP

[109] "Cleaner Production" refers to a preventive, company-specific environmental protection methodology based on organisational and technical improvements (efficient use of natural resources and energy, prevention of waste, waste water, and gaseous emissions).

[110] The Swiss NCP is placed under the authority of the State Secretariat of Economic Affairs (SECO), as part of the International Investment and Multinational Enterprises (IIME) unit. Complaints submitted to the Swiss NCP are handled by internal working groups created on an ad hoc basis. The composition of such groups depends upon the subject matter of the complaint. Members of the working group are chosen from those federal agencies that dispose of the specific expertise needed for dealing with the case in question (e.g., the FDFA / HSD for human rights issues, the FOEN for environmental issues, the SECO / DE for employment issues, etc.).

has dealt with an increasing number of requests in connection with the commodities industry (both trading and extraction). It is also actively involved at the international level in efforts to enhance cooperation with companies active in the industry.[111]

There are various grounds for Switzerland's commitment: the country's long-standing tradition in merchanting and the traditional importance of the commodities industry in Switzerland facilitate cooperation with such companies; this is coupled with a national will both to assist developing countries – in the fight against corruption, in the strengthening of good governance, and in the proper management of public finances – and to promote corporate social responsibility. In recent years resource extraction has also been the object of increased public attention. In this area, Switzerland's commitment, in addition to addressing the interests of developing countries, also focuses on the needs of businesses that operate in difficult environments – such as conflict zones – and require concrete guidance for the implementation of corporate social responsibility norms.

5.2. Legal situation with regard to cross-border business operations

The possibility of bringing action before Swiss courts against a parent company domiciled in Switzerland for acts committed by a subsidiary or a supplier in another country does exist, subject to certain conditions.

5.2.1. Civil actions

Actions before Swiss courts

A distinction must be drawn between the questions of legal jurisdiction and applicable law. While the statutory provisions on jurisdiction determine whether a given action before a Swiss court is at all possible, the question of whether a company can in fact be held liable is decided according to applicable law. These questions must be decided independently of each other. It may thus occur that even if a court rules that it has jurisdiction to hear a given case, it will still deny liability by reason of the applicable law.

Jurisdiction

In civil actions based on tort, filed in Switzerland against business undertakings, jurisdiction lies with the Swiss courts in the place where the company's registered office112 is located (Private International Law Act [PILA] art. 129; Lugano Convention [LC] art. 2, para. 1, and art. 5, para. 3). The prerequisite for filing such an action, therefore, is that the company in question be domiciled in Switzerland, a condition that is fulfilled by definition in the cases here under consideration, i.e., those of parent companies domiciled in Switzerland. Hence, it is, in principle, possible to bring suit against holding companies domiciled in Switzerland, regardless of whether the alleged tortious acts were committed by their company itself or by its subsidiaries. The same applies where action is to be brought against a subsidiary domiciled in Switzerland.

Where the company is not domiciled in Switzerland, it may nevertheless still be possible to bring action against it before the Swiss courts under certain circumstances. This would be the case, for example, if a tortious act whose effects are felt in another country was committed by a company operating out of Switzerland (jurisdiction at the Swiss place of commission), or if a tortious act committed abroad were to cause injury in Switzerland (jurisdiction at the place of injury). Thus, for example, an American company was able to be sued in Switzerland for providing technical support for the Holocaust between 1935 and 1945 from premises located in Geneva: the place of commission was situated in Switzerland.[113]

[111] E.g., the NCP seminar with the commodity industry umbrella organisation, the International Council on Mining & Metals (ICMM), held in London, in March 2012; Guide on Stakeholder Engagement in the Extractive Sector.
[112] Domicile pursuant to articles of association (PILA art. 21), and, in cases to which the Lugano Convention applies, location of main office or main branch (LC art. 60); PILA: Federal Act of 18 December 1987 on Private International Law, SR. 291; LC: Convention on Jurisdiction and the Recognition and Enforcement of Judgments in Civil and Commercial Matters (Lugano Convention), SR 0.275.12.
[113] BGE 131 III 153 and 132 III 661.

Other courts in Switzerland may also have jurisdiction, at the place where a branch office in Switzerland is located, for example, or in cases where more than one tortfeasor is involved. Finally, there are cases in which Switzerland may have default jurisdiction (PILA art. 3), where the bringing of action in another country is not possible or cannot reasonably be expected and the facts on which the claim is based have a sufficient connection with Switzerland.

Applicable law

The success of any action that is brought depends on the law that applies in the case. Before Swiss courts, applicable law in tort cases is determined pursuant to the terms of art. 132ff. of the PILA. The tortfeasor and the injured party may jointly opt to have Swiss law as the law applicable to their case. Where a choice of law has not been made by mutual agreement, the law of the country of habitual residence common to the tortfeasor and to the injured party automatically applies; by default it is the law of the place of commission that applies and, in exceptional cases, that of the place of injury. Switzerland has also ratified various international agreements that foresee special rules in specific domains, such as, for example, those of oil pollution or corruption.[114] For the purposes of the present report, however, remarks will be restricted to the Swiss statutes.

Under Swiss law, in cases of tort, it is the tortfeasor itself (i.e., in the case of tortious acts committed abroad, the subsidiary or supplier that commits the tort), and not the parent company, that bears liability. Exceptions come into consideration only where no organisational separation has been made between the parent company and the subsidiary, so that any assertion of the subsidiary's independent legal personality would constitute an abuse of process (so-called "piercing of the corporate veil"; Civil Code [CC] art. 2).[115] There is no general obligation on the part of holding companies to exercise oversight over their subsidiaries, and imposing such a duty would be contrary to the principle of the independence of legal persons; this responsibility lies with the managers and internal control bodies of the subsidiary. As a rule, therefore, it is the subsidiary that bears liability, and not the parent company.

Swiss civil procedure: tort jurisdiction

Swiss procedural law governing tort liability cases is based on the internationally recognised principle that jurisdiction should always lie with the court that has the closest connection with the subject matter of the case and is thus in the best position to adjudicate on it. As a rule, this will be the court at the place of domicile of the tortfeasor or the place of commission, that is, in cases of tortious acts committed abroad by foreign companies, a foreign court. The jurisdiction of Swiss courts in such cases will, accordingly, be admitted only reluctantly.

Conversely, it is self-evident that suits based on tortious acts committed on Switzerland's own territory may be brought at the place in Switzerland where the act was committed – a principle that is also followed in very many countries. Accordingly, as far as is known, all court cases against Swiss commodity companies that have been publicised in the media in recent years were tried at the foreign venue where the events at issue occurred, and not in Switzerland.

A fundamental responsibility on the part of holding companies for the acts of their subsidiaries does not exist under Swiss law, since legal persons are considered, as a rule, to be independent. Even in cases where a subsidiary that operates abroad is wholly owned by a Swiss holding company, it remains, from a legal point of view, entirely independent of the parent company. The identity of the beneficial owner of the company that commits the offense has, in principle, no bearing on liability.

For these reasons, the bringing of actions in Switzerland against internationally active holding companies for tortious acts committed abroad by foreign subsidiaries or suppliers is, as a rule, precluded and, even in cases where jurisdiction is admitted, such actions would be likely to suc-

[114] E.g., the International Convention on Civil Liability for Oil Pollution Damage of 29 November 1969, SR 0.814.291.
[115] Swiss Civil Code of 10 December 1907, SR 210.

ceed only in exceptional instances. Conversely, what is possible, as a rule, is the bringing of action against a "tortfeasor company" that bears responsibility, that is, suits against subsidiaries or holding companies for tortious acts that they themselves have committed, provided that a sufficient connection with Switzerland is established.

Actions before foreign courts

Whether or not multinational corporations domiciled in Switzerland can be held accountable in other countries for their own acts or for those of their subsidiaries or suppliers depends on the law of the other countries, so that it is not possible here to respond in general terms.

Insofar as can be ascertained, all actions brought before foreign courts against parent companies for offences committed by their subsidiaries in another country have been rejected. In January 2013, for example, a court in the Netherlands denied the liability of the Dutch company Royal Dutch Shell for environmental damage caused by subsidiaries in Nigeria. In the court's view, it is the subsidiary Shell Nigeria that must bear the liability. For purposes of legal comparison, attention should be drawn to the case of *Kiobel vs. Royal Dutch Petroleum*,[116] currently pending in the United States, which relates to the controversial question of the extraterritorial jurisdiction of US courts over international corporations. What is at issue is the question of whether international law requires the fulfilment of certain applicability criteria for the exercise of jurisdiction by a State (e.g., the acts in question took place on the territory of the State exercising jurisdiction). From a Swiss point of view, the existence of such requirements is to be affirmed.

The view that jurisdiction should lie with the courts that have the closest connection with the facts of the case is shared by a number of European countries that have taken a position on the aforementioned Kiobel case, such as, for example, Germany, the United Kingdom, and the Netherlands. The brief submitted to the US court by Germany draws attention to the legal situation in Germany and other European countries,[117] which is fundamentally the same under Swiss law – namely, that the liability of domestic holding companies for tortious acts committed abroad by their foreign subsidiaries is to be admitted only in exceptional cases. The countries mentioned admonish that the exercise of extraterritorial jurisdiction over such matters without the presence of sufficient points of connection (place of commission or of injury, or domicile of the "tortfeasor company" in the country exercising jurisdiction) would constitute a violation of the territoriality and sovereignty of other countries.

5.2.2. Criminal law

In criminal proceedings against business undertakings, jurisdiction lies with the authorities at the place where the company's registered office is located (Criminal Procedure Code [CPC] art. 36, para. 2).[118] Hence, prosecution can be brought in Switzerland only against those companies that are also domiciled in Switzerland –but against them it is nevertheless possible. Thus, for example, in November 2011, a company domiciled in Switzerland was fined because persons in positions of responsibility had not taken all necessary and reasonable organisational measures to prevent the payment of bribes to foreign officials in Latvia, Tunisia, and Malaysia.[119]

It should be noted, however, that other than in a small number of exceptional cases relating to the financing of terrorism, money laundering and bribery, business undertakings bear criminal liability only by default: companies may be held criminally liable only where, due to organisational deficiencies in the company, the offence cannot be imputed to any natural person.

For offences committed by natural persons, unless there is a territorial connection with Switzerland, the scope of application of the Swiss Criminal Code (SCC)[120] extends to offences commit-

[116] See http://www.scotusblog.com/case-files/cases/kiobel-v-royal-dutch-petroleum/ and http://www.supremecourt.gov/Search.aspx?FileName=/docketfiles/10-1491.htm.
[117] Brief of the Federal Republic of Germany as Amicus Curiae, p. 12, available on the Internet (see Fn. 117).
[118] Swiss Criminal Procedure Code of 5 October 2007, SR 312.0.
[119] http://www.news.admin.ch/message/index.html?lang=en&msg-id=42300
[120] Swiss Criminal Code, 21 December 1937 (SCC), SR 311.0.

ted abroad only under restrictive conditions, such as that the offender be present on Swiss territory and the offence also be punishable in the country where it was committed.[121] Where natural persons are concerned, this applies, specifically, in cases where the offender or the victim is a Swiss national.

6. Conclusions and recommendations

The commodities industry and, in particular, the merchanting of commodities, has developed into an important sector of the Swiss economy, making an increasingly significant contribution to value added, job creation, and tax revenues. Switzerland is one of the most important commodity trading centres in the world. Commodity trading conducted in a well-organised manner contributes globally to the efficient and sustainable allocation of natural resources.

Switzerland's central role in commodity trading naturally brings with it a number of complex challenges. Given the high degree of mobility characteristic of commodity companies, Switzerland faces increasing international competition in respect of business location, which has become particularly intense not only with certain EU Member States and the USA, but also with Singapore, Dubai and other Asian centres of business. This places Switzerland before the challenge of maintaining and strengthening the features that make it an attractive and reliable place for doing business, including the competitiveness of its tax regime and the efficiency of its financial centres.

At the same time, the commodities industry is also associated with other challenges that must be taken seriously, including the need to respect human rights and environmental standards in resource-exporting countries and the problem of governance deficiencies in many of those countries. These challenges may also bring with them reputational risks both for individual companies and for Switzerland. All of these issues, and the questions tied to them – including those relating to transparency in product and finance flows, and in tax and regulatory matters – must be dealt with in a constructive and sufficiently nuanced manner, within the context of the country's current financial, economic, foreign policy, and development policy objectives. In so doing, the commodity merchanting and resource extraction must be considered as separate activities, even if certain international corporations operate in both. The Federal Council expects of all companies operating in or out of Switzerland to conduct themselves responsibly, and with integrity, in complying with human rights, environmental, and social responsibility standards, both in Switzerland and abroad. It is especially in fragile states where governance is deficient that the population and the economy suffer the consequences of failure to comply with international standards.

As described in the present report, Switzerland does a great deal to guarantee both its competitiveness and its integrity as a centre for conducting business, including the business of commodity merchanting. With the exception of certain initiatives designed specifically for the commodities industry, this is done by creating for companies an overall climate that is conducive to doing business, in keeping with Switzerland's regular practice of not pursuing sectoral economic policies. In addition, Switzerland is today already active in various international bodies that deal with natural resource issues, such as the OECD, the World Bank, the IMF, and the Financial Stability Board, and engages in dialogue with the G20 in order to represent its own interests in an effective and coherent manner. There nevertheless remain areas in which Switzerland's efforts can and should be strengthened. These are addressed in the following recommendations.

Attractiveness as a business location

In connection with the commodities industry, while also taking into account other national objectives, high priority must be given to reinforcing Switzerland's competitiveness at the international level, to ensuring and enhancing market access, increasing resistance to crises, and maintaining the integrity of the financial centres.

[121] See SCC art. 4-7, double punishability, offender not present on Swiss territory, or will not be extradited, etc.

***Recommendation 1**: Switzerland should continue in its efforts to ensure that overall political, economic and legal conditions make it an attractive and reliable location for doing business in all sectors, including the commodities industry. The objective is to maintain Switzerland's prominent position as a competitive, transparent, and socially responsible merchanting centre and to sustainably secure the significant contributions in added value that the commodity companies make to Switzerland's overall economy. In the dialogue with the EU on corporate taxation, a solution should be found that preserves Switzerland's tax competitiveness as a business location, maintains budgetary balance in the cantons and the Confederation, and, at the same time, attains to a higher degree of international acceptance.*

***Recommendation 2:** Switzerland should, as a matter of principle, implement existing multilateral standards for the commodities industry. When introducing its own regulatory provisions, care should be taken to make certain that the measures have been agreed upon multilaterally so that they do not negatively influence overall conditions for companies based in Switzerland, as compared with those in competing business locations. At the international level, Switzerland should work actively both in the drafting and in the implementation of regulatory standards to make certain that they create the conditions for a level playing field worldwide.*

Transparency

In the domain of financial market regulation, the relevant international standards have already been implemented and the requisite reforms have been undertaken. Thus, for example, the reform of the markets for off-exchange traded derivatives – including the commodity derivative markets – will increase the transparency of derivative trading. Switzerland has today already satisfied the majority of the IOSCO Principles for the Regulation and Supervision of Commodity Derivatives Markets. It is neither purposeful nor appropriate for proprietary trading in derivatives by physical commodity dealers to be made subject to the licensing requirement applicable to financial intermediaries.

***Recommendation 3**: With regard to the IOSCO Principles for the Regulation and Supervision of Commodity Derivatives Markets, the FDF, working together with the FINMA, should conduct an analysis as to whether any action is required. Their findings should be taken into account, insofar as possible, as part of the revision of the regime governing off-exchange traded derivatives (OTC derivatives) currently being undertaken. In implementing the reforms of the OTC derivative markets, care should be taken to ensure, insofar as possible, that hedging transactions by commodity traders are not rendered more difficult and that Swiss commodity companies are not prejudiced in their economic interests to any greater extent than their counterparts in the EU or the USA.*

The Federal Council rejects toleration of any inflows into Switzerland of monies obtained in an illicit manner, and has developed a wide range of instruments to prevent such inflows. These include measures for combating (a) money laundering, (b) tax violations, and (c) corruption; (d) and for the repatriation of assets stolen by politically exposed persons. In the fight against money laundering, Switzerland implements international standards, and, in doing so, goes in part further than other countries. Commodity traders, insofar as they also act as financial intermediaries (client traders), are today already subject to the Anti-Money Laundering Act.

***Recommendation 4**: The regime for combating illegal financial flows should be reviewed on a regular basis and, where called for in the face of new risks that may also arise as a result of unlawful gains from commodity dealing, be adapted accordingly. As part of the revision now underway for implementation of the revised FATF recommendations, measures are proposed to further strengthen the regime in place for combating money laundering so that money-laundering abuses within the commodities industry can also be prevented.*

Switzerland considers itself as bound by the principles of fair taxation practices between States. It rejects tax evasion and tax avoidance and participates in the international discussion on tax policies in connection with the issue of base erosion and profit shifting (BEPS).

***Recommendation 5**: Switzerland should actively support the discussion in the OECD on possible ways of curbing tax avoidance and review implementation of the results in Switzerland. In that context, it is also important that fundamental legal principles be respected and that a level playing field in competition in the domains of taxation and subsidies be assured.*

With regard to the issue of transparency in physical commodity trading, the G20 has launched various initiatives, such as the Joint Organisations Data Initiative Oil (JODI Oil), the Agricultural Market Information System (AMIS), and the initiative to improve the functioning of the Oil Price Reporting Agencies.

***Recommendation 6**: The G20 initiatives to increase transparency with regard to prices and quantities in the physical commodities markets should be supported in multilateral forums.*

Improvements in transparency with regard to financial flows from resource extraction companies to governments are to be welcomed. For this reason, Switzerland is an active participant in the Extractive Industries Transparency Initiative (EITI). The advantages of the EITI are, firstly, that the standard is developed jointly by NGOs, companies, and governments, which fosters both its applicability and its sustainability; and, secondly, that more transparency is demanded not only of companies but also of governments. This approach helps, moreover, to ensure a level playing field for all companies operating in competition with each other in the same resource-producing country.

***Recommendation 7**: Switzerland should strengthen its commitment to the Extractive Industries Transparency Initiative (EITI), and actively work to enhance the influence of the EITI. In particular, Switzerland should express its support, in principle, for the proposals for reforming the EITI that are currently being discussed. These relate, among other things, to reporting requirements on financial flows on a project-specific basis and on sales by national oil companies to commodity trading companies (including those domiciled in Switzerland). At the same time, the proposals aim, while taking into account the potential sensitivity of certain business information, to promote the transparency of government contacts through the disclosure of extraction agreements between governments and commodity companies.*

***Recommendation 8:** The consequences of a potential introduction of transparency requierements – similar to those of the USA and the EU – for the Swiss commodity sector should be examined – and the drafting of a consultation draft should be considered. Switzerland should, moreover, advocate internationally a global standard that foresees transparency requirements that are clearly understandable and as similar as possible for all companies active in the extraction of resources.*

International efforts are also underway to increase transparency with regard to product flows. The aim here is to prevent products that have been extracted in breach of human rights or environmental standards, or that are used for the financing of conflicts, from passing into the market supply chain. Thus, for example, Switzerland was in 2003 among the founders of the Kimberley Process, whose objective is to eliminate conflict diamonds from the international diamond trade.

With regard to the gold trade, where, contrary to the situation in the merchanting of other commodities, the gold physically enters Swiss territory, the Federal Council is prepared to consider breaking down the foreign trade statistics on a country-by-country basis in the future. A working group under the direction of the FDF, or, more specifically, of the Federal Customs Administration, will prepare proposals in this regard.

***Recommendation 9**: Switzerland should continue to actively promote international initiatives for increasing the transparency of product flows – such as the OECD Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High-Risk Areas – and should implement the standards adopted. In addition, Switzerland should launch this year, as planned, the "Better Gold Initiative" for the creation of a value chain for the fair and sustainable extraction and trading of gold. Switzerland's foreign gold trade statistics should be broken down on a country-by-country basis in order to increase transparency in this domain. Concrete proposals for the publication of statistics should be worked out by the working group appointed by the FDF.*

Corporate responsibility and government responsibility

Corporate social responsibility is an issue that concerns not only companies in the commodities industry, but all companies and, in particular, multinational corporations. Companies involved in resource extraction nevertheless face special challenges, in that they often operate in unstable regions where the rule of law is weak. In order to promote compliance with human rights and environmental standards, Switzerland supports, among other things, the UN Guiding Principles on Business and Human Rights, the OECD Guidelines for Multinational Enterprises, and the "Voluntary Principles on Security and Human Rights" and is active in efforts to ensure that they are implemented by Switzeralnd, by companies, and by the other States. In implementation of the 2011 update of the OECD Guidelines, the Federal Council is currently in the process of reorganising the National Contact Point (NCP) so as to strengthen its effectiveness among the various stakeholders and within the Federal Administration, and to improve the efficiency of its mediation efforts. In addition, the FDFA and the EAER in 2012 launched a multi-stakeholder dialogue with NGOs, companies, and academic institutions on the implementation of the UN Guiding Principles on Business and Human Rights. At the end of 2012, the National Council then also instructed the Federal Council to prepare a report on a strategy to implement the UN Guiding Principles on Business and Human Rights.

***Recommendation 10**: Switzerland should continue in its commitment to promote corporate social responsibility and intensify the multi-stakeholder dialogue being conducted by the FDFA and the EAER on the UN Guiding Principles on Business and Human Rights. In conformity with Postulate 12.3503, "A Ruggie Strategy for Switzerland", as submitted by von Graffenried, a review of the existing regime should be conducted, the gaps identified, and measures needed for implementation of the UN Guiding Principles defined. Swiss companies should, in keeping with the principles of corporate social responsibility, exercise due diligence with regard to human rights and the environment – particularly when operating in fragile states – and institute measures to minimise risks, contributing thus to the positive image of the companies themselves and of Switzerland as a business location. Switzerland should focus its efforts to implement its state duties and promote corporate responsibilities within bothresource extraction and merchanting.*

***Recommendation 11**: A working group, in cooperation with representatives of the stakeholders involved (specifically, the cantons, as well as companies andNGOs) should prepare proposals for corporate social responsibility standards (including implementation mechanisms) for the commodity merchanting industry. Based on those proposals, consideration should be given to the submission of initiatives and international guidelines – designed, specifically, also to deal with ecological effects – before the appropriate international bodies.*

In keeping with the request of the Foreign Affairs Committee of the National Council (Postulate 12.3980), a comparison of the applicable laws should be undertaken in a report to determine whether and, if yes, in what way, corporate board members in countries comparable to Switzerland are obligated by law to exercise due diligence with regard to human rights and environmental standards in their companies' overseas operations. Based on the results of that comparative study, solutions suitable for Switzerland should be formulated. This should be done in coordination with other countries and international organisations.

***Recommendation 12**: Based on the results of the comparative study of other legal regimes (Foreign Affairs Committee of the National Council, Postulate 12.3980), a review should be conducted to determine whether the international legal environment is such that there is a need for Switzerland to take legislative action.*

Development policy

In addition to the above-mentioned initiatives (EITI, Better Gold), Switzerland, as part of its development cooperation activities, also provides assistance to developing countries and emerging economies in their efforts to improve overall conditions and build governance capacities. This is crucial in order for resource-rich developing countries to be able to better exploit their potential; the efforts undertaken aim, among other things, to strengthen rule of law structures and democratic monitoring mechanisms, to mobilise internal resources, and to promote efficient and effective systems for the administration of public finances.

***Recommendation 13**: Switzerland should continue in its existing bilateral and global commitment to development cooperation and cooperation with Eastern Europe for the promotion of good governance and should intensify its efforts in specific areas, such as those of democratic monitoring mechanisms, government capacity building, and efficient management of resource extraction revenues. This will fundamentally strengthen the abilities of resource-producing countries to reduce such risks as money-laundering, corruption, the flight of capital, and tax avoidance.*

Double taxation agreements and transfer pricing

By means of double taxation agreements (DTAs) and tax information exchange agreements (TIEA) with developing countries and emerging economies, Switzerland contributes to the ability of those countries to take legal action to counter the use of abusive transfer pricing practices. These agreements can assist developing countries in mobilising their internal resources.

***Recommendation 14**: In keeping with the current policy of the Federal Council, the conclusion of TIEAs with developing countries should be taken into consideration, whereby, however, in the presence of economic interests, and for the prevention of double taxation, the conclusion of DTAs is to be given preference. DTAs and TIEAs are fully effective only where the partner country possesses the requisite government capacities.*

Reputational risks

The sizeable economic importance of the commodities industry has also given rise to heightened public interest. One aspect of the public debate are questions concerning the economic and political risks to which Switzerland may be exposed through the presence of a large number of commodity companies on its territory. The measures recommended in this report constitute an important contribution to reducing reputational risks. At the same time, however, Switzerland should work to further enhance its ability to monitor developments in the commodities sector.

***Recommendation 15**: Developments both in the political debate and in the public debate in the media, in Switzerland and abroad, should continue to be monitored so that potential risks to Switzerland's reputation or to its attractiveness as a business location can be recognised early. Specifically, Swiss representations abroad should devote greater attention to the issue in their reports and contribute to the gathering of more detailed information. In addition, measures should be taken to strengthen efforts to inform the public on Switzerland's commitment to preserving the integrity and the competitiveness of the commodities industry here.*

Dialogue with actors outside the Confederation and interdepartmental platform

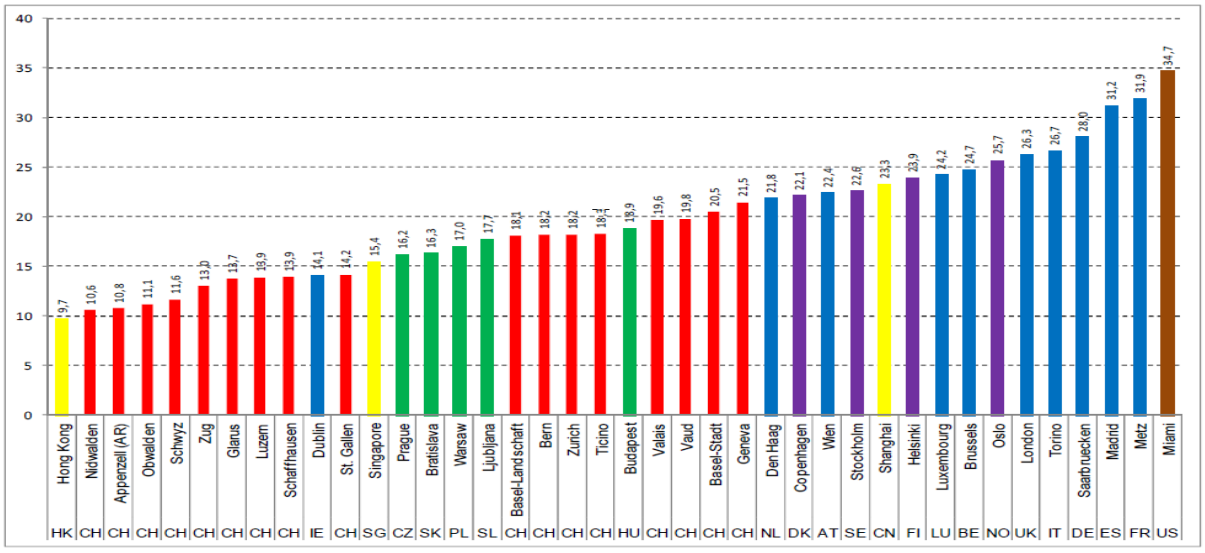
Various federal departments engage in dialogue with the cantons on the one hand and the industry (companies and industry associations) as well as with NGOs on the other, on different aspects of the commodities issue. Within the federal administration, an interdepartmental platform has been created in order to develop the foundations for dealing with natural resource issues. Measures currently being implemented are, for the most part, embedded in projects now being carried out by various federal departments and do not exclusively concern the commodities industry.

***Recommendation 16**: Contacts between the Departments, in their respective domains of responsibility, with the cantons as well as the industry (companies and industry associations) and NGOs, should continue, and be intensified, with the objective of identifying opportunities and risks and discussing common approaches to addressing these issues.*

***Recommendation 17**: The interdepartmental platform on commodities should remain in function in order to assure the proper flow of and concentration of information within the Federal Administration, to monitor and provide early recognition of international and national developments, and to coordinate dialogue with the cantons, the industry, and NGOs. It ensures reporting.*

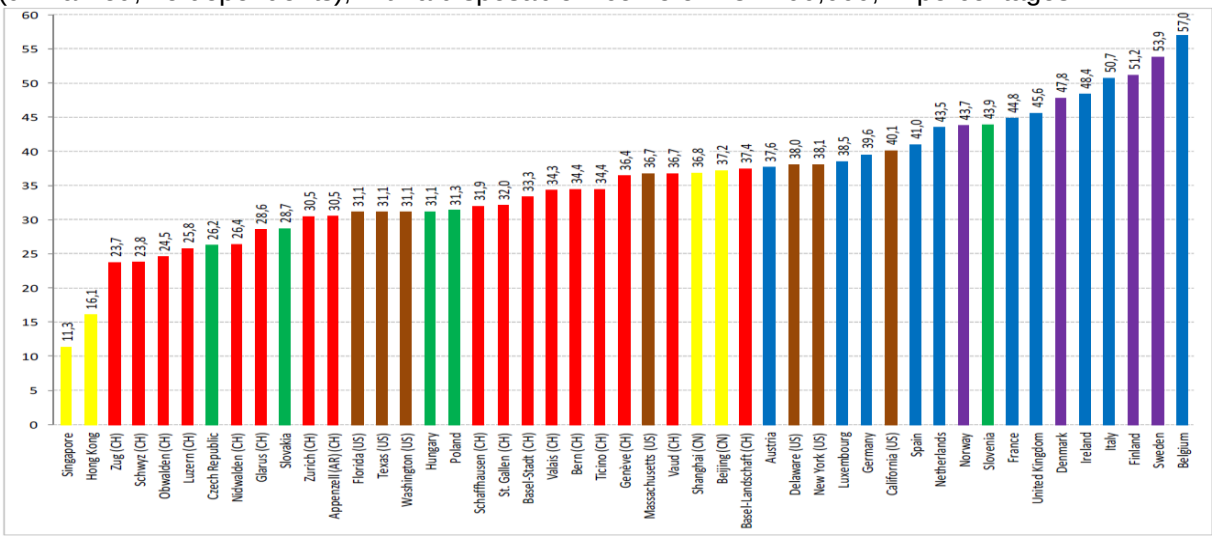
Appendix

Figure A.1: BAK Taxation Index 2011 for companies



Source: ZEW/BAKBASEL, BAK Taxation Index 2011. International Benchmarking Programme (IBP). Basel: BAKBASEL.[122]

Figure A.2: BAK Taxation Index 2011, effective tax rates levied on highly qualified manpower (unmarried, no dependents), with a disposable income of EUR100,000, in percentages.



Source: ZEW/BAKBASEL, BAK Taxation Index 2011. International Benchmarking Programme (IBP). Basel: BAKBASEL.[123]

[122] For Switzerland, the effective tax burden was calculated for the respective cantonal capitals. The other locations shown are the (economic) capitals of the regions considered. Where more than one region within a single country has been considered the average tax burden for the median is shown. The colours of the bars in the graph were assigned by regional grouping: Swiss cantons (red), Eastern Europe (green), Scandinavia (violet), Continental Europe/Ireland/United Kingdom (dark blue), USA (brown), and Asia (yellow).

[123] For Switzerland the effective tax burden was calculated for the respective cantonal capitals; for Belgium, Denmark, Finland, Italy, Norway, and Sweden the calculations were made for the national capitals. The colours of the bars in the graph were assigned by regional grouping: Swiss cantons (red), Eastern Europe (green), Scandinavia (violet), Continental Europe/Ireland/United Kingdom (dark blue), USA (brown), and Asia (yellow).

Appendix 2: Parliamentary requests 2002 – 2012. Source: Curia Vista. Search terms: "natural resources", "commodity market", "commodity agreements", "commodity prices", and "mining" (consulted 31 December 2012)

Reference number	Title	Type	Group	Federal Council stance	Status	Submission date
05.5045	Granite industry in peril	Question time	CVP-EVP		Resolved	14.03.2005
07.3465	More price transparency for food products	Motion	SVP	Rejected	Rejected - Resolved	21.06.2007
08.3270	Food crisis, commodity and natural resource shortages	Postulate	CVP-EVP	Approved	Accepted - Referred	29.05.2008
08.3310	Food staples in financial vehicles	Postulate	CVP-EVP	Approved	Accepted - Referred	11.06.2008
08.3387	Speculation excesses in the finance industry	Interpellation	CVP-EVP		Resolved	12.06.2008
09.3819	Resource shortages. Better regulation of commodity futures markets	Interpellation	Green		Resolved	23.09.2009
10.5451	Swiss chocolate without child labour	Question time	SP		Resolved	27.09.2010
10.3736	Agriculture and the cost of living in Switzerland	Interpellation	SVP		Resolved	29.09.2010
11.3343	Uranium import declaration requirement	Motion	Green	Rejected	Rejected - Resolved	12.04.2011
11.5261	Who profits from Glencore?	Question time	SP		Resolved	07.06.2011
11.3585	Security of supply with regard to rare metals	Interpellation	CVP-EVP		Resolved	16.06.2011
11.3803	Switzerland's role as country of domicile to commodity trading companies	Postulate	SP	Approved	Rejected - Resolved	21.09.2011
11.3840	Regulate commodity merchanting companies	Motion	Green	Rejected	Not yet taken up in plenary	26.09.2011
11.3859	Country-by-country financial reporting. Switzerland a regulatory oasis?	Interpellation	SP		Not yet taken up in plenary	28.09.2011
11.3905	Securing natural resource supplies for Swiss industry	Interpellation	SVP		Resolved	29.09.2011
11.3929	Securing natural resource supplies for Swiss industry	Interpellation	SVP		Resolved	29.09.2011
11.4161	No money laundering in proprietary commodity trading	Motion	SP	Rejected	Not yet taken up in plenary	23.12.2011

12.5093	Preserve Swiss agricultural production volume	Question time	SVP		Resolved	06.03.2012
12.3138	Dubious practices in awarding of mining licences in the Congo. The role of Glencore and the IMF	Interpellation	SP		Not yet taken up in plenary	13.03.2012
12.5184	More transparency regarding financial flows in international commodity trading	Question time	CVP-EVP		Resolved	30.05.2012
12.5194	Peru and Xstrata. Independent monitoring	Question time	SP		Resolved	30.05.2012
12.5195	Peru and Xstrata. Social unrest	Question time	SP		Resolved	30.05.2012
12.5201	Killing of demonstrators in Peru. Switzerland's shared responsibility	Question time	Green		Resolved	30.05.2012
12.5208	Change in Xstrata's stance in Peru	Question time	Green		Resolved	30.05.2012
12.3442	Import and export of gold. Disclosure of statistics	Interpellation	SP		Resolved	06.06.2012
12.3449	Corporate social responsibility of international companies domiciled in Switzerland	Interpellation	CVP-EVP		Not yet taken up in plenary	07.06.2012
12.3475	Rare earth metals. Natural resource strategy	Postulate	CVP-EVP	Approved	Accepted - Referred	12.06.2012
12.3499	Human rights violations by foreign subsidiaries of Swiss companies. Access of victims to justice	Interpellation	CVP-EVP		Resolved	13.06.2012
12.3517	Violations of human rights and environmental standards by subsidiaries of multinational corporations	Interpellation	SP		Not yet taken up in plenary	13.06.2012
12.444	Insider trading rules also for currency and commodity markets	Parliamentary initiative	SVP		Not yet taken up in plenary	14.06.2012
12.3627	Extractive Industries Transparency Initiative (EITI): Switzerland's position in the strategy review process	Interpellation	Green		Not yet taken up in plenary	15.06.2012
12.3741	Due diligence for commodities from conflict and high-risk zones	Interpellation	SP		Not yet taken up in plenary	20.09.2012
12.3773	Transparency in payment flows of commodity companies	Motion	SP	Rejected	Not yet taken up in plenary	24.09.2012
12.3805	Investments in the large-scale exploitation of land and water resources in developing countries	Interpellation	SP		Not yet taken up in plenary	26.09.2012
12.3862	Coherency in economic sanctions?	Interpellation	SP		Not yet taken up in plenary	27.09.2012

12.3904	Measures against corporate impunity for human rights violations and environmental damage	Interpellation	SP		Not yet taken up in plenary	30.09.2012
12.5510	Corruption scandal in Nigeria. Reputational damage for Switzerland?	Question time	SP		Resolved	05.12.2012
12.1119	Tax conditions for commmodity companies	Question	SP		Resolved	13.12.2012