

AGAINST THE TIDE

The Swiss case in favour of high
denomination banknotes

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Cash Essentials

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In the age of cash restrictions, Switzerland defies the trend issuing a new 1,000 note

General

On March 5th 2019, Switzerland presented a new version of one of the world's most valuable banknotes, to be issued on March 13th: the CHF1,000 (worth approximately US\$993)¹. This news should allow us a moment to delve deeper into the topic of cash restrictions in general, and the issuance of high denominations in particular, as it is also an inherently public debate and should concern citizens worldwide.

In 2018, the Swiss National Bank published its first ever report on consumer payment behaviour to better understand the hierarchy of payment methods as well as citizens' preferences for the different denominations (Swiss francs 10s, 20s, 50s, 100s, 200s and 1,000 franc notes). Surprisingly, the 1,000 note is still widely used, albeit less popular than other denominations. Prior to making any further judgement, it must be understood that the Swiss system is quite unique when it comes to payments for utility bills, for example. Although online banking is increasingly adopted by Swiss citizens, payments are traditionally carried out via a system of payment slips that are settled in person at any Swiss Post office – and they're most frequently paid in cash. By far, the most popular denominations in Switzerland are the 10 CHF and the 20 CHF, but 44% of survey participants confirmed having possessed at least one CHF 1,000 note in the past two years, a figure that jumps to 66% for the CHF 200. High denominations still circulate, albeit less frequently than smaller denominations.

Swiss francs are not only used by Swiss nationals. The Swiss franc is an attractive currency for investors thanks to its stability, value and elevated security (one of the hardest to counterfeit) hence it frequently leaves Swiss soil. In the report "The demand for Swiss banknotes: some new evidence" carried out by Assenmacher, Seitz and Tenhofen they found that hoarding of larger denominations was

¹ Singapore previously held the highest denomination note – the \$10,000 which was worth around US\$7,400 – until it ceased to be printed in 2014. However, it is still legal tender and in circulation.

greatly affected by different financial crises over the decades, with peaks recorded around the break-up of the Bretton Woods system, the turn of the millennium as well as the financial and euro crises². These findings point to a usage of cash beyond the simple day-to-day spending and support the argument that there is an inherent variable to cash – financial security – that other payment methods have yet to equal, particularly in times of political or financial instability, low interest rates or natural disasters.

Government trending: the race again high denominations

The recurring argument against high denomination banknotes is their perceived value for criminals - almost €6 million-worth of €500 notes fit into a briefcase, whereas "only" \$2 million USD-worth of \$100 bills would - but an official report proving the link between criminality and cash has yet to see the light of day. To date, all statements are based on assumptions and perceptions of criminality. Indeed, as Larry White, senior fellow at the Cato Institute and professor of economics at George Mason University stated, "Nobody really knows the shares of stock of large bills held by non-criminal hoarders"³. It can therefore be deduced that nobody really knows how many large bills are held by criminals either. As former head of Interpol and the Swedish Police, Björn Eriksson, once said "Little has been said about the major challenges that a cashless society brings. It infringes on people's privacy. It can make life difficult in sparsely populated areas. It can make a society vulnerable and increasingly open to sophisticated Internet crimes."⁴

² Assenmacher, Katrin; Franz Seitz and Jönr Tenhofen. „The demand for Swiss banknotes: some new evidence“. August 31, 2018.

³ White, Larry. More Evidence of the High Collateral Damage of the War on Cash. January 28, 2018. Accessed online at: <https://www.alt-m.org/2018/01/26/more-evidence-of-the-high-collateral-damage-of-a-war-on-cash/>

⁴ White, Larry. More Evidence of the High Collateral Damage of the War on Cash. January 28, 2018. Accessed online at: <https://www.alt-m.org/2018/01/26/more-evidence-of-the-high-collateral-damage-of-a-war-on-cash/>

A vocal supporter of the CHF, 1,000 former President of the Swiss National Bank, Jean-Pierre Roth suggests that “the decision to stop issuing high-denomination banknotes will receive the blessing of well-meaning souls but it will fail to meet its objective of fighting efficiently against criminality and will have negative side effects.” Similar to Professor of Criminology and Criminal Justice Nikos Passas’ analysis of cash usage and the shadow economy, that we will see later, Roth believes that dropping high denomination banknotes will only shift the problem elsewhere, at a higher cost, while depriving citizens of a very tangible store of value and reassuring tool in times of crisis. Even the most popular anti-cash advocate, Harvard Professor Kenneth Rogoff, diluted his initial discourse to a milder version of less-cash vs cashless in a video for the Centre for Economic Policy Research (CEPR)⁵ stating that “You’re not going to eliminate tax evasion, you’re not going to eliminate crime” he argues, “but you’re going to cut both of them by several percent.”

On June 12th, 2018, the EU itself announced that it will not impose any cash restrictions following a two-year consultation on the issue. Indeed, in their report “On restrictions on payments in cash”⁶ concludes that:

- Limiting the use of cash would not prevent terrorism financing
- Europeans would consider any EU-level restrictions as a breach of their personal freedom (94.94% respondents said so)
- The heterogeneous nature of current restrictions at the national level have a negative impact on the internal market
- Restrictions could eventually be useful in combatting money laundering, although “the impact of a cash restriction on money laundering in general, cannot be precisely quantified” (p.6)
- If some of the most cash-heavy countries, with the most lenient cash usage policies are also those that have the smallest shadow economies, how does the argument stand that accessibility to high

denominations is a vehicle for tax evasion and crime?⁷

The different facets of restrictions

Cash restrictions can come in many shapes and forms. They can be government-imposed, or simply a result of private sector practices. They can be carried out as a formal refusal to accept cash or they can be part of a legislation limiting payments in cash to a ceiling amount. The central bank can also play a role by deciding to phase out a given denomination or – more radically – by demonetizing one or more of its notes. For government-imposed restrictions, the main reasoning is the war on money laundering, tax evasion and crime. For the private sector, the main pretext is employee security (or employer security against employee theft?) and cash logistics, but one can speculate that the greatest motivators are loyalty programmes and consumer data collection.

Private sector-imposed restrictions have become more common with growing adoption rates of alternative payment methods by consumers. The most blatant example being Amazon Go’s cashless and cashier-less stores, but it includes the appearance of card-only stores worldwide. Frictionless shopping is portrayed as modern and trendy, but it is far from being a reality for the majority – a situation which has led a number of politicians to react. Initiatives to fight back these questionably legal practices have been popping up left, right and centre, particularly in the United States (i.e. New York⁸, Washington D.C.⁹ and New Jersey¹⁰) but also in China¹¹, where politicians are calling the cashless trend elitist and discriminatory against minorities, the unbanked and the elderly. Others are sounding the alarm in

⁷ CashEssentials. EU will not impose restrictions on cash. June 18, 2018. Accessed online at: <https://cashesentials.org/publication/eu-will-not-impose-restrictions-on-cash/>

⁸ Djakovic, Viktoria. Equal Opportunities for all, through cash. CashEssentials, January 9, 2018. Accessed online at: <https://cashesentials.org/equal-opportunities-for-all-through-cash/>

⁹ CashEssentials. Discriminatory Bill Causes Dilemma in Washington D.C. September 14, 2018. Accessed online at: <https://cashesentials.org/news/discriminatory-bill-causes-dilemma-in-washington-d-c/>

¹⁰ CashEssentials. Amazon and Walmart Delay Cashless Retailers’ Bill in New Jersey. October 12, 2018. Accessed online at: <https://cashesentials.org/news/amazon-and-walmart-delay-cashless-retailers-bill-in-new-jersey/>

¹¹ CashEssentials. China Joins Fight Against Cash Discrimination. January 23, 2018. Accessed online at: <https://cashesentials.org/news/china-joins-fight-against-cash-discrimination/>

⁵ VoxEU on Twitter featuring an interview with Kenneth Rogoff. Accessible here: <https://twitter.com/voxeu/status/932960464941797376>

⁶ European Commission. “Report from the Commission to the European Parliament and the Council on restrictions on payments in cash”. Brussels, June 12, 2019. Accessed online at: https://cashesentials.org/app/uploads/2018/07/2018_june_ec_report_from_ec_to_parliament.pdf

regards to cash accessibility in general, which could also be considered as an indirect form of restriction, the most recent example being the UK.

Following LINK's decision to lower interchange fees and the subsequent closures of bank branches and ATMs across the UK – at a rate of 488 per month only between June 2018 and December 2018¹² - the UK's Treasury Committee is calling for "urgent action to prevent the collapse of access to cash". Chair of the Committee Nicky Morgan, stated that "with the way that people access their cash seemingly on the precipice of collapsing, the Government can't just bury its head in the sand. This mustn't fall through the gaps of responsibility". She proceeds to say that the chair of the Payment Systems Regulator, Charles Randall suggested that "there is a serious discussion to be had this year about whether access to such a basic financial service should be universal, or commercially driven."¹³

But the private sector can only take part of the blame. Despite cash being a public good, governments are at the forefront of restrictions, cash having been for long associated to most of society's greatest evils - as if getting rid of images of dead presidents, politicians or national landmarks will eventually wipe criminal souls' clean. To date, no cash limitation policy is based on hard data confirming (or not) its effectiveness against crime. Indeed, quite the opposite appears to be true as there seems to be no correlation between the size of the shadow economy and the adoption of restrictions. "Austria, which has the smallest shadow economy in Europe imposes no restrictions, whereas Bulgaria which has the largest, has set a cap of just over € 5,000"¹⁴. A Deutsche Bank report went even as far to state that "abolishing cash will not eliminate profit-driven crime"¹⁵. On the contrary, as "payments go digital [and] fraud

12 Finextra. The numbers don't add up: universal provision of access to cash called into question. February 14, 2019. Accessed online at: <https://www.finextra.com/news-article/33386/the-numbers-dont-add-up-universal-provision-of-access-to-cash-called-into-question>

13 *ibid*.

14 Lepecq, Guillaume. Three questions about cash restrictions. CashEssentials, July 11, 2016. Accessed online at: <https://cashessentials.org/three-questions-about-cash-restrictions/>

15 Deutsche Bank Research. "Cash, Freedom and Crime". November 23, 2016. Accessed online at: https://www.dbresearch.com/PROD/RPS_EN-PROD/PROD0000000000441785/Cash%2C_freedom_and_crime%3A_Use_and_impact_of_cash_in.PDF

follows. An (almost) cashless Sweden sees card fraud rising" states the report. Cash-intensive economies like Germany and Austria are those with the smallest shadow economies, while Sweden is a low-cash country with a relatively high shadow economy.¹⁶ An argument that is supported by Nikos Passas who wrote for the Journal of Financial Crime that "countries with high denomination notes are low on crime and organized crime (e.g. Japan, Singapore, Switzerland or UAE), while crimes with very low denominations are high on crime (e.g. Brazil, Nigeria, South Africa or Venezuela)"¹⁷.

There are cases where cash restrictions are imposed without a proper upstream assessment of the possible implications which can lead to absurd situations, like in the case of the Bedouin tax evader in Israel¹⁸. Unable to settle the fine to the Tax Authority because the payment – in cash - exceeded the newly imposed ceiling, the defendant found himself risking a two-month jail sentence if unable to pay his dues - a situation which could have been easily settled with a bank transfer, only that the defendant's bank account had already been blocked by the Tax Authority itself.

The last two types of government-imposed restrictions are the phasing out of high denomination banknotes – as in the case of the €500 which will cease to be issued by April 2019 – or full demonetization, as in the Indian case in November of 2016. For the latter example, it is worth noting that the two most popular notes, the Rs 500 and the Rs 1,000, were initially replaced by two other notes, including an even higher denomination – a new Rs 500 and a Rs 2,000 – but the 2,000 Rs is no longer printed (although still legal tender) and could be phased out someday.

In regards to the Eurozone's largest denomination, it is interesting to observe that, once again, the decision to phase it out was not based on any conclusive data presenting criminals as the biggest users of the €500 note, but was rather based on the assumption that it is the most convenient of notes for

16 Lepecq, Guillaume. Less Cash, More Fraud. January 4, 2017. Accessed online at: <https://cashessentials.org/news/less-cash-more-fraud/>

17 Passas, Nikos. "Report on the debate regarding EU cash payment limitations" (Emerald Publishing Limited: Vol. 25. Issue 1; p.20). Accessible online at: <https://www.emeraldinsight.com/doi/full/10.1108/JFC-06-2017-0058>

18 Fein, Mordechai. New Cash Law Sparks Panic in Israel. February 2019. Accessed online at: <https://cashessentials.org/new-cash-law-sparks-panic-in-israel/>

carrying out crimes. It is only following the tragedies that shook the European continent since the 2015 terrorist attacks in Paris that it was observed that terrorists use other means – sometimes fully legal and visible – to fund their activities and move capital. Unfortunately, the conclusions of the MEPs Foreign Affairs Committee probably came too late to offer a good counter-argument against the phasing out of the €500. Indeed, the Committee's non-legislative resolution for the fight against terrorism¹⁹ offers a number of recommendations – and none ever mention cash. On the contrary, the MEPs agree that to cripple terrorist activities, what is most effective is monitoring pre-paid debit card activities, improving scrutiny of large transferred sums in traditional cultural contexts and studying the use of cryptocurrencies and other fintech technologies, to name a few.

The Indian case is arguably the most telling of all. Prime Minister Narendra Modi's overnight decision to scrap the most popular denominations, the Rs 500 and Rs 1,000, in November 2016, brought the economy to its knees and caused unfathomable hardship to millions of citizens, especially the poor. Driven by a feverish desire to corner tax evaders and fill the state's coffers, the conclusions of this risky gamble were beyond catastrophic. The proportion of "black money" believed to be circulating in the economy was disappointingly low. Indeed, the Reserve Bank of India confirmed that 99.3% of banned notes were exchanged for new ones²⁰, questioning the very foundation of the fight against corruption. What did occur however, was a drop in economic growth – which slumped to 5.6% in April-June 2017 compared to 7.9% in for the same period in 2016. "More than 100 lives were lost in the panic to exchange the notes. Millions of daily-wage earners missed their livelihoods and thousands of small businesses were closed. About a year of economic growth was lost."²¹ And in the midst of this crusade against corruption and the desire to impose

19 European Parliament. MEPs propose ways to cut cash flows to terrorists. February 21, 2018. Accessed online at: <http://www.europarl.europa.eu/news/en/press-room/20180220IPR98216/meps-propose-ways-to-cut-cash-flows-to-terrorists>

20 Reserve Bank of India. "Annual Report". Year 2018. Accessed online at: <https://rbi.org.in/Scripts/AnnualReportPublications.aspx?year=2018>

21 CashEssentials. Indian currency gamble was "A failure of epic proportions". October 17, 2018. Accessed online at: <https://cashesentials.org/news/indian-currency-gamble-was-a-failure-of-epic-proportions/>

the use of digital payments, Indians defiantly demonstrated their preference for cash, whose usage grew to exceed pre-demonetization levels²².

Public good or public foe?

Cash is a tool used for payments, and like any tool, its use is dictated by the user and not by the tool itself. Although cash doesn't have a conscious, it is often portrayed as the evildoer by its critics who fail to see cash as is and not as how they perceive it to be. Even the most innocent of tools – a coffee mug or a pencil – can become a weapon and partner-in-crime. Yet, does their potential use make them something that must be eradicated or removed from public use?

The Swiss have made a conscious decision to re-issue one of the world's highest denomination notes with the new series. This choice was made based on data pointing to a real demand. Of course, one can argue that the users of such high value currency might be motivated by dubious activities, but we have seen above that Switzerland is also one of the countries with the smallest shadow economies together with other cash-heavy nations like Germany, Austria, Singapore and Japan. It shouldn't be forgotten that some of the most damaging and far-reaching criminal schemes in the past few years were in fact carried out either through legitimate financial institutions or with the use of cryptocurrencies. As Chris Skinner mentions in his blog Finanser, "2.7% of the world's GDP that is lost to illicit financial flows. That estimate grows to 3.6% when tax evasion is included in the mix." In fact, less than 1% of the \$1.6 trillion of laundered money worldwide is caught by the financial system. Some examples include the 2008 Deutsche Bank scandal saw \$462 million miraculously disappear from the books²³, the SWIFT cyberattacks that affected numerous banks, including the central bank of Bangladesh that lost \$101 million, and the giant money-laundering affair between 2010-2014 where \$20 billion were moved out of Russian and processed in Europe through a number of British banks, including the Royal Bank of

22 Bhaka, Pratik. Cash addiction is hard to break, ATM withdrawals up 22% in April. Economic Times of India, June 20, 2018. Accessed online at: <https://tech.economic-times.indiatimes.com/news/corporate/cash-addiction-is-hard-to-break-atm-withdrawals-up-22-in-april/64658250>

23 Silver, Vernon and Elisa Martinuzzi. How Deutsche Bank made a \$462 million loss disappear. Bloomberg, January 19, 2017. Accessed online at: <https://www.bloomberg.com/news/features/2017-01-19/how-deutsche-bank-made-367-million-disappear>

Scotland, HSBC, Coutts or Lloyds, as well as US and Russian banks²⁴. One can hardly imagine what it would mean to carry 40 tonnes worth of €500 notes from Russia to the UK...

Switzerland has chosen to go against the tide and maintain its full spectrum of denominations. This might make it an easy target for criticism, yet it's the only government that has based its decision on real demand – and not on presumptions. Indeed, it has seen that cash limitations have done little or nothing to curb terrorism financing (i.e. the EU) or tax evasion (i.e. India) other than, arguably, make these illicit transactions even harder to uncover. Cash is not only a tool for payments, it is also an important player in the wider payments landscape as it acts like a benchmark and maintains a healthy competition between payment methods. And finally, cash offers an island of security in situations of crisis – such as natural disasters or cyberattacks - so it could as well be that Switzerland is being faithful to its cautious self and is simply deploying a wider risk management strategy to avoid having all its eggs in one basket.

²⁴ Harding, Luke, Nick Hopkins and Caelainn Barr. British banks handled vast sums of laundered Russian money. The Guardian, March 20, 2017. Accessed online at: <https://www.theguardian.com/world/2017/mar/20/british-banks-handled-vast-sums-of-laundered-russian-money>