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Financial Fraud

How a couple lost a fortune in an alleged Swiss banking fraud

$22mn case exposes the risks in opaque world of Zürich's independent wealth advisers

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Gabriele Gallotti, a Swiss-Italian private banker, says: 'It might take another big scandal for things to change'

The couple came into the hotel lobby tanned and laden with their beach bags. Funny how Gregory and Vera Mirlas were almost always early to every appointment, even here on the Riviera, their young friend joked, as he embraced the couple at their rendezvous in the chic French resort of Juan-les-Pins.

They strolled in the September heat across the town square, past the Parc de la Pinède, for lunch at their favourite restaurant, Le Perroquet. The couple ordered lamb, as usual. Their friend went for grilled fish and a glass of rosé. They lapsed into gentle conversation, reminiscing and catching up.

But when the Mirlases began to tell their friend — a Goldman Sachs banker — about what had been happening with their savings, he began to worry. Something sounded completely wrong, he recalls. "I left lunch worrying about them. And I got straight in touch with people I knew at their bank in Switzerland to try and set up a meeting to work out what had happened."

The Mirlases soon discovered they had been victims of an alleged fraud that took place under their noses and that of their bank, Julius Baer — one of Switzerland's most prominent private lenders. Four years later, they are still fighting for their money back in the courts.

Theirs is not an isolated case.

A safe haven?

In Switzerland, the characteristics that have made the country such a haven for the rich to safely store their money — its secrecy, its deep conservatism and its stolid, inflexible institutions — can also sometimes turn into nightmarish liabilities when things go wrong. Banks refuse to back down or admit mistakes. Lawyers will not work against the banks that otherwise keep the Swiss legal profession so well remunerated. And regulators are too weak to act.

The Mirlases' names have been changed in this article at the couple's request. They said they feared becoming pariahs in Zürich's tightly knit social scene, in which bankers dominate and critical outsiders can find themselves shunned for disrupting the status quo. In line with Swiss convention regarding defendants in criminal proceedings, the FT is also not publishing the full name of Benjamin G, their Swiss wealth adviser whom they accuse of fraud.

Gregory and Vera left the Soviet Union shortly before its collapse in November 1990. They took no luggage and had just US$495 in cash. The decision to leave came quickly after the emigration law was liberalised under glasnost.

They had been motivated by, the issues afflicting all Soviet citizens: the lack of freedom, the economic malaise and the rampant hypocrisy. But there was also, for the Jewish Mirlases, discrimination, says Gregory, who had worked as a mining engineer.

They arrived in Israel without a clear idea of their future — and got off to a bad start when they got lost on their first evening trying to find their way to the beach. But they had a stroke of luck. They ran into Kobi Richter, his wife and son, who were sitting in their car and offered them a lift.

Through the Richters, the Mirlases got their break. Gregory had found a job working at a medical start-up, developing stents. The work was a far cry from his experience, but the new problems tested his skills. It didn't last. After refusing to work outrageously long hours, Gregory was fired. Richter suggested Gregory simply set up his own company. The two founded Medinol that year.

The stents Gregory designed — at first making prototypes on wooden jigs at home — went on to become so successful that they remain the industry standard to this day. And they made the Mirlases (and the Richters) extremely rich.

In 1998, changes in Israeli law allowed citizens to legally keep their savings with foreign banks. For the Mirlases and their newfound millions, the question of where to do so seemed obvious: throughout their lives in the USSR, Switzerland and its banks had always held a particular place in the popular imagination, Gregory recalls. Nowhere could be safer.

When the Mirlases first met Benjamin G, he was employed by the Swiss arm of Britain's Lloyds Banking Group. He came with a recommendation from the Richters, and quickly proved helpful. He told the Mirlases he could get them Swiss work permits so they could move and work in a cooler climate. And he did.

Switzerland and its banks had always held a place in the popular imagination

In 2001, Benjamin left Lloyds to join Julius Baer, one of Switzerland's oldest private banks, and at the time still controlled by the Baer family of Zurich. He took the Mirlases with him.

Baer was changing fast, however. Soon, the Baer family would relinquish control and, as the bank moved to a Swiss exchange listing in an era of booming markets, it would join the advance guard of old Swiss institutions chasing the newly rich and their assets all over the world.

It was a time of huge opportunities, but also of pitfalls. Institutions that for decades had relied on trusted employees brought up in a conservative Swiss milieu now found themselves employing fresh, young and hungry bankers.

The new guard

A new layer of middlemen emerged in Switzerland between banks and their clients. Initially, there was a logic to this. Swiss banks had begun to earn a reputation for pushing their own, sometimes unsuitable, in-house products to rich clients, rather than shopping around in the marketplace. The idea of a wealthy family signing up with an independent adviser, therefore, who could direct their investments to the right banks, made sense. In reality, however, the market was plagued with problems.

Swiss wealth advisers were almost always former bankers who had worked out that, if they could take five or so big clients with them, the advisory fees they could earn would be far more than their previous bonuses.

What's more, if their old banks — full of their old buddies — could perhaps pay a fee, then maybe they could direct their clients' investments back to that bank anyway.

This phenomenon became an almost institutionalised part of the Swiss wealth advisory world. The Swiss call such payments "retrocessions".

While such payments exist elsewhere in the global asset management industry, in Switzerland they are not only more widespread, but also much larger — and, until just two years ago, they were completely secret.

The law in Switzerland now requires full disclosure of such payments, under the Swiss Financial Services Act of 2020 (FinSA) which came into force in January 2022. Financial advisers must also obtain a licence from the market regulator, Finma. It is a step change for a financial ecosystem that was, until then, largely ungoverned.

So far, Finma, has approved 950 firms (advising on SFr175bn, or $193bn, of assets) out of just under 1,750 advisory firms that have applied for licences.

"The new regulation protects clients much more," says Nicole Curti, president of the Alliance of Swiss Wealth Managers and chief executive of Capital Y. "Before the new law, you could have been a hairdresser with a lot of wealthy clients and you could one day say you were going to be a wealth adviser and just do it."

She adds: "Independent wealth advisers in Switzerland now face the same constraints in terms of KYC [know your customer], transaction checking, internal audit and so on as the banks — which was not the case before."

Curti says adviser numbers are growing and will continue to rise — particularly as traditional private banks, faced with shrinking margins, cutback on attending to niche needs.

Others in the industry, however, are less positive about the new law.

Gabriele Gallotti is a Swiss-Italian private banker who has no relationship with the Mirlases. He left US bank JPMorgan to set up his own (licensed) advisory boutique, Novum, which manages just over SFr3bn. While FinSA has been a welcome change, he says, it has definitely not led to an automatic alignment of wealth advisers' interests with those of their clients.

Gallotti suggests that, If he followed the current Swiss industry standards that he sees at many licensed peer organisations, then Novum could probably triple its bottom line. He reels off examples of abuse. In September last year, a wealthy individual came to Gallotti with a question: how was his existing portfolio, managed by a prominent wealth adviser, down 2 per cent over the past five years, in a bull market?

Gallotti checked. In the eight months prior, he discovered that SFr60mn of the portfolio, about a third, had been invested solely in structured products with one bank. The volume of those products traded during that period was SFr1.5bn. In other words, the wealth adviser had been massively churning the portfolio and earning himself [or herself], and the bank they were working with, huge commissions.

In another recent example, Gallotti recounts the story of a senior international consultant with a strangely lacklustre portfolio. It turned out that they had been sold a high-fee structured product with an upside linked to an index performance. What they hadn't been told was that the fund tracking the index would have its dividends stripped out for the bank to keep.

In a third case — which, says Gallotti, shows the limitation of the new FinSA rules — members of a rich Italian family showed him their accounts with a wealth adviser in the canton of Ticino. The adviser had promised them minuscule fees — just €2,000 annually. But, in the reams of small print, it turned out they had completely waived their right to be told about the retrocessions the adviser might get from banks.

Gallotti says: "The misalignment of advisers with client interests here is systemic, and, well, if you find a client who is not very financially literate, a client who doesn't constantly check up on what is going on, a guy who doesn't know where to look, then it's the perfect set-up for advisers to screw their clients and overcharge, and for the banks they work with to enjoy the ride."

In 2006, Gregory decided it was time to take a stepback. Richter bought out his share of Medinol, and Gregory gave a large chunk of the proceeds to his friend Benjamin to manage. Gregory and Vera deposited $38mn at Julius Baer.

In 2010, Benjamin told the couple he was leaving Baer to set up as an independent wealth adviser at Constanza, an obscure wealth advisory partnership in the ultra-low tax canton of Schwyz, which he told them was effectively a daughter company of the bank.

The Mirlases let him take their money with him and he ran it freely for a decade.

Taken advantage of

On 8 October 2019, a month after they had met on the Côte d'Azur, the Mirlases sat down with their Goldman banker friend, at the opulent headquarters of Julius Baer, all polished wood inside, with recessed lighting, and sleek, uniformed service staff gliding between soundproofed meeting rooms.

Although Benjamin had not worked at the bank for years, Julius Baer was still used by him at Constanza to keep custody of the Mirlases' money. As custodian, the bank's role was to hold the assets, but it had no say in how they were invested, or spent.

The Mirlases' banker presented a file containing their latest account details.

Within a few minutes, it became clear there was a significant difference between what the Mirlases thought they had saved with the bank and what they actually had.

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Gabriele Gallotti

Unknown to them until that point, it appeared that Benjamin had been both giving and loaning himself huge amounts of money from their account, according to criminal proceedings later filed against him, and his own admissions in police interrogations.

The bank, in accordance with the power of attorney Benjamin had presented it with, had followed every instruction he had given it.

The Mirlases were shocked. Gregory studiously scribbled notes, perhaps hoping in doing so not to have to confront the enormity of what they were hearing.

"Benjamin had been like a son to us," the couple later said. They spent weekends together, time in each others' homes. "It was humiliating, and very painful to think that all the time, we had been taken advantage of," says Vera.

The alleged theft began as far back as 2009, when Benjamin was still working at Julius Baer. But it allegedly ramped up after he became an independent wealth adviser. In 2011, he decided to become a partner in Constanza, and used SFr4mn of the Mirlases' own money to buy into the business, by acquiring his stake from a Russian businessman.

Over the course of a decade, the Mirlases believe Benjamin secretly misappropriated around SFr22mn of their assets. He allegedly passed them doctored Julius Baer statements, stripped of detail, which appeared to show their assets growing. He kept the full accounts, which Julius Baer had dutifully agreed to send to him alone, from them.

The Mirlases allege that a luxury house Benjamin bought himself in Zürich's most exclusive enclave, the lakeside suburb of Herrliberg, was at least partially paid for with their money. He also acquired an apartment on the Italian lakes, and a SFr1.5mn yacht using their savings, they say.

For the past four years, to no effect so far, the couple have tried to get some of the money stolen from them back. What has shocked them above all, they say, is Julius Baer's complete unwillingness to take any responsibility for what happened.

"They saw every transaction he made," says Gregory.

Julius Baer says, in response to questions about the Mirlas case, that it never comments on private client matters (under Swiss law, it is a criminal offence to do so).

Earlier this year, Benjamin was indicted on charges of embezzlement by Zürich's cantonal prosecutor. Shortly before this article went to print, in early October, he was found guilty and sentenced to three years in prison, 18 months to be served and 18 months suspended. He was ordered to pay the Mirlases more than SFr13mn back, as well as SFr4mn to the state.

In the interrogation files the police submitted to the court, seen by the FT, Benjamin admitted he had taken the Mirlases money to fund his personal lifestyle, but said that it had been his intention to pay it back. He has also said that several millions of Swiss francs he took were intended for legitimate investment opportunities of the kind the Mirlases had long entrusted him to undertake.

Benjamin's lawyer said he would appeal the verdict. "Our client rejects [the] allegations and is fully committed to fight them in all instances," they said. The Mirlases were "aware and duly informed" of the transactions Benjamin made on their behalf, the lawyer added.

As well as the criminal case against Benjamin, the Mirlases are suing him in the civil courts and have opened a case for damages against Julius Baer. They have also filed a complaint with Finma, the regulator, asking it to look into the bank for breaches of compliance and facilitating money laundering. Finma has not declared whether it will pursue the case.

What has shocked them above all is Julius Baer's unwillingness to take any responsibility

A senior lawyer who works for a private bank in Zurich says that, although egregious, the situation was hardly novel: it is widespread practice in Switzerland that independent wealth managers are given full power of attorney by clients.

"We have clients where, basically, the authorised representatives, their financial advisers, do things like go and buy an expensive watch or whatever, and if we say, 'No, don't do that', we will hear something back asking us why on earth we are making a fuss . . . They say they have given these people these powers, and it's not up to us to decide what is reasonable or not."

What's more, the same lawyer notes, if a bank is only being paid relatively small custody fees, and clients have willingly signed over powers of financial advice and portfolio management to a third party, then why should the bank be responsible for policing transactions?

By their own admission, the Mirlases had not visited Julius Baer for more than 10 years, and had not received a statement directly from the bank in more than six. At no point did they check up on what was going on — a quiescence the bank took to be a legitimation of Benjamin's activities.

Policing compliance

FinSA, according to the law's supporters, is a major step forward for Switzerland. But there are still question marks, as it is unclear how well Finma will be able to police compliance. The regulator said in a statement that it has "built up its resources extensively" to license and monitor wealth advisers.

Responsibility for ongoing compliance, however, does not reside with Finma professionals, at least not in the first instance. Instead, five self-appointed industry bodies — comprising members of, and paid for by, the industry itself — have been granted the status of "supervisory organisations" with whom wealth advisers must register.

Finma said: "Supervision is within the responsibility of the so-called supervisory organisations. If those supervisory organisations have exhausted their measures of ongoing supervision without success, Finma is responsible for intensive supervision and enforcement."

For critics, this is a well-intentioned system, but which easily lends itself to abuse. "The problem is, there will always be some black sheep," says one investment adviser, who is keen to defend his profession in Switzerland. "And ultimately, it's about clients doing their homework as well."

"Does it help? Yes definitely," says Gallotti. "But is this the end point? No, definitely not. Sadly, I think it might well take another big scandal, another big financial crisis even, for things to change properly."

This article is part of FT Wealth, a section providing in-depth coverage of philanthropy, entrepreneurs, family offices, as well as alternative and impact investment