

TAX HAVENS – ISLANDS NO LONGER?

Ian Young explains the background to information exchange agreements

In the editorial *Crossing Borders* in the March 2009 issue of *TAXline* I wrote about all the different international bodies, and areas of international tax, in which the Tax Faculty is involved.

In this month's editorial I return to one particular issue I mentioned in March and which has been much in the news of late. This is the work of the OECD (and also the EU) in relation to tax havens and offshore financial centres.

This is an area which has had enormous national and international press coverage not least because of the efforts of the G20 countries to shed a spotlight on the issue and to encourage governments to take steps to significantly reduce the problems with offshore centres.

Back to the beginning

The OECD established the Global Forum on Transparency and Exchange of Information in 1996 to identify harmful tax practices in the different countries in the world. The Global Forum published a first report in 1998 and a subsequent report in 2000. A number of tax havens were targeted as part of this work: these were identified as jurisdictions with no or low tax rates, no exchange of information with other jurisdictions, no or little transparency and no requirement for there to be a minimum level of activity before any resultant income could be taxed in the particular tax haven.

The OECD laid down various standards in relation to the exchange of information which it stated should be met by the identified tax havens. It then set out to try and get these countries to sign up to those standards.

To assist in this work the OECD published in 2002 a model Tax Information Exchange Agreement (TIEA) which set out a proforma of what it considered should be in bilateral agreements between tax havens and other countries. The resultant bilateral TIEAs would then ensure that there was adequate exchange of information about the affairs of taxpayers in the other jurisdictions who made investments in the tax haven countries.



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At that time the majority of tax havens agreed that they would accept the OECD standards and change their arrangements. The result of this was that while there were 35 non-cooperative tax havens on the OECD list back in 2000, by 2008 there were just three that were deemed by the OECD still to be non-cooperative: Andorra, Liechtenstein and Monaco.

However, the problem with some of the jurisdictions that had undertaken to meet the OECD standards was that their participation was dependent on all the other jurisdictions taking the same steps, ie 'we will if they will'.

The event that almost certainly created the momentum for real progress came in early 2008 when an employee of a Liechtenstein bank disclosed details of that bank's customers to Germany and other countries in Europe.

This created an international furore and led to a conference in Paris in October 2008 which tasked the OECD to:

... establish a methodology to provide a clear distinction between the countries and territories which have substantially implemented the OECD standard on exchange of information and those which have not, and to publish its conclusions in 2009.

More recent developments

By the time the G20 countries met in London on 2 April 2009 the progress made by the OECD was becoming apparent. At the time of that conference the OECD issued a list of tax havens, OECD member countries and other jurisdictions, which identified those countries which had signed up to the OECD agreed standards of transparency and exchange of information and those which had not.

Initially there was a white list of cooperative countries, two grey lists of countries who said they would do what was necessary to be declared cooperative but had not yet done it, and a black list of countries that had hitherto refused and which contained four names. In fact those four countries immediately declared that they would cooperate. So there were then 30 tax havens and 12 other financial centres in the grey list.

At the time of writing (15 August) the grey list contains only 10 financial centres. Belgium and Luxembourg have now moved to the white list and 26 tax havens plus Bahrain, Bermuda, the British Virgin Islands and the Cayman Islands have also moved to the white list.

Back in April 2009, in the week after the G20 meeting, the UK wrote to the Crown Dependencies – Jersey, Guernsey and the Isle of Man – indicating that it expected them to comply fully with the OECD standard but also:

... to set the pace in this process and put clear water between themselves and those jurisdictions that only just meet the international standard.

It also wrote to the main UK overseas territories, including Bermuda, the Cayman Islands and Gibraltar, and stated that it expected them to have signed up to the full OECD standard by September 2009.

European Union Savings Directive

The EU has also been active in this area by introducing a Savings Directive which covered not only EU member states but other European countries and the associated or dependent territories of the UK and Netherlands. In essence it required countries to notify the EU member states with details from any interest-bearing accounts in their country held by residents of EU member states. A few countries were allowed to deduct an amount from the interest rather than exchange information. The Savings Directive arrangements were introduced in mid-2005 and are now subject to review with general approval for the suggested improvements by the Council of Finance Ministers when they met on 9 June 2009.

A full report on the Savings Directive, one year after it had started, is contained in the September 2006 issue of *TAXline*.

Tax Information Exchange Agreements

In order to be put on the OECD white list, countries have to have signed up to a minimum of 12 TIEAs. These set out that countries must agree to the exchange of information and must have powers 'to obtain and provide information that is held by banks and other financial institutions'.

The TIEA system has been criticised by some civil society bodies on the basis that information can only be exchanged if it is 'foreseeably' relevant to the tax position of the taxpayer in the other jurisdiction and this means that there needs to be a real suspicion that the taxpayer has not complied with all their obligations and is, for instance, the subject of an enquiry or the equivalent. The TIEAs are not intended to allow countries to go on 'fishing expeditions' nor is there to be automatic exchange of information.

At the time of writing there are 105 TIEAs that have been signed. But as most have been signed only recently – 58 in 2009 alone – only 28 have so far entered into force.

If all the 82 countries on the OECD white and grey lists had entered into the required TIEAs, taking into account those which are already parties to double tax agreements with appropriate information exchange provisions, then there would probably need to be between 300 and 400 TIEAs in total.

Liechtenstein

One of the most recent TIEAs is the one between the UK and Liechtenstein which was signed by the two countries on 11 August 2009.

That TIEA has in practice been supplemented by two further agreements. This will involve the introduction of a five-year taxpayer assistance and compliance programme in Liechtenstein, and the Liechtenstein Disclosure Facility (LDF) to be operated by HMRC. The LDF is rather more generous than the UK's domestic New Disclosure Opportunity (NDO) which applies from 1 September 2009. The recovery of taxes under the LDF will be limited to a 10-year period, rather than a potential 20 years under the NDO, and there will be an option under the LDF to apply a composite rate of 40% to the undeclared income and gains.

Under the taxpayer assistance and compliance programme, Liechtenstein financial intermediaries will go through all their investments in Liechtenstein, whatever the form and structure involved, and where there is a UK investor involved the intermediary will notify the relevant investor. If that person cannot satisfy the financial intermediary that they are complying with

their UK tax obligations then the financial intermediary will cease to provide them with financial services (eg maintaining a bank account). In effect the UK-based investor will either have to demonstrate that they are compliant with their UK tax obligations or they will be unable to continue to invest in Liechtenstein.

Both these disclosure initiatives – the NDO and the LDF – are described in more detail in the briefings on pages 17–19.

The future

The next G20 meeting is on 24 and 25 September 2009 in Pittsburgh, USA. By that time there are likely to be rather more TIEAs than the 105 that had been signed by the middle of August.

When a significant number of these TIEAs have been entered into and have come into force, it will become clearer whether they are going to provide information which will lead to the investors' countries of residence recovering tax on income that should have been declared in the past.

That is likely to be a slow process. In the meantime there is the example of Liechtenstein which provides a more proactive approach to obtaining the required information, but even then the domestic legal arrangements in Liechtenstein will probably take a number of months to be put in place.

One matter which will also need to be kept under review is the extent to which the fiscal authorities really do treat information about individual taxpayers as confidential and take appropriate steps to ensure that such information does not find its way into the public domain.

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