

Transparency in tax matters

TAX

In a briefing for journalists published on 24 March 2009 by the Organisation for Economic Co-operation and Development (OECD) on International Tax Evasion the OECD noted that “during recent weeks international tax evasion and the implementation of standards for exchange of information and transparency in tax matters has been very high on the political agenda, reflecting recent scandals that have affected countries around the world and the spotlight that the global financial crisis has put on financial centres generally.”

The European G20 leaders, in advance of the G20 summit in London on 2 April 2009, called for **‘decisive action on tax havens’**.

Contents

Organisation for Economic Co-operation and Development	2
Bank secrecy and exchange of information	3
United States	4
European Union	5
Foot Review	6

Given the speed with which matters have moved in the early part of the year, this document provides a summary of current events and initiatives in the regulation of offshore financial centres.

In 1996 the OECD began its campaign to identify “uncooperative” jurisdictions, so called tax havens, when it launched its harmful tax practices project, the aim being to encourage them to co-operate in exchanging information with OECD countries. The OECD has subsequently turned its attention to reducing banking secrecy.

In July 2008, the G8 Heads of State and Government urged ‘all countries that have not yet fully implemented the OECD standards of transparency and effective exchange of information in tax matters to do so without further delay, and encourage the OECD to strengthen its work on tax evasion’.

Similarly, the action plan issued by the leaders of the so-called Group of 20 major economies (G20) following its summit on Financial Markets and the World Economy in Washington, DC on 14 and 15 November 2008 recognised the importance of the OECD work in this area and urged that failures to implement the standards should be “vigorously addressed”.

Among other things the final declaration expressed a commitment to ‘promote information sharing, including with respect to jurisdictions that have yet to commit to international standards with respect to banking secrecy and transparency’.

This heightened political attention has led to a number of significant developments among financial centres.

Following the G20 meeting in London on 2 April 2009 the OECD published a three-tier list that categorised tax centres, including a “white list” of those that have “substantially implemented” information-sharing agreements and a “grey list” of those that have pledged to do so. Four countries placed on the OECD “black list” because they had not agreed to share tax information immediately changed their positions under the global political pressure. Costa Rica, Malaysia, the Philippines and Uruguay have now been moved to the grey list, having promised to reform.



Organisation for Economic Co-operation and Development

The OECD's campaign, begun in 1998, to identify tax havens and encourage them to co-operate in exchanging information with OECD countries, has had considerable success.

The OECD published a model "Agreement on exchange of information on tax matters" in 2002. A large number of bilateral agreements based on this model have since been concluded, including recent agreements between the UK and Guernsey and Jersey, and between the United States and Liechtenstein.

Speaking in October 2008, Angel Gurría, OECD Secretary-General, said that of the 40 countries originally identified as tax havens, only three then remained on the list of uncooperative jurisdictions. The three jurisdictions were Andorra, Liechtenstein and Monaco. Thirty-five other jurisdictions, which were categorised as tax havens by the OECD in 2000, are now regarded as co-operative having made commitments to transparency and effective exchange of information.

By the end of 2008 a total of 27 Tax Information Exchange Agreements (TIEAs) had been signed since 2000. That number has increased rapidly in the early months of 2009, and further movement is expected, in particular:

- On 10 March 2009, Andorra announced its intention to enter into TIEAs based on the OECD model and to relax its legislation on banking secrecy.
- On 12 March 2009, Liechtenstein announced its intention to implement OECD standards of transparency and exchange of information, having already signed a TIEA with the United States.

- On 16 March 2009 Monaco was reported to have announced its intention to implement OECD standards of transparency and exchange of information.
- On 2 April 2009 HMRC issued a press release announcing that discussions had taken place with the Liechtenstein Government regarding tax transparency.
- Similar commitments have been made recently by Hong Kong, Singapore and San Marino.
- The Cayman Islands has enacted legislation that allows it to exchange information in tax matters on a unilateral basis.

A number of other non-OECD economies have also endorsed the principles of transparency and exchange of information: Argentina; China; Hong Kong; Macao; the Russian Federation; South Africa and the United Arab Emirates.

Forum on Tax Administration

As a separate matter the OECD's Forum on Tax Administration commissioned a study on the role of tax intermediaries, including banks, in September 2006. Work on this was led by HM Revenue & Customs (HMRC) and the report was considered by a meeting of the Forum in Cape Town in January 2008. The chapter on banks focused mainly on the role of investment banks in aggressive tax planning, and a follow-up study on this is due to report back in summer 2009.



Banking secrecy and exchange of information

Under Swiss law¹, violation of banking secrecy is punishable by imprisonment or a fine. The requirement of secrecy is overridden in certain cases for the purpose of law enforcement, including the provision of assistance in criminal prosecutions to overseas jurisdictions, but only for offences broadly equivalent to serious fraud.

In 2003 the OECD Committee on Fiscal Affairs (CFA) set out a common definition of tax fraud which was endorsed by all OECD member countries other than Luxembourg and Switzerland.

The definition states that tax fraud is, 'an act, attempted act or failure to act by any person that is intended to violate a legal duty concerning the accurate reporting, determination or collection of a tax'. For example, the creation of a false document is regarded as fraud, whereas simply not filing a tax Return is not regarded as a criminal matter in Switzerland.

In the past Switzerland has not generally included a full exchange of information article in its double taxation agreements, instead limiting the exchange of information to such information as is necessary to secure the effective application of the agreement itself.

Switzerland has expressed a corresponding reservation to the terms of Article 26 of the OECD model treaty, which deals with the exchange of information. On 13 March 2009, however, Switzerland announced its intention to adopt the OECD standard for administrative assistance and to withdraw its reservation on Article 26. Notwithstanding this, Switzerland has stressed that banking secrecy will remain intact. On 25 February 2009, the Swiss Federal Council announced its intention to carry out a review of banking secrecy, in the light of the United States action against UBS AG and other developments.

Various other jurisdictions have banking secrecy laws which have been seen as an obstacle to the exchange of information between tax administrations. As noted above, several of these including Liechtenstein, Monaco, Austria, Luxembourg, Andorra, and Singapore have also announced their intention to relax banking secrecy to some extent so as to allow the exchange of information for tax purposes.

Finance ministers of Switzerland, Austria and Luxembourg met in Luxembourg on 8 March 2009. According to a press release issued by the Swiss Federal Department of Finance, they expressed a willingness to extend international cooperation on taxation issues, but rejected the creation of a system of automatic exchange of information on interest payments.

The "Second Conference on the Fight against International Tax Fraud and Evasion by promoting Transparency and Exchange of Information in Tax Matters" held in Berlin on 23 June 2009 issued a communiqué which included sanctions against those countries not adhering to the OECD model for tax transparency. Switzerland, Luxembourg and Belgium are reported to have backed the communiqué.

¹ Source: <http://www.efd.admin.ch/dokumentation/zahlen/00579/00607/00621/index.html?lang=en>



United States of America

In February 2008 the United States Senate's Permanent Subcommittee on Investigations began an investigation into the possible role of "tax haven" banks in assisting US taxpayers to evade taxes.

A report was issued on 17 July 2008 detailing the Subcommittee's findings and recommendations and giving detailed case histories in relation to the Liechtenstein-based LGT Group and UBS AG of Switzerland.

Also in February 2008 the United States Internal Revenue Service (IRS) announced that it was undertaking enforcement action involving more than a hundred United States taxpayers in connection with accounts in Liechtenstein, following a disclosure of information by a former Liechtenstein trust company employee to tax authorities in multiple jurisdictions. In May 2008 a private banker formerly employed by UBS AG was arrested in the United States on charges of conspiracy and tax fraud, and on 1 July 2008 the IRS obtained leave to issue a summons to UBS AG for disclosure of names of United States clients with undisclosed Swiss accounts.

A request for administrative assistance was made to the Swiss Federal Tax Administration in July 2008 but was withdrawn on 16 March 2009. A civil action against UBS AG in the United States courts is ongoing and on 13 March 2009 the Swiss Federal Council announced that it was to instruct an American law firm to draft an *amicus curiae* brief for this action to explain Switzerland's position.

Douglas Shulman, Commissioner of the IRS, has described undisclosed foreign bank accounts as 'a top priority for the IRS'.

A "Stop Tax Haven Abuse Act" was introduced into the United States Congress on 2 March 2009 by Senator Carl Levin and others. This is a strengthened version of a bill that was introduced by Senator Levin in February 2007, with the support of then senator Barack Obama, but failed to become law. Among other things the bill would give the IRS greater enforcement powers in relation to certain specified "offshore secrecy" jurisdictions.

There has been some muted criticism of the lack of attention being paid to Delaware in the United States in its position as a State of low taxation.

On 26 March 2009 the IRS announced an "amnesty" for United States taxpayers. The IRS is offering a six month window of opportunity for taxpayers to voluntarily disclose unreported offshore income and pay tax, interest and penalties in respect of that income. In return the IRS is offering reduced levels of penalties than would otherwise be due and taxpayers will likely avoid criminal prosecution.



European Union (EU)

The European Union Savings Tax Directive (EUSTD) came into effect on 1 July 2005 and applies to all EU member states

Dependent or associated territories of EU member states have adopted equivalent rules, as have Andorra, Liechtenstein, Monaco, San Marino and Switzerland. Singapore, Hong Kong and Barbados declined to participate.

The Directive applies to an individual who is resident in an EU country and has interest paid to him in another member or participating state. It provides for automatic exchange of information on interest payments, but as a temporary measure the option of a withholding tax (currently set at 20 percent) was agreed for Austria, Belgium, Luxembourg and a number of non-EU jurisdictions including Switzerland.

The European Commission had identified the following as examples of practices which were being used to exploit loopholes to avoid or evade tax:

- Placing funds on deposit in a limited company or transferring funds into a trust or foundation.
- Moving the investment out of cash into another form of investment, for example, innovative financial products and certain life insurance products.
- Moving the funds on deposit into a jurisdiction which is outside the scope of the EUSTD, for example Singapore, Hong Kong or United Arab Emirates.

On 13 November 2008 the European Commission announced that it had adopted amending proposals to the EUSTD with a view to closing existing loopholes and eliminating tax evasion. The amending proposals would extend the responsibilities of paying agents in respect of intermediate structures established outside the EU and of certain EU trusts and foundations (introducing the concept of "beneficial owners" of offshore companies and trusts). They would also extend the scope of the EUSTD to certain payments not constituting interest.

The changes will have to be applied by Member States broadly three years after the amendments enter into force.

Mutual assistance

On 2 February 2009 the European Commission adopted two proposals for new Directives aimed at improving mutual assistance between Member States' tax authorities in the assessment and the recovery of taxes. One of the key elements of the proposals is that Member States would no longer be able to invoke banking secrecy in order to refuse cross-border cooperation.



The Pre-Budget Report in November 2008 announced a review of long-term opportunities and challenges for the UK's crown dependencies and overseas territories as offshore financial centres

The review, to be conducted by Michael Foot, will cover:

- financial supervision and transparency;
- taxation, in relation to financial stability, sustainability and future competitiveness;
- financial crisis management and resolution arrangements;
- international cooperation.

Conclusions are to be produced in 2009.

The Government has been clear that the variety of existing constitutional arrangements in place across these territories will continue to be respected, including their independence in fiscal matters and the setting of their own rates of taxation.

Only those Crown Dependencies and Overseas Territories with significant financial sectors are included in the scope of the review. In scope are: Jersey, Guernsey, Isle of Man, Bermuda, Cayman Islands, Gibraltar, Turks and Caicos Islands, British Virgin Islands, Anguilla. Out of scope are: Falkland Islands, Montserrat, South Georgia and the South Sandwich Islands, British Antarctic Territory, British Indian Ocean Territory, Sovereign Base Areas of Akrotiri and Dhekelia, Pitcairn Islands, Saint Helena.

Welcoming the launch of the review, the Financial Services Secretary, Paul Myners, said: 'I welcome the appointment of Michael Foot who brings significant experience in financial regulation to this task. Offshore financial centres must play a responsible role in the global financial system. This review will take a serious and constructive look at the challenges these centres face in the current economic climate, and how they can best respond to these'.

The Minister for the Crown Dependencies, Lord Bach, said: 'This review is an opportunity for the Crown Dependencies to demonstrate their strong track record in the regulation of their financial services industries. The review will allow the Crown Dependencies to participate in an open debate about how they can best be equipped to withstand the current difficult economic climate without calling into question their constitutional arrangements. In this regard, I am pleased to see that the Review specifically excludes constitutional change from its scope'.



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