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LECTURE BACKGROUND NOTES

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SUBJECT: **TAX INFORMATION EXCHANGE**

TOPICS: (1) the behaviour of the OECD and its members toward the micro economy jurisdictions versus the OECD's treatment amongst it own members and other economically significantly trade partners;

(2) the EU Savings Directive and other related EU Directives;

(3) the US proposal to automatically report to EU State's bank interest of their residents;

(4) the tax application of the new mutual assistance and extradition treaty between the US and EU;

(5) tax information provision agreements (TIEAs): Promises made and broken by the US to the Caribbean- time to renegotiate ;

(6) other international initiatives for the provision of tax information, such as the FATF and Offshore Group of Banking Supervisors (OGBS) partnership and finally

(7) the procedural process and practicalities of seeking tax information pursuant to an international agreement – the US experience and lack of data

Dear Fellow Government and Professional Colleagues:

I thank Professor Roy Rohatgi and yourselves for yet another opportunity to present your organization with a different perspective on a current topic. Since the start of this annual international tax conference, which has grown to become the leading regional tax conference, I have put forward arguments on then current issues, such as:

- What Common and Civil law Revenue departments' can learn from each other about applying general anti-avoidance jurisprudential principles rather than targeted legislation.
- The US' discriminatory application of transfer pricing to Asian taxpayers and how you can turn it to your advantage.
- The controlled foreign corporation policy tool to mitigate capital outflows from the OECD to the developing world: when will India and China take a stand?

Your feedback and commentary in the hallways and by email exchange afterwards has always been welcome and enlightening. I trust I will hear similarly from you by email this time.

This year I comment on the general subject of, and state of, global tax information exchange, and more particularly on: (1) the behaviour of the OECD and its members toward the micro economy jurisdictions versus the OECD's treatment amongst it own members and other economically significantly trade partners; (2) the EU Savings Directive; (3) the US proposal to automatically report to EU State's bank interest of their residents; (4) the tax application of the mutual assistance and extradition treaty between the US and EU; (5) tax information provision agreements (TIEAs); (6) other international initiatives for the provision of tax information, such as the

FATF and OGBS partnership and finally (7) the procedural process and practicalities of seeking tax information pursuant to an international agreement. As in the past, I do not want to touch much upon what you have commonly read and listened to before at conferences on this topic. Also, my public comments will go beyond the below information, which is provided as a background to the lecture as opposed to being the lecture itself. Hopefully, I am able to present you an alternative, legitimate, perspective on the main subject and also, some new, interesting, information on the underlying topics.

I do not have many slides for this presentation but rather have provided some background information on each of the topics in the following pages. However, if you want to download my few slides, please do so at my website – http://www.llmprogram.org where you will also learn more about my LL.M. programme. Also, if you think that you are sufficiently qualified to be inducted into the Royal Society of Fellows or would like to submit an article for publication in its law review, please contact it staff at http://www.royalsocietyfellows.org.

For those of you who do not know, first a brief background: I am a U.S. attorney, and founder of the Walter H. & Dorothy B. Diamond International Tax Program, hosted at St Thomas University School of Law (Miami), an A.B.A. accredited law school. The program's one hundred, forty annual students' come from upper management of significant banking, accounting and law firms located in many global offshore and onshore financial centers. The program has been operating since 1998 in the U.S. and since 1994 in South Africa, where I met Professor Rohatgi. My extensive knowledge of, and contacts in, the international tax industry result from my LL.M. program and my over ten years work experience solely in the field.

I am a Visiting Professor of International Taxation to the Masters program of the Faculty of Commerce, Law, and Management at the University of the Witwatersrand (Johannesburg) and before that was the coordinator and lecturer of the International Tax Masters of Commerce program at RAU (Johannesburg). I pioneered distributive legal education to the international tax world through creating the first Internet delivered legal degree in the United States, offered by a School of Law accredited by the American Bar Association. Before that, I created the three and five day training program International Taxation and Offshore Financial Centers, partnering since 1997 with EuroMoney-Institutional Investor, which has been taught in-house to banks, exchanges, and governments, in Hong Kong, Singapore, London, Miami, Lisbon, Mauritius, Dominica, and South Africa. I have lectured in over fifty jurisdictions on a wide array of topics as diverse as forecasting economics of B2B integrated supply chains to the discriminatory US implementation and affect of transfer pricing regulations to Indian/Pacific Rim States.

In the June 2003 Cayman Islands Royal Society of Fellows conference, the focus was upon the impact of the EU Tax Savings Directive. I brought together representatives of the US Congress (from the Congressional Black Caucus Foundation), UK Foreign and Commonwealth Office, The Financial Secretary of The Cayman Islands, The Director of Financial Services of the British Virgin Islands, The Director of Financial Services of Anguilla (formerly Director of Financial Services of The Turks & Caicos Islands), as well as many other government officials and staff from the United States and other Caribbean jurisdictions, by example, the I.R.S., F.B.I., Federal Reserve Bank, and St. Kitts. The conference's 180 participants included many major financial institutions and trust companies.

Besides authoring and editing several case books for the program published in cooperation with Kluwer Law International such as Principles of International Taxation and also Offshore Financial Centers, I co-authored the book Tax Reform for South Africa and served as Managing Editor of the Exchange Control Encyclopaedia, which was amalgamated into Butterworths' Exchange Control Encyclopaedia. For Thomson Tax, I author the US Chapter for International Tax Systems and Planning Techniques, a series by Roy Saunders and Miles Dean published in loose-leaf and on Checkpoint. I have been fortunate enough to serve as an editor to Walter Diamond of the Diamond loose-leaf series: Tax and Trade Briefs, Matthew Bender (New York) as well as an editor to Barry Spitz for the Lexicon in the Butterworths' loose-leaf Spitz's Tax Havens Encyclopaedia. These experiences have led me to Co-Author the 2004 loose-leaf series, Offshore Trusts & Companies Laws, Analysis and Tax Planning (contact Lukas Claerhout at http://www.richmondlawtax.com). I was a consultant editor for Kluwer Law International (London) for many years, during which I drafted for Kluwer's International Fiscal Association (IFA) CDROM project a methodology of categorization of taxation.

My first government consulting job was for the South African Revenue Services, as well as having produced several reports to the South Africa Tax Commission which were excerpted for the book Tax Reform for South

Africa, published by the International Law & Tax Institute. I later undertook jobs for the Botswana Revenue and presently am consulting to the UK Treasury and Foreign and Commonwealth Office.

Before full time teaching, I was a senior manager then associate director, international tax, Coopers and Lybrand, which subsequently amalgamated into Price Waterhouse. My primary clients at Coopers & Lybrand were multinational investment and also private banks, insurance companies, technology companies, and company service providers. Over the last ten or so years, I have managed to live in Asia, Europe, Africa and The Americas. In the Indian context, I (later) found out that I pioneered the Mauritius gateway to India for U.S. corporate investment, apparently being the first planner back in early '94 to utilize the double tax agreement for a significant foreign investment, while interacting with the Indian exchange control regulations in place at the time.

Regarding public service in the U.S., I serve on the board of various 501(c)(3) tax exempt charities and in 1989 founded the Last Hope Recovery Center (d.b.a. Abstract Bookshop & Café) in New Orleans, a forty person residential center dealing with dual diagnosis. The Abstract has been mentioned in several press articles, one of which received the American journalism award for its pictorial portrayal of the suffering of residents with AIDS.

I hold a degree in Political Economics, a Juris Doctorate, an LL.M., specialized in European Business and Taxation, and a three year fellowship in the field of inter-company cross-border pricing.

TAX INFORMATION EXCHANGE BACKGROUND

- OECD MODEL DTA - TAX INFORMATION EXCHANGE (ART. 26 & 27)
- OECD MODEL CONVENTION FOR MUTUAL ADMINISTRATIVE ASSISTANCE IN THE RECOVERY OF TAX CLAIMS
- CONVENTION ON MUTUAL ADMINISTRATIVE ASSISTANCE IN TAX MATTERS (OECD & COUNCIL OF EUROPE)
- UN MODEL DTA – TAX INFORMATION EXCHANGE (ART. 26)
- OECD MODEL TAX INFORMATION EXCHANGE AGREEMENT (TIEA)
- EU DIRECTIVE ON EXCHANGE OF INFORMATION
- EU DIRECTIVE ON MUTUAL ASSISTANCE FOR THE RECOVERY OF CLAIMS
- EU SAVINGS DIRECTIVE
- MUTUAL LEGAL ASSISTANCE TREATIES (MLATS) AND NEW US-EU MLATS
- IMPROVING ACCESS TO BANK INFORMATION FOR TAX PURPOSES
- FINANCIAL ACTION TASK FORCE (FATF)
- OFFSHORE GROUP OF BANKING SUPERVISORS BEST PRACTICES (OGBS)

EXCHANGE PURSUANT TO CONVENTIONS

1. OECD MODEL DTA - TAX INFORMATION EXCHANGE (ART. 26 & 27)

Article 26, Exchange of Information, of the 2003 OECD Model Convention reads:

> 1. The competent authorities of the Contracting States shall exchange such information as is necessary for carrying out the provisions of this Convention or of the domestic laws concerning taxes of every kind and description imposed on behalf of the Contracting States, or of their political subdivisions or local authorities, insofar as the taxation thereunder is not contrary to the Convention. ... Any information received by a Contracting State shall be treated as secret in the same manner as information obtained under the domestic laws of that State and shall be disclosed only to persons or authorities (including courts and administrative bodies) concerned with the assessment or collection of, the enforcement or prosecution in respect of, or the determination of appeals in relation to the taxes referred to in the first sentence. Such persons or authorities shall use the information only for such purposes. They may disclose the information in public court proceedings or in judicial decisions.

The 2003 OECD Model, pursuant to its Commentary to the article, allows the following methods of information disclosure[1]

- By request
- Automatically
- Spontaneously
- Simultaneous examination of same taxpayer between the two States
- Allowing requesting foreign Revenue examination of taxpayer in requested State
- Industry-wide exchange of tax information without identifying specific taxpayers
- Other methods to be developed between the States

The 2003 Model established limitations on the request of information:[2]

- Requested State is not obliged to go beyond its own or the Requesting State's capacity pursuant to its internal laws in providing information or taking administrative actions.
- Requested State should not invoke tax secrecy as a shield.
- Requested State is not obliged to supply information which would disclose any trade, business, industrial, commercial or professional secret or trade process.
- Requested State is not obliged to supply information regarding its own vital interests or contrary to public policy (*Ordre Public*).

Article 27 of the 2003 Model addresses assistance in the collection of taxes, stating:

> 1. The Contracting States shall lend assistance to each other in the collection of revenue claims. …
>
> 2. The term "revenue claim" as used in this Article means an amount owed in respect of taxes of every kind and description imposed on behalf of the Contracting States, or of their political subdivisions or local authorities, insofar as the taxation thereunder is not contrary to this Convention or any other instrument to which the Contracting States are parties, as well as interest, administrative penalties and costs of collection or conservancy related to such amount.
>
> 3. … That revenue claim shall be collected by that other State in accordance with the provisions of its laws applicable to the enforcement and collection of its own taxes as if the revenue claim were a revenue claim of that other State.

The limitations remain the same as under Article 26 but also include that the Requesting State must have exhausted reasonable efforts of collection and conservancy pursuant to its domestic law. Also, the Requested State's obligation is limited if its administrative burden would exceed the tax collected for the Requesting State.

2. 1981 OECD MODEL CONVENTION FOR MUTUAL ADMINISTRATIVE ASSISTANCE IN THE RECOVERY OF TAX CLAIMS

This 1981 OECD Model provides for both the exchange of information (article 5) and the assistance in recovery (article 6), which state respectively:

> **EXCHANGE OF INFORMATION**
>
> At the request of the applicant State the requested State shall provide any information useful to the applicant State in the recovery of its tax claim and which the requested State has power to obtain for the purpose of recovering its own tax claims.
>
> **ASSISTANCE IN RECOVERY**

[1] Commentary to Article 26, paragraph 1 sections 9. and 9.1, OECD Model Tax Convention, 2003.
[2] Commentary to Article 26, paragraph 2 sections 14, 15 and 16, OECD Model Tax Convention, 2003.

> 1. At the request of the applicant State the requested State shall recover tax claims of the first-mentioned State in accordance with the laws and administrative practice applying to the recovery of its own tax claims, unless otherwise provided by this Convention.

Procedurally, the documentation must state (1) the authority requesting, (2) name, address and other particulars for identification of the taxpayer, (3) nature and components of the tax claim, and (4) assets of which the Requesting State is aware of from which the claim may be recovered. The nature of the tax claim must include documentary evidence in the form of the instrumentality establishing that the tax is determined, that it is due, and that it is without further recourse to contest under the Requesting State's laws. The applicable Statute of Limitation is of the Requesting State.

The Requested State's obligation is limited, as under the OECD DTA Model Article 26 and 27, if the request requires the Requested State to go beyond its own or the Requesting State's capacity to either provide information or take administrative actions pursuant to their respective internal laws. The Requesting State has a duty to exhaust its own reasonable collection remedies before making the request which procedural requirement may be relied upon by the Requested State. All requests are also limited by *ordre public*.

3. 1988 CONVENTION ON MUTUAL ADMINISTRATIVE ASSISTANCE IN TAX MATTERS

Coming into force April 1, 1995 amongst the signatories Belgium, Denmark, Finland, Iceland, Netherlands, Norway, Poland, Sweden, and the US, this multilateral convention was originally agreed in 1988. The Convention provides for exchange of information, foreign examination, simultaneous examination, service of documents and assistance in recovery of tax claims.

Tax covered includes income, capital gains, wealth, social security, VAT and sales tax, excise tax, immovable property tax, movable property tax such as automobiles, and any other tax save customs duties. The tax also includes any penalties and recovery costs. The tax may have been levied by the State and any of its subdivisions.

The convention allows the request of information regarding the assessment, collection, recovery and enforcement of tax. The information may be used for criminal proceedings on a case-by-case basis pursuant to the Requested State agreeing, unless the States have waived the requirement of agreement.

Spontaneous provision of information shall be provided without request when a State with information:

> (1) has "grounds for supposing" a loss of tax to another State,
> (2) knows that a taxpayer receives a tax reduction in its State that would increase the tax in the other State,
> (3) is aware of business dealings between parties located in both States that saves tax,
> (4) has grounds for supposing an artificial intro-group transfer of profits, and
> (5) that was obtained from the other State has led to further information about taxes in the other State.

Similar to the OECD Model Conventions above, procedurally the requesting documentation must state (1) the authority requesting and (2) name, address and other particulars for identification of the taxpayer. For an information request, the document should include in what form the information should be delivered. For a tax collection assistance request, (1) the tax must be evidenced by documentation in the form of the instrumentality establishing that the tax is determined, that it is due and that it is without further recourse to contest, (2) the nature and components of the tax claim, and (3) assets of which the Requesting State is aware of from which the claim may be recovered.

This Multilateral Convention's limitations follow the 1981 and 2003 OECD Model, but further provide for a non-discrimination clause. The non-discrimination clause limits providing assistance if such assistance would lead to discrimination between a requested State's national and requesting State's nationals in the same circumstances.

2001 UN MODEL DTA – TAX INFORMATION EXCHANGE (ART. 26)

2003 OECD MODEL AGREEMENT FOR TAX INFORMATION EXCHANGE (TIEA)

The OECD Model TIEA was developed by an OECD Working Group consisting of the OECD Members and delegates from Aruba, Bermuda, Bahrain, Cayman Islands, Cyprus, Isle of Man, Malta, Mauritius, the Netherlands Antilles, the Seychelles and San Marino. The OECD Model TIEA obviates from several principles established in the 2003 OECD Model DTA, 2001 UN Model, 1981 OECD Convention on Tax Claims and 1988 OECD Convention on Administrative Assistance.

The Model TIEA provides that the Parties shall give "information that is foreseeably relevant to the determination, assessment and collection of such taxes, the recovery and enforcement of tax claims, or the investigation or prosecution of tax matters." The Model TIEA allows for a two year phase between information sought in criminal tax matters, i.e. criminal tax evasion, versus the later extension to information sought in civil tax matters i.e. civil tax evasion but importantly also tax avoidance.

The TIEA obviates from the traditional requirement of dual criminality, that is the underlying crime for which information is sought should be a crime in both Parties' domestic laws: "Such information shall be exchanged without regard to whether the conduct being investigated would constitute a crime under the laws of the requested Party if such conduct occurred in the requested Party."

Because the OECD Model TIEA is meant to be applied to negotiations with jurisdictions that do not have a direct tax system, the TIEA provides that the Requested Party must seek requested information even when it does not need the information for its own tax purposes. But a Requested State is not obliged to exceed the power to gather information that is allowable under its laws. However, the TIEA is specific that each Party is obliged to provide:

> "a) information held by banks, other financial institutions, and any person acting in an agency or fiduciary capacity including nominees and trustees;
> b) information regarding the ownership of companies, partnerships, trusts, foundations, "Anstalten" and other persons,…ownership information on all such persons in an ownership chain; in the case of trusts, information on settlors, trustees and beneficiaries; and in the case of foundations, information on founders, members of the foundation council and beneficiaries…."

Procedurally, the Requesting State's competent authority must provide, in order to "demonstrate the foreseeable relevance of the information to the request" the following information:

> "(a) the identity of the person under examination or investigation;
> (b) a statement of the information sought including its nature and the form in which the applicant Party wishes to receive the information from the requested Party;
> (c) the tax purpose for which the information is sought;
> (d) grounds for believing that the information requested is held in the requested Party or is in the possession or control of a person within the jurisdiction of the requested Party;
> (e) to the extent known, the name and address of any person believed to be in possession of the requested information;
> (f) a statement that the request is in conformity with the law and administrative practices of the applicant Party, that if the requested information was within the jurisdiction of the applicant Party then the competent authority of the applicant Party would be able to obtain the information under the laws of the applicant Party or in the normal course of administrative practice and that it is in conformity with this Agreement;
> (g) a statement that the applicant Party has pursued all means available in its own territory to obtain the information, except those that would give rise to disproportionate difficulties."

US TIEAS SINCE 2001

- Barbados, 3 November 1984
- Bermuda, 11 July 1986
- Cayman Islands, 27 November 2001
- Antigua & Barbuda, 6 December 2001

- Bahamas, 25 January 2002
- BVI, 3 April 2002
- Netherlands Antilles, 17 April 2002
- Guernsey, 19 September 2002
- Isle of Man
- Jersey

The BVI and Cayman TIEAs are nearly duplicate.

Tax Covered

The BVI and Cayman Islands TIEAs scope is limited to collecting information for issues of US federal "income" tax.[3] For more broad in scope are the The Bahamas[4] and Netherlands Antilles[5] (NLA) TIEAs that apply to "all federal taxes", thus by example encompassing federal estate tax, federal gift tax, federal social security tax, federal self employment tax and federal excise tax. The Barbados[6] and Bermuda[7] TIEAs apply to the specific federal taxes previously listed, which has the same broad affect as The Bahamas and NLA TIEAs.

Scope of Information

The BVI and Cayman TIEAs scope of information includes that "relevant to the determination, assessment, verification, enforcement or collection of tax claims with respect to persons subject to such taxes, or to the investigation or prosecution of criminal tax evasion in relation to such persons." The Bahamas, NLA and Bermuda TIEAs provide that information means any fact or statement, in any form, by example an individual's testimony or documents, that is foreseeably relevant or material to United States federal tax administration and enforcement. The Barbados TIEA provides more generally for the exchange of information to administer and enforce the TIEA listed taxes covered within the scope.

Jurisdiction : Parties and Information Subject to Requests

The BVI, Cayman and NLA TIEAs do not limit the scope of the request to parties that are nationals or resident in BVI and Caymans, but rather allow a request for information as long as either the information is within the jurisdiction or is in the possession of, or controlled by, a party within the jurisdiction. The Bahamas treaty does not address this jurisdictional issue directly but probably will result in the same application. The Barbados TIEA also does not limit the scope of the request to resident parties. The Bermuda TIEA, when the information is sought about a non-resident of both jurisdictions, requires that the requesting party establish the necessity of the information for the proper administration and enforcement of its tax law.

Notice to Taxpayer of Request

The TIEAs do not address the issue, however the TIEAs require that enabling legislation be enacted to ensure the carrying out of the TIEAs obligations. BVI may include in its enabling legislation that the taxpayer must receive notice that a TIEA request has been made targeting the taxpayer.

Tax Evasion Request (1 January 2004)

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[3] Agreement Between The Government Of The United States Of America And The Government Of The United Kingdom Of Great Britain And Northern Ireland, Including The Government Of The British Virgin Islands, For The Exchange Of Information Relating To Taxes, Article 1 (BVI TIEA"; Agreement Between The Government Of The United States Of America And The Government Of The United Kingdom Of Great Britain And Northern Ireland, Including The Government Of The Cayman Islands, For The Exchange Of Information Relating To Taxes, Article 1 ("CI TIEA").

[4] Agreement Between The Government Of The United States Of America And The Government Of The Commonwealth Of The Bahamas For The Provision Of Information With Respect To Taxes And For Other Matters, Article 1 d).

[5] Agreement Between The Government Of The United States Of America And The Government Of The Kingdom Of The Netherlands In Respect Of The Netherlands Antilles For The Exchange Of Information With Respect To Taxes, Article 3 f).

[6] Agreement Between The Government Of The United States Of America And The Government Of Barbados For The Exchange Of Information With Respect To Taxes, Article 3.

[7] Agreement Between The Government Of The United States Of America And The Government Of The United Kingdom Of Great Britain And Northern Ireland (On Behalf Of The Government Of Bermuda) For The Exchange Of Information With Respect To Taxes, Article 2 i).

In the BVI TIEA, criminal tax evasion, for which the exchange of information begins 1 January 2004, is defined:

> ""criminal tax evasion" means wilfully, with dishonest intent to defraud the public revenue, evading or attempting to evade any tax liability where an affirmative act constituting an evasion or attempted evasion has occurred. The tax liability must be of a significant or substantial amount, either as an absolute amount or in relation to an annual tax liability, and the conduct involved must constitute a systematic effort or pattern of activity designed or tending to conceal pertinent facts from or provide inaccurate facts to the tax authorities of either party. *The competent authorities shall agree on the scope and extent of matters falling within this definition*;" (emphasis added)[8]

The Cayman TIEA does not the last emphasized sentence. The Bahamas TIEA states more broadly that ""criminal matter" means an examination, investigation or proceeding concerning conduct that constitutes a criminal tax offense under the laws of the United States other TIEAs do not contain a specific definition of criminal tax evasion."

Legal Privilege Limitation

The BVI, Cayman and Bahamas TIEAs contain a protection for information subject to legal privilege. The BVI TIEA broadly define legal privilege:

> "items subject to legal privilege" means:
>
> (a) communications between a professional legal adviser and his client or any person representing his client made in connection with the giving of legal advice to the client;
>
> (b) communications between a professional legal adviser and his client or any person representing his client or between such an adviser or his client or any such representative and any other person made in connection with or in contemplation of legal proceedings and for the purposes of such proceedings; and.
>
> (c) items enclosed with or referred to in such communications and made -
>
> (i) in connection with the giving of legal advice; or
> (ii) in connection with or in contemplation of legal proceedings and for the purposes of such proceedings, when the items are in the possession of a person who is entitled to possession of them.
>
> Items held with the intention of furthering a criminal purpose are not subject to legal privilege, *and nothing in this Article shall prevent a professional legal adviser from providing the name and address of a client where doing so would not constitute a breach of legal privilege*; (emphasis added)

The Cayman TIEA does not contain the provision that a professional legal advisor is not prohibited from providing a client's name and address. The Bahamas definition is more restrictive in that it does not the clause (c) regarding items enclosed in legally privileged communications. The NLA and Barbados TIEAs likely incorporate legal privilege pursuant to its definition under domestic law.

OECD REPORTS

1998 HARMFUL TAX COMPETITION: AN EMERGING GLOBAL ISSUE (OECD)

In 1998, the Organization of Economic Cooperation and Development ("OECD") presented its seminal report HARMFUL TAX COMPETITION: AN EMERGING GLOBAL ISSUE ["1998 OECD Report].[9] The 1998 OECD Report addressed harmful tax practices in the form of tax havens and harmful preferential tax regimes in OECD Member countries, but primarily in non-Member countries and their dependencies. The 1998 OECD Report focused on geographically mobile activities, such as financial and other service activities. The Report defined the factors to be used in identifying harmful tax practices and regimes, proposing 19 recommendations to counteract such practices and regimes. Because Switzerland and Luxembourg abstained from the Report, these

[8] BVI TIEA, Article 4.

[9] You may obtain this Report without charge in PDF on the OECD website at http://www.oecd.org/.

two OECD members are not bound by its recommendations. The OECD has followed the 1998 Report with progress reports regarding implementation of the recommendations.

The OECD listed as four key factors to determine whether a tax regime was harmful:

1. Whether there are laws or administrative practices that prevent the effective exchange of information for tax purposes with other governments on taxpayers benefiting from the no or nominal taxation.
2. Whether there is a lack of transparency regarding revenue rulings or financial regulation and disclosure.
3. Whether there is a favourable tax regime applying only to certain persons or activities (ring fencing).
4. Whether there is an absence of a requirement that the activity be substantial, which would suggest that a jurisdiction may be attempting to attract investment or transactions that are purely tax driven.

The 2000 follow up report downgraded the 1998 factor of whether the jurisdiction imposed a minimal level of tax from a determinative factor to only as an indicative factor of tax haven status that would lead to further investigation into the four determinative factors.

The list of tax havens determined to have harmful regimes included many of the traditionally targeted, primarily uni- and micro-economy[10], international financial centres on OECD member blacklists i.e. The Bahamas, British Virgin Islands, and Cayman Islands.[11] Notably though, the list did not target jurisdictions such as Hong Kong and Singapore. Their absence from the list constituted disparate treatment, alleged the micro-economies, resulting merely from the micro-economies lack of diplomatic importance.

Also, the 1998 OECD Report, in line with general OECD member trade negotiation policy, did not address its members' ring-fenced tax policies that created harmful effects to the developing world, but rather only addressed the tax competition issues that affected the developed States. By example, the 1998 Report did not address the US tax ring-fenced policy established in 1984 of exempting from withholding tax non-resident's portfolio interest that led to the capital flight from Latin America of US$300 billion to US banks.[12] The 2000 Report listed the US' Virgin Islands as a targeted jurisdiction but did not list the US ring-fenced policy favourable toward the US Virgin Islands, and most of her other dependencies, that allows an exemption from US taxation on non-US source income for US taxpayers resident in the dependencies.[13] This factor, alleged the micro-economies, illustrated the disingenuousness of the Report. The pro-micro economy commentators alleged an OECD discriminatory cartel against non-members, and in line that the Report was merely self-serving of the cartel's interests.

The OECD proposed counter-measures to be applied against listed uncooperative, such as:

- Restricting the deductibility of payments to tax havens;
- Withholding taxes on payments to tax havens; and
- Application of transfer pricing guidelines.

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[10] The traditional micro-economies had previously been uni- agriculture economies, many exporting to their colonial parent under favourable import regimes to either counter OECD agricultural subsidy policies or as a subsidy in itself to the former/current colony to assist it with foreign exchange earnings that in turn could be used to meet the colonies trade deficit in goods. Many of the uni-economies diversified into tourism services to mitigate the trend of their lack of agricultural competitiveness. Eventually, the colonies entered the international financial services sector to mitigate against their dependency on tourism and to increase their local inhabitants standard of living.

[11] See TOWARD GLOBAL COOPERATION, PROGRESS IN IDENTIFYING AND ELIMINATING HARMFUL TAX PRACTICES, OECD (2000) at 10. Forty-seven jurisdictions were initially targeted by the OECD, approximately a quarter of the world's States and jurisdictions.

[12] The US imposes tax upon its taxpayers' interest income. See Globalization, Tax Competition, and the Fiscal Crisis of the Welfare State, Reuven Avi-Yonah, 113 HVLR 1573, 1631 (May 2000) wherein he addresses this policy in the context of President Reagan's administration's efforts to attract foreign capital to fund the ballooning US deficit.

[13] The US imposes tax upon her citizens on the basis on their nationality. Thus, regardless of residency, a US taxpayer is subject to the full impact of US domestic taxation. This tax policy's application to her own citizens is maintained in her tax treaties through the savings clause. The US grants two exceptions to this policy. The first is a exception limited to a ceiling of US$80,000 of employment income for US taxpayers resident in a foreign jurisdiction that remain outside the US at least 330 days. The second is the more egregious ring fence policy that allows an unlimited exemption from US tax on non-US source income for US taxpayers resident in the US Virgin Islands. The Virgin Islands, in turn, grants a generous tax subsidy benefit if the taxpayer's activity is conducted through an approved investment incentive vehicle.

In order to be removed from the targeted list, the micro-economies had to issue Letters of Commitment to engage in effective provision of information for criminal tax matters for tax periods starting from 1 January 2004 and for civil tax matters for tax periods starting from 2006. All Caribbean States and territories were targeted by the OECD and succumbed to commitment letters.[14] The States and Territories that have issued these Letters of Commitment have based their commitment on at least two quid pro quos: (1) a diplomatic seat at the table for future discussions regarding the issue of tax competition, and (2) a level playing field wherein the OECD obtains commitment from its members to implement its recommendations.

My commentary on the criticism of the OECD Report has been very detailed, and addresses the policy issues raised by the Report from a complex perspective.

First, the OECD States have democratically chosen government that democratically set the tax rates and rules that apply to their residents.[15] If the residents do not like the rates or the rules, then the residents must either use the democratic process to change the rates and rules or move to a different jurisdiction.[16] Thus, the often heard justification that OECD residents are justified in 'hiding income' because the OECD welfare States require high tax rates is not legitimate. Evasion, in the OECD, is a democratically established crime with legitimate sanctions.

Secondly, in the OECD, taxpayers have a jurisprudentially long-established right to arrange their affairs so as to incur the lowest incidence of tax. This is known as tax avoidance planning. Planning involves characterisation of income and transactions, timing of income, arranging activities that create value in the income value chain with a system and among systems, leveraging definitional and interpretative anomalies within a system and among systems, to name the basics.

Democratically elected governments may, even perhaps a duty to their welfare state societies, to protect their tax bases. Thus, these governments may change the tax rules to impose tax on transactions that previously avoided tax. On the other hand, retroactive regulatory changes are an affront to the jurisprudential principle of certainty and the Rule of Law. Retroactive changes have been enacted, albeit very rarely, and Courts need to be vigilant in maintaining the Rule of Law and the principle of certainty by striking down retroactive application in these situations.

The groundwork is thus set for a conflicting claim: the government for revenue and the taxpayer (assisted by tax lawyers, accountants, and consultants) to minimize taxation.

Another principle policy established by and binding upon the OECD members is free trade, albeit in mitigated application. The OECD preaches the freedom of movement of goods, services, and investment capital. The free movement of persons which was once an international norm, lost favour amongst the members, but at least amongst the EU trade bloc, has regained its principle status. The principles of free trade and the principle of taxation may create conflicting claims, both legitimate, upon taxpayers (tax subjects) and upon the chain of events that create income (tax objects). I will not go into further detail on this argument, but leave it for the lecture and our discussions.

Finally, this Report and the subsequent OECD Report on Banking briefed below, both address the Exchange ("provision" because it is one way) of Information. I leave you with this issue to consider: Does Public International Law or international jurisprudence or the jurisprudence of our respective jurisdictions (we at this BMA conference represent probably thirty different jurisdictions) establish a "right to privacy"?

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[14] By example, in June 2000, all members of the Organization of Eastern Caribbean States were listed by the OECD as tax havens. Under the threat of the OECD sanctions being implemented by its members against the Caribbean States, all issued Letters of Commitment to the OECD.

[15] I start with the democratic argument in order to ground my arguments in public international law. All OECD members are members of the UN (Switzerland having only recently joined). The OECD and UN principles hold high regard for democratic processes. Democratic participation is held up to the level of being a fundamental human right.

[16] Several OECD States have enacted anti-immigration tax statutes that continue to subject former residents (nationals in the case of the USA) to tax. I strongly disagree with this anti- free trade policy, in this case, that impacts the free movement of persons. This policy creates import barriers for low tax jurisdictions that seek to compete for the immigration of person with capital, such as retirees and entrepreneurs.

1999 PARTNERSHIP FOR PROGRESS AND PROSPERITY: BRITAIN AND ITS OVERSEAS TERRITORIES

In 1999, Robin Cook presented to Parliament a White Paper PARTNERSHIP FOR PROGRESS AND PROSPERITY: BRITAIN AND THE OVERSEAS TERRITORIES (THE "WHITE PAPER"). The White Paper's primary conclusion was that the Overseas Territories had successfully diversified their economies through developing global market positions in the offshore financial services industry but that the Overseas Territories required reputation maintenance through regulatory enhancement in order to maintain their global market position within this industry. The White Paper noted that the Caribbean Overseas Territories were potentially susceptible to money laundering and fraud because of their proximity to drug producing and consuming countries, inadequate regulation and strict confidentiality rules. Also, the White Paper proposed that Britain grant full citizenship, i.e. with right of abode, to the Overseas Territories citizens. But this right of citizenship was not in exchange for implementing the more extensive regulatory regimes in alignment with the OECD Report. In 2002, the UK enacted the British Overseas Territories Bill[17] in order to fulfil the Government's commitment, announced in the White Paper, to extend full British citizenship to those who were British Dependent Territories citizens.

Note that the nationals of the US, Netherlands, French, Portugal and Spanish territories have full parent State nationality with rights of abode. The non-colony status jurisdictions charged further discriminatory treatment, that they did not have the same rights of free movement and abode as the colonial nationals. In its Report, the OECD members targeted trade in capital and services with the stick of sanctions, but did not offer a carrot, much less a lifeline, to the independent micro-economies.

1999 REVIEW OF FINANCIAL REGULATION IN THE CROWN DEPENDENCIES (EDWARDS REPORT) / 2000 REVIEW OF FINANCIAL REGULATION IN THE CARIBBEAN OVERSEAS TERRITORIES AND BERMUDA (KPMG REPORT)

In 1999 and 2000, the UK government in association with the governments of its Crown Dependencies and Overseas Territories assessed the territories financial regulations against international standards and good practice, as well as make recommendations for improvement where any territory fell beneath the standards. In general the reports concluded that the regulatory regimes were good, give limited resources, but that significant further resources had to be employed. The primary conclusions of the reports included

(1) employment of more regulatory resources,

(2) establish an independent regulatory body in each jurisdiction,

(3) maintain records of bearer share ownership,

(4) allow disclosure of beneficial owners' names to regulators for possible onward transmittal to other jurisdiction's regulators, and

(5) expand company disclosure with regard to the directors.

2000 IMPROVING ACCESS TO BANK INFORMATION FOR TAX PURPOSES (OECD)

In 2000, the OECD issued IMPROVING ACCESS TO BANK INFORMATION FOR TAX PURPOSES. The 2000 OECD Report acknowledged that banking secrecy is "widely recognised as playing a legitimate role in protecting the confidentiality of the financial affairs of individuals and legal entities". This Report focused on improving exchange of information pursuant to a specific request for information related to a particular taxpayer. In this regard, it noted that pursuant to its 1998 Report, 32 jurisdictions had already made political commitments to engage in effective exchange of information for criminal tax matters for tax periods starting from 1 January 2004 and for civil tax matters for tax periods starting from 2006.

1990 – 2003 FINANCIAL ACTION TASK FORCE (FATF)

[17] Bill 40 of 2001-2002 was enacted to fulfil the Government's commitment, announced in March 1999 in its White Paper, to extend full British citizenship to those who were British Dependent Territories citizens.

In 1990, the FATF established forty recommendations as an initiative to combat the misuse of financial systems by persons laundering drug money. In 1996, the FATF revised its forty recommendations to address "evolving money laundering typologies". The 1996 forty recommendations developed into the international anti-money laundering standard, having been endorsed by more than 130 countries. In 2001, because of 9/11, the FATF issued eight terrorist financing special recommendations to combat the funding of terrorist acts and terrorist organizations. Regarding the micro-economies, the activities of the Offshore Group of Banking Supervisors (OGBS) have lead to agreement with the FATF on ways to evaluate the effectiveness of the money-laundering laws and policies of its members. The difficulty is that only about a half of offshore banking centres are members of OGBS.

2002 OFFSHORE GROUP OF BANKING SUPERVISORS STATEMENT OF BEST PRACTICES

In 2002, the OGBS formed a working group to establish a statement of best practices for company and trust service providers. The working group included representatives from the micro-economies of Bahamas, Bermuda, B.V.I., Cayman Islands, Cyprus, Guernsey, Gibraltar, Isle of Man an Jersey and from the OECD members France, Italy, the Netherlands, the U.K., as well as the relevant NGOs of the FATF, IMF, and OECD. The terms of reference of the working groups was to "To produce a recommended statement of minimum standards/guidance for Trust and Company Service Providers; and to consider and make recommendations to the Offshore Group of Banking Supervisors for transmission to all relevant international organisations/authorities on how best to ensure that the recommended minimum standards/guidance are adopted as an international standard and implemented on a global basis".

The Working Group concluded: "There should be proper provision for holding, having access to and sharing of information, including ensuring that –

> (i) information on the ultimate beneficial owner and/or controllers of companies, partnerships and other legal entities, and the trustees, settlor, protector/beneficiaries of trusts is known to the service provider and is properly recorded;
>
> (ii) any change of client control/ownership is promptly monitored (e.g. in particular where a service provider is administering a corporate vehicle in the form of a "shelf" company or where bearer shares or nominee share holdings are involved);
>
> (iii) there is an adequate, effective and appropriate mechanism in place for information to be made available to all the relevant authorities (i.e. law enforcement authorities, regulatory bodies, FIU's);
>
> (iv) there should be no barrier to the appropriate flow of information to the authorities referred to in 3 (iii) above;
>
> (v) KYC and transactions information regarding the clients of the Service Provider is maintained in the jurisdiction in which the Service Provider is located;
>
> (vi) there should be no legal or administrative barrier to the flow of information/documentation necessary for the recipient of business from a Service Provider who is an acceptable introducer to satisfy itself that adequate customer due diligence has been undertaken in accordance with the arrangements set out in the Basel Customer Due Diligence paper;

EU DIRECTIVE ON EXCHANGE OF INFORMATION

EU DIRECTIVE ON MUTUAL ASSISTANCE FOR THE RECOVERY OF CLAIMS

2001 US QUALIFIED INTERMEDIARY REGULATIONS

Institutions that have not entered into a QI agreement with the IRS will have US paying agents withhold backup withholding tax on payments from investments in the US to that institution. A QI agreement requires the institution to provide information to the IRS regarding the institution's US national and US resident clients. Alternatively, the institution may not disclose the name of the US taxpayer but instead withhold the required tax on earnings from the US client's account, and transfer the funds to the IRS. Institutions are subject to independent verification audit to ensure compliance with their obligations pursuant to the QI agreement.

However, I think that the QI regulations will merely change the investment behavioural patterns of non-QI institutions that do not want to bear the cost of compliance, in particular small institutions. Whereas past institutional investments may have had a substantial risk allocation portion to US equity, debt, and real estate market, future investments will be directed into the European market to avoid back up withholding. Further, investments can still be made in US equities and debt through dual listed equities and US debt on the Euro-bond market.

2003 SAVINGS DIRECTIVE AGREEMENT

On 21 January 2003, the EU Finance Ministers meeting within the Council of Ministers ("the ECOFIN Council") reached a political agreement on a "tax package", which comprises a Code of Conduct for business taxation, a proposal for a Community Directive on the taxation of interest and royalty payments and a proposal for a Community Directive on the taxation of income from savings ("the Savings Directive"). Furthermore on 7 March the ECOFIN Council agreed the text of the Savings Directive, although the Directive has not yet been formally adopted.

In its current form, the Savings Directive only applies to interest paid to individuals, and in particular it does not apply to companies.

> *Article 2*
> **Definition of beneficial owner**
> 1. For the purposes of this Directive, 'beneficial owner' means any individual who receives an interest payment or any individual for whom an interest payment is secured…"[18]

The Savings Directive requires an automatic, cross-border, exchange of information between the EU members states and their territories.[19]

> **EXCHANGE OF INFORMATION**
> *Article 8*
> **Information reporting by the paying agent**
> 1. Where the beneficial owner is resident in a Member State other than that in which the paying agent is established, the minimum amount of information to be reported by the paying agent to the competent authority of its Member State of establishment shall consist of:
> (a) the identity and residence of the beneficial owner established in accordance with Article 3;
> (b) the name and address of the paying agent;
> (c) the account number of the beneficial owner or, where there is none, identification of the debt claim giving rise to the interest;
> (d) information concerning the interest payment in accordance with paragraph 2.
>
> *Article 9*
> **Automatic exchange of information**

[18] COUNCIL DIRECTIVE 2003/48/EC of 3 June 2003 on taxation of savings income in the form of interest payments.
[19] Currently, an issue exists as to whether the directive applies to Bermuda.

> 1. The competent authority of the Member State of the paying agent shall communicate the information referred to in Article 8 to the competent authority of the Member State of residence of the beneficial owner.
>
> 2. The communication of information shall be automatic and shall take place at least once a year, within six months following the end of the tax year of the Member State of the paying agent, for all interest payments made during that year.

Three EU members, the territories and dependencies of the UK, and to date the accession state of Switzerland have been granted a transitional period of time to implement automatic exchange of information. The transitional period of time is to last until all listed non-EU members, i.e. Switzerland, Monaco, Andorra, Liechtenstein, and the USA, have entered into automatic exchange of information with the EU member states.[20] During the transition, these States and jurisdictions must collect a withholding tax of which 75% of that tax must then be forward to the Member State of residence of the beneficial owner of the interest.

> *Article 11*
> **Withholding tax**
> 1. During the transitional period referred to in Article 10, where the beneficial owner is resident in a Member State other than that in which the paying agent is established, Belgium, Luxembourg and Austria shall levy a withholding tax at a rate of 15 % during the first three years of the transitional period, 20 % for the subsequent three years and 35 % thereafter.

Each of the twenty-five members (including the accession of the new group of ten members), their relevant territories, and the non-EU members acceding to the Directive is allowed to interpret the Directive for legislative implementation under its national law.

Several interpretative issues of contention have already sprung up. In this regard, the UK Revenue has already issued an interpretative document in the form of "frequently asked questions" regarding the implementation of the directive within its legal system.[21] By example, the UK confirms that the Savings Directive does not apply to payments to companies.

> **2.4 Who isn't a relevant payee?**
>
> Individuals will not be relevant payees under the scheme if they do not receive, or have secured for them, savings income. Individuals resident in the UK will not be relevant payees for UK paying agents (because they are resident in the UK). Legal persons (e.g. companies) will not be relevant payees.

Further, the UK Inland Revenue guidance note states that the Savings Directive neither applies to Corporate Trustees nor to beneficiaries as long as the beneficiaries are not absolutely entitled to the savings income.

> **2.12 Do I report payments to trusts?**
>
> A UK trust has no separate existence in UK law and accordingly all payments to a trust are made to the trustees. Therefore, paying agents will need to determine whether the trustee is a

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[20] The Savings Directive recognises the issue of capital flight due to the sensitivity of taxpayers to exchange of information. At paragraph 24 it states, "So long as the United States of America, Switzerland, Andorra, Liechtenstein, Monaco, San Marino and the relevant dependent or associated territories of the Member States do not all apply measures equivalent to, or the same as, those provided for by this Directive, capital flight towards these countries and territories could imperil the attainment of its objectives. Therefore, it is necessary for the Directive to apply from the same date as that on which all these countries and territories apply such measures.calls for." This capital flight issue is based upon three historical benchmarks regarding the imposition of withholding tax on interest and the immediate and substantial impact that withholding tax on interest has on capital flight. The benchmarks are (1) the 1964 US imposition of withholding tax on interest that immediately led to the capital flight of hundreds of million of dollars and the corresponding creation of the London euro-dollar bond market; (2) the 1984 US exemption of withholding tax on portfolio interest that immediately led to the capital flight from Latin America of US$300 billion to US banks; and (3) the 1989 German imposition of withholding tax that led to immediate capital flight to Luxembourg and other jurisdictions with banking secrecy of over a billion DM, so substantial that the tax was repealed but four months after imposition.

[21] Frequently Asked Questions, UK Inland Revenue (July 22. 2003) republished at 2003 WTD 151-7.

> relevant payee. For this reason, if the trustee is an individual resident (according to scheme rules) in a prescribed territory he may be the relevant payee, subject to the normal rules (See Paper 2 "Reportable persons" for more information). *Payments to corporate trustees are not reportable.* (Emphasis added)
>
> Whether payments to trusts established other than in the UK are reportable under the scheme will depend on the status of the trust under the law of the jurisdiction concerned. If you are unsure, you should report the payment as if it were a residual entity.
>
> **2.13 Is savings income secured or paid by trustees reportable?**
>
> If a professional trustee receives savings income and, under the settlement, the beneficiary is absolutely entitled to that savings income, the trustee is a paying agent in respect of that income if the beneficiary is a relevant payee.

In that the Savings Directive does not apply to an investment return of capital gains or dividends, individuals may avoid the automatic exchange of information by simply moving investments into equity funds. Individuals that desire a risk allocation in cash or debt simply require a discretionary trust or company structure. And individuals may simply undertake capital flight to jurisdictions that have not acceded to the Savings Directive, such as Hong Kong, Singapore, Bahamas and Mauritius.

US RESPONSE

Partly in response to the EU Savings Directive, but going well beyond its breadth in scope, in 2000 the US proposed regulations for an automatic provision of tax information regarding bank interest to the all countries, subsequently scaled back by the Bush administration to only include the EU States. The regulations have yet to be enacted. The US Congressional testimony cited that the large capital flight that would result would destabilise Florida's, even the US', banking system required Basle reserve levels.

2003 EU-US AGREEMENT FOR EXTRADITION AND MUTUAL ASSISTANCE

On June, 25 2003 the US and EU signed an agreement, applying to all EU member States and their territories, for the Mutual Legal Assistance in Criminal Matters (MLATs). The agreement's purpose is to assist a requesting state to prosecute offenses through another State's cooperation on obtaining cross-border information and evidence.

In order to receive banking or financial information, the requesting State must provide the competent authority of the other State:

(1) the natural or legal person's identity relevant to locating the accounts or transactions;
(2) information regarding the bank/s or nonbank financial institution/s that may be involved, to the extent such information is available, in order to avoid fishing expeditions; and
(3) sufficient information to enable that competent authority to:
    a. reasonably suspect that the target concerned has engaged in a criminal offense
    b. that the bank/s or nonbank financial institution/s of the requested state may have the information requested; and
    c. that the there is a nexus between the information requested and the offense.

This US-EU has a dual criminality requirement for tax offenses. However, since 1998, tax offenses have become an established underlying crime for purposes of the offense of money laundering, which is an offense in all territories pursuant to the FATF initiative.

AGREEMENT AMONG THE GOVERNMENTS OF THE MEMBER STATES OF THE CARIBBEAN COMMUNITY FOR THE AVOIDANCE OF DOUBLE TAXATION AND THE PREVENTION OF

FISCAL EVASION WITH RESPECT TO TAXES ON INCOME, PROFITS, OR GAINS AND CAPITAL GAINS AND FOR THE ENCOURAGEMENT OF REGIONAL TRADE AND INVESTMENT

Article 24
Exchange of Information

1. The competent authorities of the Member States shall exchange such information as is necessary for the carrying out of this Agreement and of the domestic laws of the Member States concerning taxes covered by this Agreement in so far as the taxation thereunder is in accordance with this Agreement. Any information so exchanged shall be treated as secret and shall only be disclosed to persons or authorities including Courts and other administrative bodies concerned with the assessment or collection of the taxes which are the subject of this Agreement. Such persons or authorities shall use the information only for such purposes and may disclose the information in public court proceedings or judicial decisions.

2. In no case shall the provisions of paragraph 1 be construed so as to impose on one of the Member States the obligation:

(a) to carry out administrative measures at variance with the laws or the administrative practice of that or/of the other Member States;

(b) to supply particulars which are not obtainable under the laws or in the normal course of the administration of that or of the other Member States;

(c) to supply information which would disclose any trade, business, industrial, commercial or professional secret or trade process the disclosure of which would be contrary to public policy.

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