TIEAs – the dawn of the international information super-highway?

Article by Dr. Johanna Niegel

Introduction

As a result of the current economic crisis, international organizations and high tax countries are increasingly pushing offshore centres towards a level playing field by making them commit to the OECD standards of transparency and exchange of information.1

The internationally agreed standard of transparency and exchange of information, as developed by the OECD and endorsed by the UN and the G20, is primarily contained in Article 26 of the OECD Model Tax Convention on Income and Capital and in the 2002 Model Agreement on Exchange of Information in Tax Matters. On the one hand, the standard provides for full exchange of information on request in all tax matters without regard to a domestic tax interest requirement or bank secrecy for tax purposes. On the other hand, it also provides for extensive safeguards to protect the confidentiality of the information exchanged.2

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1 According to the OECD, a jurisdiction meets the key principles of transparency and exchange of information for tax purposes when it provides for (i) exchange of information on request where it is ‘foreseeably relevant’ to the administration and enforcement of the domestic laws of a treaty partner; (ii) no restrictions on exchange caused by bank secrecy or domestic tax interest requirements; (iii) availability of reliable information, particularly accounting, bank and ownership information and powers to obtain it; (iv) respect for taxpayers’ rights; and (v) strict confidentiality of information exchanged. OECD, Countering Offshore Tax Evasion, Some Questions and Answers on the Project, 12 (28 September 2009).

2 OECD, Countering Offshore Tax Evasion, Some Questions and Answers on the Project, 10 (28 September 2009).
In an effort to implement this standard, the international financial community over the past months have witnessed an increased conclusion of so-called TIEAs, a much used abbreviation which stands for Tax Information Exchange Agreements.

With a view to both Double Tax Treaties (DTTs) as well as TIEAs, it has to be stressed already at the outset of the discussion that bank secrecy is generally not incompatible with the requirements of these agreements. Bank secrecy protection, which had never been absolute, continues, but is softened, as, in future, judicial assistance in tax matters will be broadened and cover various scenarios.³

A bit of history: the various lists

Many international organizations have addressed the lack of transparency from various angles: The Financial Action Task Force (FATF), founded in 1989, is leading the fight against money laundering and the financing of international terrorism. FATF elaborated 40 Recommendations which oblige banks to identify their clients and to report certain suspicious transactions. In addition, FATF published a first Black List in 2000 with 15 countries which did not fulfil these standards and hence were qualified as uncooperative in the fight against money laundering. In 2006, the last of these jurisdictions was removed from the list since they all fulfilled the criteria set forth by FATF.

Aside from the European Union and also the United Nations, the OECD has taken on the fight against harmful tax practices. The OECD project against harmful tax practices was launched in 1998 and in 2000 OECD published a Black List of 41 uncooperative jurisdictions. Between 2000 and April 2002, 31 jurisdictions made formal commitments to implement the OECD’s standards of transparency and exchange of information and the last three which remained on the list were removed in May 2009 from the list of uncooperative tax havens in the light of their commitments to implement these standards. It is now considered that these jurisdictions have committed to the internationally agreed tax standard but not yet substantially implemented it.⁴

In the meantime, on 2 April 2009, following the G20 Paris Summit, the OECD Secretariat had published a detailed report on progress by financial centres around the world towards the implementation of an internationally agreed standard on exchange of information for tax purposes which inter alia includes the acceptance of Article 26 and the renegotiation of existing DTTs as well as the conclusion of at least 12 TIEAs.

³ Depending on the form of the agreement, judicial assistance, as for example in the case of Liechtenstein, will now not only be given in the case of tax fraud but also, under certain circumstances, in the case of tax evasion. As a result, there will no longer be a distinction between tax evasion and tax fraud. But Liechtenstein had already given judicial assistance in the past in the case of criminal action. The key point, however, is that the bank–client confidentiality remains in place for all foreign clients not affected by a request.
⁴ They remain on the so-called "Grey-List".
The Report consists of three lists which followed different criteria as compared with previous lists: it ‘blacklisted’ four jurisdictions which had not yet committed to the internationally agreed tax standard. The so-called Grey List included 38 jurisdictions which were designated as jurisdictions that had committed to the internationally agreed tax standard, but had not yet implemented that standard. Forty other jurisdictions were included on a White List, having substantially implemented the internationally agreed tax standard.

Shortly after the publication of the first Progress Report, OECD reported that all four blacklisted countries had committed to the internationally agreed tax standard and had henceforth been moved to the Grey List. In order to be removed from the Grey List, a jurisdiction needs to conclude at least 12 compliant tax information exchange agreements. According to the Progress Report on OECD Work on Tax Havens as of 21 April 2010, there are currently 69 jurisdictions on the White List, 17 on the Grey List and none on the Black List. Since the April 2009 G20 London Summit, some 200 tax information exchange agreements were concluded in order to meet the OECD standard on tax transparency, up from the 45 TIEAs which were signed between 2000 and 2008. In addition, 116 DTTs have been brought up to the standard.

**Means for international information exchange**

*Background of international information exchange in tax matters*

In today’s increasingly borderless financial world, tax assessment has become difficult as taxpayers may have assets located all over the world but according to the principle of territorial application of tax laws, tax authorities cannot cross borders to take action to collect taxes. Therefore, they have to rely on information exchange and conclude international agreements to overcome the territoriality issue.

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7 OECD, Promoting Transparency and Exchange of Information for Tax Purposes, 13 (February 2010).
Various types of agreements

It must be noted that, apart from TIEAs, there are several types of international agreements that contain provisions on tax information exchange. They may be bilateral or multilateral.\(^8\)

In practice, one comes across two types of bilateral agreements: DTTs and TIEAs. There is also a third type of bilateral agreement, the Mutual Legal Assistance Treaty (MLAT). An MLAT is an agreement between two countries for the purpose of gathering and exchanging information in an effort to enforce public laws or criminal laws. But some of these MLATs allow for information exchange in criminal tax matters, whereas others specifically exclude tax matters.

DTTs

DTTs aim at preventing income or profits gained through international economic activity being taxed twice for this purpose and also contain a provision on information exchange. The OECD plays an important role in shaping these treaties as it published a Model Tax Convention on Income and Capital which is updated frequently\(^9\) and serves as a template for bilateral DTTs.

Article 26 of the Model Tax Convention provides an obligation to exchange information that is foreseeably relevant to the correct application of a DTT as well as for purposes of the administration and enforcement of domestic tax laws of the contracting parties. Article 26 however only covers information exchange upon request. Moreover, Article 26 is not directly applicable on its own, ie it must first be made part of international agreements.

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, collection, enforcement, prosecution or the determination of appeals in relation to taxes. Such persons or authorities shall use the information only for such purposes but they may disclose the information in public court proceedings or in judicial decisions. But in no case shall a contracting party be obliged to carry out administrative measures at variance with the laws and administrative practice of that

\(^8\) In my Editorial, I shall only deal with information exchange in bilateral treaties. A summary of multilateral efforts on information exchange can be found in Arthur J. Cockfield, Protecting Taxpayer Privacy Rights under Enhanced Cross-Border Tax Information Exchange: Toward a Multilateral Taxpayer Bill of Rights, University of British Columbia Law Review (forthcoming, 2010), cited from internet working paper, 5 ff.

\(^9\) Last updated on 17 July 2008.
or of the other contracting party, ie to supply information which is not obtainable under the laws or in the normal course of the administration or supply information which would disclose any trade, business, industrial, commercial or professional secret or trade process, or information the disclosure of which would be contrary to public policy (ordre public).

Article 26 has been revised and extended in recent years. The current 2008 OECD Model Tax Convention—the next one is expected to be released already in 2010—has significantly expanded the scope of Article 26 by addition of two more paragraphs. Article 26 para 4 requires a country to use its information gathering measures to obtain information for the other contracting party even though it does not require the information for its own tax purposes. Article 26 para 5 requires a contracting party to supply information held by a bank or other financial institution, a nominee, agent or fiduciary as well as ownership interests in an entity.

Austria, Belgium, Luxemburg and Switzerland had initially made a reservation to Article 26 by declaring that they would not include Article 26 para 5 in their treaties. In early 2009, shortly before the G20 London Summit, these reservations were withdrawn.

Article 26 of the OECD Model Tax Convention nowadays provides the most widely accepted legal basis for bilateral exchange of information for tax purposes. More than 3000 bilateral DTTs are based on this Model Convention.

**TIEAs**

TIEAs aim at establishing a legal framework for the mutual exchange of information relating to taxes, but they do not cover the allocation of taxing rights.

They are intended to ease the way for the conclusion of a DTT, to complement DTTs or they are signed with countries for which a DTT is not appropriate as the treaty partner does not levy any or low taxes on income or profits. They are also concluded in cases where a DTT is considered inappropriate as the other contracting party has a different tax regime or does not levy tax at all or if reservations have been made to Article 26 of the DTT, and thus the DTT does not provide for efficient information exchange.

Although the scope of TIEAs is much narrower than those of DTTs, the TIEAs are much more detailed on the subject of information exchange. In 2002, the OECD introduced a
Model Agreement on Exchange of Information on Tax Matters, which by itself is not binding, but needs to be implemented by a corresponding state treaty. The Model Agreement contains a bilateral and multilateral version. The multilateral version is not a multilateral agreement in the traditional sense but provides the basis for an integrated bundle of bilateral TIEAs. A party to the multilateral agreement is however only bound by the Agreement to the specific parties it wishes to be bound. The Model TIEA Agreement does not intend to prescribe a specific format of how an effective exchange of information for the purposes of the OECD initiative on harmful tax practices is to be achieved but concedes that it is only one of several ways in which this standard can be implemented.

The OECD Model Agreement on Exchange of Information on Tax Matters

Scope (Article 1)

The Model Agreement is limited to exchange of information that is foreseeably relevant to the administration and enforcement of the laws of the applicant party concerning the taxes covered by the Agreement. Resident, as well as non-resident, persons falling under the taxing authority of a contracting party are covered by the Agreement. Procedural rights and safeguards generally remain applicable to the extent that they do not unduly prevent or delay effective exchange of information. Information that precedes the effective date of the Agreement may only be requested provided it relates to a taxable period or chargeable event following the effective date.

Taxes Covered (Article 3)

Bilateral TIEAs cover at least four categories of direct taxes, namely income or profits, capital, net wealth and estate, inheritance or gift taxes, unless both contracting parties agree to waive one or more of them. Each contracting party for itself may decide to omit any or all of the four categories from its list of covered taxes but it would nevertheless be obliged to respond to requests for information with respect to the taxes listed by the other contracting party. The contracting parties may also agree to cover taxes other than the four categories of direct taxes to be able to take into account substantially different tax regimes. The Model Agreement automatically applies to identical, a term which is to be broadly construed, and also to substantially similar taxes, when the contracting parties so agree, which become imposed after the date of signature in addition to or in place of existing taxes if the competent authorities of the contracting parties so agree. The contracting parties, by mutual agreement, can also expand or modify the taxes covered.

12 The Model Agreement has, to date, only been implemented in its bilateral form; OECD, Promoting Transparency and Exchange of Information for Tax Purposes, 7 (February 2010).
Exchange of Information Upon Request (Article 5)

The Model Agreement allows for information exchange between tax authorities on request only, ie excluding automatic and spontaneous exchanges, by lifting bank secrecy, domestic tax interest and dual incrimination principles. Information exchange for both criminal and civil tax matters is covered and hence information in connection with criminal tax matters must be exchanged irrespective of whether or not the conduct would also constitute a crime under the laws of the requested party.

While Article 26 DTT does not create an obligation to obtain the information, but only to use the existing means that national tax authorities already make use of for their own tax purposes, the TIEAs go further and oblige the contracting parties to take action to obtain the information requested and not to rely solely on the information in the possession of its competent authority. If its own information proves inadequate, it must take all relevant information gathering measures, ie measures which are capable of obtaining the requested information, to provide the applicant party with the information requested. The information must be exchanged regardless of whether the requested party needs the information for its own tax purposes. However, a requested party may need to edit the information unrelated to the request if such provision of information would be contrary to its own laws.

Upon request each contracting party shall provide:

- information held by banks, other financial institutions, and any person acting in an agency or fiduciary capacity including nominees and trustees;
- information regarding the ownership of companies, partnerships, trusts, foundations, ‘Anstalten’ (establishments) and other persons, including, within the constraints of its jurisdiction, 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.
- no obligation is created to obtain or provide ownership information with respect to publicly traded companies or public collective investment funds or schemes unless such information can be obtained without giving rise to disproportionate difficulties.

When making a request for information under the Agreement, the applicant party shall provide the following information to demonstrate the foreseeable relevance of the information to the request:
• the identity of the person under examination or investigation;
• a statement of the information sought including its nature and the form in which the applicant party wishes to receive the information;
• the tax purpose for which the information is sought;
• 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;
• to the extent known, the name and address of any person believed to be in possession of the requested information;
• a statement that the request is in conformity with the law and administrative practices of the applicant party; and
• 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.

Possibility of Declining a Request (Article 7)

Article 7 identifies situations in which a requested party is not required to supply information. This is the case if:

• the applicant party would be able to obtain the information under similar circumstances under its own laws for purposes of the administration or enforcement of its own tax laws.
• the request is not made in conformity with the Agreement.
• the provision of information would disclose any trade, business, industrial, commercial or professional secret or trade process.
• the information requested is protected by the attorney–client privilege.
• the disclosure of the information would be contrary to public policy (ordre public).
• the information requested by the applicant party would be used to administer or enforce tax laws of the applicant party, or any requirements connected therewith, which discriminate against nationals of the requested party.

Finally, a requested party is not obliged to provide information which is neither held by its authorities nor in the possession or control of persons who are within its territorial jurisdiction.
**Drawbacks on international information exchange**

*Introduction*

After having examined the key provisions of the OECD Model Agreement, it is necessary to put the factual implementation of TIEAs under scrutiny.

There are several problem areas which hamper the implementation of TIEAs in practice. Above all, it must not be forgotten that the provisions of the TIEA Model Agreement, as most international agreements, only provide the smallest possible denominator. The TIEA Model Agreement itself is not binding; it is merely a model text that can be used as a basis for state treaties as negotiated and signed by the relevant countries.

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**Domestic legal implementation**

Despite the commitment to the OECD standard of transparency and exchange of information, one must bear in mind that, before TIEAs can in fact be concluded, states need to ensure that their domestic laws allow for their implementation. This might involve political approval as well as referenda, procedures which are often time consuming and which may delay or even jeopardize the conclusion of a TIEA. Then the negotiation process of a TIEA is itself a time-consuming procedure.

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**Lack of information**

Information Exchange by means of a TIEA presupposes that both contracting parties to the TIEA have adequate information as well as information gathering mechanisms in place. In the worst case, there might be no information to exchange simply because a contracting party to a TIEA does not collect any or that particular kind of information.
Information exchange upon request only

Both DTTS but especially TIEAs only require information to be exchanged upon request. This ‘upon request only’ requirement provides the necessary protection against so-called fishing expeditions, i.e. cases in which information is sought without having a concrete case at hand. Hence, a mere suspicion will not enable a requesting party to come up with a detailed request.

Procedural rights of the taxpayer

Since a uniform global system of taxation will inevitably fail due to the sovereign right of states to institute their own tax systems, TIEAs provide for an alternative to overcome the territoriality issue without a need to change the internal tax laws.

International information exchange on the other hand will inevitably conflict with the concept of information privacy of taxpayers, i.e. their claim to determine for themselves, when, how and to what extent information about them is communicated to others. In addition, tax information may allow making conclusions about an individual's personal information and circumstances. Effective and fair information exchange is therefore a prerequisite to safeguard taxpayer's rights. States will need to assure by fair TIEAs that their taxpayers' rights, including privacy, will be respected in a similar manner as provided by domestic law and policy once information crosses a border.

Apart from the safeguards foreseen in the OECD Model TIEA domestic laws provide for a variety of protection for persons who are affected by international information exchange. Such procedural rights include information requirements, a right to be heard as well as rights to challenge the information exchange as such or the information gathering methods applied by the requested state party.

OECD also endorses taxpayers’ rights and protection by aiming to improve taxpayers’ collective rights, yet an international statement on this has thus far not been achieved. Some authors argue that in addition to human rights, there should be a separate statement of taxpayer's rights.
Conclusion

As TIEAs do not foresee an automatic exchange of information, they also do not open the gate to an international information exchange highway. Precedents for multilateral automatic information exchange, such as the European Savings Directive which has been in force since 2005, exist and follow the example set forth by the comprehensive multilateral Convention of the Council of Europe and the OECD on Mutual Assistance in Tax Matters of 1988\textsuperscript{18}. This Convention covers an automatic as well as exhaustive information exchange. Despite their existence\textsuperscript{19}, the acceptance of multilateral initiatives has been very slow so far, for example, the Convention on Mutual Assistance in Tax Matters which only has 14 member states. Whether such multilateral initiatives will be successful in the future will heavily depend upon a political weighing of state interests.


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\textsuperscript{18} http://www.oecd.org.