# The Development of Tax Transparency in OECD Countries

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Over the course of globalisation, governments have been confronted with the growing international dimension of financial transactions as taxpayers' activities have turned increasingly global, and now include cross-border investments and establishments, as well as personal and capital movements. In order to prevent tax evasion, different jurisdictions need to cooperate to ensure the full and proper application of their domestic tax laws. One of the most prominent ways to do this is through the exchange of information on taxation. This report aims to explain why we need tax cooperation, how the OECD countries and the EU in particular have taken action in order to increase global tax transparency, and to what extent legislative measures have been implemented effectively.

As far as cross-border taxation is concerned, jurisdictions find themselves faced with two opposing principles: the territoriality principle and the universality principle, eventually creating a tax enforcement and assessment gap. Generally, all jurisdictions are subject to the formal territoriality principle: investigation measures and other enquiries or determination procedures are forbidden on foreign sovereign territory. The substantial territoriality principle (source principle) would accordingly prohibit linking legal consequences according to national law to foreign issues. However, for taxation matters this has been almost completely replaced by the universality principle (world income principle), which requires the state to take legal action irrespective of the nationality and location of the subject. Thus, jurisdictions are faced with a disparity between the university principle and formal enforcement possibilities, which they try to close through intergovernmental agreements and the exchange of information on tax matters.

[1] Ifo Institute (both).

### Fundamental types of tax exchange of information

In order to properly understand international movements towards tax transparency, it is essential to differentiate between three fundamental types of tax exchange of information.

#### *Information exchange on request*

Information exchange on request is a situation in which one authority asks another for particular information on a specific tax case. In the following, the requested authority transmits the requested information. This represents a passive exchange of information because the requesting state has no control or influence over the actions of the requested state.

**Table 1**

| **Intended timelines for first automatic exchanges*** |
|---|
| Jurisdictions undertaking first exchanges by 2017 (54) |
| Anguilla, Argentina, Barbados, Belgium, Bermuda, British Virgin Islands, Bulgaria, Cayman Islands, Colombia, Croatia, Curaçao, Cyprus, Czech Republic, Denmark, Estonia, Faroe Islands, Finland, France, Germany, Gibraltar, Greece, Greenland, Guernsey, Hungary, Iceland, India, Ireland, Isle of Man, Italy, Jersey, Korea, Latvia, Liechtenstein, Lithuania, Luxembourg, Malta, Mexico, Montserrat, Netherlands, Niue, Norway, Poland, Portugal, Romania, San Marino, Seychelles, Slovak Republic, Slovenia, South Africa, Spain, Sweden, Trinidad and Tobago, Turks and Caicos Islands, United Kingdom |
| Jurisdictions undertaking first exchanges by 2018 (47) |
| Albania, Andorra, Antigua and Barbuda, Aruba, Australia, Austria, The Bahamas, Bahrain, Belize, Brazil, Brunei Darussalam, Canada, Chile, China, Cook Islands, Costa Rica, Dominica, Ghana, Grenada, Hong Kong (China), Indonesia, Israel, Japan, Kuwait, Lebanon, Marshall Islands, Macao (China), Malaysia, Mauritius, Monaco, Nauru, New Zealand, Panama, Qatar, Russia, Saint Kitts and Nevis, Samoa, Saint Lucia, Saint Vincent and the Grenadines, Saudi Arabia, Singapore, Sint Maarten, Switzerland, Turkey, United Arab Emirates, Uruguay, Vanuatu |
| * The United States has indicated that it is undertaking automatic information exchanges pursuant to FATCA from 2015 and has entered into intergovernmental agreements (IGAs) with other jurisdictions to do so. The Model 1A IGAs entered into by the United States acknowledge the need for the United States to achieve equivalent levels of reciprocal automatic information exchange with partner jurisdictions. They also include a political commitment to pursue the adoption of regulations and to advocate and support relevant legislation to achieve such equivalent levels of reciprocal automatic exchange. |

Source: OECD (2016a).

**Table 2**

**Development of Art. 26 OECD MTC**

| OECD-information Clause Model | Type |
|---|---|
| Art. 26 OECD MTC 1963 = limited major clause | Not only in conducting the DTT, but limited on residents of the state parties and such tax types are mentioned in the DTT |
| Art. 26 OECD MTC 1977 = limited major clause | Omission of the requirement of state party residency |
| Art. 26 OECD MTC 2000 = unlimited major clause | Enlargement on all types of taxes of the state parties |
| Art. 26 OECD MTC 2005 = unlimited major clause without a restriction by bank secrets | Examination by the requested state does not depend neither on its own public tax interests nor on a national bank secret |
| Art. 26 OECD MTC 2012 = use information received for tax purposes and for non-tax purposes | Provided such use is allowed under the laws of both states and the competent authority of the supplying state authorizes such use |

Source: European Parliament (2015).

The information exchange on request is subject to three OECD principles (OECD 2015). Firstly, the requested state has to do everything in its power in order to assist the requesting state. Secondly, the subsidiary principle requires the requesting state to use its investigating powers to their full extent before submitting the request. Finally, the information requested has to be relevant to the enforcement of the domestic laws of the relevant state.

***Spontaneous exchange of information***

Spontaneous exchange of information is the provision of information in a singular case to another state that is foreseeably relevant to that other party and has not previously been requested. In this, it is a very effective tool to counter tax evasion since it transmits information on taxation that the other state could hardly have detected autonomously.

***Automatic exchange of information***

The automatic exchange of information focuses on the systematic communication of predefined cases without a concrete suspicion of violation of tax law or tax losses. The exact content and extent of automatic exchange is subject to the jurisdictions' negotiations. As can be seen from Table 1, the automatic exchange of information is increasingly being implemented and thus becoming the norm.[2]

[2] Table 1 is also available in the DICE Database (DICE Database 2016b).

**Legal basis for information exchanges on tax matters**

***Information clauses modelled on Art. 26 OECD Model Tax Convention***

Many countries signed a wide series of Double Tax Treaties, of which Art. 26 of the OECD's Model Tax Convention (MTC) forms the basis. With Art. 26, the residence requirement disappeared as a requirement for personal tax circumstances. This standard provides the classical mutual assistance for information exchange on request and for spontaneous information exchange in single examined cases. The automatic exchange of information requires further negotiations between the parties in order to define the scope of the information to be transmitted.

As shown in Table 2 on the development of Art. 26 OECD MTC, until its amendment in 2000, Art. 26 was restricted to resident taxpayers for a limited range of taxes. Since 2000, all taxes except social security contributions have formed part of DTTs. Since 2005, the OECD's standards have been an unlimited major clause without any restriction of bank secrets. Thus, there is a distinction between the protection of banking secrecy and of commercial secrets. Whilst commercial secrets are seen as essential for a competitive market, banking secrecy often helps a state to retain local advantages based on taxation rules. In 2012, Art. 26 was again amended to allow for the use of information retrieved for tax purposes also for non-tax purposes.

Since 2002, many OECD countries have implemented Tax Information Exchange Agreements (TIEAs) with tax havens as identified by the OECD, basing

their TIEAs on the OECD Tax Information Exchange Agreement Model Convention (TIEA MC), which involves the exchange of fiscal information between OECD member states and tax havens. This model agreement is not a binding instrument, but can be seen instead as a base for bilateral and multilateral agreements. In this, the OECD model is an extension of available resources within informational exchange.

The primary focus of the OECD TIEA MC is the exchange of information on request, whereas spontaneous exchange and automatic exchange of information should be subject to individual negotiations. As far as the individual request disclosure is concerned, the OECD TIEA MC conforms with Art. 26 of the OECD MTC. In addition, the OECD TIEA MC allows tax audits and deals with withholding tax information. Similar clauses and limits on the exchange of information are specified as in the OECD MTC. The OECD TIEA MC concerns direct taxes, capital and wealth taxes, real estate taxes and inheritance or gift taxes.

***Information exchanges between EU countries based on EU-Law***

Mutual assistance between EU member states in direct taxation matters has predominantly been regulated by Art.26 OECD MTC, which has been incorporated in many of the EU's tax directives.

In 1977, facing the challenges to taxation caused by increasing European integration and internationalisation of economic processes, the EU passed the EC Mutual Assistance Directive. This, however, did not provide for a mandatory automatic exchange of information. Thus, in 2003 the Savings Directive was passed with the aim of making savings income accumulated in the form of interest payments by beneficial owners in one EU country who are fiscally resident in another EU country subject to effective taxation. The Savings Directive essentially sets a minimum amount of information to be reported by the paying agent to the competent authority of its member state of establishment. To date, Austria is the only EU member state still refusing to participate in the automatic exchange of information.

In 2011, the EU Directive on Administrative Cooperation (DAC1) was passed, widening the scope, instruments and speed of the information exchange as specified by the Savings Directive. Its aim was to strengthen the cooperation between EU tax authorities by setting a minimum standard for intergovernmental cooperation in tax matters.

DAC1 was replaced by DAC2 in 2014, when the EU responded to the international development of information on financial accounts, in particular to the US Foreign Account Compliance Act and the OECD "Standard for Automatic Exchange of Financial Account Taxation Matters". The EU widened the automatic exchange of information to an automatic exchange of financial account information standard. By doing so, it increased the range of application of the automatic exchange of information to include income from securities, from the sale, refund or redemption of the debt claims and benefits from life insurance contracts. In addition, DAC2 unified the common reporting standard between EU member states.

***Information exchanges on a multilateral legal basis***

The Joint Council of Europe / OECD Convention on Mutual Administrative Assistance in Tax Matters was passed in 1988 and amended in 2010 and 2014. It forms the main legal basis for information exchanges between the EU member states and third countries. Simplifying the information exchange to a common standard, it aims to enable each party to counter international tax evasion, to enforce its national laws in a better way whilst, at the same time, respecting taxpayers' rights. In contrast to DAC1 and 2, it covers all forms of compulsory payments to governments, including social security payments. It also applies to countries not part of the DAC1 and 2 such as Australia, Canada, Japan and the United States.

In the 2010 amendment, the Joint Convention was opened up to non-EU and non-OECD countries and bank secrecy could be overcome in order to gain tax transparency. In 2014, further common standards for Automatic Exchange of Financial Information (AEFI) were introduced and additional states were forced to follow them.

***Concurrences of the legal bases***

As far as international taxation is concerned, the variety of legal sources might form concurrences. The question to be asked is in what hierarchical order they apply. In the EU, national laws based on EU Directives are superior to Double Tax Treaties, Tax Information Exchange Agreements and multilateral conventions. Thus, EU member states are bound by DAC as implemented in national laws. In this, DAC acts as a minimum standard where DTT information clauses, TIEAs and multilateral conventions only apply when their scope extends the EU Directive. As a result, they are almost only relevant in relation to third countries, i.e. to non-EU member states.

**Table 3**

**Development of Art. 26 OECD MTC**

| Jurisdiction ratings following a Phase 2 review | |
|---|---|
| Australia, Belgium, Canada, China (People's Republic of), Colombia, Denmark, Finland, France, Iceland, India, Ireland, Isle of Man, Japan, Korea, Lithuania, Mexico, New Zealand, Norway, Slovenia, South Africa, Spain, Sweden | Compliant |
| Albania, Argentina, Aruba, Austria, Bahamas, Bahrain, Belize, Bermuda, Botswana, Brazil, British Virgin Islands, Cameroon, Cayman Islands, Chile, Cook Islands, Cyprus, Czech Republic, El Salvador, Estonia, Former Yugoslav Republic of Macedonia, Gabon, Georgia, Germany, Ghana, Gibraltar, Greece, Grenada, Guernsey, Hong Kong (China), Hungary, Italy, Jamaica, Jersey, Kenya, Latvia, Liechtenstein, Luxembourg, Macao (China), Malaysia, Malta, Mauritania, Mauritius, Monaco, Montserrat, Netherlands, Nigeria, Niue, Pakistan, Philippines, Poland, Portugal, Qatar, Russia, San Marino, Senegal, Singapore, Slovak Republic, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Saudi Arabia, Seychelles, Switzerland, Turks and Caicos Islands, United Kingdom, United States, Uruguay | Largely compliant |
| Andorra, Anguilla, Antigua and Barbuda, Barbados*, Costa Rica, Curaçao, Indonesia, Israel*, Samoa, Sint Maarten, Turkey, United Arab Emirates | Partially compliant |
| Jurisdictions not yet rated because they cannot move to Phase 2 | |
| Federated States of Micronesia, Guatemala, Kazakhstan, Lebanon*, Nauru*, Trinidad and Tobago, Vanuatu* | |

* The jurisdiction is undergoing a supplementary review.

Source: OECD (2016b).

**Comparing implementation of information exchange standards in the OECD**

In order to ensure growing implementation, as well as the quality of exchange of information agreements amongst OECD countries, the Global Forum on Transparency and Exchange of Information for Tax Purposes was established. Comprising almost 100 jurisdictions, it is a multilateral framework dedicated at ensuring and implementing tax transparency and the exchange of information on tax standards. In this regard, it has set up international standards (see OECD MTC and OECD TIEA MC) and conducts peer reviews.

The peer reviews break down the international OECD standards into ten points covering the availability of information, the access of information and the exchange of information. For a more detailed list of the ten points, please refer to the DICE table on "Compliance with International Exchange of Information Standards" (DICE Database 2016a). The OECD's peer reviews are structured into two-phases: in phase one, the jurisdiction's legal and regulatory framework is assessed against the ten elements. Only if there is a positive assessment result, a country will move to phase two where the application of the international standards in practice is assessed. In the DICE table on "Compliance with International Exchange of Information Standards" (DICE Database 2016a), we can see the results of the peer reviews for 2016. From Table 3 it is clear that all EU countries comply or largely comply with the OECD international standards, whilst many of the developing countries still struggle to implement tax transparency.

The OECD report "Tax Transparency 2015" shows that international movements towards greater tax transparency are making progress. All jurisdictions rated as non-compliant in 2014 improved in 2015, pointing to a positive overall trend towards the exchange of information on tax matters until 2017. In addition, since the new standard for automatic exchange of information was published in 2011, a large increase has been seen in the number of taxpayers reporting the existence of foreign financial accounts, with figures rising from 1.2 million in 2011 to 1.8 million in 2014, thus implying that the implementation of the automatic exchange of information on fighting tax evasion has had a positive impact.

**Legal protection of taxpayers**

A central risk that comes with exchanging information on tax matters is that of data privacy and of the legal rights of citizens. In the EU, exchange of information is subject to legal protection rights. Information exchange of personal data has to be based on Parliamentary Law and justified by a clearly defined public purpose. The amount of personal data retrieved has to be in relation to the goal of information exchange, with limitations on the collection and processing of personal data for tax goals. Table 4 shows details of the rights that apply to the exchange of information in order to protect taxpayers.

**Table 4**

**EU legal protection of taxpayers**

| Instruments | Content |
|---|---|
| Notification right | Tax authority or financial intermediaries have to inform the taxpayer before transmitting his/her data to the foreign tax authority |
| Hearing right | Right of the taxpayer to be heard before transmitting his/her data to the foreign tax authority |
| Right of filing an objection | Right of the taxpayer to intervene against the transmittance of his/her data in front of a court of his/her home state |
| Preliminary injunction right | Right to get preliminary legal protection by an interim suspension |
| Right of damage compensation | As a last resort: at least financial compensation |

Source: European Parliament (2015).

## References

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