OECD plans a tax information superhighway

Background

As financial institutions work toward the implementation of the Foreign Account Tax Compliance Act (FATCA), they will be aware that automatic information exchange is not going to be a US-only phenomenon. In April 2013, the G5 (France, Germany, Italy, Spain and the UK) agreed to develop and pilot a multilateral automatic tax information exchange.¹ In their announcement they called on other EU Member States to join the pilot; since April 2013 over 30 countries are known to have endorsed this plan.

Other initiatives recently announced in this area include:

- The European Commission (EC) is refocusing efforts to agree revisions to the European Union Savings Directive (EUSD), and also has plans to introduce new financial information reporting provisions into the Directive on Administrative Cooperation (DAC).

- The Organisation for Economic Co-operation and Development’s (OECD) issuance of a report - A Step Change in Tax Transparency (the Report). This Report was issued in June 2013 at the request of the G8, and set out the steps needed to put a global model of automatic exchange of information into practice. This was followed by supportive statements from the G20 Finance Ministers and Central Bank Governors in July and then by the G20 leaders in September 2013.

While there is great political will to act, a plethora of systems, standards and reporting requirements is in no-one’s interest: the costs associated with such an outcome would be significant for financial institutions and national tax administrations. Currently, it seems that the OECD’s plans have the most momentum and political support in terms of developing a true global standard. It seems likely that the G5 initiative will leverage this work rather than seeking out an alternative solution.

Meetings took place at the OECD in the week commencing 14 October to discuss at an operational level how to progress the plans that were set out in the Report. These meetings took place under the auspices of Working Party No.10 on Exchange of Information and Tax Compliance.
The stated aim of the meetings was to develop a model competent authority agreement and a common reporting standard with a view to putting this to the OECD’s Committee for Fiscal Affairs (CFA) for approval in early 2014. Industry responses to this have been generally supportive in that the OECD is seen as best placed to develop a true global standard.

While the OECD has indicated that its focus will be on drafting the competent authority agreement and the common reporting standard, it also noted its intent to look at the synergies between the common reporting standard and the Treaty Relief and Compliance Enhancement (TRACE) project. At its very simplest, TRACE focused on how to simplify the process by which portfolio investors claim reduced rates of withholding tax pursuant to a double tax treaty or under relevant domestic law. Financial institutions with an interest in this area, such as asset-servicing organizations and portfolio investors, should welcome this since any simplification in process would be a positive development. However, there may be some challenges with this since TRACE envisaged reporting to source countries rather than residence countries. As such, detailed thinking needs to take place in order to identify these leverage opportunities.

Details of the OECD proposals

The Report notes the risks posed by the potential proliferation of different and inconsistent models for automatic information exchange. Such a proliferation would potentially impose significant costs on both government and business in terms of both data collection and ongoing operation. In addition, any automatic information exchange model should be global in nature, in order to solve the problem of tax evasion rather than “relocating” it elsewhere. This has been a perceived weakness of the EUSD.

The Report is explicit in its objectives by referencing the Model 1 Intergovernmental Agreement (IGA) developed for the purposes of FATCA. The Report states that the “... Model 1 IGA contains a number of key features of an effective automatic exchange model. This, along with the fact that governments and financial institutions around the world are already investing to implement it, makes the Model 1 IGA a logical basis on which to build.”

The report identifies and discusses four main implementation steps and also addresses the specific actions that would be needed to meet the information requirements set out in the Model 1 IGA:

1. **Enact broad framework legislation**
   Although a limited number of jurisdictions are already adopting such legislation, most jurisdictions will need to adopt new legislation to implement the Model 1 IGA and in particular, the domestic reporting obligations. The OECD recommends that such legislation should be enacted on the basis that it allows additional jurisdictions to be subsequently added without the requirement to separately amend primary legislation each time a new agreement is entered into.

2. **Elect a legal basis for the exchange of information**
   The report notes that while bilateral treaties such as those based on Article 26 of the OECD Model Tax Convention permit such exchanges, it may be more efficient to establish automatic exchange relationships through a multilateral information exchange instrument such as the OECD Multilateral Convention on Mutual Administrative Assistance in Tax Matters (Convention) as amended in 2011. More than 60 countries, including all G20 countries, have either signed the Convention or have committed to do so.

3. **Adapt the scope of the reporting and due diligence requirements and coordinate guidance to ensure consistency and reduce cost**
   The Report proposes drawing upon the Model 1 IGA with appropriate amendments to support a standardized multilateral model that addresses the needs of all participating jurisdictions and remains workable for financial institutions and government agencies. These changes include: simplifying the rules by removing items specific to the US that are not needed or feasible for a multilateral approach; changing effective dates; and building on what already exists at the EU level and in the area of anti-money laundering standards.
Other changes being considered include:

- **Eliminating the de minimis thresholds that are contained in the Model 1 IGA.** The Model 1 IGA has de minimis thresholds under which accounts do not have to be reported (such as $50,000 for accounts held by individuals).

- **Changing the exceptions to reportable accountholders.** The IGA covers US residents and citizens, but a multilateral model would only need to cover residents. In the interests of simplicity, the Report notes that an approach where each country proposes a list of entities that would be excluded on the grounds of low risk, would be potentially complicated for financial institutions to operate and may be difficult to legislate domestically.

- **Making appropriate modifications to due diligence procedures to remove US specificities.** This would include the reliance on US forms and possibly taking inspiration from the due diligence procedures included in the EUSD.

4. **Develop common or compatible IT standards**

The Report details how the OECD has already brought together its member countries, the EU and representatives of the business community to assist in the development of a reporting format (schema) for implementing the Model 1 IGA. The development of the reporting format is based on Standard Transmission Format and incorporates many elements of FISC 153, which is the standard used within the EUSD. The reporting schema and a first version of the related instructions are planned to be finalized within the second half of 2013.

The road to implementation

As noted above, the OECD’s Working Party 10 met during the week commencing 14 October to discuss these plans. Representatives from industry were invited to join one of the sessions in order for the Working Party to hear and provide feedback. The OECD Secretariat will now be working to prepare a revised draft of the model competent authority agreement and the common reporting standard that takes into account feedback from this meeting. This will then move forward for approval from the OECD’s Committee for Fiscal Affairs in early 2014. If approved, this could potentially have countries seeking to agree and sign competent authority agreements during 2014. For early adopting countries, it is possible that reporting under this model could take place in 2016, and this will have a knock-on effect for financial institutions that will be required to change existing processes and procedures such as customer on-boarding well in advance of this date.

Implications

In terms of what financial institutions should do at this stage, there are a number of points to be considered, including:

- Given the challenging timelines associated with FATCA, there should be no change of scope of in-flight programs.

- Financial institutions should continue to monitor these developments and as details emerge, they should consider transforming FATCA programs into a more general automatic exchange of information program and leverage existing program governance and resource.

- Financial institutions should also consider engaging with relevant industry bodies to raise concerns and contribute to the development of this automatic exchange of information global standard.

Endnote

1. See EY Global Tax Alert, *France, Germany, Italy, Spain, and UK agree to pilot for multilateral exchange of tax information*, issued on 12 April 2013.
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