

Tax Information Exchange Agreements and Data Protection. Conflict and Balance.

Introduction.

A global economy with personal taxation on a world wide basis can no longer accept territorial limitations to its taxing authority. Increased cross border flows of income and capital require states to coordinate their efforts. Territorial and sovereignty based limitations can no longer hinder the fight for fiscal justice. But fiscal justice can only be achieved by legal means and with respect for the fundamental human rights of each and every citizen and taxpayer. Exchange of a subjects tax information is an infringement of the human right to data protection and self determination and can only accepted by respecting the rule of law by a transparent authority.

The OECD has issued in 1998 a report on “Harmful Tax Competition”¹. The report deals with the adverse consequences of global tax competition (also known as ‘race to the bottom’). The report identifies tax havens on the basis of four criteria: no or minimal income tax, lack of effective information exchange for tax purposes, lack of transparency with respect to ownership companies, no substantial activity. The only surviving criterion has remained the lack of effective exchange of information for tax purposes. The report therefore concludes with the recommendation to provide for cross border exchange of information for tax purposes. All OECD member states, with the exception of Switzerland, Belgium, Luxembourg and Austria, have agreed to the report. These non-cooperative member states have motivated their position basically with the argument that they do not wish to end the bank secrecy provisions in their countries.

A serious revision of article 26 of the OECD Model treaty in 2002 by the tax committee of the OECD and the draft of a model TIEA (Tax Information Exchange Agreement)² has lead to new developments and practises. The OECD member states have forced the non-member states to accept the new ‘standard’ under pressure of being labelled ‘non-committed countries’. The revision of the OECD Model took place in 2005 with the adoption of paragraph 4 and 5 to article 26. The major change in paragraph 4 has been that the treaty parties agreed to provide the requested information, also when this information is not necessary for their own tax purposes (in the requested country). Same applies for paragraph 5 that provides that a treaty partner cannot refuse to provide banking information on the reason that it is held by a bank of financial institution. This paragraph ends the bank secrecy. Austria, Luxembourg and Belgium have filed reservations to this paragraph 5, whereas Switzerland has a reservation against the whole of art 26. The Swiss are prepared to provide assistance, only when the information is necessary for the application of the tax treaty and in case of tax fraud. Many states being invited to commit to the new standard, have made a commitment, but had until the end of 2008 not delivered. In the autumn of 2008 new scandals on stolen banking information have lead to a more severe stance of the G-20 member countries. In their meeting in Washington on 15 November 2008 the G-20 member states announced severe

¹ OECD report, Harmful Tax Competition, an emerging global issue. See www.oecd.org.

² OECD, see www.oecd.org/taxation/

repercussions for those countries that continued to refuse to enter into effective information exchange with at least 12 member states of the OECD. The OECD secretariat had prepared a list of countries that have not converted the 'standard' (black list) or have not converted sufficiently (grey list) in TIEA's. In the meeting in London on 2 April 2009 the G-20 decided to take protective measures against the non-cooperative states. It was because of these threats to the financial system that the Swiss Government has decided on 13 March 2009 to withdraw the reservations to article 26 OECD in all. The other non-cooperating OECD member states Austria, Belgium and Luxembourg have done the same with their reservation to paragraph 5 of art 26. Interesting to note that Switzerland did not, until today, sign any TIEA. It made however amendments to existing DTA's, e.g. with France, Germany, United Kingdom, United States, Netherlands.

The latest development here is the launch of the so-called peer review process. In a first step 18 jurisdictions will be reviewed as part of a three-year process approved in February 2010 by the Global Forum on Transparency and Exchange of Information. For Terms of reference, Methodology and Assessment criteria, I refer you to the website of the OECD. The reviews will be carried out in two phases: assessment of the legislative and regulatory framework (phase 1) and assessment of effective implementation in practice (phase 2).

The Standard.

The standard for 'effective exchange of information' can be summarized in the Swiss saying of being 'specific' and 'justified'. The standard is implemented in the TIEA and in art. 26 OECD Model.

Specific.

A request is 'specific' if it relates to the tax affairs of an identified tax payer, which prohibits so-called 'fishing expeditions', being a request for information "that is unlikely to be relevant to the tax affairs of a given tax payer"³. Fishing can also be described "as a roving inquiry, by means of examination and cross-examination of witnesses, which is not designed to establish means of evidence allegations of fact which have been raised bona fide with adequate particulars, but to obtain information which may lead to obtaining evidence in general support of the party's case"⁴.

Article 5 of the standard TIEA deals with the conditions applicable to a request for information. Such a request can only be made when the requesting party has no other means of obtaining the information, with the exception in the situation that obtaining such information domestically would lead to incomparable difficulties. The requesting party must deliver a statement that the request is in conformity with domestic law and that the information sought would be obtainable under domestic law.

The request must be specific with respect to

- a. The identity of the person under examination or investigation (sometimes the identity can be given by other means than name and address).
- b. The period for which the information is requested. (This is relevant in relation to the entry into force of the TIEA. A TIEA can not authorize request for information retroactively, dating back to periods before the entry into force of the TIEA, unless it is for criminal tax matters; always take article on entry into force in consideration)

³ OECD commentary number 5, ad. art 26 paragraph 1.

⁴ Kerr LJ, in *Re State of Norway's Application* (No 1), Court of Appeal, Civil Division, All England Law reports/1989/Volume1/ReState of Norway's Application (no1)-[1989]1All ER 661, pag 23 Issue E: Fishing.

- c. The nature of the information sought and the form in which the requesting Party would like to receive it. (Sometimes requesting party needs the information in specific format).
- d. The tax purpose for which the information is sought (more or less must be established that the information relates to the assessment, recovery or investigation/prosecution of criminal tax matters).
- e. grounds for believing that the information requested is held in the requested Contracting Party or is in the possession of or obtainable by a person within the jurisdiction of the requested Contracting Party,
- f. to the extent known, the name and address of any person believed to be in possession of the requested information,

Justified:

The element of 'justified' is written in the Scope of the Agreement. The requested information must be 'necessary' or 'foreseeably relevant' for the administration and enforcement of the laws of the Contracting Parties concerning taxes covered by this Agreement, including information that is foreseeably relevant to the determination, assessment and collection of these taxes, the recovery and enforcement of tax claims, or the investigation or prosecution of criminal tax matters. A request is not 'justified' if the information sought is merely 'useful'. The crucial element is 'necessary' in the meaning of 'foreseeably relevant'. Data are foreseeably relevant if in the concrete case at hand there is the serious possibility that the other Contracting Party has a right to tax and there is nothing to indicate that the data are already known to the competent authority of the other Contracting Party or that the competent authority of the other Contracting Party would learn of the taxable object without the information. It means that data collected by the requested party that appear not to be relevant or appear to be already in possession of the requesting party, shall not be exchanged. Of course it is not so easy for the requested party to verify if the data collected are foreseeably of relevance, and therefore the element of justification of the request becomes important. The requested party must make its own assessment, which can be motivated and defended against scrutiny. It requires a concrete aanknopingspunt.

The request must be justified with respect to

- a. the reasons for believing that the information requested is foreseeably relevant to the tax administration and enforcement of the tax law of the requesting Contracting Party, with respect to the person identified in subparagraph a)

Obligations of the requested party.

A TIEA is an agreement by which the requested party undertakes to provide information to the requesting party. In the case that the information is not readily available, the requested party undertakes/commits to use all its investigative powers for the collection of the data, even if the requested party does not need the data for its own tax assessment. Especially treaty parties that do not levy an income tax will face a problem when having to investigate a certain subject in order to obtain the requested information. It will require these parties to introduce substantive legislation that authorizes the authorities to collect the information. The TIEA provides for the obligation to introduce prevailing legislation. By this it is not said that there will not exist limits to the undertakings by the contracting parties. The choice of which investigative powers to use is discretionary for the requested party. It has also

discretion in the allocation of men and material. Although this is not always said in so many words, the obligations of the requested party are thus qualified and depend on availability of resources. The law must provide for the possibility, but the party does not need to allocate more than reasonable resources. Because certain treaty partners will always be on the requesting side, it is reasonable that these parties give benefits to those countries that will be on the requested side. The Netherlands e.g. have in the beginning given other treaty benefits to the contracting party. With Jersey and Guernsey additional treaties have been signed with respect to participation exemption applicable to companies resident of Jersey and Guernsey. Also an undertaking to enter into full double tax agreements is sometimes a good compensation. But since the pressure on non-OECD members to enter into TIEA's has mounted, the Netherlands has refrained from giving such additional undertakings.

Investigations abroad.

One of the additional obligations deriving from the TIEA is the obligation to accept a foreign official in an investigation. The commitment is subject to national rules. It does not commit the requested state to include such a possibility in its domestic rules, but if it does, it cannot refuse to accept the foreign visitors. Visitors are authorized to be present at an investigation, but are not allowed to ask questions or inspect documents without the approval of the person under investigation. This rule stems from UK Taxes Management Act which act allows the subject of the investigation to permit or refuse such an investigation. It gives a direct influence on the subject of the investigation to refuse to be questioned in the investigation or documents to be looked at.

Protection of the data-subject.

Is the data-subject protected under the TIEA? A TIEA does not make much reference to the data-subject. The Agreement is between states and does not contain clear provisions that are directly applicable to the data-subject. It is not in the power of the data subject to challenge the discretionary authority of the requested state of to challenge the questions. All that is in the hands of the competent authority. In relation to the data protection there are more options. Within the European Union there are strict data protection rules which prohibit and prevent the exchange of data with third countries, non-EU member states. We will come to that soon. On the issue of Confidentiality the TIEA often contains besides the basic provision in art 8, additional provisions in the protocol to art. 8.

The basic provision in this respect is that the information received will be held confidential and can only be used for the specific purpose for which the request was made. The 'purpose-specific' information can also be used for other purposes with the consent of the requested party that has provided the information. The information may in general be disclosed in public court hearings and juridical judgements. Violation of this 'speciality' rule can give rise to damage and compensation. This is specifically the case with respect to items subject to legal privilege, or any trade, business, industrial, commercial or professional secret or trade process, provided that information described in paragraph 4 of Article 5 shall not by reason of that fact alone be treated as such a secret or trade process. These items do not need to be exchanged. Whether or not an item is a commercial or professional secret can only be said by the subject of the investigation. He should then be aware of the fact that the information has been obtained and will be exchanged, unless he invokes an exclusion. In the situations that information will only be exchanged after a notification procedure, that will be under his control. But it may be more difficult in situations of joint investigations or when no

notification procedure is applied. These situations should be negotiated thoroughly before the information is passed on to the authorities.

Almost all TIEA's contain the provision that the involved person shall be informed in relation to his information and of the use of that information. The requirement can be passed if it is in the interest of the investigation. It is the requesting state and not the information supplying state that has the obligation under the TIEA to inform the data subject⁵. In all aspects the data protection rules that remain applicable are those of the requested state. The obligation to inform the data subject is (often) made conditional upon an application by the data subject to the requesting authority. Which is of course difficult in case the data subject has not been informed of the data exchange. In the Liechtenstein-procedure, the data subject will already be informed once the request has been received by the Liechtenstein authority, unless this jeopardizes the investigation. But in many cases it will be a surprise to the data subject that information on him has been exchanged.

Conflict with data-protection.

The rules that relate to informing the data subject are in conflict with EU data protection rules. Firstly, an exchange is possible, if it is necessary for a given purpose. Secondly the data should be proportionate with the purpose, which precludes automatic and spontaneous exchange. Further, data can only be exchanged with third countries, if that third country has a data protection law, which is adequate and at level with the European system. Unless there is a decision of the European Commission to that effect, cross border exchange of information is forbidden⁶. So, European member states can receive information from outside the EU, but cannot provide information outside the EU, unless compatible systems. Most of the TIEA's, either directly in art. 8 or through protocol, provide for data protection at a level equivalent to the 'acquis européenne'. But that is not sufficient, because what matters is whether the requesting country has domestically a sufficient data protection system. Under the European system, the data controller is obliged to inform the data subject of the exchange of information relating to him. Almost all of the countries, except for Liechtenstein and Switzerland, do not respect that strict legal obligation. The data subject has a right to verify the correctness of the information before it is exchanged, has a right of adjustment and has a right to compensation if it turns out that not correct information has been passed over. In most of the TIEA's the data subject has only recourse on his own government and not on the supplying agency. But strictly and based on the law of the supplying agency, he may have recourse on that agency. Therefore the TIEA provides that, between the states, the supplying agency will have recourse on the requesting agency in case it suffers damages because of the exchange.

The conflict between data protection and information exchange is far from being resolved. The OECD has made it its position that

“the rights and safeguards secured to persons by the laws or administrative practice of the Requested Party remain applicable to the extent that they do not unduly prevent or delay effective exchange of information”.

The problematic phrase is “to the extent”. The OECD wants to make domestic rights and safeguards subordinate to an effective exchange, which of course will not work. Germany has in most of its TIEA's deleted the sentence “to the extent etc”. In the conflict of norms, it is not said that 'effective exchange of information' is of a higher priority than complying with

⁵ See for an example TIEA BRD-Gibraltar, protocol 1, sub e

⁶ Approved countries are: Argentina, Australia, Canada, Faroe islands, Guernsey, Isle of Man, Jersey and Switzerland.

data protection rules. Data-protection has increased its respect since the promotion of article 286 TEC into article 16 TFEU (Principles of EU):

“1. Everyone has the right to the protection of personal data concerning to them”. It has been promoted from article 8 in the Charter of Fundamental Rights of the European Union, which is made directly applicable under article 6 TEU (old art 6 TEU) to being equivalent to a treaty provision. Article 8 reads:

“1. Everybody has the right to the protection of personal data concerning him or her.2. Such data must be processed fairly for specified purposes and on the basis of the consent of the person concerned or some other legitimate basis laid down by law. Everyone has the rights of access to data which has been collected concerning him or her, and the right to have it ratified. 3. Compliance with these rules shall be subject to control by an independent authority.”

Data protection is a fundamental human right and cannot be made subordinate to effective exchange of information, even if treaty partners have an obligation to create effective procedures to secure exchange of information. In can only be done under respect for domestic rights.

Conclusion.

The exchange of fiscal information is an infringement of a fundamental right, protected by the Charter of Fundamental Rights of the European Union and by article 16 of the Treaty on the Functioning of the European Union. It can be justified if it necessary for the given purpose, proportionate and subject to supervision and redress. Tax information exchange is not an ex-third pillar area (police cooperation and judicial cooperation in criminal matters), but even it is was, full data protection would still apply.

A TIEA will establish a legal basis for a specific transfer of personal data, but it will not constitute a legal framework for data protection. Such must be found in the domestic law of both the supplying and the receiving country. Missing that framework will prevent the exchange of information. There is no guarantee that individuals’ rights are actually respected. It is a right of every citizen to decide on the disclosure and use of his or her personal data (Informationelle Selbstbestimmung).

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