



Progress Towards a Level Playing Field?

The Organization for Economic Cooperation and Development (OECD) Global Forum on Taxation

Over 130 representatives of 55 governments, the Commonwealth Secretariat and the European Commission met on 15-16 November 2005 in Melbourne, Australia to review progress towards the OECD's stated objective of transparency and effective exchange of information for tax purposes (the so called "level playing field based on high standards"). And what an extraordinary gathering it was, with tiny islands like Vanuatu and Niue sitting down at the same table as the US, the EU member states, and Canada!

But first a little bit of history. Back in 1998, the OECD issued a report entitled "Harmful Taxation and Offshore Centers" in which it introduced the strange concept of "harmful tax competition". The basic premise of that report was that low tax jurisdictions - predominantly offshore - represented "harmful competition" to the high taxing jurisdictions that make up a majority of the OECD member nations. In the face of opposition from the US, Switzerland and the other offshore centers, the OECD was eventually forced to refocus its attack as a review of "Harmful Tax Practices" - i.e. to move away from the socialist notion that tax competition between nation states is, in and of itself, "harmful" - and it also had to accept that many of its key member states practiced some, if not all, of the so called "harmful practices". In a face saving move, the US agreed to support the OECD in a refocused effort to get offshore jurisdictions to agree to share financial information with the OECD members - and so the OECD Global Forum on Taxation was born.

The two day discussions, which were based upon the review of the legal and administrative frameworks on transparency and exchange of information in tax matters currently in place in over 80 countries, showed that a global level playing field in the areas of transparency and effective exchange of information in tax matters is gradually developing. However, the Forum's discussions identified a number of areas where further progress needs to be made. The Forum's review will be published as a formal report in 2006.

All of the jurisdictions that have agreed to co-operate with the OECD in the Forum have made their commitment subject to a major condition, which can best be described as the "level-playing field get-out clause". It essentially says that the offshore jurisdictions will not have to do anything unless all the other jurisdictions

agree to do it and the OECD member states all implement the same standards. That effectively gives each offshore jurisdiction a “veto” on future developments.

As a result, the OECD realized that it had to include the offshore financial centers in all future discussions about global tax harmonization. Accordingly, the Global Forum on Taxation was forced to give the offshore financial centers a seat at its table. The result is a bizarre list of disparate countries participating in the Forum, as follows: Anguilla, Aruba, Antigua and Barbuda, Australia, Bahamas, Bahrain, Belize, Bermuda, British Virgin Islands, Canada, Cayman Islands, Cook Islands, Cyprus, Denmark, Dominica, Finland, France, Germany, Gibraltar, Greece, Grenada, Guernsey, Hungary, Iceland, Ireland, Isle Of Man, Italy, Japan, Jersey, Korea, Malta, Mexico, Mauritius, Montserrat, Nauru, Netherlands, Netherlands Antilles, New Zealand, Niue, Norway, Panama, Poland, Czech Republic, Portugal, Samoa, San Marino, Seychelles, Slovak Republic, Spain, St. Kitts & Nevis, St. Vincent and the Grenadines, St. Lucia, Sweden, Turkey, Turks And Caicos Islands, United Kingdom, United States, U. S. Virgin Islands, Vanuatu.

In addition, the following countries were invited to contribute to the factual assessment and to attend the Global Forum meeting in Melbourne:

Andorra, Argentina, Austria, Barbados, Belgium, Brunei, China, Costa Rica, Guatemala Hong Kong (China), Liberia, Liechtenstein, Luxembourg, Macao (China), Malaysia, Marshall Islands, Monaco, Philippines, Russian Federation, Singapore, South Africa, Switzerland, United Arab Emirates (Dubai), Uruguay.

Outcome of the Forum

The OECD statement issued after the Forum claims that the review undertaken suggests that “both OECD and non-OECD countries have implemented or made considerable progress towards implementing many of the transparency and effective exchange of information standards that the Global Forum wishes to see achieved”. Apparently, there is no longer any OECD country where a domestic tax interest, of itself, is an impediment to exchange of information. And a growing number of non-OECD economies are negotiating agreements that provide for exchange of information, many countries have improved transparency by implementing the FATF customer due diligence requirements, and several countries have recently required bearer shares to be immobilized or held by an approved custodian (e.g., the British Virgin Islands, the Cook Islands and St. Kitts & Nevis). The Global Forum welcomed these developments but states that further progress is needed if a global level playing field is to be achieved.

The process endorsed by the Forum for further progress states that a combination of individual, bilateral and collective actions will be needed both to achieve and to maintain the goal of a level playing field. The Forum claims that an indicator of the developing co-operation between OECD and non-OECD countries is the increase in tax information exchange agreements and double taxation agreements.

One example of this co-operation was announced at the Forum. Australia and Bermuda announced that they have signed a bilateral agreement to share tax information, a move welcomed by the OECD as a step “to counter abuse of the financial system”.

Under the agreement, the first such accord by Bermuda with any OECD country other than the US, each party may request information from the other on a specific tax matter under investigation or audit. The agreement is the second tax sharing agreement signed by Bermuda, following a deal inked in 1988 with the United States. A similar agreement was also signed last month between the Netherlands and the British crown dependency the Isle of Man.

The OECD Forum states that further progress is required in some countries to remove constraints placed on international co-operation to counter criminal tax abuses. The OECD calls on all countries to co-operate with other countries in the fight against “financial crimes”.

Further progress is apparently also required in the area of access to bank information for tax purposes. Although most countries reported being able to obtain such information for criminal tax matters, a number of countries continue to have strict limits on access to bank information which excessively constrain their ability to respond to specific requests for information in civil and criminal tax cases, according to the OECD (i.e. Switzerland).

Most countries reviewed reported requiring the keeping of accounts by companies and partnerships. However, certain exceptions to this requirement exist, notably in the context of some international company regimes.

The Forum also reports that most countries now have access to legal ownership information of companies, trusts, partnerships, foundations and other organizational structures. Beneficial ownership information is available in a far fewer, but an increasing, number of countries. However, a large number of countries still allow bearer shares - which the OECD does not like, because the ownership of bearer shares is not transparent. The OECD also claims that the availability of ownership information is sometimes complicated by the fact that responsibility for corporate laws is in the hands of political sub-divisions. This comment lead to a statement from the Center for Freedom and Prosperity Foundation in the US that reads in part, as follows: “...the Paris-based bureaucracy reiterated its opposition to market-friendly incorporation laws and - in a swipe at America - urged nations with federal systems to pressure "political subdivisions" into changing their policies in order to help hinder the flow of capital from high-tax nations. The Center for Freedom and Prosperity Foundation and several members of the Coalition for Tax Competition condemned the [OECD] for attacking America's federal system, and also expressed their concern that the [US] Treasury Department delegation at the Melbourne conference acquiesced to the attack”.

For the sixth straight year, the Center for Freedom and Prosperity Foundation hosted a conference on “Tax Competition” the day before the OECD Forum (this year with Australia's Centre for Independent Studies). Following the OECD's Global Tax Forum, Andrew Quinlan, President of the Center for Freedom and Prosperity Foundation, stated: "Since the United States is the only nation with a decentralized system for incorporating companies, it does not take a Sherlock Holmes to figure out that the OECD is targeting Delaware, Nevada, and other states. It is very disappointing that the Treasury bureaucrats at the meeting allowed this attack on America's Constitutional system."

The “Level Playing Field”

The concept of a level playing field is a critical component of the participation by the offshore centers in this initiative. Just how important it is can be seen from the statement issued by the Cayman Islands at the Forum. The Honourable Alden McLaughlin, Minister with Special Responsibility for International Initiatives Affecting the Financial Services Sector, stated:

“We commend the valuable work of all those involved in the efforts of the sub-group, which has worked diligently since [2004] on identifying the legal frameworks for the exchange of tax information which are in place in OECD and non-OECD participating partners, as well as a number of other countries which have significant presence in the global financial services sector.....Equity and long-term self-interest require that countries receiving tax information do not use that information in a manner which in effect produces, reinforces or enhances discrimination against either a tax information provider country, or its nationals, residents or enterprises. Similarly, equity and long-term self-interest require that countries not implement exchange of tax information when doing so would permit discrimination against their national interests or against their nationals, residents or enterprises.

.....For our part we will advance the level playing field on every available occasion, and will accept nothing less.

In other words, the offshore centers will only make changes where all the other financial centers, and the OECD members, make identical changes at the same time.

Relevance of OECD List of Tax Havens Published in 2000

The Forum noted that a number of countries have expressed concern at the way in which some countries have used the 2000 OECD list.

In 1998 the OECD started to review 47 jurisdictions as targets for the “unfair tax competition” investigation. Over the next two years the OECD negotiated with those jurisdictions. Finally, in 2000, the OECD published a “blacklist” of 35 offshore nations. The OECD stated that if the countries listed failed to commit to reform before a set date (the deadline for which was frequently extended), the OECD member states would consider abrogating tax treaties allowing companies to write off tax paid in the territories and impose other sanctions (such as shutting those jurisdictions off from the global banking system). Co-operative jurisdictions were offered assistance to develop other parts of their economies.

Bermuda, the Cayman Islands, Cyprus, Malta, Mauritius and San Marino were not included in the final published list because they each individually signed letters stating that they would co-operate fully with the OECD. Another six - Costa Rica, Jamaica, Dubai, Brunei, Macao and Tuvalu - were apparently dropped because they passed OECD tests.

The 35 named offshore jurisdictions included the British Virgin Islands, Gibraltar, Grenada, Guernsey, the Isle of Man, and Jersey.

The Isle of Man's Chief Minister Donald Gelling has criticized the OECD for its continued support of the list that features his Island. Mr. Gelling recently visited Washington DC in an effort to remove the Isle of Man from various US blacklists.

He said that US state and federal departments are adopting the OECD list automatically, without considering the consequences for jurisdictions such as the Isle of Man.

Mr. Gelling points out that: "The OECD list should be updated as there is no system to get the Isle of Man off it. Individual [US] senators come forward with private member's bills about things that can take money away from the state and they all use the same definition of a tax haven."

The states of Montana, Maryland, Michigan and Pennsylvania all have current proposed bills that list the Isle of Man as a tax haven. There are also several bills at federal level that do the same. None of the bills has been passed, but if they were, it could threaten the continued or future existence of US-owned operations based in the Isle of Man.

In response, the OECD Forum stated: "If a country chooses to use a list of countries derived from the OECD list, it should do so based on the relevant current facts. Thus, progress made in the implementation of the principles of transparency and effective exchange of information in tax matters should be taken into account by such countries and their legislatures. The 2000 OECD list should be seen in its historical context and as an evaluation by OECD member countries at a particular point in time of which countries met the criteria set out in the 1998 Report. More than five years have passed since the publication of the OECD list and positive changes have occurred in individual countries' transparency and exchange of information laws and practices since that time. The Report, once completed and as updated periodically, will provide more up-to-date information. This does not reflect any judgment by the Global Forum on the tax or other policies underlying country lists."

Conclusion

In my view, the EU and the OECD have wasted a monumental amount of time and resources in the process of pursuing the offshore financial centers. In the final analysis, the changes implemented by the offshore jurisdictions as a result of the attacks have actually made them stronger and more relevant, not weaker. In addition to their strengthened business practices, the offshore financial centers now have considerably enhanced negotiating positions going forward. Since most of their commitments to cooperate are conditional on the achievement of a "level playing field" - so that if some jurisdictions fail to comply, then the others do not have to either - the offshore financial centers have now had to be included as equal partners in the ongoing discussions of the OECD's Global Forum on Taxation, even though they are not formally members of the OECD.

W William Woods specializes in the development of offshore financial centers (OFCs) and has lived, and/or done consulting work for, inter alia, Bermuda, Cayman Islands, Dubai, Gibraltar, Hong Kong, Singapore and Labuan. He is the

Chairman and CEO of WWoods & Co. Limited, a financial services consultancy, and the author of an online Blog about OFCs at www.bizoffshore.com.