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Background

1. The EU Savings Tax Directive has been in force since 2005. Last year the EU Commission conducted a second review of the workings of the Directive. Whereas the first review of the Directive in 2008 focused on issues of interpretation, this second review covered the functioning of the Directive, including an economic evaluation. The report into the findings was published earlier this year[1].

2. In addition the UK, Germany and Austria have announced details of a tax agreement with Switzerland[2,3]. These agreements were to resolve long standing disputes over untaxed investments within Swiss accounts. The agreements are based upon the establishment of withholding tax regimes and greater coordination between Swiss paying agents and national tax authorities. Objections from the EU Commission led to amendments over the legal structures of these agreements, but the substance remains unchanged in essence[4]. Greece is expected to follow suit and sign a corresponding treaty with Switzerland.

3. In light of these developments EPF has conducted a parallel study of member state experiences of the Directive. The objective of this study is to identify how far the problems associated with the exchange of information have been tackled. The study also seeks to review how successful the withholding tax alternative has proved, particularly with regard to actual collection of revenue. This report follows the first EPF study on this issue, *Challenges facing the Savings Tax Directive*, which was published in 2008[5].

4. The 2008 report raised concerns about high compliance costs faced by banks in implementing an extension of the EU saving tax and also noted that revenue authorities in the EU "seem to be struggling to implement an effective system of information exchange with long delays, inaccurate data and problems in following up reports of interest income received by tax payers in other countries."

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[1] COMMISSION STAFF WORKING DOCUMENT, presenting an evaluation for the second review of the effects of the Council Directive 2003/48/EC, *Accompanying the document* REPORT FROM THE COMMISSION TO THE COUNCIL in accordance with Article 18 of Council Directive 2003/48/EC on taxation of savings income in the form of interest payments {COM(2012) 65 final}

[2] Agreement between the Swiss Confederation and the UK on co-operation in the area of taxation, 6 October 2011; http://www.hmrc.gov.uk/taxtreaties/swiss.pdf; as amended under Protocol to the Agreement 12 March 2012; http://www.hmrc.gov.uk/taxtreaties/protocol-amend-ukswiss-agree.pdf

[3] Protokoll, zur Änderung des am 21. September 2011 in Berlin unterzeichneten Abkommens zwischen der Bundesrepublik Deutschland und der Schweizerischen Eidgenossenschaft über Zusammenarbeit in den Bereichen Steuern und Finanzmarkt;

[4] Abkommen, zwischen der Schweizerischen Eidgenossenschaft und der Republik Österreich über die Zusammenarbeit in den Bereichen Steuern und Finanzmarkt; http://www.sif.admin.ch/00488/index.html?lang=en&msg-id=44130

[5] Mather, G. & Boyfield, K., *Challenges facing the Savings Tax Directive,* The Infrastructure Forum, November 2008

Highlights from EPF's 2008 Report

The *information* exchange system is affected by significant delays in the provision and hence the processing of information. Six member states had by late 2008 not provided the European Commission with data for 2006.

One revenue authority said that it had to ask for more information in almost every case with regard to information exchanged under the savings tax directive. The report says this does not seem ideal, involving significant additional manual effort and resources by revenue authority staff.

Smaller European economies like Estonia have to follow complex procedures for information exchange even though they have no domestic tax on interest income for their own citizens at all.

The 12 smaller EU states which produced figures for 2006 on the sums which they had reported under the information exchange system of the Savings Tax (Czech Republic, Denmark, Estonia, Finland, Greece, Lithuania, Latvia, Malta, Poland, Portugal, Slovenia and Slovakia) reported between them only €90.43m – a combined total amounting to less than 1% of the amount reported by the largest financial centre, the United Kingdom, which reported €9132.49m.

The information exchange system is revealing itself in operation to be:

- Seriously affected by quality of data received;
- Prone to lengthy delays;
- Frequently requiring manual follow up and further inquiries by tax authorities;
- Prone to confusion on what is taxable with regard to the sum reported, which may be interest or dividend payments, sales proceeds or even a bank withdrawal;
- Disproportionate for small countries without large financial centres.

A withholding tax system can be more efficient in operation than the exchange of information system because the deduction of real cash and its transfer to the revenue authorities of another member state is a more concrete act than the passing of large numbers of data files. In those cases it is often unclear what has happened to the data received by a particular revenue authority.

It seems clear that much of the information received automatically from other authorities in the past has gone essentially unused. Lack of transparency by revenue authorities who claim that such information is confidential makes it still more difficult to be confident that the information exchange system is working well.

Findings of the EU Commission's Review 2011

5. The economic analysis of the Commission in its recent work has helped to illuminate the monetary value of automatic exchange of information. The peak year for information exchanged was 2007 where reported transactions reached €38.9 billion (€3.6 billion of interest), but the figure slumped to €9.9 billion in 2009 (€2.3 billion in interest)[6]. Table 1 breaks down the figures by member states. Withholding tax shared by all countries under the Directive decreased from €700 million in 2008 to €495.9 million in 2009. A breakdown of the data is outlined in Table 2. These decreases can partially be explained by the financial crisis.

[6] COMMISSION STAFF WORKING DOCUMENT, presenting an evaluation for the second review of the effects of the Council Directive 2003/48/EC, *Accompanying the document* REPORT FROM THE COMMISSION TO THE COUNCIL in accordance with Article 18 of Council Directive 2003/48/EC on taxation of savings income in the form of interest payments {COM(2012) 65 final}

***Table 1**; Information on interest payments exchanged by Member States to other EU*

Member States, (amounts in million Euro)

Member State	2005 (2nd half)	2006	2007	2008	2009
AT	n.a.	n.a.	n.a.	n.a.	47,68**
BE	n.a.	n.a.	n.a.	n.a.	n.a.
BG	n.a.	n.a.	1,42	2,03	3,64
CY	5,23	15,01	25,44	32,39	35,61
CZ	2,92	7,82	9,68	11,52	8,33
DE	109,08	181,82	158,14	196,48	287,70
DK	-	119,90	124,90	51,26	58,37
EE	-	4,40	-	1,34	0,89
EL	6,69	22,83	19,46	25,20	13,98
ES	224,25	198,86	273,30	256,21	220,91
FI	26,02	60,93	7,80	2,86	1,85
FR	41,1	113,55	123,63	149,88	123,78
HU	-	3,72	3,06	7,07	17,10
IE	131,14	426,96	795,36	290,5	-
IT	11,3	124,91	141,84	84,12	803,16
LT	-	0,09	0,18	0,37	0,48
LU	76,79	270,46	368,01	432,54	102,83
LV	0,17	0,64	1,32	2,12	1,93
MT	1,01	2,10	1,73	4,62	2,65
NL	88,08	789,42	200,30	232,98	236,73
PL	-	7,28	10,05	5,57	7,37
PT	2 k	,56	3,74	16,93	20,22
RO	n.a.	n.a.	7,31	10,75	22,14
SE	-	-	-	-	-
SI	0,6	1,35	1,48	3,07	37,54
SK	0,95	4,52	-	7,76	2,53
UK	293,63	293,90	1.282,93	562,69	259,39
Total	**1.018,96**	**2.651,03**	**3.561,08**	**2.390,26**	**2.316,81**

***Austria has reported information exchanged in their statistics in 2009 despite coming under the withholding tax regime of the Directive and not having a voluntary disclosure provision in place. At the time of publication, the Commission had not received any explanation from AT for this statistic regarding whether it would derive from information exchanged under Art. 4(2) or could otherwise be justified*

Source: Commission Staff Working Document Presenting an evaluation for the second review of the effects of the Council Directive 2003/48/EC

***Table 2**; Tax revenue shared by countries with withholding tax regime (million Euros)*

Note: Data for 2005 covers only the second half of the year.

EU Member States	2005	2006	2007	2008	2009
Austria	9,48	44,32	59,53	67,01	49,48
Belgium	7,51	19,61	25,92	-	-
Luxemburg	35,90	124,59	153,00	174,72	122,95
Total	52,89	188,52	238,45	241,72	172,43
Third Countries					
Andorra	3,50	12,77	16,34	18,84	13,94
Liechtenstein	1,94	7,08	9,06	11,30	7,17
Monaco	3,75	11,70	-	-	-
San Marino	1,13	7,47	10,75	15,40	14,02
Switzerland	77,23	255,92	298,23	348,90	265,64
Total	87,54	294,93	334,39	394,43	300,78
Dependent and Associated Territories					
British Virgin Islands	0,00	-	-	-	-
Turks and Caicos	0,01	0,02	-	-	-
Guernsey	4,93	16,83	-	14,24	5,51
Jersey	13,26	32,15	38,34	33,55	9,94
Isle of Man	13,26	20,35	23,39	16,89	7,12
Netherlands Antilles	-	0,05	0,15	0,08	0,11
Total	31,47	69,39	61,88	64,76	22,67
Overall total	171,90	552,84	634,73	700,92	495,87

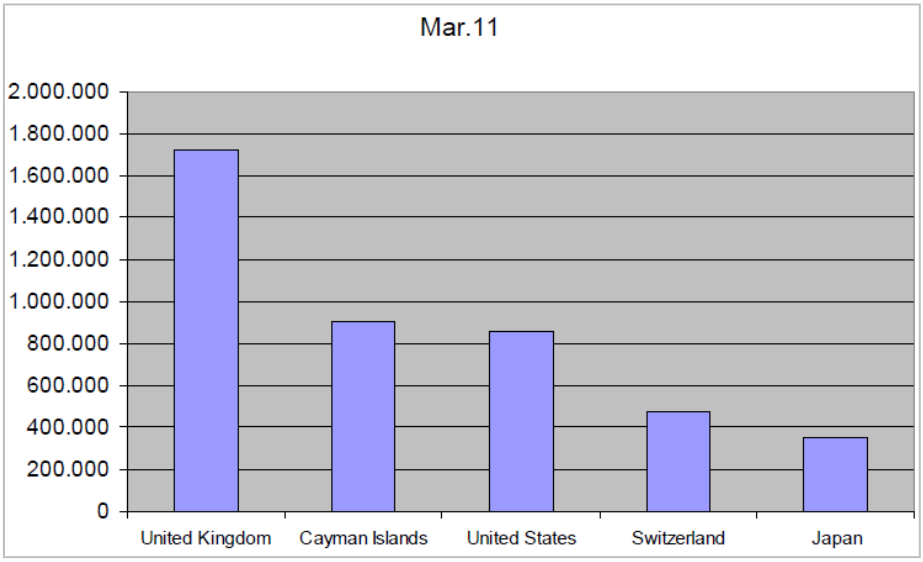
Source: Commission Staff Working Document *Presenting an evaluation for the second review of the effects of the Council Directive 2003/48/EC*

6. The Commission's report provided an insight into the development of key EU and non-EU markets for savings products. Most of the important offshore financial centres did not agree to the disclosure of their bilateral positions. However publicly available BIS data[7] indicated that the amount of foreign non-bank deposits for the Cayman Islands in 2011 is comparable to that of the US. For the year 2007 in total 65% of all non-bank deposits in member states and in jurisdictions within the network of the Savings Agreements, were held by customers in offshore jurisdictions. Furthermore, data released from the Swiss National Bank[8] identified a strong client base in offshore jurisdictions inside and outside the network of Savings Agreements.

[7] BIS Locational banking statistics http://www.bis.org/statistics/bankstats.htm, Table 3B External loans and deposits of banks in individual reporting countries, In all currencies vis-à-vis the non-bank sector http://www.bis.org/statistics/qcsv/anx3b.csv

[8] Banks in Switzerland, http://www.snb.ch/en/iabout/stat/statpub/bchpub/stats/bankench

***Table 3**; Largest BIS reporting countries/jurisdictions based on foreign non-bank deposits*



Source: ibid

7. From this data the Commission has concluded that the use of intermediary structures is undermining the effectiveness of the Savings Directive. "This [the SNB data] confirms the urgent need to address such cases where intermediary structures in offshore jurisdictions are involved in the payment of savings income." This concern has led to the statutory recognition of entities or legal arrangements which are not subject to taxation in the member states where they are resident as Paying Agents Upon Receipt. Look through arrangements can oblige Paying Agents Upon Receipt to identify the beneficial owner. These measures are held to be required and necessary for the Directive and Savings Agreements to function properly.

8. On the one hand the Commission seems to suggest in some of its materials that the Savings Tax Directive is working well. In its Communication on "Concrete ways to reinforce the fight against tax fraud and tax evasion including in relation to third countries", published on 27 June 2012[9], the Commission says that "the experience of the Savings Directive demonstrates the benefits of such cooperation. **On average more than 4 million records are sent each year from source countries to residence countries representing on average 20 billion euro of savings income"**. (emphasis added).

9. On the other hand the Communication noted that the Commission's second review of the Savings Directive "confirms the widespread use of untaxed offshore structures interposed between the payer and the ultimate beneficiary in order to obscure the actual beneficial ownership. 35% of the non-bank deposits in member states (65% for deposits in Savings Agreement countries) are held by such structures located in offshore jurisdictions. The review also revealed that the market for structured financial products (€767.3 billion current outstanding amount of sales) has been increasing annually at more than 30% on average in recent years". This led the Commission to suggest that its proposals for amending the Savings Tax Directive, which have long

[9] COM (2012) 351

been stalled in the Council of Ministers, "are essentially agreed by member states and it is vital that these changes are now adopted without delay."

10. A coverage simulation on the data provided by the European Central Bank[10], to establish whether data provided by member states under the Directive reflected a satisfactory coverage of the potential tax base, found that 11 member states fell below a 70% benchmark. The report concluded that the data submitted by the paying agents is not of a satisfactorily high completeness.

11. So the Commission's economic analysis has shown that automatic exchange of information under the Directive, as it currently stands, is not working effectively. **This is accepted by the Commission in its conclusion that there is urgent need for reform, based on an extension of the Directive, to cover insurance products and the structured product market, as well as an adoption of measures to facilitate controversial look-through arrangements.**

12. The ECB coverage simulation led the Commission to conclude that "the results of the simulation exercise further support the need for member states to consider the use of systematic controls on the completeness of the data submitted by their paying agents."

13. In its report the Commission identified three key problems specifically concerned with the exchange of information system.

- Lack of integration with national tax databases
- Need for a manual process of cross checking
- Lack of collaboration between central tax administrations and the local collection offices

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14. Responses to the Forum's 2012 survey allowed us to estimate how far the problems associated with the exchange of information model have been tackled, in comparison with the withholding tax alternative.

15. Responses were received from Austria, Estonia, Germany, Ireland, Latvia, Lithuania, Luxembourg, Malta, Portugal and the United Kingdom. This level of response, approximately half the member states, is in line with the response rate to the EPF 2008 review.

16. Austria and Luxemburg continue to operate a full withholding tax system. Austria has provided up-to-date 2011 figures showing the payment the country has made to other jurisdictions arising from the operation of the withholding tax.

17. Notwithstanding the financial crisis, reductions in interest rates and the deterrent of the higher rate of withholding tax to 35% introduced under the EU Directive, the

[10] REGULATION (EC) No 2423/2001 OF THE EUROPEAN CENTRAL BANK of 22 November 2001 concerning the consolidated balance sheet of the monetary financial institutions sector (ECB/2001/13)

Austrian data shows a robust return in which sizeable revenue transfers continue to be made, as set out in Table 4

18. The uncomplicated nature of the withholding tax allows Austria to provide accurate and detailed figures. In accordance with the terms of the Directive, 25% of tax revenue generated is retained by Austria, with 75% transferred to the Treasuries of the other member states.

***Table 4**; Withholding tax receipts transferred from Austria*

Withholding Tax transferred from Austria

LAND	2006	2007	2008	2009	2010	2011
Aruba	311,81	751,61	1.467,69	3.311,32	253,06	170,59
Belgien	28.587,52	118.959,98	534.848,59	207.831,50	194.068,75	117.986,97
Bulgarien	-	-	119.377,13	157.165,14	148.974,88	81.955,16
Dänemark	9.723,61	35.390,63	47.700,18	305.694,60	56.214,25	38.120,37
Deutschland	6.837.738,51	33.036.864,69	42.356.649,33	54.241.342,36	47.194.421,39	37.998.500,61
Estland	3.089,60	13.318,70	63.151,92	21.428,14	18.807,66	19.489,48
Finnland	3.175,71	13.704,44	14.347,96	22.744,45	19.348,70	10.346,81
Frankreich	77.733,46	351.185,88	490.909,64	591.867,35	507.435,94	393.772,89
Griechenland	62.104,57	247.808,63	267.969,03	273.633,44	245.959,03	110.263,44
Guernsey	160,48	218,26	1.334,74	726,64	-	-
Isle of Man	8,53	54,79	60,47	-	5.072,82	7.452,68
Irland	8.665,51	36.941,31	42.430,87	46.237,43	37.360,98	27.951,08
Italien	1.101.138,39	5.340.418,77	7.161.361,19	9.928.077,24	9.291.841,83	4.298.044,37
Jersey	8,34	60,75	113,54	50,88	221,43	34,19
Lettland	8.974,15	30.630,08	17.012,08	22.270,29	23.773,80	10.108,67
Litauen	1.700,01	5.655,82	12.768,89	21.508,39	83.284,57	15.225,77
Luxemburg	6.657,26	15.514,38	20.981,76	43.949,25	25.966,68	18.643,14
Malta	9.566,27	19.564,97	22.293,94	20.381,06	18.828,86	20.918,53
Montserrat	2.659,49	8.315,90	-	9.774,80	-	-
Niederländische Antillen	4.522,00	15.633,05	1.837,02	3.442,62	6.188,07	918,85
Niederlande	156.518,47	575.522,33	662.260,20	954.681,98	829.772,59	513.141,16
Polen	61.053,50	263.326,87	325.622,72	399.167,64	333.145,43	238.614,99
Portugal	6.808,93	95.544,46	-	321.393,30	-	-
Rumänien	-	-	270.267,44	299.824,12	303.164,83	149.260,50
Schweden	54.057,25	234.337,37	326.207,39	449.617,16	396.070,87	263.281,81
Slowakische Republik	84.576,90	336.710,34	548.520,26	794.211,88	777.152,63	480.161,02
Slowenien	357.258,03	1.229.652,27	1.664.626,15	2.340.071,63	2.077.051,70	1.177.831,93
Spanien	73.751,17	296.867,48	399.364,00	528.825,69	507.949,13	348.978,28
Tschechische Republik	160.231,21	558.536,40	768.888,23	1.095.112,64	970.498,02	771.354,07
Ungarn	147.326,08	654.959,12	2.272.642,89	1.710.085,17	1.855.137,40	1.583.228,57
VereinigtesKönigreich	213.037,12	757.850,90	1.086.497,75	1.198.264,52	1.054.647,19	766.514,86
Zypern	8.607,10	21.037,66	28.041,75	47.831,10	24.309,02	14.600,30
Total	**9.489.750,98**	**44.315.337,84**	**59.529.554,75**	**76.060.523,73**	**67.006.921,51**	**49.476.871,09**

19. In contrast with this system, respondents to the Forum survey identified several continuing issues with automatic exchange systems which are outlined below.

The nature of the data exchanged prevents direct transfer of the data into national tax regimes.

20. **Austria** reports using the automatic system as a first step, before a manual follow up is required, where it is estimated that a third of the initial data received is non-attributable.

21. In **Estonia** savings income is not taxed therefore the authority reported no need to make use of the data.

22. With **Germany**, the data received by the Federal Central Tax Office (*Bundeszentralamt für Steuern*) is given the taxpayer's tax identification number and must be collated for forwarding to the federal states for the purpose of evaluation. The nature and scope of the evaluation is a matter for the federal states.

23. **Ireland** reported that information received must be manually matched with the relevant tax regimes and is then simply stored in the national data warehouse. Any relevant information can be retrieved manually using the Integrated Business Intelligence application to audit any suspected discrepancies.

24. **Latvia** responded that the data exchanged is simply stored for the purpose of cross checking Latvian residents' income declarations.

25. **Luxembourg**, which has experience of both systems under the Directive, similarly reported that the information received must be first validated, before being distributed to the local tax offices for attribution of the data to individual taxpayer records.

26. **Malta** outlined a three stage process, which entails firstly processing the information, secondly identifying material monetary sums that may need to be reviewed, and finally making use of the data in revenue risk assessment processes.

27. **Portugal** likewise reported that the information transferred can only be used for manual cross checks with the national tax database, with no direct assimilation into the national tax system.

28. The **United Kingdom** stated that "data received under the EUSD is not used automatically in tax assessments as there is no presumption that the data in exchange of reportable payments would match with income or gains for UK tax purposes calculated according to UK rules for personal taxation."

There is no effective utilisation of the data; the vast bulk of which lies redundant.

29. **Austria** revealed that it does not have any "detailed or reliable data as regards the percentage of actual use…From the data available we can however deduct that in 2008 in about 5% of the cases there were follow-up assessments."

30. No use of the data is required in **Estonia** given the absence of any corresponding tax within the national tax regimes.

31. In **Germany** the authorities only analyse data which falls outside defined risk parameters (e.g., frequency of foreign interest payments, amount of payments) and are identified for review. Federal reviews are made available annually at pre-arranged submission dates.

32. **Ireland** stated that data is evaluated only on a case by case basis manually, according to identified tax risk.

33. Similarly **Latvia** responded that it was impossible to evaluate the use of information exchanged as there is no systematic use of the data,

34. **Luxembourg** furthermore uses the data for verification purposes against individual declarations, though was unable to provide any detailed information as to the actual use of the data as a percentage of total tax assessments.

35. The systems in **Malta** do not record the number of cases identified from the data for review and so it is unknown to what extent there is effective use of the information.

36. In parallel with other member states, **Portugal** does not use the data is any systematic manner but on a case by case basis, and is unable to give any specific information on the number of cases.

37. Asked about whether it was possible to identify the number of cases and total tax recovered, where automatic information reported under the Savings Tax Directive led to the discovery of undeclared income, the **United Kingdom** replied that it does not keep separate statistical data about compliance interventions emanating from information received under the EU Savings Directive.

The quality of the information exchanged is poor and often prevents tax authorities from making use of the data.

38. The tax authorities in **Austria** noted that attribution of the data is such a time-consuming exercise that by the time the information is actually processed it may well no longer be up to date.

39. **Germany** replied that the quality was generally satisfactory but required more precise information about personal circumstances.

40. The poor quality of information has required **Ireland** to often seek mutual assistance before any decision to intervene from cross checks is made.

41. **Latvia** replied to say that the quality is often not sufficiently accurate to allow attribution of the data, especially given the widespread lack of use of TIN. “For instance we have 59 persons with name Janis Berzins and it is not possible to state which one is the right person.”

42. The quality of data has allowed **Luxembourg** to utilise the larger part of the data but there is still a significant amount which cannot be attributed to any individual.

43. The issue over failure to provide TINs was further highlighted as a major shortcoming by **Malta.**

44. **Portugal** similarly replied that there is a worrying lack of accuracy over the fundamental details, including the TIN and date of birth. Another issue highlighted was the failure to identify whether information was really taxed in the source country and if so to what amount.

45. Regarding the clarity of the information received, the **United Kingdom** considers that most information received from member states is generally found to be good and adopts the agreed standard format of FISC153, but there is a drawback: "as the reported payments will not necessarily equate with income or gains for UK tax purposes determined according to UK tax rules and may arise in periods that do not necessarily fit easily with UK tax years so it has to be considered carefully and may need to 'interpreted' before it can be used effectively in relation to UK personal tax".

46. It is clear from these reports that the mass of data received under the EU Savings Directive turns out to be of relatively small practical use in collecting tax. In practice it is the exception rather than the rule that significant use is made of it. A huge amount of information collected and circulated compares with little practical use made. This is highlighted most clearly in the estimated tax yields relating to the Anglo–Swiss withholding tax treaty. It is currently predicted that the agreement will secure the UK Treasury between £4 – £7 billion by 2015. This figure exceeds the €4.6 billion of total income reported to the UK by all other participating counties under Exchange for Information for the year 2010/11.

47. Furthermore to obtain these findings the European Policy Forum had to spend over 6 months contacting and pressing the tax authorities of member states. It is clear that the data is not readily available for disclosure and this undermines the major alleged benefit of the exchange of information system. The enhanced transparency that was supposed to follow the establishment of exchange of information has not materialised.

48. This lack of transparency is reflected in the recent trend of the EU Commission to keep secret the discussions regarding the Savings Tax Directive between member states and EU officials.

49. As already noted above, none of the highlighted shortcomings arise with the withholding tax regime, as all matters are dealt with at source. This would again suggest that the relative straightforwardness and certainty of a withholding tax makes such arrangements much more effective than an exchange of information.

50. Let us illustrate this point with a two-country example, a comparative analysis of revenue/data sent by **Belgium** before and after the adoption of automatic exchange of information at the end of 2009. The amount of tax revenue raised by other countries from savings accounts of their nationals in Belgium has slumped since Belgium swapped from the withholding tax regime to automatic exchange of information. For example, for fiscal year 2009 Belgium transferred €343,583 to Portugal under the withholding tax scheme. For fiscal year 2010, Belgium reported total interest payments to Portugal of €1,447,880; if this amount had been taxed at source it would have raised tax revenue of €289,576. However Portugal reported difficulties in attributing data to individuals and only uses the information to cross check tax returns on a case by case basis. So it is highly improbable that the actual amount of revenue to be raised (Portugal is still processing data from 2009) will even be close to this figure. As a result of the change, Portugal will receive significantly less revenue from Belgium.

Table 5; *Comparative figures of data/revenue transferred from Belgium to Portugal*

	Total 2009	Belgium 2009	Total 2010	Belgium 2010
Amount of withholding tax	6,183,428	343,583	585,663	0
Amount of interest payments	36,592,985	0	30,413,467	1,447,880
Amount of sale proceeds	59,882,839	0	53,441,817	3,155,600

51. The loss of revenue for member states which followed Belgium's transition to exchange of information is likely by extension to reflect a wider loss of revenue in respect of exchange of information as opposed to the withholding tax model. Table 6 outlines the potential revenue which would have arisen had a pan-EU withholding tax been in place across all member states.

52. Data from the EU Commission, recording the total value of information each member state received under exchange of information, enabled a calculation of the potential tax revenue. Table 6a outlines the potential revenue from a pan-EU withholding tax, at the transitory rates of 15% and 20%. Table 6b outlines the potential revenue at the current rate of 35%.

53. The tables highlight the billions of euros which could be raised from a withholding tax across all member states and reinforce the huge tax revenue potential for hard-pressed member states. In contrast to the exchange of information regime which hopes to improve tax revenues over the years, a withholding tax taxing savings income at source start to raise serious sums at once.

Table 6a; *Withholding tax revenue at transitory rates of 15% and 20%*

Potential Tax Revenue under Withholding Tax (at transitory rates of 15% and 20%)	**Austria 2008**	**Austria 2009**	**Austria 2010**
	40,055,599	55,007,456	75,642,053
	Estonia 2008	**Estonia 2009**	**Estonia 2010**
	277,871	465,412	711,017
	Germany 2008	**Germany 2009**	**Germany 2010**
	1,030,832,250	467,956,377	546,760,536
	Ireland 2008	**Ireland 2009**	**Ireland 2010**
	199,719,818	149,371,898	53,680,504
	Latvia 2008	**Latvia 2009**	**Latvia 2010**
	837,244	3,105,519	3,234,883
	Lithuania 2008	**Lithuania 2009**	**Lithuania 2010**
	632,126	3,866,214	11,277,133
	Luxembourg 2008	**Luxembourg 2009**	**Luxembourg 2010**
	86,380,364	51,559,890	11,277,133
	Malta 2008	**Malta 2009**	**Malta 2010**
	104,410,470	3,836,439	6,352,066
	Portugal 2008	**Portugal 2009**	**Portugal 2010**
	28,885,507	19,187,810	16,558,096
	UK 2008	**UK 2009**	**UK 2010**
	613,087,166	970,994,533	808,974,265

Table 6b; *Withholding tax revenue at current rate of 35%*

	Austria 2008	**Austria 2009**	**Austria 2010**
	93,463,065	96,263,049	132,373,593
	Estonia 2008	**Estonia 2009**	**Estonia 2010**
	648,367	814,471	1,244,280
	Germany 2008	**Germany 2009**	**Germany 2010**
	2,405,275,252	818,923,660	956,830,938
	Ireland 2008	**Ireland 2009**	**Ireland 2010**
	466,012,909	261,400,821	93,940,882
	Latvia 2008	**Latvia 2009**	**Latvia 2010**
Potential Tax Revenue under Withholding Tax (at current rate of 35%)	1,953,571	5,434,659	5,661,045
	Lithuania 2008	**Lithuania 2009**	**Lithuania 2010**
	1,474,960	6,765,874	19,734,983
	Luxembourg 2008	**Luxembourg 2009**	**Luxembourg 2010**
	201,554,184	90,229,808	23,333,380
	Malta 2008	**Malta 2009**	**Malta 2010**
	243,624,432	6,713,768	11,116,115
	Portugal 2008	**Portugal 2009**	**Portugal 2010**
	67,399,517	33,578,668	28,976,668
	UK 2008	**UK 2009**	**UK 2010**
	1,430,536,722	1,699,240,433	1,415,704,965

54. The figures above show that in 2010 each member state lost potential tax revenue to the average sum of £224,949,294. Going forward member states are foregoing approximate potential tax revenue to the average sum of £387,896,758.

55. Emphasising how this revenue is currently lost revenue and does not later materialise under exchange of information upon analysis of the data, Table 7 estimates the current amount of UK tax revenue from returned overseas savings. The figures are estimates based on the amount of income declared by UK individuals as no specific record is kept by HMRC. The ratios of each tax band are based on UK savings tax revenue.

Table 7; *2010/11 UK Tax Revenue from returned overseas savings income*

Amounts in Millions

	Starting rate	Basic rate	Higher rate	Additional rate	Total
Declared Overseas Savings Income	20.2	321	219	161.2	723
Tax Revenue from Overseas Savings Income	2.02	64.2	87.6	80.6	234.42

56. Therefore, while it was calculated in Table 6a that the UK could have received £808,974,265 from a pan-EU withholding tax for tax year 2010/11, actual estimated revenue from all overseas savings income, as shown in Table 7, was approximately a third of this amount. This substantial difference highlights the ineffectiveness and inefficiency of exchange of information.

57. In contrast, the UK has secured tax revenue of £25,497,816 in the past 4 years alone from the withholding tax in Jersey. Furthermore, data released by the tax authority for Jersey has confirmed that tax revenue increased 15% in the past year[11].

Bilateral Agreements

58. Not least because withholding taxes provide a more robust guarantee of receiving tax revenue over the past year a number of EU member states have been introducing new withholding tax regimes. Each of the bilateral agreements specifically confirm the withholding tax regimes to "have an enduring effect equivalent to the outcome that would be achieved through an agreement to exchange of information"[12]

Anglo – Swiss Tax Agreement

59. The agreement, signed on 20 March 2012, establishes a withholding tax regime between the two countries. According to Treasury figures the current forecast for the yield of the retrospective tax from the UK-Switzerland tax agreement is expected to be in the range £4 billion to £7 billion.

60. The concerns of the EU Commission regarding compatibility with EU law have been removed. The agreement remains in essence unchanged from the draft version published last October. The withholding tax provided for under the agreement should not be levied on interest payments insofar as a retention tax in accordance with the EU Agreement on the Taxation of Savings was levied (currently 35%). In this case, however, a final payment amounting to 13% is to be paid in addition to the retention tax.

61. A final withholding tax is due on investments of UK taxpayers in Switzerland, to correspond in terms of content to the UK's taxation of income and gains. The rates of the final withholding tax are in line with the United Kingdom's marginal tax rates on income and gains, and amount to 48% for interest income, 40% for dividend income, 27% for capital gains and 48% for other income.

62. In relation to retrospective taxation of previously untaxed assets, a one-off, flat-rate tax payment will be made anonymously. This will be forwarded to the UK tax authorities. In principle, the assessment basis is the capital present in Swiss accounts or deposits on a specific reference date in the past. The combination of an assessment basis and tax rate when calculating the tax will take into account how long the assets were held untaxed in Switzerland. The individual charge will then range from 19% to 34%. The

[11] http://www.gov.je/TaxesMoney/InternationalTaxAgreements/EUSD/Pages/RetentionTaxPayments2011.aspx

[12] Agreement between the Swiss Confederation and the UK on co-operation in the area of taxation, 6 October 2011;

calculation of this individual charge will be based on the duration of the client relationship as well as the initial and final amount of the capital. Anyone who does not wish to pay the one-off, flat-rate tax can consent to the disclosure of the data necessary for individual taxation to the relevant UK tax authorities. Whoever declares that they do not wish their untaxed assets in Switzerland to be taxed using a flat rate or taxed individually must close their accounts or deposits in Switzerland. Switzerland will provide aggregated data on this.

63. Inheritance is now covered by the agreement in order to eliminate a loophole. In the case of inheritance, the heirs must consent to either collection of a tax (at the marginal rate of 40%) or disclosure.

64. In order to combat "black money" a security mechanism is to be introduced, whereby HMRC can request for the Swiss authorities to verify whether an individual holds an account or deposit in Switzerland. However such a request may only be made where the UK authorities believe there to be unlawful activity, and an annual cap of 500 requests has been put in place.

German – Swiss Agreement

65. On the 5th April 2012 Germany and Switzerland signed a withholding tax agreement, which largely reflects the Anglo-Swiss agreement. The agreement is estimated to raise €10 billion according to German authorities. The principles and key measures of the agreements are identical, though there is a degree of variation as to the details.

66. German inheritance is to be taxed at a rate of 50% or disclosure.

67. The one-off flat rate tax for past investment is to range from 21% - 41%.

68. Requests for information over potential "black money" accounts are to be capped at 1300 per year.

69. Future income is to be taxed at 26.4%.

70. The agreement contains symmetrical legal structures as the UK agreement, with regard to ensuring no conflict with the EU Savings Tax Directive.

Austrian – Swiss Agreement

71. A week after the signing of the above agreement, Austria followed suit and finalised a symmetrical treaty. From the one-off retrospective tax alone Austria is expecting to raise around €1 billion. The agreement models the withholding tax regimes already in place with Britain and Germany, though again the details somewhat vary.

    - The rate for the one-off flat tax is between 15% and 38%.
    - Future income is to be taxed at 25%, to reflect the Austrian capital gains tax.
    - Inheritance is not taxed, as there is no such tax in Austria.
    - No additional enquiry possibilities have been agreed, given both countries are satisfied with current procedures

***Table 8**; Comparative table of Bilateral Agreements*

	United Kingdom	Germany	Austria
Tax on Past Income	19% - 34%	21% - 41%	15% - 38%
Future Income	48%	26.4%	25%
Inheritance	40%	50%	N/A
Requests for Information	Cap of 500 per annum	Cap of 1300 per annum	N/A

Greek – Swiss Agreement

72. The most recent member state to pursue the withholding tax approach is Greece, which is expected to sign a bilateral tax treaty with Switzerland. Greece's Deputy Finance Minister has commenced the last round of talks in Bern and while the details are yet to emerge the treaty is expected to heavily reflect the terms of the corresponding treaties with Germany and the UK, though with a withholding tax of 30%. According to calculations from Global Financial Integrity an estimated US $261 billion in undeclared money was transferred abroad from Greece between 2003 and 2011.

Other potential agreements

73. On 6 September 2012 Belgium's Foreign Minister, Didier Reynders, announced that the country was interested in negotiating a similar agreement with Switzerland. News reports have suggested that the agreement would involve a backdated one-off tax at the rate of 34% on the €30 billion investments held in Switzerland by Belgian residents, which would therefore net a substantial sum for Belgium; a 25% withholding tax would apply to future interest payments.[13]

74. The above bilateral agreements have wider implications for the balance between automatic exchange of information and withholding tax regimes. Firstly, the acceptance by the EU Commission of the legality of the existing agreements is expected to lead to numerous other member states following suit. Switzerland is looking to reach similar tax arrangements with its French and Italian neighbours, with working groups already established and meetings with French and Italian Presidents Francois Hollande and Mario Monti earmarked for later this year. Secondly, it challenges the EU Commission's attempts to enforce automatic exchange of information throughout EU member states.

75. These agreements, and the large sums of revenue to be raised from them, mark a major turning point in this field and effectively validate the withholding tax approach. Such a shift supports the EPF findings as to the problematic nature of exchange of information and reinforces the view of the EPF, that withholding tax regimes are the most effective approach to combating tax evasion.

[13] Agence Europe, 7 September 2012.

76. In the Autumn Statement 2012 the UK Chancellor, George Osborne, emphasised the effectiveness of the withholding tax approach, as developed in these bilateral treaties. "Next year, for the first time in our history, money will be flowing from bank accounts in Switzerland to Britain instead of the other way round. Because of the Treaty we've signed, we expect to receive £5 billion over the next 6 years from the undisclosed Swiss bank accounts of UK residents. It is the largest tax evasion settlement in British history."[14]

The Commission's current plans

77. However, having acknowledged the flaws of the exchange of information model, the report by the Commission completely overlooks the far simpler alternative of withholding tax regimes. This is notwithstanding the fact that the Savings Directive already accommodates withholding tax regimes for Austria and Luxembourg, and for all those non-EU states subject to the Savings Agreements.

78. Crucially the EU review highlighted data from the IMF Coordinated Portfolio Investment survey[15] which revealed that investment in Luxembourg, which applies the withholding tax rather than exchange of information, has significantly increased.

79. Instead of shifting towards the withholding tax approach which demonstrably works, the Commission is struggling to tighten an exchange of information system which is clearly not sufficient. In its Communication it says that "the Commission has developed computerised formats for saving income and is currently developing new formats for income covered by Directive 2011/6 in order to implement secure and enhanced automatic exchange of information within the EU".

80. The Commission is also planning the radical step of introducing for every European taxpayer a European Tax Identification Number. It says that "the Commission will therefore carry out an impact assessment with a view to proposing, where appropriate, a European taxation number assigned to each country engaged in cross-border activity. Giving member states' tax administrations direct access to relevant areas of each other's national databases together with an extension of the scope of automated access in the VAT area should also be envisaged".

81. These are far reaching proposals and it is far from clear whether a proper cost benefit assessment will suggest that they are as effective as a withholding tax system. Equally they mark a significant political extension of the Commission's role in the tax affairs of member states. Recent experience has suggested that not all member states are comfortable with such an expanded role and the continuing refusal of Austria and Luxembourg to agree to the Commission's further proposals for the Savings Directive may be an indication of difficulty ahead in this area too.

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[14] http://www.hm-treasury.gov.uk/as2012_statement.htm

[15] http://www.imf.org/external/np/sta/pi/cpis.htm; See also, **COMMISSION STAFF WORKING DOCUMENT, presenting an evaluation for the second review of the effects of the Council Directive 2003/48/EC, *Accompanying the document* REPORT FROM THE COMMISSION TO THE COUNCIL in accordance with Article 18 of Council Directive 2003/48/EC on taxation of savings income in the form of interest payments** {COM(2012) 65 final}, p.p. 57 - 67

82. Further radical plans include the Commission's development of a "taxpayers charter" which is intended to develop "motivation incentives in the form of voluntary disclosure programmes and encourage their tax payers to correct their errors spontaneously".

83. If taxpayers do not spontaneously correct their errors there is a suggestion that criminal sanctions will be introduced: "the Commission will propose rules to strengthen the fight against fraud affecting the EU financial interest by means of criminal law".

84. These measures are part of a rather dramatic aim to step up Europe's tax competence. The Commission's Communication complains, for example, that the OECD's global forum on Transparency and Exchange of Information for Tax Purposes does not consider the question of "fair tax competition", a principle which the EU upholds internally via the Code of Conduct for Business Taxation.

85. As previous Forum work has noted this Code of Conduct is a soft law non-treaty measure operated in secret by EU fiscal authority representatives, which seeks to stamp out low tax incentives and special regimes in member states by prohibiting new incentives and rolling back existing systems. As a result of such measures Europe's attraction for foreign direct investment looks highly problematic by contrast, for example, with Asian economies who widely employ tax incentives, as do the economies of the Gulf, the Middle East, and much of Latin America.

86. The Commission's Communication notes that it aims to present a tax action plan towards the end of 2012 and it is worth highlighting the radical nature of these measures;

> "The aim is to establish a set of measures, procedures and tools for co-ordinated actions. This could include a mix of defensive measures or sanctions for countries which practice unfair tax competition and incentives for those countries to see such practices. The Focus will be on co-ordinated measures. The Communication will also address issues of aggressive tax planning".

87. The Commission therefore seems to be threatening to declare war on internationally-competitive low tax countries with measures including sanctions. It is difficult to envisage all EU countries agreeing to such an approach, or indeed it being deployed against powerful economies of, for example, the BRIC countries. It is more likely to be used against smaller economies.

Conclusions

88. The EU Commission's 2011 review into the workings of the Savings Tax Directive highlighted serious continuing shortcomings with automatic exchange of information.

89. Research on Member State experiences of the Directive by the EPF has brought to light further problems with the exchange of information approach.

90. The exchanged information cannot be used in an effective way by fiscal authorities within the taxation process. This is also a general finding of the EC; in its report of March 2nd 2012, the Commission proposed in response to the weaknesses of the system the following "best practices": integration of a savings directive database with national tax databases; development of risk management and more automated

process of cross-checking the data; streamlining of the dissemination of data between central tax administrations and local collection offices.

91. In recent months there has been a move away from automatic exchange of information in favour of withholding tax regimes in bilateral tax treaties, not least because they hold out the promise of larger tax revenues achieved more simply, more quickly and less intrusively.

92. The Swiss withholding tax system guarantees the correct imposition of the revenues concerned. The studies suggest that banks are able to deliver outcomes which fiscal authorities are not able to carry out in the framework of the automatic information exchange.

93. The concrete gains and enhanced efficiency of a withholding tax regime provide a more effective alternative to automatic exchange of information, as a means of ensuring implementation of national tax claims while respecting the protection of bank clients' privacy.

94. The European Commission's current plans point in a different direction towards a more ambitious and intrusive system which, on the evidence, would probably collect less tax than a withholding tax system.