



# EU Savings Taxation Directive

One piece in the puzzle of cross-border tax policy

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**Five years after the Ecofin Council reached agreement on the Savings Taxation Directive, the European Commission has submitted a proposal on its extension.** The goal pursued by the Commission and a number of Member States remains the same – to eliminate or reduce circumvention and evasion of the payment of tax by private investors on their cross-border interest income.

**The prevailing political climate for more cooperation and exchange of information between the States has improved significantly in recent months.** A flurry of new bilateral agreements, initiatives at OECD level and further EU proposals for directives underscore the momentum that has gathered here. This has produced more change so far than in the previous 15 years, negotiations on amendment of the Savings Taxation Directive will presumably not drag on again.

**The Savings Taxation Directive in its present form has had limited impact,** both fiscally and on investors. However, owing to the difficult data situation there are problems with robust statements on the investor side.

**In addition to many technical modifications, the amending proposal focuses essentially on extending the scope of application of the Directive.**

Specifically, it is planned to broaden the definition of the term interest income and expand the group of 'persons' concerned. This will result in more administrative work and expense, but also in greater transparency.

**From an economic perspective, efficient cross-border taxation, i.e. capital export neutrality, should be the aim, with a view to avoiding distortions in investment decisions.** Broadening the Directive towards more equal treatment of different investment vehicles can therefore be appropriate.

**But despite all this cooperation and more intensive exchange of information, the EU must not lose sight of the limits and costs of such a policy.**

Government overdrive must not be permitted to hamstring individuals and businesses in their economic choices. Moreover, tax competition helps, in a positive sense, to confine government's fiscal acquisitiveness to a level in tune with its citizens' preferences.

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## Introduction

Five years after the Ecofin Council reached agreement on the Savings Taxation Directive and slightly more than three years since the legislation entered into force, the European Commission has submitted a proposal on its amendment. However, the Savings Taxation Directive is only one element of current endeavours by the majority of EU member states to enforce their right to charge tax beyond their internal borders. At present there are further initiatives, both by the EU and OECD, to improve cooperation between the tax authorities while also stepping up their battle against so-called 'tax havens'. The group of G20 countries has similarly increased the pressure on many 'tax havens' to transpose existing standards (such as those set by the OECD) into agreements and to provide for greater transparency and exchange of information. More has been achieved in this respect since January 2009 than in the previous 15 years. Germany has followed suit with a proposal for new national legislation.<sup>1</sup>

The purpose of the proposal to extend the scope of the Savings Taxation Directive remains the same, the primary concern being to close loopholes in the payment of tax on cross-border interest income by private investors and eliminate tax evasion. From an economic perspective, distortions in investment decisions resulting from tax considerations should be minimised. It was with this aim that the existing Directive was adopted. There are deliberately no provisions to harmonise either the taxation of interest income or the rates of taxation.

### 1. Core elements of the present Directive

#### Underlying principle

Adopted in 2003 but not for application until July 1, 2005,<sup>2</sup> the Directive follows the basic principle that individuals' interest income should be taxed in accordance with the laws of their country of residence. From an economic viewpoint, that can minimise distortions in investment decisions. For this, it is in principle necessary for the country of residence to be provided with information on the interest income earned in other EU Member States so that this can be recorded for income tax purposes and tax then charged on it.

#### Exchange of information

Information exchange is therefore currently the rule (in 24 of the 27 Member States) and is conducted as follows: The competent authorities in the Member States automatically issue details (consisting of at least the account number, identity, name and address as well as interest payments) on interest paid by the so-called paying agent (as a rule a bank) to the beneficial owner (the recipient of the interest).<sup>3</sup>

<sup>1</sup> See Steuerhinterziehungsbekämpfungsgesetz (January 2009) (German Act to Combat Tax Evasion). The United States rigorously asserts its right to charge tax beyond its national borders. Only recently it signed a bilateral Tax Information Exchange Agreement with Liechtenstein, which enters into force at the beginning of 2010. See Meier, G. in: NZZ. February 28, 2009

<sup>2</sup> The delay is explained by the many agreements required with dependent territories and third countries such as Switzerland and Liechtenstein on the introduction of equivalent measures (as a rule withholding tax).

<sup>3</sup> The States must provide information on this at least once a year. In Germany the Directive was transposed into national law by the Zinsinformationsordnung (Interest Information Ordinance). The Bundeszentralamt für Steuern (BZSt, Federal Central Tax Office) passes on information on EU citizens not resident in the Federal Republic who earn interest income at banks in Germany to the competent authorities of their relevant Member States.

<b>Transitional arrangement</b>	However, a transitional arrangement exists for three States – Austria, Luxembourg and Belgium. Belgium recently announced its intention to adopt the automatic data exchange system and amend the relevant agreements on this. During the transitional period the States are not obliged to provide information on interest payments. Instead they levy a withholding tax of at present 20%. As from July 1, 2011 the Directive stipulates a rate of 35%. 75% of the revenues generated are transferred to the Member State of residence of the beneficial owner, while the rest may be retained by the withholding state. The beneficial owner's Member State of residence must also ensure the elimination of any double taxation of the interest payments which might result from the imposition of this withholding tax. It can do so by crediting the withholding tax paid and reimbursing any excess tax withheld. However, beneficial owners may also opt to take part in the automatic information exchange regime in Member States that operate the withholding system.
<b>Transitional period</b>	The transitional period will not end until Switzerland, Andorra, Liechtenstein, Monaco and San Marino can guarantee effective and comprehensive exchange of information on interest payments. Additionally, the Council must decide unanimously that the USA has committed to providing information <sup>4</sup> on request. However, the countries concerned may also introduce automatic data exchange of their own accord.
<b>Scope of the Directive</b>	The scope of the Directive covers interest payments on debt claims, e.g. cash deposits, account balances, loans, bonds and income from investment funds that invest more than 40% of their assets in interest-bearing securities. It does not, however, comprise all other income from investment funds, dividends, certificates, interest on claims arising from life insurance contracts and pensions, certain transferable debt claims and also gains from shares, inter alia. The tax liability extends only to individuals but does not cover legal entities such as companies, foundations or trusts.

## **2. Further development of the Savings Taxation Directive**

### **2.1 Problems and general criticism**

<b>Long run-up to adoption</b>	The Directive's entry into force was preceded by protracted debate; the first drafts were tabled in 1989 and 1998 but failed to garner the support of all Member States. <sup>5</sup> Even the compromise represented by the Directive currently in force was achieved only after much haggling. The passage in Article 18 of the Directive instructing the Commission to report every three years on its practical operation and propose any amendments to the Council "that prove necessary in order better to ensure effective taxation of savings income and to remove undesirable distortions of competition" is not therefore surprising.
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So even at that time it was foreseeable – as far as the Commission and many, mainly large EU Member States were concerned – that the Directive would only be an initial step, given that its adoption was based on minimal consensus among the members. Does the Directive live up to its promise, or does it thus far represent no more than a political signal? The jury is still out with regard to its impact

<sup>4</sup> The OECD's model Agreement on Exchange of Information on Tax Matters is cited as the model for this. Cf. OECD, Tax Information Exchange Agreement (TIEA), see Box 2 in this paper for details.

<sup>5</sup> Cf. Kellersmann, Dietrich; Treisch, Corinna (2002), p. 249ff.

and effectiveness, particularly in terms of the effective protection against tax evasion that a number of states were looking for. Criticism, too, is sparked by different elements.

### Modest revenues in Germany

The tax revenues generated as a result of the Directive are on a modest scale. The example of Germany clearly illustrates that both revenues from withholding tax paid over (less than EUR 200 m, see Table 1) and the interest income declared (roughly EUR 1.5 bn, see Table 4) are of an order far removed from the dimensions quite frequently discussed. The latest available statistics from the Bundesbank, for example, show bonds held abroad by enterprises and private individuals alone – the interest income from which is subject to the Savings Taxation Directive at least for private individuals – worth a total of roughly EUR 435 bn.<sup>6</sup>

EU savings tax	Germany withholding tax revenue from abroad – hardly a torrent					
	2005		2006		2007	
	Amount of withholding tax in €	Share of total revenue in %	Amount of withholding tax in €	Share of total revenue in %	Amount of withholding tax in €	Share of total revenue in %
<b>EU Member States:</b>	20,891,950	54.80%	75,799,590	52.47%	107,893,014	55.15%
Belgium	1,158,274	3.04%	2,960,697	2.05%	4,059,269	2.08%
Luxembourg	12,895,938	33.82%	49,465,366	34.24%	61,477,095	31.43%
Austria	6,837,739	17.93%	23,373,527	16.18%	42,356,649	21.65%
<b>EU third countries:</b>	16,551,020	43.41%	67,534,374	46.75%	86,502,850	44.22%
Andorra	23,482	0.06%	99,583	0.07%	127,961	0.07%
Liechtenstein	1,191,151	3.12%	4,398,953	3.05%	5,516,838	2.82%
Monaco	88,803	0.23%	331,864	0.23%	0	0.00%
San Marino	6,794	0.02%	15,025	0.01%	23,600	0.01%
Switzerland	15,240,791	39.97%	62,688,949	43.40%	80,834,451	41.32%
<b>Depend. and assoc. regions:</b>	684,218	1.79%	1,120,427	0.78%	1,229,055	0.63%
British Virgin Islands	47	0.00%	69	0.00%	8	0.00%
Islands	0	0.00%	0	0.00%	0	0.00%
Guernsey	86,913	0.23%	318,154	0.22%	325,151	0.17%
Jersey	270,179	0.71%	802,204	0.56%	903,896	0.46%
Isle of Man	327,079	0.86%	0	0.00%	0	0.00%
Netherlands Antilles	0	0.00%	0	0.00%	0	0.00%
<b>Total</b>	<b>38,127,190</b>	<b>100.00%</b>	<b>144,454,391</b>	<b>100.00%</b>	<b>195,624,918</b>	<b>100.00%</b>

Sources: Federal Ministry of Finance, Börsenzeitung

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### Debate on extending scope of the Directive

Attention therefore focuses on extending the scope of the Directive. Aspects specifically under discussion include widening the group of beneficial owners and also broadening the definition of interest income in the Directive. This is explained on the grounds that only a small range of interest and savings income is currently covered, making the Directive relatively easy to circumvent.<sup>7</sup> There are also calls to expand the territorial scope of application by establishing an information exchange system with further non-EU states (e.g. USA,

<sup>6</sup> See Bundesbank (2009).

<sup>7</sup> See for example the empirical research by Klautke and Weichenrieder. With reference to the development in premiums on certain securities not covered by the Directive they demonstrate that significant possibilities for evasion exist and are used. In their estimation the Savings Taxation Directive is therefore of little relevance to investors. See Klautke, Tina; Weichenrieder, Alfons (2008).

**Capital export-neutral taxation should be the aim**

Hong Kong and Japan) and extending the existing agreements with third countries.

However, the Savings Taxation Directive expressly does not touch on bank secrecy, which forms part of the Proposal for a Council Directive on administrative cooperation in the field of taxation presented in February 2009 (see Box 1, p. 10). Criticism is also levelled at the not inconsiderable work that the Directive involves for financial institutions. Even in the absence of practically any robust statistical material on this, an expansion in scope will lead to extra time and effort on information gathering.<sup>8</sup>

Economically speaking, i.e. from an efficiency aspect, preference should be given to capital export-neutral cross-border taxation.<sup>9</sup> That requires enforcement of the residence principle and the taxation of world-wide income, or at least their maximum possible realisation. It means the tax authorities must have information on the income of residents abroad, which is usually very difficult to ascertain. In the context of the Savings Taxation Directive it presupposes individuals' tax honesty about their income outside their country of residence and/or increased control density. The Directive assumes here that all is not well with regard to tax honesty.<sup>10</sup> Information exchange is by all means welcome from an efficiency aspect as it increases transparency and can make competition fairer.

It is important to note that the general introduction of information exchange may reduce the attraction for foreign investors. Countries' interests in introducing systems of this kind therefore vary. An automatic incentive to gather information and offer it to other states exists only if the country itself requires information from other states. A unilaterally cooperative attitude towards other states makes sense only if the states are identical (i.e. it does not matter to investors where they invest their capital). But if, as in the EU, this is not the case, the states' interests differ and the introduction of central regulation becomes necessary.<sup>11</sup>

In the light of this, regulation at the European level makes sense. But in practice, as with all Directives, the concept of the Directive itself is part of the problem. The necessity of transposing it into national law always leaves the Member States a certain amount of implementation and interpretation scope. In the context of subsidiarity – i.e. in this case broad deference to national circumstances – this is by all means sensible. However, through (greater or lesser) exploitation of this scope in the process of national implementation the Member State may enhance its attraction unilaterally to its own benefit.

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<sup>8</sup> A survey of the European Banking Federation by the European Commission (40 banks were polled from 6 Member States) arrives at average costs of EUR 2 m per unit (and EUR 100,000 running costs per unit). The term unit refers to the paying agent. More than one unit may act as a paying agent within a single bank. See European Commission 2008 [SEC(2008)2767], pp. 10ff.

<sup>9</sup> See Homburg, Stefan (2007), pp. 271ff and pp. 307f. The residence principle in conjunction with the world-wide income principle guarantees efficient allocation of resources, because only then is capital export neutrality given.

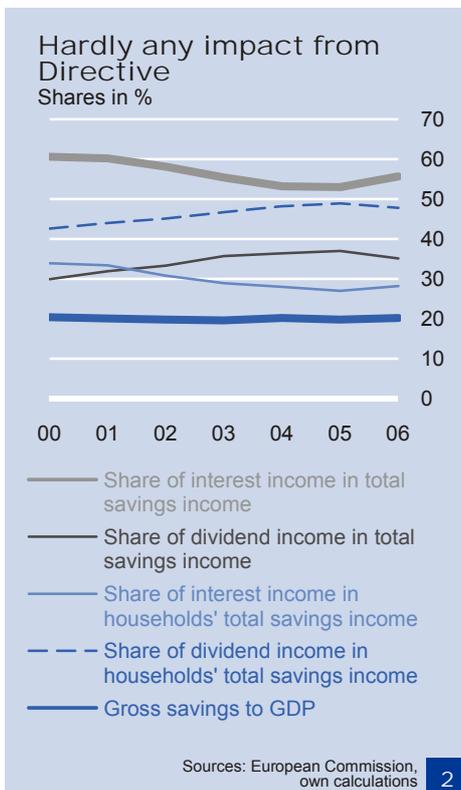
<sup>10</sup> Recent research on tax evasion clearly indicates that stepping up pressure always produces two opposite effects. While it does increase the likelihood of detection, it may also have a negative influence on tax morale, which in turn encourages tax evasion. For a more detailed examination of this see Gläser, Lars; Halla, Marin (2007), particularly pp. 86-89.

<sup>11</sup> See *ibid.* pp. 96f. In effect net capital exporters (i.e. net importers of information such as Germany) will benefit more from the exchange of information than net capital importers.

**EU working group since 2005**

**Comprehensive report September 2008**

**Commission recommends extending Directive scope**



**2.2 (Empirical) evaluation of the Directive**

The Savings Taxation Directive currently in force provides for the Commission to prepare a report every three years on the Directive's operation and to submit proposals on any amendments that may prove necessary to make it work more efficiently. For this purpose, various working parties have been formed since the end of 2005 (usually consisting of representatives from the Member States' tax administrations) to discuss the various aspects of the Directive. In addition to experts from the Commission, a group of business representatives was also engaged in reviewing the Savings Taxation Directive.<sup>12</sup>

In April 2008 a fairly comprehensive interim working document was published<sup>13</sup>, incorporating the results of the working groups. This was followed in September 2008 by presentation of the comprehensive report on evaluation of the effects of the Directive (accompanied by an extensive working document from the Commission Services with a statistical appendix).<sup>14</sup>

The bottom line is hardly surprising: The Savings Taxation Directive is very easy to circumvent, particularly by using interposed investment vehicles (such as foundations and trusts) and by restructuring investment portfolios (into certain financial instruments, particularly life insurance contracts, equivalent to those already explicitly covered) so that income does not constitute the payment of interest as defined in the Directive. Criticism is further directed against the failure sometimes fully to understand and apply the Directive and against the absence of some key statistics.

The data limitations are a general problem in reviewing the Directive. Even the Commission currently has only very limited possibilities for analysis at its disposal.<sup>15</sup> In its report the Commission attempted to examine income from investments covered by the Directive and the effects of the Directive on different types of investment. On balance it can establish no significant change in the composition of savings income. The shares of interest income in total savings income and interest income in households' total savings income have both dropped only marginally; conversely the shares of dividend income have climbed slightly.<sup>16</sup> Gross savings as a percentage of GDP have held stable at around 20%.

The Commission also had some access to bilateral data from the Bank for International Settlements (BIS).<sup>17</sup> These show a slight shift in non-bank deposits from states applying the Directive to third countries – although this was already evident ahead of the Directive's entry into force.

<sup>12</sup> Working documents, agendas and summary presentations of the results of the various working parties can be found on the website of the Directorate General Customs and Taxation Union. See DG Taxation (2009).  
<sup>13</sup> See European Commission (2008a), [SEC(2008)559].  
<sup>14</sup> See European Commission (2008b), [COM(2008)552] and European Commission (2008c), [SEC(2008)2420].  
<sup>15</sup> Many Member States do not, for example provide any information on the amount of the taxpayers' foreign and domestic interest income (which these state in their returns), the number that provide information or those that opt for withholding tax. Moreover, they typically specify only the total amount of withholding tax and the total number of reports issued since 2005. What is more, longer time series are available only for items that cover a scope larger than that of the Directive. As a result there is no ideal benchmark available.  
<sup>16</sup> For the following particulars see European Commission (2008c), [SEC(2008)2420], pp. 3f.  
<sup>17</sup> However, not all Member States report to the BIS and some of the BIS reporting countries did not agree to the use of BIS data.

### Tax revenues of withholding tax countries\* in € m

	Q2 2005	2006	2007
<b>EU Member States:</b>			
Austria	9,48	44,32	n.a.
Belgium	7,51	19,61	25,92
Luxembourg	35,90	124,59	153,00
<b>EU third countries:</b>			
Andorra	3,50	12,77	n.a.
Liechtenstein	1,94	7,08	n.a.
Monaco	3,75	11,70	n.a.
San Marino	1,13	7,47	n.a.
Switzerland	77,23	255,92	n.a.
<b>Dependent and associated regions:</b>			
Brit. Virgin Islands	0,00	n.a.	n.a.
Turks and Caicos Islands	0,01	0,02	n.a.
Guernsey	4,93	16,83	n.a.
Jersey	13,26	32,15	n.a.
Isle of Man	13,26	20,35	n.a.
Netherlands Antilles	n.a.	n.a.	n.a.

\*Tax revenues shared with EU Member States by countries that impose a withholding tax on interest payments

Source: EU Commission, 2008 **3**

## The Commission proposes extending

... the definition of interest ...

... and the 'persons' affected

With regard to the total payment flows triggered by the Directive, data is now available for the first time for the whole of the EU on interest income and withholding tax revenues declared by the EU States. It shows a rise in interest income and withholding tax revenues, with Germany, Italy and the United Kingdom registering the highest receipts. Switzerland and Luxembourg were the major sources of this revenue. Unfortunately, however, a massive problem with the data is also evident here in that there are huge gaps.<sup>18</sup>

On the basis of the data available, the Directive has therefore had hardly any impact on the capital market or savings. From a fiscal perspective, the revenue generated has been limited. The Directive has worked within its limited scope, but the billions' worth of revenues some politicians had hoped for have not been realised. Ultimately, the Directive in its present form should therefore be seen more as a political signal for closer cooperation and information exchange among the tax administrations.

### 2.3 The proposal by the European Commission

In essence, the November 2008 proposal for an amending Council Directive<sup>19</sup> consists of broadening the definition of interest income and extending the group of 'persons' coming under the Directive (i.e. expanding the paying agents' obligation to cooperate). But there are no plans to extend the Directive indiscriminately to cover all cross-border payments (i.e. also dividends, capital gains and payments from pension insurance systems, for example), as some Member States have demanded.<sup>20</sup> Nor are all legal structures to be included across the board.

Specifically, in extension of the definition of interest it is proposed to classify income deriving from securities that are, or can be regarded as, equivalent to debt claims as interest payments coming within the scope of the Directive (notably if the return on capital is fixed and at least 95% of the capital invested is returned to the investor, i.e. crucially in the case of financial innovations).<sup>21</sup> This is also to apply to certain life insurance contracts (particularly if their performance is fully linked to interest or equivalent income within the meaning of the Directive and risk coverage is lower than 5% of the capital invested). It is also planned to treat – and thus tax – income from investment funds (inasmuch as they come within the scope of the Directive) equally, irrespective of the funds' legal form. This would do away with the different treatment of UCITS (Undertakings for Collective Investment in Transferable Securities) and non-UCITS.

As far as an extension of the group of 'persons' affected is concerned, the following is planned: Where a paying agent (as a rule a bank) established in the EU pays interest to certain intermediate structures listed in Annex 1 of the Directive (most notably foundations and trusts) outside the EU, the paying agent shall also apply the provisions of the Directive (i.e. withholding tax levy or information exchange) to this. This is conditional on the beneficial owner as defined in the Anti-Money Laundering Directive

<sup>18</sup> See Table 3 and 5. The regression analysis attached in addition to the Commission's descriptive analysis is not therefore particularly informative, and the result should be interpreted very carefully. It shows no statistically significant and robust effect from the Savings Taxation Directive on either the level of private households' interest income or the share of interest income in total household income.

<sup>19</sup> See European Commission (2008e), [COM(2008)727 final].

<sup>20</sup> See European Commission (2008g), [SEC(2008)2768], particularly p. 8.

<sup>21</sup> See here and in the following amendments to Articles 4 und 6, European Commission (2008e), [COM(2008)727 final].

## Transparency may help make tax competition fairer

### Box 1

#### Commission proposals on administrative cooperation in the field of taxation

At the beginning of February 2009 the Commission adopted two new Proposals for Directives designed to replace and expand the 1977 Mutual Assistance Directive.

The aim is better collaboration between the tax administrations of the Member States, i.e. greater exchange of information across the Union's internal borders. Clearer and more precise rules (e.g. rules of procedure, common forms) and more direct contact between central, and also local, authorities are envisaged (e.g. the establishment of central liaison offices). Both automatic and spontaneous exchanges of information are to be made possible, and even the cross-border deployment of tax administration officials is provided for. It is expressly stated that in future information may not be refused on the grounds of any bank secrecy that may exist. Moreover, a Member State may not refuse information to, or collaboration with, another State such as the Member State grants to a third country.

The Commission also wishes to achieve a general improvement in mutual assistance with the "recovery" of taxes, duties and other measures. This means, for example, that compulsory social insurance contributions will also be recovered. It is additionally planned to prescribe spontaneous exchanges of information on tax refunds to non-residents by national tax authorities and likewise to enable representatives of administrative authorities to carry out investigations outside the territory of their own Member States.

See European Commission (2009a),[COM(2009)29] and European Commission (2009b),[COM(2009)28].

being known to the paying agent and being a private individual. For payments to intermediate structures established in the EU a modified concept of the so-called 'paying agent upon receipt' is applied. For this, too, a 'positive' list is scheduled.<sup>22</sup> The structures specified there must also apply the Directive (by levying withholding tax or exchanging information) if they receive interest payments from an upstream unit (irrespective of whether this is from within or outside the EU).

The amendments to Articles 4 and 6 of the proposal mentioned here constitute the most important points. Additionally, many technical amendments are proposed with a view to simplifying application of the Directive (e.g. definition of residence, remarks on implementation and also statistical reporting requirements incumbent on the Member States).

Implementation of the proposals would thus quite considerably broaden the scope of the Directive and presumably close a number of loopholes for the tax authorities. While this comes at the cost of significantly more work, it does increase transparency. The latter would be welcome in the context of fairer tax competition. We must not forget, though, that the agreements with third countries would also have to be revised to incorporate the amendments. And that would be anything but easy.

### 3. Further initiatives – the air is getting thinner (for 'tax dodgers')

The proposal on amendment of the Savings Taxation Directive cannot be viewed in isolation. Since the beginning of 2009 in particular, there has been a lot of movement at various levels on issues of cooperation between states in tax collection. In addition to national measures in individual states or bilateral negotiations, efforts are also being stepped up at the OECD level, not least through G20 initiatives like the recent one in London. 'Different-coloured' lists were drawn up and amended again there, undertakings given on information exchange and assistance with tax evasion and fraud, and a number of bilateral agreements concluded between different countries. How do these initiatives differ?

This activity was triggered partly by revelations of serious cases of evasion in various European states and the very decided attitude of the US tax administration over the past two years. To date it has renegotiated a raft of double taxation agreements with countries in Europe (such as Switzerland and Liechtenstein) and extended the exchange and provision of information in the process.

To complement the Savings Taxation Directive, in February 2009 the European Commission submitted another two proposals for better administrative cooperation and mutual assistance in the field of taxation (see Box 1). Were both to be implemented, bank secrecy for non-residents would effectively be almost completely abolished. The additional passage on third countries contained in the proposal (i.e. that a Member State may not refuse to provide to another State the information or cooperation that it grants to a third country) must be seen above all in the light of the US agreement policy. Ultimately

<sup>22</sup> Essentially these are trusts and foundations in the Member States that manage assets and do not pursue any charitable objectives. But in Germany these also include, for example, KG (limited partnerships) and OHG (commercial partnerships). The list is not exhaustive, amendments may be made to it and the Member States must complete it themselves subject to certain criteria (e.g. exemption of the structure from taxation).

## Article 26 OECD Model Convention as the standard

### Box 2

#### DTA and TIEA – what's what?

When taxpayers obtain income from abroad they usually face charges to tax from two countries, one from the source country and one from the country of residence. To avoid double taxation of the income most countries have therefore concluded bilateral instruments, known as double taxation agreements (DTA) to apportion the charge to tax according to specific methods. Such (international) agreements generally regulate the entire spectrum of government revenues. As a working basis the OECD has drawn up a Model Convention, which is adapted from time to time. The present Model Convention also contains a template on a potential exchange of information (Article 26, last revised in 2005). The model does not, however, impose an obligation on contracting states to include this passage in the wording of their agreements. Most countries maintain bilateral DTA. As a rule negotiations on these instruments drag on for years and subsequent amendments are generally extremely laborious.

In contrast, Tax Information Exchange Agreements (TIEA) are confined to the exchange of information on tax matters. In this respect, however, they go into much more detail than DTAs. TIEAs are also based on an OECD model and are generally used by countries that have not negotiated comprehensive DTAs. See OECD (2009c).

the proposal sets out to overcome to a certain extent the internal borders between the national tax jurisdictions, although only as far as the tax authorities are concerned. On the taxpayer side there would be little change in the 27 tax systems with which they are confronted.<sup>23</sup>

Mainly in response to pressure from the G7 and G20 countries, efforts by the OECD towards more transparency and information exchange (i.e. against tax evasion and hence so-called 'tax havens') have also received fresh impetus. The key starting points here are Article 26 of the OECD's Model Convention (to avoid double taxation) and the so-called Tax Information Exchange Agreements (TIEA, see Box 2). Both instruments can serve countries as the basis for bilateral or multilateral agreements. Article 26 of the OECD Model Convention in particular sets out certain minimum requirements on the mutual exchange of information, e.g. the provision of information on tax issues on request. In debate so far, individual countries' compliance or non-compliance with these provisions has determined whether the country is labelled a 'tax haven' or not.

The G20's April 2009 initiative focussed on tightening up the criteria as a whole and trying to exert greater pressure by drafting a new list of 'tax havens'.<sup>24</sup> Since the beginning of 2009 a whole range of new declarations of intent have been published and new agreements inked.<sup>25</sup> For instance, Jersey, Guernsey, the Isle of Man and Belgium recently signed up to agreements with Germany on tax information exchange.<sup>26</sup> In these accords they stated their willingness to provide the necessary information for taxation purposes to the German tax authorities on request.

An illustration of action at the national level is Germany's January 2009 draft Steuerhinterziehungsbekämpfungsgesetz (German Act to Combat Tax Evasion). Following various revisions, the draft has entered the legislation process, but the decision has not been taken yet. The scope of the Act is still subject to controversy.<sup>27</sup> The draft would grant the authorities sweeping powers to bring pressure to bear to obtain information in the event that a country does not meet the OECD standard on administrative assistance. The intention is to impose sanctions on business relations in countries with which no agreement on information exchange subject to Art. 26 of the 2005 OECD Model Convention exists (as is regularly the case with countries that have DTA). Specifically, this would mean that certain tax regulations would not be applied in part or in full to business relations with certain countries, e.g. limiting tax deductions for business or income-related expenses (or having to comply with further requirements to furnish evidence). Moreover, private individuals would be subject to much-broadened requirements on

<sup>23</sup> In view of this it is astonishing that the proposal for a Common Consolidated Tax Base is no longer a subject of discussion. See Zipfel, Frank (2007), Deutsche Bank Research, EU-Monitor 49.

<sup>24</sup> The OECD list revised and published in April was based, for example, on the requirement that a country must have concluded at least 12 agreements complying with Art. 26 of the OECD Model Convention in order to avoid being blacklisted. See OECD (2009a). Under political pressure from China, however, Macao and Hong Kong were not listed from the outset.

<sup>25</sup> See the announcements on the OECD website (2009b), according to which Andorra, Hong Kong, Liechtenstein, Luxembourg, Macao, Monaco, Austria, Switzerland and Singapore have announced their intention of concluding agreements.

<sup>26</sup> See announcement by the Federal Ministry of Finance [FMF] (2009a).

<sup>27</sup> See Federal Ministry of Finance (2009b).

cooperation and compulsory record-keeping on capital investments abroad and audit rights extended. However, this extremely far-reaching draft bill overshoots the mark as it would lead to the disclosure of practically all of a company's business relations and would in principle make suspects of all taxpayers. And what is more, it would likely cause the companies concerned – not to mention the banks – considerable expense.

#### 4. Conclusion

The Savings Taxation Directive can be seen as part of a puzzle or a package of measures enabling countries to enforce their right to charge tax beyond their national borders. Extension of the Directive is certainly sensible in terms of more equal treatment of different forms of investment. Efficient cross-border taxation is guaranteed chiefly by securing capital export neutrality, i.e. through the taxation of world-wide income and in the country of residence. For this the tax authorities require information on income earned abroad, which is usually very difficult to ascertain. They are reliant on the taxpayer's cooperation and/or increased control density. Both have their upsides and downsides. It is clear that extreme versions (no control at all vs. the totally transparent citizen) are not the answer. The solution lies somewhere in between.

#### **Savings Taxation Directive part of a package of initiatives**

#### **More cooperation between countries on tax matters**

Just lately, there are signs of greater cooperation and collaboration between national jurisdictions on tax information exchange. In many countries (including Switzerland, Belgium and Liechtenstein) broad debate has been set in motion, already leading to some rethinking. Countries that have largely refused to cooperate so far are quite rightly in for some problems (in the context of fair tax competition). One very important driver here is the ongoing financial market crisis and its indirect fallout on public budgets, making governments increasingly unwilling to countenance the erosion of their tax take through international tax avoidance and evasion while simply sitting on their hands. This is turning measures to combat tax evasion at the international level into a key issue. As a result, it is clearly emerging, particularly in Europe, that the days of banking secrecy (for non-residents) in its strict form are very likely numbered where it runs counter to justified requests from the tax authorities for information on capital income. Generally speaking, better cooperation – particularly on tax matters – is quite welcome. At the level of the EU, and also beyond, the necessary information exchange needs to be formalised through multilateral agreements (between several EU states and also together with third countries).

#### **Little acceptance for go-it-alones**

However, go-it-alone initiatives will not promote closer cooperation. As a rule national efforts of this kind do not produce the desired effect; on the contrary, they tend to spark greater resistance. They are far better embedded in joint campaigns (e.g. EU, G20 countries etc.). Without broader consensus little acceptance is likely, most certainly not beyond Europe.

#### **No decades-long negotiations again**

As far as the time frame is concerned, the negotiation process on the Savings Taxation Directive is unlikely to be concluded this year. But given the altered political climate, it is scarcely likely to take another ten years before the states have negotiated a new compromise. At present much appears possible that would have looked extremely unlikely only last year. It must be borne in mind, though, that if Article 26 of the OECD Model Convention on the extension of information exchange were established internationally, expansion of the scope of the Savings Taxation Directive would lose much of its relevance.

**State must not overshoot the mark**

But despite all this cooperation and exchange of information, individuals, companies and government must consider the costs involved and, most importantly, the limits. On the one hand is the issue of state intrusion into the individual's private sphere. Government must not overstep the mark and force people to disclose everything, as this would seriously stultify economic development. Then there is the question of government's urge to steadily increase budgets. Fair tax competition is a useful way of curbing government acquisitiveness. Competition of this kind is not rendered intrinsically unfair just because it is conducted through tax rates. And it must be viewed separately from the issue of aiding and abetting tax avoidance. A tax cartel that paralyses fair tax competition does a disservice to both private individuals and businesses.

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## Information provided to and by Germany over the years (receipts 2005/2007)

Country	Interest information to DE in € total per country	Share of total revenue in %	Interest information provided by DE in € total per country		Share of total revenue in %	
			2006	2008	2006	2008
<b>EU Member States</b>	1,444,167,361	96.91	1,546,780,561	1,192,365,077	1.00	99.8
Austria	- <sup>1</sup>	- <sup>1</sup>	122,371,502	233,287,655	7.89	19.5
Belgium	- <sup>1</sup>	- <sup>1</sup>	133,537,901	55,501,963	8.61	4.7
Bulgaria	-	-	-	5,072,982	-	0.4
Czech Republic	839,893	0.06	19,610,862	27,783,553	1.26	2.3
Cyprus (Greek part only)	152,947	0.01	5,227,076	6,922,732	0.34	0.6
Denmark	-	-	7,314,666	14,361,508	0.47	1.2
Estonia	29,283	0	154,855	234,601	0.01	0.0
Finland	42,995	0	3,973,441	4,828,638	0.26	0.4
France	44,888,250	3.01	154,227,379	131,609,878	9.95	11.0
Greece	409,929	0.03	25,587,739	49,991,368	1.65	4.2
Hungary	3,869,061	0.26	14,620,919	16,327,413	0.94	1.4
Ireland	29,218,762	1.96	8,177,730	9,772,154	0.53	0.8
Italy	49,698,253	3.33	68,431,158	100,686,611	4.41	8.4
Latvia	39,193	0	818,408	1,068,361	0.05	0.1
Lithuania	36,281	0	639,244	1,241,827	0.04	0.1
Luxembourg	683,649,151	45.88	24,827,768	25,531,333	1.60	2.1
Malta	49,430	0	32,297,771	4,254,091	2.08	0.4
Netherlands	13,631,801	0.91	56,707,130	106,719,131	3.66	8.9
Poland	1,865,775	0.13	10,465,536	15,191,442	0.68	1.3
Portugal	-	-	17,106,537	15,412,976	1.10	1.3
Romania	-	-	-	8,852,837	-	0.7
Sweden	706,053	0.05	21,323,712	29,581,740	1.38	2.5
Slovakia	538,770	0.04	2,450,141	4,016,551	0.16	0.3
Slovenia	192,889	0.01	4,689,204	7,534,791	0.30	0.6
Spain	152,567,301	10.24	279,397,374	143,771,936	18.02	12.0
United Kingdom (incl. Gibraltar)	461,493,939	30.97	532,822,508	172,150,654	34.37	14.4
<b>EU third countries:</b>	43,002,712	2.89	-	-	-	-
Andorra	- <sup>1</sup>	- <sup>1</sup>	- <sup>1</sup>	- <sup>1</sup>	- <sup>1</sup>	- <sup>1</sup>
Liechtenstein	989,967	0.07	- <sup>1</sup>	- <sup>1</sup>	- <sup>1</sup>	- <sup>1</sup>
Monaco	177,295	0.01	- <sup>1</sup>	- <sup>1</sup>	- <sup>1</sup>	- <sup>1</sup>
San Marino	-	-	- <sup>1</sup>	- <sup>1</sup>	- <sup>1</sup>	- <sup>1</sup>
Switzerland	41,835,450	2.81	- <sup>1</sup>	- <sup>1</sup>	- <sup>1</sup>	- <sup>1</sup>
<b>Dependent/assoc. territories:</b>	3,065,980	0.21	3,547,019	1,217,474	0.23	0.1
British Virgin Islands	-	-	20	4,410	0	0
Turks and Caicos Islands	-	-	- <sup>1</sup>	- <sup>1</sup>	- <sup>1</sup>	- <sup>1</sup>
Guernsey	339,447	0.02	1,512,419	364,722	0.10	0.03
Jersey	1,547,454	0.1	538,739	740,873	0.03	0.06
Isle of Man	914,178	0.06	187,283	97,285	0.01	0.01
Netherlands Antilles	-	-	1,305,651	129,405	0.08	0.01
Anguilla	103	0	- <sup>1</sup>	- <sup>1</sup>	- <sup>1</sup>	- <sup>1</sup>
Cayman Island	229,984	0.02	- <sup>1</sup>	- <sup>1</sup>	- <sup>1</sup>	- <sup>1</sup>
Montserrat	192	0	1,761	-	0	-
Aruba	34,623	0	1,146	10,184	0	0
<b>Total</b>	<b>1,490,236,053</b>	<b>100</b>	<b>1,550,327,580</b>	<b>1,193,582,551</b>	<b>100</b>	<b>100</b>

<sup>1</sup>) no interest reports planned

Sources: Federal Ministry of Finance, BZSt

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Interest income\* reported by countries with automatic data exchange – Modest total in difficult data situation  
in € m

	Q3 & 4 2005	2006	2007
<b>EU Member States:</b>			
Austria	-	-	-
Belgium	-	-	-
Bulgaria**	-	-	1,54
Cyprus	5,26	15,05	25,54
Czech Republic	2,92	17,81	26,75
Denmark	n.a.	415,31	6,931
Estonia	n.a.	4,40	n.a.
Finland	26,02	60,93	n.a.
France	568,14	2.020,04	n.a.
Germany	660,73	1.392,06	942,09
Greece	6,85	23,11	n.a.
Hungary	62,03	5,22	n.a.
Ireland	258,88	771,00	1.901,24
Italy	280,53	1.615,92	n.a.
Latvia	0,18	0,66	n.a.
Lithuania	0,09	0,09	n.a.
Luxembourg	1.119,79	4.188,68	n.a.
Malta	1,02	2,10	n.a.
Netherlands	320,65	816,22	370,26
Poland	4,84	15,40	n.a.
Portugal	n.a.	0,56	n.a.
Romania**	-	-	7,34
Slovakia	1,87	4,76	n.a.
Slovenia	0,59	1,35	n.a.
Spain	488,11	423,42	274,64
Sweden	n.a.	n.a.	n.a.
United Kingdom***	9.132,49	n.a.	n.a.
<b>Total</b>	<b>12,940.99</b>	<b>11,824.10</b>	-

\*Voluntary information on interest income subject to Art.9 of the Directive

\*\*Bulgaria and Romania joined the EU in 2007, consequently no data for 2005 and 2006

\*\*\*In the United Kingdom the fiscal year ends on April 5

Source: EU Commission, 2008 5

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