Manager
International Tax Treaties Unit
International Tax and Treaties Division
The Treasury
Langton Crescent
Parkes, ACT, 2600
E-mail: taxtreatiesunitconsultation@treasury.gov.au

Submission on Intergovernmental Agreement to Implement FATCA
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The Tax Justice Network Australia (TJN-Aus) welcomes this opportunity to make a submission to the consideration of an intergovernmental agreement with the US regarding Australian financial institutions complying with the US *Foreign Account Tax Compliance Act* (FATCA).

Background on the Tax Justice Network Australia
The Tax Justice Network Australia (TJN-Aus) is the Australian branch of the Tax Justice Network (TJN). TJN is an independent organisation launched in the British Houses of Parliament in March 2003. It is dedicated to high-level research, analysis and advocacy in the field of tax and regulation. TJN works to map, analyse and explain the role of taxation and the harmful impacts of tax evasion, tax avoidance, tax competition and tax havens. TJN's objective is to encourage reform at the global and national levels.

The Tax Justice Network aims to:
(a) promote sustainable finance for development;
(b) promote international co-operation on tax regulation and tax related crimes;
(c) oppose tax havens;
(d) promote progressive and equitable taxation;
(e) promote corporate responsibility and accountability; and
(f) promote tax compliance and a culture of responsibility.

In Australia the current members of TJN-Aus are:
- ActionAid Australia
- Anglican Overseas Aid
- Australian Education Union
- Baptist World Aid Australia
- Caritas Australia
- Columban Mission Institute
- Jubilee Australia
- Oaktree Foundation
- National Tertiary Education Union
- Social Justice Around the Bay
- Synod of Victoria and Tasmania, Uniting Church in Australia
- TEAR Australia

Intergovernmental Agreement on FATCA
TJN-Aus sees FATCA as part of a growing global trend towards requiring automatic exchange of tax related information between tax authorities as a measure to stem tax evasion through shifting income offshore. The TJN-Aus sees the move towards automatic information exchange between tax authorities, with appropriate safeguards on the privacy of the information and against its misuse, as highly desirable. The OECD recently endorsed automatic information exchange as

proving "to be a useful way to implement enhanced international tax co-operation".[1] The OECD has outlined the benefits of automatic information exchange as:[2]

> *"It can provide timely information on non-compliance where tax has been evaded either on an investment return or the underlying capital sum. It can help detect cases of non-compliance even where tax administrations have no previous indications of non-compliance. Other benefits include its deterrent effects, increasing voluntary compliance and encouraging taxpayers to report all relevant information. Automatic exchange may also help educate taxpayers in their reporting obligations, increase tax revenues and thus lead to fairness – ensuring that all taxpayers pay their fair share of tax in the right place at the right time."*

The OECD reports the EU experience with the Savings Directive suggests that in the absence of automatic information exchange in excess of 75% of taxpayers may not have complied with their residence country tax obligations.[3]

The OECD has also published a guide on ensuring the protection of taxpayer information, entitled "Keeping it Safe: the OECD Guide on the Protection of Confidentiality of Information Exchange for Tax Purposes".[4] It is disappointing that developing countries, that often feel the greatest negative impacts from tax evasion, have had only limited access to initiatives involving automatic information exchange.

The legal basis for automatic information exchange is the exchange of information provision of a double taxation convention based on Article 26 of the OECD or UN Model Convention or Article 6 of the *Convention on Mutual Administrative Assistance in Tax Matters.*[5]

The TJN-Aus believes it is desirable to have an agreement with the US that strengthens the moves towards automatic information exchange in relation to tax matters as being the norm, and therefore it is desirable to have an agreement that would ensure US authorities automatically transfer information about accounts Australian residents hold with US financial institutions. This may be particularly desirable as US banks feature prominently amongst those accused of offering services to high net worth individuals to manage assets offshore to dodge tax.[6]

Australia already requires financial institutions to have to report interest payments on accounts held by non-residents, although the financial institution is not required to obtain a Tax Identification Number (TIN) or date of birth of the non-resident. This should make it relatively easy for Australian financial institutions to comply with obligations in an intergovernmental agreement with the US.

The TJN-Aus notes that Australia already provides information on tax related matters to over 40 countries and receives information automatically from 20 countries. Australia sent more than one million records in a particular year.[7] The US already does automatic information exchange with 25 countries.[8]

A growing number of intergovernmental agreements with the US over FATCA will encourage an increasing number of financial institutions to accept automatic information exchange. As an

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[1] OECD, "Tackling Offshore Tax Evasion. The G20/ OECD Continues to make progress", June 2012, p. 2.
[2] OECD, "Tackling Offshore Tax Evasion. The G20/ OECD Continues to make progress", June 2012, p. 4.
[3] OECD, "Tackling Offshore Tax Evasion. The G20/ OECD Continues to make progress", June 2012, p. 18.
[4] OECD, "Tackling Offshore Tax Evasion. The G20/ OECD Continues to make progress", June 2012, pp. 3-4.
[5] OECD, "Tackling Offshore Tax Evasion. The G20/ OECD Continues to make progress", June 2012, p. 14.
[6] Tax Justice Network Media Release, "Revealed: global super-rich has at least $21 trillion hidden in secret tax havens", 22 July 2012.
[7] OECD, "Tackling Offshore Tax Evasion. The G20/ OECD Continues to make progress", June 2012, pp.16-17.
[8] OECD, "Tackling Offshore Tax Evasion. The G20/ OECD Continues to make progress", June 2012, p. 17.

increasing number of countries participate in the FATCA system, the viable offshore investment opportunities for tax evaders globally will diminish.[9]

As an example of the growing acceptance of automatic information exchange, the British Bankers Association stated to the US Treasury in:[10]

> *"the longer term, we urge the US and other nations to work towards an alternative global multilateral solution, where there would be reciprocal arrangements for all jurisdictions, and where information could be collected and exchanged between governments. We propose that consideration of a multilateral solution be an agenda item for upcoming meetings of the G20 since this is clearly an issue of international concern that requires a coordinated response."*

TJN-Aus acknowledges that the passthru payment rules of FATCA have the potential to drive financial institutions away from the FATCA system. This could occur, if non-participating financial institutions decide they do not want to do business with participating financial institutions because of the additional withholding. The more likely risk is that financial institutions decide they don't want to suffer the administrative burden of determining passthru payments and all the other requirements of FATCA.[11] Thus an intergovernmental agreement will mean Australian financial institutions will be more likely to be accepting of automatic information exchange.

TJN-Aus notes FATCA has already resulted in Swiss financial institutions refusing to do business with US citizens and closing existing accounts with US citizens. This has a benefit of closing off avenues for tax evasion by US citizens, but has also resulted in hardship for some US citizens who have mortgages with Swiss financial institutions. There is doubt that such accounts would be caught under the reporting requirements of FATCA and it is speculated this might be an attempt by Swiss financial institutions to try to build a base of US citizens to lobby for repeal of FATCA.[12]

Concerns about the USA as a tax haven and secrecy jurisdiction

There are concerns about the US acting as a secrecy jurisdiction for foreign investments, assisting foreigners who invest in the US with tax dodging. Dr Eduardo Morgan of the Yale University Law School and Senior Partner of Morgan and Morgan and former ambassador for the Republic of Panama in Washington DC, has argued the US has acted as a tax haven for foreigners itself. He has stated the US has accepted between $7 trillion and $10 trillion of passive foreign investments that it does not tax.[13] However, other estimates put the figure at around $2 trillion.[14] The US has not provided information on those investments to third countries (except Canada). Foreign investors have been offered a shield on disclosing their investments to their home countries, as a means of attracting foreign investment into the US.[15]

The IRS tried in 2001 and again in 2011 to introduce regulations that would have required financial institutions to provide information to other jurisdictions on deposits held by their residents in the

[9] J. Richard Harvey Jr., "Offshore Accounts: Insider's Summary of FATCA and Its Potential Future", Villanova Public Law and Legal Theory Working Paper Series, December 2011, p. 24.

[10] British Bankers Association, "Comments for Notice 2010-60", 29 October 2010, http://www.bsmlegal.com/PDFs/FATCA_BBA_20101029.pdf.

[11] J. Richard Harvey Jr., "Offshore Accounts: Insider's Summary of FATCA and Its Potential Future", Villanova Public Law and Legal Theory Working Paper Series, December 2011, p. 20.

[12] J. Richard Harvey Jr, "FATCA – A Report from the Front Lines", *Tax Notes*, 6 August 2012, pp. 715-716.

[13] Eduardo Morgan, "OECD Double Standard in the Global Forum on Transparency and Exchange of Information. The rating of the United States", 26 April 2012, p. 5.

[14] Robin Sidel and Laura Stevens, "Banks sweat as tax net tightens", *The Australian*, 30 December 2011.

[15] Eduardo Morgan, "OECD Double Standard in the Global Forum on Transparency and Exchange of Information. The rating of the United States", 26 April 2012, p. 5; and Markus Meinzer, "Bank account registries in selected countries. Lessons for registries of trusts and foundations and for improving automatic tax information exchange", Tax Justice Network and ccdf-terre solidaire, 21 August 2012, pp. 42-44.

US. This proposal was strongly opposed by US financial institutions, and many congressmen and senators.[16]

In 2001, the US implemented the Qualified Intermediary (QI) system, which aimed to address two problems:[17]

- That a US tax payer could invest in US source assets with a foreign financial institution, but the foreign financial institution was not required to report anything to the IRS.
- US withholding agents (for example, banks) were not obtaining adequate documentation from foreign financial institutions to document a reduced US withholding tax rate on payments to foreign customers of such foreign financial institutions. This result was not surprising given that the foreign financial institution had the customer relationship, and the US withholding agent did not. Plus, the foreign financial institution was not anxious to share the identity of its clients with a potential competitor (for example, a US bank).

However, the QI system showed little desire to assist foreign tax authorities in combating tax evasion lost through investments by their residents in the US, as the QI could keep the identity of their foreign customers secret as long as the correct amount of US withholding tax was imposed on any payments of US source income to such customer.[18]

In April 2006 the US Government Accountability Office published a report "Company Formations, Minimal Ownership Information is Collected and Available", which led Senator Levin to try and introduce a bill that would have required States to identify clients of legal persons. The Senator introduced the bill again in 2008, 2009 and 2011 and each time it was strongly opposed by senators from Nevada and Delaware, which do the most business with legal entities, of which a high percentage are sold abroad.[19]

The LGT and UBS scandals of 2008 highlighted the way in which US tax payers were able to use loopholes in the QI system to continue evading tax offshore.[20] This formed part of the impetus to develop FATCA. When FATCA was being designed, there was a clear understanding that it would not eliminate all opportunities for a US taxpayer to hide income offshore. For example, a US taxpayer could invest in non-US source assets with a financial institution not part of the QI system (NQI) and avoid reporting to the IRS. However, the hope was that substantially all reputable foreign financial institutions would become QIs. If this occurred, US tax cheats would be relegated to second and third tier foreign financial institutions that could cause the US tax cheat to question whether they really wanted to invest in such an institution.[21] Further, to defeat US tax evaders, it was hoped the US would be able to convince other governments to adopt FATCA style systems, or alternatively participate in a multilateral participating financial institution system.[22]

Nearly two million corporations and limited liability companies are being formed under the laws of US States each year. Very few States obtain meaningful information about the beneficial owners of

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[16] Eduardo Morgan, "OECD Double Standard in the Global Forum on Transparency and Exchange of Information. The rating of the United States", 26 April 2012, pp. 5, 9.

[17] J. Richard Harvey Jr., "Offshore Accounts: Insider's Summary of FATCA and Its Potential Future", Villanova Public Law and Legal Theory Working Paper Series, December 2011, pp. 4-5.

[18] J. Richard Harvey Jr., "Offshore Accounts: Insider's Summary of FATCA and Its Potential Future", Villanova Public Law and Legal Theory Working Paper Series, December 2011, p. 5; and Markus Meinzer, "Bank account registries in selected countries. Lessons for registries of trusts and foundations and for improving automatic tax information exchange", Tax Justice Network and ccdf-terre solidaire, 21 August 2012, pp. 42-44.

[19] Eduardo Morgan, "OECD Double Standard in the Global Forum on Transparency and Exchange of Information. The rating of the United States", 26 April 2012, p. 5., pp. 10-11.

[20] J. Richard Harvey Jr., "Offshore Accounts: Insider's Summary of FATCA and Its Potential Future", Villanova Public Law and Legal Theory Working Paper Series, December 2011, pp. 5-9.

[21] J. Richard Harvey Jr., "Offshore Accounts: Insider's Summary of FATCA and Its Potential Future", Villanova Public Law and Legal Theory Working Paper Series, December 2011, p. 11.

[22] J. Richard Harvey Jr., "Offshore Accounts: Insider's Summary of FATCA and Its Potential Future", Villanova Public Law and Legal Theory Working Paper Series, December 2011, p. 13.

corporations and limited liability companies formed under their laws.[23] This makes them potential vehicles for the laundering of funds from tax evasion and other criminal activity.

Limited liability companies sold to foreigners by US States, who have no operations in the US, are not subject to US taxes and do not have to file tax returns, making them completely invisible to the IRS.[24]

This current inability of the US authorities to collect information on assets held by entities may partly undermine the benefits to Australia from an intergovernmental agreement with the US over FATCA.[25]

Actions by the US outside of FATCA to combat tax evasion

TJN-Aus notes that IRS regulations issued on April 2012, which will come into force on 1 January 2013, will provide the IRS with basic information on interest paid on bank accounts held by certain non-resident individuals. However, not all financial accounts or interest bearing instruments will be included and reported, nor will all non-resident recipients of interest payments be covered. Similarly, the QI Rules will remain unchanged so that foreign financial institutions and non-US branches of US financial institutions still have the opportunity to avoid reporting of bank deposit interest (as well as dividend and capital gains reporting and other types of passive income).[26] Corporate or other legal entity recipients are not included.[27]

The Financial Crimes Enforcement Network of the US Department of the Treasury has called for a roundtable meeting on 5 October to continue gathering information on the Advance Notice of Proposed Rulemaking on customer due diligence requirements for financial institutions. The consultation started back in March and is considering an obligation for financial institutions to have to collect beneficial ownership information of their customers.[28]

Dr Mark Zirnsak
Secretariat
Tax Justice Network Australia
c/- 130 Little Collins Street
Melbourne, Victoria, 3000
Phone: (03) 9251 5265
E-mail: mark.zirnsak@victas.uca.org.au

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[23] Eduardo Morgan, "OECD Double Standard in the Global Forum on Transparency and Exchange of Information. The rating of the United States", 26 April 2012. p.11.
[24] Eduardo Morgan, "OECD Double Standard in the Global Forum on Transparency and Exchange of Information. The rating of the United States", 26 April 2012, p.11.
[25] Vanessa Houlder and Shahien Nasiripour, "US and Europe in accord on tax evasion", Financial Times.
[26] Markus Meinzer, "Bank account registries in selected countries. Lessons for registries of trusts and foundations and for improving automatic tax information exchange", Tax Justice Network and ccdf-terre solidaire, 21 August 2012, p. 41.
[27] Markus Meinzer, "Bank account registries in selected countries. Lessons for registries of trusts and foundations and for improving automatic tax information exchange", Tax Justice Network and ccdf-terre solidaire, 21 August 2012, p. 42.
[28] Financial Crimes Enforcement Network, "Customer Due Diligence Requirements for Financial Institutions", 77 FR 13046, 5 March 2012.