



The ATOZ Chair for European and International Taxation welcomes you to:

TAX COOPERATION vs TAX COMPETITION: CROSS-ATLANTIC PERSPECTIVES

FATCA, CRS, and EU-US Cooperation on Exchange of Information

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Introductory remarks



- Approx. **25%** of private wealth in the Middle East, Africa and Latin America is booked offshore (totaling approx. **\$ 3.1 trillion**)*
- Revenue losses negatively affect ability to meet human rights commitments of the respective countries
- In the interest of fairness, tax administrations have a responsibility to tackle compliance problems

* Boston Consulting Group

Introductory remarks



- In the U.S., vigorous debate about the public disclosure of tax returns since the enactment of the income tax
- Since 1976, **tax return data is confidential** and cannot be disclosed by the IRS **except under specific circumstances** outlined in the statute
- **No financial privacy** for U.S. citizens and residents with respect to disclosure of information to the IRS with respect to **U.S. banking transactions**

What is FATCA?



- U.S. Response to War on Tax Evasion in 2010
- Inspired Increased Taxpayer Reporting
 - TP must report total value of all specified foreign financial assets
 - Includes foreign stock or securities not held in a financial account as well as
 - investment vehicles such as foreign hedge funds & foreign private equity funds
- Failure to Report = Penalty

Is FATCA a Drone...?



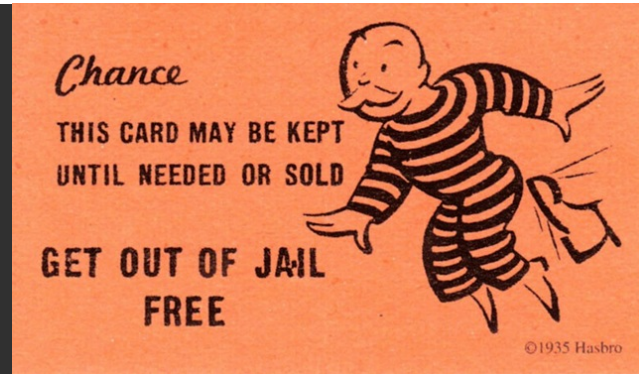
- "It's obnoxious, expensive, arrogant, extraterritorial, and likely to cause a fair amount of collateral damage while occasionally hitting its targets." – *Lee A. Sheppard*

FATCA Imposes Reporting Requirements on Foreign Banks

- Reports from **Foreign Financial Institutions (FFIs)** to IRS
- FFIs must annually report directly to IRS certain information about financial accounts held by U.S. taxpayers, or
- **by foreign entities in which U.S. taxpayers hold a substantial ownership interest**
- **Enforcement: 30% withholding on U.S. source income**



Offshore Voluntary Disclosure Programs (OVDP)



- IRS sought to encourage people with hidden offshore accounts to come forward
- Participants are able to avoid civil fraud charges, non-filing penalties, and criminal prosecution in exchange for disclosure of bankers and those who facilitated opening the accounts
 - **Approximately 55,800 people have participated since 2009**
 - **OVDP have generated collections of \$9.9 billion in taxes, interest, and penalties**

Is FATCA a Snowball...?



From FATCA to CRS

- 'That "giant sucking sound" you hear? It is the sound of money rushing to the USA to avoid FATCA reporting.' (Global FATCA=CRS=FATCA)
- U.S. obstructs other tax administrations from remedying their tax evasion problems
- As other governments improve their financial transparency, the share of offshore wealth destined for the U.S. increases

Common reporting standard (CRS)

- Automatic exchange of information is the **most effective way** to fight offshore tax evasion
- +100 jurisdictions have committed to implementing CRS by 2018 **but the United States is not one of them**
- The U.S. is falling behind its peers with respect to financial transparency due to legislative and regulatory inaction caused by political gridlock.

New Approach: Reciprocal IGAs

- **Intergovernmental Approach-Treasury Model I**
 - *Uniform Model Agreement* for government-to-government information sharing
 - Allows FFIs to report required FATCA info to their own governments
 - which would then transmit data to IRS
 - **Shift** from FATCA's *unilateral* arrangement to *reciprocal* relationship
 - More than 50 reciprocal FACTA agreements
 - All EU Member States except Austria (Model II) have signed such IGAs

Reciprocal Exchange of Account Data under FATCA

- Despite U.S. pledge of reciprocal information sharing in its FATCA IGAs with more than 50 jurisdictions
- **U.S. legally only able to share amount of interest paid** to foreign recipients of 40 specified countries that meet IRS's stringent safeguard, privacy, and technical standards
 - Revenue procedure issued in December 2016 provides countries with whom U.S. will engage in automatic exchange of information and
 - Added Israel, Republic of Korea, and Saint Lucia to list.

Reciprocal Exchange of Account Data under FATCA

- This is in lieu of the more detailed information required by FATCA from over 235,000 Foreign Financial Institutions (FFIs)
- For example, FATCA requires FFIs to ascertain the **substantial U.S. owners of certain legal entities**
- while the U.S. banks are only reporting on the **individual accounts of foreign residents**

Reciprocal Exchange of Account Data under FATCA

- Info exchange rules for U.S. banks with respect to foreign residents are easily avoided by holding bank account in the name of a shell corporation
- Tax Notes Reporter Lee Sheppard pointed out in 2013, the then new bank deposit regulations only affected
- **'the stupid rich. Because the sophisticated rich use corporations and Delaware LLCs, they would not be affected.'**

Reciprocal Exchange of Account Data under FATCA

- Information is being exchanged and global financial transparency has increased.
- In 2016, **over 4 million disclosures** were made by the IRS with respect to reportable accounts maintained by residents of foreign jurisdictions in U.S. financial institutions
- to competent authorities of foreign governments that have concluded reciprocal IGAs with the U.S. and
- **'are deemed to be an appropriate jurisdiction with which to have an automatic exchange relationship.'**

United States as a Tax Haven

- Global Forum deemed U.S. only Largely Compliant concerning ownership information for entities during its peer review
- Unavailability of beneficial ownership of info in several states such as Delaware, Nevada, and Wyoming



EU – US COOPERATION

- European Parliament's Committee of Inquiry into Money Laundering, Tax Avoidance and Tax Evasion met with U.S. lawmakers in D.C. and Delaware in March, 2017 as part of a fact finding mission
- Chairman appealed to U.S. and Delaware **to close its loopholes by introducing beneficial ownership registers**
- Delegation was told **it was too early in Trump Administration to discern policy direction** as key high-level positions need to be filled
 - Assistant Secretary of the Treasury for Tax Policy has been nominated but not yet confirmed by U.S. Senate.

EU – US COOPERATION

- U.S. will be subject to a second round of peer reviews by the Global Forum, which
- will assess strengthened standard on availability of beneficial ownership information
 - May incentivize the U.S. to take the required legislative action
 - But given the current political climate, it will probably yield nothing

Reciprocal Exchange of Account Data under FATCA

- Must enact whatever legislation is necessary to ensure **appropriate exchange of information with treaty partners** to aid them in respective wars on tax evasion
- Required to fulfil the **obligation of reciprocity promised by many of the FATCA IGAs** that U.S. negotiated.
- Must honor commitments made in IGAs with FATCA partners to support **'relevant legislation to achieve such equivalent levels of automatic exchange.'**
- Expand bank deposit regulations to entities.

Common reporting standard (CRS)

- OECD, in latest economic survey of U.S., called for adoption of the CRS by 2017 or 2018
- **OECD explicitly acknowledged that information supplied by U.S. pursuant to FATCA IGAs is not identical to information required to be supplied under CRS**
- **'Congress has yet to enact the required proposed legislation'** to establish parity with CRS as to specific types of information exchanged

Common reporting standard (CRS)

- Tax Justice Network **put U.S. at third place on its financial secrecy index** because of its unwillingness to participate in **transparency initiatives such as CRS** and **creation of public registers of beneficial ownership**
- Study commissioned by Greens/European Free Alliance group in European Parliament **has recommended that EU consider including U.S. on its common European black list of tax havens**
 - 'unless it effectively ensures registration of beneficial ownership information for companies and commits to equal levels of automatic exchange of information with European countries.'

Concluding remarks

- Time to pressure on U.S. to join global movement for increased financial transparency
- Former U.S. Treasury Secretary Lew admitted in his May 5, 2016 letter to Congress that
 - **'gaps remain in our laws that allow bad actors to deliberately use U.S. companies to hide money laundering, tax evasion, and other illicit financial activities.'**

Concluding remarks

- Civil society must demand financial transparency legislation from U.S. Congress
- 115th Congress appears to be rolling back previous transparency initiatives
 - In February 2017, Congress removed SEC rule relating to “Disclosure of Payments by Resource Extraction Issuers”

Concluding remarks

- Certain members of Congress have not given up on efforts to repeal FATCA
 - 'goes well beyond what is appropriate' and
 - violates U.S. citizens' constitutional right to privacy under the Fourth Amendment as well as
 - creating 'unnecessary burdens.'
- House bill is similar to effort to repeal FATCA (S. 887) made by Sen. Rand Paul in 2013
 - it never reached the Senate floor.

Concluding remarks

- Although, **repeal of FATCA is Republican National Committee's official position** and President Trump has demonstrated his policy of deregulation,
- **It is unlikely that Trump Administration will be able to repeal FATCA**
 - Too much investment in IGAs, competent authority agreements.
 - Exchanges have already been taking place.
 - FATCA continues to be the excuse of the U.S. as to why it does not need to enact CRS.

Concluding remarks

- Secrets: *On the Ethics of Concealment and Revelation*
 - 'Less obvious than the risks of active abuse..., but cumulatively as harmful to society, are the acts of omission that secrecy makes possible –
 - such as the failure of many to carry their part of the collective tax burden whenever they can conceal some of their income.'

THANK YOU FOR YOUR ATTENTION

A U.S. Perspective on BEPS and the State Aid Cases

Daniel Shaviro, NYU Law School
Tax Cooperation vs. Tax Competition:
Cross-Atlantic Perspectives
Luxembourg, May 30, 2017

A story I've never quite understood

Aesop's "The Man & the Satyr" perplexed me as a child - & still does.

"On a cold winter day, as a man & a satyr sat together in friendship, the man put his fingers to his mouth & blew on them. When the satyr asked why, he said he did it to warm them, as they were so cold.

"Then steaming hot food arrived. The man raised a dish towards his mouth & blew on it. When the satyr asked why, the man said he needed to cool it, as it was so hot.

"The Satyr sprang angrily to his feet, saying: 'Begone! I'll have nothing to do with a man who can blow hot & cold with the same breath!'"

But ... but ...

A modern update?: Apple's "Irish" income from the EU state aid case.

Underlying facts from the *Apple* case

Apple's US employees developed technology for products sold WW.

Apple used in-house cost-sharing agreements to create FSI, for US legal purposes, on its EU sales (its Irish sub owns the IP for such sales).

Under Irish law, >99% of "Irish" income (in 2011) went to a phantom "head office" that continues to elude non-paranormal investigators.

EC: Irish tax concessions amounted to illegal state aid, improperly reducing Irish taxes by \$14B.

If sustained, this will raise Apple's WW tax rate on the "Irish" income from under 1% (for some years) to 12.5%.

The IRS/Treasury blow hot & cold

IRS agrees with Apple: under U.S. “cost-sharing” rules, this is foreign source income.

U.S. Treasury (White Paper) tells the EC: this is U.S. source income.

Hence, the EU can't tax it – even though the U.S. doesn't either.

--Can income be at an “intermediate temperature,” like the breath of the Satyr's guest?

It's hard to argue, post-BEPS, that countries can't reasonably take note of double non-taxation.

And does it really matter, from a U.S. standpoint, that Ireland might be the “wrong” EU country in which to tax the income?

4 underlying international tax policy ambiguities

Controversiality of BEPS/state aid issues (on both sides of the Atlantic) reflects unresolved underlying disputes.

1) What does “source” mean? – Origin vs. destination concepts; relevance of artificial conventions.

2) How define optimal policy re. taxing “outbound”? – And how achieve it politically / administratively once defined?

3) How define optimal policy re. taxing “inbound”? (E.g., given intra- vs. extra-EU tax competition).

4) How evaluate foreign-to-foreign profit-shifting? (Note CFC rules)

U.S. international tax policy dissensus

2 warring sides: anti-tax (MNEs, Republicans, some academics) VS. anti-tax avoidance (some Democrats, some academics).

On BEPS & (especially) state aid, much more was heard from the anti-tax side.

This reflected U.S. companies' prominence as targets, & retroactivity concerns.

(The latter despite U.S. case law on tax avoidance, & reflecting U.S. tax advisors' red faces.)

What to expect next from the U.S.

Had the 2016 U.S. presidential election gone as most expected, more of the same was highly likely.

That is, from the Treasury, some (but limited) BEPS cooperation, some voicing of State Aid concerns, but no significant retaliation.

And from Capital Hill, little or nothing given the partisan divide.

The actual 2016 U.S. presidential election outcome makes prediction harder, as we're in less charted waters.

But based on what we've seen so far...

The Trump Administration, regardless of its views on BEPS & State Aid, has bandwidth issues. (E.g., are they capable of considering the application of §891?)

The bandwidth issues reflect, not just temperament & the degree of expertise at the top, but light staffing throughout the Executive Branch.

Republican Congressional majorities have generally been embarrassing themselves – & this is likely to continue.

Very large rate cuts, plus territoriality (but without Dave Camp-style safeguards), remain a good bet. But beyond that??

Encouraging (?) final words

The U.S. is going through a self-absorbed period.

Impulsive, ill-considered war-making is possible, but this would most likely be in Asia or Africa.

Whether ideal or not, U.S. self-absorption is not the worst possible outcome under existing parameters.

EU countries therefore can, but in any event probably must, chart their own courses, both re. BEPS & State Aid, and more generally.

CCCTB – Lessons to Learn from U.S. Formulary Apportionment

Yariv Brauner
University of Florida

Luxembourg, May 2017

Introduction

- CCCTB
- Formulary Taxation in the United States
- Lessons
- Distinct Transfer Pricing discourse
- Impact of the CCCTB
- Conclusion

CCCTB

- EU
 - CCTB
- Background – Single market & definition of European project / goals
- Formulary Apportionment
 - Formulary Taxation
 - Not a transfer pricing reform
 - Administrative benefits
 - Efficiency benefits
 - Political benefits
- Double taxation

Formulary Taxation in the United States

State Income Taxes

- Independent competence of states to tax
- Income tax important since the beginning of the 20th century
- Separate Accounting first
 - Expensive and unreliable
- Single factor apportionment
 - Based on assets (tangible)
 - Critical industries such as railroads fit the bill best
 - Critique due to diversity of states
- Shift to multiple factor formulary apportionment
 - Massachusetts Formula

Formulary Taxation in the United States

State Income Taxes

- A multistate tax commission / consortium – post WWII
- By the end of the 1970s almost full standardization
- Yet, ever since increased reliance on sales
 - Also due to belief that otherwise it would discourage investment, people and assets, in the state
- Today, the Massachusetts Formula has largely been abandoned
- A large number of states rely on sales only or heavily on sales
- Double taxation therefore is inevitable
 - Raised as an “issue” but not beyond that
 - Double taxation not a concern

Formulary Taxation in the United States

State Income Taxes

- Independent competence of states to tax
 - Not subject to Tax Treaties
 - SALT deduction
- Competition framework
- Tiebout
- Independent formulae, yet,
 - Nexus issue
 - Digital economy – key problem
 - Services – some use “market based” sourcing rules, yet have similar difficulties
 - Intangibles
 - States use factors of production (R&D, for example) as proxy for sales, yet then lose the perceived benefits of sales only formula

Formulary Taxation in the United States

State Income Taxes

Other issues are important for global FA discussion

- Domestic / Worldwide base – constitutional, but Federal pressure
- The use of alternative formulae in special cases
 - Controversial and difficult application
 - Fairness
- Profit shifting
 - Also, since only to business income in some states (ringfencing issue)
 - Must have factual connection to state – again difficult boundaries
- Difficulties with reporting: consolidated or separate

Formulary Taxation in the United States

The Federal Income Tax

- Uncommon
- Arm's length based transfer pricing rules
 - But, CPM (& PS) dominate
- Formulary rules for allocating deductions
 - Interest expense
 - R&D

Formulary Taxation in the United States Lessons?

- The SALT experience highlights challenges
 - Services
 - Digital economy
- What is the purpose of the formula?
- Yet, it works well and quite flexibly in a competitive environment (is this what the EU wishes to achieve?)
- Caution I: the need to establish base from scratch
- Caution II: Consolidation
- Caution III: Double Taxation issues
 - The single Tax Principle in the discourse
- But, formulas familiar in United States tax practice

Transfer Pricing

- Main area for discussion of FA
- Obscured by the dichotomy FA/ALS
- Discourse focuses on U.S. states factors..
 - To the exclusion of others
- Many proposals based on beliefs about political realities
 - Or administrability
- Should not be confused with the Business Tax Reform discourse

Impact of CCCTB

- With or without consolidation
- Tax treaties – general
 - Tax base
 - Consortium agreement
 - Need to renegotiate?
- Will the base dominate tax accounting worldwide
- Winners and losers

Conclusion

- Clear thinking
 - States compete and not within a single market
 - Formulae diverse and impacted by path dependence
 - Tiebout
- Importance of clear goals
- Winners and losers
- Technical possibility – partial and gradual reform
 - Impact on the international tax regime
 - But different social views / tax accounting
- “Competitiveness”
 - Impact on future coordination
 - EU vs. World reform