Automatic Information Exchange: Will Germany follow the US in going the extra mile?

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There is a very important project in the new US budget proposal for financial year 2014 supported by the Obama administration. If this proposal is carried through into law (or regulation), the odds for a truly effective global system of automatic information exchange on tax data about the wealthiest citizens would dramatically increase. Alex Cobham has identified the issue (see here) and the original text of the proposal can be found on page 202, of this pdf document.

It is worthwhile quoting at length and unpacking some of the detail:

> *"Provide for reciprocal reporting of information in connection with the implementation of the Foreign Account Tax Compliance Act (FATCA).—*
> *In many cases, foreign law would prevent foreign financial institutions from complying with the FATCA provisions of the Hiring Incentives to restore Employment Act of 2010 by reporting to the IRS information about U.S. accounts. Such legal*

impediments can be addressed through intergovernmental agreements under which the foreign government agrees to provide the information required by FATCA to the IRS.

Requiring U.S. financial institutions to report similar information to the IRS with respect to nonresident accounts would facilitate such intergovernmental cooperation by enabling the IRS to reciprocate in appropriate circumstances by exchanging similar information with cooperative foreign governments to support their efforts to address tax evasion by their residents.

The proposal would provide the Secretary of the treasury with authority to prescribe regulations that would require reporting of information with respect to nonresident alien individuals, entities that are not U.S. persons, and certain U.S. entities held in substantial part by non-U.S. owners, including information regarding account balances and payments made with respect to accounts held by such persons and entities."

This legislative proposal is crucial for the effectiveness of any future multilateral system for automatic tax information exchange for a number of reasons. First, the current regulations for reciprocating data exchange by the US under FATCA are a welcome first step away from the role of the US itself as a major tax haven (see background here), but are very narrow in scope (we have shown this in our analysis of bank account registries, on pages 41-42, in the chapter on the US, here). Most importantly, interest on government and corporate bonds as well as account balances and other crucial tax data is not currently available for reciprocating FATCA. This is the reason why FATCA model 1 agreements which the US has signed with many countries, among them key European allies, contain quite explicit langauge about the need for the US to improve its capacity to reciprocate under FATCA by additional legislation. For instance, article 6.1 of the German draft model 1 agreement states (full pdf here):

> *"Reciprocity. The [Government of the] United States acknowledges the need to achieve equivalent levels of reciprocal automatic information exchange with [FATCA Partner]. The [Government of the] United States is committed to further improve transparency and enhance the exchange relationship with [FATCA Partner] by pursuing the adoption of regulations and advocating and supporting relevant legislation to achieve such equivalent levels of reciprocal automatic exchange."*

It is encouraging to see that the US administration appears to be willing to walk the talk. While it will be challenging to force this proposal through against a Republican dominated House, and it is doubtful if a modification of the US' QI program will be in the package of reform, the intention of engaging in this battle are a sign of decreasing hypocrisy currently embedded in many Western's fiscal policies (see background here).

This leads us the the second major reason why this initiative in the US may be decisive for a functioning global system. The long term effects of this political signal to earnestly fight for domestic reforms to reduce damages done in the rest of the world by the superpower may help restore and enhance its moral integrity and legitimacy to demand reform in other places. Recently, we heard Swiss, Austrian and also German politicians to (rightly) point out deficiencies in US and UK fiscal, anti-money laundering and transparency policies. The capacity to use those arguments as an excuse for defending the indefensible, the criminal and the opaque financial and tax arrangements in these German speaking nations would decrease dramatically if the US were to offer true domestic reform.

And here is where Germany still has some homework to do. German authorities at the moment do not collect from German banks, or German foundations or German Treuhand and trustees the information required for effective automatic information exchange (see page 29 here, and here, and here). There is a cloak of secrecy shed over any non-resident investor in interest bearing financial accounts and bonds, sweetened by tax exemption. Germany would need to modify, or better still, abolish its domestic "Abgeltungssteuer" and replace it by broad reporting obligations to the tax administration about financial account balances and payments. Now, they will need to do this for US accounts under FATCA. In the past, Germany's centre-right government has tried to do the opposite by fighting for the anonymous withholding deal with Switzerland (see here). And they may try to wriggle out of broad reform under the recently announced G5-initiative for AIE, e.g. by limiting exchange on interest on the narrow categories covered by the current EUSTD.

The question is: will Germany continue to do the minimum necessary not to be seen as a tax haven, and only require reporting about accounts of a few selected country's residents? Developing countries would be left out, and Germany would continue to finance its economy partly at the cost of the most vulnerable people on this planet. Or will Germany go the extra mile, as the US now appears willing to do, in order to collect the information of all non-resident accounts, so that Germany can support developing countries with collecting their fair share of tax from investments in the German financial market? Will it yield to supreme power, or will it use its power for the benefit of the "least among us"?

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