



EUROPEAN UNION

Delegation of the European Union to Switzerland and the Principality of Liechtenstein

The final withholding tax – not crossing the Rubicon

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Check Against Delivery
Seul le texte prononcé fait foi
Es gilt das gesprochene Wort

Times of change in Switzerland

Recent commitments made by Switzerland in the field of good governance in the area of taxation are very positive – the acceptance of the OECD standards, the conclusion of Double Taxation Agreements, the abolition of the distinction between tax fraud and tax evasion, thus the move towards more transparency, all that are welcome developments.

We welcome the announcement of '**white money policy**' as a step in the right direction. The acceptance of this principle, and the rejection of black money, logically supports the use of automatic exchange of information in order to ensure that black money is uncovered and white money stays white. We are looking forward to learn more on how to implement this new policy.

Let us be clear: we also have an obligation towards the vast majority of the honest taxpayers in all our countries to make sure that tax fraud or tax evasion do not pay. When talking about black money we are talking about a minority, although a minority controlling a lot of money. Figures are never clear and ever changing, but there is talk of \$2 trillion of the offshore banking industry with an estimated \$600-700 billion of undeclared assets still hidden in the country.

Personal data protection is important – the EP recently rejected the result of the negotiations with the US. However, one has to evaluate the interest of the public against the individual rights and the data transmitted is relatively limited, limited to interest accrued. Compare this to the amount of data travelling when you book a flight to the US!

Thus, the EU and its Member States have strong expectations that Switzerland will continue on its way towards increased tax transparency and (automatic) exchange of information – this was recently also confirmed by the EP.

Within the EU automatic information exchange is the rule, applied by 25 out of the 27 Member States. Belgium has accepted this system beginning of this year, without difficulties and without increasing its bureaucracy.

One major Swiss argument in favour of the application of a final withholding tax is based on the criticism of the automatic exchange of information under the EUSD, that there is no information on how much tax revenue the information exchange is effectively delivering. Conversely, the Swiss withholding tax operated under the EU CH STA is advertised as being very efficient as it resulted in the annual transfer of up to 550 million CHF to EU Member States.

However, the dissuasive effect of the automatic information exchange on tax payers should not be underestimated. In many instances the taxation of the interest is secondary to the taxation of the principle which is usually the overall amount of undeclared revenue. Furthermore, compare the just mentioned 550 million to the reported 93 billion CHF legalised because of the ongoing *scudo fiscale*.

Let me underline that this trend, this change of paradigm is a world-wide one. In this context, let me recall that the OECD/ G-20 initiative on good governance in taxation is increasingly reducing the scope for tax havens to market their lack of transparency as a means of attracting business. As a result the pressure on the Swiss and EU banking sector from unfair competition by such jurisdictions is reducing progressively.

Switzerland should not wait for tax havens to adopt the internationally accepted standards before taking the necessary steps. In order to maintain its status as an internationally recognised and respected financial centre, Switzerland should be ready to lead by example and be at the forefront of international developments. Even small jurisdictions, like Liechtenstein, can have an impact when picking up on change.

It is in the interest of national finance sector to apply the new standards and to prepare for their further development in a timely manner in order to preserve their competitiveness and access to the international markets. As a consequence the Swiss opening towards tax transparency will ultimately help the Swiss banking sector to defend its important role in the world of international finance.

A satisfactory and comprehensive solution to the problems stemming from black money invested in Switzerland can only be found at European level and not exclusively through bilateral agreements with a few individual Member States.

How to move forward

The Commission expects Switzerland to confirm its readiness to enter into negotiations with a view to amending the EU-CH **Savings Taxation Agreement** and to agree on effective measures equivalent to the amending proposal to the EU-Savings Taxation Directive once the Council e.g. the EU has agreed the text of this proposal. This was already promised by the then president Pasqual Couchepin accompanied by Finance Minister Merz when calling on President Barroso in December 2008.

Further expectations as regards the amending proposal to the EU- Savings Directive:

The consequences of a possible reinforcement of the mechanism of the paying agent on receipt in EU legislation would deserve particular consideration in relation to Switzerland, as this mechanism is not enshrined at all in the currently applicable EU-Switzerland Savings Taxation agreement.

The "look through approach" for payments to certain untaxed entities and arrangements having their place of effective management outside the territorial scope of the savings measures could be satisfied also by CH banks, which could use the information already collected by them under the requirements of the CH Anti-Money laundering legislation in conformity with the Financial Action Task Force standards.

The Council expects to create a level playing field amongst Member States and relevant third Countries. In this context the Commission has started negotiations with Norway on the conclusion of an EU-Norwegian Savings Agreement incorporating the provisions agreed by Member States for the amending EU-Savings Directive proposal. Furthermore, the Commission is continuing talks with other third countries such as Hong-Kong, Singapore and Macao and technical meetings held there at the end of May provided some encouraging signals.

Turning to the initiative for a final withholding tax (RUBIK):

The Commission has taken due note of this proposal developed primarily by the Swiss Bankers' Association.

However, the Rubik proposal is not an appropriate model for the tax treatment of EU residents with regard to their capital income from Switzerland for the following reasons:

- Although the Rubik proposal could appear interesting for budgetary reasons, it is clearly not in line with the European and international standards of good governance and transparency in tax matters. Rubik might at first sight satisfy the budgetary interests of certain Member States but it would not help their efforts to strengthen transparency and combat tax evasion. Such efforts are particularly important in relation to a country like Switzerland which has such close relations with the EU.
- The Commission cannot respond favourably to Rubik as it could impair agreements on tax information exchange with other 3rd countries. (Agreeing to a discussion with Switzerland on the Rubik proposal would give a wrong signal to those 3rd countries with which the Community (EU) is currently negotiating or intends to enter into mixed anti-fraud agreements which also include tax information exchange, such as with Liechtenstein.
- The practical application of Rubik seems doubtful as a final withholding tax could only be applied in relation to those Member States who themselves apply a final withholding tax or at least a fixed tax rate on the income concerned. This is not the case in other Member States which apply either progressive tax rates or different tax brackets on all forms of income covered by individual income tax. It is not clear how Swiss banks should identify the relevant tax rate when the investor's state of residence does not apply a single flat rate in respect of the relevant income. It is also unclear how any differences in the national criteria for determining the taxable base would be taken into account.
- Rubik could lead to a difference in treatment between investments within the state of tax residence and those in Switzerland. If a final withholding tax would be applied despite the existence of progressive tax rates or the application of different tax brackets in the investor's Member State of residence there would be a difference in treatment between investments in the Member State concerned and in Switzerland. Equal treatment of domestic and cross-border investment can only be observed by the taxation of the relevant income in the Member state of residence of the beneficial owner at its individual tax rate.

Having said this, I have the impression that Rubik helped to move the discussion forward in Switzerland – it signalled that the need for change was perceived and understood. Policies which worked well in the past are not necessarily the policies which will serve a country well in the future. Whether it meant passing the Rubicon remains to be seen.

The domestic consequences of international change became clear: the cantons point out that abolishing the mentioned distinction between tax fraud and evasion only internationally would discriminate their tax authorities.

Businesses, whether active in the production of goods or in the financial sector need predictability, transparency and a clear legal environment to base their investment decisions on – this includes nowadays a settled relationship with the most important neighbour, the EU in the case of Switzerland.

Quid pro quo?

In preparing for talks Switzerland is trying to build up a negotiating position, to be ready for a sort of quid pro quo – a legitimate endeavour. As a non-member state of the Union and the EEA Switzerland would like to improve market access especially in the financial market.

Nevertheless, Switzerland obtained under the Savings Taxation Agreement of 2004 access (static not dynamic) to the provisions from the EC Parent Subsidiary Directive and the Directive on Interests and Royalties and is in this respect more integrated than Liechtenstein, which is a member of the EEA. However, CH banks cannot offer financial services to clients in the EU without using a subsidiary which explains Swiss interest in a sectorial agreement on financial services.

The road available to Switzerland for obtaining better access to the EU's services market is the integration in the EU services market by means of the conclusion of an all-embracing services agreement including the obligation to take over the entire relevant *acquis*.

- Market access in services, including financial services, is an exclusive competence of the EU by virtue of *Article 207 TFEU*. It follows that the European Union has the exclusive right to negotiate and conclude bilateral trade agreements with third countries in the area of trade in (financial) services.
- ***Therefore, Member States are not in a position to conclude with Switzerland any bilateral agreements or other kind of arrangement granting preferential access into the EU services market.***
- From a legal perspective, the unilateral granting of preferential market access to Swiss (financial) services providers would breach EU law on the distribution of competences in the Union.
- Hence, the Commission would be entitled to commence infringement procedures against those Member State for failure to implement EU law (*Article 258 TFEU*). From a political perspective, the unilateral search for advantages would also be unacceptable.
- ***Services liberalization shall be built on the fundamental principles of the GATS***, such as the principle of non-discrimination. Only the conclusion of an *Article V GATS*-compliant free trade agreement on trade in services would prevent any such liberal concession from the extension on an MFN-basis to third countries.
- Article V GATS alludes, among other requirements, to the necessary "**substantial sectoral coverage**" of the agreement to be exempted from its MFN application; this implies that the agreement must be horizontal and comprehensive, and not just narrowed to financial services. This legal argument carries considerable weight.
- Adding to the previous point, ***the Swiss approach is in strong contrast with the EU position as set out in the negotiating mandate specifying that we can only contemplate comprehensive services negotiations with Switzerland.***
- Besides, any such inclusive-services agreement should ensure that Switzerland adopts the relevant *acquis* in full and its flanking policies as a precondition, in particular relevant competition rules, tax and consumer policies as stated in the 2002 mandate.
- *Why are we so adamant on the automatic implementation of the acquis by the Swiss?* There are two main reasons for this:

a) the necessary provision of a level playing field between EU and Swiss service providers and a comparable level of consumer protection; and

b) the EU has to ensure that Member States and members of the EEA are not disadvantaged by third countries getting market access on more favourable terms.

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