WILL FATCA OPEN THE DOOR TO TAXING CAPITAL INCOME IN EMERGING COUNTRIES?

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Draft of May 27, 2013

Note to Readers: This paper is intended in large measure for an audience of emerging economy finance ministry officials and tax academics interested in issues of cross-border tax compliance (to whom it will be presented in July). In the paper I endeavor to provide practical, immediately relevant insight and advice to developing and emerging economy finance ministries in an academic framework. As the paper represents part two of a two-part series, it assumes some level of familiarity with international developments in the battle over offshore tax evasion over the last five years.

I look forward to our discussion.

Abstract:

For many emerging and developing economies, it is exceedingly difficult to constrain residents from evading tax liability on income from capital, whether earned domestically or abroad. An international regime for combatting offshore tax evasion is emerging: the form of the new regime will be established during a narrow window of opportunity over the span of the next few years. A uniform, multilateral automatic information exchange system would improve emerging countries’ ability to tax the offshore accounts of their residents and, perhaps more importantly, their capacity to collect information about and tax domestic-source income from capital. However, a fragmented automatic information exchange regime likely would not benefit countries outside the developed economies.

Interestingly, the concerns of emerging countries with the contours of the emerging international regime align with the concerns of multinational

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financial institutions. Both groups have strong reasons to support the emergence of a uniform regime. As a result, they may find that they are improbable allies in the battle over taxing offshore accounts. With the G-20 as an agenda-setter and international financial law as the model, a governance structure for an automatic information exchange regime that could be useful to emerging countries’ tax administrations could materialize. The paper explores the necessary architecture, and steps emerging countries may take to help develop that architecture.
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**EMERGING COUNTRIES AND OFFSHORE ACCOUNTS**

**WORK IN PROGRESS – COMMENTS WELCOME**

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**Introduction**

For many emerging and developing economies, it is exceedingly difficult to constrain residents from evading domestic tax liability on income from capital—whether earned domestically or abroad—by using offshore accounts. More than a quarter of all Latin American household wealth and almost one-third of all Middle Eastern and African wealth is held offshore. For countries where a large part of household wealth is held offshore, the question is not whether their wealthy taxpayers’ access to offshore accounts will weaken tax enforcement, but whether given such access taxes on capital income can be enforced at all. In many of these countries, widespread awareness of tax evasion by the wealthy is often thought not only to reduce government revenues, but also to undermine the authority and effectiveness of the state. Data on actual revenues lost by developing countries and emerging economies overall from offshore tax evasion is unreliable. Nevertheless, some experts have speculated that those revenue losses are of a magnitude that approximates all official development assistance worldwide (totaling $120 billion per year).

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2 Thanks to Hugh Ault, Steve Cohen, David Gamage, Markus Meinzer, Susan Morse, Eloise Pasachoff, Michael Plowgian, Kirk Stark, David Super, Victor Thuronyi, Eric Zolt, and participants at the UCLA Tax Policy and Public Finance Colloquium for comments on earlier drafts of this paper and/or helpful conversations about the project more generally. Dan Connelly, Mathews Vattamala, and Esther Zuckerman contributed excellent research assistance. All errors remain my own.

3 The data set defines global wealth to include all assets under management across all households worldwide, including worldwide cash deposits, money market funds, listed securities held directly or indirectly through managed investments, and to include all onshore and offshore assets. It excludes wealth attributed to individuals’ own businesses, residences, and luxury goods. See BOS. CONSULTING GRP., GLOBAL WEALTH 2011: SHAPING A NEW TOMORROW 5, 7, 13 (June 2011), available at https://www.bcgperspectives.com/Images/BCG_Shaping_a_New_Tomorrow_May_2011_tcm80-77766.pdf [hereinafter BCG, NEW TOMORROW].

4 See infra note 115 and accompanying text.

Globally, approximately $7.8 trillion, representing more than 6% of all household wealth, is managed through offshore accounts. At the start of the twenty-first century few mechanisms provided effective assistance to a sovereign attempting to tax assets held offshore by the sovereign’s residents. However, the global landscape began to change dramatically in the last few years, largely in response to major tax-evasion scandals involving some of Europe’s best-known banks. New approaches to enhanced cross-border tax cooperation, based on automatic information exchange, have recently been pursued in related projects spearheaded by the United States, the OECD, the European Union, and, most recently, the United Kingdom along with France, Germany, Italy, and Spain. These projects describe mechanisms for information to flow automatically from financial institutions to residence-country governments on investment (illicit financial flows out of developing countries estimated at $850 billion to $1 trillion a year). However, Clemens Fuest and Nadine Riedel are skeptical of all the figures and further conclude that “most existing estimates of tax revenue losses in developing countries due to evasion and avoidance are not based on reliable methods and data.” Clemens Fuest & Nadine Riedel, Tax Evasion, Tax Avoidance and Tax Expenditures in Developing Countries: A Review of the Existing Literature, at VI (Oxford University Centre for Business Taxation, Working Paper 2009).

6 BOS. CONSULTING GRP., GLOBAL WEALTH 2012: THE BATTLE TO REGAIN STRENGTH, 11 (May 2012), available at https://www.bcgperspectives.com/Images/BCG_The_Battle_to_Regain_Strength_May_2012_tcm80-106998.pdf [hereinafter BCG, BATTLE TO REGAIN]. For purposes of the data, wealth managed through offshore accounts is defined as “assets under management booked in a country where the investor has no legal residence or tax domicile.” Id. at 11.

7 The details read like a thriller. Bankers smuggled toothpaste tubes full of diamonds across borders, while governments bought stolen disks that identified tax evaders and handed new identities to the informants. Lynneley Browning, Ex-UBS Banker Pleads Guilty in Tax Evasion, N.Y. TIMES, June 20, 2008, at C8; Carter Dougherty & Mark Landler, Tax Scandal in Germany Fans Claims of Inequity, N.Y. TIMES, Feb. 18, 2008, at C8; Liechtenstein Tax Evasion Scandal: Informant in Investigation ‘Fears’ for His Life, SPIEGEL ONLINE INT’L (Mar. 3, 2008), http://www.spiegel.de/international/business/0,1518,540283,00.html. Under pressure from the G-20, an international standard requiring governments to exchange tax information upon request emerged. On its own, however, information exchange upon request is inadequate to combat offshore tax evasion because it requires the requesting tax administration to know which foreign jurisdiction to ask for information about which taxpayer, and to have other details that prove a credible suspicion of tax evasion. Thus, a number of governments and NGOs began calling for systematic automatic exchange of tax information to curb tax evasion through offshore accounts. The Tax Justice Network has been particularly active and effective in encouraging civil society to focus on the issue of automatic exchange of tax information. See Tax Havens Cause Poverty, TAX JUSTICE NETWORK, http://www.taxjustice.net/cms/front_content.php?idcatart=2&lang=1.
income earned through offshore accounts, thereby facilitating enforcement of residence-country taxation of income earned through offshore accounts.

Switzerland, which manages approximately 30% of the world’s offshore wealth, has generally rejected automatic information exchange. In a rearguard action to prevent automatic information exchange from becoming a global standard, the Swiss have been offering anonymous withholding to a few—and only a few—large developed economies, on a bilateral basis. Under this regime, Swiss banks collect tax from non-resident accountholders and remit the total amounts to the resident countries without identifying the accountholders. One important goal of this Swiss policy appears to be to help Swiss banks continue to offer bank secrecy for the wealthy in emerging countries, even as they cooperate with a few large, developed financial centers to address their offshore tax evasion concerns.

This paper represents the second part of a two-part series. In a prior paper, The Battle Over Taxing Offshore Accounts, I highlighted the commonalities between automatic information exchange and anonymous withholding, and argued that we are witnessing the birth of a new international regime in which financial institutions act as cross-border tax intermediaries with respect to offshore accounts. The paper then explained why cross-border automatic information reporting solutions are preferable to cross-border anonymous withholding. One key point was that automatic information exchange could plausibly be made multilateral,

8 See BCG, BATTLE TO REGAIN, supra note [ ] at 11; see also Mathew Allen, Switzerland under siege as tax row escalates, SWISSINFO.CH (Apr. 14, 2013), http://www.swissinfo.ch/eng/business/Switzerland_under_siege_as_tax_row_escalates.htm l?cid=35501440 (quoting Swiss President Maurer as saying “the state should completely respect the privacy of individuals... There is absolutely no reason that this [automatic exchange of information] should be a theme for us.”). Switzerland’s refusal to accept automatic information exchange is an important obstacle to implementation, both in its own right and because Switzerland can act as a leader of other offshore asset-management jurisdictions.


10 From the perspective of a tax administrator, this comparison is between two second-best alternatives. The ideal compliance system would provide for both non-anonymous withholding and information reporting. This paper does not address that possibility because it is not presently under consideration internationally.
whereas anonymous withholding would not be. More generally, I pointed out that the advantages of multilateral automatic information exchange over anonymous withholding were most important for developing and emerging economies, but did not explore the implications of that point in significant depth. This paper focuses directly on developing and emerging economies’ concerns.

Internationally, automatic information reporting now has the upper hand over anonymous withholding, largely as a result of the United States’ willingness to aggressively leverage its financial markets to coerce asset management jurisdictions into accepting automatic information reporting.\(^\text{11}\) However, to date both U.S. and European efforts have focused primarily on addressing their jurisdiction-specific concerns with offshore tax evasion by their own citizens and residents. As of now, the compliance architectures proposed for these efforts do not take emerging countries’ tax evasion concerns into account.

Tax administrations in emerging and developing economies have a significant stake in ensuring that whatever benefit the large developed economies obtain in the form of automatic information exchange is available to them, too. For these countries, a uniform multilateral automatic information exchange system could positively affect their ability to address offshore tax evasion and, further, could serve to improve the structure of their domestic information reporting and withholding regimes more generally. However, the prospect of these countries benefitting from automatic information exchange turns heavily on the question of whether any new regime provides for uniform or fragmented compliance by financial institutions.

Meanwhile, most multinational financial institutions\(^\text{12}\) would also benefit from a single internationally consistent system for cross-border tax

\(^{11}\) The German parliament’s decision to reject an anonymous withholding agreement with Switzerland is another important part of the story. See David D. Stewart, Swiss Tax Agreement Fails Second Vote in German Parliament's Upper House, WORLDWIDE TAX DAILY, Feb. 6, 2013, available at LEXIS 2013 WTD 25-2; see also Press Release, Swiss Federal Department of Finance (FDF), Switzerland regrets Germany’s “No” to signing of withholding tax Agreement (Dec. 12, 2012), http://wwwefd.admin.ch/dokumentation/medieninformationen/00467/index.html?lang=en&msg-id=47158.

\(^{12}\) The preferences of a multijurisdictional financial institution with a significant tax evasion business would probably differ from the preferences described herein.
administrative assistance. Under any cross-border automatic information reporting or anonymous withholding regime, multinational financial institutions will be co-opted by at least some governments as cross-border tax agents. Financial institutions are interested in avoiding a situation in which they are required to implement multiple different systems in order to satisfy different sovereigns’ demands. Therefore, although their starting points are different, both multinational financial institutions and developing and emerging economies have a shared interest in a single, uniform, broadly multilateral regime for addressing offshore accounts.

Part I of this paper explains why current trends in addressing offshore accounts may risk producing a suboptimal equilibrium that provides fragmented automatic information reporting to a limited number of developed economies under varying compliance rubrics, and only limited improvement for those sovereigns facing the most severe offshore tax evasion problems. Part I argues that the window of opportunity is narrow—a span of perhaps only a few years—in which to begin establishing a robust framework for uniform multilateral automatic information exchange. Part II highlights the potential benefits for emerging countries’ tax administrations of a uniform automatic information exchange regime for taxing income from capital. These benefits relate both to income earned through offshore accounts and income from capital earned domestically. Importantly, for emerging and developing economies a multilateral system to address offshore tax evasion can have compliance benefits that go beyond addressing offshore tax evasion. However, Part II emphasizes that only a uniform regime is likely to provide a benefit to emerging countries. Part II goes on to highlight, why a uniform multilateral regime should also be of interest to multinational financial institutions, such that the interests of these two stakeholders are improbably aligned. Part III proposes the application of international financial law principles to the development of standards for automatic tax information exchange. It describes the institutional components that would be needed to create a uniform multilateral tax-transparency regime that could benefit emerging countries.

13 See, e.g., Letter from James Badenach, Chairman, Capital Mkts. Tax Comm. of Asia (CMTC), to Jeffrey Owens, Dir., Ctr. for Tax Policy & Admin., OECD (Aug. 17, 2010), available at http://www.oecd.org/tax/treaties/46019879.pdf (“because of the plethora of countries involved, our members are very concerned that attempts by tax administrations to gather information are coordinated, in order to avoid separate disclosure regimes applying in different contexts and in different jurisdictions . . . a high degree of standardization is necessary to minimize the compliance burdens that will be increasingly levied on financial institutions, in order to avoid costly inefficiencies arising.”)
and describes steps emerging countries could take to promote the creation of that regime.

Part I. The Dialectic of FATCA

The most influential event in the shift toward automatic information exchange has proven to be the enactment by the United States of legislation known as “FATCA.”\(^\text{14}\) Negotiations between the United States and other countries for the automatic information reporting FATCA requires are broadly credited with substantially accelerating global discussions about multilateral, automatic information exchange.\(^\text{15}\) Paradoxically, this impetus for multilateral progress began as a highly unilateral piece of legislation enacted by Congress with scant overt thought for foreign partners.

The conflicts of law created by FATCA as legislated ensured that, for the most part, the regime initially enacted by Congress would not be the regime that would be implemented worldwide. Meanwhile, the coercive force and political imperatives that motivated FATCA ensure that some regime will in fact come into force. The result is an ongoing dialectic—effectively a search for something better than FATCA to replace it while addressing the same policy concerns—with the outcome depending largely on sovereigns outside the United States.

A. U.S. Policy on Offshore Tax Evasion

1. FATCA as Legislated—The First Phase

In 2010, following the UBS offshore tax-evasion scandal, the United States Congress enacted sections 1471 to 1474 of the Internal Revenue


\(^{15}\) Automatic Response, supra note 14; see also Letter from Pierre Moscovici, Wolfgang Schäuble, Vittorio Grilli, Cristóbal Montoro Romero, and George Osborne, to Algirdas Šemeta, Comm’r for Taxation & Customs Union, Audit & Anti-Fraud, Eur. Comm’n (Apr. 9, 2013), available at http://www.hm-treasury.gov.uk/d/g5_letter_to_european_commission_090413.pdf (letter from the finance ministers of the five largest European economies to the European Union Commissioner for Taxation stating that the impetus for their new initiative to promote automatic information exchange system as an international standard was their discussions with the United States over FATCA).
Code (“FATCA”), which requires foreign financial institutions to report information on financial accounts of U.S. persons and foreign entities with significant U.S. ownership (“U.S. accounts”) directly to the IRS beginning in 2015. Foreign financial institutions must report the account balance or value of each U.S. account and the amount of dividends, interest, other income, and gross proceeds from the sale of property credited to a U.S. account. The rules are intended to provide reporting both on accounts held directly by individuals and on interests in accounts held by shell entities owned by U.S. individuals.

FATCA’s intent was to “force foreign financial institutions to disclose their U.S. account holders or pay a steep penalty for nondisclosure.” Accordingly, FATCA imposed a withholding “tax” on specified payments from U.S. sources and the proceeds from disposing of certain U.S. investments (“withholdable payments”) on foreign financial institutions that do not comply and become a participating foreign financial institution, or “FFI.” This withholding tax also is imposed by the statute.


17 The statutory effective date is January 1, 2013, but regulatory guidance has delayed implementation. See U.S. Dep’t of the Treasury, Timelines for Due Diligence and Other Requirements Under FATCA, Announcement 2012-42 (2012), available at http://www.irs.gov/pub/irs-drop/A-12-42.pdf. U.S. accounts are technically defined as financial accounts that are held by specified U.S. persons or U.S.-owned foreign entities. I.R.C. § 1471(d)(1)(A). Financial accounts are broadly defined by the statute in a manner that is intended to pull in interests in hedge funds, private equity funds, and other investment arrangements.


21 In a conventional withholding tax, withholding on a given payment is associated with the U.S. income tax liability or potential U.S. income tax liability of a given taxpayer in connection with the payment on which withholding is imposed. FATCA is not a conventional withholding tax. It is better understood as a penalty regime intended to force foreign financial institutions to disclose information to the IRS.

22 More technically, withholdable payments are generally any payment of fixed or determinable annual or periodical income, if such payments are from sources within the United States, and gross proceeds from the sale or other disposition of any property of a
on certain other payments for which funding can be attributed to withholdable payments ("passthru payments").

Importantly, this withholding tax is not limited to payments to U.S. persons. If foreign financial institutions do not agree to report to the United States on income earned by U.S. individuals, FATCA requires withholding on a wide range of payments from the United States to those same financial institutions, regardless of whether the payments benefit U.S. persons, non-U.S. customers of the institution, or the institution itself.

FATCA as enacted also required, by means of the passthru payment rules, that participating foreign financial institutions withhold on payments to nonparticipating foreign financial institutions. Those rules were intended to (1) induce foreign financial institutions that were investing in or through participating financial institutions, but that were not investing in the United States, to participate in FATCA, and (2) make participating foreign financial institutions consider whether they would stop doing business with non-participating financial institutions after FATCA was implemented, because business between participating and non-participating financial institutions would require withholding under U.S. law. FATCA’s intent was to use the combined weight of U.S. financial markets and financial institutions that must, as a practical matter, do business in the U.S. markets as leverage with other foreign financial institutions to ensure near-comprehensive compliance with FATCA reporting.

As part of the FFI Agreement, § 1471 requires participating FFIs to deduct and withhold a tax equal to 30% of any passthru payment which is made by the participating FFI to a recalcitrant accountholder or a non-participating FFI. I.R.C. § 1471(b)(1)(D)(i). The statute defines recalcitrant accountholders to be those accountholders that fail to comply with reasonable requests for information by a participating FFI in order for it to meet its reporting obligations under an FFI Agreement, or that fail to provide a waiver in any case in which any foreign law would (but for such waiver) prevent the reporting of any information an FFI is required to report under its FFI Agreement. I.R.C. § 1471(d)(6).

When an FFI is not acting as a custodian or nominee and is not a tax-transparent entity receiving payments on behalf of its members, payments that FFI makes to accountholders (including investors in its equity or debt instruments) would be treated under generally applicable U.S. tax principles as non-U.S. source income of those accountholders, and therefore would not be “withholdable payments.” Thus, in the absence of a “passthru payment” concept, many FFIs that do not do business directly in U.S. securities, and their accountholders, would generally fall outside the scope of FATCA.
2. **FATCA in Practice—The Second Phase**

Nevertheless, it was clear even before enactment that the United States could not unilaterally achieve near-comprehensive financial institution participation with FATCA.\(^{25}\) FATCA as enacted requires foreign financial institutions to report information directly to the U.S. government, and can require closure of certain accountholders’ accounts and/or withholding on payments made by a foreign financial institution to accountholders and other foreign financial institutions. As a result, compliance with FATCA in the manner provided for in the legislation requires foreign financial institutions in many jurisdictions to violate contractual relationships as well as the data protection, bank secrecy, and other laws of the jurisdiction in which they are located.\(^{26}\)

Nevertheless, despite calls for a different approach,\(^{27}\) the U.S. Treasury claimed that it intended to bring FATCA into effect in a manner that accomplished the law’s broad legislative aims and would not defang the provision. Non-U.S. financial institutions felt trapped between a rock and a hard place. It dawned on them that they might have to choose between violating the law of the country where they were based and U.S. rules that could punish them quite seriously if they did not comply with FATCA.\(^{28}\)

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\(^{28}\) *See, e.g.*, Comment Letter from Juan Carlos Jimenez Rojas, Asociacion de Bancos de Mexico, to Manal Corwin et al., U.S. Dep’t of the Treasury (May 10, 2012), http://www.deloitte.com/assets/Dcom-UnitedStates/Local%20Assets/Documents/Tax/us_tax_Asociación_de_Bancos_de_México_Intermediarios_Bursáiles_073012.pdf.
The result was that many financial institutions proceeded down two independent paths: they urged the repeal of FATCA while they also urged governments outside the United States to help them find a way to comply with FATCA without violating local law. In the almost two-year period between enactment of FATCA and the public launch of the intergovernmental FATCA process, there was substantial discussion of FATCA repeal or collapse. Tax practitioners regularly commented that the administrative regime envisioned by the statute was entirely implausible. But that public commentary by private-sector representatives was accompanied by intensive private lobbying of foreign sovereigns to find a solution in intergovernmental discussions with the United States.

The dynamic around calls for FATCA’s repeal changed profoundly when, in February 2012, the United States and five large European governments (France, Germany, Italy, Spain, and the United Kingdom, hereafter the “G-5”) issued a joint statement announcing that they had reached an intergovernmental agreement for implementing FATCA. The intellectual and diplomatic groundwork for that joint statement obviously had been in the making for some time. Joint Statement I benefited substantially from financial institutions lobbying governments outside the United States to find a way to make FATCA compliance possible. This was the first manifestation of the dialectic of FATCA: the legislation’s infirmities, when juxtaposed with its political force, forced financial institutions to lobby foreign governments for a more workable regime.

The joint statement explained that FATCA “raised a number of issues,” including that financial institutions in the European joint statement countries “may not be able to comply with the reporting, withholding and account closure requirements because of legal restrictions.” Accordingly, the six joint statement countries made a

31 Id.
32 Id. In Europe, the primary legal impediment was European data-protection law. “U.K. data protection law currently precludes financial institutions from complying with the U.S. requirements. However under the IGA, the U.K. has agreed to introduce legislation which will enable U.K. financial institutions to provide the data the U.S. requires without
commitment to work together to achieve common reporting and due diligence standards for financial institutions in order to support a move to a more global system to combat offshore tax evasion. The framework adopted in the joint statement was based on reporting by financial institutions to the tax authority of the country in which they are located, followed by reciprocal automatic information exchange between governments. Thus, non-U.S. financial institutions would report information on U.S. persons to the country in which the institution resides and then have the information transferred to the United States by the foreign sovereign, and vice versa. That routing mechanism, in contrast to FATCA’s statutory direct, one-way reporting to the IRS, resolved the conflict-of-law issues. Notably, it did so by bringing the United States into line with the routing mechanism of the European Union Savings Directive (EUSD) and by enshrining information exchange in an international agreement. More importantly, the United States committed, along with its partners, to work toward a common model for automatic information exchange based on full reciprocity. That commitment, along with adoption of the EUSD routing mechanism, created the outlines of a potentially replicable model for a multilateral system.

By July 2012 the U.S. Treasury and the G-5 had turned the joint statement into a detailed model intergovernmental agreement (Model I IGA) to improve tax compliance based on reciprocal automatic information exchange. Since then the U.S. Treasury reports that it has held

33 See Joint Statement I, supra note 30.
34 See Joint Statement I, supra note 30.
35 Id. Joint Statement I ended with a commitment to work in the medium term toward a common model for automatic exchange of information. Further, Joint Statement I suggested that the six governments would develop a shared approach to incentives and mandates, reporting, and customer identification.
discussions with more than seventy-five countries regarding intergovernmental agreements to implement FATCA.\textsuperscript{37} Thus far, agreements based on the Model I IGA have been signed with the United Kingdom, Denmark, Norway, Ireland, and Mexico.\textsuperscript{38} Manal Corwin, until recently America’s leading international tax official and negotiator, spent much of 2012 describing FATCA as evolving toward a global model.\textsuperscript{39}

Indeed, a number of technical features of the Model I IGA agreement are structured to allow FATCA to become a global model. The basic decisions to adopt the EUSD routing model and to embrace reciprocity and multilateralism as aspirations are of course helpful. The


Model I IGA also largely “turns off” the passthru payment rules and gross proceeds withholding of FATCA as legislated with respect to Model I agreement countries. The decision to modulate the most coercive (and most clearly extraterritorial) parts of FATCA with respect to Model I IGA countries is consistent with the joint statement declaration that a collaborative approach to incentives and mandates (which could also be described as “defensive measures”) was under consideration to ensure that other countries and institutions join an automatic information exchange system. A multi-government commitment to finding a substitute approach to achieve the policy objectives of foreign passthru payment and gross proceeds withholding that minimizes burden is more likely to achieve universal or near-universal compliance with FATCA than unilateral U.S. action. Finally, the Model I IGA provides for reporting and due diligence standards that are widely viewed as being less commercially onerous than the FATCA regulations. In principle differentiating among jurisdictions in this way effectuates the policy purpose of encouraging jurisdictions to cooperate in developing FATCA and entering government-to-government automatic information exchange arrangements with the United States.

3. **Sources of Concern under FATCA**

Unfortunately, the relatively simple story of FATCA agreements as a precursor to a multilateral cross-border reporting system is complicated by potential limitations on U.S. reciprocity that may be imposed by U.S. politics, agreements the U.S. Treasury has reached to allow for FATCA implementation outside the reciprocal Model I IGA context, and the compliance model embedded in the Model I IGAs.

As part of the February 2012 joint statement, the United States committed to collecting and automatically reporting information on U.S. accounts of residents of the five large European economies with which the United States issued that statement. But the text of the Model I IGA does

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40 See Reciprocal, supra note 36; Nonreciprocal, supra note 36, at Art. 1(1)(jj), Art(4)(1), Art (6)(2). More specifically, the Model I IGA suggests that a “practical and effective alternative approach” to passthru payments and gross proceeds withholding will be developed. Art. 6(2). The model IGA can thus be read to suggest that certain foreign passthru payment and gross proceeds withholding by withholding agents in Model I IGA countries may be avoided in agreement with relevant IGA Model I partners.

41 See Reciprocal, supra note 36; Nonreciprocal, supra note 36, at Art. 1(1)(jj), Art(4)(1), and Art (6)(2).

42 See Joint Statement I, supra note 30.
not provide for completely reciprocal reporting obligations between the
United States and its FATCA Model I IGA partners. Rather, the IGAs
generally commit partner countries to collect information on all income
earned through financial accounts of U.S. persons, gross proceeds received
in those accounts, and the balance of those accounts. U.S. reportable
accounts are generally defined to include depository accounts, securities
accounts, and interests in hedge funds, private equity funds, and other
investment arrangements. In contrast, the U.S. obligation to report is
limited to those types of accounts on which the United States has authority
to collect information under current U.S. law and regulations. Further, the
income information the U.S. will provide in connection with those accounts
is limited primarily to information on U.S. source interest and dividends
received in those reportable accounts, and there is no account balance
reporting. The Model I IGAs then include a provision in which “the
government of the United States acknowledges the need to achieve
equivalent levels of reciprocal automatic information exchange . . . [and] is
committed to . . . pursuing the adoption of regulations and advocating and
supporting relevant legislation to achieve such equivalent levels of
reciprocally automatic exchange.”

The United States’ commitments in the Model I IGA implicitly
acknowledge certain domestic political constraints that may limit its
capacity to provide full reciprocity to its partners or lead the way to a
working multilateral system. Some banking interests in Florida and Texas
benefit from investment by Latin American residents that allow those
persons to evade their residence-country tax obligations. The United States
is the single most important offshore center for residents of Latin
America. Furthermore, a small number of U.S. senators are deeply
committed to maintaining U.S. competitiveness as a secrecy jurisdiction.
Their willingness to agitate against cooperation to address other countries’

43 See Reciprocal, supra note 36, at Art. 2(2)(a).
44 See Reciprocal, supra note 36, at Art. 1(t)-(v), (dd), Art. 2(2)(a).
45 See id., at Art. 1(t)-(v), (cc), Art. 2(2)(b).
46 See Reciprocal, supra note 36; see also MARY C. BENNETT ET AL., BAKER & MCKENZIE,
TREASURY RELEASES MODEL INTERGOVERNMENTAL AGREEMENTS, OPENS NEW CHAPTER
IN FATCA IMPLEMENTATION 2–3 (2012).
47 Reciprocal, supra note 36, at Art. 6(1).
48 See BCG, BATTLE TO REGAIN, supra note 3, at 4–5, 11.
49 See Letter from Rand Paul, Senator, Jim DeMint, Senator, Saxby Chambliss, Senator, &
Mike Lee, Senator, to Timothy Geithner, Sec’y, U.S. Treasury (July 25, 2012) available at
Senator DeMint has retired and Senator Chambliss has announced he will do so).
offshore tax evasion concerns may limit the U.S. Treasury’s ability to move toward full reciprocity with its FATCA partners, including through international agreements that would require ratification by the U.S. Senate. Shortly after the U.S. Treasury finalized regulations allowing it to collect and report information on all nonresident depository accounts, the House of Representatives passed a bill that would have, *inter alia*, delayed the effective date of those rules had the bill been enacted into law. These political factors may put some pressure on the U.S. Treasury not to go further in international tax cooperation than is necessary to implement FATCA and address U.S. offshore tax evasion concerns. On the other hand, the U.S. Treasury appears to be prepared to confront those pressures; the FY 2014 budget includes a proposal to require U.S. financial institutions to collect information on non-resident accounts that would permit the United States to provide full reciprocity under FATCA.

In June of 2012, the United States and Switzerland agreed to facilitate FATCA compliance in a manner that did not commit to automatic information exchange between governments. Instead, it generally provided for direct reporting by Swiss financial institutions to the United States Internal Revenue Service (IRS), with consenting accountholders reported upon individually and non-consenting U.S. accountholders

50 See Excerpts are Available of U.S. Bill to Bar Regulatory Action, Delay Treasury Regs., WORLDBWIDE TAX DAILY, July 30, 2012, available at LEXIS 2012 WTD 146-29. The Senate did not seriously consider that House bill, but the bill is indicative of the challenges the U.S. Treasury may face in passing additional legislation to ease FATCA implementation.


reported about on an aggregate basis (consistent with FATCA rules).\textsuperscript{54} Switzerland then agreed to provide information exchange upon request with respect to these ascertainable groups of non-consenting U.S. accountholders.\textsuperscript{55} The mechanism is more cumbersome than Model I IGA automatic information exchange, but the end result for the United States is that the Swiss, in essence, agreed to provide information automatically to the IRS. The U.S. receives basically the same information as it would have received under one-step automatic information exchange. However, the routing mechanism of the ensuing agreement differs from the routing mechanism of the Model I IGA. Japan and Bermuda have indicated that they are also interested in pursuing this alternative arrangement with the United States.\textsuperscript{56} If one were to expand the system in the Swiss-U.S. agreement (based on a “Model II IGA”) to all residence countries, every financial institution in the world would have to report to every government on Earth. That model is not commercially viable; it cannot form the basis of a multilateral system.

Meanwhile, the FATCA Model I IGA system may be evolving in a direction that is conducive to uniform, multilateral automatic information exchange only in the sense that it creates a new dialectic: the world may be forced to move toward a multilateral agreement that improves upon FATCA. As discussed further in Part II.B, multinational financial institutions are concerned that the way FATCA is evolving, they will need to contend with a series of different local-country rules for FATCA compliance in each Model I IGA country, further versions of FATCA compliance as a result of Model II IGAs, and, quite separately, compliance with the U.S. Treasury’s FATCA regulations for countries not in an agreement with the United States. Beyond FATCA, they are also concerned that they will need to contend with new rules under the EUSD, the emergence of other FATCA-like initiatives, Swiss anonymous withholding, and other national initiatives. The result may be further calls from these institutions for governments to create a more uniform and less onerous system than is currently evolving to implement FATCA.

\textsuperscript{54} See Joint Statement II, supra note 53, at II(A)(3); Model II Agreement, supra note 53, at Article 2(1)(b)-(e).

\textsuperscript{55} See Joint Statement II, supra note 53, at II(A)(3); Model II Agreement, supra note 53, at Article 2(1)(b)-(e).

B. The Potential Impact of Policy Decisions of Major EU Governments

As I argued in *The Battle Over Taxing Offshore Accounts*, a comprehensive, multilateral system is less likely to emerge if anonymous withholding is accepted.\(^{57}\) Consistent coercive pressure from the large, developed economies is needed to forge a working multilateral system, and bilateral anonymous withholding agreements between major players necessarily diffuse this pressure.\(^{58}\)

In late 2011, Switzerland and the U.K. struck a bilateral anonymous withholding agreement.\(^{59}\) This agreement provides that the investment income and capital gains of U.K. residents with Swiss deposits or accounts will be taxed by Switzerland at agreed rates, with the proceeds remitted anonymously to the U.K.\(^{60}\) Once Swiss financial institutions impose the withholding tax, the investor’s tax obligations to the U.K. are completely fulfilled.\(^{61}\) The U.K. remains unaware of its residents’ Swiss accounts, even though those assets are “regularized.” The U.K. resident has no reporting obligation to their home country on income or capital gains on which the anonymous withholding tax is imposed.\(^{62}\)

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57 See Grinberg, *supra* note [ ].
58 See Grinberg, *supra* note [ ].
60 The U.K. agreement provides for rates slightly below the regular U.K. rates on the relevant categories of income. Thus, the Swiss-U.K. agreement provides that future investment income and capital gains of U.K. residents with Swiss deposits or accounts will be taxed by Switzerland at a rate of 40% on dividend income, 50% on interest income and other investment income, and 27% on capital gains. See U.K.-Switz. Agreement, *supra* note 59, at art. 19(1); U.K.-Switz. Amendment, *supra* note 59, at art. 8.
Switzerland’s leadership recognized that a small number of anonymous withholding agreements with key countries could potentially diffuse the pressure to offer uniform automatic information reporting to a broader group of countries. Thus, the Swiss insisted that the U.K. agree not only to support the anonymous withholding model, but also not to work against it in future dealings with third parties. After the U.K. reached its agreement with Switzerland, and Germany announced a similar deal with Switzerland, other European countries, including Belgium, Greece, and Italy, started negotiating anonymous withholding agreements with the Swiss.

In June of 2012, however, in order to avoid the withholding sanctions FATCA imposed, Switzerland effectively abandoned bank secrecy in its dealings with the United States. Recognizing that it was possible to insist on automatic information exchange from Switzerland, the upper house of the German parliament then refused to ratify the Swiss-German anonymous withholding agreement. Given Germany’s leading

64 The agreement provides that the parties will “neither violate the provisions [of the agreement] through an unilateral act nor work against the agreed provisions in their dealings with third parties.” U.K.-Switz. Agreement, supra note 59.
66 The German government’s policy toward anonymous withholding has been somewhat inconsistent. On the one hand, Germany’s CDU government negotiated an anonymous withholding agreement with Switzerland. Protokoll zur Änderung des am 21. September 2011 in Berlin unterzeichneten Abkommens zwischen der Schweizerischen Eidgenossenschaft und der Bundesrepublik Deutschland über Zusammenarbeit in den Bereichen Steuern und Finanzmarkt [Protocol Amending the Agreement between the Swiss Confederation and the Federal Republic of Germany on Cooperation in the Area of Taxation and Financial Markets Signed in Berlin September 21, 2011], Ger.-Switz., Apr. 5, 2012 (Ger.), available at
role in the EU, the German decision to abandon their treaty with the Swiss slowed and perhaps even stopped other EU jurisdictions from finalizing agreements akin to the U.K.-Swiss agreement. Following the German vote, the Swiss press was filled with pronouncements that anonymous withholding was dead as an alternative to automatic information exchange. Nevertheless, the Swiss finance ministry continues to maintain that more anonymous withholding agreements will be negotiated.

In contrast with Germany, the U.K. proceeded to ratify its anonymous withholding agreement with Switzerland. After the United States, the U.K. is the financial center with which Switzerland has the strongest ties. The U.K. thus could have pressured Switzerland for arrangements similar to the information reporting agreement with the U.S.

http://www.news.admin.ch/NSBSubscriber/message/attachments/26526.pdf. However, the opposition (Germany’s Green party and the German Social Democrats) holds the majority of the seats in the German upper house of parliament, and after the U.S.-Swiss deal, they blocked ratification of the Swiss-German anonymous withholding agreement that the German finance ministry had negotiated. David D. Stewart, German Parliament Rejects Swiss Tax Agreement, WORLDWIDE TAX DAILY (Dec. 14, 2012) available at LEXIS 2012 WTD 241-1. See also Itai Grinberg, Anonymous Withholding Agreements and FATCA’s Future, 137 TAX NOTES 413 (2012) (adapted from author’s testimony before the Finance Committee of the German Bundestag on September 24, 2012).


68 See, e.g., “The Concept of a Withholding Tax has Failed”, SWISSINFO.CH (Nov. 24, 2012), http://www.swissinfo.ch/eng/politics/The_concept_of_a_withholding_tax_has_failed.html?cid=34031006 (surveying Swiss newspapers’ reactions to the Bundesrat vote against the Swiss-German anonymous withholding deal).

69 Switzerland has been in negotiations with Italy and Greece regarding anonymous withholding arrangements, but the timing of any agreement with those two countries is now very much unclear. See, e.g., German-Swiss Tax Deal Sinks at Last-Ditch Meeting, SWISSINFO.CH (Dec. 12, 2012), http://www.swissinfo.ch/eng/business/German-Swiss_tax_deal_sinks_at_last-ditch_meeting.html?cid=34174628. Switzerland had also proposed “Rubik” arrangements to certain other EU governments. See, e.g., Switzerland Proposes Rubik Agreement with Belgium, DE BROECK – VAN LAERE & PARTNERS, http://www.dvp-law.com/documents/nieuwsarchief/20120913-switzerland-proposes-rubik-agreement-with-belgium.xml?lang=en.


71 The U.K. might very well have taken this step under a Labour government. The U.K. Treasury under Gordon Brown was more committed to a multilateral automatic
Instead, as a result of the U.K. ratifying their anonymous withholding agreement, Switzerland argues that the U.S. agreement represents a special case. The Swiss have thus stated that they do not intend to reprise their U.S. agreement with another jurisdiction, and that they are only interested in anonymous withholding with neighboring countries (France, Germany, Italy, and Austria). The Swiss-U.K. agreement therefore helps establish the basis for a suboptimal equilibrium that militates against the emergence of a uniform multilateral automatic information exchange system.

The Swiss-U.K. agreement sits in uncomfortable tension with the UK’s subsequent efforts to “work on a pilot multilateral exchange facility… using the model agreed with the U.S.” with France, Germany, Italy and Spain (the “G-5 Proposal”). Recent progress in that direction has been impressive; indeed the UK has persuaded most of its crown dependencies and overseas territories to commit to joining the proposed FATCA-based multilateral exchange facility. The Swiss-U.K. agreement is also inconsistent with HM Revenue and Customs’ (HMRC) claims that the U.K. will pursue bilateral agreements consistent with the U.K.–U.S. FATCA IGA, and the G-20’s April 19, 2013 agreement to work toward a new international standard of automatic information exchange.

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72 See Yves Hulmann, L’échange automatique d’informations n’est pas requis par l’OCDE, LE TEMPS (March 1, 2013), available at http://www.letemps.ch/Page/Uuid/4c179008-81e4-11e2-a107-60c2515ed554%7C0#.UTP1UTCG2So; Yves Petignat, D’autres pays de l’UE restent intéressés, LE TEMPS (March 4, 2013), available at http://www.letemps.ch/Page/Uuid/a838dd4a-449c-11e2-8c3e-b0a99c10909d%7C0#.UTP0HjCG2So.

73 See Press Release, Swiss Federal Department of Finance (FDF), supra note 12.

74 Letter from Pierre Moscovici et al. to Algirdas Šemeta, supra note 16.


The internal contradictions of U.K. policy are important, because the U.K.’s overseas territories and crown dependencies are, in the aggregate, enormously important managers of offshore wealth. Together with London, they manage at least 20% of the world’s offshore wealth, second only to Switzerland in this regard.

Furthermore, the U.K. has acted to assert substantial control over the development of rules and procedures for future multilateral developments in automatic information exchange. First, the U.K., exerted its authority in FATCA IGA negotiations regarding the process and rules under which information on U.S. accounts held in U.K. overseas territories and crown dependencies would be passed to the United States. By asserting that control, the U.K. gained greater influence over the shape of a future global settlement on information exchange. Now the U.K. is encouraging overseas territories to enter into automatic information exchange IGAs with the U.S. and the U.K. at the same time. It then apparently will offer the other EU countries who chose to join the European multilateral automatic information exchange pilot access to information from the overseas territories under the same set of rules established for information exchanged by the dependent territories with the UK. That development potentially makes the UK a central arbiter of rules for an emerging multilateral automatic information exchange system.

Unfortunately, the U.K. Treasury’s initial administrative approach to FATCA compliance has not been conducive to developing a robust multilateral automatic information exchange system. The U.S. FATCA regulations consistently suggest that FATCA compliance does not require asking U.S.-specific due diligence questions for new accountholders. In negotiations with the United States, however, the U.K. insisted—understandably from a sovereignty perspective—that it would legislate the manner in which U.K. financial institutions comply with FATCA.

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77 BCG, BATTLE TO REGAIN, supra note 3, at 11.
78 BCG, BATTLE TO REGAIN, supra note 3, at 11.
79 This insistence departs from historic U.K. policy with respect to tax information exchange; historically the U.K. allowed its crown dependencies to reach their own individual arrangements with other jurisdictions.
U.K. guidance could have supported a uniform, multilateral automatic information exchange system simply by requiring U.K. financial institutions to systematically collect residence information for new accounts and capture citizenship information where it was made available by the customer. Instead, Her Majesty’s Revenue and Customs’ (HMRC) Guidance Notes for FATCA compliance encourage U.K. financial institutions to modify their procedures for new accounts such that prospective customers will self-certify whether they are or are not U.S. persons. Then additional information that would enable automatic information exchange (such as a taxpayer identification number) would be collected only for those persons who represent that they are U.S. accountholders. Laurence HMS Revenue and Customs’ (HMRC) Guidance Notes for FATCA compliance encourage U.K. financial institutions to modify their procedures for new accounts such that prospective customers will self-certify whether they are or are not U.S. persons. Then additional information that would enable automatic information exchange (such as a taxpayer identification number) would be collected only for those persons who represent that they are U.S. accountholders. Presumably, these rules would need to be changed if a multilateral automatic information exchange pilot involving the U.K. were to become operational. The question will then be whether the U.K. will continue to limit information collection by UK financial institutions to information of residents of EU countries participating in the pilot, or to residents of all jurisdictions. For now, the most recent U.K. political commitments to address offshore tax evasion multilaterally and U.K. regulatory action on the issue diverge.

C. Actions of the European Commission and Consequences of EU Law

The European Commission has been attempting to use FATCA as leverage to build broader automatic information exchange within the EU for a few years. The Commission also regularly suggests that FATCA intergovernmental agreements may lay the foundation for an automatic information exchange agreement between the EU and the U.S. and may

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81 See Guidance Notes, U.K. HM Revenue and Customs, supra note 33 (note that for interest-earning accounts certain information will continue to be collected to comply with the EUSD). HMRC provides the following example of how this would operate: “An individual makes a telephone call to a financial institution requesting to open an account in line with the financial institution’s normal account opening procedures. The telephone operator asks: ‘can you confirm that you are not resident in the U.S. for tax purposes and that you are not a U.S. citizen?’ The individual confirms this on the call and the operator records the confirmation in the financial institution’s system.” As HMRC explains, U.K. legislation will then require financial institutions to verify the reasonableness of the self-certification against other records of the individual obtained by the financial institution, including under anti-money laundering / know your customer procedures. Id. at 40-43. However, “where no other information exists the reasonableness [of the self-certification] is confirmed based on the information in the account opening instruction alone.” Id. at 44.
ultimately lead to a more global arrangement. However, recent European Commission actions may encourage the emergence of competing standards for automatic information exchange that will prevent a uniform multilateral system from emerging.

In 2005 the European Union implemented the European Union Savings Directive (EUSD), a regime intended to meet the relatively narrow goal of ensuring information reporting or withholding on interest payments earned by EU residents holding, in their own name as individuals, accounts earning interest at financial institutions within Europe. Today, to comply with the EUSD, most countries in the EU choose to report information on interest income earned by non-residents residing in other EU jurisdictions to their EU counterpart tax administrations. However, the EUSD requires only that EU member states either report information or withhold anonymously at a rate of 35% on interest earned by EU residents in accounts held at an EU financial institution located outside the country in which the individual resides. Austria and Luxembourg, the two remaining bank secrecy jurisdictions within the EU, use this “transitional” withholding tax system. Since 2012, the European Commission has taken the position that if Austria and Luxembourg sign FATCA agreements with the U.S. to limit the burden of FATCA on their domestic financial institutions, then under a directive agreed in 2011, the Directive on Administrative Cooperation in the Field of Taxation (2011 Directive) and other EU law, Austria and Luxembourg must exchange information automatically with their EU partners as well. Thus, the European Commission used FATCA

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85 EUSD, supra note 83. The withholding tax option is assessed at a rate of 35%. Id. at art. 11(1).
86 Art. 19 of the February Directive provides that “where a Member State provides a wider cooperation to a third country than that provided for under this Directive, that Member State may not refuse to provide such wider cooperation to any other Member State wishing to enter into such mutual wider cooperation with that Member State.” February Directive, supra note 81; Implications of the Foreign Account Tax Compliance Act Agreements with Austria and Luxembourg—Questions, WRITTEN QUESTION TO THE CHIEF
as a source of leverage to broaden automatic information exchange within Europe. That pressure worked. After resisting automatic information exchange for 15 years, Prime Minister Jean-Claude Juncker announced in his April 2013 state of the nation address that Luxembourg would abandon bank secrecy by signing a Model 1 IGA with the United States and then begin to report automatically with respect to interest income of EU member-state residents under the existing EUSD starting in 2015.  

Austria is now completely isolated within the EU on the issue of exchanging savings income information automatically under the EUSD.  

If the need for FATCA agreements forces Austria to join the information reporting mechanism of the EUSD, that will represents a victory for the European Commission and for limited automatic information exchange within the EU. However, stakeholders and analysts almost uniformly agree that the scope of the EUSD is quite narrow.  

The EUSD only provides reporting on interest income, and only on such income earned through conventional depository and custodial accounts held by individuals holding the accounts directly in their own names or through certain passthru entities. Even reporting in those contexts can be avoided on account of various loopholes.  

Further, the EUSD does not cover interest payments made by non-EU paying agents to EU individuals, and it does not cover payments made to most legal entities and arrangements, regardless of where those


Even Austria has suggested it will exchange information on savings income automatically so long as Switzerland does, too.  


entities are organized.\textsuperscript{91}

In February 2011, the EU adopted a roadmap to broaden automatic information exchange among EU member states by going beyond the existing arrangement on interest income to other categories of income.\textsuperscript{92} The Directive on Administrative Cooperation in the Field of Taxation (2011 Directive) requires the European Commission to submit proposals to the European Council before July 1, 2017 for additional categories of income that member states report to one another, potentially including capital gains, dividends, and royalties.\textsuperscript{93} If the European Council decided to require such mandatory information reporting, in addition to interest reported through the European Union Savings Directive (EUSD), EU information reporting would generally overlap with the income reporting (but not the account balance reporting or due diligence) required under FATCA.

The 2011 Directive can be understood not only to require EU countries that enter into a FATCA agreement to join the reporting regime of the EUSD, but further to require EU countries to give each other “most favored nation” (MFN) treatment with respect to all tax information

\[\text{entities are organized.}\textsuperscript{91}\]

\[\text{In February 2011, the EU adopted a roadmap to broaden automatic information exchange among EU member states by going beyond the existing arrangement on interest income to other categories of income.}\textsuperscript{92}\]

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\[\text{If the European Council decided to require such mandatory information reporting, in addition to interest reported through the European Union Savings Directive (EUSD), EU information reporting would generally overlap with the income reporting (but not the account balance reporting or due diligence) required under FATCA.}\]

\[\text{The 2011 Directive can be understood not only to require EU countries that enter into a FATCA agreement to join the reporting regime of the EUSD, but further to require EU countries to give each other “most favored nation” (MFN) treatment with respect to all tax information}\]
exchange. Under that interpretation of the 2011 Directive, if a country enters into a Model I IGA and reports dividends, interest, and other income earned by U.S. persons to the IRS, then it must provide that same level of automatic reporting in each of those income categories to its fellow EU member states as well. Under this latter interpretation, FATCA in combination with the MFN obligation is a powerful weapon in the hands of European governments interested in receiving comprehensive automatic information exchange from other EU jurisdictions.

Of course, the latter, more expansive reading of EU “most favored nation” obligations is contestable. Indeed, taken to its logical conclusion, the MFN analysis produces an odd result. It suggests that whatever rules are agreed with the U.S. could become the rules for exchange within the European Union for any country that wishes to reduce FATCA compliance burdens for its financial institutions by signing a FATCA agreement. This would mean, in the extreme case, that the U.S. would be able to shape not just the types of information that would be reported within Europe but the identification, due diligence, and verification process for an EU-wide cross-border automatic information exchange system through bilateral agreements.

Cherished notions of sovereignty and of the EU as a counterweight to U.S. influence in Europe may lead one to believe that the full-bore “most favored nation” position will not necessarily be victorious within the EU. Even though it has used the MFN argument affirmatively to date, the EU Commission resists the full MFN rationale, at least in part because that would deprive the Commission of a role in determining the architecture for automatic information exchange within Europe. In fact, the European

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95 Whether some middle ground as to the meaning of the “most favored nation” obligation can be found remains to be seen.

96 Commissioner Semetas has already emphasized the need for improvements to the EUSD in response to the G-5 initiative suggesting that EU countries use FATCA IGAs as the basis for multilateral automatic information exchange. EU Commissioner: Time to Move ‘Quicker and Harde’ Against Tax Evasion, Spiegel (Apr. 15, 2013),
Commission has expressed strong support for the political intent, but not the technical detail, of the G-5 Proposal to create a FATCA-based European model for a multilateral system. European Commissioner for Taxation Algirdas Semeta suggested in response to the proposal that the EU should strengthen the EUSD, adopting rules that would be different than FATCA, but that could “probably be made compatible” with U.S. FATCA reporting requirements.97

The European Commission is particularly eager to see adoption of amendments to the Savings Directive proposed by the EU Commission in November 2008 to address some of its present loopholes with respect to reporting on interest income.98 Unfortunately, those amendments, while improving the EUSD, do not create a viable platform for global automatic information exchange. The EUSD, both in its present form and under the proposed amendments, lacks a mechanism to impose coercive force outside the boundaries of the EU in order to ensure compliance with the regime. That lack of extraterritorial coercive force inevitably means that the reporting envisioned in the EUSD can be avoided through use of non-EU entities as payment recipients and non-EU financial institutions as custodians and payment agents. The proposed amendments to the EUSD attempt to address these weaknesses by listing specific organizational forms in various non-EU jurisdictions and requiring EU paying agents to look through these entities if (and only if) the EU paying agent has information on the payment recipient’s ultimate owners. One difficulty with this approach is that the list of entities can never be complete. It can always be arbitrated by tax evaders who find an appropriate entity that is not “listed,” or ensure that anti-money laundering rules do not disclose sufficient information for the EU paying agent to know the identity of the ultimate beneficial owner of the payment. Since the EUSD asks for a party other than the party closest to the ultimate beneficial owner of the payment. Since the EUSD asks for a party other than the party closest to the ultimate beneficial owner (the final EU “paying agent”) to use its AML information to determine ultimate ownership of an item of income, the information used to determine beneficial ownership will


routinely be subpar. Finally, country-specific entity listing systems are politically difficult to maintain in a multilateral system in which countries with listed entities are desired participants. Thus the EUSD is not scalable into a global system. Nevertheless, energy exerted to further develop this suboptimal regime may very well create a competing international standard to FATCA-style exchange, and detract from the establishment of an effective, uniform, multilateral automatic information exchange regime.

D. Where We Are Today

Cross-border administrative assistance involving automatic information reporting or withholding requires adjustments by both tax administrations and global financial institutions regulated by multiple nation-states. Cross-border tax administrative assistance can advance substantially over relatively short periods despite high costs and coordination difficulties. However, the institutional structure is particularly susceptible to punctuated equilibrium, meaning that while there are short periods of advancement, one should expect long periods of stasis.\footnote{The term “punctuated equilibrium” was originally coined by Niles Eldridge and Stephen J. Gould to describe the evolution of species, and contrasts with a slow and gradualist understanding of the process of evolution. Niles Eldridge & S. J. Gould, Punctuated Equilibria: An Alternative to Phyletic Gradualism, in Models in Paleobiology 82, 115 (T.J.M. Schopf ed. 1972).}

The history of information exchange upon request provides an illustrative example.\footnote{See Grinberg, supra note 9, at Part I.} The major developed economies and the OECD spent most of the last forty years attempting to achieve comprehensive information exchange upon request with few results, until the April 2009 G-20 Summit that prompted, within one year, wholesale international adoption of information exchange upon request as a new global norm.\footnote{Following the release of the G-20’s April 2009 communiqué, previously recalcitrant jurisdictions made formal commitments to the OECD information exchange upon request standard and shortly thereafter began passing legislation and entering international agreements to implement their stated commitments. The Group of Twenty, Declaration on Strengthening the Financial System, G-20 (Apr. 2, 2009), http://www.g20.utoronto.ca/2009/2009ifi.pdf (last visited May 28, 2012). See also Grinberg, supra note 9, at Part I.A.}

Since cross-border administrative assistance is likely to be characterized by punctuated equilibria, the development of financial institutions as cross-border tax intermediaries will be path-dependent.
Suboptimal initial choices made now, in this moment of flux, by a small number of powerful actors, may dictate the long-term institutional outcomes both for those actors and for the rest of the world. For instance, policymakers in countries that do not have enough leverage to force asset-management jurisdictions to provide cross-border tax administrative assistance should prefer automatic information reporting to anonymous withholding because the latter cannot be globalized. Yet the adoption or retention of anonymous withholding in just a few key bilateral relationships could stifle the development of multilateral automatic information exchange, precisely because only a small number of jurisdictions have the leverage to coerce asset management jurisdictions to cooperate with a multilateral regime. Similarly, inconsistent sets of rules for automatic information exchange promulgated by a few powerful actors can limit the set of countries that benefit from those rules.

The U.S. Office of the International Tax Counsel’s success in achieving an international legal framework for FATCA implementation has masked the lack of institutionalized multinational coordination to push for uniform multilateral automatic information exchange. FATCA as legislated, IGA Model I, and IGA Model II each represent somewhat different compliance architectures. Each model addresses identification, reporting, scope, verification, routing, and incentive issues in somewhat different ways. These are six key architectural features that must be reconciled in any uniform cross-border information-reporting regime. Furthermore, IGA Model I effectively opens the door to different FATCA compliance processes in every jurisdiction that enters into such an agreement with the United States. These inconsistencies are compounded by the potential lack of coordination with the EU’s proposed expansion of the EUSD. Swiss successes in promoting anonymous withholding for those jurisdictions with sufficient leverage could significantly aggravate the problem.

The result could be a highly fragmented international architecture for cross-border administrative assistance. The United States would receive FATCA reporting from around the world, although under assorted local-country compliance models. The U.K. might insist that all of its dependent

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102 Stafford Smiley, Qualified Intermediaries, The EU Savings Directives, Trace—What Does FATCA Really Add?, 38 CORP. TAX’N, no. 5, 2011, at 20. Doubts are even being raised about whether the G-5’s initiative based on FATCA IGAs will be entirely consistent with the FATCA IGAs.
territories provide the U.K. with information on most U.K. residents automatically. General-purpose automatic information exchange within the EU, perhaps even including dependent territories of EU member states, could also become a reality under an improved version of the EUSD, a model based on the reporting and due diligence obligations envisioned in UK FATCA-style IGAs, or some hybrid thereof. The Swiss (and perhaps other asset-management centers like Liechtenstein) might impose anonymous withholding for a short list of countries, complemented by information provision to the U.S alone. Alternatively, if the EU were to act boldly, it might be able to extract automatic information provision from certain asset managers that are closely linked to the EU (i.e., Switzerland, Liechtenstein) without multilateral coordination. For emerging countries, however, in the absence of coordinated action through multilateral bodies, a more broadly applicable, uniform automatic information exchange system would not be likely to emerge.

On the other hand, on April 19, 2013, the G-20 took an important step toward possibly institutionalizing multilateral coordination on automatic information exchange. The G-20 Finance Ministers’ Washington communiqué suggested that the OECD should work with G-20 countries to make progress toward developing an international standard on automatic information exchange. This G-20 mandate should help put the longstanding expertise of the OECD’s Centre for Tax Policy and Administration (CTPA) regarding automatic information exchange in the service of the development of a uniform automatic information exchange

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104 Certainly the April 2013 announcement by the finance ministers of the five largest EU economies stating that they wish to develop a FATCA-like agreement within the EU makes this outcome more likely. See Letter from Pierre Moscovici et al., to Algirdas Šemeta, supra note 16.

105 Presumably a country like Germany could also strike out on its own and use market-based coercion to insist on financial institutions around the world acting as cross-border information collection agents for its tax authority.

system. As discussed in Part III, that expertise could help support the emergence of a uniform automatic information exchange system.

E. Time Pressures on Action

U.S. support for a uniform, multilateral automatic information exchange system is likely a necessary although insufficient condition for effective international tax cooperation in the area of reporting on offshore accounts. U.S. support is necessary because the United States remains the world’s largest financial market. A window exists for enlisting U.S. support to develop a uniform multilateral system, but that window is likely measured in years, not decades.

FATCA is not yet operational. As a result, the U.S. likely remains amenable to a multilateral solution to address reporting to residence countries with respect to income earned through offshore accounts, and could be relatively flexible about the details of any multilateral system that integrates with FATCA and meets that statute’s objectives. However, once enough IGA Model I and Model II agreements are in force, the U.S. may find that it obtains some measure of FATCA compliance without a consistent platform for multilateral exchange. Furthermore, even if future U.S. Treasury officials recognize that FATCA implementation will be more successful within a multilateral framework, those officials will be bound by their role to implement FATCA in a manner that is focused primarily on offshore tax evasion by U.S. persons. Finally, given domestic political pressures, the U.S. Treasury is in a somewhat tough spot. Their ability to maneuver, at least in the absence of external pressure from foreign sovereigns, may be limited.


109 See Letter from Rand Paul to Timothy Geithner, supra note 50.
If IGA partner countries implemented FATCA by mandating information collection and reporting by financial institutions on all non-resident accounts, and not just by requiring collection of information on U.S. persons, and pushed to establish that practice as an international standard, it would put significant international pressure on the United States to adhere to that standard as well. Such international pressure might be useful to U.S. Treasury officials confronting opponents of automatic information exchange domestically. Thus, action by important trading partners to lay the foundation for a common reciprocal reporting standard could help the United States meet its IGA commitment to move toward full reciprocity.

If an international standard for automatic information exchange were to emerge, one could then imagine the threat of FATCA’s pass-thru payment and gross proceeds withholding being used to help coerce jurisdictions to join a nascent multilateral system. In such a structure, the U.S. would essentially be loaning the force and weight of its financial markets to the world in the service of addressing offshore tax evasion both by U.S. persons and globally. That would mimic the way the threat of U.S. capital-market sanctions is used in other international financial law contexts, like the Financial Action Task Force’s work to address international money laundering and terrorist finance.110

However, if by the end of the decade the U.S. has a functioning—if less satisfactory—unilateral system that addresses offshore tax evasion by U.S. persons, it is more difficult to imagine that the U.S. capital-markets “hammer” will be readily on loan to the global community. As a result there is a kind of race underway today between the establishment of a satisfactory framework for multilateral automatic information exchange and the establishment of a working unilateral U.S. FATCA regime. The more successful a “unilateral” version of FATCA becomes in terms of compliance with U.S. tax law by U.S. persons, and the less progress is made toward a more promising multilateral system over that same time period, the more difficult it will be to get the U.S. to revise FATCA to accommodate a multilateral system or to use its coercive force in a way that benefits both the U.S. and other governments.111 Meanwhile, European

110 See infra note173 and accompanying text.
111 If unilateral FATCA implementation is completed and can be described as a success, convincing the U.S. to change FATCA may raise the same set of issues that the OECD’s CIV/Authorized Intermediary/TRACE project (AI) raise for the United States. The U.S.
efforts to revise the EUSD could distract from efforts to build a truly multilateral system. So the time for stakeholders outside the United States and the EU to begin working actively toward functional, uniform, multilateral automatic information exchange is now.

**Part II: Emerging Economies and Multinational Financial Institutions Have Similar Concerns**

Both emerging country tax administrations and multinational financial institutions have reason to advocate for a uniform automatic information exchange system. Adoption of that system is possible but will require more proactive engagement from many stakeholders than has occurred to date. This Part takes up the concerns of emerging countries and multinational financial institutions. Part III addresses the role of the G-20 and what emerging countries may do to influence events.

**A. Emerging- and Developing-Country Tax Administrations**

Emerging countries frequently lack the administrative ability to collect taxes on certain portfolio income from capital and domestic business income. Uniform automatic information exchange to address the problem of offshore tax evasion would offer substantial opportunities to improve the availability of tax information both from abroad and at home.\(^{112}\) Thus, for many emerging countries, what is at stake in the way FATCA is (or is not) converted into a multilateral system is both their ability to address offshore tax evasion and their ability to use the global effort to tackle offshore tax evasion as an opportunity to improve the information regarding income

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from capital received from domestic sources for tax enforcement purposes. In many emerging countries, an inability to collect tax on capital income of the wealthy may severely undermine tax morale and threaten the broader administration of the domestic tax system. Moreover, in administrative regimes characterized by limited competence, widespread awareness of tax evasion by the wealthy or privileged is often thought to undermine the authority and effectiveness of the state. Thus, for many emerging countries, the stakes associated with establishing a uniform multilateral automatic information exchange regime may go well beyond mere revenue collection for the fisc.

113 See generally Richard M. Bird & Eric M. Zolt, Technology and Taxation in Developing Countries: From Hand to Mouse, 61 NAT’L TAX J. 791 (2008). Taking as a given the current institutional barriers to the administration of capital income taxation on offshore accounts of developing countries residents, many scholar-practitioners are remarkably agnostic on the question of whether developing countries should even attempt to tax portfolio income earned from foreign sources. Bird and Zolt endorse a dual-rate system that attempts to tax income from capital at a lower flat rate as a more administrable compromise that could both raise revenue and symbolically ask more of elites. See Richard M. Bird & Eric M. Zolt, Dual Income Taxation and Developing Countries, 1 COLUM. J. TAX L. 174 (2010). Part of the rationale is simply that income from capital that can be taxed at flat rates through final withholding taxes should be so taxed. Information exchange can help keep capital flight from undermining the efficacy of this pragmatic approach.


115 The Indian Supreme Court, which handled a series of cases associated with corruption and tax evasion in recent years, described the problem as follows: “Unaccounted monies, especially large sums held by nationals and entities with a legal presence in the nation, in banks abroad…would also indicate a substantial weakness in the capacity of the State in collection of taxes on incomes generated by individuals and other legal entities within the country. The generation of such revenues is essential for the State to undertake the various public goods and services that it is constitutionally mandated, and normatively expected by its citizenry, to provide. A substantial degree of incapacity, in the above respect, would be an indicia of the degree of failure of the State; and beyond a particular point, the State may spin into a vicious cycle of declining moral authority, thereby causing the incidence of unlawful activities in which wealth is sought to be generated, as well as instances of tax evasion, to increase in volume and in intensity.” Ram Jethmalani & Ors v. Union of India & Ors, (2011) 8 S.C.C. 1, ¶ 8 (India).
1. **Addressing Offshore Tax Evasion**

More than one-quarter of all Latin American household wealth, representing $900 billion, and almost one-third of all Middle Eastern and African wealth, representing $1.5 trillion, is held offshore.\(^{116}\) Wealth is also much more concentrated\(^{117}\) and growing at a significantly faster rate outside North America, Japan, and Western Europe, with experts expecting that trend to continue.\(^{118}\) In countries with extreme inequality of wealth, widespread awareness of tax evasion through offshore accounts by the wealthy or privileged may be particularly politically salient.\(^{119}\) Meanwhile, their lower administrative capacity reduces many emerging countries’ ability to combat offshore tax evasion with the tools currently available to them.\(^{120}\)

Indeed, offshore tax evasion with respect to portfolio investment income is sufficiently severe that a number of countries simply choose to exempt foreign-source portfolio income in order to avoid imposing a tax obligation that cannot be enforced. The lack of effective enforcement mechanisms also may induce policymakers to reduce tax rates on domestic-source portfolio income to levels that are lower than they would otherwise

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\(^{116}\) **BCG, BATTLE TO REGAIN,** *supra* note 3, at 6, 11.

\(^{117}\) In Europe, for example, 1.1% of households held more than $1 million in assets under management, representing in total 26% of European wealth. *See BCG, New Tomorow,* *supra* note 4, at 5, 7, 7 n.1. In contrast, in Latin America, 0.24% of households held more than $1 million in assets under management, representing 36% of total Latin American wealth, and in the Middle East and Africa, 0.3% of households held more than $1 million in assets under management, representing 54% of total Middle Eastern and African wealth. *Id.*


\(^{119}\) *See Pravin Gordhan,* *Foreword to OECD, Engaging With High Net Worth Individuals on Tax Compliance* (2009).

\(^{120}\) These countries often lack the audit and investigative capacity to determine which country to ask about which resident taxpayer in order to take advantage of information exchange upon request. In contrast, a country like the United States is able to develop a sustained multiyear effort to address offshore tax evasion by using information exchange upon request to help develop the threat of criminal prosecution, and as a result can successfully couple that threat with a voluntary disclosure initiative. *See Prepared Remarks of IRS Commissioner Doug Shulman before the AICPA, TAX NOTES TODAY* (Nov. 7, 2012), available at LEXIS, 2012 TNT 217-14.
select in an attempt to reduce capital flight.\textsuperscript{121} The availability of relevant information is the starting point for processes and systems designed to collect tax.\textsuperscript{122} If information regarding the income flows into offshore accounts were reported to residence-country tax administrations using taxpayer identification numbers or dates of birth, systems could be devised in many countries to electronically match information received in cross-border exchange with taxpayer returns.\textsuperscript{123} This would substantially improve the ability of these tax administrations to collect tax on foreign-source portfolio income and to maintain their desired tax rates on portfolio income generally.

Another important form of offshore tax evasion experienced by emerging countries involves taxpayers evading tax by fraudulently shifting domestic taxable income offshore. Thus, not only is investment income earned through offshore accounts evading tax, but the principal that funds the relevant investments may also have evaded tax.\textsuperscript{124} For instance, an


\textsuperscript{124} See OECD, Seoul Declaration, Third Meeting of the OECD Forum on Tax Administration (September 15, 2006) (thirty-five tax commissioners and deputy tax commissioner from OECD and non-OECD economies express concern regarding outright fraud to conceal income and assets using offshore business entities).
individual might operate an unincorporated domestic business, form a third-country corporation of which he is the disguised owner, and maintain an offshore bank account in the corporate name. The business enters into a contract with the corporation under which the corporation agrees to perform services for the business. Such services are never performed, but the business pays substantial fees for the service, and the fees are deposited into the offshore bank account of the corporation. The business then records the fees as expenses on the business books and records, and because those books and records are used to prepare the individual’s income tax return, his reported domestic taxable income is substantially understated. An automatic information exchange system that reports account balances as well as income flows into offshore accounts may call attention to the existence of foreign assets of a domestic taxpayer that were funded from domestic-source income, profits, or gains that evaded taxation.

Of course, in order for automatic information exchange to improve enforcement of tax obligations tax administrators must be interested in taxing income from capital and opposed to impunity for wealthy tax evaders. In some cases, this condition may not hold. However, the availability of information about offshore accounts may help shift the balance in favor of unbiased tax administration in countries where relatively corruption-free tax administrations or individual tax administrators battle with other state actors to improve tax administration.

Furthermore, many countries have in recent years established semi-autonomous tax administrations. In a country struggling with corruption or fears those in power may abuse that power, an automatic information exchange system may reduce the pressures on a semi-autonomous tax administration because, unlike information exchange upon request, investigations begun as a result of automatic information exchange are less likely to be perceived as politically motivated.125 Similarly, a tax

125 Some commentators claim that bank secrecy needs to be preserved precisely because corrupt and/or authoritarian governments exist and would misuse taxpayer information. This argument conflates the idea that the benefits of a multilateral information exchange system should not be extended to all governments with the proposition that any individual, regardless of whether they reside in a just or unjust, democratic or undemocratic, corrupt or well-administered state, should have the option to individually elect to securely evade their taxes. Governments will invariably decide to deny another specific sovereign information regarding its residents based on a conclusion that the other sovereign’s tax administration is corrupt or the government is fundamentally unjust. Saying sovereigns may properly deny information to certain jurisdictions is different from saying that the wealthy and sophisticated should be able to individually elect to evade paying tax to their state of
administration may find it less difficult to open an audit of politically connected persons when information that suggests such an audit should be conducted is provided from abroad.

2. **Benefits for the Domestic Tax Administrative Architecture**

Importantly, for emerging and developing economies a multilateral system to address offshore tax evasion can have compliance benefits that go beyond addressing offshore tax evasion. The benefits even go beyond improving compliance for domestic business income that today evades tax through the use of offshore accounts. If a uniform compliance regime for offshore accounts emerged, the large, multinational financial institutions would likely implement standardized processes for obtaining proof of residency and tax identification numbers (or dates of birth) as part of their account-opening procedures across jurisdictional boundaries. They would similarly have incentives to undertake firm-wide IT projects aimed at enabling information reporting on dividends, interest, other income, and account balances to governments in a standardized way, with respect to all accounts the financial institution manages. In the context of a multijurisdictional IT project undertaken by a multinational financial institution, reporting on new accounts opened by residents likely would not entail a substantially greater expense than reporting on non-resident accounts alone. Indeed, implementing the same processes for account opening, due diligence, and reporting for resident and non-resident accounts might simplify compliance, particularly if other distinctions presently incorporated into FATCA (e.g., the exclusion of all “low-value” accounts)\(^\text{126}\) were dispensed with in developing the multilateral compliance architecture.

The resulting reporting system could create a base from which to build a more effective domestic tax-compliance system for income taxation residence simply by taking their wealth offshore. See text accompanying *infra* note__ for a discussion of protections against misuse of taxpayer information in an automatic information exchange system.

\(^{126}\) *See* Reciprocal, *supra* note 37, at Annex I, III.A.; Treas. Reg. 1.1471-4(c)(5). U.S. Treasury regulations also provide a “local FFI exception” for local banks that do not solicit accountholders outside their country of organization and at which at least 98% of the accounts by value maintained by the FFI are held by residents. *See* Treas. Reg. 1.1471-5(f)(1)(i). In a unilateral FATCA context, these local FFI exceptions are understandable, but on a forward-going basis there is no reason that financial institutions should not identify all customers’ country of tax residence, particularly when opening a new account.
in emerging countries, and not just for income earned through or held in offshore accounts.\textsuperscript{127} Coercing financial institutions by means of FATCA to use a simple, standardized system for reporting on income from capital, intended to facilitate automatic record-matching, may function like a program for upgrading the capacity of some domestic tax administrations.\textsuperscript{128} Furthermore, providing information on account balances may change risk-reward calculations for would-be evaders with respect to tax evasion for income earned through unincorporated businesses, including in cases when the income on which tax has been evaded is accumulated in domestic accounts.\textsuperscript{129} Finally, even the simplest version of a dual-rate income tax—one that uses flat rate final withholding taxes to impose tax on dividend and interest income earned domestically—benefits from cross-border automatic information reporting as a backstop to limit evasion of that withholding tax by means of capital flight.

That FATCA can be described as a regime imposed by the United States may help some tax administrators overcome political resistance to improved information-reporting systems domestically.\textsuperscript{130} Just entering into a Model I IGA can lend the coercive force of the U.S. Treasury’s regulatory authority to tax authorities wishing to require both multinational financial

\textsuperscript{127} C.f. Kristen A. Parillo and Jaime Arora, Tax Analysts Exclusive: Conversations: Michael Plowgian, 139 TAX NOTES 153 (2013) (Michael Plowgian, formerly of the Office of the International Tax Counsel of the U.S. Treasury Department stating that “I have heard from some countries that they hope that the work being done on standards under FATCA and exchange under the IGAs will help them update their existing [information reporting] systems and bring them into the modern age.”).

\textsuperscript{128} One perpetual issue even in the largest developed economies concerns the leverage that the government is able to reasonably exert to pass the administrative costs of tax compliance on to the financial sector by mandating that they act as domestic tax intermediaries. The challenges in this regard are heightened in the context of weaker sovereigns.

\textsuperscript{129} Richard M. Bird & Eric M. Zolt, Redistribution via Taxation: The Limited Role of the Personal Income Tax in Developing Countries, 52 UCLA L. REV. 1627, 1683 (2005). Many emerging-country governments lack effective information-reporting systems to support the taxation of domestic income earned through unincorporated businesses, even when that income accrues in domestic accounts. Some also lack effective systems to support the taxation of portfolio income from capital earned domestically.

\textsuperscript{130} Of course, this assumes that tax administrators are interested in taxing portfolio income from capital and that the tax administration itself is not corrupt or interested in maintaining the impunity of wealthy tax evaders. In some cases, the tax administration may indeed be entirely beholden to a corrupt state. But many countries have in recent years established semi-autonomous tax administrations, and in some countries relatively corruption-free tax administrations face political struggles with other parts of the state in their efforts to improve tax administration.
institutions and purely local financial institutions to engage in more effective information reporting on income from capital of resident accountholders. Under the Model I IGAs, so-called local FFIs—financial institutions that have no fixed place of business outside the IGA jurisdiction and aim to serve only resident accountholders—are exempt from U.S. FATCA withholding only if they satisfactorily perform either information reporting or withholding at source to enforce the domestic tax obligations of accountholders resident in the IGA jurisdiction.\(^{131}\) If a local financial institution fails to adequately report or withhold for its domestic authorities with respect to resident-country taxpayers, it risks declassification as a “deemed compliant” FFI under FATCA. Non-compliant FFIs are subject to 30% withholding on most payments the financial institution receives from U.S. sources, both for its own account and for the accounts of its customers.\(^{132}\) Thus, local financial institutions in a country in a Model I IGA have a substantial incentive to satisfy the reporting demands of their home-country tax administration.

To put improved reporting in perspective, consider that in recent years, tax and development scholarship has suggested that emerging countries should adopt dual-rate income tax systems that attempt to tax wages progressively and income from capital at a lower but significant flat rate. And indeed, tax policy in many emerging countries has moved in that direction. The idea is to embrace administrable systems that can both raise revenue effectively and symbolically ask more of elites.\(^{133}\) But offshore tax evasion limits policymakers’ flexibility to move in this direction. Better reporting systems that apply both to offshore and domestic accounts can create policymaking space, and thus, a more cooperative international information exchange environment could be a significant source of support for many emerging country income tax systems.

\(^{131}\) See, e.g., U.S.-Ir. Agreement, supra note 39, at Annex II, II.B (similar provisions also appear in Annex II of the other Model I IGAs); Treas. Reg. § 1.1471-5(f)(1)(ii)(A). See also supra note 118.

\(^{132}\) In this sense, FATCA Model I IGAs are responsive to the G-20 mandate to treat tax information exchange as a mechanism by which to help build sustainable revenue bases for inclusive growth and social equity by providing support for developing-country tax administrations. See G-20, Seoul Summit Leader’s Statement (Nov. 12, 2010), available at http://www.g20.org/documents/#p2 (last visited Feb. 25, 2013).

\(^{133}\) See, e.g., Bird & Zolt, Dual Income, supra note 108.
B. Issues for Multinational Financial Institutions

The variation in compliance architectures that current international agreements portend would impose duplicative costs on multinational financial institutions. Shortly after the February 2012 FATCA joint statement was issued, financial institutions emphasized their desire for a universal model to implement FATCA, including consistent compliance requirements and reporting frameworks.\(^\text{134}\) Financial institutions welcomed the intergovernmental agreement approach to implementing FATCA for this reason. But over the last year, financial institutions have realized that even if the rules applicable under each Model I IGA agreement were entirely consistent, financial institutions operating cross-border would still need to familiarize themselves with multiple different compliance regimes: FATCA IGA Model I, FATCA IGA Model II, and regulatory FATCA unmodified by any IGA.\(^\text{135}\)

Moreover, even FATCA Model I IGAs are not uniform; they are evolving toward a local-country compliance model, in which financial institutions are forced to customize compliance processes for each jurisdiction in which they operate.\(^\text{136}\) Under the Model I IGA agreements,


\(^{136}\) See Jeremiah Coder, Extensive FATCA Negotiations Underway, Treasury Announces, 137 TAX NOTES 722 (2012) (quoting Robert Foley of State Street Bank and Trust Co. at a November 8, 2012 American Bar Association Section of Taxation conference); c.f. European Comm’n, supra note 85 (expressing concern regarding the lack of uniformity in FATCA IGAs). The IRS reports that it is in discussions with partner jurisdictions about the possibility of instituting a single computer data format for reporting FATCA information, whether that information is reported directly to the IRS or to the tax administration of a Model I IGA jurisdiction, but that is only one small part of the puzzle. See Regulations Relating to Information Reporting by Foreign Financial Institutions and Withholding on Certain Payments to Foreign Financial Institutions and Other Foreign Entities, 78 Fed. Reg.
financial institutions report about U.S. persons to their home government. The details of how that reporting should be structured, and how due diligence should be conducted to identify U.S. accounts, will be specified in local regulations, even as the general contours of what due diligence needs to be completed is specified in an annex to the IGA agreements. Indeed, U.S. government spokespersons now caution financial institutions that the new FATCA regulations do not apply to financial institutions located in IGA Model I countries, and that for those institutions the relevant details regarding compliance will be a matter of local law. The U.K. Guidance Notes for FATCA compliance discussed in part I.B. provide an example. Without multilateral coordination, every country could issue different guidance to address the core implementation issues associated with identification, due diligence, and verification under FATCA.

Pascal St. Amans, the director of the secretariat to the Committee on Fiscal Affairs (“CFA”), which brings together the senior international tax official of each OECD member state government, identified the consistency challenges posed by the emerging bilateral approach to FATCA.
implementation early in the intergovernmental agreement process. In a letter directed primarily to multinational financial institutions, he wrote:

We also understand your concerns about the two-phased approach outlined in the Joint Statement and the possible cost implications for all stakeholders. As you rightly point out, this approach is dictated by the fast-approaching deadline for implementing FATCA. It will therefore be a challenge to reconcile the need of the United States to meet the FATCA implementation deadline with the wider interest of other countries and financial institutions to ensure that the objectives of the intergovernmental approach are reached on the broadest possible basis without triggering duplicative investments.\footnote{141}{Letter from Pascal Saint-Amans, Dir., Ctr. Tax Policy & Admin., OECD, to Chris Lenon, Chair, BIAC Comm. Taxation & Fiscal Affairs (Apr. 11, 2012), available at http://www.uscib.org/docs/095_PSA_Letter_to_Chris_Lenon.pdf.}

From the perspective of multinational banks,\footnote{142}{Domestically focused financial institutions— institutions with business in only one country or substantially in only one country— would likely have a different perspective. They do not face the duplicative cost problem that confronts multinational financial institutions. Importantly, domestically focused financial institutions are sometimes quite politically influential. The problem is substantially less severe for investment fund managers with a global presence. Any Model I IGA allows a fund manager to know that all accounts opened by distributors in a country with which the U.S. has an IGA are FATCA compliant. Keith Lawson, \textit{Coordinated and Consistently-Applied FATCA Responses Will Benefit the Global Fund Industry} (forthcoming in the Columbia Journal of Tax Law, manuscript draft on file with author).} a local-country compliance model for FATCA, even if the obligations in any given country are “thin,” is probably more expensive than a broader, universal system of FATCA compliance.\footnote{143}{\textit{C.f.} MARY C. BENNETT ET AL., BAKER & MCKENZIE, \textit{TREASURY RELEASES MODEL INTERGOVERNMENTAL AGREEMENTS, OPENS NEW CHAPTER IN FATCA IMPLEMENTATION} 2–3 (2012); see also Lawson, supra note 127.} Informal discussions are said to be ongoing among some IGA Model I countries to alleviate the duplicative cost concerns, but such informal discussions have yet to show results, and no institutional structure has been created to produce soft law or hard law that would make the outcomes of those discussions binding.\footnote{144}{\textit{C.f.} MARY C. BENNETT ET AL., BAKER & MCKENZIE, \textit{TREASURY RELEASES MODEL INTERGOVERNMENTAL AGREEMENTS, OPENS NEW CHAPTER IN FATCA IMPLEMENTATION} 2–3 (2012); see also Lawson, supra note 127.} It is doubtful that compliance rules for FATCA will be made consistent without some formal institutional structure or legal instrument.
Furthermore, unless FATCA is made multilateral, duplicative and inconsistent reporting burdens may multiply internationally. It remains to be seen how the G-5 Proposal for a FATCA-like inter-European system relates either to FATCA Model I IGAs or to a strengthened EUSD. The U.K. is asking financial institutions in overseas territories and crown dependencies to identify U.K. accounts through a process that is similar but not identical to the due diligence required by FATCA. Even as multinational financial institutions address various forms of FATCA-like reporting, they will simultaneously need to facilitate anonymous withholding by their Swiss operations for the United Kingdom, Austria, and any other jurisdictions that enter into anonymous withholding agreements with the Swiss. Passage of the proposed amendments to the EUSD would impose an entirely unrelated set of new compliance obligations for financial institutions. Other countries’ independent reporting initiatives may also consume resources. The fear that international developments will collectively produce a system with disparate, localized compliance burdens animates most recent expressions of concern from financial institutions. For this reason, organizations like the British Bankers’ Association reserve expressions of support for the ongoing process to address offshore tax evasion to the commitment in the Model I IGAs to a

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145 Letter from Pierre Moscovici et al. to Algirdas Šemeta, supra note 16.
148 Aspirational government pronouncements suggest TRACE or FATCA-like reporting may eventually be required for a variety of jurisdictions. See, e.g., Automatic Response: The Way to Make Exchange of Tax Information Work, supra note 15. The EUSD also appears poised for reform and as of this date there is no public indication that it will be reconciled with FATCA. Id.
149 See, e.g., European Comm’n, supra note 85 (European Banking Federation seeks harmonized approach).
common international framework for reporting and due diligence for automatic information exchange.\textsuperscript{150}

Paradoxically, the lack of uniformity in compliance models for offshore accounts creates a source of significant productive tension. Now that the FATCA IGA process is well under way, it is again apparent that the world is faced with a FATCA architecture that may not work smoothly, with the burden of any inefficiencies falling primarily on financial institutions. Financial institutions have been asking the United States Treasury to ensure that the implementing procedures for FATCA compliance are consistent across jurisdictional boundaries, but the limits of U.S. sovereignty have forced the United States to accept other governments’ authority over the relevant regulatory details. At the same time, the burden of non-compliance for financial institutions is very high, and the odds of FATCA repeal are slim to none. Meanwhile, FATCA has paradoxically reduced resistance to amending the EUSD. Thus, FATCA stakeholders are pushed to search for an alternative, more uniform solution. Indeed, industry leaders and government decision makers began reporting earlier this year that such a process was quietly underway.\textsuperscript{151} Then the G-5 finance ministers announced in early April 2013 that they wished to promote FATCA-like automatic information exchange as “the new international standard, including through the various international fora, with the ultimate aim of agreeing a multilateral framework.”\textsuperscript{152} Finally, the G-20 asked the OECD to work on developing an international standard on automatic information exchange.\textsuperscript{153} These developments are just another part of the dialectic of FATCA: FATCA is a catalyst that forces the world to search for something better than FATCA itself, which can effectively replace it while also addressing the underlying policy concerns.


\textsuperscript{152} Letter from Pierre Moscovici et al. to Algirdas Šemeta, \textit{supra} note 16.

C. An Unusual Alignment of Interests

Only a multilateral solution is likely to provide the automatic information reporting that may allow those countries that lack substantial independent leverage over multinational financial institutions to address their offshore tax-evasion concerns. For these countries, the emergence of a fragmented, inconsistent system in which financial institutions serve as cross-border tax intermediaries is troubling. In particular, multinational financial institutions adopting a local-country compliance model for FATCA is antithetical to a uniform system that identifies accountholder country of tax residence, regardless of jurisdiction—the most fundamental building block for any uniform automatic information exchange system. Emerging country tax administrations interested in improving their capacity to tax income from capital should therefore share the concerns that financial institutions express over the potential emergence of a local-country compliance model for FATCA. In this sense, emerging and developing countries’ concerns are consistent with the compliance cost concerns of multilateral financial institutions. Multinational financial institutions would much rather collect information on all account holders in one way than on various subsets of account holders in a half dozen or more different ways.

A more cooperative international tax environment that benefits emerging countries is a shared norm endorsed by the major developed economies and has been reiterated at a series of G-20 summits.154 Rejecting emerging countries’ demands for uniform, consistently available automatic information exchange that is of utility beyond the G-7 economies would require hypocrisy from the finance ministries of the G-7 countries. In the post-financial-crisis environment, it is easy to pillory financial institutions’ demands for commercially reasonable, internationally consistent cross-border regulation as an attempt to scuttle reform by means of delay. Emerging countries evoke a level of sympathy that multinational financial institutions will never receive. Financial institutions would therefore be

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154 The G-20’s London Declaration explicitly committed to a “new more cooperative international tax environment,” and that commitment has been reiterated at each subsequent G-20 meeting. G20, Declaration on Strengthening the Financial System—London Summit (2009) [hereinafter London Communiqué], available at http://www.g20.utoronto.ca/2009/2009ifi.pdf. The G-20 highlighted offshore tax evasion as a particular area of concern by treating work to counter the erosion of developing countries’ tax bases and promote information exchange as one of only two separate action items under the tax pillar of its development agenda. See G-20, Seoul Development, supra note 115.
well-served to support emerging countries’ desire to address offshore tax evasion multilaterally. Meanwhile, some financial institutions may have better access to developed-country finance ministries than many emerging countries. Thus, from the perspective of emerging economies, technical expertise and political support from multinational financial institutions in proposing changes to an emerging automatic information exchange regime may be instrumentally useful.

Part III: Automatic Information Exchange as a Subset of International Financial Law

A uniform, multilateral automatic information exchange regime would require some form of governance structure. This part begins by sketching out the institutional architecture of other successful international financial governance initiatives. It then explores potential institutional details for a governance structure for automatic information exchange.

A. The Architecture of International Financial Law

Across a wide array of subfields of international financial regulation, one sees organizations that drive standard-setting agendas at the international level. Although they are constituted by and issue agreements and declarations with no formal sense of international obligation, these organizations successfully function to regulate complex cross-border financial matters. They typically possess highly developed institutional structures with membership and decision-making rules and processes.  

The Basel Committee, the Financial Action Task Force (FATF), the Financial Standards Board (FSB), and the International Organization of Securities Commissions (IOSCO) provide just a few examples.  


156 Brummer, supra note 148, 63–69. The Financial Standards Board is focused on standards for macro-prudential regulation; the Basel Committee on Banking Supervision is most well-known for its standards of capital adequacy at the individual institutional level; and the International Organization of Securities Commissions is known for setting standards for international securities regulation. None of these organizations have any formal legal basis in the sense of traditional international law, but each has deep influence on international regulatory coordination in member and non-member states alike. Id. at 76. Other “soft law” financial standard setters have narrower mandates, including the International Accounting Standards Board, the Committee on Payments and Settlement...
The effectiveness of these standard setters is highly dependent on their enmeshed relationship with the G-20, a body with the power to demand international coordination, as well as monitoring bodies, enforcement vehicles, and technical assistance providers (“enablers”). At least since the financial crisis, the G-20 has acted as the primary agenda setter for international financial governance, defining broad strategic objectives for international financial regulation. The G-20 provides the political momentum to create international standards. Once those standards are developed in a standard-setting body, a monitoring body determines whether countries are meeting that standard, thereby imposing discipline. Enforcement mechanisms, often established by the G-20 and tied to the monitoring body's judgments, provide further assurance that standards will be met. Finally, technical assistance providers ensure that jurisdictions have the capacity to meet the standards. Taken together, the G-20 and its associated standard setters, monitoring bodies, enforcement mechanisms, and enablers have created a soft-law framework for international financial law.

The cross-border tax evasion scandals of 2008 led presidents and finance ministers from France, Germany, the United States, and the United Kingdom to insist on improved transparency to combat offshore tax evasion. As a result, the G-20 added offshore tax evasion to the international financial regulatory agenda beginning in 2009. As a first step, the G-20 brought tax information exchange upon request into the international financial regulatory fold. That subfield of international tax law now incorporates internationally agreed-upon standards as well as a compliance monitor, enabling bodies, and enforcement mechanisms—in other words, a governance structure that includes all the features of modern international financial law.

In contrast, the G-20 had, until recently, addressed automatic information exchange to only a limited extent. At the November 2011 G-20 Summit, all G-20 countries committed to sign the protocol to the Multilateral Convention on Mutual Administrative Assistance in Tax Systems (known for its Recommendations for Central Counterparties and Core Principles for Systematically Important Payments Systems), and, perhaps most notably, the Financial Action Task Force (FATF).

157 See Brummer, supra note 147, at 68.
158 See id. at 61–114.
Matters (Multilateral Convention), which allows for multilateral automatic information exchange. In other words, the Multilateral Convention provides a legal vehicle for automatic information exchange should jurisdictions choose to adopt the practice. Furthermore, membership in the convention is open to all countries, with particular emphasis placed on including developing economies so that they might benefit from a “new cooperative international tax environment.” But in November 2011, the G-20 countries agreed merely that they would “consider exchanging information automatically on a voluntary basis as appropriate and as provided for in the convention.”

Thus, although G-20 declarations brought offshore tax evasion under the international financial-law rubric, the architecture of modern international financial law for automatic information exchange was not established. Instead, the OECD has been promoting voluntary norms in what is otherwise a U.S.-centric process driven by FATCA. Voluntary participation in multilateral automatic information exchange as envisioned in the November 2011 summit communiqué is insufficient for those wishing to avoid a fragmented information exchange system. Defection from broadly multilateral automatic information exchange carries too many benefits for asset management jurisdictions. Thus, the G-20 needs to be pushed to create a complete international financial law institutional architecture for automatic information exchange. Importantly, the G-20 began to take the first steps in that direction in its April 19, 2013 communiqué. That communiqué “welcomes progress toward automatic exchange of information which is expected to be the standard,” asks the

161 All that is required for the multilateral convention to become a primary legal platform for automatic information exchange (along with bilateral tax treaties and information exchange agreements) is for competent authorities of governments that are signatories to the Convention to enter into a memorandum of understanding that brings automatic information exchange into force. Multilateral Convention, art. 6.
162 April 2009 London Communiqué, supra note __ at 5.
164 Of course, a multilateral automatic information exchange regime also requires a technical architecture. In The Battle Over Taxing Offshore Accounts I explained that there are six key features to building a uniform, multilateral automatic information exchange system—namely routing, reporting, identification, scope, verification, and incentives. See also infra note 165.
OECD to work with G-20 countries to develop that standard, and declares that “the Global Forum will be in charge of monitoring.”165 The remainder of this Part provides some preliminary observations about what a complete international financial law institutional architecture should look like in the case of automatic information exchange.

B. Standard-Setting

Standard setters like the Basel Committee, CPSS, FATF, and IOSCO are charged by the G-20 (or the G-7 in an earlier era) with the development of industry- and financial sector–specific guidelines to achieve objectives determined by the convening body for specific subareas of international financial law.166 To succeed, an emerging automatic information exchange system similarly requires an explicit standard-setting body. At the multilateral level, the relevant staff-level standard-setting expertise for automatic information exchange lies almost exclusively within the OECD’s Centre for Tax Policy and Administration (“CTPA”). Any standard-setter for automatic information exchange should look to the staff of the CTPA for support.

Historically the OECD’s Committee on Fiscal Affairs (“CFA”)—controlled by representatives of the developed economies—has been the dominant multilateral actor in international tax matters. However, the OECD’s role in the international tax regime is currently under some threat because the OECD membership’s share of the global economy is shrinking. From an emerging-country perspective, the development of automatic information exchange through the traditional CFA working-party structure is not ideal, because emerging countries generally are not yet members of the OECD and therefore do not participate or have voting rights in the

166 See BRUMMER, supra note 147; c.f. David Zaring, International Law by Other Means: The Twilight Existence of International Financial Regulatory Organizations, 33 TEX. INT’L L.J. 281, 289 (1998). See also J.C. Sharman, International Organizations and the Implementation of New Financial Regulations by Blacklisting, in INTERNATIONAL ORGANIZATIONS AND IMPLEMENTATION: ENFORCERS, MANAGERS, AUTHORITIES? 48, 50 (2008). These standard setters are most successful when both country representatives and the staff have experience assisting in developing and maintaining sector- or issue-specific guidelines that both address the global problem at hand and consistently accommodate the realities of varied institutional capacity across governmental agencies (e.g. tax administrations) and financial institutions around the world.
CFA.\footnote{A standard-setting project for automatic information exchange could be located within the existing Working Party No. 10 at the OECD, which focuses on information exchange. Under the rules for observership and full participation in working parties, non-OECD members could participate in that work. See Global Relations, Non-member participation in formal OECD bodies, OECD, http://www.oecd.org/globalrelations/nonmemberparticipationinformaloecebdodies/ (last visited Apr. 11, 2013). However, it is doubtful that broad participation on an equal basis from non-member countries could be achieved within a traditional OECD working party. Furthermore, unlike the coordinating body of the multilateral convention (or a Part II OECD body) working party No. 10 of the CFA would include participants from OECD member countries opposed to automatic information exchange (Austria, Switzerland, and, at least historically, Luxembourg) in the standard-setting work.} Furthermore, the working party would have to include participants from member countries that continue to oppose automatic information exchange. But the CTPA professional staff has been actively strengthening the vehicles within the OECD’s architecture where emerging countries can participate as full members and the CTPA staff can effectively respond to their concerns.

The Multilateral Convention provides a legal platform that could be used to create standards for automatic information exchange and take full advantage of the CTPA in a forum that fully integrates emerging countries. The stated objective of the Multilateral Convention is to enable each party to the convention to counter international tax evasion and better enforce its national tax laws. So far, more than fifty developed and emerging countries have signed the Convention, with more countries expected to join soon.\footnote{OECD, OECD SECRETARY-GENERAL REPORT TO THE G20 FINANCE MINISTERS 35 (2013), available at http://www.oecd.org/tax/2013-OECD-SG-Report-to-G20-Heads-of-Government.pdf.} The Convention includes features that allow it to serve as an attractive standard-setting body. It has a “coordinating body” with legal authority to furnish opinions on questions of application of the provisions of the Convention, including those governing automatic information exchange.\footnote{Multilateral Convention, art. 24; Explanatory Report to the Convention as Amended by the Protocol, Protocol Amending the Convention on Mutual Administrative Assistance in Tax Matters, ¶ 240 (May 27, 2010), available at http://www.oecd.org/dataoecd/7/62/48091084.pdf.} The technical support for this coordinating body is provided by the OECD through the CTPA.\footnote{See Explanatory Report to the Convention as Amended by the Protocol, Protocol Amending the Convention on Mutual Administrative Assistance in Tax Matters, ¶ 238 (May 27, 2010), available at http://www.oecd.org/dataoecd/7/62/48091084.pdf.} The membership of the Coordinating Body is limited to competent authorities of jurisdictions that have signed the Convention.
and thereby shown a commitment to deepening international administrative assistance in tax matters. This allows standard setting within the Coordinating Body to exclude jurisdictions opposed to automatic information exchange. The Coordinating Body is authorized to convene an expert group on automatic information exchange under its auspices with the authority to study methods and procedures to increase international cooperation in tax matters. The opinions developed by that expert group can be made public by the Coordinating Body. Public legal opinions as to best practices for automatic information exchange under the Convention would effectively become an international standard.

Regardless of the forum, the standard-setting body would need to address information exchange issues associated with routing, customer identification, reporting, due diligence, verification, and scope. In addition the standard-setter would need to address rules to prevent misuse of exchanged taxpayer information. Clear, agreed standards on this issue should be of particular importance from an emerging-country perspective. The risk of misuse of taxpayer information is the main limiting concern both for the United States and for many other jurisdictions worldwide in connection with the expansion of FATCA-type automatic information reporting into a multilateral model. Settling the issue of

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171 One difficulty is that the recent Protocol to the Multilateral Convention was negotiated primarily to allow all countries to obtain the benefit of information exchange upon request, and countries have joined the Convention for that reason. Thus, the members of the Coordinating Body may not be the appropriate group through which to develop standards for automatic information exchange, which was not the primary purpose for which the Multilateral Convention was developed.

172 Alternatively, a standard setter for automatic information exchange could be set up as an OECD Part II Program. OECD Part II programs allow member and non-member countries to participate within the OECD on an equal footing. In those bodies, OECD and non-OECD economies contribute financially on the same GDP-weighted scale and have the same voting rights. The Financial Action Task Force (FATF) is one such body. The Global Forum on Transparency and Information Exchange is another. See also Grinberg, supra note 9, at Part III. Some of the substantive system design questions raised by these six elements of any uniform multilateral automatic information exchange system are addressed therein.

173 One of the critical principles under today’s existing international standards for information exchange upon request is that the residence state receiving information must ensure that exchanged information is only used for legitimate tax administration purposes. Countries that do not abide by this standard are not entitled to information exchange upon request under current international standards. OECD Model Convention, at art. 26(2).

174 See, e.g., Letter from Alastair M. Fitzpayne, Assistant Sec’y Legislative Affairs, U.S. Treasury Dep’t, to Francisco Canseco, Member Cong. (Feb. 27, 2013), available at LEXIS 2013 TNT 44-21 (assuring member of Congress that the U.S. Treasury has carefully
what protections would be expected for such information in an automatic information exchange system would be a major building block for a uniform, broadly multilateral automatic information exchange system. 176

C. Monitoring Compliance

In various international financial regulatory areas, expert multi-country teams analyze the extent to which a peer country has formally adopted agreed international standards in its domestic laws. In a smaller set of regulatory areas, reviewers also engage in deeper scrutiny of whether national regulators actually implement the principles embodied in international regulatory standards (thereby monitoring implementation). 177

In 2009, when the G-20 chose to make tax information exchange upon request part of international financial law, it reorganized the preexisting Global Forum in order to turn it into a monitoring body focused on both legal frameworks and implementation. 178 Monitoring of the kind performed by the Global Forum imposes a source of discipline to ensure cross-border regulatory coordination to agreed standards.

The current Global Forum is an appropriate monitoring body for automatic information exchange, too. 179 In just a few years, it established itself as the largest international tax grouping in the world, with over 110

examined Mexico’s protections for exchanged information, and also emphasizing that the United States would not exchange information with Venezuela out of concern for misuse of taxpayer information for non-tax purposes by the government in that jurisdiction). 176

Indeed, a multilateral system should include the existing Multilateral Convention’s absolute requirement that governments have laws in place consistent with international standards to prevent the misuse of exchanged information. Monitoring systems, including to prevent such misuse, would also be necessary. 177 See BRUMMER, supra note 147, at 157. For instance, the OECD monitors compliance with the OECD Anti-Bribery Convention through the OECD Working Group on Bribery. The working group uses a peer-review system that consists of three phases: Phase 1 assesses the adequacy of implementing legislation; Phase 2 assesses the effectiveness of the legislation; and Phase 3 assesses the adequacy of the country’s enforcement. See Country monitoring of the OECD Anti-Bribery Convention, OECD, http://www.oecd.org/daf/briberyininternationalbusiness/countrymonitoringoftheoecdanti-briberyconvention.htm (last visited Feb. 13, 2013).


179 The Global Forum would not be an appropriate standard setter for automatic information exchange, given the large numbers of Global Forum members who have not begun to seriously explore automatic information exchange.
member jurisdictions. It has already developed an extensive peer-review mechanism for information exchange upon request that is rivaled in its sophistication only by the FATF, which may have the world’s most lauded peer review mechanism. ¹⁸⁰ “Phase I” peer reviews of Global Forum members examined whether legal and regulatory regimes were in compliance with current international standards for tax information exchange upon request. ¹⁸¹ As a result of that work, many jurisdictions improved their legal and regulatory infrastructure for transparency and exchange of information in tax matters, and others are in the process of doing so.

Global Forum peer reviews could be deepened to examine jurisdictions’ legal regimes and practices surrounding automatic information exchange. Indeed, the G-20 Finance Ministers reached that conclusion at their April 19, 2013 meeting. ¹⁸² The Global Forum should start by evaluating legal regimes and implementation in countries that are already committed to multilateral automatic information exchange. Through this process, they would set monitoring standards against which

¹⁸⁰ For more than twenty years, the Financial Action Task Force (FATF) has focused both on setting standards intended to address money laundering and terrorist financing threats, and monitoring compliance with FATF’s standards. See generally FATF, AN INTRODUCTION TO THE FATF AND ITS WORK (2010), available at http://www.fatf-gafi.org/media/fatf/documents/brochuresannualreports/Introduction%20to%20the%20FATF.pdf; see also FATF, THE FATF RECOMMENDATIONS: INTERNATIONAL STANDARDS ON COMBATING MONEY LAUNDERING AND THE FINANCING OF TERRORISM & PROLIFERATION (2012), available at http://www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/FATF%20Recommendations%20(approved%20February%202012)%20reprint%20May%202012%20web%20version.pdf [hereinafter FATF RECOMMENDATIONS]. The works of the FATF, including its peer-review mechanisms, are widely recognized to have had a significant impact on the global detection and prevention of money laundering and terrorist financing. Over 180 jurisdictions have now committed to implement the FATF Recommendations and to accept peer review by regional FATF bodies to enforce the regime. See FATF ANNUAL REPORT 2010–2011, , at 3; Ian Roberge, Financial Action Task Force, in HANDBOOK OF TRANSNATIONAL GOVERNANCE: INSTITUTIONS & INNOVATIONS 46 (Thomas Hale & David Held eds., 2011). As a result, it has led to the implementation of more robust AML/CFT regimes by financial institutions around the world.

¹⁸¹ After being convened into action by the April 2009 G-20 meeting, the Global Forum developed a “terms of reference” and a “methodology” for determining whether countries were meeting global standards regarding tax information exchange upon request. OECD, IMPLEMENTING THE TAX TRANSPARENCY STANDARDS: A HANDBOOK FOR ASSESSORS AND JURISDICTIONS (July 27, 2010).

¹⁸² Communiqué, Meeting of Finance Ministers and Central Bank Governors, April 18–19, 2013 (Washington).
other countries could be evaluated by first imposing discipline on “members of the club.” One could expect the United States to support a rigorous monitoring effort if it focused on FATCA-type exchange, and if plans for the monitoring body were established before FATCA compliance was otherwise routine. However, timeliness is important. U.S. support is likely a necessary although not sufficient condition for establishing a rigorous monitoring body, and would be less likely to be forthcoming once FATCA begins to operate successfully on a unilateral basis.

The reliability of automatic information exchange is highly dependent on the quality of customer identification and due diligence conducted by financial institutions. Thus, it may be appropriate for the Global Forum to consider a mechanism through which financial institutions’ compliance with AML/KYC and other agreed standards in the automatic information exchange area could eventually be reviewed. There are of course many more financial institutions in the world than the Global Forum would ever wish to review, but it may be possible to establish a risk-based process in which the monitoring body could nominate financial institutions for review in appropriate cases. Such reviews could involve agreed-upon procedures performed by private accounting firms, reporting from internal financial institution audit functions, auditing by tax administration officials, or some combination thereof. Once these reviews were completed, the fact that a review of a particular institution had occurred and the results of the review could be made public. It would be important for strong rules to be established such that no one jurisdiction would be overly active in nominating institutions for review, and to ensure that the resources of the Global Forum were employed in a prudent way.

The Global Forum should also examine whether taxpayer confidentiality is being respected by jurisdictions benefitting from automatic information exchange. Importantly, the current Global Forum review process already includes examination of protections for taxpayer confidentiality.

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183 In this sense, expanding automatic information exchange should emulate the history of the FATF. In contrast, the development of international standards for monitoring automatic information exchange should not mirror the path that was taken with information exchange upon request, where jurisdictions that wished to retain bank secrecy were invited to participate in the Global Forum, a body charged with elaborating how compliance with international standards should be monitored, from the outset. In the medium term, once a standard for automatic information exchange is agreed internationally it would be necessary to determine which less-developed jurisdictions are not expected to comply with that standard.
information and adherence to global norms regarding taxpayers’ rights.\footnote{184 See OECD, IMPLEMENTING THE TAX TRANSPARENCY STANDARDS, supra note 174. (terms of reference describing the globally agreed standard against which all 102 members of the Global Forum are presently being assessed, including terms of reference C.3. and C.4. regarding protecting against misuse of information and ensuring safeguards for taxpayers).} Further, over the last couple of years, the professional staff of the Global Forum learned some invaluable lessons about how to monitor implementation of this issue in practice.\footnote{185 OECD, GLOBAL FORUM ON TRANSPARENCY AND EXCHANGE OF INFORMATION FOR TAX PURPOSES, KEEPING IT SAFE: JOINT OECD/GLOBAL FORUM GUIDE ON THE PROTECTION OF CONFIDENTIALITY OF INFORMATION EXCHANGED FOR TAX PURPOSES (2012), available at http://www.oecd.org/tax/transparency/final%20Keeping%20Safe%20with%20cover.pdf.} Thus it could be reasonably straightforward to amplify the Global Forum’s work in this area to address the risks around misuse of information in an environment characterized by automatic information exchange.\footnote{186 The source of the concern with confidentiality of taxpayer information is a fear of dishonest tax officials who will misuse exchanged information in order to elicit bribes or worse. Individual deviations are of course difficult to detect. But monitoring of the protection of taxpayer confidentiality is likely to have positive benefits in combating corruption in tax administrations more generally.}

D. Enabling Jurisdictions to Benefit

At minimum, certain tax administrations would need an organized program of IT support and training to be established for a consistent information reporting architecture at the level of financial institutions to be of any use to them.\footnote{187 Government IT systems and administrative capacity in developing countries are often inadequate for the purpose of taxing income from capital. See FISCAL AFFAIRS DEP’T, INT’L MONETARY FUND, REVENUE MOBILIZATION IN DEVELOPING COUNTRIES 21 (2011), http://www.imf.org/external/np/pp/eng/2011/030811.pdf; see generally Bird & Zolt, Technology and Taxation, supra note 108.} In 2010–2012, in order to promulgate the new standards for information exchange upon request worldwide, the Global Forum searched for “enablers” that would help countries that lacked sufficient human capital and technical capacity to implement the new information exchange upon request standards.\footnote{188 Concern developed that developing countries would be viewed as failing to meet international standards, and would be unable to benefit from a more cooperative international tax environment or, worse, be subject to sanctions for failing to meet international standards as the result of lack of capacity rather than an intention to disregard the standard. However, the OECD lacked capacity or experience engaging in technical
eventually took on much of this enabling work. The Global Forum also acted as an informal matchmaker between member countries either looking for or being willing to provide technical assistance.\(^{189}\)

G-20 countries could support emerging countries by creating meaningful technical assistance programs intended to facilitate usage of a multilateral information-reporting architecture. The IMF, OECD, United Nations, and the World Bank all recommend that G-20 countries act in concert with or on behalf of developing countries in parallel to their own actions to address offshore tax evasion.\(^{190}\) G-20 technical assistance programs could provide an information-technology architecture for utilizing the automatic information reporting provided by financial institutions, training on how to use that IT architecture, training on how to integrate cross-border automatic information exchange with existing IT systems, or advice on policy changes that might be considered given the availability of automatic information exchange.\(^{191}\) These programs are more likely to be useful to the extent that the compliance architecture for a multilateral automatic information exchange system is uniform across jurisdictions and financial institutions.

There are no “silver bullet” solutions to ensure that automatic information reporting of offshore accounts held by the residents of emerging countries would produce tax revenues for their residence-country tax administrations. One key point is that emerging countries need to develop political will to take on the problems associated with tax

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\(^{189}\) It remains unclear how useful tax information exchange upon request has been for developing-country tax administrations that endeavored to meet the international standards monitored by the Global Forum.

\(^{190}\) See IMF ET AL., supra note 115. The most advanced economies systematically use risk management techniques based on information technology and combined with legislative, educative, and soft and hard enforcement measures to address offshore tax-evasion compliance risks. These advanced economies can provide support in using similar techniques to other jurisdictions. Id. at 27. See also OECD, CTR. FOR TAX POLICY & ADMIN., A FRAMEWORK FOR SUCCESSFUL OFFSHORE VOLUNTARY COMPLIANCE PROGRAMMES (2010), available at http://www.oecd.org/ctp/exchange-of-tax-information/44893002.pdf [hereinafter OECD, Framework].

\(^{191}\) See generally OECD, FRAMEWORK, supra note 184. Note that the Global Forum has repeatedly affirmed its commitment to serve as a platform to facilitate the coordination of technical assistance with respect to information exchange. See, e.g., OECD, GLOBAL FORUM ON TRANSPARENCY AND EXCHANGE OF INFORMATION FOR TAX PURPOSES 12, ¶ 10 (2012), available at www.oecd.org/ctp/harmfultaxpractices/43757434.pdf.
compliance on income from capital or offshore accounts. Nevertheless, technology will continue to alter the environment in which governments seek to collect tax revenue. Colombia trumpets its recently developed ability to match taxpayer information and use statistical-sampling models and other risk-based indicators to select cases for audit. In the Dominican Republic, as of 2005, no tax return had ever been filed electronically and no integrated IT system existed to process paper returns. By 2011, 75% of income tax returns were filed electronically and, in principle, computerized matching was making risk-based auditing possible. The Brazilian revenue administration moved from a paper filing system to successfully processing electronic filing for 98% of the fifty-two million individual tax returns filed each year in the space of thirteen years.

Progress on IT projects to improve tax administration is possible in middle-income countries—even if it is uneven and sporadic.

Furthermore, international standards for participation in an automatic information exchange system might create benchmarks to which domestic tax authorities in less sophisticated countries might aspire. So automatic information exchange on offshore accounts may have compliance benefits even for countries with insurmountable medium-term limitations to participation in a multilateral system.

192 See Glenn P. Jenkins, Information Technology and Innovation in Tax Administration, in INFORMATION TECHNOLOGY AND INNOVATION IN TAX ADMINISTRATION 3 (Glenn P. Jenkins ed., 1996); Richard Bird & Eric Zolt, Tax Policy in Emerging Countries, 26 ENV’T & PLAN.: GOV’T & POL’Y 73, 83 (2008) (“Three ingredients seem essential to effective tax administration: the political will to administer the tax system effectively, a clear strategy for achieving this goal, and adequate resources for the task.”).

193 See Bird & Zolt, Technology and Taxation, supra note 108, at 804.


197 See Letter from Bruno Gurtner to Robin Moncrieff Oliver, supra note 116.
E. Enforcement Mechanisms

International financial regulatory bodies have hard-law effects only if and when international standards are incorporated in domestic legislative and regulatory mandates. A wide range of disciplinary sources, beginning with reputational consequences and explicit institutional shaming and ending with the application of explicit sanctions, appear to effect substantial compliance pull in various areas of international financial law. In some instances, the promise of reciprocity from large states can be sufficient to engender state-level compliance from many jurisdictions. But in other cases, “outcasting” mechanisms and threats of sanctions are needed to enforce new international norms.

For information exchange upon request, achieving universal compliance with international standards required global leaders to declare that they “stand ready to take agreed action against those jurisdictions that do not meet international standards for tax transparency,” and list specific suggested sanctions and non-cooperative countries. Within a few years of being threatened with sanctions by the G-20, those jurisdictions previously unwilling to exchange information upon request in accordance with OECD standards, including some OECD member states, changed their position and began to comply with what was now a global norm. In the aftermath of the April 2013 G-20 Finance Ministers’ communiqué, it is possible to imagine a similar threat of sanctions against major financial centers that are not prepared to participate in automatic information exchange.

198 See BRUMMER, supra note 147, at 112; see also George W. Downs & Michael A. Jones, Reputation, Compliance, and International Law, 31 J. LEGAL STUD. 95, 109 (2002). That compliance pull is directly attributable to the soft-law foundation of international financial law, because the soft-law foundation allows for a much more rapid response to changing international conditions.

199 See generally Oona Hathaway & Scott Shapiro, Outcasting: Enforcement in Domestic and International Law, 12 YALE L.J. 252 (2011). Being labeled as a non-cooperative country can carry real costs; to provide just one example, Standard and Poor’s changed Liechtenstein’s outlook from stable to negative when Liechtenstein was blacklisted by the FATF. See DIANE HINTON & BARRY HANCOCK, STANDARD & POOR’S, OUTLOOK ON LGT BANK IN LIECHTENSTEIN A.G. REVISED TO NEGATIVE; RATINGS UNCHANGED (2000), available at Standard & Poor’s, Global Credit Portal, RatingsDirect 155755.

200 London Communiqué, supra note 146, at 4–5.
FATF and the Financial Stability Board, like FATCA, threaten capital market sanctions as the ultimate tool for ensuring compliance with their respective international regulatory architectures. The burden of imposing those sanctions is borne largely by the large developed economies. That said, just the prospect of capital market sanctions creates a great degree of uncertainty and therefore few costs are actually imposed on the countries threatening sanctions. Instead, significant incentives emerge for financial institutions and other governments to comply.\textsuperscript{201} This same dynamic—basically a game of chicken—explains why FATCA’s 30% withholding threat has been effective in creating a global process toward a system that automatically provides information on U.S. accountholders’ offshore accounts to the IRS.

A similar coercive mechanism imposed by multiple sovereigns may be needed to ensure compliance with (as opposed to nominal commitment to) a multilateral automatic information exchange system that provides benefits to multiple sovereigns. Otherwise non-cooperative jurisdictions and institutions benefit from defecting from the emerging regime, because they can become repositories of choice for tax evaders’ assets without paying a significant price for making that business decision. Unlike the United States, most jurisdictions lack sufficient leverage (via the threat of withholding or other penalties on inbound investment) to unilaterally force cross-border financial institutions to change their due diligence and reporting procedures with respect to residence-country nationals. However, in a multilateral system, not all countries would need to employ the same level of coercive force.

The final FATCA regulations imply a timeframe to develop an international enforcement architecture for automatic information exchange to which the United States might contribute substantially. The treatment of gross proceeds received by entities in Model I IGA countries (not subject to withholding) as contrasted with the treatment of gross proceeds under the FATCA regulations (withholding delayed until 2017), which applies to countries that are not in a FATCA agreement, already suggests that the United States intends to make further use of its coercive force to push recalcitrant jurisdictions into some form of intergovernmental agreement by 2017. Similarly, the final FATCA regulations exempt foreign passthru

\textsuperscript{201} See BRUMMER, supra note 147, at 154.
payments occurring before at least January 1, 2017 from withholding. At that point, though, the U.S. Treasury will need to figure out what to do with these two coercive tools. That opens the possibility for a four-year process in which the United States could agree to coordinate defensive measures against nonparticipating jurisdictions or institutions with other countries. Consistent with the terms of the Model I IGA, countries in Model I agreements would be exempt from any such measure.

The U.S. could potentially threaten to implement gross-proceeds withholding, and (with cooperation from its IGA partners), perhaps passthru-payment withholding against a limited number of noncompliant financial institutions in recalcitrant jurisdictions after 2017. Realistically, though, any step the United States takes to promote a multilateral system would occur only in concert with harmonized measures imposed by other sovereigns. Withholding along the lines of FATCA or denial of treaty benefits for investors using non-compliant financial institutions are realistic sanctions for use by some jurisdictions. Other jurisdictions may fear the deleterious consequences on inbound investment and therefore express interest in less onerous defensive measures. More graduated sanctions to be used by other jurisdictions would, however, be possible in a compliance architecture that featured standard-setting and monitoring bodies and

202 The United States may have chosen to replace passthru-payment withholding in favor of collaborative defensive measures with respect to Model I IGA countries, but intends to require financial institutions outside Model I IGA jurisdictions to withhold on passthru payments in order to remain compliant FFIs after 2017. See Final FATCA Regulations, supra note 129, at 5,877.

203 The history of implementation extensions in the FATCA regulatory process suggests that the U.S. Treasury could delay implementation of foreign passthru payment withholding again before 2017, thereby giving itself and other governments more time to negotiate coordinated defensive measures. Under the current regulations, U.S. implementation of any agreed measure would be gradual, with a six month window for relevant institutions and jurisdictions to come into compliance, and with the weight of any defensive measure growing gradually thereafter.

204 By definition, FATCA-recalcitrant jurisdictions and recalcitrant institutions in the 2013 to 2017 period will be those institutions the U.S. could not effectively coerce on its own. Most observers agree that some such institutions and jurisdictions are likely to exist. The limits of U.S. unilateral action to address recalcitrant jurisdictions and institutions create an opportunity for other countries to condition continued FATCA cooperation after 2017 on a U.S. approach to implementing FATCA withholding after that date that takes other countries’ concerns with their domestic offshore tax-evasion problems into account.
therefore could easily invoke reputational sanctions and more graduated penalties.\textsuperscript{205}

Indeed, the U.S. penalty withholding tax imposed under FATCA combined with the IRS lists of participating and nonparticipating FFIs may set the stage for reputational sanctions to be effective.\textsuperscript{206} Many of the potential defectors in a multilateral system—in particular, financial institutions with regular cross-border dealings and a tax evasion business—operate in a reputational market that can have important influence on behavior under appropriate circumstances.\textsuperscript{207} The FATCA withholding tax penalty is sufficiently high that it prompts self-identification by compliant financial institutions, and the FATCA reporting rules that require reporting to the IRS about transactions with non-compliant FFIs raise concerns on the part of FFIs about the consequences of dealings with non-compliant institutions. In those circumstances, reputational consequences from being labeled non-compliant by a multilateral body would likely be a salient reputational threat. Thus, compliance might improve if, as discussed in Part III.C., a monitoring body were able to review financial institutions’ compliance in appropriate instances.

F. FATCA IGA Negotiations as a Prelude to Multilateral Automatic Information Exchange

Establishing a full, G-20-mandated international financial-law architecture for automatic information exchange is unlikely, as a practical matter, to happen in less than a couple years. Before that time, many developing and emerging economies will likely engage the U.S. Treasury on FATCA IGAs. Rather than viewing IGAs as a necessary step with limited benefits, emerging and developing economies should see two distinct opportunities in these negotiations.

\textsuperscript{206} C.f. Alex Raskolnikov, \textit{Revealing Choices: Using Taxpayer Choice to Target Tax Enforcement}, 109 COLUM. L. REV. 689, 701–05 (2009) (describing the separation function of penalty regimes in the individual taxpayer context); Final FATCA Regs., \textit{supra} note 129, at 105 (providing that the IRS will publish the first list of participating FFIs along with their “Global Intermediary Identification Numbers” on December 2, 2013); Treas. Reg. § 1.1471-3(d)(4); Treas. Reg. § 1.1471-3(e)(3) (FFIs may be removed from the list of participating FFIs); Reciprocal, \textit{supra} note 37, at, art. 5 (2)(b).
\textsuperscript{207} See Susan Morris, \textit{Tax Compliance and Norm-Formation under High-Penalty Regimes}, 44 CONN. L. REV. 675, 687 (2012).
1. Additional Domestic Compliance Benefits in the Bilateral Setting

Tax administrators from emerging countries should conceive of IGA discussions with the United States as an opportunity to negotiate with the U.S. Treasury about steps financial institutions will need to take in their local operations to avoid a sanction imposed by the United States. Thus, tax administrations may wish to review the reporting or withholding that they have wanted financial institutions to do locally. If the relevant reporting or withholding is consistent with FATCA principles, properly negotiated provisions of the IGA may add the threat of U.S. withholding tax as a source of leverage to induce those domestic changes in financial institution tax compliance that have proven difficult to achieve otherwise.

The U.S. Treasury may tell emerging-country tax administrators that IGAs are increasingly standardized rather than negotiated. However, it is clear from the first half-dozen IGAs that there are some variations from agreement to agreement. The U.S. Treasury has acceded to minor variations to accommodate jurisdictional redlines that did not undermine the basic policy purposes of FATCA. Furthermore, although the U.S. Treasury has resisted weakening the provisions of the Model I IGA regarding financial institution compliance, it does not follow that the U.S. Treasury would resist provisions intended to strengthen an IGA’s requirements.

For example, the Model I IGA provides that new or existing individual accounts need to be reviewed, identified, and potentially reported upon only if the account balance exceeds $50,000, unless the FATCA partner country chooses otherwise in domestic regulations. Compliance requirements for accounts under $1 million are minimal. The tax administrations of prospective FATCA partners that want to institute more comprehensive domestic information-reporting systems might consider demanding lower thresholds for their IGAs, consistent with their domestic reporting needs. They would then need to amend the IGA Model I rule that allows financial institutions to elect U.S. Treasury regulations rather than the rules embedded in the IGA if U.S. Treasury regulations are more favorable. These modifications to the Model IGA could assist emerging

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208 A number of U.S. Treasury officials have said recently in public speeches that they believe that the period of IGA modification in country-by-country negotiations is coming to an end.

209 See Reciprocal, supra note 37, at Annex I, ¶ I(C).
countries in using FATCA compliance (U.S. regulatory authority) as a tool to encourage local financial institutions to report and/or withhold more effectively on domestic financial accounts held by resident taxpayers, with negligible but positive effects on U.S. enforcement (such that the modifications should be unobjectionable to the U.S. Treasury).

2. **Encouraging the Emergence of a Multilateral System**

As described in part II, a uniform, multilateral automatic information exchange system could be of substantial benefit to emerging-country tax administrators. Reciprocal automatic information reporting provided to tax administrators by the United States alone is certainly nice, but it will not realistically provide the same benefit in addressing offshore tax evasion. In presenting FATCA to the world, the U.S. Treasury leadership repeatedly said that IGAs to implement FATCA “cannot be the end of the story.”210 Rather, they indicated that “our efforts to implement FATCA and to resolve the challenges it poses can and should advance the important work already begun by the OECD and the European Union to develop multilateral, global approaches to the exchange of financial account information for tax purposes.”211 Thus, the Model IGA includes provisions committing the parties to work with the OECD and other countries to adapt the terms of the Model I IGAs to a multilateral automatic information exchange system.

As discussed in Part I, emerging countries are particularly vulnerable to being left with reporting obligations but very limited benefits in a fragmented automatic information reporting equilibrium. Emerging countries may therefore wish to use upcoming IGA negotiations with the United States as an opportunity to advance a multilateral solution to offshore tax evasion that meets their needs. One option would be for a coalition of like-minded emerging country tax administrations to propose a multilateral IGA negotiation with the United States. The coalition could be led by a few sophisticated emerging jurisdictions that are not offshore financial centers but have already begun bilateral discussions with the United States. One goal of such a multilateral negotiation would be to develop a new Model I IGA that is consistent with earlier IGAs and the

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211 Id.
legislative intent of FATCA, but more effectively addresses the particular circumstances of emerging countries, especially those without well-developed domestic reporting and withholding systems on portfolio income from capital. A group of countries could agree on a short list of amendments that strengthened rather than diluted the Model I IGA (e.g., reporting to the government on a wider range of accounts, elimination of the local-country FFI compliance exception). They could then collectively signal to the U.S. Treasury that they were ready to sign such an IGA contingent on their amendments. That “emerging country” IGA would help inform future negotiations over a multilateral automatic information exchange system.

A multilateral negotiation with a significant number of emerging economies for a developing-country-oriented IGA could be attractive to the U.S. Treasury. FATCA withholding is scheduled to begin on January 1, 2014. As of now the Treasury’s Office of the International Tax Counsel simply lacks the resources to effectively negotiate IGAs bilaterally with all interested jurisdictions before that time. Furthermore, the U.S. Treasury’s prioritization of IGA negotiations with major economies and financial centers may mean that after 2014, the bulk of FATCA withholding will be on financial institutions in smaller, poorer economies. State Department officials focused on development issues and developing countries may already be sensitive to that possibility. As the possibility becomes more real, the Office of the International Tax Counsel will face pressures from both within and without the U.S. government to address the problem. The U.S. Treasury has no incentive to see substantial FATCA withholding result because of the special circumstances of emerging countries that are not financial centers.

A formal mechanism should also be developed by which those emerging countries that are not offshore financial centers could pre-commit to support multilateral automatic information exchange. That mechanism could define an emerging country coalition that could push for a uniform multilateral system. The U.S. Treasury should welcome the development of this formal mechanism since it could ease FATCA implementation—allowing the United States to rely on a formal multilateral commitment to specify jurisdictions with respect to which FATCA withholding should be delayed while a multilateral automatic information exchange system is being developed under the auspices of the G-20. After all, FATCA’s palatability globally is based in part on the U.S. Treasury’s political commitment to use FATCA as a stepping stone to addressing offshore tax
evasion for those countries that are both susceptible to the problem and unable to address it on their own.

Conclusion

Emerging international tax norms assume multinational financial institutions should function as cross-border tax intermediaries. The single most important development causing this new international regime to emerge is the U.S. legislation known as FATCA. If FATCA evolves into a multilateral system, it has the potential to substantially improve the ability of emerging countries to tax portfolio income from capital and much domestic business income. In addition to improving tax morale and revenue collection, for these countries, the capacity to tax such income may be key to addressing broader governance concerns. Some scholars suggest that visible and widely recognized taxation of capital income and closely-held business income at the top of the income distribution is a necessary symbol of the commitment to fairness in a liberal democracy.212 Others suggest that imposing taxes on mobile assets in a transparent manner encourages collective bargaining with the sovereign and thus results in the emergence of more representative and classically liberal government.213 A uniform multilateral automatic information reporting system that identifies prosperous individual taxpayers and requires them to participate in the act of paying taxes would help achieve both of these ends.

Whether FATCA will develop into a uniform multilateral system remains unclear. Instead, a fragmented automatic information exchange system that serves only the interests of the strongest states may emerge. In the absence of successful G-20 leadership, the most likely outcome is a regime that sets standards for automatic information exchange but only achieves automatic information reporting to the United States, and among EU member states, perhaps complemented by some bilateral anonymous

212 See, e.g., Maureen B. Cavanaugh, Democracy, Equality, and Taxes, 54 Ala. L. Rev. 415 (2003); Bird & Zolt, supra note, at 1683 (noting that “symbols matter” and that in the developing world a progressive income tax, “whatever its defects in practice, may be an important and sometimes critical symbol of concern with the distributive outcomes of the market system”). See also Michael J. Graetz, 100 Million Unnecessary Returns, A Simple, Fair, and Competitive Tax Plan for the United States 52–58 (2008) (noting that even schoolchildren conclude that fairness in a democracy involves some degree of progressive taxation based on ability to pay); Roger C. Altman et al., Path to Prosperity 8 (2008); Kenneth M. Scheve & Matthew J. Slaughter, A New Deal for Globalization, 86 Foreign Aff. 34–47 (July/Aug. 2007).
213 See Bates & Lien, supra note; Levi, Of Rule and Revenue, supra note. Niall Ferguson suggests that direct taxes on elites are positively associated with the growth of representative institutions. See Ferguson, The Cash Nexus, supra note at 51, 77–87.
withholding by Switzerland and perhaps other asset-management centers. Such a fragmented, local-compliance architecture would primarily benefit only developed economies.

This fragmented automatic information-reporting regime would be suboptimal for emerging countries for two reasons. First, it would deny them the benefit of a more cooperative international tax environment focused on addressing offshore tax evasion, a problem that afflicts them with particular severity. Second, it would limit their ability to leverage the global effort to tackle offshore tax evasion to assist them in improving their domestic mechanisms to tax portfolio income from capital. For emerging countries, uniform, multilateral automatic information exchange is required to reduce the administrative and political costs of taxing income from capital, whether earned or held through domestic or offshore accounts.

A fragmented international regime would require multinational financial institutions to undertake multiple compliance projects that would incur duplicative costs. Multinational financial institutions would prefer to collect information on all accountholders in one consistent way than to have to develop a dozen different ways of doing so to comply with multiple regimes. The concerns of multinational financial institutions are thus aligned with those of emerging countries. As a result, financial institutions and emerging and developing economy tax administrators may find improbable allies in one another as they navigate the battle over taxing offshore accounts.

With the G-20 as an agenda setter and international financial law as the model, a governance structure for a uniform automatic information exchange regime could emerge that would be useful to emerging-country tax administrators and simultaneously lower multinational financial institutions’ compliance costs. To create such a regime, the G-20 should, with the help of the CTPA (1) use the Multilateral Convention as the primary legal vehicle and standard-setting body for multilateral automatic information exchange; (2) embed a robust monitoring system for examining automatic information exchange practices at both the tax administration and financial institution levels into the existing Global Forum; (3) demand that financial centers commit to automatic information exchange or risk defensive measures, and endorse a long-term enforcement mechanism that is consistent with FATCA’s 2017 deadline for passthru-payment and gross-proceeds withholding; and (4) support technical assistance projects to make uniform, multilateral automatic information exchange useful to tax
administrators of emerging countries. Emerging countries may discuss FATCA IGAs with the United States before the G-20-mandated process to develop multilateral automatic information exchange standards has concluded. They should consider taking positions in those negotiations intended to produce a model for FATCA implementation that can be of benefit to emerging countries and inform standard-setting for a multilateral automatic information exchange system.

Collaboration between emerging-country governments and multinational financial institutions may also help establish a working, commercially reasonable, uniform, multilateral automatic information exchange regime. At the very least, a lobbying partnership between these two stakeholders might make a uniform, multilateral system easier to achieve, with benefits for all parties.