



BANKING & FINANCE

The future of the Luxembourg Banking Secrecy

TAX

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Agenda

- ◆ Definition and forms of mutual assistance in tax matters
- ◆ Current banking secrecy rules in Luxembourg
- ◆ Tax offences under Luxembourg law
- ◆ Current legal framework for mutual assistance in Luxembourg
- ◆ OECD standards and initiatives
- ◆ Recent developments
- ◆ Impact on current Luxembourg legal framework?
- ◆ Impact on the EU Savings Directive?



Definition and forms of mutual assistance in tax matters (1/5) - *General principles*

There are two different forms of exchange of information:

- ◆ mutual assistance in judicial matters; and
- ◆ mutual assistance in administrative matters.



Definition and forms of mutual assistance in tax matters (2/5) - *Mutual assistance in judicial matters*



- ◆ Exchange of information between authorities of two different countries to identify the authors of a crime or penal act;
 - ◆ Information is usually exchanged in a retrospective manner;
 - ◆ Purpose: fact-finding in criminal matters;
 - ◆ Necessarily involves a judge or public prosecutor in both countries concerned.
- ➔ *Issues: diverging national laws, diverging definitions of criminal liability in different jurisdictions!*

Definition and forms of mutual assistance in tax matters (3/5) - *Mutual assistance in administrative matters*



- ◆ Mutual assistance in administrative (including tax) matters can be done between public officers without involving law enforcement agencies (judge, public prosecutor);
 - ◆ Exchange of information takes place between administrative authorities of two States, usually without the intervention of a judge (e.g. tax authorities of both States) on an ongoing basis within an administrative procedure;
 - ◆ Purpose: supervise and check the accuracy of the documents provided in the course of a first instance administrative procedure (e.g. tax assessment to be issued).
- ➔ *Issues: diverging national laws and investigation capacities of administrative authorities in different States!*

Definition and forms of mutual assistance in tax matters (4/5) - ***Main forms of mutual assistance***

◆ Exchange of information on demand or upon request:

→ most commonly used means for exchange of information between administrative bodies of different states;

→ Pre-requisites:

- a tax inspector or public officer of one state has a doubt whether a resident of the respective country has declared income or capital taxes in his country of residence correctly and
- disposes of some kind of information according to which the taxpayer may have failed to declare income from another country.

→ Often included in Double Tax Treaties!

Definition and forms of mutual assistance in tax matters

(5/5) - *Main forms of mutual assistance*

◆ Automatic exchange of information:

- Goes beyond the exchange of information foreseen in most Double Tax Treaties;
- Automatic report (by banks or other paying agents) of all income paid to customers to their tax administration who will in turn send this information to the administration of the home country of the bank's customer;
- Practiced independently of whether there is a suspicion of tax fraud or not;
- Main field of application: EU Savings Directive; however, according to Article 10 of the Directive, Belgium, Luxembourg and Austria may levy withholding tax on savings income on an anonymous basis during a transitional period (see below).
- Other fields of application for automatic exchange of information between tax authorities of the EU: VAT matters.

Current banking secrecy rules in Luxembourg

Luxembourg (1/3) – *Banking Law*



◆ Art. 41 of the law of 5 April 1993:

“(1) The directors, members of the management or the supervisory board, managers, employees and other persons which are at the service of financial institutions, or other professionals of the financial sector, [...], are held to treat any information obtained in the course of their professional activity as being secret. Any disclosure of information is punishable in accordance with Article 458 of the Luxembourg Criminal Law.

(2) The Banking Secrecy ceases to exist in case the disclosure of information is authorized or imposed by law.

...”

Current banking secrecy rules in Luxembourg Luxembourg (2/3) - *Criminal Law (Code Pénal)*



◆ Art. 458 of the Criminal Law (Code Pénal):

“Medical practitioners, surgeons, health officers, pharmacists, midwives and all other persons upon whom, by virtue of fact or profession, secrets are entrusted, shall in case of undue disclosure be punishable by law to a term of imprisonment of eight days to six months and a fine of € 500 to €1’500. The above shall not apply in case where the person has been held to stand as witness in court or where the law prescribes to disclose these secrets.”

Current banking secrecy rules in Luxembourg

Luxembourg (3/3) - *General Tax Law (Abgabenordnung)*



◆ §178bis AO

“No information for the purpose of taxation of the taxpayer shall be requested:

- 1. of credit institutions;*
- 2. of other professionals within the financial sector;*
- 3. of holding companies within the meaning of the law of 31 July 1929, as modified [...];*
- 4. of undertakings for collective investment within the meaning of the law of 30 March 1988;*
- 5. of private wealth management companies (SPF).”*

→ Provision precludes the Luxembourg tax authorities from investigations in the banking & financial sector; information may however be obtained by the law enforcement agencies in charge (court, public prosecutor) in criminal procedures!

Tax offences under Luxembourg law – *Tax fraud*



◆ §396 AO Tax Fraud (« escroquerie fiscale »):

“
...

(5) If the fraud is over a substantial amount, either in absolute terms or in relation to the annual tax liability and was committed through the use of systematic fraudulent methods with the object of concealing the relevant facts from the tax authorities or to convince these of incomplete facts, the act shall be punished as tax fraud with a term of imprisonment of one month to five years and a fine of € 1'250 to the tenfold of the amount of evaded taxes.

...”

→ Provision should only be applicable in case of large amounts (ca. €100'000) or when more than 25% of the total tax liability was evaded;

→ Apart from the « escroquerie fiscale », there are no tax offences under Luxembourg law which are avenged by imprisonment; all other tax offenses are punishable only by fine.

→ Issue: Lower requirements for criminal liability in other jurisdictions!

Current legal framework for mutual assistance in Luxembourg (1/4) - *Overview*

Legal basis:

- ◆ Luxembourg domestic law
- ◆ International treaties
- ◆ Double Tax Treaties



Current legal framework for mutual assistance in Luxembourg (2/4)

– *Luxembourg domestic law*

- ◆ Legal provisions regarding mutual assistance in Luxembourg domestic law are – *amongst others* – contained in the Grand-Ducal Decree of 15 March 1979:
 - Art. 4: Permission of the Luxembourg tax authorities to provide information on the direct tax status of taxpayers to other EU countries;
 - But only if in line with Luxembourg laws and regulations;
 - No exchange of information foreseen with respect to non-EU countries in national law;
 - No exchange of information allowed if a professional secrecy needs to be respected; e.g. the Banking Secrecy (Art. 7 of the said Decree).



Current legal framework for mutual assistance in Luxembourg (3/4) – *International treaties*

- ◆ **European Convention on Mutual Assistance in Criminal Matters (1959); Art. 2 (a), however, provides that assistance may be refused in tax matters;**
- ◆ **In addition, Luxembourg is state party to the European Convention on Extradition (1957); however, also in this regard, no assistance is carried out in relation to tax matters.**



Current legal framework for mutual assistance in Luxembourg (4/4) - *Double Tax Treaties*

- ◆ **Most Double Tax Treaties concluded by Luxembourg are in principle based on the OECD Model Convention;**
- ◆ **As a consequence, these treaties in general already foresee clauses for mutual administrative and legal assistance in assessing and collecting taxes as specified by the respective treaty;**
- ◆ **However, most of the Double Tax Treaties currently in force do not fully comply with latest OECD standards with regard to the mode and extent of exchange of information yet (see below).**





- ◆ Number of OECD initiatives since the year 2000 to improve exchange of information for tax purposes in the light of banking secrecy;
- ◆ *Improving Access to Bank Information for Tax Purposes Report 2000;*
- ◆ *Agreement on Exchange of Information on Tax Matters Report 2002;*
- ◆ Update of article 26 par. 5 of the OECD Model Convention in 2005:

Exchange of information shall not be declined by a contracting state “solely because of the fact that the information is held by a bank or other financial institution, ...”

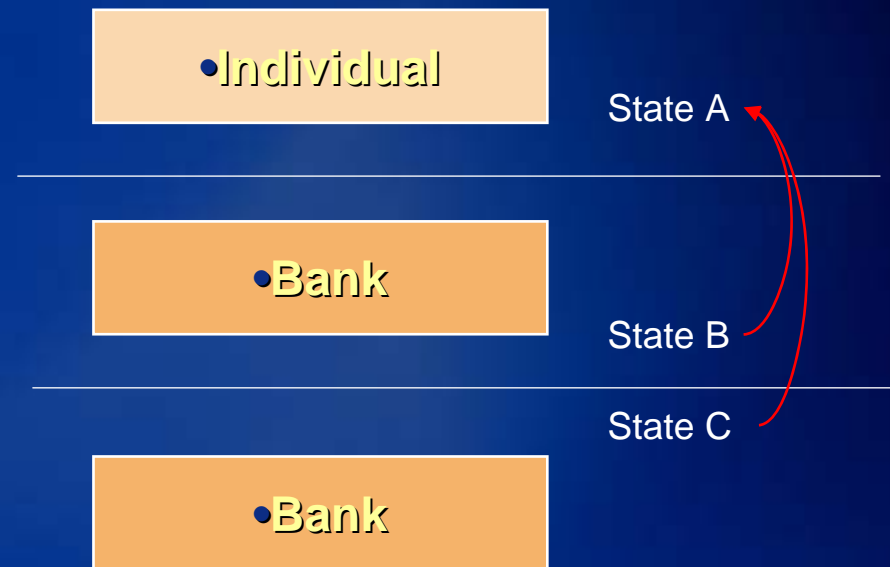
➔ According to this paragraph, a contracting state may thus not decline to supply information anymore on grounds of banking secrecy!

OECD standards and initiatives

(2/3) - *Example*



- A taxpayer of State A withdraws all funds from his bank account and visits a bank in both State B and C and returns to State A without cash. State A sends a request to States B and C for information regarding bank accounts of the taxpayer.
- State B and C should provide information to State A on the accounts. There are grounds to believe that information is held by state A and B.



OECD standards and initiatives (3/3) – *Previous practice in Luxembourg*



- ◆ Luxembourg law knows a banking secrecy under penalty of law;
 - ◆ Exchange of information only if in line with Luxembourg laws and regulations;
 - ◆ Restrictions to the investigation capacities of the Luxembourg tax authorities and law enforcement agencies in the banking and financial sector.
- *Consequence: Luxembourg (together with Austria and Belgium) reserved the right not to include new art. 26 par. 5 of the OECD Model Convention in its Double Tax Treaties in the past!*

Recent developments – ***Announcements of the Luxembourg government***



Announcement of the Luxembourg government on March 13, 2009:

- ◆ Luxembourg plans to relax its strict banking secrecy rules and to increase its cooperation with foreign tax authorities;
- ◆ However, “banking secrecy isn’t incompatible with OECD rules” and “Luxembourg will therefore maintain its banking secrecy as an instrument for protecting private life”.
- ◆ “Luxembourg is in favour of exchanging information on demand, but only in precise cases and with clear proof” of suspicion on fraud;
- ◆ Continuous efforts to be in line with OECD standards on transparency and exchange of information in tax matters but “no fishing expeditions”;
- ◆ Sharing of information on savers with other countries on a case-by-case basis but not automatically!

Impact on current Luxembourg legal framework? (1/4) – *Limits within the OECD framework and scope of discretion?*



- ◆ Exchange of information limited to information foreseeably relevant to the determination, assessment and collection of taxes, recovery and enforcement of tax claims and investigation of tax matters;
- ◆ No obligation to disclose information not in possession of the relevant authorities or persons within territorial jurisdiction;
- ◆ However: information to be provided regardless of whether the conduct investigated would be a crime under the laws of the requested party or not!

Impact on current Luxembourg legal framework? (2/4) – *Limits within the OECD framework and scope of discretion?*



- ◆ Possibilities for declining a request for example if requesting authority would not be able to obtain the information in its own jurisdiction and under its own laws or if disclosure would be contrary to the public policy of the requested country;
 - ◆ Limits to national investigations: a contracting state is in principle not bound to go beyond its internal laws and administrative practice in putting information at the disposal of the other contracting state;
 - ◆ Access to information held by banks and other financial institutions by direct means or indirectly through a judicial or administrative process;
- ➔ *However, refusal may not be based on reasons related to a person's status as a bank or financial institution!*

Impact on current Luxembourg legal framework? (3/4) – *Double Tax Treaties*



- ◆ It can be expected that Luxembourg will live up to OECD expectations to share information with other countries on suspected tax offenders by updating its Double Tax Treaty network;
- ◆ Insertion of new expanded exchange of information clauses which are in line with article 26 par. 5 of the OECD Model Convention is expected.

Impact on current Luxembourg legal framework? (4/4) – *Luxembourg domestic rules*



◆ Adaptations to legislation currently in force in Luxembourg?

- Loosening of the banking secrecy rules laid down in Luxembourg banking law (Art. 41 of the law of 5 April 1993)???
- Granting of investigation capacities to the Luxembourg tax authorities in the banking & finance sector in future (modification of § 178b AO)???
- Lowering of the requirements for criminal liability in case of tax offences (modification of § 396 AO)???

Impact on the EU Savings Directive ?

Impact on the EU Savings Directive? (1/7)

Overview



- ◆ The Directive is aimed at savings income in the form of interest payments made in one Member State to beneficial owners who are individuals resident in another Member State;
- ◆ The ultimate aim of the Directive is the exchange of information as decided at the Council of Feira in 2000;
- ◆ During the “transitional period”, Austria, Belgium and Luxembourg are permitted to apply a withholding tax on interest payments on an anonymous basis instead of exchanging information with other jurisdictions;

Impact on the EU Savings Directive? (2/7) – *Transitional period*



◆ According to the Directive, the transitional period shall end at the end of the first full fiscal year following the later of the following dates:

- The date of entry into force of an agreement between the European Union, following a unanimous decision of the Council, and the last of the following signatories provide for the exchange of information upon request as defined in the OECD Model Agreement on Exchange of Information on Tax:

Switzerland, Liechtenstein, San Marino, Monaco and Andorra

- the date on which the Council agrees by unanimity that the USA is committed to exchange of information upon request as defined in the OECD Model Agreement.

➔ ***Consequence: once the above criteria are met, Luxembourg may have to agree to an automatic exchange of information!***

Impact on the EU Savings Directive? (3/7) – *Recent developments*



◆ Last week

- the **Swiss** Confederation,
- the Principality of **Liechtenstein**,
- the Principality of **Monaco** and
- the Principality of **Andorra**,

announced that they would adopt the rules regarding the exchange of information upon request as defined by OECD standards

- ◆ **Belgium** had agreed earlier on to switch to exchange of information system as defined by the EU Savings Directives as from 2010
- ◆ **Hong Kong** and **Singapore** announced that they would also adopt the rules regarding the exchange of information upon request as defined by OECD standards

Impact on the EU Savings Directive? (4/7) – *Recent developments*



Announcements of the Luxembourg government on Friday, March 13, 2009:

- ◆ “Luxembourg will maintain its banking secrecy”
- ◆ Luxembourg explicitly announced that it would adopt the OECD Model Agreement on exchange of information; the current interpretation foresees an exchange of information only upon request in specific cases and based on specific evidence (“preuves concrètes”);
- ◆ Cooperation on sharing information on savers with other countries on case-by-case basis and not automatically;
- ◆ In addition, the Luxembourg Government announced that the OECD standards on exchange of information “should be the sole standard to be applied within the EU”.

Impact on the EU Savings Directive? (5/7) – *Recent developments*



Recent EU initiatives:

- ◆ Proposal for a Council Directive concerning mutual assistance for the recovery of claims relating to taxes, duties and other measures dated February 2, 2009 (2009/0007 (CNS))
- ◆ Proposal for a Council Directive amending Directive 2003/48/EC on taxation of savings income in the form of interest payments (COM (2008) 727) → proposed updates of Savings Directive

Impact on the EU Savings Directive? (6/7) – *Outlook*



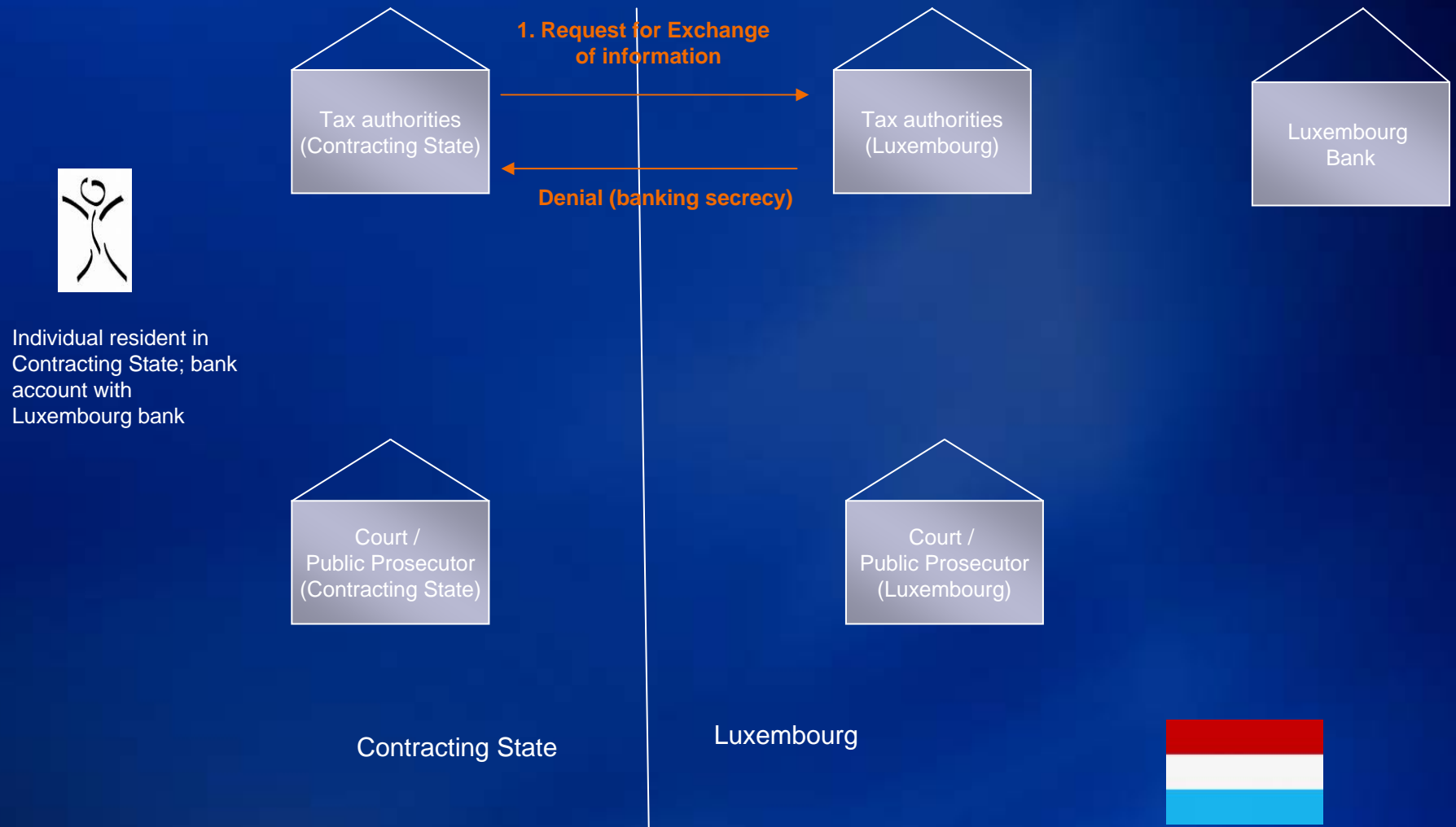
- ◆ Automatic exchange of information as defined in Article 9 of the Savings Directive would violate the Luxembourg banking secrecy in its current form as defined in Article 41 of the Law of 1993;
- ◆ In addition, article 9 of the Savings Directive does not require any request by another foreign tax authority nor any well-founded suspicion of tax evasion or tax fraud;
- ◆ Following the recent developments, it has become more likely that the transitional periods as defined under the EU Savings could be renegotiated in the near future.

Impact on the EU Savings Directive? (7/7) – *Outlook*

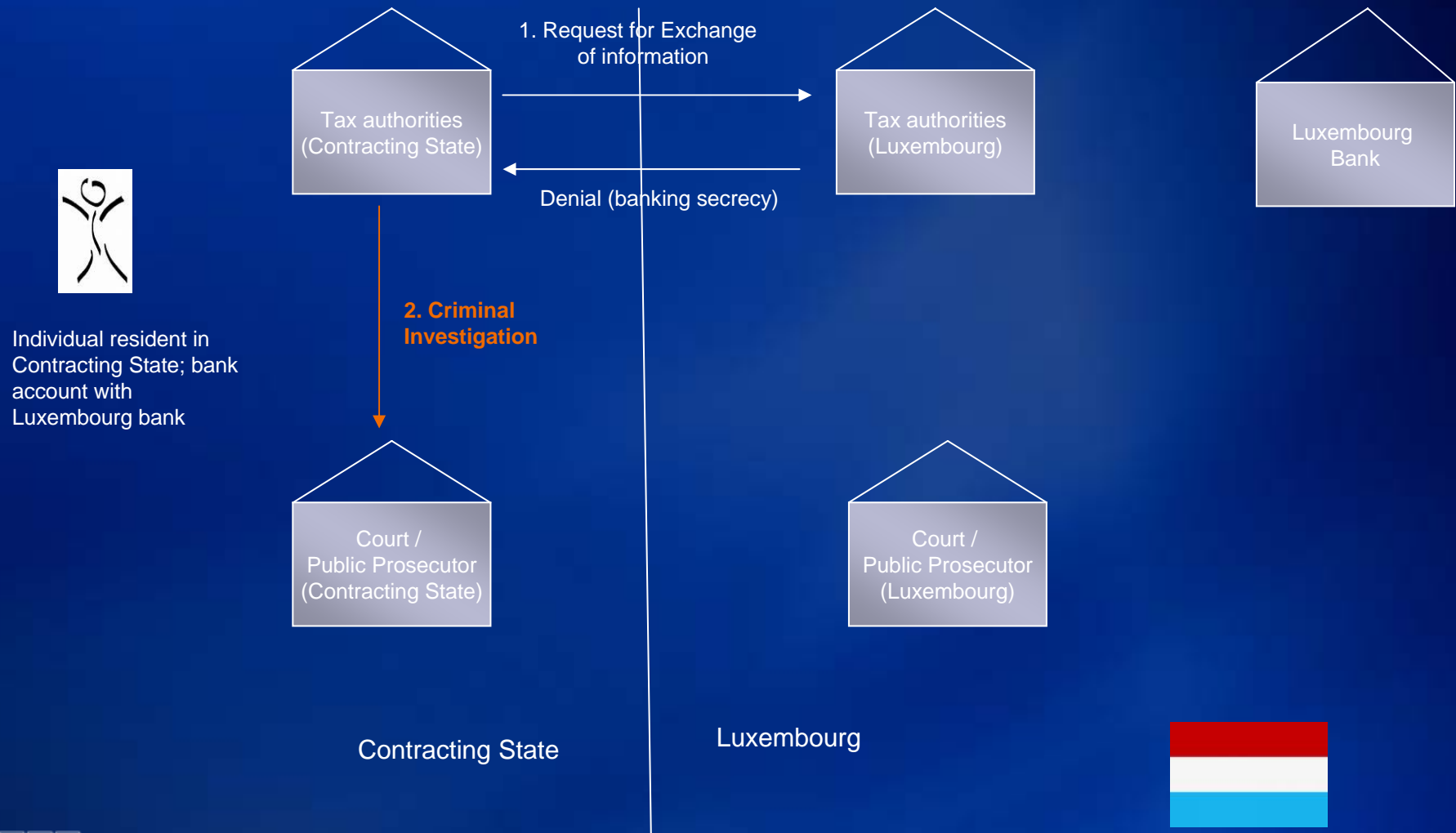


- ◆ No “automatic” adaptation of EU Savings Directive through recent announcements; adaptation requires “unanimous consensus” of all Member States including Luxembourg;
- ◆ However, political scope of discretion may become narrower and political pressure may become even higher with a number of “classical” banking jurisdictions announcing the introduction of exchange of information systems in line with OECD standards.

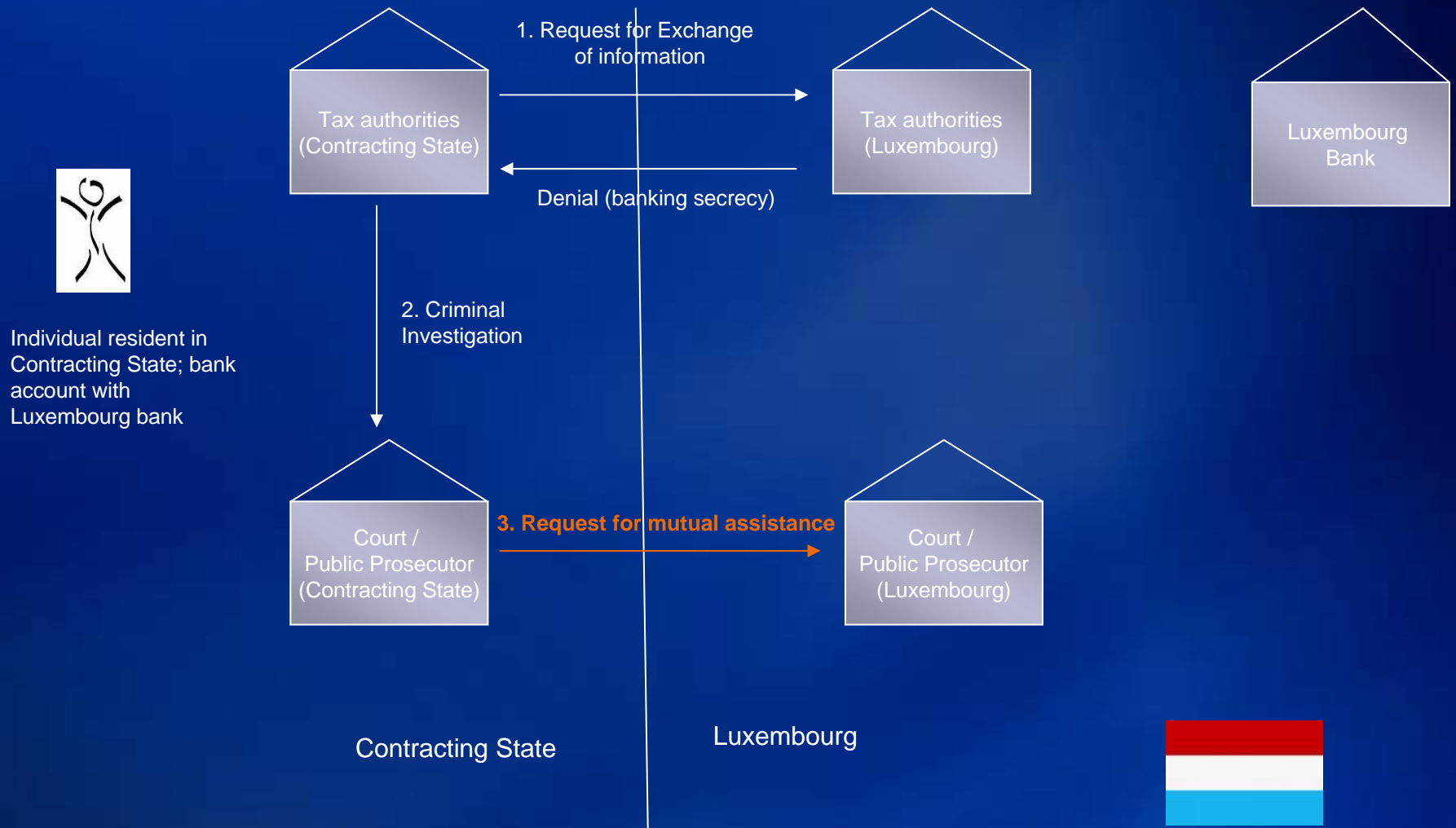
Example: mutual assistance and exchange of information (1/8) – *Current procedure*



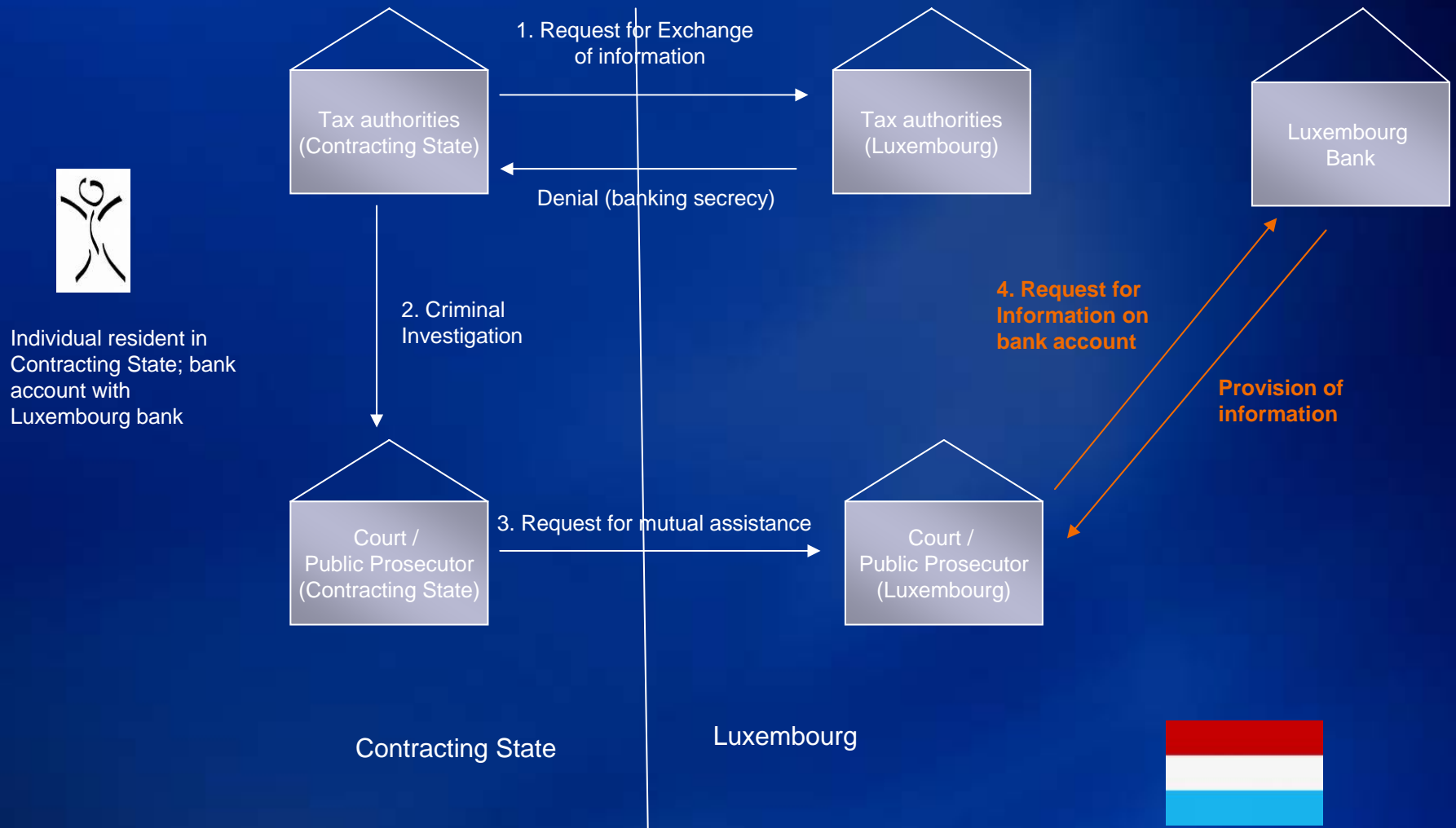
Example: mutual assistance and exchange of information (2/8) – *Current procedure*



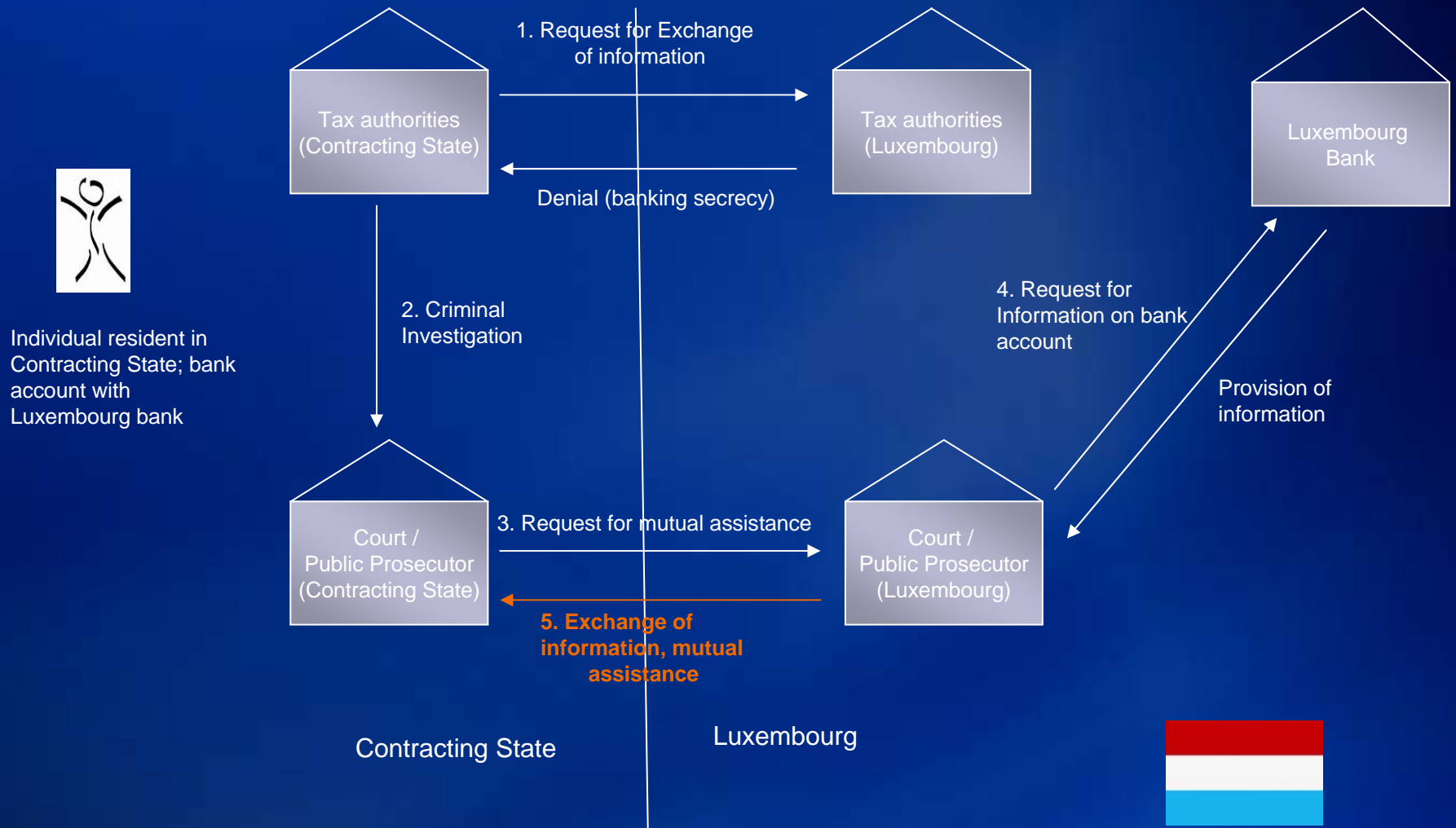
Example: mutual assistance and exchange of information (3/8) – *Current procedure*



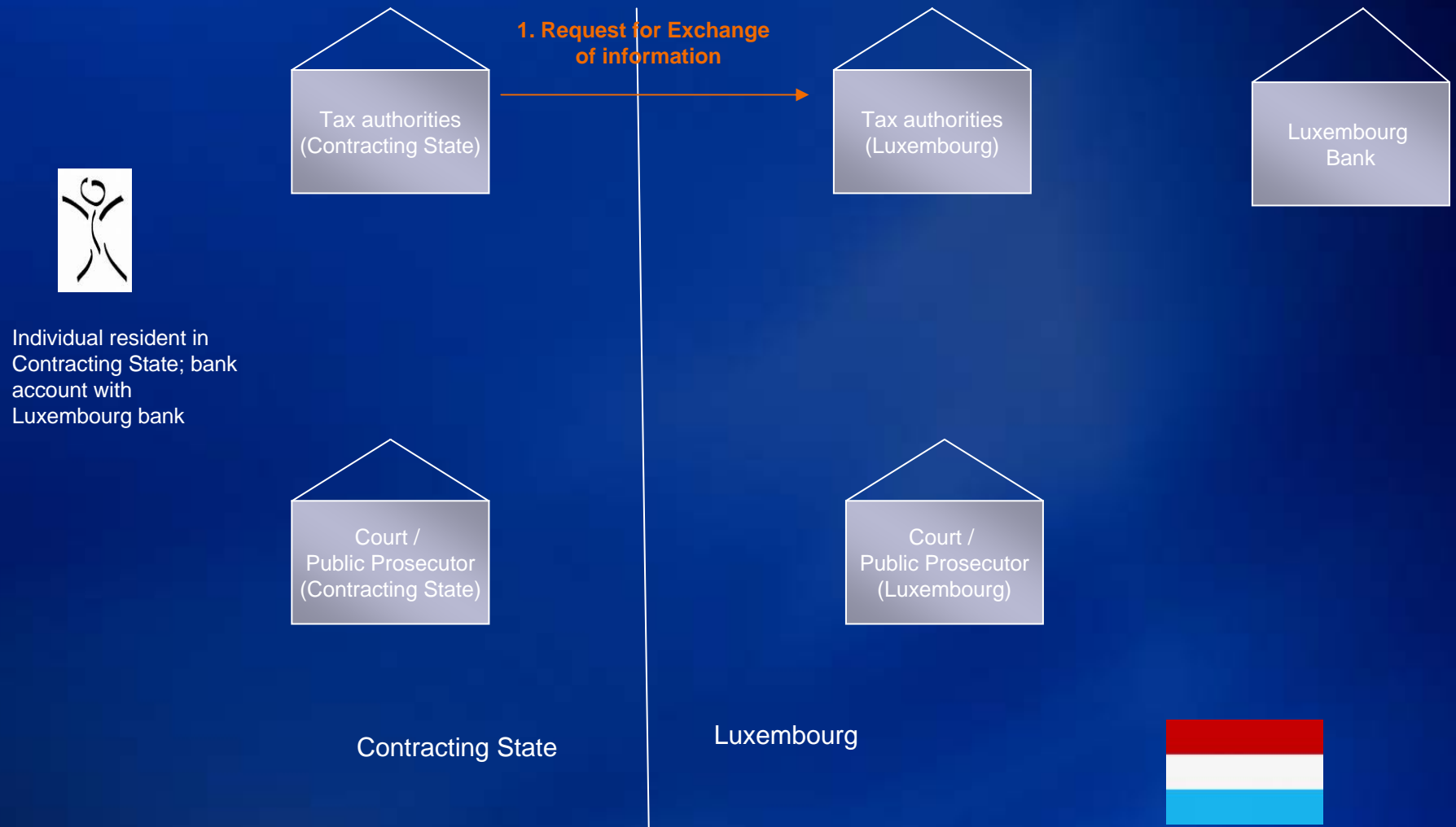
Example: mutual assistance and exchange of information (4/8) – *Current procedure*



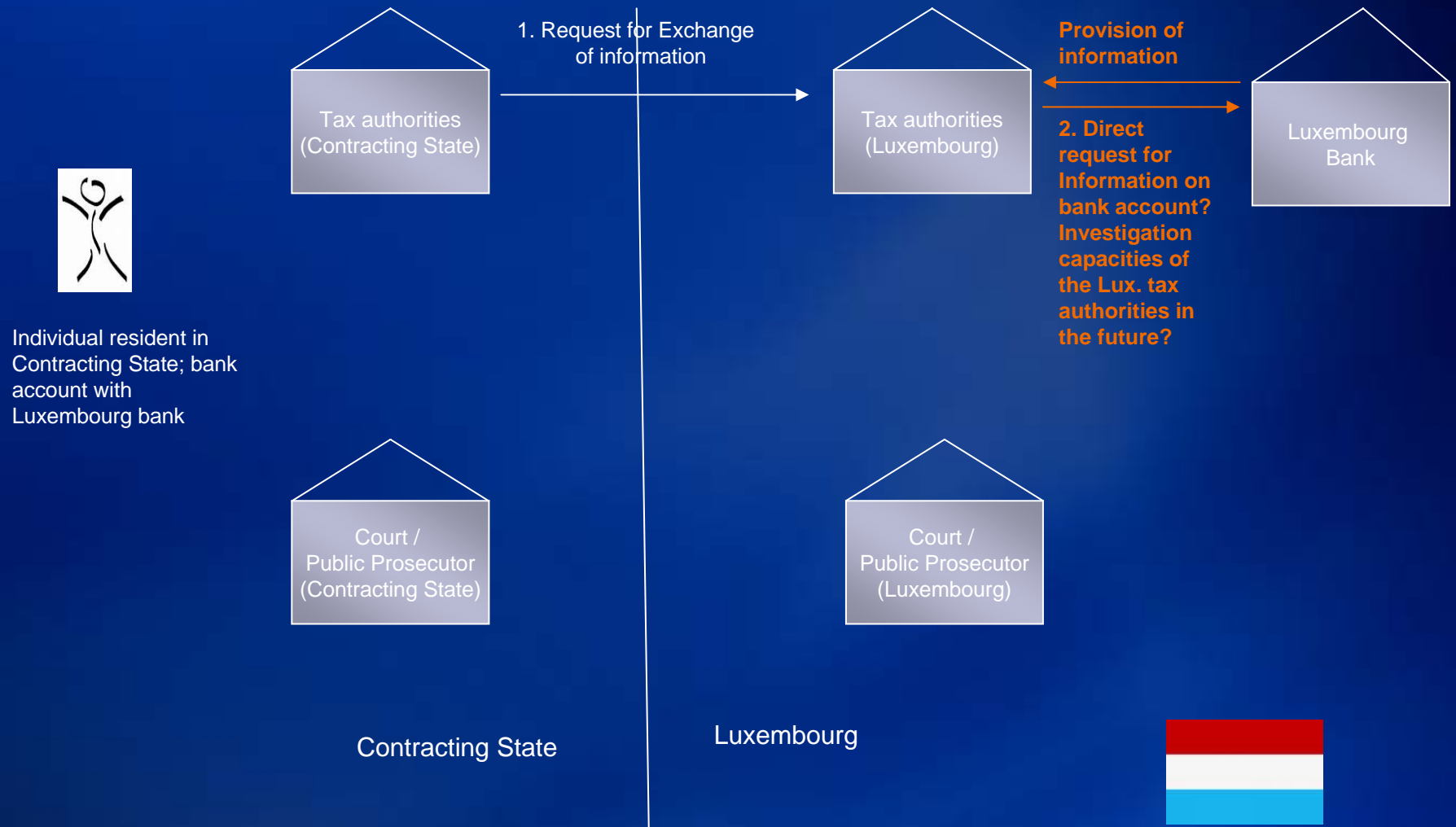
Example: mutual assistance and exchange of information (5/8) – *Current procedure*



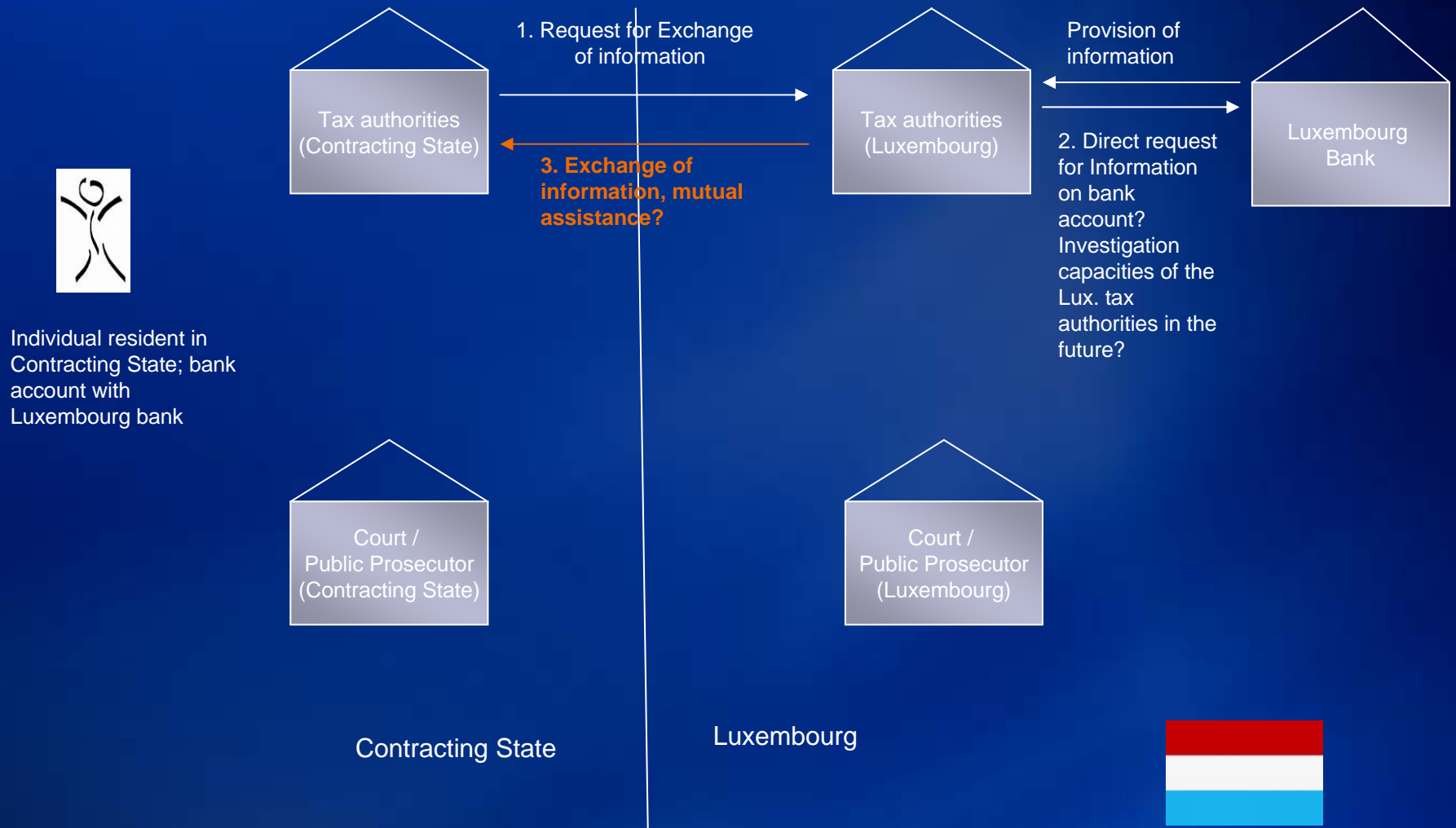
Example: mutual assistance and exchange of information (6/8) – *Future scenario?*



Example: mutual assistance and exchange of information (7/8) – *Future scenario?*



Example: mutual assistance and exchange of information (8/8) – *Future scenario?*



Conclusion

Thank you
Discussion
Q&A
Wrap Up
Cocktail



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