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What do the Tax Authorities Learn? Automatic Exchange of Information in 2018

With the world becoming increasingly globalized, it is easier for taxpayers to make, hold, and manage investments outside their countries of residence. Vast amounts of money are kept offshore and go untaxed, to the extent that taxpayers fail to comply with the tax duties of their home jurisdictions. Co-operation among tax authorities is critical in the fight against tax evasion.

In this article, we summarize the basic principles of exchange of information in the field of taxation. We do not list all of the kinds of information exchanged nor do we comment on individual legal sources*, i.e.,* EU Directives, Tax Information Exchange Agreements (TIEA), double tax treaties, multilateral conventions, and local law.

Automatic Exchange of Information (AEOI) is a term used to describe a range of agreements tax authorities across the world have entered into to exchange data automatically. AEOI allows for the exchange of data regarding non-resident taxpayers with the tax authorities in the taxpayers' countries of residence. Participating jurisdictions send and receive information automatically, mostly on an annual basis.

Although the original EU Directive on Administrative Cooperation in the Field of Taxation (DAC1) and several bilateral agreements allowed for the automatic exchange of information declared in tax returns, the number of participating countries is limited. The amended DAC2, together with global OECD standards (GATCA), were inspired by the US Foreign Account Tax Compliance Act (FATCA). The framework of the OECD's Multilateral Competent Authority Agreement (MCAA) on the Automatic Exchange of Financial Account Information allows for exchange of information in a standard electronic format – the Common Reporting Standard (CRS). As with the FATCA, the CRS model imposes duties on financial institutions to identify reportable accounts and to obtain the information on the account holder required to be reported for such accounts to their local tax authorities. This avoids the need to conclude multiple bilateral agreements. The information on the account holder, capital gains, account balances and income from the sale of financial instruments is reported. Data was exchanged for the first time in 2017 for 2016, with 54 countries participating. In 2018, 104 jurisdictions, including many "tax havens," participate.

It works simply. For example, in the British Virgin Islands, if a bank account is owned by a Czech tax resident, the BVI bank reports to the BVI tax authorities and they share the data with the Czech tax authorities. The Czech tax authorities are informed of the Czech tax resident´s accounts and income, and can easily verify his/her Czech income tax returns. The same applies *vice versa* in cases where Czech accounts or passive entities are owned by foreign tax residents.

Based on the DAC3, information about cross-border tax rulings and advance pricing arrangements are exchanged.

Based on the DAC4, MCAA, and other treaties, 57 countries participate in Country by Country Reporting (CbC) according to BEPS Action 13. Multinational groups with an annual consolidated turnover exceeding EUR 750 million are required to prepare a CbC report. On an annual basis, the CbC report provides the tax authorities with information on revenues generated with related parties, profits, income tax paid, retained earnings (accumulated losses), number of employees, and net book value of tangible assets in all of the jurisdictions in which the MNE Group operates.

Based on the DAC5, selected information on beneficial owners is collected pursuant to the AML Directive and accessed by tax authorities.

The DAC6 focuses on intermediaries such as tax advisors, accountants, and lawyers who propose or recommend tax planning arrangements. These intermediaries will have to report arrangements that may be aggressive.

The DAC7 … well … is expected to come soon.

The spontaneous exchange of information (*i.e.,* passing on of information obtained during examination of a taxpayer's affairs or otherwise, which might be of interest to the receiving state) or exchange of information on demand (the oldest type of information exchange among tax authorities) were slow, ineffective and did not keep pace with the world of the 21st century. Computerized data processing is the key to effective cooperation. The automatic exchange of information on financial accounts with 104 participating jurisdictions is revolutionary. Reporting financial institutions, taxpayers, and tax lawyers face a significant challenge. The automatic exchange of information about various kinds of taxpayers provides tax authorities with a huge amount of data and additional effective tools for reviewing tax compliance.

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