

Taxation of savings in Europe: a problem of implementation

On 21 January 2003, the European council of economic and finance ministers (ECOFIN Council) reached a compromise over the thorny question of the “tax package” which had divided its members for a long time. With regard to the most contentious part of this package - the taxation of savings - the European ministers decided on the broad outline of a system based on the automatic exchange of information or a withholding tax. Essentially, it was a return to the so-called “co-existence” model that Switzerland had in principle found acceptable, but which had been dismissed in June 2000.

As a reminder, the debate is related to the EU’s adoption of a Directive on the taxation of savings’ income derived from investments made by European nationals outside their own country and received in the form of interest payments. As this kind of tax measure could lead to the flight of capital outside the EU, it is essential - for the EU - that financial centres located in third countries agree to impose so-called “equivalent measures”. This is why Switzerland and five other countries (USA, Andorra, Liechtenstein, Monaco and San Marino) were approached by the European Commission.

Content of the compromise on the taxation of savings

The broad lines of the political agreements reached by the fifteen members are as follows:

- Twelve member states will engage in the automatic exchange of information (AEOI) with the EU. The remaining three member states (Cyprus, Malta and the UK) will engage in the automatic exchange of information with the EU.
- The EU will agree to exempt from taxation the interest payments received by the EU member states from the EU member states.

- Voluntary exchange of information (i.e. if the client who is a EU resident, asks it of his Swiss banker).
- Review clause.

Similar agreements will have to be entered into with the four small countries mentioned above. On the other hand, the ECOFIN Council has not judged it necessary to negotiate a similar agreement with the USA. No doubt this is because the USA has refused to discuss this topic with the EU.

Switzerland still needs to have many questions answered. Firstly, the review clause will have to be worded in such a way as not to prejudice the future. Secondly, Switzerland will insist that such an agreement will protect it from pressure from EU member states aimed at making it adopt rules it considers unacceptable regarding the exchange of tax information. Thirdly, Switzerland will make sure it is not discriminated against, be it in relation to EU member states, other third countries (e.g. United States of America) or offshore financial centres dependant on EU member countries (e.g. the Channel Islands or Cayman Islands). Finally, it should not be forgotten that the Swiss government wants to see these negotiations aligned with the other issues at stake in the second round of bilateral negotiations in order to obtain a global balanced result.

A problem of implementation

From a practical point of view, the target date of 1 January 2004 for the implementation of these measures appears unrealistic. In Brussels, the European Banking Federation has already voiced the lack of understanding of its members and underlined the complexity of the systems that the EU financial institutions will have to set up (whether it is for the automatic exchange of information or for the withholding tax).

The situation is not any easier in Switzerland, even though the Swiss authorities already published a fairly detailed feasibility study in February 2001. But, for the Swiss banks additional uncertainties complicate the order further. These are related to the long institutional path that still has to be followed before a binding agreement can be sealed. The main stages are:

- The political negotiation must be carried through to completion.
- The fifteen double taxation agreements between Switzerland and the EU member states must be amended, which will entail as many technical negotiations.
- These measures will have to be submitted to the two chambers of the federal parliament for ratification.
- Come what may, the three-month waiting period for a referendum will have to be respected and, if a referendum is successfully launched, the vote will have to be put to the people.

In view of these many uncertainties, it would be difficult to expect the actors of the Swiss financial centre to already commit large sums – in terms of both money and manpower – to establishing extremely complex systems that this possible bilateral agreement would impose on them. Indeed, it would not be justifiable to require these financial institutions (banks, securities houses, the Post Office, etc.) to make such investments before being quite certain that this new system would well and truly come into operation.