

## **The OECD's project on High Net Worth Individuals**

### **Society of Trust and Estate Practitioners (STEP) Response to the OECD Public Discussion Paper issued on 30 October 2008**

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**Q1 Important features of tax administration in dealing with HNWI**

*What are the important features of tax administration that may facilitate the co-operative compliance approach? Please build on positive and negative experiences when dealing with your tax administration.*

HNWIs represent a unique tax segment. Their affairs are generally characterised by enhanced mobility and a high degree of complexity that commonly transcends national borders. Sometimes, their fiscal affairs will be the result of a disorganised accumulation of assets over a period of time. Increasingly, however, HNWIs seek the advice of experts with a view to rationalising their affairs in line with overarching planning objectives, (e.g. in terms of control, confidentiality or succession). Where their affairs transcend national borders, conflicts may arise as a result of different legal and fiscal systems. In order to effectively deal with HNWIs, national tax authorities need to understand the tax issues that concerns them. This also means that tax administrations need to be conversant with the different taxes that make up a national tax system, as established families will focus on both direct taxes and capital taxes. In the UK, the problem caused by the division of responsibilities for the administration income tax and capital gains taxes became evident in the context of the recent changes to the taxation of individuals who are resident but non-domiciled (in the English law sense of the term) in the UK, as the draftsmen initially struggled to draft around certain income tax issues relating to the taxation of benefits paid out of offshore trusts, notwithstanding that similar provisions already existed in the capital gains tax legislation.

To the extent permitted by the local laws and practices, tax authorities should seek to solve issues by way of dialogue rather than confrontation. In this context, dialogue need not be client specific, and tax authorities may find it useful to interact with tax intermediaries and wealth planners on a regular basis (e.g. consultations, training, induction on specific issues) with a view to understanding common concerns and current trends. Recruitment from the private sector (and vice-versa) is also beneficial, as this helps the relevant tax authorities to gain precious insight into practitioners' concerns.

In certain circumstances, national tax authorities should also be prepared to adopt a multilateral approach to deal with truly international issues, which may include multilateral rulings in relation to such issues as tax residence. The need for a multilateral approach to deal with international families is dealt with under paragraph 7 of the Annex.

**Q2 Whether dedicated unit to deal with HNWI's good idea**

*Do you think that having a dedicated unit (or units) as part of your tax administration (either at national or regional level) with particular responsibilities for HNWI's is a good idea? If so, what roles and responsibilities do you think such a unit should assume?*

A dedicated unit may function as a collector of know-how and best practices in relation to issues that are common to many HNWI's. However, it is important that technical excellence be matched by an equal degree of approachability and proximity to the taxpayer and his advisors. In practice, therefore, there is a natural tension between centralisation of knowledge and closeness to the 'trenches' ; one solution might be to create special support units to work alongside tax administrators. Either way, easy access should be a central feature, so that practitioners and tax administrators alike may refer specific issues to an expert group.

Whether or not a dedicated unit is created, tax authorities should consider taking additional safeguards to protect sensitive information concerning to HNWI's. As will be explained under paragraph 4 of the Annex, confidentiality plays a central role for many HNWI's and recent scandals concerning the loss of information by tax authorities in various countries are a cause for concern that needs to be addressed.

**Q3 Existing dedicated units for HNWI's: assessment**

*If you are from a country that currently has a dedicated unit dealing with HNWI's what advantages or disadvantages have you seen in having such a unit and do you have any comments on the way it was set up and is operated? What are the features that you find the most useful?*

We would regard the current arrangements in the UK with specific centres for complex returns as only really a 'halfway house' in the context of a dedicated unit servicing high net worth individuals. In particular whilst these units provide some form of administrative efficiency in concentrating HMRC's resource into specific centres for those with more complex returns, there are various shortcomings such as the lack of an overall understanding of all taxes: Presently, these units are really only responsible for the annual income and gains tax filing and specifically do not have the capacity to deal with in particular inheritance tax and stamp duty issues which typically generate tax issues relevant to HNWI's alongside income and gains tax issues where an integrated response from Revenue authorities is desirable. By way of greater detail, it is noteworthy that for example, in the UK, the issue of domicile can be relevant for both the taxpayers inheritance tax position and his income and gains tax position - the experience of

practitioners is that there is some times an inconsistent approach adopted on domicile issues by the specialists units within the different parts of HMRC. The other point we would observe is that the fact that the specialist teams who deal with complex anti-avoidance issues such as s720 and s731 of the UK Income Tax Act 2007 bare separate from those dealing with day-to-day compliance means in our view that they tend to have on the whole a more adversarial approach to matters. We would therefore take the view that if consideration is being given to the formation of a more dedicated unit in the UK these points should be carefully borne in mind.

**Q4 What would encourage HNWIs to opt into enhanced relationship approach**

*If the tax administration offered this or a similar approach, what would encourage HNWIs and their advisors to opt into it?*

STEP welcomes the principle of 'enhanced relationship' and would ask the Focus Group to properly consider the behavioural differences between large corporations and private individuals are properly understood and addressed. The concept of 'enhanced relationship' was developed in connection with large corporate taxpayers. However, HNWIs represent a very distinct segment of taxpayers. This aspect is discussed further under paragraph 3 of the Annex. Accordingly, the framework for enhanced relationship may not be the same for large corporate taxpayers and private individuals. In particular, the financial affairs of private individuals are not the subject of formal third party reporting and their concerns usually have a long-term dimension (whereas many corporate managers need to focus on the short- to medium-term delivery of an effective tax rate). The specificity of the HNWI segment is discussed further under paragraph 3 of the Annex.

**Q5 Framework for voluntary disclosure schemes**

*The Focus Group seeks input from HNWIs and their advisors about the framework for voluntary disclosures and what particular elements would encourage taxpayers to come forward, e.g. solutions to issues such as lack of back-year records, inability to calculate final tax liability, concerns regarding privacy.*

This aspect is addressed in paragraph 8 of the Annex.

**Q6 Merits of product ruling regime**

*Please express your views on the merits of a product ruling regime in connection with HNWIs, to include any form of advance certainty (whether formal rulings or not) and also consider which*

*segments of HNWI's you think would be the users of the types of products for which product rulings could be made available (ie certain HNWI's might be more likely to enter into tailor made arrangements that do not lend themselves to product rulings).*

STEP represents practitioners dedicated to delivering tailor made solutions to private clients and the institutions that cater for them (banks, trust companies, family offices). The development of tax and financial products for market use is therefore not our area of primary competence. However, we are aware that HNWI's may choose such products and in this context, product rulings are a positive step forward in giving financial institutions clarity before marketing potential products to high net worth individuals as to the tax consequences of entering into such arrangements. In turn, this may assist the client's advisors.

In individual circumstances, rulings are a very useful tool that is widely used in various countries, including Switzerland and the Netherlands. In these countries, it is sometimes possible to explore the merits of a ruling on a 'no-names' basis. This is particularly useful e.g. when an individual is considering becoming tax resident in the relevant country. In the preliminary phase of discussions there is a legitimate requirement for privacy, as the individual concerned may decide not to become resident and therefore he/she may feel strongly about limiting circulation of sensitive information. The importance of confidentiality is discussed further under paragraph 4 of the Annex.

## Annex

### 1. Executive summary

- 1.1 The building blocks of the concept of ‘enhanced relationship’<sup>1</sup> were developed in the context of large corporate taxpayers. However, HNWIs represent a completely different segment of taxpayers. Accordingly, the nature of the relationship between these categories of taxpayers and the relevant revenue authorities is very different.
- 1.2 Confidentiality plays a much bigger role for HNWIs than for large corporate taxpayers, whose financial affairs are subject to continuous scrutiny not only from the revenue authorities, but also from the markets and for whom the dissemination of financial data may represent an opportunity to raise investments and increase their profile. In the case of HNWIs, additional safeguards and security procedures should apply to ensure the highest level of confidentiality.
- 1.3 The scope of the discussion paper is to improve compliance relationships within the existing legal framework. However, the quality of compliance relationships is the result of the prevailing legal and fiscal framework. Reference is made to the UK where the primary responsibility for making an assessment of the tax payable each year falls on the individual taxpayer, not the UK tax authorities (self-assessment system). Unless the legal framework is adapted, the concept of ‘enhanced relationship’ is unlikely to work in some countries.
- 1.4 An increasing number of HNWIs operate internationally. For many of them, a domestic or a bilateral solution based on tax treaties produces unsatisfactory results. One way to improve compliance relationships would be to adopt a multilateral approach, e.g. multilateral rulings in relation to residence, and also multilateral alternative dispute resolution.
- 1.5 As behaviours shift, past non-compliance has become an increasing issue. As a result of modern money-laundering legislation, some HNWIs are afraid to interact with tax intermediaries. In addition, for many taxpayers practical problems such as the lack of back-year records, inability to calculate the final tax liability and concerns regarding privacy may act as a deterrent to come forward.

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<sup>1</sup> (1) understanding based on commercial awareness; (2) impartiality (consistency and objectivity); (3) Proportionality; (4) Openness and transparency by taxpayers; and (5) Responsiveness.

## 2. Background

### 2.1 2008 study into the role of tax intermediaries and large corporate taxpayers

In January 2008, the OECD's Forum on Tax Administration (which brings together senior tax administrators to share information and resolve particular tax administration issues) published a study into the role of tax intermediaries in corporate tax planning<sup>2</sup>. That report was spurred by the concern of national tax authorities in relation to the 'spread of aggressive tax planning marketed by some tax intermediaries (e.g. law and accounting firms, other tax advisors and financial institutions)'. However, the study came to the conclusion that large corporate taxpayers (which represented the principal focus of the study) 'set their own strategies for tax-risk management and determine their own appetite for tax risk. They are the ones who decide whether to adopt particular planning opportunities. Taxpayers represent the demand side of aggressive tax planning', with tax intermediaries being the 'supply side'. Accordingly, the focus of the study shifted from tax intermediaries to their clients and examined strategies to improve the relationship between tax authorities and large corporate taxpayers and to respond to tax intermediaries who engage in 'unacceptable tax minimisation arrangements.'

The study looked at the 'behavioural drivers' of large corporate taxpayers, noting that this segment of taxpayers 'place a high value on the ability to finalise their tax positions quickly, particularly if this can be done in real time. This helps them minimise unpredictability of earnings projections and achieve predictability of future cash flows, allowing more accurate assessment and public reporting of the value of the business (...)' In most large companies, taxes are viewed no differently than payroll and other operating costs. For some large corporate taxpayers, this means there is an emphasis on delivering a low or relatively low effective tax rate (ETR), particularly by comparison to other companies in the same industry. ETR and other metrics used to enhance shareholder value are now important beyond the corporate tax department and are carefully watched, not only by senior management but also by analysts, rating agencies and institutional investors. Some tax executives are under enormous and continuing pressures to effectively manage the ETR and other measures of shareholder value.'

Against this backdrop, the report suggested that the relationship between revenue authorities and large corporate taxpayers (which traditionally tended to be confrontational rather than co-operative) could be improved if revenue authorities showed commercial awareness (through training and dialogue on broader non-client specific issues), responsiveness as well as impartiality and proportionality. The study suggested that if

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<sup>2</sup> Available online at: <http://www.oecd.org/dataoecd/28/34/39882938.pdf>

revenue bodies demonstrated these attributes and have effective risk-management processes in place<sup>3</sup>, this should encourage large corporate taxpayers to engage in a relationship with revenue bodies based on co-operation, openness (disclosure and transparency) and trust, with both parties going beyond their statutory obligations and embracing an 'enhanced relationship'. As to those taxpayers who were unwilling to offer disclosure and transparency, the study recommended an approach based on increased risk assessment and focused resource allocation. In addition, the study looked at the tax disclosure schemes adopted by some countries, including the US and the UK.

## 2.2 Project on HNWIs

Though it focused exclusively on large corporate taxpayers, the 2008 report noted that consultations identified high-net-worth individuals 'are generally agreed to represent the [other] greatest risk in relation to aggressive tax planning'. Accordingly, in March 2008 the OECD set up a focus group of 14 interested countries<sup>4</sup> to carry out the follow-up study on so-called HNWIs<sup>5</sup>.

The main purpose of the discussion paper is to explore whether the concept of 'enhanced relationship' could be applied to HNWIs. The discussion paper itself incorporates many of the underlying principles such as proportionality and early certainty identified in the study on large corporate taxpayers and the focus group confirmed that it is prepared to examine whether the 5 pillars identified in the study on large corporate taxpayers (i.e. commercial awareness, impartiality, proportionality, openness and responsiveness).

In addition, the discussion paper explores ways to encourage voluntary disclosure regarding past domestic and offshore non-compliance. In addition, the paper asks views on the merits of a product ruling regime in connection with HNWIs.

## 2.3 The involvement of STEP so far

STEP has been involved in the consultation process from an early stage-given that its membership serves the needs of the HNWI sector. On 16 October 2008 STEP provided a

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<sup>3</sup> With regards to risk management, the study noted that 'as well as benefiting revenue bodies, risk management can also benefit many taxpayers. For example, while taxpayers who demonstrate significant risk can expect to attract greater scrutiny and enforcement attention, taxpayers who behave transparently and who represent lower risks can reasonably expect a more co-operative approach from revenue bodies and therefore lower compliance costs'.

<sup>4</sup> Australia, Canada, Ireland, Italy, France, Germany, Japan, Mexico, the Netherlands, New Zealand, Norway, South Africa, the UK and the US.

<sup>5</sup> The paper recognises that different terms are used to refer to the top taxpayer segment and uses the term 'HNWI' broadly to refer to taxpayers at the top of the wealth or income scale and does not attempt to otherwise define the term.

participant who took part in a meeting organised by the focus group in Paris to discuss the content of a draft of the discussion paper and to provide relevant experience from an adviser's perspective as to how the UK tax system currently serves HNWIs.

### 3. **HNWIs: a unique segment of taxpayers**

- 3.1 The OECD focus group of 14 countries involved in the HNWI project recognises that the situation of HNWIs is in many ways significantly different from the situation of large corporate taxpayers.
- 3.2 In its study on large corporate taxpayers, the OECD came to the conclusion that large corporate taxpayers viewed taxes no differently than payroll and other operating costs and that in some cases tax executives were put under enormous and continuing pressure by management, analysts, rating agencies and institutional investors to deliver a low or relatively effective tax rate so as to enhance shareholder value. In these circumstances, large corporate taxpayers were likely to look favourably at the concept of enhanced relationship, as the early resolution of tax issues would offer large corporate taxpayers the ability to minimise unpredictability of earnings projections and achieve predictability of future cash flows, allowing more accurate assessment and public reporting of the value of the business.
- 3.3 Unlike corporate taxpayers, individuals are not subject to external pressures and scrutiny. For large corporate taxpayers, the publication of their financial data may represent a regulatory requirement. However, it also enables them to attract fresh investment, it enhances their credit rating and may bolster their position in the marketplace. In other words, for many large corporate taxpayers transparency and openness represents a strategic tool in their armoury for survival and growth.
- 3.4 By contrast, most individuals are jealous of their privacy and have a legitimate interest in keeping their affairs confidential, whether in relation to their private life or their financial affairs. This principle is recognised by many countries and is reflected internationally by the growing number and complexity of data protection laws. For some leading families, privacy (as opposed to secrecy) plays a central role in all their affairs. There are many reasons for wanting to preserve confidentiality, including concerns about the consequences that open knowledge of the family's wealth may spoil young and other impressionable members of the family or may expose them to exploitation from other members of society. Whilst revenue authorities need to have sufficient information to be able to assess the tax burden of the family, many families may find it difficult to discuss their affairs openly with the tax authorities. This may be particularly an issue where tax authorities are based locally, though on the other hand, proximity to the taxpayer may increase the level of mutual trust.

- 3.5 There are other important differences between large corporate taxpayers and HNWIs, and in particular leading families. Managers are transient, but families remain. Accordingly, many leading families are less preoccupied with achieving a low tax burden in the short term than with providing a safe transition of wealth in the long term. In many cases, this long-term vision translates into risk-aversion and desire to keep a low profile away from controversies. On the other hand, these families will allocate vast resources to securing wealth preservation and safe generational transition. Thus, these families are likely to look favourably at wealth planning tools such as foundations and trusts and the poor understanding of (if not open warfare against) these planning tools from some national revenue authorities is a cause of great frustration for many international families. In this context, STEP agrees with the conclusion contained in the 2008 study on tax intermediaries that commercial awareness, proportionality and impartiality are key attributes in the relationship between national revenue authorities and leading international families.
- 3.6 As the focus group acknowledged in its discussion paper, HNWIs are not an homogeneous group and it is therefore impossible to summarise all their behavioural drivers of HNWIs. However, it is possible that income-rich individuals, especially first-generation wealth creators, may take a different attitude than established wealth-rich families. In any event, it is impossible to compare HNWIs with large tax corporations. Accordingly, the framework within which the concept of 'enhanced relationship' may develop is different.

#### **4. The importance of confidentiality and data protection**

- 4.1 As mentioned above, confidentiality represents a key behavioural driver of many HNWIs. However, the increased use of electronic information devices, the ability to exchange electronic information across borders, and the potential abuse of information gathering powers by government bodies represents a real threat to many individuals, including many HNWIs. The requirement of confidentiality is understood by many revenue authorities, whilst others regard confidentiality with suspicion. This is the cause of many conflicts between taxpayers and national tax authorities.
- 4.2 Some countries allow intermediaries to approach the tax authorities in the context of a ruling on a no-name basis. Obviously, any ruling needs to contain a direct reference to the facts, including the identity of the taxpayers, but the possibility of discussing legal issues on an anonymous basis encourages tax intermediaries to reach a mutually satisfactory solution with the tax authorities concerned without unnecessary disclosure at the early stage of discussions.

- 4.3 Whilst the idea of 'enhanced relationship' has some merits, many taxpayers' concerns about confidentiality remain unresolved and need to be addressed urgently.
- 4.4 To give some examples, in November 2007 the UK tax authorities reportedly lost computer disks containing confidential details of 25 million child benefit recipients. The disks contained such confidential information as addresses and bank accounts. This was not the first time the UK tax authorities had to apologise for the loss of sensitive data. More recently, a memory stick containing confidential passcodes to the online Government Gateway system, which covers everything from tax returns to parking tickets was found in a pub car park<sup>7</sup>. On a smaller scale, it was reported that a local authority allegedly abused anti-terrorism powers to check whether a child lived in a school catchment area and to spy on fishermen<sup>8</sup>. The potential abuse of anti-terrorism legislation is also at the heart of the international crises that embroils the UK and Iceland over the recent collapse of Icelandic banks and the subsequent seizure of Icelandic assets<sup>9</sup>.
- 4.5 The UK is not the only country to have experienced problems with data protection. On 30 April 2008, the Italian revenue authorities posted the tax returns of all Italian taxpayers for 2005 on their official website, spurring violent polemics. Notwithstanding a dramatic u-turn from the tax authorities, it has been reported that the tax returns remain available on file-sharing sites<sup>10</sup>. Always in Italy, the government has recently intervened against the growing publication of intercepted telephone conversations<sup>11</sup>, whilst in France it was revealed that the head of domestic intelligence services kept confidential information on politicians, but also on certain HMWIs (including a singer and a kick-boxing champion).<sup>12</sup> According to an article in The Economist magazine, CDs of the Italian database were made available, same day on E-bay for \$75, showing how effectively private parties exploit government lapses; Media reports in the Italian press at the time noted that the result of the data publication by the Italian authorities was that the mafia's efforts at kidnapping and extortion would be aided by use of the government database which would spare them the effort of research on potential victims. Finally, Prime Minister

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<sup>6</sup> <http://news.bbc.co.uk/1/hi/uk/7103911.stm>

<sup>7</sup> <http://www.dailymail.co.uk/news/article-1082402/Tax-website-shut-memory-stick-secret-personal-data-12million-pub-car-park.html>

<sup>8</sup> <http://www.telegraph.co.uk/news/uknews/2043799/Spying-council-investigated-for-privacy-breach.html>

<sup>9</sup> See The Landsbanki Freezing Order 2008: [http://www.opsi.gov.uk/si/si2008/uksi\\_20082668\\_en\\_1](http://www.opsi.gov.uk/si/si2008/uksi_20082668_en_1)

<sup>10</sup> <http://www.repubblica.it/2008/04/sezioni/economia/redditi-online/redditi-online/redditi-online.html>

<sup>11</sup> <http://it.reuters.com/article/topNews/idITCON92397020080609>

<sup>12</sup> <http://www.timesonline.co.uk/tol/news/world/europe/article5062832.ece>

Brown was quoted on 2 November 2008 in the headline of a Daily Telegraph piece on UK data losses as indicating "data will never be completely safe with the Government", acknowledging that they won't/can't protect.

- 4.6 At the other side of the spectrum there are the reported scandals involving the abuse of banking secrecy laws by financial institutions in Switzerland and Liechtenstein. Whilst STEP considers that tax evasion is unacceptable, the episodes mentioned above show that confidentiality is a real concern that needs to be dealt with on a national and international level. With regard to taxation, this issue is exacerbated by the exchange of information under tax treaties, which means that an individual with international connections has no control over the level of security of his data.
- 4.7 Against this backdrop, it is suggested that, in order to work, the concept of 'enhanced relationship' as developed in the 2008 study on tax intermediaries and large corporations may need to be adapted to address the legitimate concerns of HNWIs in relation to confidentiality.
- 4.8 One possible solution might be for tax inspectors with access to substantial files to use pseudonyms or acronyms instead of real names and also to restrict access to the files concerned (Chinese walls, additional passwords, etc.).
- 4.9 Whilst overarching concerns about confidentiality may prevent tax advisors to discuss openly specific circumstances with national tax authorities, each side would benefit from gaining an insight into the work of the other side. This can be achieved in many ways, including consultations of the type spearheaded by the discussion paper, meetings and, most importantly, mutual training on non-client specific issues.
- 4.10 Another important aspect of privacy is client/solicitor confidentiality, which in many countries is protected with criminal sanctions. The benefits of professional privilege are particularly evident in the context of voluntary disclosure schemes, where the individual concerned may feel reassured about the prospect of confiding openly to a professional equipped to help him/her. In the UK, the importance of professional privilege is recognised in the Proceeds of Crimes Act 2002 ('POCA') which contains the UK's anti-money laundering legislation (see ss. 330 (10) and (11), s. 333D(2) and 342(4) POCA). In the context of 'enhanced relationship' the constraints imposed by the duty to client confidentiality may be easily overcome by clients providing their solicitors with consent to liaise with the tax authorities.

## 5. **The relationship between national revenue authorities and taxpayers – a product of the prevailing legal framework**

- 5.1 In a recent article<sup>13</sup> discussing the concept of cooperative compliance contained in the discussion paper, the Head of the Aggressive Tax Planning Unit at the OECD and the HNWI project coordinator noted that ‘relationships between HNWIs (typically represented by their advisors) and tax administrations can sometimes be difficult. To some degree, this may reflect the overall legal framework and the applicable tax burden. However, other factors are also at play. Some advisors have characterised the current situation as “trench warfare”. They have suggested that there is a lack of dialogue, no meaningful point of contact and little possibility for discussion before a tax return is filed. Other advisors have indicated that while in general, relationships are good, there is a need for more advance certainty, in particular in international transactions’.
- 5.2 At the meeting held in Paris on 16 October 2008, the focus group clarified that it represented tax administrations, rather than policymakers of the 14 countries represented. Accordingly, the purpose of their work was to improve compliance within the existing legal framework, rather than change the overall legal and tax landscape that may influence the behaviour of wealthy individuals (such as tax rates, types of taxes, treaty networks, etc.). This position is reflected in the discussion paper. However, it is difficult to see how the relationship between revenue authorities and taxpayers may be forged without reference to the legal and tax framework that governs.
- 5.3 Also, the obligations to promote mutual harmony and trust are bilateral: The UK failure to consider creditability of the annual £30,000 levy applicable to non-domiciliaries against taxes owing by US citizens was a glaring example of tax policy/tax administration insensitivity to basic taxpayer needs. Accurately or not, many also perceived it as deliberate provocation to high net worth individuals. Tax administrations which seek cooperative, trusting and open relationships with high net worth individuals must show that they are cognisant of taxpayer interests.
- 5.4 The concept of ‘enhanced relationship’ may be particularly difficult to implement in countries that operate a self-assessment system of taxation (such as the UK). The key feature of the self-assessment system is that the primary responsibility for making an assessment of the tax payable each year falls on the individual taxpayer, not the UK tax authorities. In other words, the taxpayer has to work out his own tax bill. It has been reported that self-assessment has reduced the costs of tax administration in the public

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<sup>13</sup> Achim Pross and Chris Orchard, Exploring Cooperative Compliance for HNWIs in Tax Notes International, December 2008, pp 713 et seq.

sector and has increased significantly the government's cash flow, as tax payments are made more promptly than they were under the old system. The other side of the coin is an increase of costs in the private sector (due to the increased use of professional advisors) and also an increased distance between the taxpayers and the tax authorities, whose role has shifted from assessing and collecting tax, to investigating perceived irregularities.

## 6. The role of tax intermediaries

- 6.1 The study on large corporate taxpayers concluded that most large corporations 'set their own strategies for tax-risk management and determine their own appetite for tax risk'. The same applies to many HNWI's. As indicated above, many leading families are intrinsically risk-averse and the role of tax intermediaries is to manage their tax risk efficiently within the prevailing legal and fiscal framework.
- 6.2 However, risk management is not the only function of tax intermediaries who work with HNWI's. The increasing mobility of individuals has caused the emergence of truly international tax and wealth planning advisors. Often, their role is to analyse the interaction between the legal and fiscal systems of various countries with a view to minimising the risks that arise from any mismatches.
- 6.3 One of the examples made at the hearing of 16 October 2008 in Paris related to a UK taxpayer who was advised by his French notary to write a Will under which the UK taxpayer would leave a '*usufruit*' in relation to his French property to his spouse, with the '*nue propriété*' passing to his children. Under the current French rules the gift of the '*usufruit*' to the surviving spouse would not be taxed, whilst the '*nue propriété*' would be taxed immediately in the hands of the UK taxpayer's children at a rate up to 40%, though they would benefit from a discount calculated by reference to the life expectancy of the '*usufruitier*'. On the other hand, the death of the '*usufruitier*' would not trigger any additional tax in France, although it would trigger inheritance tax in the UK up to 40%<sup>14</sup> In practice, therefore, the creation of a '*usufruit*' would give rise to tax in France up to 40% on the death of the testator and to tax in the UK (also up to 40%) on the death of his surviving spouse, without any possibility of offsetting the two taxes under the relevant treaty.
- 6.4 STEP does not agree with the perception amongst some national tax authorities that HNWI's represent a high risk segment of taxpayers and that the main reason for using tax

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<sup>14</sup> At least to the extent that the '*usufruit*' (which is an unknown concept under English law) is characterised as a life interest (a special type of trust).

intermediaries is to avoid paying their fair share of tax. The example above is illustrative of the fact that many clients need complex advice in order to deal with rules which are ill-considered in a domestic, and certainly in a trans-border, context so that much of the advice-taking relates simply to clarification of responsibilities and avoiding double or triple taxation.

- 6.5 Whilst the concept of 'enhanced relationship' was primarily conceived as part of a study to curb 'unacceptable tax minimisation arrangements', it is suggested that the scope of the discussion paper be extended to encompass an analysis of possible ways of reducing unacceptable double or multilateral taxation.

## **7. The need for a multilateral approach, including ADR**

- 7.1 The example just mentioned shows how systemic differences between two or more legal and tax systems may lead to unacceptable results.
- 7.2 In the case of truly international HNWIs, similar issues arise e.g. where their lifestyle is such that it is impossible to determine their centre of vital interests with absolute certainty. In these cases, tax treaties only offer limited comfort. Even if the tax authorities of two countries may reach an agreement as to where the taxpayer is resident for the purposes of the relevant treaty, a dispute may arise with the tax authorities of a third or fourth country.
- 7.3 In order to avoid an open warfare with the tax authorities of various countries, some taxpayers may seek to keep low profile, though in many situations they would prefer to achieve early certainty. However, in a case like this, the only certainty can be achieved by involving all the relevant tax authorities. If national tax authorities are desirous of improving compliance relationships, they should be prepared to take a multilateral approach and, if possible, to engage in multilateral rulings and/or alternative dispute resolution involving the taxpayer.
- 7.4 The concept of multilateral rulings is not novel, as it is used in the context of transfer pricing.
- 7.5 As to the framework for alternative dispute resolution, reference is made to the mutual agreement procedure under Art. 25 of the OECD Model Tax Convention. One of the disadvantages of that procedure is that it usually takes place when is too late for the taxpayer, who by then is likely to have spent a fortune in legal representation and diverted precious attention from his/her real business concerns. A much better approach would be to work together with the tax authorities of all countries concerned from an early stage with a view to reaching a sensible solution.

## 8. **Encouraging disclosure of past non-compliant behaviour: practical aspects**

- 8.1 Recent scandals have shown that non-compliant behaviour is still alive in some quarters. However, modern money laundering legislation mean that this type of taxpayers are on their own.
- 8.2 Legitimate tax intermediaries concern themselves only with 'white' money. The duty to report non-compliant clients to regulatory authorities under the laws of many countries means that the minority of clients with undisclosed assets wishing to keep those affairs away from the discussion table may, in some cases, be inclined to screen out such data from their advisers. This fact may hamper the practical ability of such tax advisers to assist tax authorities in the effective reform of non-compliant structures.
- 8.3 Even when an individual decides to tackle his/her past non-compliant behaviour and contacts his tax advisors to this end, there may be situations where finality may be difficult to reach, typically because of back-year records or the inability to clearly identify taxable items as a result of a commixture of funds.
- 8.4 For clients seeking to regularise their affairs, whilst concern about admitting past-non-disclosure represents the main reservation in most cases, some taxpayers may be deterred from entering into discussions with the tax authorities because of the financial and administrative costs of disclosure. Whilst the decision to waive penalties and/or interests is likely to be a matter of tax policy (rather than tax administration) in many countries, revenue authorities should consider the financial benefit of bringing assets within the tax net and, where possible, take a pragmatic approach. In this context, it might be helpful if the revenue authorities and the relevant tax intermediary could agree a framework for co-operation at the outset. This would significantly assist in enhancing the relationship between intermediaries and tax authorities.