**White Paper**

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**An inquiry into whether exchange of information in tax matters has (or is about to) become part of customary international law?**

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**Introduction:**

The commission the League of Nations gave in 1923 to the four economists was to find general principles accepted by States in avoiding double taxation.

They, according to Cowcher[[1]](#footnote-1), found no general principle. The reason given by Cowcher was simple. There was no accepted principle.

Following this 1923 commission, the same League of Nations, appointed a committee of technical experts on double taxation and tax evasion. With the benefit of hindsight, this committee had the right foresight to, in the words of its chairman, *confine themselves to indicate general rules, leaving particular points of difficulty to be dealt with –in the spirit of accepted general principles- by those negotiating bilateral conventions*.

This spirit of general principles did not exist, according to a young Judeo-German scholar by the name of Albert Hensel who wrote, by the same timeline, there was no limit to the power rights to impose taxes[[2]](#footnote-2).

Can we disagree with Cowcher and Hensel 80 years later? Is International Taxation ready to say there are commonly accepted principles today? Do they bind countries in their inter-nation relations?

Reuven Avi-Yonah[[3]](#footnote-3), has recently defended these principles do exist. Avi-Yonah mentions the use of foreign tax credits in absence of treaties, the arm-length’s standard, non-discrimination and other persuasive arguments to support his thesis of binding principles since they have become customary international law.

Graetz, Rosembloom, Roin, Kane and Dagan deny, under the current state of international law, the existence of customary international law, holding an opposing view to Avi-Yonah.

This article supports Avi-Yonah’s view and tries to explore how a recent request of Colombia to Panama to sign an exchange of information agreement may show the making of customary international law.

**1. Customary International Law and its definition**:

Customary international law is “international custom, as evidence of a general practice accepted as law”[[4]](#footnote-4).

For this practice to exist it needs to be identifiable. The world, remembers a time were no real consensus existed concerning exchange of information in tax matters. Arguably, the first time the issue is raised, outside the treaty network, is in the Gordon Report of January 1981. Richard Gordon advocated a largely ignored US led initiative. At that point, what may be perceived, as an American initiative is clearly not regarded as being international consensus.

Fifteen years later a consensus is reached within a limited number of seven countries in the G7 meeting at Lyon in 1996. At this moment, G7 commissioned OCDE to find measures to curb down harmful tax competition.

OECD then issues its 1998 “Harmful Tax Competition and Emerging Global Issue” report. Two years later OCDE publishes a tax haven list and a date line is set for blacklisted jurisdictions to either change its “harmful” tax practices or face sanctions.

The mere need to have a non-complying list evidences 1998 as a point in time were no custmary practice exists concerning exchange of information in tax matters.

However, this is a key point in time since the international community did not reach a consensus and partly rejected the principles embodied on the OECD’s Report. Instead of adhering to these principles (ie in an international convention or at least supporting it in mass), not only tax havens opposed this initiate but the largest economy also did[[5]](#footnote-5) by the words of, Paul Oneil, its Secretary of the Treasury.

**Oneil’s Letter:**

Oneil’s letter shifted OECD’s 1998 initial wide range and encourage tax havens to consider earlier commitments as no longer valid[[6]](#footnote-6). This provoked a shift from what Oneil called “wide range” to an exchange of information in tax matters centered effort. Additionally, because of the request made by blacklisted jurisdictions OECD launches 2003’s Ottawa’s meeting accepting the “playing level field” does not exist. One of Ottawa’s conclusion is to find a definition to the term “playing field”. This definition is never to found and dropped off OECD’s language. In no small part this change in language and goals signals lack of consensus in parts other than Exchange of Information in tax matters.

After OECD’s effort centered on exchange of information the United States did not object to any of the following reports and no serious objection was raised by blacklisted jurisdictions.

Does this mean the world reached consensus around the need to exchange information in tax matters?

By this time, a second scholar noted Avi-Yonah’s thesis and published an article arguing for the crystallization of an international tax regime[[7]](#footnote-7). Although recognizing that the regime may not exist at that moment Brauner look at 4 key elements for an effort to achieve harmonization of tax rules. The four elements he identified are visible in the current state of Exchange of Information development.

**Brauner’s 4 elements for a harmonization of tax rules**:

The first element being the participation of a significant part of major economies and trade forces of the world. This element is not only present but exceeded in the recent signing of a compromise to exchange tax information automatically at the Berlin meeting of the Global Forum on October 2014.

The second element being acceptance of non-negotiable rules as domestic legislation that will apply to treaty and non-treaty partners. This second element is also present in the Berlin meeting commitment and arguably present in the facto practice that compels countries to sign commitments with OECD countries or face sanctions.

The third element mentioned by Brauner is a flexible but binding interpretation similar to the OECD model commentaries. This flexible but binding interpretation is given by the willingness to exchange information with no real detail of what “information” not “automatic” means.

The final element Brauner gives is an easily accessible conflict resolution system. To the authors writing this article, black lists that no country, so far, have denounce as violating international law have developed this system. Should a country feel in need of tax information a request is made to its peer. This country may deny an exchange of information agreement and the other party sets a list with sanctions to the requested party. The country then lifts these sanctions if the other party is willing to negotiate an exchange of information treaty.

**Beyond these 4 elements**:

We want to propose a fifth element to the four mentioned by Brauner. This fifth element is the inability of a country to get rid of its obligation. This fifth element is evident in Panama’s case who started this discussion by saying no exchange of information was to be given (a pre-1998 stance), later accepted to exchange information (in 2002) and ultimately did sign exchange of information agreements with 25 countries (between 2010 and 2013).

We believe this fifth element is present in the case of Panama that only needed a pen and 12 willing signatories to comply with its Global Forum commitments. Instead of signing treaties with its neighbors, this led to signing treaties with unlikely partners such as Quatar, Faroe Islands, Vietnam, Greenland and Iceland.

However, the countries willingness to comply with its commitments gets tested when the country was unable to deny Colombia what had already given to countries with less economic and cultural ties.

We further propose a sixth element in a marketable fairness argument behind the alleged custom. When the debate starts in 1998, the most stubborn sovereignty claims were raised in Panama and other tax havens. These claims of sovereignty were backed by little more than anti-colonialism talks and libertarian ideas. These ideas quickly died off at the diplomatic table since little support is found for an argument based on “I could care less if your tax base is eroded”.

A seventh element is that it needs to be an issue better dealt multilaterally rather than on a bilateral basis. This is the case of exchange of information since a consensus is easier reached than in other areas where proposed harmonization have failed (source rules, definition of income, treatment of electronic commerce, etc.)

**How Exchange of Information becomes (or is about to) customary in international law**:

Up until 2002, no real consensus exists concerning EI, especially since the US sent Oneil’s letter. In the last decade, however a real consensus is seen inside and outside the developed world as of the need of exchange information between countries.

Taking Panama as an example, we did signed a commitment letter in April 15, 2002[[8]](#footnote-8) accepting to exchange information on tax matters. Colombia, a country that was not even close to the 1998 OECD Report felt, in 2013, the need to draw up a list of non-cooperative jurisdictions. A year later, Colombia put Panama on that list starting a media war between both countries. This tension ends when Panama signed a commitment to exchange tax information with its neighbor on an OECD based model.

The case may be argued that the fact that Panama feels compelled to sign an exchange of information treaty with Colombia is not legally relevant. However, at the same time, the practice followed by both Colombia and Panama follows the path the rest of the world has followed regarding the need to negotiate an exchange of information agreement or face unilateral sanctions.

Is that path becoming “custom” in international law? Is this customary international law in the making? Will the 4 economists, transported to the 21st century, be able to see in exchange of information a “general principle accepted by States in avoiding double taxation”?

The International Court of Justice faced a similar question above asked in the 1970s in the Muroroa Affair.

**Muroroa’s Precedent:**

An interesting parallel between unilateral letters signed by Panama along with public statements concerning the willingness to sign exchange of information agreements is the Muroroa precedent.

This case concerns New Zealand and Australia claiming France violated International Public Law by continuing nuclear experiments on Muroroa. The Court did not refer to whether France violated IPL but rather ruled that unilateral commitments and public statements declaring the cease of these nuclear tests bound her under IPL[[9]](#footnote-9).

France’s public statements have a striking similarity to those signed by Panama and other tax haven jurisdictions in the past.

On October 2014 Panama and Colombia committed themselves to negotiate to exchange tax information using article 23 of the OECD model convention. Panama got out of its neighbor list only by agreeing to exchange information.

The authors of this article see that legal documents may evidence 1st acceptance in the past of a “harmful” practice in not exchanging tax information, 2nd persuasion as to the equity of the measure, 3rd real sanctions that are in accordance with IPL.

**Boiling big numbers**:

Panama’s brawl with its neighbor comes at a time when OECD brags about a 51 country consensus regarding automatic exchange of information.

How many countries does the international community need to say a consensus exists? Does the list starts at 100?

To the authors of this report the mere willingness of a country that, 20 years ago, could care less about exchange of information to ask its neighbor for a treaty means that a consensus is approaching.

Additionally, the lack of arguments Panama has to deny its neighbor what has given to 25 countries indicates a consensus regarding the existence of a right to “ask” even if a refusal comes from other grounds different from a mere “I could care less” argument.

A further consensus seems to be that a country may refuse to exchange information on tax matters and face sanctions from the other party.

**Is there a way out for Panama**:

International Law gives Panama and any other State a way out of the consensus the authors of this article see. This way is to denounce its treaty obligations along with its commitments with OECD’s Global Forum.

This act will bring Panama sanctions by the international community and it is unlikely that the difficulties this entails will not persuade the country back from its commitments. Additionally, the case may be argued that, along the Muroroa affair precedent that Panama is bound by its own will to comply with exchange of tax information.

**Conclusion**:

Almost a century after the League of Nations’ commission to find principles accepted by States in avoiding double taxation the World is seeing real evidence of these principles outside the bilateral treaty network.

The authors of this article predict that exchange of information will be the first international accepted principle of international law. We do not believe a multilateral convention will be signed, however we predict there will be little room to argue no exchange of information will be given and countries will feel compel not to restrict another country from exchanging tax information.

This effort signals the path to follow by similar efforts to harmonize tax rules in the future as the current G20-OECD BEPs initiative.

1. W.B. Cowcher. The Economic Journal, Vol 33, No. 132, (Dec., 1923), pp.566-579. [↑](#footnote-ref-1)
2. Albert Hensel. Derecho Tributario. Traducción de Leandro Stok y Francisco M.B. Cejas. Nova Tesis. Editorial Jurídica. Reimpresión de 2004. SS4 (Pág 97) [↑](#footnote-ref-2)
3. Reuven Avi-Yonah. International Taxation as International Law. Cambridge University Press. 2007. [↑](#footnote-ref-3)
4. Article 38(1)(b) of the Statute of the International Court of Justice. As evidenced by Brian D. Lepard, this is a concept that needs further precision in International Law (Customary International Law. A new theory with Practical Applications. Cambridge University Press. 2010. ISBN 978-0-511-68236-0). [↑](#footnote-ref-4)
5. Paul O’Neil, US Treasury Secretary, sent letter PO-366 on May 2001 basically saying that OCDE’s effort were of no interest to his country and expressing his concerns over its wide reach which included interfering with the fiscal policy of countries that should decide to have low tax rates. [↑](#footnote-ref-5)
6. Panama sent OCDE a letter on December 2002 considering the “playing level field” violated and cancelling its previous commitment. On December 13, 2002 Antigua and Barbuda followed Panama as reported by the Bermuda Sun’s Edition of December 18, 2002. Sir Ronald Sanders, High Commissioner of Antigua in London and negotiator to the OECD, sent this letter. [↑](#footnote-ref-6)
7. Yariv Brauner. An International Tax Regime in Crystallization. 56 Tax L. Rev. 259. 2003. [↑](#footnote-ref-7)
8. This is Note 101-02-471-DMEyF addressed to OCDE’s General Secretary. [↑](#footnote-ref-8)
9. Press conferences by French public officials are very similar to those given by Panamanian authorities in which a willingness to sign treaties to Exchange tax information is reaffirmed. [↑](#footnote-ref-9)