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Towards Global Tax Co-operation

REPORT TO THE
2000 MINISTERIAL COUNCIL MEETING
AND RECOMMENDATIONS
BY THE COMMITTEE
ON FISCAL AFFAIRS

**Progress in Identifying and Eliminating
Harmful Tax Practices**



ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT

ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT

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EXECUTIVE SUMMARY

For a global economy to succeed, governments must intensify their co-operation and provide international frameworks for the effective management of global issues. Taxation is no exception. In this context, the OECD in 1998 established an international framework to counter the spread of harmful tax competition by adopting its Report, “*Harmful Tax Competition: An Emerging Global Issue*” (the “1998 Report”).¹ Ministers in 1998 welcomed this Report and mandated OECD to pursue the work. The goal is to secure the integrity of tax systems by addressing the issues raised by practices with respect to mobile activities that unfairly erode the tax bases of other countries and distort the location of capital and services. Such practices can also cause undesired shifts of part of the tax burden to less mobile tax bases, such as labour, property, and consumption, and increase administrative costs and compliance burdens on tax authorities and taxpayers.

It is important to note at the outset that the project is not primarily about collecting taxes and is not intended to promote the harmonisation of income taxes or tax structures generally within or outside the OECD, nor is it about dictating to any country what should be the appropriate level of tax rates. Rather, the project is about ensuring that the burden of taxation is fairly shared and that tax should not be the dominant factor in making capital allocation decisions. The project is focused on the concerns of OECD and non-OECD countries, which are exposed to significant revenue losses as a result of harmful tax competition. Tax base erosion as a result of harmful tax practices can be a particularly serious threat to the economies of developing countries. The project will, by promoting a co-operative framework, support the effective fiscal sovereignty of countries over the design of their tax systems.

To counter harmful preferential tax regimes, the Recommendations adopted with the 1998 Report provide a set of Guidelines and a timetable for OECD member countries to identify, report, and eliminate the harmful features of their preferential regimes. They also provide for a dialogue with non-member economies on how they would apply the Guidelines. To counter the spread of tax havens, the Recommendations

1. The Report was approved by the OECD Council, with abstentions from Luxembourg and Switzerland, on 9 April 1998, and was presented to Ministers on 27/28 April 1998.

provide for the Forum to identify jurisdictions that meet specified criteria for being tax havens. The 1998 Report also sets out a general framework for a common approach to defensive measures for restraining harmful tax competition.

This Report to Ministers outlines the results obtained up to date of the Forum's work in these areas. It includes, in particular:

- a) an identification of potentially harmful preferential regimes in Member countries under the factors of the 1998 Report;
- b) an identification of jurisdictions meeting the criteria for being tax havens under the factors of the 1998 Report; and
- c) an update on work with non-member economies and proposals for taking this work forward.

The initial reaction to this project has been encouraging. A number of jurisdictions reviewed under the tax haven criteria and also a number of non-member economies have shown an interest in the project, resulting in an open dialogue. Accordingly, this reporting is not intended to be condemnatory or final, as the process is open and dynamic; it aims to move forward co-operatively so long as a co-operative approach bears fruit. Member countries are already working to eliminate harmful tax practices, and many jurisdictions meeting the tax haven criteria are actively considering taking a commitment within the next 12 months to eliminate harmful tax practices in accordance with the 1998 Report.

To take forward the work, this Report includes proposals by the Committee on Fiscal Affairs (the "Committee") on the follow-up for preferential regimes, for jurisdictions meeting the tax haven criteria, and for non-member economies.

With regard to the preferential tax regime work, the Committee has endorsed the development on a generic basis of guidance on applying the preferential regime criteria of the 1998 Report to the categories and types of preferential regimes that are represented among the regimes identified as potentially harmful. The Forum will work directly and where appropriate through other subsidiary bodies of the Committee in developing the guidance (application notes). The application notes will assist Member countries in determining which of their potentially harmful regimes are, or could be applied to be, actually harmful, and then in determining how to remove the harmful features of such harmful regimes. The application notes also will assist tax havens and other non-member economies in eliminating their harmful tax practices, and will assist the Forum in verifying that Member countries and co-operative jurisdictions have met their respective commitments to eliminate harmful tax practices within established timetables.

With regard to the tax haven work, the Committee has endorsed an approach to extend and to take forward co-operatively the dialogue with jurisdictions that meet the tax haven criteria. In particular, the Committee is now planning to develop

a List of Uncooperative Jurisdictions that could be the subject of a co-ordinated approach to defensive measures, comprised of jurisdictions meeting the tax haven criteria that choose not to eliminate their harmful tax practices.

With regard to non-member economies, the Committee has endorsed a work programme to encourage these economies to associate themselves with the 1998 Report and also to encourage them to take positive steps to remove any harmful features of their preferential tax regimes.

The Committee accepts that the changes necessary for jurisdictions meeting the tax haven criteria that commit to remove their harmful tax practices may adversely affect the economies of some of those jurisdictions. The OECD will work with other interested international and national organisations to examine how best to assist co-operative jurisdictions in restructuring their economies.

The Committee has been engaged in a dialogue with the business community and civil society since the 1998 Report was issued, and this dialogue will be continuing during the period of implementation of the Report's recommendations.

The OECD's work through the Forum has evolved into a consensus-building, co-operative approach with interested parties who are willing to make positive change and contribute to emerging international principles of transparency, fairness, and disclosure. This evolution should be viewed in the context of other international efforts to encourage offshore financial centres to improve their regulatory environment. For example, the widespread financial crisis of the late 1990s has led to the creation of the Financial Stability Forum, the strengthening of the International Monetary and Finance Committee of the IMF, and other proposals to improve the transparency and operation of financial markets, including the functioning of offshore financial centres. Other institutions, such as the FATF and the UN Commission on Money Laundering, are addressing serious international criminal activities and money laundering in particular. The present Report represents the first stage in implementing the 1998 Report in a manner complementary to these other international efforts.

I. Introduction

1. This Report responds to the mandate given by Ministers in April 1998 to counter the spread of harmful tax competition. The mandate is contained in the OECD Report: Harmful Tax Competition: An Emerging Global Issue (the “1998 Report”).² The 1998 Report contains 19 recommendations (the “Recommendations”) to counter harmful tax practices, with a scope aimed at geographically mobile financial and other service activities. The OECD created the Forum on Harmful Tax Practices to carry out the work.

2. To counter harmful preferential tax regimes, the Recommendations provide a set of Guidelines and a timetable for OECD member countries to identify, report, and eliminate the harmful features of their preferential regimes. They also provide for a dialogue with non-member economies on how they would apply the Guidelines. To counter the spread of tax havens, the Recommendations provide for the Forum to identify jurisdictions that meet specified criteria for being tax havens. The 1998 Report also sets out a general framework for a common approach to defensive measures for restraining harmful tax competition.

3. This Report to Ministers outlines the progress made to date of the Forum’s work in these areas.

2. The Report was approved by the OECD Council, with abstentions from Luxembourg and Switzerland, on 9 April 1998, and was presented to Ministers on 27/28 April 1998.

II. The Review Process

A. Process of Reviewing Member Country Regimes

4. As part of the 1998 Report, the Council adopted Guidelines for Dealing with Harmful Preferential Regimes in Member Countries. Under these Guidelines, which form an integral part of the Council Recommendation, the harmful features of preferential regimes in Member countries must be removed within 5 years (*i.e.* by April 2003). There is a limited “grandfather clause” for taxpayers benefiting from such regimes on 31 December 2000; these benefits are to be removed at the latest by 31 December 2005. The Guidelines include a “standstill” provision requiring that Member countries refrain from adopting new measures or extending the scope of existing measures that constitute harmful tax practices.

5. Part III(a) of the 1998 Report sets out “features of tax regimes which suggest that they have the potential to constitute harmful tax competition” (see paragraph 60 of the 1998 Report).³ To carry out the work on identifying harmful preferential tax regimes, the Forum requested that each member country perform a self-review of its preferential regimes with regard to these features (hereinafter the “preferential regime criteria”). At the same time as the self-reviews were undertaken, cross-country reviews by Study Groups were carried out with respect to specific types of preferential regimes. The cross-country reviews were intended to be generic, *i.e.* the basic features of similar regimes were described without reference to country names. After the self-reviews were completed, a peer review process was undertaken for each reported preferential regime (for financial and other service activities) according to the preferential regime criteria. The peer review process involved the development of extensive questionnaires, containing both specific questions about regimes and generic questions about the preferential regime criteria, which

3. In brief, there are four main factors, similar to the tax haven criteria discussed in the next section: 1) the regime imposes low or no taxes on the relevant income (from geographically mobile financial and other service activities); 2) the regime is ring-fenced from the domestic economy; 3) the regime lacks transparency, *e.g.* the details of the regime or its application are not apparent, or there is inadequate regulatory supervision or financial disclosure; and 4) there is no effective exchange of information with respect to the regime. There are also a number of other factors to be considered, including the extent of compliance with the OECD Transfer Pricing Guidelines.

were submitted to Member countries, answered in writing, and discussed at meetings of the Forum.

6. Three Working Groups were established within the Forum to review preferential tax regimes and these Working Groups and the Forum met and worked intensively between November 1999 and May 2000. The results of those reviews are described in Part III.A. below.

B. Process of Reviewing Jurisdictions under the Tax Haven Criteria

7. Part II(b) of the 1998 Report described its starting point for identifying a tax haven as whether the jurisdiction has no or nominal taxation on financial or other service income and offers or is perceived to offer itself as a place where non-residents can escape tax in their country of residence. Other key factors are used to confirm the existence of a tax haven (hereinafter referred to as the “tax haven criteria”)⁴ that focus on transparency, exchange of information, and local business activities of foreign enterprises. The fact that a jurisdiction may impose no or nominal tax on the relevant income is a necessary but not sufficient condition for the jurisdiction to be considered a tax haven. Whether a jurisdiction meets the tax haven criteria is determined based upon all the facts and circumstances, including whether the jurisdiction has a significant untaxed offshore financial/other services sector relative to its overall economy.

8. The evaluation of jurisdictions under the tax haven criteria was based on an in-depth factual review of such jurisdictions that appeared to have the potential for satisfying the criteria. Starting from published sources, the Forum identified an initial grouping of 47 such jurisdictions. These jurisdictions were asked to submit information pertinent to the application of the tax haven criteria in the context of their facts and circumstances. The Forum examined, discussed, and reviewed this information, using a series of bilateral contacts (under the auspices of small Study Groups comprised of Forum members) and through multilateral consultations with the Forum itself. The Study Groups prepared factual jurisdiction reports with input from, and in many cases agreement by, the jurisdictions as to the factual accuracy of the reports. In these contacts and consultations, the full participation of each jurisdiction was invited and encouraged.

4. The four key factors, similar to the preferential regime criteria discussed in the preceding section: 1) there is no or nominal tax on the relevant income (from geographically mobile financial and other service activities); 2) there is no effective exchange of information with respect to the regime; 3) the jurisdiction’s regimes lack transparency *e.g.* the details of the regime or its application are not apparent, or there is inadequate regulatory supervision or financial disclosure; and 4) the jurisdiction facilitates the establishment of foreign-owned entities without the need for a local substantive presence or prohibits these entities from having any commercial impact on the local economy.

9. On the basis of the information submitted by the jurisdictions, the factual jurisdiction reports, the bilateral and multilateral contacts with the jurisdictions, and the Forum's discussions, the Forum in November 1999 made technical evaluations of which jurisdictions met the tax haven criteria. Each technical evaluation was undertaken on the facts and circumstances of the particular jurisdiction under review specifically with regard only to the criteria of the report. The Forum's conclusions reflect only those criteria, notwithstanding that among the jurisdictions meeting the criteria there is a wide range of circumstances both in relation to these criteria (*e.g.* some jurisdictions meet higher standards of transparency, openness, and exchange of information than others) as well as in relation to other important standards (*e.g.* the quality of their internal financial regulation and willingness to co-operate internationally in tackling money laundering and other financial crime). The results of those evaluations are described in Part III.B. below.

III. Evaluations and Follow-Up Work

A. Member Country Preferential Regimes

10. From among the preferential tax regimes reviewed as discussed above, the Forum has identified below preferential tax regimes as potentially harmful, consistent with paragraphs 59 and 60 of the 1998 Report. In order to be as comprehensive as possible, a preferential tax regime is identified as potentially harmful if it has features that suggest that the regime has the potential to constitute a harmful tax practice, even though there has not yet been an overall assessment of all the relevant factors to determine whether regimes are actually harmful. Further, economic effects as described in paragraphs 80 to 84, as informed by paragraph 27, of the 1998 Report have not been assessed. Accordingly, the potentially harmful regimes include, *e.g.* regimes where the question of actual harm depends on the regime's application in specific circumstances, and regimes that have features of concern to the Forum under the preferential regime criteria but that have not been determined at this stage to be actually harmful or not actually harmful. Further work will assist Member countries in determining which of their potentially harmful regimes are, or could be applied to be, actually harmful, and in determining how to remove the harmful features of such harmful regimes, as described in paragraphs 13-15.

11. The preferential tax regimes identified as potentially harmful are:⁵

Country	Regimes ⁶
Insurance	
Australia	Offshore Banking Units
Belgium	Co-ordination Centres

5. It is recognised that there may be additional regimes which will be examined as part of the future work of the Forum. See paragraph 25.

6. The preferential tax regimes are listed category-by-category. Certain regimes allow investors to carry out many different types of activities. Forty-seven preferential regimes are identified, but some are included in more than one category of the listing.

Finland	Åland Captive Insurance Regime
Italy	Trieste Financial Services and Insurance Centre ⁷
Ireland	International Financial Services Centre
Portugal	Madeira International Business Centre
Luxembourg	Provisions for Fluctuations in Re-Insurance Companies
Sweden	Foreign Non-life Insurance Companies

Financing and Leasing

Belgium	Co-ordination Centres
Hungary	Venture Capital Companies
Hungary	Preferential Regime for Companies Operating Abroad
Iceland	International Trading Companies
Ireland	International Financial Services Centre
Ireland	Shannon Airport Zone
Italy	Trieste Financial Services and Insurance Centre ⁸
Luxembourg	Finance Branch
Netherlands	Risk Reserves for International Group Financing
Netherlands	Intra-group Finance Activities
Netherlands	Finance Branch
Spain	Basque Country and Navarra Co-ordination Centres
Switzerland	Administrative Companies

Fund Managers⁹

Greece	Mutual Funds/Portfolio Investment Companies [Taxation of Fund Managers]
Ireland	International Financial Services Centre [Taxation of Fund Managers]
Luxembourg	Management companies [Taxation of management companies that manage only one mutual fund (1929 holdings)]
Portugal	Madeira International Business Centre [Taxation of Fund Managers]

Banking

Australia	Offshore Banking Units
Canada	International Banking Centres
Ireland	International Financial Services Centre
Italy	Trieste Financial Services and Insurance Centre ⁸
Korea	Offshore Activities of Foreign Exchange Banks
Portugal	External Branches in the Madeira International Business Centre
Turkey	Istanbul Offshore Banking Regime

7. Non-operational.

8. Non-operational.

9. The taxation of fund managers is complex, given the various legal forms that can be used to structure fund management advice. These issues will be studied further in connection with the development of the application notes described in paragraph 13 in order to ensure that all similar regimes are treated the same.

Headquarters regimes

Belgium	Co-ordination Centres
France	Headquarters Centres
Germany	Monitoring and Co-ordinating Offices
Greece	Offices of Foreign Companies
Netherlands	Cost-plus Ruling
Portugal	Madeira International Business Centre
Spain	Basque Country and Navarra Co-ordination Centres
Switzerland	Administrative Companies
Switzerland	Service Companies

Distribution Centre Regimes

Belgium	Distribution Centres
France	Logistics Centres
Netherlands	Cost-plus/Resale Minus Ruling
Turkey	Turkish Free Zones

Service Centre Regimes

Belgium	Service Centres
Netherlands	Cost-plus Ruling

Shipping¹⁰

Canada	International Shipping
Germany	International Shipping
Greece	Shipping Offices
Greece	Shipping Regime (Law 27/75)
Italy	International Shipping
Netherlands	International Shipping
Norway	International Shipping
Portugal	International Shipping Register of Madeira

Miscellaneous Activities

Belgium	Ruling on Informal Capital
Belgium	Ruling on Foreign Sales Corporation Activities
Canada	Non-resident Owned Investment Corporations
Netherlands	Ruling on Informal Capital
Netherlands	Ruling on Foreign Sales Corporation Activities
United States	Foreign Sales Corporations ¹¹

10. The analysis of shipping is complex given the particularities of the activity. The criteria must be developed so as to take into account and be consistent with those particularities and will be considered further in connection with the development of application notes as regards shipping. Also, such further consideration shall compare tax equivalence of alternative regimes and should aim to establish similar standards for all comparable regimes.

11. As is the case with all regimes, the foreign sales corporation regime is only within the scope of the Report to the extent that it applies to mobile financial and other service activities. It should be noted that the treatment of the foreign sales corporation regime or any other regime for purposes of this Report has no bearing on its classification or treatment in connection with trade disciplines.

12. Holding company regimes and similar preferential tax regimes are not included above, although such regimes may constitute harmful tax competition. The Forum was presented with a number of holding company regimes and similar provisions, but in light of the complexities raised by such regimes, including their possible interaction with tax treaties and with generally applicable principles of domestic law, the Forum reached no conclusions concerning their status as potentially harmful preferential regimes. Continuing the work on holding company regimes and similar preferential regimes will be a high priority in the ongoing work of the Forum, with the aim of reaching firm proposals within the context of preparing application notes (see paragraph 13 below) by early 2001. Holding company regimes and similar preferential tax regimes in the following countries are being examined: Austria, Belgium, Denmark, France, Germany, Greece, Iceland, Ireland, Luxembourg, Netherlands, Portugal, Spain, Switzerland.

13. More work is needed in interpreting the manner in which the criteria apply. In the next stage of the work, the Forum will develop guidance on applying the preferential regime criteria of the 1998 Report to the categories and types of preferential tax regimes that are represented among the regimes identified as potentially harmful. This guidance (application notes) would be provided on a generic basis (*i.e.* not referring to specific country regimes) and would be equally applicable to any regime of the category or type being addressed. The application notes will illustrate what features, generically, would be problematic for particular categories or types of regimes under the relevant factors of the 1998 Report. The application notes will build upon the cross-country reviews undertaken in the initial evaluation of preferential regimes.

14. The Forum will work directly and where appropriate through other subsidiary bodies of the Committee in developing the application notes. For example, the Forum has asked the Committee's Working Party on Taxation of Multinational Enterprises to work on developing guidance in the area of rulings systems and other transfer pricing issues, and the Forum has asked the Committee's Working Party on Tax Avoidance and Evasion to provide advice on effective exchange of information. The Committee's Working Party on Tax Policy Analysis and Statistics may also need to assist in particular cases to the extent that economic analysis is relevant.

15. Member countries will be assisted by the application notes in making the assessment whether potentially harmful regimes are, or could be applied to be, actually harmful, and then in determining how to remove the harmful features of such harmful preferential regimes, in order to meet their commitments to eliminate the harmful features of harmful preferential tax regimes by April 2003. In respect of taxpayers benefitting from such regimes on 31 December 2000, the benefits they derive are to be removed by 31 December 2005. The Forum will undertake a verification process to ascertain that OECD countries have met this commitment, and will report back to the OECD Council no later than June 2003 to list any preferential regimes that have been

found to be actually harmful and whose harmful features remain in OECD Member countries at that time. The application notes will assist the Forum in verifying whether Member countries and co-operative jurisdictions (as described below) have met their respective commitments to remove harmful tax practices within established timetables. The application notes also are expected to assist co-operative jurisdictions and other non-member economies in eliminating their harmful tax practices.

16. Work on removing the harmful features of preferential tax regimes in OECD countries must continue in parallel with that on counteracting the effects of tax havens, as discussed below. The application of the deadline set in the 1998 Report for Member countries to remove the harmful features of any harmful preferential tax regime is not contingent on the Forum determining that the regime is harmful. If harmful features are not eliminated by the prescribed deadlines, other countries may wish to take defensive measures (as foreseen in paragraph 96 of the 1998 Report). Accordingly, the proposal to develop application notes described above is not intended to affect the timing of national efforts by countries to remove the harmful features of any of their harmful preferential tax regimes. Rather, the objective is to develop application notes simultaneously with those efforts. However, it will be a priority for the Committee to ensure sufficient progress is made by the Forum on the development of the application notes to allow for timely guidance to countries, and to facilitate consistency and fairness.

B. Tax Haven Work

17. A small number of the jurisdictions reviewed by the Forum have, in advance of this reporting, made a public political commitment at the highest level (an “advance commitment”) to eliminate their harmful tax practices and to comply with the principles of the 1998 Report.¹² In recognition of this commitment, this

12. An advance commitment jurisdiction also agrees to a standstill, i.e. not to enhance existing regimes that the Forum finds constitute harmful tax practices, and not to introduce new regimes that would constitute harmful tax practices. An advance commitment jurisdiction will develop with the Forum an acceptable plan by 31 December 2000, describing the manner in which the jurisdiction intends to achieve its commitment, the timetable for so doing, and milestones to ensure steady progress, including the completion of a concrete and significant action during the first year of the commitment. All advance commitment jurisdictions must fulfil their commitments by the date on which Member countries must remove the benefits to taxpayers benefiting on 31 December 2000 from any harmful preferential regimes (31 December 2005, which is 2-½ years after the main deadline by which Member countries have committed to eliminate the harmful features of their harmful preferential regimes). The follow-up for advance commitment jurisdictions is discussed in Part IV below. An advance commitment is similar but not identical to the post-June “scheduled commitment” described in Part IV.

Report does not include the names of jurisdictions that have made this advance commitment (“advance commitment jurisdictions”) even if they presently meet the tax haven criteria.¹³ Otherwise, the jurisdictions below were found to meet the tax haven criteria of the 1998 Report. These evaluations were presented to the Committee in January 2000, confirmed by the Committee in May 2000, and endorsed by the Council on 16 June 2000. This listing is intended to reflect the technical conclusions of the Committee only and is not intended to be used as the basis for possible co-ordinated defensive measures. Rather, as discussed below, a further list will be developed in the next 12 months for this purpose.

Andorra	The Republic of the Maldives
Anguilla – Overseas Territory of the United Kingdom	The Republic of the Marshall Islands
Antigua and Barbuda	The Principality of Monaco
Aruba – Kingdom of the Netherlands ^a	Montserrat – Overseas Territory of the United Kingdom
Commonwealth of the Bahamas	The Republic of Nauru
Bahrain	Netherlands Antilles – Kingdom of the Netherlands ^a
Barbados	Niue – New Zealand ^b
Belize	Panama
British Virgin Islands – Overseas Territory of the United Kingdom	Samoa
Cook Islands – New Zealand ^b	The Republic of the Seychelles
The Commonwealth of Dominica	St Lucia
Gibraltar – Overseas Territory of the United Kingdom	The Federation of St. Christopher & Nevis
Grenada	St. Vincent and the Grenadines
Guernsey/Sark/Alderney – Dependency of the British Crown	Tonga
Isle of Man – Dependency of the British Crown	Turks & Caicos – Overseas Territory of the United Kingdom
Jersey – Dependency of the British Crown	US Virgin Islands – External Territory of the United States
Liberia	The Republic of Vanuatu
The Principality of Liechtenstein	

a) The Netherlands, the Netherlands Antilles, and Aruba are the three countries of the Kingdom of the Netherlands.

b) Fully self-governing country in free association with New Zealand.

13. Ministers in their communiqué welcomed these highest-level commitments.

i) Preparing a List of Uncooperative Tax Havens

18. During the process of consultations, a number of the jurisdictions under review indicated an interest in the possibility of co-operating with the OECD by committing to the elimination of harmful tax practices. The extent of the interest in co-operation was not fully foreseen at the time that the 1998 Report was presented to Ministers. In response to this development, the Committee believes that a process should be established to promote co-operation and positive changes to comply with the principles of the 1998 Report. Such a step would be in harmony with the Council Instruction of 9 April 1998 to make proposals for further improvements in the co-operation to counter harmful tax practices, and also in harmony with the 1998 Report itself, which provides that in implementing the Recommendations of the Report, account should be taken of the commitment which the jurisdictions involved make to the elimination of harmful tax practices.

19. To facilitate the taking forward of a co-operative process, the Committee has already invited jurisdictions to consider making commitments to the elimination of harmful tax practices, and the Council has in its 16 June 2000 Recommendation instructed the Committee to continue these efforts over the next 12 months. The Council also instructed the Committee to produce, from the list of jurisdictions meeting the tax haven criteria (*i.e.* the list in paragraph 17 as it may be amended in the future) an OECD List of Uncooperative Tax Havens. This List is to be completed by 31 July 2001. Any jurisdiction listed in paragraph 17 above that by this deadline does not make the commitment to eliminating harmful tax practices in the manner and substance as described in *ii)* below would automatically be included in the List of Uncooperative Tax Havens.¹⁴

20. To recognise the ongoing efforts being made by some of the jurisdictions to continue the dialogue, and to encourage jurisdictions to make commitments to the tax competition work, the Committee recommended and the Council agreed that the co-ordination of a common approach to defensive measures should not be undertaken with respect to jurisdictions that have committed to the tax competition work, as discussed below (*i.e.* those jurisdictions not appearing on the List of Uncooperative Tax Havens). Accordingly, the co-ordination of defensive measures foreseen in the 1998 Report, as described in Part IV below will not be implemented prior to 31 July 2001.

14. A jurisdiction making an advance commitment (pre-June 2000) also would not appear on the List of Uncooperative Tax Havens and would not be subject to co-ordinated defensive measures. There will be an annual review by the Forum to determine whether the established milestones and timetables are being met. If the milestones and timetables are not met and there is at any time evidence that the jurisdiction's commitment to the tax competition work is no longer in good faith, the Committee will place the jurisdiction on the List of Uncooperative Tax Havens.

ii) Commitment to Eliminating Harmful Tax Practices

21. The commitment necessary to avoid inclusion on the List of Uncooperative Tax Havens is a public political commitment by a jurisdiction to adopt a schedule of progressive changes to eliminate its harmful tax practices by 31 December 2005. This is the date set in the 1998 Report for Member countries to remove the benefits to taxpayers benefiting on 31 December 2000 from any harmful preferential regime (which is approximately 2-½ years after the main deadline by which Member countries have committed to remove the harmful features of their harmful preferential tax regimes). A jurisdiction making this commitment (a “scheduled commitment”) will develop with the Forum an acceptable plan within 6 months of having made the commitment, describing the manner in which the jurisdiction (a “co-operative jurisdiction”) intends to achieve its commitment, the timetable for so doing, and milestones to ensure steady progress, including the completion of a concrete and significant action during the first year of the commitment. The jurisdiction must also agree to a “standstill” during the period of the commitment, *i.e.*, not to enhance existing regimes that the Forum finds constitute harmful tax practices; not to introduce new regimes that would constitute harmful tax practices; and to engage in an annual review process with the Forum to determine the progress made in fulfilling its commitment and to assess the use being made of its existing regimes.

22. A co-operative jurisdiction, at the time of making its scheduled commitment, would not be included in the List of Uncooperative Tax Havens for an initial period of one-year from that time. A co-operative jurisdiction is eligible for successive renewals of its status by making a new public commitment to move to the next stage of the plan of progressive changes. However, a jurisdiction would be placed on the List of Uncooperative Tax Havens if any harmful aspects of its regimes remain after the deadline for their elimination. Also, if the milestones and timetable are not met and there is at any time evidence that the jurisdiction is not acting in good faith in accordance with its commitments, the Committee will place the jurisdiction on the List of Uncooperative Tax Havens.

23. The procedure for making a scheduled commitment is that a jurisdiction submits a written statement of the commitment of its government as described in paragraph 21 above. The statement is to be in the form of a letter to the Secretary-General of the OECD, and signed by an authorised official.¹⁵ This letter is to be accompanied by an annex setting forth the specifications to which the jurisdiction is agreeing, as discussed with the Forum.

¹⁵An authorised official would be an official having authority in regulatory and fiscal matters and appointed by the jurisdiction to represent the jurisdiction in dealing with the Forum.

C. Dynamic Nature of the Evaluations of Preferential Regimes and Tax Havens

24. The evaluations given in this Report are dynamic for both potentially harmful preferential regimes and for jurisdictions meeting the tax haven criteria. Accordingly, the evaluations will be regularly updated as the work is taken forward. With regard to the tax haven work, jurisdictions that will appear on the List of Uncooperative Tax Havens remain eligible to make scheduled commitments at any time and thereby be removed from the List of Uncooperative Tax Havens. Further, a jurisdiction's name would be removed from the List of Uncooperative Tax Havens and no longer be identified as meeting the tax haven criteria if the jurisdiction were to eliminate its harmful tax practices, without regard to whether a scheduled commitment is made. The process of pursuing a scheduled commitment can be initiated by a listed tax haven by writing to OECD Secretariat or to the Chair of the Committee.

25. The OECD's work in this area must not only address existing tax havens and harmful tax practices, but it must be vigilant against adverse developments. Such developments could be new jurisdictions entering the field, the introduction of new harmful preferential regimes by jurisdictions/ countries that are already being evaluated, a change in posture as regards commitments to eliminate the harmful aspects of their regimes, or the discovery of other jurisdictions/regimes that constitute harmful tax practices. The dynamic nature of this work has resource implications for the OECD that must be addressed in the context of the Committee's priorities, as indicated in paragraph 39.

D. Extending the Dialogue with Co-operative Jurisdictions

26. The Committee intends to continue the dialogue with co-operative jurisdictions. Such work will include:

- The development of a model vehicle for exchange of information (*e.g.* an OECD Model Tax Information Exchange Agreement or a multilateral agreement).
- The creation of a multilateral framework under the Forum for consultation with co-operative jurisdictions, on exchange of information and other relevant issues pertaining to the elimination of harmful tax practices.
- An examination of the types of assistance that jurisdictions will need in the transition, recognising that an initial reduction in certain financial and other service activities may occur in some jurisdictions as a result of complying with the principles of the Report. OECD governments may consider:
 - Examining how their bilateral assistance programmes can be re-targeted.

- Encouraging international organisations to take into account the special needs of these jurisdictions in the design of multilateral assistance programmes.
- Offering under the auspices of the OECD and other organisations specific assistance in the design of their tax systems and in the strengthening of their tax administrations.
- Encouraging jurisdictions to initiate co-operative programmes to improve tax administration and enforcement by using existing organisations such as Intra-European Organisation of Tax Administrations (IOTA), Inter-American Centre of Tax Administrators (CIAT), Commonwealth Association of Tax Administrators (CATA), the Caribbean Community – (CARICOM), Centre de rencontres et d'études des dirigeants des administrations fiscales (CRE-DAF), and the Organization for Economic Cooperation (OEC).

27. The Committee accepts that the changes that will be necessary for jurisdictions meeting the tax haven criteria that commit to remove their harmful tax practices may adversely affect the economies of some of those jurisdictions. The OECD will work with other interested international and national organisations to examine how best to assist co-operative jurisdictions in restructuring their economies. A dialogue has already been launched with the OECD's Development Assistance Committee. Also, the Committee on Fiscal Affairs, by means of its CCNM-sponsored outreach programme, is prepared to assist jurisdictions in meeting the standards contemplated by the 1998 Report.

IV. Involving Non-Member Economies

28. Harmful tax competition is by its very nature a global phenomenon and therefore its solution requires global endorsement and global participation. Countries outside the OECD must have a key role in this work since a number of them are either seriously affected by harmful tax practices or have potentially harmful regimes. Three regional seminars that brought together over 30 non-member countries were held prior to the finalisation of the 1998 Report: in Mexico (for the Latin American region); by the Asian Development Bank in Singapore (for the Asian region); in Turkey (for the NIS region). These three seminars have enabled the Committee to gain a better understanding of the concerns of countries outside the OECD area. Non-member economies should be invited to continue a dialogue with the OECD in relation to the work on tax competition.

29. Some non-member economies feature strongly in the global financial marketplace, with possibly major distortions being caused by the harmful tax practices they have put in place. There is a significant risk that a failure to address these practices in parallel with the work in relation to Member countries will cause a shift of the targeted activities to economies outside the OECD area, giving them an unwarranted competitive advantage and limiting the effectiveness of the whole exercise.

30. It is important to take forward the work of the Forum with regard to eliminating harmful tax practices on a global basis. To this end, the Committee will encourage non-member economies to associate themselves with the 1998 Report and to agree to its principles; and hold regional seminars that will encourage and assist non-member economies to remove features of their preferential regimes that are potentially harmful. This work programme should progress on a timetable that would facilitate the removal of harmful tax practices in non-member economies by 31 December 2005.

31. The Committee proposes that the Forum continue and intensify its dialogue to explore ways in which non-member economies that share the concerns of OECD members and that are prepared to accept the same obligations as OECD members could be more closely associated with the Forum. In this way, non-member economies can become partners in the development of an international framework

appropriate in an era of liberalised financial markets. The Committee will initiate the dialogue regarding this approach on 29-30 June 2000 at a high-level meeting for non-member economies co-hosted by the Finance Minister of France.

V. Framework for Implementing a Common Approach to Restraining Harmful Tax Practices

32. One objective of identifying harmful tax practices is to facilitate through co-ordination the OECD Member countries' actions against such practices, recognising the limitations on the effectiveness of unilateral actions.

33. The Committee recommends a general framework within which Member countries can implement a common approach to restraining harmful tax competition. This framework will facilitate the ability of countries to take defensive measures swiftly and effectively against jurisdictions that persist in their harmful tax practices. Defensive measures are important so that the adverse impacts from uncooperative jurisdictions can be addressed and so that these jurisdictions do not gain a competitive advantage over co-operative jurisdictions. In the application of the co-ordinated defensive measures, no distinction shall be made between jurisdictions that are dependencies of OECD countries and those that are not. These defensive measures would be at the discretion of countries and taken under their domestic legislation or under tax treaties. Moreover, each country may choose to enforce the defensive measures in a manner that is proportionate and prioritised according to the degree of harm that a particular jurisdiction has the potential to inflict, and taking into account the effectiveness of its existing defensive measures.

34. The 1998 Report suggested that defensive measures would be more effective if applied by a wide number of countries in a similar manner. A number of potential measures were identified for further study by the Forum. Paragraph 35 sets out these measures together with a number of other possible measures that the Forum believes might be able to form the framework of a common approach against harmful tax practices. The Committee on Fiscal Affairs will be working within the next six months to a year to consider these possible measures, finalise its recommendations, and adopt an implementation strategy and timetable. Those co-operating with the tax competition work will then be invited to adopt such of the measures recommended by the Committee to the extent possible and appropriate within their national systems, to be implemented against Uncooperative Tax Havens as of 31 July 2001. Countries may also take note of the defensive measures for purposes

of combating any harmful tax practices that persist after the time by which they are expected to be removed.

35. The range of possible defensive measures identified to date as a framework for a common approach with regard to Uncooperative Tax Havens as of 31 July 2001 are as follows:

- To disallow deductions, exemptions, credits, or other allowances related to transactions with Uncooperative Tax Havens or to transactions taking advantage of their harmful tax practices.
- To require comprehensive information reporting rules for transactions involving Uncooperative Tax Havens or taking advantage of their harmful tax practices, supported by substantial penalties for inaccurate reporting or non-reporting of such transactions.
- For countries that do not have controlled foreign corporation or equivalent (CFC) rules, to consider adopting such rules, and for countries that have such rules, to ensure that they apply in a fashion consistent with the desirability of curbing harmful tax practices (Recommendation 1 of the 1998 Report).
- To deny any exceptions (*e.g.* reasonable cause) that may otherwise apply to the application of regular penalties in the case of transactions involving entities organised in Uncooperative Tax Havens or taking advantage of their harmful tax practices.
- To deny the availability of the foreign tax credit or the participation exemption with regard to distributions that are sourced from Uncooperative Tax Havens or to transactions taking advantage of their harmful tax practices.
- To impose withholding taxes on certain payments to residents of Uncooperative Tax Havens.
- To enhance audit and enforcement activities with respect to Uncooperative Tax Havens and transactions taking advantage of their harmful tax practices.
- To ensure that any existing and new domestic defensive measures against harmful tax practices are also applicable to transactions with Uncooperative Tax Havens and to transactions taking advantage of their harmful tax practices.
- Not to enter into any comprehensive income tax conventions with Uncooperative Tax Havens, and to consider terminating any such existing conventions unless certain conditions are met (Recommendation 12 of the 1998 Report).
- To deny deductions and cost recovery, to the extent otherwise allowable, for fees and expenses incurred in establishing or acquiring entities incorporated in Uncooperative Tax Havens.
- To impose “transactional” charges or levies on certain transactions involving Uncooperative Tax Havens.

36. Governments are invited to take into account that a jurisdiction is listed as an Uncooperative Tax Haven in determining whether to direct non-essential economic assistance to the jurisdiction. The Committee also intends to continue to explore what other defensive measures can be taken, including non-tax measures.

37. Governments are also reminded of Recommendation 17 of the 1998 Report, which recommends that countries with particular political, economic, or other links with tax havens ensure that these links do not contribute to harmful tax competition. Also, paragraph 153 of the 1998 Report indicates that countries that have such ties should consider using them to reduce the harmful tax competition resulting from the existence of these tax havens.

38. The Committee invites Member countries to refrain from using the names of jurisdictions in paragraph 17 to identify jurisdictions against which new or enhanced defensive measures should be applied, but rather to use the List of Uncooperative Jurisdictions for this purpose. The Forum recognises that Member countries retain the right to apply, or not apply, defensive measures unilaterally to any jurisdiction.

VI. The Resource Implications for the OECD

39. The success of the work programme outlined above will depend upon OECD Member countries being prepared to strengthen the parts of their administrations dealing with international tax issues and to ensure that the organisation has the resources necessary to carry out this work which the Committee recognises may require a review of priorities within the OECD budget. The Committee does not underestimate the constraints that countries face in providing such resources. Ministers are therefore encouraged to ensure that their national administrations and the OECD have the resource bases from which to move to a successful conclusion of this work.

**RECOMMENDATION OF THE COUNCIL
ON IMPLEMENTING THE PROPOSALS CONTAINED
IN THE 1998 REPORT ON HARMFUL TAX COMPETITION
(ADOPTED BY THE COUNCIL ON 16 JUNE 2000)**

THE COUNCIL,

- Having regard to Article 5*b*) of the Convention on the Organisation for Economic Co-operation and Development of 14 December 1960;
- Having regard to the Report entitled “Harmful Tax Competition; An Emerging Global Issue” (the “*1998 Report*”);
- Having regard to the Recommendation of the Council dated 9 April 1998 on counter-acting Harmful Tax Competition adopted by the Council on 9 April [C(98)17/FINAL];*
- Having regard to the Report adopted by the Committee on Fiscal Affairs on “Progress on Identifying and Eliminating Harmful Tax Practices” (the “*2000 Report*”) (DAFFE/CFA/FHP(2000)11/REV2/CONF, attached as Annex I) at its meeting on 25 May 2000;
- Recognising the OECD’s role in promoting an open, multilateral trading system and the need to promote the “level playing field” which is essential to the continued expansion of global economic growth;
- Recognising that the process of globalisation and the development of new technologies has brought about prosperity for many citizens around the world, but also raises challenges for governments to minimise tax induced distortions in investment and financing decisions and to maintain their tax base in this new global environment;
- Considering that if governments do not intensify their co-operation, the tax base will be eroded, a part of the tax burden will shift from income on mobile activities to taxes on non mobile activities and that such a shift would make tax systems less equitable and may have a negative effect on employment;
- Recognising the need for an ongoing dialogue with non-member economies to encourage them to associate themselves with the recommendations set out in the *1998 Report*;
- Noting, in this respect, the high-level meeting with non-member economies co-hosted by France and the OECD, scheduled for 29-30 June 2000 to explore ways in which they can be more closely associated with the *1998 Report*;
- Noting, furthermore, the high level political commitment made by Bermuda, Cayman Islands, Cyprus, Malta, Mauritius, and San Marino to eliminate harmful tax practices in accordance with the principles set out in the *1998 Report*;

* Luxembourg and Switzerland abstained.

- Having regard to the jurisdictions identified in the *2000 Report* that meet the criteria set out in the *1998 Report* for being a tax haven;
- Noting the proposal of the Committee on Fiscal Affairs to produce by 31 July 2001 a List of Uncooperative Tax Havens and to use this List as the basis for implementing co-ordinated defensive measures;
- Having regard to preferential tax regimes in OECD Member Countries identified as potentially harmful;

On the proposal of the Committee on Fiscal Affairs:

1. **RECOMMENDS** that Member countries having approved the 1998 Report:
 1. Collectively through the Committee on Fiscal Affairs take forward an active dialogue with the jurisdictions identified in the *2000 Report* as meeting the tax haven criteria with a view to obtaining the commitment of these jurisdictions to eliminate harmful tax practices in accordance with the principles of the *1998 Report*;
 2. Refrain from using the identification of jurisdictions meeting the tax haven criteria in the *2000 Report* as a basis for new or enhanced defensive measures, but rather to use the list of un-cooperative tax havens for this purpose.
 3. Individually and collectively explore ways, on a global as well as regional basis, to assist co-operative jurisdictions to move away from harmful tax practices.
2. **INSTRUCTS** the Committee on Fiscal Affairs to:
 1. Establish a co-operative process to promote the elimination of harmful tax practices by the jurisdictions identified in the *2000 Report* as meeting the tax haven criteria;
 2. Produce an OECD List of Uncooperative Tax Havens, by 31 July 2001;
 3. Include automatically on the OECD List of Uncooperative Tax Havens any jurisdiction identified in the *2000 Report* as meeting the tax haven criteria if the jurisdiction does not by 31 July 2001 commit to eliminate harmful tax practices in accordance with the *1998 Report* in a manner satisfactory to Member countries;
 4. Update regularly the OECD List of Uncooperative Tax Havens;
 5. Carry out work through the Forum on Harmful Tax Practices and, where appropriate, through other subsidiary bodies of the Committee, to develop guidance (application notes) to assist Member and non Member Countries in assessing whether their potentially harmful preferential regimes are, or could be applied to be, actually harmful, and in determining how to remove the harmful features of such regimes, in order to meet their commitments under Recommendation 15 of the *1998 Report* to remove harmful features of harmful preferential tax regimes by April 2003;
 6. Undertake a verification process to ascertain that OECD countries have met their commitments, and report back to the OECD Council no later than June 2003 regarding compliance with Recommendation 15 of the *1998 Report*;
 7. Explore ways in which non-member economies that share the concerns of Member countries to counter harmful tax practices can be brought into an active dialogue with the Forum on Harmful Tax Practices;
 8. Work with interested international and bilateral assistance agencies to assist co-operative jurisdictions to meet the tax and regulatory standards set out in the *1998 OECD Report* and to work with these jurisdictions during the transitional period to support their economies as they move away from harmful tax practices.

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