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## Proposed article 26 (proposed 2007) of the United Nations Model Tax Convention between Developing Countries

### Proposed commentary on paragraphs 1-3 prepared by the Subcommittee on Exchange of Information

#### *Summary*

The proposed article 26 (proposed 2007) of the United Nations Model Tax Convention between Developed and Developing Countries was developed by the Subcommittee on Exchange of Information. The proposed commentary discussed the confidentiality requirements and the exceptions that a Contracting State may apply to the exchange of information.

The proposed commentary on paragraphs 1-3 and the inventory of exchange of information are contained in E/C.18/2007/11.

\* The present note has not yet been acted upon by the full Subcommittee. All comments received from members of the Subcommittee are reflected in the document. The views and opinions expressed are those of the authors and do not necessarily represent those of the United Nations.



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\* See E/C.18/2007/11.

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## **Proposed United Nations commentary**

### **Article 26** **Exchange of information<sup>1</sup>**

#### **General considerations**

1. Article 26 embodies rules under which information may be exchanged to the widest possible extent, both to facilitate the proper application of the treaty and to assist the Contracting States in the enforcement of their domestic tax laws. Consequently, the obligation to exchange information under this article should be interpreted broadly, and the limitations on that obligation should not be extended by analogy beyond their specific meaning. In particular, the article should be understood to require the Contracting States to promote an effective exchange of information.

1.1. In a global economy, cooperation among nations on fiscal matters has become increasingly important, and the former reluctance of nations to concern themselves with the revenue laws of other countries mostly has disappeared. Article 26 provides a basis for the effective exchange of information between the Contracting States, whereas article 27 provides for assistance in collection. From the perspective of many developing countries, article 26 is particularly important not only for curtailing cross-border tax evasion and avoidance but also to curtail the capital

2. Article 26 was modified substantially in 2007 with a view to clarifying certain issues, expanding the scope of the article and limiting exceptions to the obligation to exchange information. In some cases, the changes made were not intended to be substantive but rather were intended to remove doubts as to the proper interpretation of the article. For example, the term “necessary” in paragraph 1 was changed to “may be relevant” to clarify the intended meaning of the prior language. In contrast, the change in that paragraph providing for an exchange of information with respect to taxes not mentioned in article 2 was intended to be a substantive change.

2.1. In some cases, the issue of whether a change made to article 26 is intended as substantive or interpretative depends on the prior practices of the Contracting States. For example, in some cases, the addition of paragraph 5, which removes, inter alia, domestic bank secrecy laws as a basis for refusing to exchange domestic securities information, was intended to be a substantive change.

decline to provide the information in the specific form requested if, for instance, the requested form is not known or permitted under its law or administrative practice. A refusal to provide the information in the form requested does not affect the obligation to provide the information.

3.2. Contracting States may wish to use electronic or other communication and information technologies, including appropriate security systems, to improve the timeliness and quality of exchanges of information. Indeed, the Contracting States may be obligated to provide requested information in electronic form if such action is necessary for an effective exchange of information. Contracting States which are required, according to their law, to observe data protection laws, may wish to



tax (VAT). To accomplish that outcome, the following language might be substituted for paragraph 1:

“1. The competent authorities of the Contracting States shall exchange such information as may be relevant for carrying out the provisions of this Convention or for the administration or enforcement of the domestic laws of the Contracting States *concerning taxes covered by the Convention and [insert specific taxes] of a Contracting State*, in so far as the taxation thereunder is not contrary to the Convention.”

6.2. The obligation to provide requested information applies whether or not the person, with respect to whom the information is requested, is a resident of either Contracting State or is engaged in economic activity in either Contracting State. For example, a Contracting State may request information about the bank deposits of an individual who is resident in some third State.

7. The obligation imposed under paragraph 1 is for an *effective* exchange of information. A Contracting State may not avoid its obligations under paragraph 1 through unreasonable time delays or by imposing unreasonable or burdensome procedural barriers.

8. The examples provided in paragraphs 8.1 and 8.2 below illustrate the application of paragraph 1 of the Convention in particular cases. Some of these examples are drawn from, but are not identical to, the examples provided in paragraphs 6 and 7 of the OECD commentary on article 26. In all of these examples, the requested State (the Contracting State that has been asked for information) has the obligation under paragraph 1 of the Convention to provide the requested information.

8.1. Application of the Convention (between State A and State B):

exercised for more than 183 days in State B. That State may request that State A provide it with information on the amount of the income exempted from taxation in State A in accordance with article 23 A (Exemption method for relieving double taxation).

(g) State A is attempting to impose a corporate income tax on an entity claiming to be a partnership. State A may request information from State B that would be helpful to it in properly classifying the entity for tax purposes, including information about the way the entity is classified for tax purposes by State B.

(h) State A is being asked to provide to one of its residents a tax credit under article 23 B for income taxes allegedly paid to State B. State A may request from State B information about whether the alleged payment of the tax actually occurred.

#### 8.2. Implementation of domestic laws:

(a) A company in State A supplies goods to an independent company in State B. State A wishes to know from State B what price the company in State B paid for the goods supplied, with a view to a correct application of the provisions of its domestic value-added tax.

(b) A company in State A sells goods through a company in State C (possibly a low-tax country) to a company in State B. The companies may or may not be associated. There is no convention between State A and State C, nor between State B and State C. Under the Convention between State A and State B, State A, with a view to ensuring the correct application of the provisions of its domestic laws to the profits made by the company situated in its territory, asks State B what price the company in State B paid for the goods.

(c) State A, for the purpose of taxing a company situated in its territory, asks State B, under the convention between A and B, for information about the prices charged by a company in State B, or a group of companies in State B with which the company in State A has no business contacts in order to enable State A to check the prices charged by the company in that State by direct comparison (e.g., prices charged by a company or a group of companies in a dominant position).

(d) A resident of State A holds a bank account in State B and the income from that account is exempt from tax under the domestic laws of State B. State A may request that State B provide information on the amount of interest income earned on that account.

(e) A financial intermediary invests money of its account holders in State A, earning therein dividends and interest. State A requires that the financial intermediary keep records of the beneficial owners of the accounts but does not routinely request those records in enforcing its domestic laws. State B suspects that some of the beneficiaries of the account holders of the financial intermediary are its residents and are properly taxable under its domestic laws. State B may request that State A obtain for it the information about the account holders from the financial intermediary.

(f) A corporation resident in State A has affiliated companies located in State B and State C. State B believes that the affiliated company doing business in its territory has been skimming profits into the affiliated company located in State C. State B may request that State A provide it with information about the profits and expenses of the affiliated company located in State C.



**Paragraph 2**  
**Obligation to confidentiality**

9. A Contracting State cannot be expected to provide confidential financial information to another Contracting State unless it has confidence that the information will not be disclosed to unauthorized persons. To provide the assurance of secrecy required for effective information exchange, paragraph 2 provides that information communicated under the provisions of the convention shall be treated as secret in the receiving State in the same manner as information obtained under the domestic laws of that State. Sanctions for the violation of such secrecy in that State will be governed by the administrative and penal laws of that State.

10. Of course, the information received under article 26 would be useless to the requesting State (the Contracting State requesting the information) if the prohibition against disclosure were absolute. Paragraph 2 provides that information received under article 26 can be disclosed to persons and authorities involved in the assessment or collection of, the enforcement or prosecution in respect of, or the determination of appeals in relation to the taxes mentioned in paragraph 1. In addition, it is understood that the information may also be communicated to the taxpayer, his proxy, or to witnesses in a civil or criminal proceeding.

10.1. As stated in paragraph 10, the information obtained can be communicated to the persons and authorities mentioned and on the basis of the last sentence of paragraph 2 of the article can be disclosed by them in court sessions held in public or in decisions which reveal the name of the taxpayer. Once information is used in public court proceedings or in court decisions and thus rendered public, it is clear that from that moment such information can be quoted from the court files or decisions fcan be lereedisucs,17(he)equesti5la btparh 1.cle that frosene741( of5)r, his pd1e couroT4(2be qu)-

11.3. Contracting States wishing to broaden the purposes for which they may use information exchanged under this article may do so by adding the following text to the end of paragraph 2:

“Notwithstanding the foregoing, information received by a Contracting State may be used for other purposes when such information may be used for such other purposes under the laws of both States and the competent authority of the supplying State authorises such use.”

12. The OECD Model Convention, as amended in 2005, includes a provision that would allow the sharing of information obtained under article 26 with persons charged with the oversight of the persons allowed to obtain such information. That provision is not included in paragraph 2, due to opposition from some members of the Committee from developing countries, who feared that the oversight bodies, which typically are political entities, would not be subject under domestic law to the same strict rules of confidentiality as tax officials.

12.1. Excluding oversight bodies from the persons entitled to receive confidential information obtained through information exchange presents problems in some countries because their oversight bodies typically expect to have access to such information in order to fulfil their oversight duties. Contracting States wishing to address this issue without providing a blanket authorization for oversight bodies to receive confidential information might add the following language to the end of paragraph 2 of article 26:

“In appropriate cases, the competent authorities may agree to allow the sharing of information received under paragraph 1 with an oversight body if that information is necessary for the oversight body to fulfil its oversight duties. In such cases, members of the oversight body must be subject to confidentiality requirements at least as strict as those applicable to tax administration and enforcement officials.”

12.2. Countries wishing to adopt the position taken in the OECD Model Convention with respect to the sharing of information obtained under paragraph 1 with oversight bodies may modify paragraph 2 as follows (the changed language shown in italics):

“2. Any information received under paragraph 1 by a Contracting State shall be treated as secret in the same manner as information obtained under the domestic laws of that State. However, if the information is originally regarded as secret in the transmitting State, it shall be disclosed only to persons or authorities (including courts and administrative bodies) concerned with the assessment or collection of, the enforcement or prosecution in respect of, or the determination of appeals in relation to, the taxes referred to in paragraph 1, *or the oversight of the above*. Such persons or authorities shall use the information only for such purposes. They may disclose the information in public court proceedings or in judicial decisions.”

12.3. If paragraph 2 is amended to authorize information to be disclosed to oversight bodies, that disclosure should be limited to information necessary for those bodies to fulfil their oversight duties. Such oversight bodies include authorities that supervise tax administration and enforcement authorities as part of the general administration of the Government of a Contracting State. Such sharing is permitted only if the persons engaged in oversight activities are subject to confidentiality requirements at least as strict as those applicable to tax administration and

enforcement officials. The competent authorities shall agree as to the bodies that constitute an oversight body within the meaning of this paragraph.

**Paragraph 3**

**Limitations on obligation to exchange information**

13. Paragraph 3 of article 26 contains provisions that limit the obligation of the requested State under paragraph 1. The limitations provided in paragraph 3,



permitted under its own administrative practices to seize documents in the possession of a taxpayer without court authorization may refuse to seize such documents on behalf of a requesting State if the requesting State would be precluded by law from making such a seizure itself without court authorization. The purpose of this rule is to prevent a requesting State from using the administrative measures of the requested State to avoid limitations imposed on the requesting State by its own Government.

16.1. Different countries will necessarily have different mechanisms for obtaining and providing information. Variations in laws and administrative practice may not be used as a basis for the requested State to deny a request for information unless the effect of these variations would be to limit in a significant way the requesting State's legal authority to obtain and provide the information if the requesting State itself received a legitimate request from the requested State.

16.2. The general rule of paragraph 16 has no application when the legal system or administrative practice of only one country provides for a specific procedure. For instance, a Contracting State requested to provide information about an administrative ruling or advance pricing agreement (APA) it has granted cannot point to the absence of a ruling or APA regime in the requesting State to avoid its obligation under paragraph 1 to provide such information.

17. Most countries recognize under their domestic laws that information cannot be obtained from a person to the extent that such person can claim the privilege against self-incrimination. A requested State, therefore, may decline to provide information if its self-incrimination rules preclude it from obtaining that information or if the self-incrimination rules of the requesting State would preclude it from obtaining such information under similar circumstances. In practice, however, the privilege

18.2. Unless otherwise agreed to by the Contracting States, it can be assumed that the information requested by a Contracting State could be obtained by that State in a similar situation unless that State has informed the other Contracting State to the contrary.

18.3. It is often anticipated, when a Convention is entered into between a developed country and a developing country, that the developed country will have a greater administrative capacity than the developing country. Such a difference in administrative capacity does not provide a basis under subparagraph 3 (b) for either Contracting State to avoid an obligation to supply information under paragraph in

law to confidential communications may differ among States, the protection provided under subparagraph 3 (b) does not extend so broadly so as to hamper the effective exchange of information.

19.2. Notwithstanding the provisions of domestic law in the requested State, that State may decline to supply requested communications between attorneys, solicitors or other admitted legal representatives and their clients only if, and to the extent that, such representatives act in their capacity as attorneys, solicitors or other admitted legal representatives and not in a different capacity, such as nominee shareholders, trustees, settlors, company directors or accountants, or under a power of attorney to represent a company in its business affairs. More specifically, the communication must have been produced in good faith for the purpose of seeking or providing legal advice or for use in existing or contemplated legal proceedings.

19.3. In no event may a requested State decline to disclose communications between attorneys, solicitors or other admitted legal representatives and their clients if those persons have themselves participated with their clients in a plan to commit tax evasion or fraud.

19.4. A claim that information is protected as a confidential communication between an attorney, solicitor or other admitted legal representative and its client should be adjudicated exclusively in the Contracting State under the laws of which the claim arises. Thus, it is not intended that the courts of the requested State should adjudicate claims based on the laws of the requesting State.

20. Subparagraph 3 (c) permits a requested State to decline to provide information if the disclosure of that information would reveal any trade, business, industrial, commercial or professional secret or trade process.

