

RiR 2010:24

Sweden's tax treaties with other countries – effects of the government's work

Summary

The Swedish National Audit Office has audited the government's work in negotiating tax treaties with other countries.

Fact Box

More about tax treaties: When two states tax the same taxpayer for one and the same income, and the final tax thereby exceeds the tax levied in the state with the higher tax level, a case of international double taxation can be said to have occurred. Such double taxation may be mitigated or undone by means of unilateral measures, e.g. provisions on deducting foreign tax. International double taxation may also be avoided by means of tax treaties. A tax treaty is an agreement under international law entered into by Sweden and another state (or jurisdiction) in which the parties mutually waive their tax claims. Avoiding double taxation by means of a treaty is usually more effective than just applying internal rules.

Why tax treaties are important for Sweden: The principal aims of tax treaties are to

- undo or mitigate the effects of international double taxation
- encourage investments between the treaty states and create the best possible competition conditions for the Swedish export industry
- prevent international tax evasion.

Background to the audit

Grounds: Sweden has historically been very active in the tax treaty area and is known to have an extensive and competitive tax treaty network. A preliminary study to this audit indicated that the rate of agreements, i.e. the number of new and renegotiated tax treaties, had dropped in recent years. This could mean that there is a risk that the government's objective for a modern and updated tax treaty network is not being fulfilled.

Purpose: This audit examines the effects of the government's tax treaty work by analysing a number of problems in the Swedish tax treaty network. The audit also analyses the causes behind these problems by describing the tax treaty process and the priorities behind the government's work. The purpose is to investigate whether the government's objective for the tax treaty policy can be regarded as fulfilled.

Implementation: The audit has been carried out by means of interviews with the Ministry of Finance and the Swedish Tax Agency to clarify what priorities and assumptions have been the basis of Sweden's negotiations in recent years. To investigate the competitiveness of the Swedish tax treaty network, a comparative study has been carried out in which certain tax treaty articles that are central to Swedish companies have been compared to the corresponding articles in a number of competing countries. Interviews with the finance ministries of Finland and the Netherlands were held in order to determine what priorities govern negotiations there. A seminar on problems in the Swedish tax treaty network was held with representatives from the Ministry of Finance, the parliamentary committee on taxation, the Swedish Tax Agency, the Confederation of Swedish Enterprise, Uppsala University, accountancy firms and Swedish corporations.

Results of the audit

The audit has resulted in the following central observations and conclusions:

The treaty rate is dropping: Over the last ten years the treaty rate, measured by the number of new or renegotiated tax treaties, has decreased gradually along with pre-negotiation work. According to the Ministry of Finance, competition issues have been given a lower priority

in the tax treaty context since the end of the 1990s. Since 2004 no new, complete tax treaty has been signed. This downward trend in regular tax treaty work can partly be explained by the government's efforts to improve transparency and information exchange in the tax area. The Ministry of Finance has emphasised that tax treaty work takes a long time to learn. An extended period of inactivity can thus lead to a lowering of the competence to negotiate new tax treaties. This in turn means that once the decision is made to increase efforts again, the start-up period may be long.

Shifting focus towards information exchange: Within the framework of a joint Nordic project, Sweden has since 2007 signed many new information exchange agreements with what are known as tax havens. According to the Ministry of Finance, the work with signing new information exchange agreements has shifted the focus and resources away from competition issues and the efforts to renegotiate and enter into new tax treaties. However, the information exchange agreements cannot explain the entire reduction in tax treaty efforts as a whole, as this reduction began long before the work on information exchange agreements was initiated. Furthermore, since 2009 it has been possible to handle tax information agreements largely through correspondence and by telephone. This has meant that Sweden has been able to save time and resources, as it has participated with two representatives at most of the negotiations with the first group of tax havens.

The Finnish finance ministry instead underlines that it has been able to continue giving priority to the competition aspects of tax treaty efforts thanks to the fact that the Nordic cooperation project has helped with the information exchange agreements.

Important information exchange agreements have not yet been updated: According to the Swedish Tax Agency, Sweden has more foreign transactions than the other Nordic countries, and Switzerland is the country with the incomparably largest amount of Swedish funds in secret bank accounts. Updated information exchange articles in Sweden's tax treaties, not least with Switzerland, are thus important. Despite the fact that the government has prioritised information exchange over other tax treaty efforts, and despite the fact that negotiations carried out within the Nordic project take less time, Sweden has still not updated the information exchange clauses in the tax treaties with Switzerland, Singapore and Belgium – treaties that are not part of the Nordic cooperation project. Denmark, Finland and Norway, however, have renegotiated their tax treaties with the above-mentioned countries.

Old tax treaties can be abused in tax avoidance schemes: The Swedish Tax Agency's analyses for 2006 showed that Sweden's tax treaty with Austria generated revenue shortfalls in the billions. The tax treaty with Austria has been renegotiated, but similar problems remain in relation to a number of other countries. An alternative or complement to renegotiating old tax treaties is to review the possibility of introducing general rules to prevent these tax avoidance schemes, which has been suggested by the Tax Agency. The government promised in 2007 to come back to the issue, but as yet no such review has been initiated.

Risk of a lowering of the competitiveness of Sweden's tax treaty network: A comparative analysis of the level of tax at source in Swedish tax treaties and those of a number of competing countries shows that Sweden has worse terms than many of the competing countries in individual treaties. A comparison between Sweden's terms today and in 1995 furthermore shows that there are more countries in the study with better terms than Sweden today, than there were fifteen years ago. Part of this change can be explained by the fact that several of the competing countries have "caught up with" Sweden, but SNAO also notes that in several cases it is a question of other countries having got better terms than Sweden in renegotiations during recent years. The indication of a relative deterioration of the Swedish treaty network is confirmed in a comparative analysis of the Swedish tax treaty network carried out in the autumn of 2010 by the Confederation of Swedish Enterprise.

One particularly criticised treaty has not been evaluated: The power to tax the employment income of cross-border commuters between Sweden and Denmark is regulated in the Nordic multilateral double taxation treaty. A bilateral protocol to the Nordic multilateral treaty between Sweden and Denmark from 2003 contains a *compensation system* that regulates how Denmark and Sweden are to be compensated for uncollected taxes from cross-border workers. This protocol has been criticised in the Riksdag (the Swedish parliament) and elsewhere both for its formulation and its application. A common theme in all the criticism is the perception that the compensation system creates an imbalance in the distribution of taxes from the cross-border commuters between Denmark and Sweden, to Sweden's disadvantage. Despite the extensive criticism of the bilateral protocol, the government has not produced relevant documentation in order to be able to analyse the outcome of the protocol, something the protocol furthermore stipulates. At the time of writing the government still does not have access to such documentation. The lack of a proper analysis of the effects of the bilateral protocol between Denmark

and Sweden has also led to the government providing incorrect information to the Riksdag.

Summary conclusion: The government's priorities in the tax treaty area have led to clear risks that the Swedish tax treaty network will lose competitiveness. Moreover, known tax leakage problems remain. Despite the government's making information exchange a priority, Sweden does not have, at the time of writing, updated information exchange agreements with important tax havens. Furthermore the government has been satisfied, despite extensive criticism, with incomplete documentation of the effect of the compensation system between Sweden and Denmark.

SNAO's recommendations

Recommendations to the government:

- The government should clarify its strategy in the tax treaty area and account for how it works to achieve its goals. If the goals of the tax treaties remain, the focus on competition issues must increase in order to avoid a worsening of the competition situation for Swedish companies.
- The government should consider continuing with Nordic cooperation in order to liberate resources for other tax treaty work.
- The government should urgently produce documentation for an evaluation of the Swedish-Danish compensation system.