

**TAX HAVENS:
POLITICS, MARKET AND DEMOCRACY***

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Abstract: Through analysis of a distant reality for many, this work is part of an effort to understand the dynamics of tax havens in the current system, seeking to show the reality of a major social phenomenon that promotes inefficiency and imbalance in the economy through structures of highly-organized and specialized in the removal of capital. These structures, built and maintain a complex infrastructure that extraterritorial acts as an interface to a parallel global economy by facilitating and encouraging the flight to territorial regulations, promoting large-scale relocation of capital from poor countries to rich, contributing significantly to increasing inequality, distorting global markets to the detriment of innovation and entrepreneurship, diverting investment and slowing down of economic growth, endangering the integrity of tax systems and respect for the rule of law. Its secrecy allows, on the other hand, complex schemes of money laundering originating from drug trafficking, weapons and corruption. This new geo-economic requires rethinking the nature and geography of corruption, forcing the society to address the major flaws of the international financial architecture and to overcome the political power of large vested interests, thinking of a new form of globalization.

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explore readings on the most recent research done by experts and allow a review of bibliography.

In the last part of this work we critically and synthetically analyze the approach undertaken, stressing strong and weak points of the work done and focusing our attention on the present frame of international financial system, leaving possibilities open for future explorations.

2. TAX HAVENS: CONCEPTS

2.1. Conceptual Framework

At the source of Tax Havens one can find behaviours of resistance to taxation, which go back to early civilizations and assumes forms as varied as human imagination allows¹.

The term Tax Haven evokes a heavenly island with sun and palm trees, located at the tip of the world and where some multimillionaires get rich while sleeping. This first picture can be deceiving and harmful, for the capital that is forwarded to Tax Havens is growing in importance². According to the Bank for International Settlements (BIS), about half of international financial flows pass through these places³, whereas its origin is more and more diverse and consequences appear dramatic from many standpoints.

The History of Tax Havens is neither continuous nor linear, but built on ruptures and mutations according to the place and time. It met a great development during two important moments of economic globalization: first in the 19th Century, with the deepening of capitalism, and second in the post-war 20th Century, in the fifties, with the creation of the eurodollar market⁴. It was over the last thirty years, however, that its amount and importance grew exponentially, due to liberalization and deregulation of the

¹ Plate-Forme Paradis Fiscaux et Judiciaires; 2007; *Paradis Fiscaux et Judiciaires Cessons le scandale*; Secours catholique – Caritas Cœur.

² Júlio Mota *et Al*; *Paraísos Fiscais: Mercadorização Onshore e Offshore*; DOC TAGV/FEUC; 2009; p.7.

³ Bank for International Settlements (BIS), in <http://www.bis.org/>, consulted at Feb 2010.

⁴ Ronen Palan *et Al*; *Les Paradis Fiscaux*; La Découverte; 2007; p.28.

financial sphere and all the other markets, which took place from the early 80s with the rise of Reagan and Thatcher to power.

The eurodollar market appears in a time when the monetary market is no longer under North American ruling. It has spread in the meantime and now is called euromarket, the market where foreign currency negotiations are held. Its use presupposes, through an international security, a non-native currency where it is commercialized, rated according to the currency in which it is issued and, usually, to the bearer and tax free withheld tax. These securities can be negotiated worldwide and London is a major center. Its commercialization is done through a compensation system, being Euroclear and Clearstream the most common.

Since Tax Havens arise much controversy, international institutions use several definitions when approaching the subject. Although they possess many common features, there is no general agreement on the prevailing definition. This difficulty is shown by the variety of names attributed to the phenomenon: Tax Haven, Offshore Financial Center, Free Trade Zone, Tax Relief Zone, among other denominations.

Currently, these territories are characterized by enormously easy allocation of allowances for the opening of companies with unknown origins, therefore protecting the owner's identity by guaranteeing absolute secrecy. An offshore financial center is an international financial center where operations that somewhat evade the control by national and international public policies are carried out, and that is what makes it so special.

In short, one can assume there are three fundamental behaviours attached to the existence of a Tax Haven: tax planning, avoidance and evasion. Tax planning is a way to minimize tax costs and can go from the most primitive means to the most sophisticated techniques, allowing for the taxpayer to refrain from paying taxes. The line between tax avoidance and tax evasion lies in the legal or illegal form that covers capital flux. It is considered avoidance when tax relief is achieved through legal means, and evasion if obtained illegally by procedures punishable by law.

In fact, one has to conclude that the concept of Tax Haven depends on the perspective of the object being studied. On one hand, the users' community, their beneficiaries, talks about Tax Havens as a space for tax optimization. On the other hand, the non-user community and some international institutions do not see them that way, but instead as a space where democracy and market rules are subtracted.

Due to the fact that there is no official definition, researchers point out some criteria to recognize a Tax Haven, some of which will be underlined.

According to Christian Chavagneux and Ronen Palan (2007:11), experts in offshore finance, there are ten criteria:

1. Low or absent taxation for non-residents;
2. Bank secrecy;
3. Professional secrecy;
4. Simple registration procedures;
5. Full freedom of international capital movements;
6. Fast implementation;
7. Support from a big financial group;
8. Economic and political stability;
9. Good brand image;
10. A panoply of bilateral agreements so as to avoid double taxation.

In 1998, the Organization for Economic Co-operation and Development (OECD) established four key-factors for the recognition of Tax Havens:

1. Absence or reduced income tax;
2. Weak effective exchange of information;
3. Lack of transparency;
4. Non existence of material activity.

The question arose in the OECD in the nineties, at a time when the probability to obtain revenues diminished in face of the rise in costs.

The International Monetary Fund (IMF) calls them offshore financial centers and points three criteria for recognizing them:

1. Jurisdictions that have a large number of financial institutions committed mainly to businesses with non-residents;
2. Financial systems with foreign assets and liabilities;
3. Centers that supply with services such as low or zero taxation, moderate financial regulation and bank secrecy.

The choice of a Tax Haven depends on the level of specialization of its own opacities, something that highlights its usefulness for the using entity with which it identifies.

2.2. Main Mechanisms and Entities

Understanding how Tax Havens function requires explaining some of the aspects connected with the usual mechanisms and the entities involved.

The main mechanisms in the use of Tax Havens are summed up by the following features:

- **Manipulation of transfer prices** – it consists in manipulating prices that are practised during transactions between juridical distinct entities that may or may not be part of the same group, through over or under-invoicing of those transactions, with the intention of transferring capital gains to spaces with a favourable taxation;
- **Use of conventions for tax relief** – consisting in transporting income by entities that are seated in jurisdictions signatory of conventions that establish non-taxation or moderate taxation on certain types of income;
- **Form mismatch to substance** – consists in the juridical enforcement of an activity that is material enforced outside that territory, and the income from such activity are transferred as loans and commissions.

As for the involved entities, large international companies are among the biggest users. Their goal is to optimize the tax burden, minimizing the amount of tax to be paid. They use every possibility offered by the same jurisdictions by so doing. One could highlight large banks, multinationals and all activities related to exploring natural resources on a non-transparent way. Due to its opacity, Tax Havens are also a base for secret services. Neo-colonial regimes as well, patronized by Western policies, are big users. International mafias and weapon dealers actually depend on offshore centers, for it is through this option that they manage to launder revenues from illicit activities. All these activities permanently interact with Tax Havens through traders, brokers and dealers.

3. TAX HAVENS: POLITICS, MARKET AND DEMOCRACY

With the basic concepts necessary to the exploring of the thematic of Tax Havens gathered, we move now to the core of this work, where we will try to find a stable answer to the starting question, that is the characterization of Tax Havens, for they reveal incoherencies of the systems where they are located, whenever it supports the existence of these specific jurisdictions.

In fact, the capitalist system has grown to become global, rooted in principles like competition mechanisms and market transparency. In this frame, it is ever more incoherent to permit those completely opaque national spaces and associated juridical structures exist and bias the principles they supposedly stand for with globalization. One can assume to question, factually, a globalization that sets foot in a reasoning that perverts competition, in what comes to producing assets and services, which tax competition entails. It is not acceptable the fact that for so long and until very recently even large International Institutions have borrowed Milton Friedman's words: "Competition between national governments in the public services they offer and the

taxes they impose is as productive as competition between individuals or companies in the products and services that they want to sell by the prices they want to make.”⁵

This incoherence produces another one, not less relevant: the system's articulation between the political, that is the democratic, and the market level, the one that expresses the economic freedom by the agents. Destabilizing mechanisms are thus created at the social level, due to the asymmetries created, in which the social basis for taxation is biased, releasing itself or letting the vectors for more wealth potential.

The system's incoherencies are revealed in the raw by the following facts:

1. Capitals generated by productive economies don't meet its development;
2. Wealth-generating economies are being drained of capital;
3. Tax Havens exist because of legislation that concedes tax benefits for the economic development, but that is not what really happens;
4. Tax Havens accumulate capital and have no productive structure.

Dramatic consequences derive from the flight of capital to those juridical structures, and those are felt in several levels, such as: loss of tax revenues; market distortion; tax equity and efficiency principles distortion; adverse effects in the balance of payments; money laundering; perversion of the economic system, promoting speculative bubble and potentially causing economic crises.

3.1. The consequences

3.1.1. *Loss in Tax Revenues*

⁵ *apud* John Christensen, *The Engines of Chaos: Secrecy Jurisdictions and Global Crisis*, Tax Justice Network, 2009, p.17.

It is the most visible direct consequence, either for the States, which are cut of tax revenues due to the fact that resident citizens escape significant amounts of taxes through the use of Tax Havens (revenues that would be useful for the functioning of companies and public services), or for the very Tax Havens, which may fall into losses in tax revenues if fees are applied in a generalized and non-circumscribed manner. It was precisely this fact that made OECD raise the problem and it was from then on that the Financial Action Task Force (FATF) came up, something we will deal with later.

It is difficult to assess such losses, since the use of offshore centers is done mostly by camouflage. Nonetheless, due to a growing evasion the USA has been making official assessments of such use and of the loss in tax revenue involved. In 2006, the Permanent Investigation Subcommittee of the US Senate, presided by Carl Levin, took to the Senate the abuses committed by the offshore industry, unmasking some of the biggest frauds, such as the Anderson Affair⁶.

3.1.2. *Market Distortion*

The different degrees e possibilities for the use of Tax Havens, deregulation, tax secrecy and incentives distort the trade system in favour of each user's interests and additionally attract capital from emergent nations and even more seriously from developing nations, thus disrupting other possible ways for economic development.

Based on data by the Bank for International Settlements (BIS), Palan (2006) shows the disparity between the high amounts of foreign assets in Cayman and the Bahamas compared to other international financial centers such as the US, Belgium and the Netherlands. The former reveal a considerable offshore activity. In fact, when one observes a country such as the Cayman Islands, for instance, you face an empty shell. There is no production. With a population of about 50,000 inhabitants, it has more than 270 banks⁷, whose product represents about 30% of the GDP⁸.

⁶ Norm Coleman, Carl Levin; *Tax Haven Abuses: The Enablers, The Tools and Secrecy – ANDERSON CASE HISTORY: HIDING OFFSHORE OWNERSHIP*; UNITED STATES SENATE, Permanent Subcommittee on Investigations; 2006; p.49.

⁷ Cayman Islands businesses directory and island company information guide, *in* <http://www.ecayman.com/fin/banks.html>, consulted at Feb 2010.

Levin (2006), at the US Senate, states that opaque jurisdictions are beginning to undermine national sovereignty and the democratic ways to govern, once they allow creating an asymmetric offer of legal and economic information, which affects the efficiency of global markets⁹.

3.1.3. *Distortion of the Tax Equity and Efficiency Principles*

Another consequence felt in a market desirably free and perfect is the distortion of the tax equity and efficiency.

Equity is no longer existent for equal or even higher income levels of residents within the same State are diversely taxed.

Efficiency is also affected because the choices on the places for investing depend on tax reasons.

3.1.4. *Adverse Effects in the Balances of Payments*

Adverse effects are noticeable in the Balances of Payments due essentially to three factors:

- Capital transfers from normal taxation states to Tax Havens;
- Return of the investments set on Tax Havens usually does not revert to the State of resident of the head office;
- The use of some specific mechanism, such as the manipulation of transfer prices by the artificial invoicing of inter-company transactions, has the effect of debilitating the Balance of Payments in States with normal taxation.

⁸Cayman Islands Government, *in* http://www.gov.ky/portal/page?_pageid=1142,1&_dad=portal&_schema=PORTAL, consulted at Feb 2010.

⁹ Carl Levin *et Al*; *Tax Haven Abuses: The Enablers, The Tools and Secrecy – ANDERSON CASE HISTORY: HIDING OFFSHORE OWNERSHIP*; UNITED STATES SENATE, Permanent Subcommittee on Investigations; 2006; p.1 and following.

3.1.5. *Money Laundering*

Trade and bank secrecy, along with the absence of restrictions in transfers, enables money laundering. According to John Christensen, from the International Secretariat of Tax Justice Network, annually about a trillion dollars is put in accounts at Tax Havens coming from illicit activity. Nearly half that amount comes from developing countries. Despite the numerous anti-laundering initiatives, the failure rate of such initiatives is very high. According to Bernard Bouzon from ATTAC (Faculty of Economy of the University of Coimbra, March 2009), Tax Havens were questioned mostly because of the easiness for the establishment and development of screen societies within these spaces, as well as a judicial protection that enables money laundering that comes from financial crime.

3.1.6. *Perversion of the Economic System*

Finally, one of the most relevant consequences of the existence of Tax Havens consists in the fact that, due to their opacity, they pervert the whole of the economic system, creating harsh and unbearable tax asymmetries and being one of the catalysts of speculative bubbles and thus bringing the risk of stimulating economic crises. Opaque jurisdictions contribute to the creation of an extreme concentration of wealth, which may cause economic instability and long recessions.

Evasion corrodes tax systems in modern States and the capacity of the State to make the services demanded by citizenship available. Furthermore, it represents the highest form of corruption, for it deprives society of legitimate public resources. Over the last 50 years, through the use of the mechanisms that characterize Tax Havens, a parallel global economy has been built to escape taxes and territorial regulations. Such economy is sustained by an infrastructure of banks, jurists, accountants, small legislative assemblies, small judicial systems and associated financial intermediaries, who join together to function as an extraterritorial interface between licit and illicit economies. This structure has stimulated and facilitated the flight of capital from

poorer to richer countries on a large scale. It has also enabled the displacement of tax burden from capital to work, significantly adding up to inequality.

This form of jurisdiction has been degrading tax systems and reduced the respect by the State's Rule of Law. Secret businesses and special treatments weaken democracy itself. Global markets are distorted and innovation and entrepreneurship are harmed, with the rhythm in economic growth being diminished by the promotion of compensations without effort and diverting investments. That is one of the main causes for the growth in corruption, which functions through the conspiracy of financial intermediaries in the private sector and the governments of States that shelter the activities of Tax Havens.

3.2. Economic Manipulation

The great advantage for companies in negotiating through subsidiaries established in these locations is the use of what technicians in international law call transfer prices, above described as the price in transactions between distinct juridical entities, integrated or not in the same economic unit. The manipulation of this price with artificial under or over invoicing of transactions gives highly attractive net profit margins.

For instance, if a company in the US wishes to acquire a product made in France and does it through an affiliate at the Cayman Islands the low cost by which the buy is done to the French producer enables it to obtain extra profits, inasmuch it will be its affiliate of the Cayman Islands that will do the selling to the US, with a trade margin that benefits from being under taxed. The affiliate buys at low cost and sells at high price, making the company with an affiliate in Cayman to obtain enormous profits, whereas the French affiliate, the producer, has no profit. Profits are allocated to the subsidiary, the unit in these groups to which taxation is reduced. That is what is appealing to multinationals and that is what motivates them in using Tax Havens.

Nonetheless, a study conducted by Boyrie, Pak and Zdanowicz¹⁰, New Mexico State University, Penn State University and Florida International University

¹⁰ Maria E.Boyrie; Simon J.Pak; John S.Zdanowicz; *Money Laundering and Income Tax Evasion: The Determination of Optimal Audits and Inspections to Detect Abnormal Prices in International Trade*; Paper; New Mexico State University; Penn State University; Florida International University; 2005.

respectively, shows how evident the exaggeration price manipulation can reach is, revealing a pure tax fraud.

After the events of September 11 in 2001, the United States gave priority to the problems related with the financing and support to terrorist organizations. The opacity of transactions has been, however, a major barrier for the detection of financial flows proceeding from illicit activity, for it obstructs the investigation of the activities in offshore financial centers by external authorities, making it easy for criminal activities to do money laundering and other actions, such as fraud, misappropriation of funds, theft, corruption, drug dealing, illegal weapon traffic, forgery of documents, use of privileged information, issue of counterfeit money, change in transfer price formation and tax evasion (Christensen; Hampton, 1999).

To incorporate money that comes from illicit activities into trade transactions complex schemes are conceived with the use of extraterritorial structures that disguise the profit of crime and tax evasion. According to Riches, Superintendent Detective Des Bray, from the Trade and Electronic Crime Division, in an interview with Sam Riches (2007), money laundering methods vary from the simplest to highly structured complex trade scenarios. Criminal insiders in legitimate deals are beginning to become more and more investigated. None of them could perform such activities if lawyers did not assist them, as well as consulting firms and financial assessors that consciously help them launder and hide assets¹¹.

Estimates from the Hedge Fund Reserach (HFR) confirm a huge difference between the amounts that go into offshore centers and those that proceed onshore. Visibly, offshore centers collect about the double of the onshore market amounts¹².

The GDP vs. International Banking Activity relation indicator, reflected in GDP multiples, data from the HFR, reveals that these financial centers are used as offshore warehouses given the high number of those multiples, compared to the GDP in each of those regions¹³.

¹¹ *apud* John Christensen, *The Engines of Chaos: Secrecy Jurisdictions and Global Crisis*, Tax Justice Network, 2009, p.9 – Detective Superintendent Des Bray, of the Commercial and Electronic Crime Branch, interviewed in the Adelaide Advertiser, Lawyers helping to launder money, 4 June 2007.

¹² *vide* figure 1 *in* Attachment.

¹³ *vide* figure 2 *in* Attachment.

The steep rise of profits from North American companies in Ireland between 1999 and 2002, achieved through low average rates of income tax to non-residents, besides distorting competition, has perverted the system, what was later confirmed with the collapse of the Irish economy, corroborating the theory of economic manipulation.

Contrary to the dream-like pictures that the term offshore brings to mind, it would be a mistake to think of it as something detached from the larger States. Geographically, many Tax Havens are located in small islands spread through the spectre of time zones. But, politically and economically, the majority is intimately united to OECD's frontline States and the term is nothing more than a political statement on a country's relationship with its territory parts (Palan, 1999). If one consider the case of London, such structures operate in British overseas territories, dependent on the British Crown.

Links between money laundering, corruption, financial markets' instability, income inequality and growing poverty, and offshore jurisdictions are beginning to be identified as the common denominator to all these problems.

3.3. The City

The United Kingdom itself is a Tax Haven, for starters because one of the tax principles it follows is having separate tax legislations for nationals and non-residents, that is, those who have their tax domicile elsewhere. These represent a great share of income that is not taxed, to what experts call *loophole*.

London is, in fact, a Tax Haven, for at the end of the 50s, 1957 to be more exact, the Bank of England supported the creation of an innovative financial instrument, the so-called eurodollar market¹⁴. The eurodollar is a currency, in the case the dollar, that is deposited and/or loaned in a bank outside its national territory. This market emerged following the Bank of England's realization that the pound sterling had lost its status as international currency for the dollar. The dollar was becoming a very important international currency. At the time, they began allowing deposits and loans in dollars outside the public scrutiny, something that strongly impelled financial liberalization and

¹⁴ Ronen Palan *et Al*; *Les Paradis Fiscaux*; La Découverte; 2007; p.44.

offshore financing. The Bank of England agreed on the enlargement of the eurodollar market held at the City of London. And it was a winning strategy.

London is today the first financial center in the world. It was through the diversification of the services in the eurodollar markets that big companies developed the behaviour in Tax Havens applicable to the rest of the world. British financial authorities are themselves a banking system used as a Tax Haven¹⁵.

The volume of offshore transactions is controlled by the financial district of London, known as the City, although many of its financial intermediaries operate in overseas offices and under the Crown's superintendence. Such jurisdictions give the impression they operate autonomously. However, in practice they act mostly as reception centers for instructions issued by the financial center of London and by other large financial centers. The financial district of London offers maximum or total tax relief and is guarded by financial secrecy norms, including the non-disclosure of companies and trusts' beneficiaries, and it is protected by regimes even more permissive than onshore regimes, at the very City. Many Tax Havens are tied directly to the United Kingdom due to having the statute of foreign territory under the dependence of the Crown or because they are part of the British Commonwealth.

Chavagneux and Palan made calculations to try to measure the position of financial operations in international banks and confirmed that about half of the international financial operations in banks is done through offshore centers and, proportionately, that half is divided into 40% in London, 30% in other large financial centers in developed countries and 30% in exotic islands.

The financial market for such financial operations, with its commissions, represents today an important share of the UK's GDP, from 10 to 15 per cent. It employs many people and allows for the development of highly sophisticated activities. So, it is placed among the most profitable segments and with most qualified personnel. From that standpoint, it is always an advantage to any country.

3.4. Consulting Firms as a Link in the System

¹⁵ Ronen Palan *et Al*; *Les Paradis Fiscaux*; La Découverte; 2007; p.33, 34 e 35.

Consulting firms give fiscal guidance to its customers. After mergers, incorporations and the bankruptcy of Arthur Andersen currently there are four major consulting firms. These are, ordered by size: PricewaterhouseCoopers (PWC), Deloitte Touche Tohmatsu, KPMG and Ernst & Young. Each one operates in at least 139 countries. All possess offices in the main Tax Havens in the world and are deeply involved in the promotion of the activities in such spaces.

In 2003, PWC, Ernst & Young and particularly KPMG were greatly criticized for advertising the selling in the USA of what the Permanent Subcommittee of the US Senate called tax products.¹⁶ This Subcommittee found out that some of these products were illegal. It was discovered that KPMG has generated at least 180 million dollars in revenues from the sale of such schemes and that collectively the schemes sold brought losses of 85 billion dollars to the US Treasury¹⁷. Deloitte e Andersen was criticized by the Senate for the work done for Enron in the report on the companies' bankruptcy. Enron declared profits of 2,3 billion dollars between 1996 and 1999, but paid no taxes. In order to achieve that it established a network of nearly 3,500 companies, 440 of which were registered in the Cayman Islands.

KPMG was highly criticized by the American Bankruptcies Court for its role in the creation of tax saving schemes with no economical consistency in the name of WorldCom before its bankruptcy. These schemes were sketched so that the company could spare billions in taxes, through something KPMG denominated preventive management.

Evidence about the inappropriate behaviour by the consulting companies is not only common in the USA. In 2005, the European Justice Court delivered an opinion on the scheme promoted by KPMG to avoid the payment of VAT in the United Kingdom. In its sales promotional material, KPMG admitted it knew that the tax authorities in the UK would consider the scheme as unacceptable tax evasion. Despite that, it has advertised the scheme as a tax product. The court concluded that the KPMG tax scheme was an inappropriate attempt to avoid the VAT.

¹⁶ Investigations by the Permanent Subcommittee of the US Senate (2003), *The Tax Shelter Industry: the role of accountants, lawyers and financial professionals*, Washington DC, US Senate.

¹⁷ Carl Levin *et Al*; *Tax Haven Abuses: The Enablers, The Tools and Secrecy*; UNITED STATES SENATE, Permanent Subcommittee on Investigations; 2006; p.1 and follows.

3.5. G20 and the European Union

The Global Forum on Taxation (GFT), guided by the work of the OECD's Committee on Fiscal Affairs, has developed also a norm, approved by the G20 and United Nations Expert Committee on International Co-operation in Fiscal Matters, which now serves as basis for the majority of bilateral Fiscal Agreements and as a norm internationally agreed on information exchange.

The basis used in the distinction between jurisdictions that execute the norm and those that do not has passed through an objective assessment of the situation in several countries. Although not drawing a strict delimitating line in the way to measure the achieved progress, it has been using the assessment of whether a jurisdiction has signed 12 agreements for information exchange as an indicator of progress.

One should note that going from 70 to none in the black list of Tax Havens resulted only from a change in criteria, which include now bilateral agreements between the States.

Tax evasion is nowadays a problem for the European Union, and so much that the States began having revenues problems and furthermore because the Stability Pact limits fiscal instruments. Along this line, in 2005 the so-called Saving Directive was established, according which all countries in the Union are obliged to supply information on capital income from non-residents to their respective countries.

This joint decision by the EU's countries is, however, challenged by the fact that three of its members, namely Belgium, Austria and Luxemburg still adopt bank secrecy. They withhold tax, transferring most of it anonymously to the country of origin of the taxed person. Such situation is to end soon, states Laszlo Kovacs, EU's Commissioner for Fiscal Affairs, for it is predicted that this rule is transitory and ends when the other 5 Western European countries that are not members of the EU (Switzerland, Liechtenstein, San Marino, Monaco and Andorra) agree with the supplying of information about their banks' customers. Switzerland is the country where negotiations are more difficult, for it intends to negotiate individually with each country so as to save at any cost its bank secrecy, instead of agreeing on a general pact with the block.

The European policy has adopted a directive that intends to harmonize taxations within the European perimeter. However, exceptions were given to Belgium, Austria and Luxemburg so they could compete with Switzerland, for this country, in order to safeguard competition, allows competition situations that adulterate the system.

The World Bank and the IMF have developed also their own anti-corruption agendas, but none of them is significantly connected with the opacity of the offshore bank system, with the exception of the restrictive programmes that concern money laundering.

The Financial Action Task Force (FATF), formed by the Heads of State of the G7 in 1989 to lead a global anti-laundering programme, has published a report on Money Laundering Trade Transactions in June 2006, in which it has identified three main methods through which financial terrorists run those tranches, by hiding their origins and infiltrating its integration in the circuits of formal economy. Those methods are the use of the financial system, the physical movement of money and the movement of assets and services through the international trade system.

The FATF has focused its investigation on the financial system, paying less attention to flows made through physical movement of capital and disregarding movements that result from the manipulation of the international trade system. This system clearly offers a range of hazards and vulnerabilities that can be explored by criminal and terrorist organizations. It composed a text with forty recommendations and intended for introduction within the legislative framing of each country. However, this barely echoed. And it seems that the FATF has become more aware of it, for it has legitimized opaque jurisdictions that commit themselves to co-operate in the investigation of the income from drug trafficking and the funding of terrorism.

The G20 has also sent a message, at a meeting in April 2009, to non-collaborative Tax Havens and jurisdictions¹⁸ that it is essential to protect public finance from the risks that come from non-collaborative jurisdictions, making an appeal to the adhesion to international prudence norms of the *anti-money laundering and counter-terrorist financing* (AML/CFT) areas. To this goal, each country's competent bodies are suggested to conduct and reinforce the supervision aim, based on existing processes,

¹⁸ G20- Declaration on strengthening the financial system – London, 2 April 2009

namely through the *Financial Services Action Plan* (FASP)¹⁹, and adopting the international standard for information exchange, approved by the G20 in 2004²⁰, reflected in the UN's fiscal convention model. It is the IMF's duty, co-operating with the *Financial Stability Board* (FSB), to assess the implementation in the relevant juridical orders.

However, this G20 meeting, besides being weakly participated by a minority of 8 countries represented by its Finance Ministers, has not been consensual. Is this a proof of conflicting interests from the member states?

Despite all efforts, it would probably more effective than an action focused on Tax Havens to center attention on the legislative dispositions that protect them. States, in coordination, may refuse the recognition of the legality of the present statute of such entities.

The most visible measure so far came from North American President Barack Obama, which resulted from his own political will and not from co-operation, with the lifting of the bank secrecy in about 300 bank accounts in the UBS (Union of Swiss Banks).

All these small steps reflect, above all, the absence of political will, something that can go beyond a declaration of intentions. Why is that? Chavagneux and Palan believe that Tax Havens, originally and mainly sought by rich people to escape taxes, are now an essential part of the globalized economic system.

4. CONCLUSION

This assignment inscribes itself in an effort to understand a reality that is more and more present, therefore trying to comprehend the dynamics of Tax Havens in a capitalist system, trying to show the facts of one of the main phenomena that promote

¹⁹ The *Financial Services Action Plan* (FSAP) is a key-element in the EU for the attempt to create a whole market for financial services. It was created in 1999 for a previewed period of six years and contained 42 articles relating with the harmonization of the financial services market in the EU.

²⁰ O *Group of 20* (G20), created at 1999, it's a group formed for the financial ministers and chiefs of the central banks of the 19th major economies of the world plus European Union.

inefficiency and the instability of the political and liberal economic organization of a world composed of states under the Rule of Law.

These jurisdictions are today small territories with special powers and through which circulates something the IMF estimates as being half of the worldwide financial flows. Such territories are mainly characterized by the inexistence of tax burdens, allowing for capitals to escape national taxation, and by an opacity and secrecy that allow for complex money-laundering schemes with its root in corruption and weapon and drug traffics.

A series of scandals were made public and affect realms as important as political parties from developed countries or the world of sport. An enormous amount of capitals is out of the countries where it is generated control. The obscure part played by these territories was publicly denounced by publications such as the *Le Monde Diplomatique* or international organizations like the *Association pour la Taxation des Transactions pour l'Aide aux Citoyens* (ATTAC) and *Tax Justice Network* (TJN), that ever since their foundation scrutinize this reality. The money-laundering schemes that pass by these jurisdictions, coming from all over the world, are usually sophisticated. They use fictitious companies by which financial flows circulate until its source and trace are lost, ending up in a legitimate account at some acknowledged bank. However, rudimentary methods are still being used effectively, such as briefcases containing real money, hidden in private jets.

Secretly, professional structures that are highly organized and specialized in the displacement of capital to the TH built a parallel global economy to escape taxes and territorial regulations. This economy is supported by a complex infrastructure that serves as an offshore extraterritorial interface. This interface has been facilitating and stimulating the flight of capital on a large scale, thus significantly contributing to increase inequalities, distorting global markets and harming innovation and entrepreneurship, as well as diverting investments and diminishing the rhythm of economic growth, for it promotes compensation without effort, and even jeopardizes the integrity of tax systems and the respect for the Rule of Law.

In retrospect, and following Palan and Chavagneux's ending of their book *Les Paradis Fiscaux* (2007:115), “Ironically, offshore territories could only become centers for contemporary capitalism by hanging on the growing acknowledgement of the state's sovereignty principle since the beginning of the 19th Century. Then and today, the State

and the globalization of capitalism, far from sitting in opposite seats, share the same space and yet don't get along”.

The new geo-economics demands for a rethinking of the nature and geography of corruption, forcing society to face the great gaps of international financial architecture and to overcome the political power from the larger established interests, envisaging a new model for international relations.

6. ATTACHMENT

Figure 1

Estimated Amounts Going to the Offshores

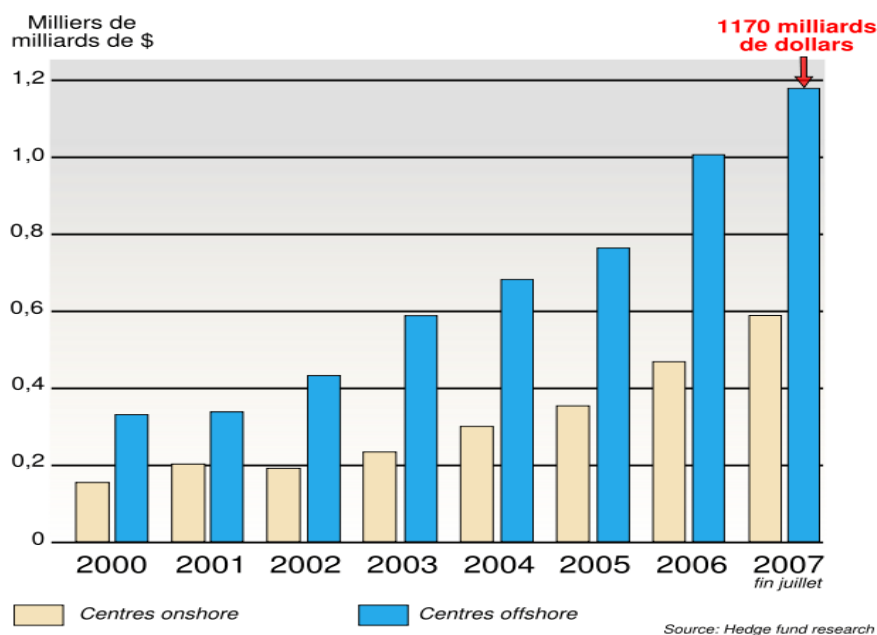


Figure 2

International Banking Activities vs. GDP

(final 2000)

	GDP (US\$ billion)	BIS	
		(US\$ billion)	GDP multiple
Cayman Islands	0,9	482	518
British Virgin Islands	0,3	25	86
Crown Dependences	4,6	234	51
Bahamas	5,6	172	31
Bermuda	2,4	32	13
Luxemburg	19,3	245	13
Singapore	85	221	2,6
Hong Kong	159	193	1,2
United Kingdom	1,442	1,508	1,05
U.S.A.	9,152	2,096	0,2

Source: BIS, World Bank, CIA & Bank of England, *apud* Palan, *The Offshore World*, 2006.

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