

MULTINATIONAL
CORPORATIONS,
TAX HAVENS
AND THE
SIGNIFICANT
OF WEALTH

AN ECONOMY
ADRIFT

Regulate Finance
for Development



WWW.CCFD-TERRESOLIDAIRE.ORG

CHAPTER 1

WHEN INDICATORS LOSE THEIR DIRECTION 6

THE FUTURE UNDER THE PALM TREES LOOKS PROMISING 8

PUTTING MONEY ON THE (OTHER) SHORE 13

ENCOURAGING COMPANY START-UPS: WHEN VICE OVERCOMES VIRTUE 14

MAXIMUM PRODUCTIVITY: TAX HAVENS = MODEL EMPLOYEES? 16

PHONEY EXCHANGES - DUBIOUS DATA OF INTERNATIONAL TRADE 18

AND THE LEADER IS... 20

CHAPTER 2

MULTINATIONAL COMPANIES SETTling THEIR ACCOUNTS 22

MULTINATIONAL COMPANIES AND TAX HAVENS - SILENCE IS GOLDEN 24

DISCONNECTING STRATEGIES 31

LEGAL MENTIONS

PRODUCTION AND PUBLICATION

CCFD-Terre Solidaire
4, rue Jean-Lantier
75001 Paris
Tel. 01 44 82 80 00
ccfd-terresolidaire.org

AUTHORS

This report has been written by Jean Merckaert and Cécile Nelh, with the assistance of Laurence Estival.

If you have any comments regarding this report, we would be very interested to hear them. Please contact: Mathilde Dupré, Advocacy Officer, Financing for Development, m.dupre@ccfd.asso.fr

DIRECTOR OF PUBLICATION:

Catherine Gaudard

PRODUCTION MANAGER:

Emmanuel Cauchois

DESIGN: www.entrez-sans-frapper.com

PRINTING: Mail-Édit

DATE OF FIRST PUBLICATION:

December 2010

REFERENCE: 8071010A

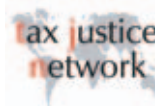
TRANSLATION:

The translation of this report from French to English was done by A&J Communication asbl www.ajcommunication.eu. This document is the English translation of the report "L'Economie Déboussolée, Multinationales, Paradis Fiscaux et Captation des richesses", published in December 2010. Please,

note that data have not been updated. All the information presented in chapter 2, about the 50 biggest European companies are the result of an original research done between June and November 2010 on the annual reports they published. For the other case-studies, we used public information that we tried to double check, as often as possible.

PARTNERS

This report has been produced by CCFD-Terre Solidaire as part of the project "Regulate Finance for Development" (www.regulatefinancefordevelopment.org). This project unites six European NGOs:



Bretton-Woods Project / ActionAid UK (United Kingdom), Campagna per la Riforma della Banca Mondiale (Italy), Eurodad (European Network on Debt and Development, Brussels), Glopolis (Czech Republic), WEED (Germany) and CCFD-Terre Solidaire (France).

SUPPORT

Intermon Oxfam (Spain), Misereor (Germany), Oxfam France, Somo (The Netherlands) and the Tax Justice Network (London). This report is also the result of 5 years of reflections within the framework of the *Plateforme Paradis*

Fiscaux et Judiciaires [Tax and legal havens platform].

ACKNOWLEDGEMENTS

We would like to thank the following people for their useful comments and contributions: John Christensen, Martial Cozette, Antoine Dulin, Mathilde Dupré, Renaud Fossard, Maria Garcia, Catherine Gaudard, Geneviève Guénard, Martin Hearson, James Husband, Maureen Jorand, Maylis Labusquière, Martial Lesay, Olivier Longchamp, Katrin Mc Gauran, François Méchin, Maria Jose Romero, Susana Ruiz Rodriguez, Rémi Saintagne, Georg Stoll and Philippe Tournaud.



**WHEN THE REAL ECONOMY IS DOMINATED
BY THE OFFSHORE ECONOMY -
A NEGATIVE SUM "GAME" 38**

WITNESSING RESOURCES FLIGHT 40
UNDERMINING THE SOCIAL CONTRACT 42
GOVERNMENTS RENDERED IMPOTENT 44



**THE EU AND THE G20
HAVE THE H(E)AVENS' KEYS. THEY JUST
NEED TO OPEN THE RIGHT DOOR 46**

THE G20: AN INDETERMINATE STRATEGY 48
PUTTING USERS UNDER PRESSURE 50
OUR RECOMMENDATIONS 52



RECOMMENDATIONS


**REQUIRING MULTINATIONALS TO PUBLISH
THEIR ACCOUNTS ON A COUNTRY-BY-COUNTRY BASIS,
WITH A PROVISION FOR A SUBSIDIARY-BY-SUBSIDIARY BASIS**

PUTTING AN END TO SHELL COMPANIES

**REINFORCING SANCTIONS
AGAINST ECONOMIC AND FINANCIAL CRIME**



A LIE DETECTOR TEST NEEDED FOR MULTINATIONAL COMPANIES' FINANCIAL STATEMENTS



This report tells the extraordinary story of a world held hostage by its smallest countries¹. It is a world where they say that Goliath stumbles before David, and the major powers bow down before the shamelessness of “tax havens”, despite their huge arsenal of black and grey lists. A world where they say that global wealth is largely generated and exchanged offshore. A world where they say that the British Virgin Islands, Jersey, Mauritius, Bermuda and even Luxembourg have become the matrix for the global economy.

This report tells a story that is hard to believe, as it has almost never been heard before. Tax havens attract unbelievably little attention from economists, who are too obsessed with modelling their assumptions to be able to understand a phenomenon that is by definition hard to quantify on a watertight basis. Christian Chavagneux, a French economist and journalist, and Ronen Palan, a British political scientist, are considered as pioneers in this area. The argument developed in this report owes a considerable debt to the work that they have carried out with Richard Murphy, a chartered accountant.

This report tells the story of a fraud. This fraud is abetted by the tax havens, which reflect a false map of the global economy in their distorting mirrors. The statistical

trickery, which makes Mauritius the leading investor in India, or Jersey the leading banana supplier in Europe, is blatant. However, artificially locating economic activity far away from its real sources, in these transit zones of global finance, has other effects, and ones that are much more serious. The process distorts the distribution of wealth on a global basis, by depriving governments of their variable tax bases² – and therefore of the taxes that the wealthiest ought to pay, and by depriving workers of their livelihood. It also illegally deprives developing countries of several hundreds of billions of euros per year, money that would enable them to invest in their future, to provide healthcare, education and food for their people, while also taking the freedom to forgo international assistance and debt away from them. Today, this huge gap between the real geography of wealth and the one reflected by tax havens is the crucible for global inequality.

ARTIFICIALLY LOCATING
ECONOMIC ACTIVITY FAR AWAY
FROM ITS REAL SOURCES,
IN THESE TRANSIT ZONES
OF GLOBAL FINANCE, (...)
DISTORTS THE DISTRIBUTION
OF WEALTH ON A GLOBAL BASIS

However, the liars are not so much the tax havens themselves, who are consenting participants in a fraud that others want to keep secret – but actually the main economic players in the global economy: the banks and multinational companies. The omnipresence of these players in the black holes of global finance – we have identified 4,748 subsidiaries just for the fifty largest European groups – has two simple explanations. One explanation, of course, reflects the legitimate economic activities of said groups: one group’s plant in Ireland and the other’s franchise in Switzerland, for example. As far as the other significant explanation is concerned, the aim for an overwhelming majority of multinational companies is to be free to shield the value that they create from taxes, or even from demands for higher

1 The total area of 36 of the 60 tax havens that we have listed (see p. 7) hardly amounts to 16,000 km², i.e. half the size of Belgium!

2 The tax base is the taxable amount. Just as consumers and property represent bases that are practically immovable, so personal fortunes and multinational companies’ profits can easily bypass borders.

••• salaries – and sometimes from stock market regulators or the law. In order to achieve their goals, they are assisted by armies of legal and tax professionals who have turned this issue into a business, and by the enormous growth of the intangible economy (research, development, brands, licenses, insurance, etc.), which can relocate on a whim³.

Are multinational companies above the law? They dominate whole sectors of the global economy. It should therefore not come as a surprise that some of them believe that they can bypass the rules that apply to the man in the street. Even better, through the intermediary of banks, audit and advisory firms on tax planning, they create legislation adapted to their interests in territories that put their sovereignty up for sale.

THE LIARS ARE NOT SO MUCH THE TAX HAVENS
THEMSELVES BUT ACTUALLY THE MAIN ECONOMIC
PLAYERS IN THE GLOBAL ECONOMY:
THE BANKS AND MULTINATIONAL COMPANIES.

However, multinationals are not the only ones to blame. If they can lie so easily in their financial statements, in order to locate a capital gain wherever they want to, it is because the law does not prevent them from doing so. Is the law badly written? Is it not applied properly? In the words of Denis Healey, the former British Finance Minister, the line between legality (optimisation) and illegality (fraud) is as thin as *“the thickness of a prison wall”*. In practise, however, the risk of criminal proceedings is almost non-existent. Both finance directors and chartered accounts can prepare and certify inventive financial statements at their leisure, and still end up on the right side of the wall, without breaking any laws because *“tax avoidance often relies on the existence of a doubt regarding interpretation of the law [and] it is often hard to resist playing the tax laws of one country off against the laws of another.”*⁴

There ought to be a simple way of reconciling a company’s accounting with its economic reality, namely requiring companies to give a detailed account of their business on a country-by-country basis. Although it would not remove the temptation for companies to locate their intangible assets in countries with attractive tax regimes, this type of transparency requirement would oblige them to provide truthful

THERE OUGHT TO BE A SIMPLE WAY OF RECONCILING
A COMPANY’S ACCOUNTING WITH ITS ECONOMIC
REALITY, NAMELY REQUIRING COMPANIES
TO GIVE A DETAILED ACCOUNT OF THEIR BUSINESS
ON A COUNTRY-BY-COUNTRY BASIS.

accounts. In fact, the way in which a company accounts for its business activities is not strictly a private matter. The preparation⁵ and audit of accounting standards, which is now the monopoly of investors, multinational companies and the large accounting firms, ought to be considered as a matter of general interest.

The importance that multinational companies have acquired in the global economy assigns them significant responsibilities towards society. Evidently – and tax is unfortunately not the only area –, they are incapable of fully shouldering those responsibilities without being forced to, despite the goodwill shown by some of them. What is in play here is sovereignty and our ability to choose our destiny as human beings and to tell the strongest among us what the law is, rather than putting up the law imposed on us by the latter. In the 19th Century, Lacordaire declared that *“Between the weak and the strong, between the rich and the poor, freedom is the oppressor and the law is the liberator”*. The time has come to assess the health of our world based on the fate reserved for the weakest among us. Will the G20 be able to do this, or even want to? It will have the chance to prove it in Cannes in 2011✱

Jean Merckaert

3 “63% of the value of the [101 listed European countries] studied is represented by intangible assets”, according to Ernst and Young, in *Capital immatériel, son importance se confirme*, January 2008.

4 C. Chavagneux, R. Murphy et R. Palan, « Les paradis fiscaux : entre évasion fiscale, contournement des règles et inégalités mondiales », *L’Economie politique* n°42, 2009, p. 29.

5 By the International Accounting Standards Board (IASB), based in London, and the Financial Accounting Standards Board (FASB), in the USA.

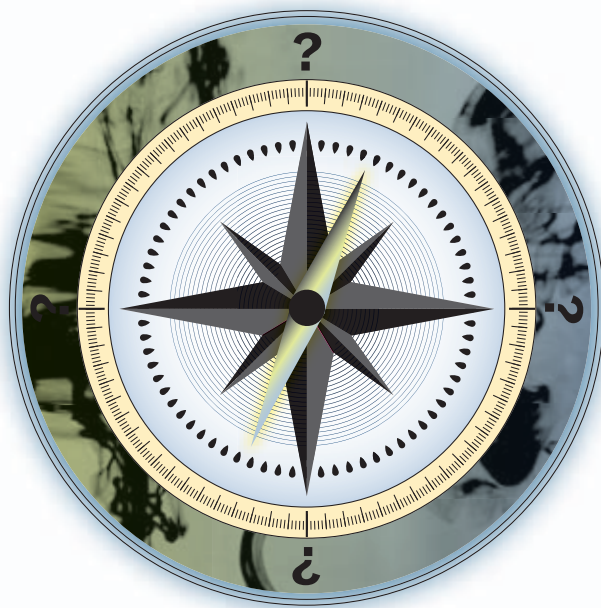


CHAPTER



INVESTMENT, TRADE, SAVINGS, AND PRODUCTIVITY:
THE MAIN MACRO-ECONOMIC BAROMETERS DISPLAY MEANINGLESS
NUMBERS THAT ARE OBVIOUSLY DIVORCED
FROM THE REAL ECONOMY. SECRECY JURISDICTIONS
ARE AT THE HEART OF THESE MISLEADING STATISTICS.
CAN GOVERNMENTS REALLY STEER THE GLOBALISED ECONOMY
WITHOUT RELIABLE TOOLS?

WHEN INDICATORS LOSE THEIR DIRECTION



REFERENCE POINT

THE FINANCIAL SECRECY INDEX

■ More than 80 % opacity ■ 60 to 79 % opacity ■ 40 to 59 % opacity ■ This country is not a secrecy jurisdiction

It is impossible to find a list of tax havens on which there is total consensus. Unlike the OECD and FATF lists, the list of “secrecy jurisdictions” published in November 2009 is not subject to any diplomatic pressure.¹ In order to draw up that list, Tax Justice Network, a network of NGOs and experts, has focused on the 60 countries that were mentioned at least twice in the 15 or so lists issued by various authors and institutions since the 1970s.

The ranking opposite is the result of a two-step approach:

a) calculating the degree of secrecy according to an array of 12 criteria, including, for example, compliance with anti-money laundering standards, the potential existence of shell companies or legal vehicles that enable the identity of their owners to be hidden, or even the quality and depth of tax cooperation.² This secrecy index determines the colours that we have assigned to territories throughout the report – from red for total secrecy to yellow for lower-level secrecy.

b) TJN has combined this index with the importance of each territory in the offshore finance sector (its share of the global non-resident financial services market), in order to assess the real damage that each territory does to the world economy.

You can find the ranking on www.financialsecrityindex.com

¹ For an accurate analysis of the OECD lists, see Jean Merckaert and Renaud Fossard, “Paradis fiscaux : bilan du G20 en 12 questions [A Review of the G20 in 12 Questions]”, in the April 2010 *Terre Solidaire* report.

² For a list and detailed explanations of the indicators, see: www.argentsale.org

RANKING TAX HAVENS ACCORDING TO THEIR OPA- CITY SCORE (TAX JUSTICE NETWORK)

BAHAMAS
BARBADOS
BELIZE
BRUNEI
DOMINICA
MALAYSIA (LABUAN)
SAMOA
SEYCHELLES
SAINT LUCIA
SAINT VINCENT AND THE
GRENADINES
SWITZERLAND
TURKS AND CAICOS
ISLANDS
VANUATU
MAURITIUS
ANTIGUA AND BARBUDA
BAHRAIN
BERMUDA
BRITISH VIRGIN ISLANDS
CAYMAN ISLANDS
COOK ISLANDS
COSTA RICA
GIBRALTAR
GRENADA
MARSHALL ISLANDS
NAURU
PANAMA
PORTUGAL (MADEIRA)
SUDAN
UNITED ARAB EMIRATES
UNITED STATES VIRGIN
ISLANDS
UNITED STATES (DELAWARE)
AUSTRIA
LEBANON
ISRAEL
LIBERIA
ANGUILLA
JERSEY
LIECHTENSTEIN
LUXEMBOURG
MACAO
URUGUAY
ANDORRA
ARUBA
ISLE OF MAN
MALTA
PHILIPPINES
MALDIVES
GUERNSEY
MONTSERRAT
SINGAPORE
CYPRUS
HUNGARY
LATVIA
NETHERLANDS ANTILLES
BELGIUM
MONACO
HONG KONG
IRELAND
THE NETHERLANDS
UNITED KINGDOM (CITY
OF LONDON)

DEFINITION OF FDI
 Foreign Direct Investment, or FDI, involves a transaction whereby an agent establishes a company abroad, reinvests part of its profits in a foreign subsidiary or branch, or even acquires shares or investment units (a minimum of 10%) in a foreign company that already exists, in order to influence its management.

THE FUTURE UNDER THE PALM TREES LOOKS PROMISING

Tax havens are international investment hubs

In theory, this is what a Luxembourg national invests in the EU every year, i.e. 110 times more than a French national, 130 times more than a German national and 210 times more than an Italian national (average amounts for the period between 2005 and 2008).

BUT WHAT IF INTERNATIONAL INVESTORS WERE NOT THE ONES AT THE VERY TOP OF THE INTERNATIONAL RANKINGS?

THE IMPORTANCE OF SECRECY JURISDICTIONS SKEWS THE STATISTICS TO SUCH AN EXTENT THAT THERE IS REASON TO DOUBT THE RELEVANCE OF POLICIES THAT HAVE BEEN INTRODUCED TO ATTRACT INTERNATIONAL CAPITAL, PARTICULARLY BY SOUTHERN COUNTRIES.

DISTURBING STATISTICS

If foreign investment is a growth engine, the numbers published by UNCTAD last July should provide solace to international institutions that have made international investment the cornerstone of their development policy: developing or transitional countries are now the recipients of over half of these monetary inflows. However, a more detailed examination of the statistics provided by the OECD throws up a number of surprises. On a per capita basis, the inhabitants of the British Virgin Islands win the award for investing internationally. The territory (BVI in financial-speak) has an especially large presence in China, where its importance is four times greater than Japan's in volume terms. In total, the BVI, Singapore, Hong Kong, the Cayman Islands and Mauritius are behind 71% of foreign direct investment in the People's Republic of China! These territories are also tempted by Northern countries. In theory, every inhabitant of the BVI archipelago invests

¹ According to the United Nations, the 10 most powerful economies in 2009 were: the United States, China, Japan, Germany, France, the United Kingdom, Italy, Russia, Brazil and Spain. Given the lack of data for Russia, we used India in its place for our calculation.

€ 128,000



KEY FIGURE ▶

PROOF BY EXAMPLE

LUXEMBOURG: SMALL IS BEAUTIFUL

Luxembourg, the smallest member of the European Union after Malta, is one of the 10 main global financial centres. The country is the second-ranked centre for investment funds after the United States; it is also the leading international private banking centre in the euro zone. Luxembourg's legal and tax framework also makes it a centre that is "renowned for the advantages granted to holding companies"⁴ that set up operations there. In 2002, 15,000 holding companies owned a "war chest" of €2,274 billion⁵ in Luxembourg, i.e. 44 times the Grand-Duchy's GDP.

2 These numbers are the result of our calculations based on data provided by the OECD, the French Embassy in Brazil, www.uschina.org/statistics/fdi_cumulative.html, http://www.dipp.nic.in/fdi_statistics/india_fdi_oct_2006.pdf and Fortune Global 500.

3 Idem 2

4 Information report on tax havens issued by the Commission des Finances, de l'Économie Générale et du Contrôle Budgétaire (French Finance, General Economic and Budget Monitoring Commission) and presented by D. Migaud on September 10th 2009.

5 Source : V. Peillon, « Le Grand Duché du Luxembourg », *Rapport d'information de l'Assemblée Nationale*, n° 2311, volume 5, 2002.

6 Source: Calculations based on the *CIA Factbook* and *Fortune Global 500*

PROOF BY EXAMPLE

THE ADVANTAGES OF DOMINICA

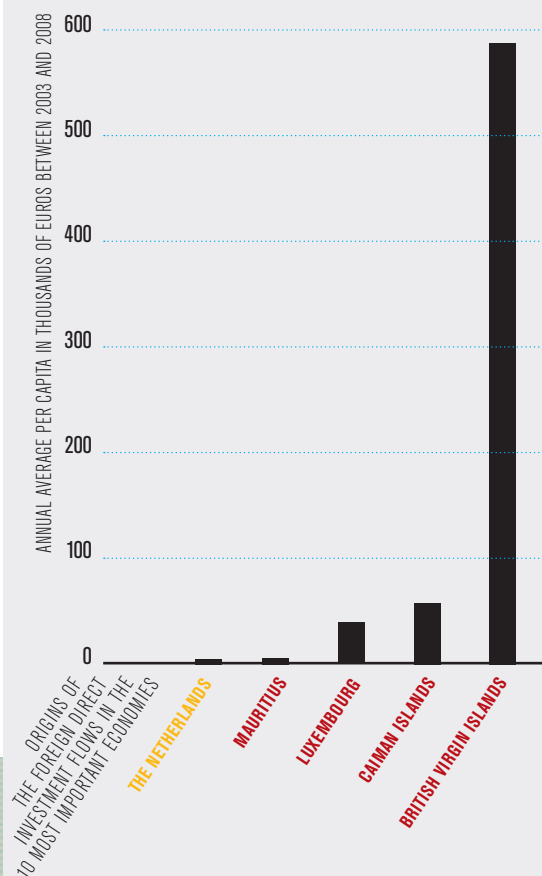
“Dominica authorises “nominee directors”, who are very useful for clients who want to remain anonymous. “[...] We can, of course, provide this service. [It] enables you to run the company, exercise any right, make any declaration, pay and receive any amount and acknowledge receipt of payments. Bearer shares are also authorised. These two major advantages enable you to invest on a tax-free basis, without any of your associates or other interested parties knowing the real identity of the company's beneficiary or discovering the number of bank accounts held by a company.”
CCP Inc., a tax “optimisation” consultancy

... a record amount of €589,000 per year in the ten most powerful global economies.¹ The BVI, the Cayman Islands, Luxembourg (the largest investor in France), Mauritius and the Netherlands account for only 1% of global GDP and for 0.27% of the world's population. They are home to just 14 of the world's 500 largest companies. However, these five countries combined weigh 1.7 times more than the United States and three times more than Japan, Germany and France put together in terms of foreign direct investment. Given that the last four powers account for 44% of global GDP and are home to 57% of the world's companies, these numbers are beyond understanding!² Unless living in a tax haven makes people boundlessly optimistic about the future...

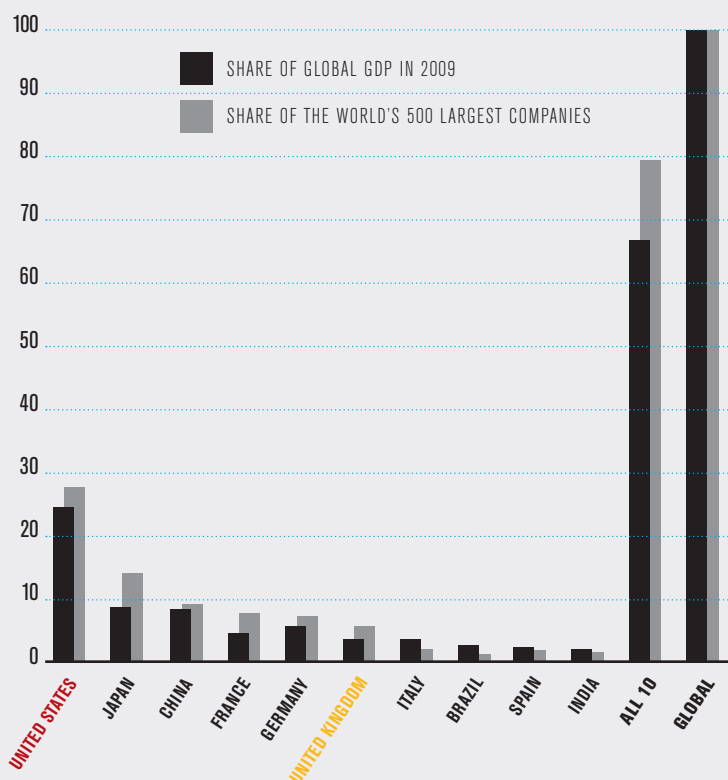
“Freedom of investment is a crucial pillar of economic growth, prosperity and employment. [...] we remain committed to minimize any national restrictions on foreign investment.”

G8 Heiligendamm Summit Declaration, June 2007

THE TOP FIVE NATIONALITIES OF INVESTORS IN THE WORLD'S 10 LARGEST ECONOMIES³



SIZE OF THE 10 MAIN ECONOMIC POWERS IN 2009⁶



MAURITIUS GOES TO BOLLYWOOD⁷

Mauritius is a heavenly island with an area of 1,865 km² and around 1.3 million inhabitants, which does not just appeal to tourists. To avoid tax, many wealthy Indians also make frequent – often virtual – visits to the island, in order to invest their money in Port-Louis, the Mauritian capital. The aim is to reinvest that money in their native country, tax-free. This back and forth process, which enables them to jettison tax and customs duties with impunity, is known as “round-tripping”, or the reason why Indian capital invested in India is accounted for as “foreign” investment.

Due to “treaty shopping”, the same goes for many multinational companies and members of the Indian diaspora. Thanks to its double-taxation treaty with India, Mauritius – which does not levy tax on capital gains – enables capital to be exempt from tax. These two tricks have contributed towards making Mauritius the largest global investor in India for the past ten years, and by a very significant margin (43.6% of foreign investments, compared with 5.4%, for example, for the United Kingdom). The Mauritian Government, which justifies its strategy in the name of the island’s development, adapts its legislation to clients’ requirements: an offshore company can

be established for 1,500, without even going there. Officially, the corporate tax rate has risen to 15%, from 0% in 1998; however, a tax proxy enables an effective rate of 3% to be paid.

The Tax Justice Network ranks the island as one of the most opaque territories in the world (see p. 7). With an opacity score of 96%, it is also a regular transit point for international corruption.

New Delhi estimates the earnings shortfall for the Federal Government at hundreds of millions of dollars – which means the same shortfall for agricultural or healthcare policies. They have repeatedly threatened to repeal the tax treaty linking India to Mauritius and even turned down some investments in 2009, in order not to encourage treaty shopping. The companies involved include Goldman Sachs and Japan Tobacco.⁸

In February 2010, Shri Pranab Mukherjee, the Indian Finance Minister, stated that the “*The role of tax havens and low tax jurisdictions has become an area of great concern for a country like India which is putting its all acts together to mobilize resources to attack on poverty and illiteracy.*”⁹

7 This box is largely inspired by Jean Merckaert’s article : “Île Maurice : l’autre paradis (Mauritius, the Other Paradise)”, in *Faim et Développement Magazine*, February 2010.

8 Business Standard (India), “Stop ‘treaty shopping’ denials for FDI: FIPB tells revenue dept”, 7th November 2009.

9 Indian Government, *FM inaugurates International seminar on transfer pricing*, 17 February 2010. <http://pib.nic.in/release/release.asp?relid=57917>

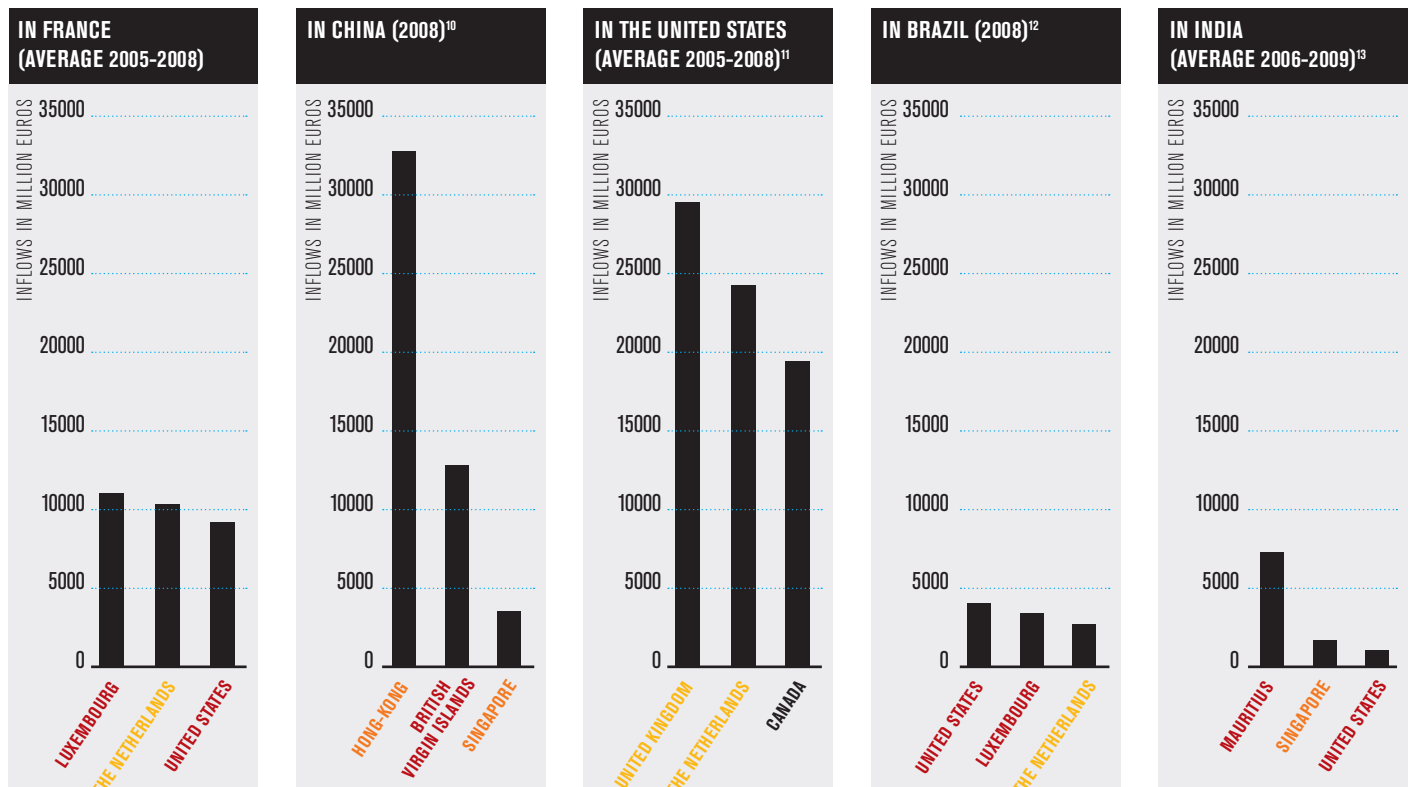
10 USCB, *Foreign Direct Investment in China*, 2009

11 OECD Database 2008, *op. cit.* p 6.

12 French Embassy in Brazil, *Le Brésil et la France en chiffres*, 2009.

13 Indian Government, *Fact sheet on foreign direct investment*, 2009. http://dipp.nic.in/fdi_statistics/india_fdi_october2009.pdf

THE THREE FIRST INVESTORS



... SACRIFICES WITH UNKNOWN CONSEQUENCES

These numbers, which are obviously skewed, fundamentally call into question the benefit of FDI for countries that are trying to attract.

According to its backers, FDI has three potential advantages for destination countries: creating jobs, technology transfer and tax payment. In practice, however, diverting the tax base through tax havens makes this last supposed advantage quite meaningless (see chapter 3).¹⁴ This is enough to cast doubt on the policies recommended by international financial institutions, headed by the EU, the IMF and the World Bank, which make welcoming foreign capital the be all and end all for economic lift-off. Financial backers have encouraged developing countries to make numerous sacrifices to attract foreign capital, against all the economic evidence.¹⁵ This attitude has penetrated so far that the World Bank's Doing Business report produces a ranking of countries where the climate is viewed to be the most favourable for business for the intention of investors, and makes the corporate tax rate one of the key factors in those rankings. Unsurprisingly, tax havens took four of the five top spots in the rankings in 2009!¹⁶ In the name of funding development and combating poverty, financial backers have, in effect, encouraged the expansion of tax havens for investors. And there is no indication that they have stopped doing so (see box "How development organisations invest through tax havens").

In addition, we may even doubt the very existence of FDI when it is obviously not foreign investment, like in the case of the Indian funds routed through Mauritius (see box "Mauritius Goes to Bollywood"). The FDI amounts should also be taken with a pinch of salt: in fact, the French Embassy in Brasília has actually stated that: "the numbers put forward by Luxembourg and the Netherlands should be handled with great care. These countries are actually home to the tax headquarters of many groups established in other European countries."¹⁷

14 See also the Norwegian Government report, *Tax Havens and Development*, Norad, June 18th 2009.

15 A study conducted by McKinsey in 2004 shows the ineffectiveness of tax sacrifices aimed at attracting FDI. See *The McKinsey Quarterly 2004 - 1*, McKinsey and Company, 2004.

16 Singapore (1), Hong Kong (2), United Kingdom (3) and USA (5) - same ranking in 2010.

17 French Embassy in Brazil, *op. cit.*, 2009.

SPOT THE MISTAKE

HOW DEVELOPMENT ORGANISATIONS INVEST THROUGH TAX HAVENS

Despite repeatedly advertising their intention to combat tax avoidance and illegal capital flight, the development backers use the services of tax havens themselves.

Some do not hesitate to support investment funds domiciled in tax havens. This is the case of the European Investment Bank (EIB) and of several of its projects intended for Africa, the Caribbean and the Pacific (ACP), like the €20 million granted in December 2008 to Africinvest Ltd, a company focusing on the expansion of SMCs in East and West Africa and managed by Africinvest Capital Partners, which is domiciled in Mauritius.¹⁸ Another example is the International Finance Corporation (IFC), which is responsible for providing support to the private sector within the World Bank, and openly invests in companies based in Mauritius, Bermuda, Luxembourg and the Cayman Islands - like Kosmos, a company to which it lent €172 million to develop hydrocarbon reserves in Ghana.¹⁹

Undoubtedly, investing in Africa is not easy, given the lack of reliable banking services in many countries. Tax havens offer tried and tested banking and financial services, and those services can be used without the intention of encouraging fraud. However, investment in or through secrecy jurisdictions should be at least justified by development agencies, and accompanied by an increased transparency requirement, especially since there is nothing inevitable about this type of investment.

In fact, the Norwegian Government, which ordered a report on the subject in 2008,²⁰ was concerned that Norfund, its development fund, used Mauritius, the Cayman Islands, the British Virgin Islands, the Bahamas, Panama and the Seychelles for its regional investments in Africa. As he was of the view that development ought not to support tax avoidance, Erik Solheim, the Norwegian Development Minister, forbade any further investment in secrecy jurisdictions from that point onwards, unless those havens had signed a tax information sharing agreement with Oslo. In October 2009, 15 European financial backers drew up codes of conduct regarding their offshore investments.²¹ Although they are timid today, these measures nonetheless open the door to a global clean-up of development agencies' practices in tax havens, which is so very necessary.

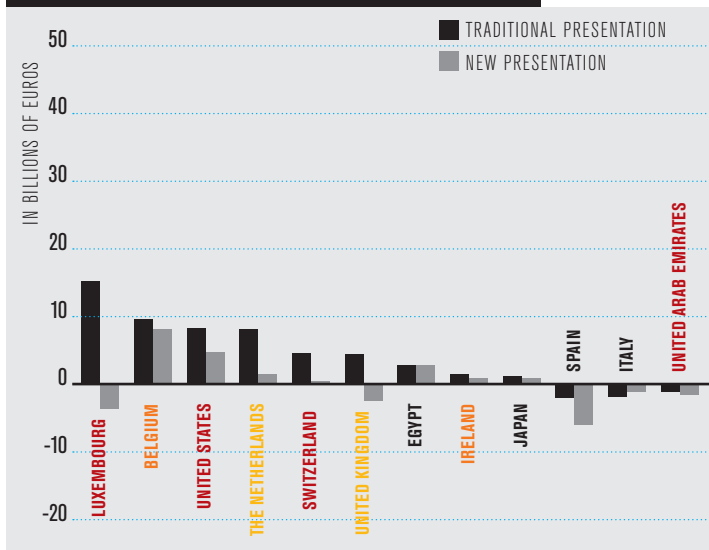
18 Marta Ruiz and Greg Atken, *Un enfer pour le développement. Comment la Banque européenne d'investissement cautionne les paradis fiscaux*, December 2009.

19 Sébastien Fourmy and Antonio Tricarico, « Is the IFC supporting tax evading companies? », *Study made by Eurodad, CRBM, IBIS, Oxfam France and Tax Justice Network*, December 2009.

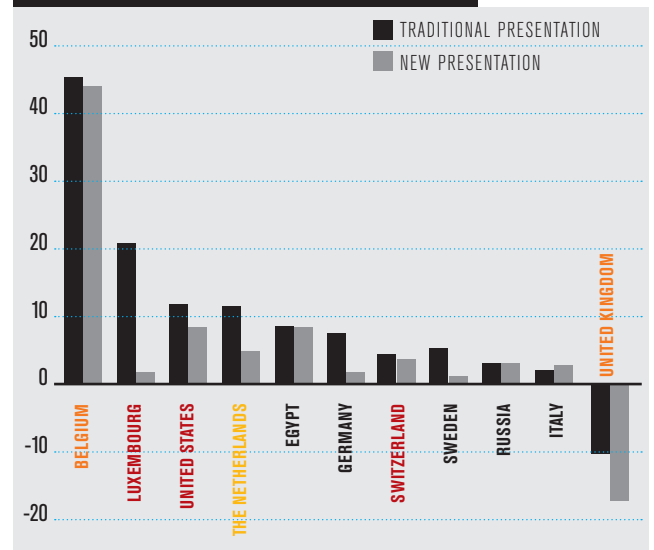
20 *Tax Havens and Development*, June 2009.

21 European Development Finance Institutions (EDFI). Cf. www.edfi.be

MOST IMPORTANT FDI COUNTRIES OF ORIGIN IN FRANCE²²



MAIN DESTINATION COUNTRIES FOR FRENCH FDI²³



... TOWARDS A STATISTICAL CLEAN-UP?

In order to improve the way in which the reality of FDI is reported, the OECD recommends in the 2008 edition of its “Benchmark Definition of Direct Foreign Investment” that loans between entities in the same group which are located in different countries should no longer be taken into account. The OECD believes that the creation of entities specialising in finance or group treasury management has artificially inflated FDI fund flows. The new calculation method significantly changes the landscape, according to the study published by the Bank of France.²⁴ Luxembourg, which was the largest investor in France according to the traditional calculation method, becomes that country’s second largest “disinvestor”²⁵ in terms of FDI flows according to the new calculation method (see chart). According to this study, FDI inventories should also be revised downwards: by 30% for outgoing FDI and by 43% for incoming FDI, as at the end of 2008.

Another calculation method in the OECD’s new toolbox, which is based on the “end-investor”, puts the statistics into

even sharper perspective. The organisation is suggesting no longer considering investments between subsidiaries in the same group that are located in different countries as FDI in the conventional sense of the term. What is now taken into account is not the entities’ geographical location but the group’s nationality. For example, subsidiary a1 (based in Luxembourg) of Company A (based in France) invests in its (French) subsidiary a2, either through its share capital or in the form of reinvested profits. According to this new method, these investments are considered as foreign investments in France, originating in France. So **the number one destination for French foreign investment is France and foreign investments in France are very largely made by French groups!** The imperative statistical clean-up backed by the OECD may make the fiction of tax havens disappear in the long-term, although it is only at the initial stages. The study published by the Bank of France, for example, only concerns intra-group loans at this point, so capital transactions performed by holding companies continue to be recorded according to the traditional method. ○

²² B. Terrien, 2009, « Une nouvelle norme de construction et de diffusion des statistiques d’investissement direct étranger », *Bulletin de la Banque de France* n° 177.

²³ *Idem.*

²⁴ *Idem.*

²⁵ Through the artifice of repatriating profits to Luxembourg and of intra-group loans that are no longer attached to a Luxembourg financial company but to the group head office.

PUTTING MONEY ON THE (OTHER) SHORE

Valuable but footloose savings

THE IDEA BEHIND THE FREE CIRCULATION OF CAPITAL IS OPTIMISING THE ALLOCATION OF SAVINGS, IN ORDER TO SUPPORT PRODUCTIVE INVESTMENTS.

THE PRIVATE SAVINGS FIGURES TELL AN ALTOGETHER DIFFERENT STORY.

TAX HAVENS ARE AT THE HEART OF THE FOUL PLAY.

With its €2,200 billion in reserves, China makes the big money-men dizzy. However, those savings only amount to €1,454 on a per capita basis, a number that bears no relationship to the €2.8 million – the equivalent of 110 years of the French minimum wage – theoretically saved by everyone living in Jersey,¹ who apparently saves 60 times more than a resident of Switzerland and 1,035 more than a resident of France.² Given the amount of money that they stash away, the inhabitants of Jersey ought to play a pivotal role in global economic growth, since, according to liberal theorists, saving should be systematically encouraged, as the amounts made available in this way promote the granting of cheap loans, which are a source of economic vitality.

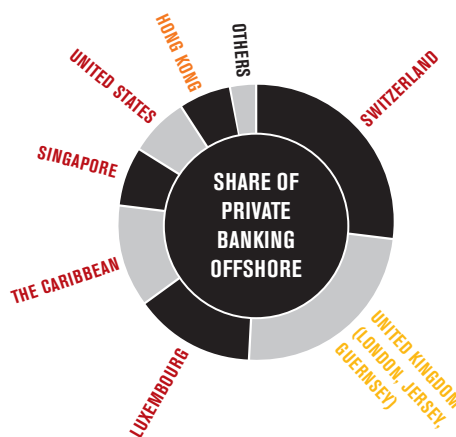
of assets under management), before Luxembourg (14 %), the Caribbean (12 %), Singapore (7 %), the United States (7 %) and Hong-Kong (6 %).⁴ Based on research produced by the Bank for International Settlements (BIS), the Boston Consulting Group and by McKinsey's Research Department, the Tax Justice Network estimates that €9.2 trillion in deposits are held offshore.⁵

These tax havens also deprive developing countries of their savings, as wealthy individuals in Latin America and Africa often prefer to invest their savings abroad.⁶ Half the fortune of wealthy South Americans is thought to be held in offshore banks.⁷ In 2001, Brazil saw US\$ 4 billion take flight just to the Bahamas and the

“Increasing savings and ensuring that they are directed to productive investment are central to accelerating economic growth.”

United Nations Department of Economic and Social Affairs³

The reality, however, is much more complex: the wealth deposited in Jersey is obviously not mostly owned by its inhabitants, but by wealthy individuals who have been advised to invest their fortune on the island by banks or other financial intermediaries. Including London, Jersey, and Guernsey, the United Kingdom accounts for 24% of the global “private banking” sector. Switzerland nonetheless remains the offshore wealth management champion (27%



1 Calculations based on the Tax Justice Network's *Jersey Fact Sheet*.

2 Calculations based on: J. Accardo et alii. [2009] « Les inégalités entre ménages dans les comptes nationaux, une décomposition du compte des ménages », *L'Economie Française 2009*, INSEE, p. 78. Figures from 2003.

3 2005 Report, *Mobilising National Financial Resources for Development*, UN ECOSOC.

4 Figures available at: www.gardinerfinance.com/fr/

5 Murphy, J. Christensen et J. Kemmis, [2005] « *Tax us if you can* », Tax Justice Network p18. http://www.taxjustice.net/cms/upload/pdf/TJUYC_-_edition_francaise_-_30_Aout_2005.pdf

6 They may be motivated by other factors than tax, including the political situation or the weakness of the banking system.

7 Boston Consulting Group, 2003, *Global Wealth Report*.

••• Cayman Islands.⁸ The proportion of capital that takes flight may even be higher for Africa. Global Financial Integrity, American think tank headed by Raymond Baker, estimates that illegal outflows of funds from Africa, including tax avoidance and corruption, have amounted to €1,440 billion (an average of €36 billion per year) over the past four decades, a trend that is accelerating and exceeded the €140 billion per year mark in 2007 and 2008.⁹ In the 1960s, development aid was invented, and the target was set at 0.7% of GDP, specifically to remedy the domestic savings shortfall of the countries that were then known as the “Third World”. Sadly, History is repeating itself: just the illegal portion of the funds fleeing Africa is far in excess of the foreign aid received by that continent.

The result is that savings that disappear are rarely reinvested in situ. Due to the lack of liquidity, local banks apply high interest rates, between 23% and 25% in Ghana, for example¹⁰ and struggle to grow: there is less than one bank branch per 100,000 inhabitants in Ethiopia, Uganda and even Tanzania...○

8 F. E. Stiftung, “Money Laundering and Tax Havens: the Hidden Billions for Development”, *Occasional Paper n°3*, March 2003.

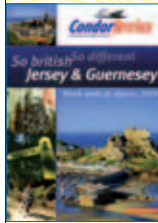
9 Our calculations based on D. Kar and D. Cartwright-Smith, 2010, “Illicit Financial Flows from Africa : Hidden Resource for Development”, *Global Financial Integrity*.

10 United Nations 2008, “Boosting Domestic Savings in Africa” in *Africa Renewal*, vol. 22.3, pp. 12- 8. <http://www.un.org/french/ecosocdev/geninfo/afrec/vol22no3/223-epargne.html>

PROOF BY EXAMPLE

JERSEY, A TREASURE ISLAND

Set sail from Saint-Malo: the ferry company does not try to hide the attractions of the Island of Jersey, which covers an area of 116 km² tucked between France and the United Kingdom. Its brochure baldly informs you that “you can already escape on board” and it is tempting



to see a reference to more than just the island’s scenic charms in that statement. The territory offers many advantages: “*Low taxes and inheritance tax make the island a popular tax haven*”, is the view of the CIA.¹¹ In addition to the absence of taxation for non-residents and the poor quality of its tax information exchange mechanism, Jersey’s key to success is based on its trusts. These

legal vehicles, which are very common in English-speaking countries, involve one individual (the trustor) irreversibly entrusting the management of their wealth to a trustee (a trusted person) for the benefit of a third party. However, the regulatory authorities often find it impossible to identify the parties hiding behind the trustee – who becomes just a frontman when the trustor and the beneficiary are one and the same. Jersey is one of the most innovative financial centres in this area, allowing the trustor to withdraw their wealth on demand (sham trust), for example, which is contrary to traditional practices. Jersey also authorises companies to register on its territory in cases where it has no information about the owners and the business involved... In total, 53% of its GDP is derived from financial activities.¹² The island manages around €500 billion in assets,¹³ as well as 1,030 hedge funds,¹⁵ and has one bank for every 1,125 people.¹⁶

11 CIA Fact Book, 2010, <https://www.cia.gov/library/publications/the-world-factbook/geos/je.html>

12 Tax Justice Network, *Jersey factsheet*, February 2009.

13 This number corresponds to the total amount of the funds deposited in Jersey-registered banks and to the assets held by companies or hedge funds, for example, which are registered in Jersey. It therefore does not include the financial assets in opaque vehicles like trusts, where it is impossible to establish the amount of the assets held. Source: *Tax Justice Network* (<http://taxjustice.blogspot.com/2009/03/ending-offshoresecrecy-system.html>).

14 Figure from the *AGEFI* newspaper, June 16th 1998.

15 Figure from: <http://fr.transnationale.org/pays/jer.php>

ENCOURAGING COMPANY START-UPS

When vice overcomes virtue

THE RED CARPET IS ROLLED OUT FOR ENTREPRENEURS. CONSIDERED AS THE NEW HEROES OF THE MODERN AGE, THEY ARE SUPPOSED TO INSTIL GROWTH AND CREATE JOBS, ALTHOUGH THEIR IDENTITY AND THE NATURE OF THEIR BUSINESS ARE NOT ALWAYS CHECKED...

This is the number of companies registered per inhabitant in the British Virgin Islands, which were home to around 830,000 companies for 24,491 inhabitants in 2010. In France and Germany, the opposite situation prevails: on average, you need to find 28 and 46 inhabitants respectively for every company.

"You've got a building in the Cayman Islands that supposedly houses 12,000 corporations.

That's either the biggest building or the biggest tax scam on record."

Barack Obama, 5th of January 2008

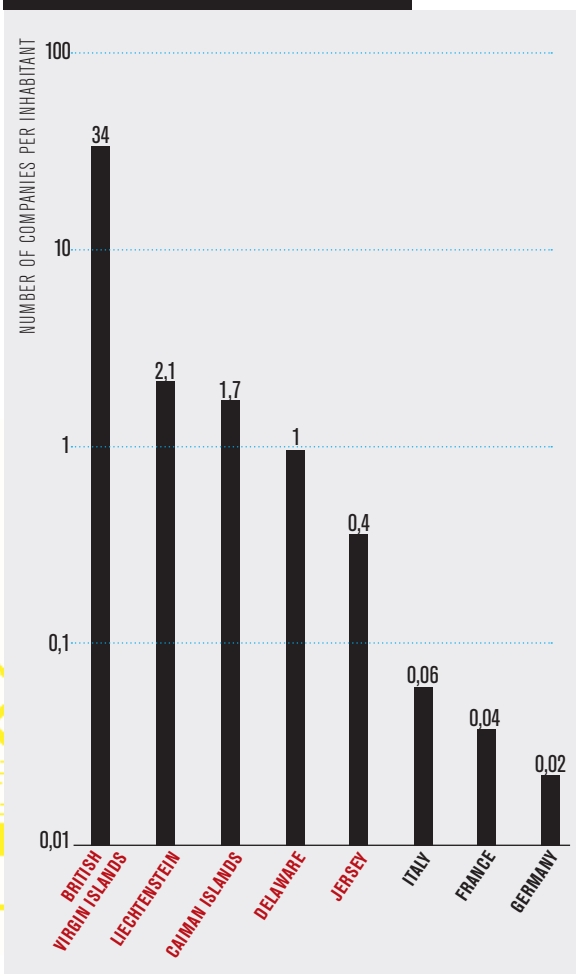
ENTREPRENEURSHIP IS ACCLAIMED

For the European authorities, there is no room for doubt: *"Policies that promote entrepreneurship and create a favourable environment for business, in particular small and medium-sized enterprises, are crucial if the European Union is to rise to its number one challenge of stimulating economic growth and creating new jobs."*¹ The G20, meanwhile, is not to be outdone: *"dynamism, innovation and entrepreneurship (...) are essential for economic growth, employment and reducing poverty."*² (Washington Declaration, November 15th 2008). According to this approach, where an entrepreneur only takes risks so as to benefit the public interest – albeit while extracting a personal profit –, it becomes essential to remove any obstacles to its business! The time has come, however, for improving economic regulation... But is entrepreneurship really imbued with all the virtues that the European Union and the G20 see in it?

EMPTY SHELLS

One thing is certain, and that is that the numbers are surprising. Eva Joly, the current Chairwoman of the European Parliament Development Commission, who went on a fact-finding mission to Mauritius, explained that she had discovered that *"nine people were running 1,500 companies, which makes all the economists roar with laughter"*.³ Three countries, Liechtenstein, the Cayman Islands and the BVI, have the apparent merit of being home to more companies than people. We should note that the State of Delaware is not far behind, as if only one inhabitant was required to establish a company in this small state on the East Coast of the United States (0.27% of the US population), when there is only one company per 14 inhabitants in the rest of the country.⁴ An ethnological study might enable the existence of an insatiable spirit of entrepreneurship to be identified among nationals of these territories. More likely, the vast majority of the companies registered there, like in all tax havens, are nothing more than a letter box. The only reason for creating these shell companies is avoiding tax and regulatory constraints, and even the law.

NUMBER OF COMPANIES PER INHABITANT



¹ First European SME Week, http://ec.europa.eu/enterprise/policies/entrepreneurship/sme-week/documents/8_entr_sme09i_leaflethr_fr.pdf

² European Commission, *Declaration summit on financial markets and the world economy*, November 15th 2008.

³ "Who Benefits?"; movie produced by the NGOs coalition Counter Balance, 2010.

⁴ In 2010, there were 23 million companies for 310 million inhabitants in the United States.

... IT WILL TAKE YOU 45 MINUTES AND COST YOU 555 EUROS

The competition is such that major powers like the United States and the United Kingdom, which are concerned with encouraging as much capital as possible to transit through their financial centres, have developed legislation that is quite as lax as that in Caribbean countries. This is reflected in the study conducted in 22 countries by Jason Sharman, a professor at Griffith University (Australia). The results of that study are edifying: the academic discovered that in 17 of those countries, including 13 countries in the OECD and four tax havens, it was possible to create your own company simply by going online and investing a minimum €16,000. *"The most welcoming havens for someone who wants to disguise their financial transactions – whether they are a member of the Mafia or just a cheat – are not the Caribbean Islands or Switzerland, but the United States and the United Kingdom!"*⁵ Across the Channel, for example, setting up a company takes 45 minutes and costs €555. The whole process can be performed without revealing your identity! Once the shell company has been registered, the new entrepreneurs have the option of opening a bank account, without providing any proof of identity at this stage either. These simplified procedures are apparently standard in all tax havens, according to the Tax Justice Network. *"In practice, concludes Jason Sharman, OECD countries have much laxer regulation on shell corporations than classic tax havens. And the US is the worst on this score, worse than Liechtenstein and worse than Somalia."*⁶ ○

REFERENCE POINT

BVI
45% of offshore companies (International Business Companies or IBCs) are believed to be registered in the British Virgin Islands (BVI), according to a review by KPMG in 2000.⁷ These companies pay no duties there and corporate income tax is around 8%, above a basic €8,000 threshold. Given the many advantages that they offer, the BVI are one of the most prosperous countries in the Caribbean, and one of the most sought-after locations for multinational companies.

⁵ Xavier Harel, *La Grande évasion, Les liens qui libèrent*, Paris, 2010.

⁶ *The Economist*, "The G20 and tax-haven hypocrisy", March 26th 2009.

⁷ KPMG, *Review of Financial Regulation in the Caribbean Overseas Territories and Bermuda*. Foreign and Commonwealth Office, London, 2000.

ACCORDING TO MULTINATIONAL COMPANIES, FINANCIAL STATEMENTS, THE PROFITABILITY OF THEIR EMPLOYEES IN TAX HAVENS BEARS NO RELATION TO THE PROFITABILITY OF THEIR OTHER SUBSIDIARIES...

A Bermudan employee appears to be 11 times more profitable than one in Switzerland or the Netherlands, and 46 times more profitable than average employees around the world! For every €100 in salary paid in Bermuda, US multinationals reap €3,500 in profits! In other words, their profit rate per employee (excluding any interest income and dividends received from investment portfolios) amounts to 3,500%, a record that is only equalled by Barbados. With respective profitability rates of 660% and 160%, Ireland and Switzerland almost pale in comparison, even if their performance is above the average 84% rate recorded on a world-wide basis... These numbers, extracted from a report by Robert E. Lipsey,¹ are enough to make your head spin!

Labour productivity is defined as the value added generated per employee, or per work hour. According to economic theory, productivity gains can be obtained through organising the workload, motivating employees (managing human resources), investing in equipment and employee qualification levels. Is the theory all wrong? Evidently, the

PROOF BY EXAMPLE

BERMUDA

The Bermuda Archipelago, which consists of 123 islands spread over an area of 53 km², is a British Overseas Territory (the United Kingdom takes care of its security and diplomatic affairs), and the fourth wealthiest country in the world on a per capita basis.² As a specialist in the reinsurance and captive insurance market (see p. 20), the archipelago offers several advantages. Insurance legislation is almost non-existent and companies are not subject to any tax charges,³ a factor that also attracts many hedge funds. In 2009, 15,392 multinational companies were registered in Bermuda,⁴ i.e. around one multinational for every four inhabitants.

¹ C. Chavagneux [2008] « Mondialisation : les multinationales adorent les paradis fiscaux », *Alternatives Économiques*, September 2008, n° 727.

² From the *CIA World Factbook*

³ <http://www.paradis-fiscal.fr/monde/bermudes.htm>

⁴ US State Department <http://www.state.gov/r/pa/ei/bgn/5375.htm>

MAXIMUM PRODUCTIVITY

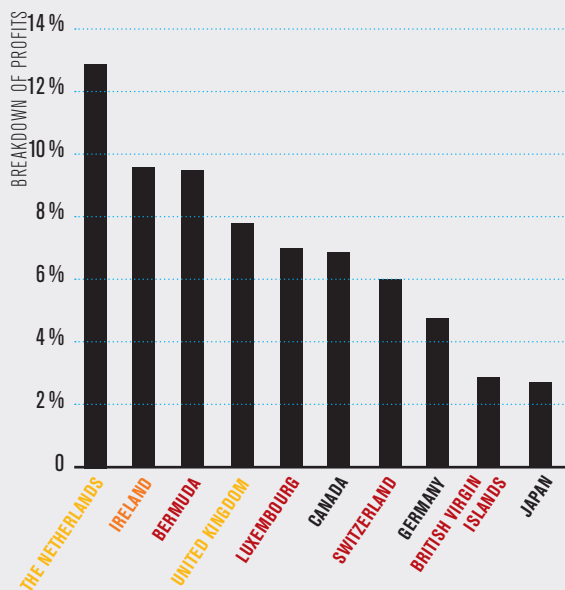
Tax havens = model employees?

... number of palm trees and of financial institutions plays a not insignificant role... According to a report issued by the OECD in 2009, which reduces GDP to the number of hours worked, Luxembourg is top of the employee productivity rankings, followed by Norway (where the GDP is inflated by oil), Ireland, the United States, Belgium and the Netherlands, in front of France and Germany.⁵ Here again, we have a fine cluster of tax havens at the top of the rankings.

It is not just profits per employee that are hitting records in offshore centres: the amount of the assets takes your breath away too. At the global level, that amount is €800,000 per employee. Assets per employee amount to between €3.2 and €4.0 million in Switzerland, the Netherlands and Ireland, to €17 million in Barbados and to €36 million in Bermuda!

The importance of the gaps is explained both by the low denominator and by the high numerator. First, the number of employees in these territories is relatively low, since the businesses that are legally registered there bear no (or little) relation to the business actually conducted in the territory. Second, companies inflate their profits and assets in these territories. In 2003, US companies generated half their foreign profits in six small countries – the Netherlands, Ireland, Bermuda, Luxembourg, Switzerland and the Channel Islands – which do not even have 30 million inhabitants between them, but do offer particularly low tax rates (see chart). Meanwhile, where assets are concerned, the increasing role played by intangibles (licences, brands and logos), which represented 60% of a company's value in 2007 according to the Ernst & Young consultancy group,⁶ enables them to be located in a way that is not connected to the manufacturing sites. This is the heart of the problem ○

WHERE US COMPANIES GENERATED THEIR PROFITS IN 2003*



REAL TAX RATE PER COUNTRY (%)

THE NETHERLANDS	5,3
IRELAND	6,1
BERMUDA	1,7
UNITED KINGDOM	20,1
LUXEMBOURG	-1,8
CANADA	23,5
SWITZERLAND	4,5
GERMANY	8,2
BRITISH VIRGIN ISLANDS	1,3
JAPAN	36,9

5 Sources: OCDE, StatExtracts : <http://stats.oecd.org/Index.aspx?DatasetCode=PDYGT>

6 Ernst & Young, Capital immatériel, son importance se confirme, January 2008.

7 K. A. Clausing, R. S. Avi-Yonah "Reforming corporate taxation in a global economy: a proposal to adopt formulary apportionment", *The Hamilton Project*, June 2007, p. 8.

KEY FIGURE

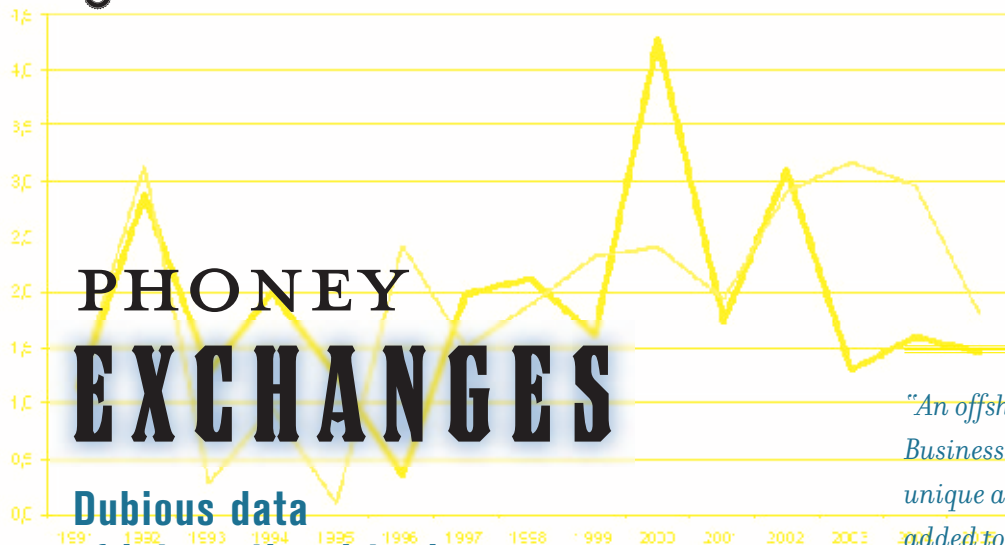
A Bermudan employee is over

46 TIMES MORE PROFITABLE

than the average global employee!

60% OF WORLD TRADE

is now between the subsidiaries of trans-national groups, according to the OECD.¹



Dubious data of international trade

TRADE STATISTICS: A SLIPPERY SLOPE

The real banana skin in the path of world trade statisticians is what the 2007 *Guardian* investigation revealed about the international banana trade (see box on “the banana’s journey”), which does not just amount to the unequal way the value of the fruit that is eaten is distributed, harming the grower, or the complexity of the tax avoidance strategies involved. It also reveals the vacuousness of a portion of world trade. On the banana road, the major players in the sector increase the number of transactions with offshore subsidiaries. These transactions involve services that are often used within a multinational company (insurance, brand usage, management, distribution network, etc.), although the location of the relevant subsidiaries often does not correspond to any economic reality – without even mentioning the compensation level of those subsidiaries (see Chapter 2). “(...) *Large corporations are creating elaborate structures to move profits through subsidiaries to offshore centres such as the Cayman Islands, Bermuda and the British Virgin Islands (...)*” [*The Guardian*, November 6th 2007] This is how *The Guardian* can point to

eight commercial transactions where just one (between the grower and the consumer) would probably have been enough. The result is an inevitable increase in international trade exchanges... But should we nonetheless see the promise of a shared increase in global economic wealth in these numbers? Nothing is more uncertain.

The boom in commercial exchanges over the past 40 years leaves no room for doubt: global goods exports increased sixtyfold between 1967 and 2007,² rising from €173.6 billion to €10,548 billion. At the same time, global GDP expanded by a factor of 24, increasing from €1,782 billion to €44,094 billion. However, over the past few years, the reliability of the numbers has become questionable, since intangible assets and services are increasingly located offshore. Finally, it would be absurd to generalise the clean-up of international trade statistics prompted by the banana trade. However, the fact that statisticians, like Governments, are unable to confirm the reality of intra-group trade transactions, which amount to between 50% and 60% of international trade, is a reason for caution. This is especially so since half of world trade transactions are believed to pass through tax havens.³

*“An offshore company (IBC, International Business Company) in Dominica represents a unique advantage for tax planning. It should be added to medium-sized companies’ and private investors’ commercial plans. (...) Thanks to that company, you can work with (...) onshore and/or offshore companies in any country, manage your business anywhere in the world, open subsidiaries or agencies, acquire investment units (sic) in other companies, open any kind of account, sign any type of agreement, invest your funds, play the stock market, and especially generate profits without paying taxes (except for US\$150 in annual government fees). No annual audit is required”.*⁴

“Caribbean Citizenship Program” (CCP Inc.), a “tax planning” consultancy in Dominica.

AN ABSOLUTE DISADVANTAGE

According to one of the tenets of liberal economics, namely the comparative advantage theory, every country has the option of putting its advantages to good use (availability of natural resources, technological progress, etc.) through exports, in order to obtain foreign currency to reinvest in its development. This specialisation is expected to result in a better allocation of capital at the international level, and to enable a country to obtain imported goods and services at lower cost, given the comparative advantage of its commercial partners

¹ The OECD is talking about 60 to 70% for sophisticated products and around 40% (or less) for manufactured products involving simple processing. See <http://www.oecd.org/dataoecd/6/18/2752923.pdf>

² H. Boumellassa, M. Fouquin, C. Herzog & D. Ünal, *Panorama de l'économie mondiale*, CEPII, December 2009.

³ *Tax Justice Network*, quoting the OECD.

⁴ Translated from French.

MISSILE LAUNCHERS AT 42 EUROS EACH...

Simon Pak, a professor at Pennsylvania State University (USA), has highlighted some bizarre data thrown up by US customs statistics concerning trade between the parent companies and subsidiaries of multinational companies. In fact, he has discovered Czech plastic buckets imported to the United States at €778 each, washcloths imported from China at €3,297 per kilo, missile-launchers exported to Israel at €42 each, car seats priced at €1.33 each bound for Belgium, etc., depriving the US budget of €42.4 billion in tax receipts in 2001, according to his calculations.⁶

In 2006, Simon Pak also studied trade between the United States and Africa. He found imported and exported products at prices that were significantly lower or higher than their median international price. Once more, the statistics throw up major inconsistencies: gross industrial diamonds and wooden beds were exported from Ghana to the United States at €28 per carat (the median price is €1,089) and €4 euros each (the median price is €96); Ghana imported car tyres from the United States priced at €2,688 each (the median price is €33.60), carburettors priced at €48,000 each (the median price is €50.40), etc. In total, there were illegal capital outflows of €76 million from Ghana to the United States in 2005, and of €664 million between 1996 and 2005. Ghana is one example among others, and Simon Pak has calculated that over €24.8 billion left Africa for the United States between 1996 and 2005.⁷

“Trade and development are closely linked. Effective and targeted aid to assist trade will contribute towards removing the obstacles faced by developing countries, which deprive them from taking full advantage of the benefits of globalisation.”⁵

Shisir Priyadarshi, the Head of the World Trade Organisation’s Development Department, speaking at the United Nations General Assembly on April 23rd 2010.

... in fields that are complementary to its own. Swearing only by this theory, international organisations, and particularly the WTO, continually urge the various countries on the planet, especially developing countries, to open their borders even wider.

However, faced with the new trade practices, David Ricardo must be turning in his grave. The father of the comparative advantage theory, which is at the origin of free trade and the international division of labour, is seeing his theory collide head on with the boom in international trade

transactions that do not involve any actual trade – and where the sole purpose is to post an offshore profit. This kind of transaction with tax havens can only amount to a negative sum game for countries that are watching their tax base take flight without any service being offered in return. From comparative advantage to absolute disadvantage...It is hard, in these conditions, to make trade liberalisation the favoured means for increasing the wealth of all nations. ○

PROOF BY EXAMPLE

THE BANANA’S JOURNEY

The banana’s journey on paper:⁸
The banana’s real journey: →



Jersey, a Channel Island that is renowned for the tax advantages that it offers, would be also one of the largest exporters of bananas to Europe. Are there bananas on an island off the coast of Saint-Malo? Yes, at least on paper: a large amount of the Central American banana trade passes through Jersey-based subsidiaries. According to an investigation by *The Guardian* newspaper in 2007, which, to our knowledge, was never challenged by the companies concerned, Dole (26% of the market), Chiquita (25%), Del Monte (16%) and Fyffes (8%) sheltered a large number of subsidiaries and significant profits in tax havens, thus rendering them of little benefit to producer countries. However, the banana’s extraordinary journey was a fiction. In fact, the banana only travelled from the producer country to the consumer country.

The investigation underlined that these companies earned 48% of their revenues in tax havens, thereby minimising the tax paid, to the detriment of the countries where the bananas were consumed (where 40 % of their declared revenues were located), and especially of the producer countries (12 % of revenues). Up until it arrived at the dockside, prior to being distributed within the European market, it therefore appeared that 80 % of the price of a banana stays in tax havens, compared with only 20 % in the producer country... “Fresh Del Monte, which generates 48% of its sales in the United States, has lost €28.2 million in that country, while it has made profits of 107 million abroad. It has therefore never paid any taxes in the United States.”⁹

5 Translated from French.
6 Simon Pak’s report, *False Profit, Robbing the Poor to Keep the Rich Tax-Free*, March 2009, was commissioned by Christian Aid UK.
7 Simon Pak « Estimates of capital movements from African countries to the US through trade mispricing », presentation during the workshop “Tax Poverty and Finance for Development”, Essex University (RU), July 6th and 7th 2006.
8 F. Lawrence et I. Griffiths, November 6th 2007, « Revealed : how multinational companies avoid the taxman » in *The Guardian*.
9 Idem.

AND THE LEADER IS...

CAPTIVE INSURANCE COMPANIES, HEDGE FUNDS, ONLINE BETTING, E-COMMERCE, CYBERSEX, FLAGS OF CONVENIENCE...

WHAT THE PROFESSIONALS CALL "PALM TREE COUNTRIES" HAVE AN EXTRAORDINARY ATTRACTION FOR CERTAIN BUSINESS SECTORS.



CAPTIVE INSURANCE COMPANIES

Captive insurance companies are subsidiaries created by companies to fulfil the role of a conventional insurer. They take care of risk for the parent company and the other subsidiaries in the group. Tax havens, which are home to around three quarters of these captive insurance companies on a world-wide basis, top the rankings (see table).¹ Caribbean islands occupy five of the eight top positions in the ranking of countries that attract the most captive insurance companies, with Bermuda well ahead of the pack.

HEDGE FUNDS

Ronen Palan, Christian Chavagneux and Richard Murphy, the authors of a reference work on tax havens, explain that the *"the Cayman Islands, the British Virgin Islands, Bermuda and the Bahamas shelter 52% of the world's speculative funds. However, those numbers are disputed. The Cayman Islands Financial Services Agency agrees that 35% of the industry is located on its territory, while some even mention the unlikely number of 80%."*² The Cayman Islands are the leading domicile haven for speculative funds: 9,400 hedge funds and pension funds were

domiciled there in 2007.⁴ Jersey also welcomes them with open arms... There is no official definition of a hedge fund, but it is usually a highly profitable investment vehicle, which is unregulated and very secretive. Having been accused of magnifying the financial crisis in 2008, and of being at the heart

ONLINE BETTING

of the Greek crisis and of commodity price speculation, hedge funds are now in the sights of financial regulatory institutions. However, the financial lobby is doing everything to stop the move to bring these funds into line, particularly in Brussels.

Antigua and Barbuda, a member of the British Commonwealth, where the Queen of England is the Head of State, is home to around a quarter of online betting sites.⁵ The archipelago shares this trait with Costa Rica and Malta, which both have over 200 online gaming companies, and a high level of financial secrecy (92% opacity score for the first two and 83% for Malta). These companies, whose activities are being authorised in an increasing number of European countries,⁶ pay no taxes on profits generated outside the country.

Money-laundering experts have highlighted the role of these companies in circuits aimed at laundering dirty money. In traditional casinos, according to Eric Vernier, *"all you need to do is to buy gaming chips for cash and head towards the tables or the slot machines. [...] The pretend gambler then heads back to the cash desk and exchanges the chips obtained at the entrance for a cheque signed by the*

1 C. Chavagneux R. Palan, R. Murphy, *Tax Havens. How Globalization really works*, Cornell University Press, p. 97, 2010.

2 *Idem.*

3 *Idem.*

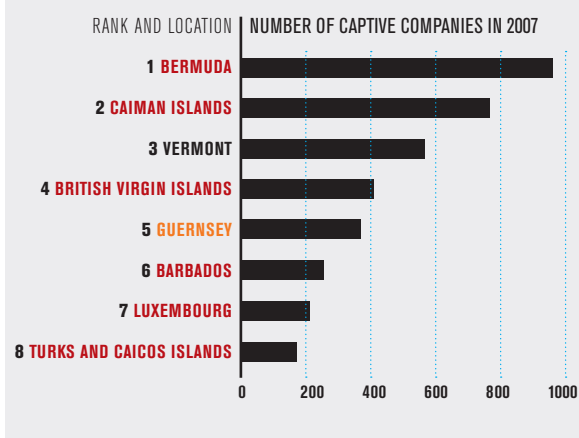
4 Tax-News, *CIMA Chief urges finance sector to up its game*, February 8th 2008.

5 This is the number put forward on October 7th 2010 by François Asensi, the French Deputy, quoting the impact assessment study of the draft "tax information exchange agreement" between France and Antigua.

6 Online betting is currently authorised in Ireland, Lithuania, Latvia, Estonia, Bulgaria, Slovakia, Malta, the United Kingdom and France, and is currently under review in Italy, Belgium, Denmark, Spain, Austria, the Czech Republic, Poland and Romania. Source: *La Croix*, June 8th 2010.

7 This paragraph is largely based on Richard Murphy's "Google's Taxes Under The Spotlight", December 21st, 2009, <http://www.taxresearch.org.uk/Blog/2009/12/21/>

DOMICILIATION OF CAPTIVE INSURANCE COMPANIES³



THE GOOGLE AFFAIR?

Google, a US company, located its European Head Office in Dublin, where corporate income taxes are low. That is not all: Google Ireland is owned by a company based in Bermuda, where corporate profits are not taxed. The company is highly profitable, generating total world-wide profits of €4.68 billion on turnover of €17.44 billion in 2008, i.e. a profit margin of 26.8% (post-tax).⁸ Google declares 14% of its sales, or €2.44 billion, in the United Kingdom. According to Richard Murphy, an accountant who campaigns against tax avoidance,⁹ if Google's profit margin across the Channel was the same as its profit margin world-wide, "Google would have made a profit of €654 million* [on which] it ought to have paid €186.4 million* in taxes in the United Kingdom" (corporate tax rate of 28.5%). In fact, an investigation conducted by Terry MacAlister in 2009 caused a scandal in the United Kingdom: according to *The Guardian* newspaper, "Google is believed to have paid only €880,000* to the UK tax authorities"¹⁰ and even less according to Richard Murphy, who estimates that the payment was only €208,000, and

wonders what might have enabled Google to pay so little tax: "I suspect that Google Ireland pays Google Bermuda for use of Google's technology."¹¹

London is not the only loser. Subsequently, in January 2010, France's president, Nicolas Sarkozy¹² also singled out Google's¹³ practices and invited the French Finance Ministry to "open an investigation as soon as possible, so as to understand the tax position of the advertising activities conducted by the major portals and search engines present in the French market. Currently, these companies are taxed in the country where their head office is based, although they are taking a significant share of our advertising market. This is called tax flight and it is particularly harmful". At the European level, a Community directive on "intra-community services" was adopted in 2008, in order to stem VAT avoidance. From 2015 onwards, the rate of VAT will not be that of the country where the website is located, but the rate in the country where the customer lives.

* Conversion made by the authors (amounts initially given in dollars)

... casino. The money is then clean. Today, the recent expansion of virtual casinos or cyber-casinos, whose websites are domiciled in certain tax havens, is also supporting these laundering activities. It is impossible to trace the source of the money, since criminals use a plethora of internet addresses and mirror sites that are tangled up with one another, sit on top of one another and are often based in countries where information technology legislation is very flexible".¹⁴

ONLINE RETAIL SITES

Luxembourg wins the European trophy for the country sheltering the highest number of online retail sites. Although Google chose Ireland (see box), PayPal, the world leader for online payment services, can be found in the Grand-Duchy, alongside eBay, Amazon, iTunes (Apple group), and even Skype. These companies, which are leaders in their sector, use Luxembourg to localise the profits generated by their activities throughout Europe. For instance, Ernst and Young, the accountancy firm, praises the "favourable environment for economic players" created by the Luxembourg government, which not satisfied with already having the lowest VAT rate in Europe (15%), lowered it to 3% "on digital television and entertainment services, and some copyrights" and "introduced a tax

measure allowing the exemption of 80% of copyright royalties on computer software, licences, manufacturing or trade brands, and on registered drawings or models." The aim is "to increase the attractiveness of Luxembourg in the new technology sector".¹⁵

CYBER-SEX

Tuvalu, a Pacific Island officially headed by Queen Elisabeth II of England, is the least populated country in the world, after the Vatican, but is also the leading player in the online sex market. That market amounted to US\$2 billion in world-wide revenues in 2005.¹⁶ In theory, cyber-sex revenues are split between the country where the call is made and the country where it is received. The strategy of the tax havens, which rent low-cost telephone lines, "consists in acting as an intermediary for those phone calls. Calls between countries are diverted to these territories, which are therefore able to capture part of the cost of the call."¹⁷ Their low number of inhabitants enables these countries to offer 3 to 4 digit numbers, which are highly prized by specialist companies.

FLAGS OF CONVENIENCE

Liberia and Panama vie for first place in the flags of convenience

market, followed by the Bahamas, Malta and Cyprus.¹⁸ "Panama offers ship owners rapid registration and favourable legislation, including a guarantee that they will not be bothered in the event that they fail to comply with international regulations. Several thousand shell companies are based there. Liberia is the number two player in the flags of convenience market, although it has to be said that a number of the ships have never seen its shores".¹⁹ In other words, these tax havens allow ships to be registered in territories where there are few constraints in terms of tax, safety or employment rights ○

googlestaxes- under-the-spotlight/

⁸ Richard Murphy *op. cit.*

⁹ Richard Murphy is also the co-author of "Tax Havens. How Globalization Really Works", *op. cit.*

¹⁰ T. MacAlister, « Google is accused of UK Tax Avoidance », *The Guardian*, 20 April 2009.

¹¹ From « Google's Taxes Under the Spotlight » *op. cit.*

¹² In "Voeux au monde de la culture", a speech given by Nicolas Sarkozy, on January 7th 2010, <http://www.elysee.fr/president/les-actualites/discours/2010/voeux-au-monde-de-la-culture.1618.html>; V. Collet "Nicolas Sarkozy stigmatise Google", in *Le Figaro*, January 7th 2010.

¹³ N. Sarkozy: "We are going to ask the Competition Authority for an opinion on the potentially dominant position that Google has acquired in the online advertising market", *op. cit.* Our translation.

¹⁴ É. Vernier, *Techniques de blanchiment et moyens de lutte*, Dunod, p. 65, 2008. Our translation.

¹⁵ Bart Van Droogenbroek (Ernst & Young Luxembourg), « Le Luxembourg comme site d'implantation d'activité IT - Quels avantages, quelles stratégies ? », *Letzebuurger Journal*, March 23rd 2010.

¹⁶ *Op. cit.* Inquiry report of Finance Commission in French Parliament, D. Migaud, September 10th 2009.

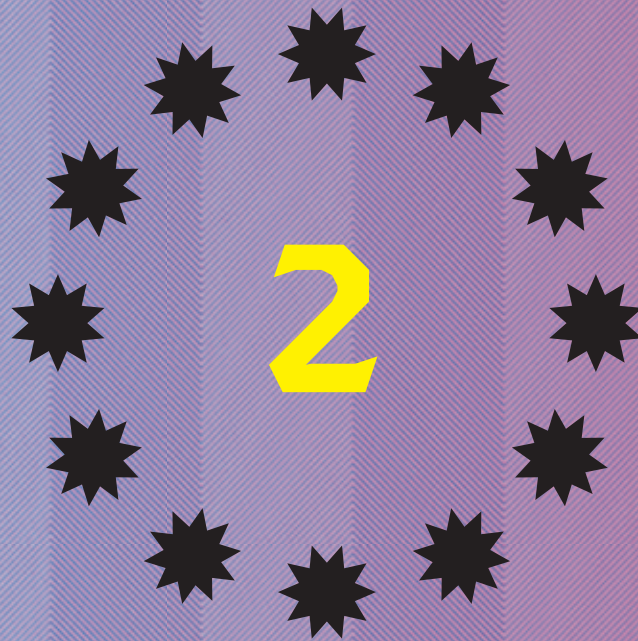
¹⁷ ICD London, « Paradis fiscal : l'ampleur du phénomène offshore ».

¹⁸ A. de Ravignan, « Une marine très complaisante » *Alternatives Economiques* n° 246 - Avril 2006.

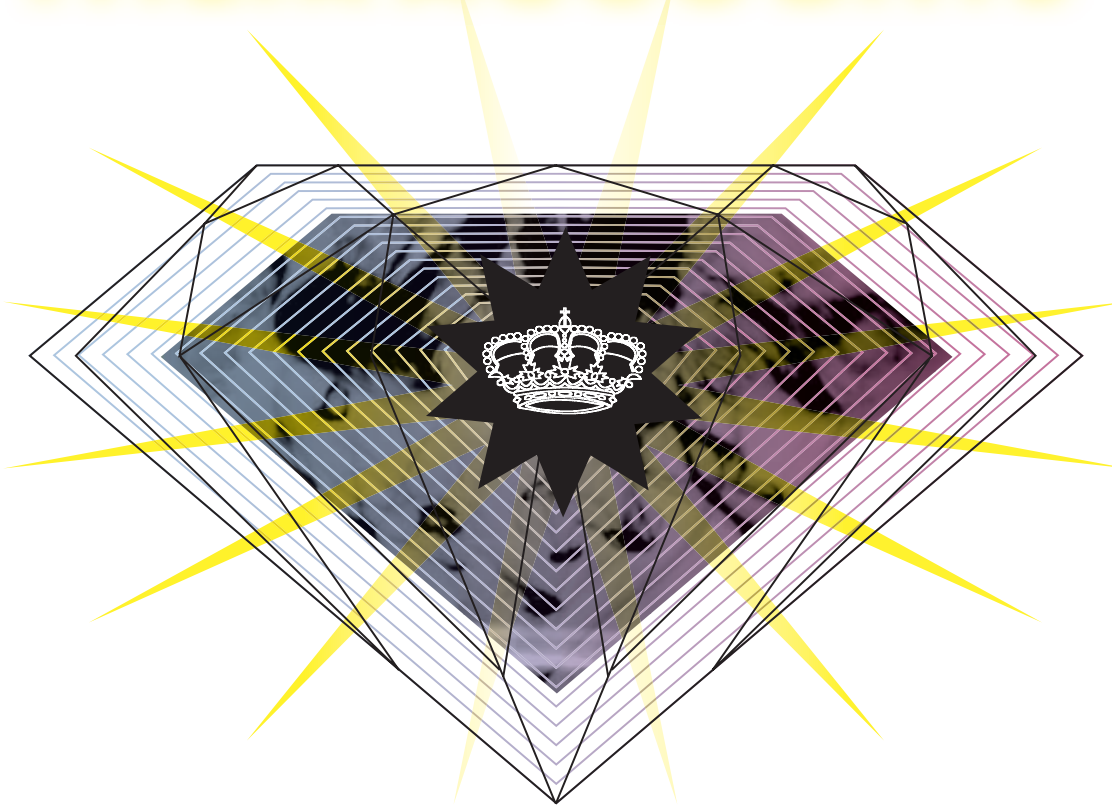
¹⁹ Information report on tax havens issued by the Commission des Finances, de l'Économie Générale et du Contrôle Budgétaire (French Finance, General Economic and Budget Monitoring Commission), *op. cit.*, p. 73. Our translation.



CHAPTER



MULTINATIONAL COMPANIES SETTLING THEIR ACCOUNTS



ECONOMIC STATISTICS ARE A VERY POOR REFLECTION
OF THE REAL ECONOMY. MULTINATIONAL COMPANIES
AND THEIR ADVISORS, WHO REDRAW THE GEOGRAPHY OF GLOBAL
WEALTH AS IT SUITS THEM,
ARE AT THE HEART OF THE SCAM. THEY MAINTAIN A CLOAK OF SECRECY
AROUND THEIR FINANCIAL STATEMENTS.

REFERENCE POINT

GLOBALISA- TION HEAVY- WEIGHTS

Multinational companies dominate whole sectors of the global economy. To mention just a few sectors, the world's civil aviation is mostly dominated by Boeing and Airbus, while 94% of the global military aviation market, 86% of the global banana market and half the green coffee beans sold world-wide are all in the hands of five companies. Many multinational companies have ultimately become more powerful than many Governments. The combined revenues of the 10 largest companies exceed the combined GDP of India and Brazil! The revenues of the 50 leading European companies accounted for 22% of the wealth created (GDP) in the European Union in 2010...



MULTINATIONAL COMPANIES AND TAX HAVENS:

silence is golden

WE HAVE STUDIED THE DATA THAT THE 50 LEADING EUROPEAN COMPANIES DISCLOSE TO THE PUBLIC REGARDING THEIR OPERATIONS IN TAX HAVENS,¹ AND HAVE TRIED TO UNDERSTAND THE REASONS FOR THEIR PRESENCE IN THOSE TERRITORIES. THIS EXERCISE IS MUCH MORE COMPLICATED THAN IT APPEARS.

In theory, it is not a crime for an international group to conduct business in the Netherlands, Switzerland or even the Cayman Islands. For example, it is perfectly legitimate for an insurance company to have clients who reside in the Cayman Islands, and to open a subsidiary intended for them. However, if that were the case, the insurance company could easily account for its presence in the Caribbean and its business volumes there in its annual report. It is when the information is not available, particularly in territories that are renowned for their secrecy, that offshore operations become suspicious. Here are the main conclusions of our study:

1. INFORMATION IS HARD TO ACCESS

In most European countries, there is no way that a citizen or a shareholder can be certain about the existence and location of all the subsidiaries of a major European group. For example Tesco, which is based in the United Kingdom, lists only its “principal subsidiaries”,² (26% of which are in tax havens)³, as do Repsol, based in Spain,

ArcelorMittal in Luxembourg and EADS in the Netherlands. You cannot really rely on a company’s website to understand. Some groups put their annual report, which is intended for their shareholders, online, although others content themselves with providing partial information. For example, the Royal Bank of Scotland (RBS) lists eight subsidiaries on its website, compared with 1,110 at Companies’ House. To confuse matters a little further, some companies list subsidiaries on their websites that are not mentioned in their annual report, and vice versa. For example, the Société Générale website mentions four subsidiaries in Switzerland and three in Luxembourg, but when you read the 2009 annual report, you come across two subsidiaries in Switzerland and 10 in the Grand Duchy! One difference in the United Kingdom is that you need to spend one pound sterling to access an annual report.

2. EVERY MULTINATIONAL HAS A PRESENCE IN A TAX HAVEN

Among the 50 leading European companies, two (Lloyds and Bosch) do not provide sufficient information on

REFERENCE POINT

FIGURES CORRESPONDING TO EUROPE’S 50 BIGGEST COMPANIES
> €138 billion profit in 2009
> €3,500 billion turnover in 2009
> 15 German companies,
11 French,
8 British,
5 Italian,
3 Dutch,
2 Spanish,
2 Swiss,
1 from Luxembourg,
1 from Norway,
1 Swedish
and 1 Belgian.

¹ Each company’s annual reports and websites, and Trade Registry declarations.

² “Principal subsidiaries”, list available in the company’s 2009 annual report.

³ Our calculation.

METHODOLOGY CLARIFICATIONS

The 50 companies selected: we chose the 50 leading European companies (outside Russia) in terms of their revenues (three-year average, between 2007 and 2009), based on the rankings drawn up by *Fortune Magazine*, the US publication.⁴

Sources: the study that we conducted is based on the shareholder information available in the annual reports published by these companies, which can often be consulted on the company's website and/or at the trade registry in the country where the company's head office is located. All the reports relate to the 2009 financial year, except in Allianz's case, where only the 2008 report was available. Please note that Bosch, the German company that is included in the top 50, is not listed, and is not, therefore, under the same obligation to deliver public accounts to its shareholders. We tried to find out whether the business activities, profits, the number of employees and the taxes paid were disclosed for each listed subsidiary (an entity where the parent company has a stake of at least 50%).

List of tax havens: we selected the 60 territories listed by the Tax Justice Network (TJN) as part of its financial secrecy index (see page 7). However, the absence of some "new" tax havens, like Ghana, should be noted, as should the fact that, since the index dates from November 2009, a country like Belgium would probably see a decrease in its opacity score (73%) after agreeing to the automatic exchange of tax information in 2010 within the framework of the European Savings Directive. In order to calculate the number of subsidiaries that each company has in tax havens, we excluded those in the country where the company has its head office, even though the choice of head office location may be a function of tax considerations, as in the case of EADS in the Netherlands or of ArcelorMittal in Luxembourg. In addition, we did not include subsidiaries in the United States or the United Kingdom (see box on the "Anglo-American bias" on p. 26).

... where their subsidiaries are located for us to be able to take a view on whether they have a presence in tax havens. The 48 others do have a presence in those territories, where they admit to 4,748 subsidiaries between them, i.e. 21% of all their subsidiaries. In other words, these 48 European multinationals have around one hundred subsidiaries each, on average, in tax havens. That number would reach 150 or even 200 per group if we added subsidiaries in the United Kingdom and United States.

3. NONE OF THEM EXPLAINS EXACTLY WHY

None of the 50 major European companies fully explains the reasons behind their tax haven operations in their annual report. If such an explanation was available, we could make a distinction between genuine business activities and tax optimisation. However, although some do better than their competitors (see below), none of the 50 major European multinational companies explains the business that they conduct in their subsidiaries, either for each subsidiary or for

each country where they operate, in terms of the nature of their business, their revenues, the profits generated, the number of people employed and the taxes paid. Since January 1st 2005, the consolidated financial statements of listed European companies must be drawn up according to the international IAS/IFRS⁵ standards established by the IASB,⁶ which are mandatory within the European Union. These standards were drawn up first and foremost to satisfy investors' expectations, so that they could compare different companies.

4. GERMANY MAKES A BIT MORE EFFORT

In France, a law introduced in June 2009⁷ requires banks to publish accurate financial information regarding their operations in tax havens. French banks have issued a large amount of information on the issue, including information on the closure of certain subsidiaries. It remains that the list of tax havens mentioned by the law, which was drawn up by the Finance Ministry, only included 18 territories in 2010, accounting for just 0.2% of

the global offshore finance market! Germany is the only country that is home to major European groups where listed companies are required to comply with additional financial transparency obligations. Companies' annual reports must include an appendix with a list of their subsidiaries that specifically provides the following information: the name and location, the amount held in and the profits generated by companies in which they have a stake of over 20%.⁸

However, there are exceptions that weaken the scope of this obligation.⁹ This is the case when a company considers that the information is damaging for its subsidiary or for itself, or views it as "non-significant". It is up to those responsible for preparing the information to assess whether the nature of that information is significant, depending on its relevance and its significance in terms of the group's net asset and financial position, etc. BMW, for instance, only lists 41 of its subsidiaries, and argues that the others involve intangible items. However, it is precisely these intangible items, via which value is transferred offshore, that require an explanation.

⁴ All the comments included in this report do not just apply to those 50 companies. When this is the case, we expressly mention the "50 leading European companies" or the "50".

⁵ *International Accounting Standards / International Financial Reporting Standards*.

⁶ *The International Accounting Standards Board*, which draws up the accounting standards for over 100 countries.

⁷ The law relating to the merger between the Banque Populaire and the Caisses d'Epargne.

⁸ Law: *Handelsgesetzbuch (HGB)* paragraphs 264, 285 and 289 a.

⁹ HGB paragraphs 286.3.1 and 286.3.2.

THE ANGLO-AMERICAN BIAS

The United Kingdom and the United States are respectively indebted to the City of London and to some US States like Delaware (see box p. 36) or Nevada for their high rankings among the 60 territories listed by TJN. However, the presence of a substantial number of subsidiaries belonging to European groups in these countries is explained first and foremost by the size of their respective markets. Taking all these subsidiaries into account would have significantly inflated the numbers in our study, to the point where the rest of the information that we have gathered would have been drowned out. We have tried to identify only those subsidiaries in London and in the most opaque US states, although the way in which companies provide information on where their subsidiaries are located is too random in some cases – and only 27 provide it. We have therefore excluded those countries from the scope of our study.

5. DON'T RELY ON A GOVERNMENT SHAREHOLDER TO GUARANTEE TRANSPARENCY

The fact that a Government holds a stake in a company does not mean increased transparency: although EDF (which is 84% owned by the French Government) and RBS (which is 84% owned by the British Government) do rather better than their competitors as far as specifying the business activities of each of their subsidiaries is concerned,¹⁰ Lloyds Bank, in contrast, appears to be hiding behind the 41% stake held by the Government to issue as little information as possible. Aside from the specific case of German companies, there are few European companies that demonstrate a will to explain the reasons behind their operations on a country-by-country basis. The only company that goes one step further is a private French company, namely Saint-Gobain, which does, in fact, provide total revenue and employee numbers for most of its subsidiaries and, where applicable, for the subsidiaries of its subsidiaries. In addition, we note that all the subsidiaries have employees, except for Saint-Gobain Nederland, a finance subsidiary located in the Netherlands, and for the Group's Swiss and Dutch holding companies.

6. THREE COMPANIES THAT ARE MASTERS OF SECRECY¹¹

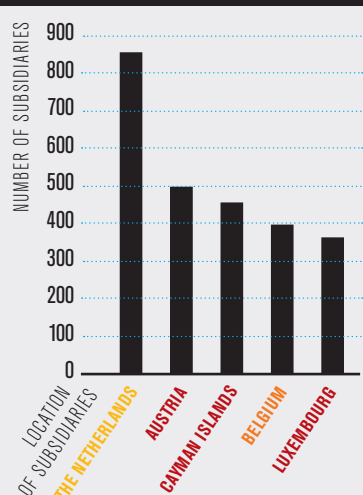
There are three multinational companies that provide almost no information on their subsidiaries. Lloyds Banking Group, the British bank, lists only eight subsidiaries, none of which is based in a tax haven. Total, the French oil and gas giant, only provides a name for 217 subsidiaries among the 712 that are consolidated in its annual financial statements, without even indicating the place where they are located: shareholders are forced to guess the location from the name of the subsidiaries.¹² Robert Bosch, an unlisted company, uses exceptions in force in Germany to reveal nothing about its subsidiaries, which amount to over 300, in its annual report. Finally, we would remind you that Allianz, the German insurance company, did not make its 2009 annual report public.

¹⁰ Repsol and Peugeot adopt the same method.

¹¹ According to the Oxford English Dictionary (2010), the term means "not able to be seen through, not transparent, or difficult or impossible to understand". TJN, meanwhile, has developed an opacity score that applies to different territories (see p. 7).

¹² See pp. 266-67 of the annual report at http://www.total.com/MEDIAS/MEDIAS_INFOS/3242/FR/2009-documentreference-vf.pdf. Shareholders can also cross-check the information with the map of countries where Total operates (including the Virgin Islands), which is shown in a press release at: http://www.total.com/MEDIAS/MEDIAS_INFOS/3331/FR/Total-2009-essentiel-vf.pdf.

THE 50 LEADING EUROPEAN COMPANIES' FAVOURITE TAX HAVENS



7. THE DUTCH ACHIEVEMENT

Among the 60 tax havens that we examined, a handful is markedly more attractive than the others: the top 10 account for around 80% of the subsidiaries identified. Unsurprisingly, European countries take pride of place, even if the popularity of the Cayman Islands should be mentioned, particularly with banks (Barclays owns 168 subsidiaries there and Deutsche Bank 137), and to a lesser extent, the popularity of Hong Kong (9th), which is home to 202 subsidiaries, including 49 owned by E.ON and 29 owned by Tesco. The Netherlands alone, where each of the 50 leading European groups has around 20 subsidiaries on average, account for

... 18 % of the subsidiaries located in tax havens. Aside from Royal Dutch Shell, which has its head office there, the Netherlands appeal particularly to European oil and gas giants. BP, Total, ENI, Statoil, and Repsol have 161 subsidiaries there, i.e. a third of all the subsidiaries that they declare in tax havens. Aside from the privileged status of holding companies under Dutch law, a good portion of these subsidiaries undoubtedly conduct genuine business operations in the country, which is the world's 16th largest economy. It remains that only the publication of detailed financial statements for each country, or for each subsidiary, would enable readers to verify that the activities of the 20 Dutch subsidiaries owned by each major European group, on average, are genuine. The same goes for their eight Luxembourg subsidiaries. Finally, we should specify that taking London and Delaware into account would have substantially altered our rankings. The 27 companies in our study that specify where their operations are located in the United States and the United Kingdom list 662 subsidiaries in Delaware and 335 in London. Deutsche Bank, in particular, has no less than 459 subsidiaries in Delaware and 173 in London; between them, both territories account for 40% of the German bank's subsidiaries.

8. 363 SUBSIDIARIES IN THE WORST TAX HAVENS

Some tax havens are even more suitable than others for enabling a company to conceal its business activities. In fact, there are 33 territories that the *Tax Justice Network* (TJN) describes as having an opacity score of over 90%. The 50 leading European companies admit to having 1,713 subsidiaries in these black holes of the world economy! Worse, they declare 363 subsidiaries in the 13 territories 100% secretive listed by TJN (this includes 234 subsidiaries in Switzerland and 54 in Bahamas). Generali, the Italian insurance company, actually declares 26 subsidiaries in Switzerland and 10 in the Bahamas, while BP declares 58 subsidiaries in territories with a 100% opaqueness ratio and 153 in 12 countries where the opacity score is above 90%. We would like these companies to provide an explanation.

9. NATIONAL PREFERENCES

For reasons of geographical proximity, or historical, linguistic or legal reasons, the practices of multinational companies vary from one country to another. Among those featuring in the European top 50, British multinationals display a preference for the Cayman Islands, while the attractions of their Belgian neighbour are French multinationals' first port of call. Meanwhile, German companies prefer Delaware and Italian companies choose Austria. The Netherlands' financial centre is in permanent second place. We should specify that these rankings, which are based on a narrow sample of companies, only provide a vague indication of each country's appeal. For instance, Switzerland does not feature among the three destinations favoured by the 11 French companies in our study, although it ranks second if we look at the 40 leading French companies.¹³

10. THE BANKS ARE IN THE LEAD...

... in terms of the number of subsidiaries in tax havens (and BP, which has 332 subsidiaries, is right beside them). Among German multinational companies, Deutsche Bank is the largest tax haven client by far, with 446 subsidiaries in tax havens, notwithstanding its 632 other subsidiaries in London and Delaware! Among British companies, Barclays has 383 "tax haven" subsidiaries (i.e. 36 % of all its subsidiaries). The French BNP-Paribas Group, which has 347 tax haven subsidiaries, is tied with the Italian Unicredit group and its 345 subsidiaries. One thing is certain: the 17 banks and insurance companies that we studied prefer the sunny climes of the Cayman Islands, where they have 417 subsidiaries, to Austria (330) and Luxembourg (249)! In other words, the leading European bank and insurance companies have 25 subsidiaries each, on average, in the Cayman Islands...with Barclays, which has 168 subsidiaries there, in the lead. It would be hard to explain the financial sector's fascination with the Cayman Islands based solely on the local clientele ✱

REFERENCE POINT

IT IS CURRENTLY IMPOSSIBLE TO ESTABLISH A RELIABLE RANKING OF OPAQUE COMPANIES

We have tried to identify those among the 50 leading European companies that have the most to hide in tax havens. This ought to serve as an invitation for rating agencies to take this phenomenon, which they currently completely ignore, into account, even though it represents a considerable financial, legal and reputational risk for major companies. However, the information currently available to the public is so sketchy that it makes such an exercise too unpredictable.

The main weakness of our methodology is that any attempt to rank the companies based on these public information sources remains dependent on the dubious quality of the information available in companies' annual reports. If, for example, we had relied on the number of operations in tax havens, combined with the level of secrecy in each of those territories, we would have been in danger of awarding the top rankings to the companies that display the most transparency about their significant offshore operations, and of paradoxically rewarding some groups that have a very large offshore presence, although they hardly mention it in their annual report. We have therefore given up trying to rank the companies in this way. Ultimately, only country-by-country or even subsidiary-by-subsidiary transparency in corporate financial statements will dispel any doubts about the reality of the business being conducted and enable companies to be ranked.

"We must be able to come to a consensus among ourselves regarding reporting [on a country-by-country basis]".

Jean Arthuis, Chairman of the French Senate Finance Commission, November 4th, 2010.¹⁴

¹³ A survey of CAC40 companies published by *Alternatives Economiques* in March 2009

¹⁴ See François d'Aubert's testimony before the Senate Finance Commission. Jean Arthuis, a member of the Union Centriste group, was the Juppé government's Finance Minister between 1995 and 1997. Our translation.



SWEDEN



BELGIUM



SWITZERLAND



LUXEMBOURG



NORWAY



ITALY



THE NETHERLAND

853

IRELAND 305

CAYMAN ISLANDS 453

ISLE OF MAN 36

GUERNSEY 62

JERSEY 145

MONACO 13

ANDORRA 1

GIBRALTAR 16

PORTUGAL (MADEIRA) 112

LIBERIA 3

BAHAMAS 54

TURKS AND CAICOS ISLANDS 1

BERMUDA 60

BRITISH VIRGIN ISLANDS 37

US VIRGIN ISLANDS 5

ANTIGUA AND BARBUDA 1

DOMINICA 1

SAINT LUCIA 1

BARBADOS 11

BELIZE 1

ARUBA 1

NETHERLANDS ANTILLES 10

COSTA RICA 25

PANAMA 37

URUGUAY 24

WHAT ARE THEY RE

Where the 50 leading European

FRANCE



SPAIN



THE NETHERLANDS



GERMANY

DAIMLER



BELGIUM
394

LUXEMBOURG
360

SWITZER-
LAND
234

AUSTRIA
495

HUNGARY
281

HONG
KONG
202

Delaware (United States)
and London (United
Kingdom) are not featured,
as the information available
is too fragmented
(see box p. 26).

LATVIA 15

LIECHTENSTEIN 7

CYPRUS 25

LEBANON 5

MALTA 34

ISRAEL 79

BAHRAIN 4

UNITED ARAB EMIRATES 58

MACAO 2

PHILIPPINES 33

BRUNEI 1

MALAYSIA (LABUAN) 57

SEYCHELLES 1

SINGAPORE 125

VANUATU 1

MAURITIUS 42

ALLY DOING THERE?

companies' tax haven operations are located



**MR. WHITE,
CHIEF FINANCIAL
OFFICER OF A MAJOR
EUROPEAN GROUP¹**

What does a multinational company do to avoid taxes?

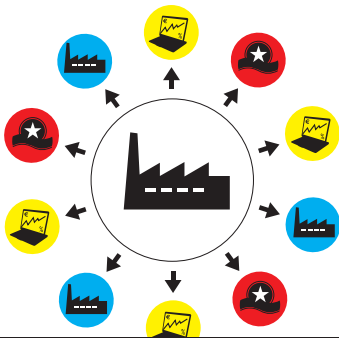
Half of global trade is intra-group trade. You can re-invoice a foreign subsidiary not only for a physical asset, but also for the right to use the company's patents and brands. We try to attach the highest value possible to these intangible assets. Let's say I sell you a beer. I break down the beer into several items: the container, the contents, a brand, drawings and designs, the shape of the bottle, etc. There are products where I have to apply the OECD arm's length principle and charge the price that I would charge for comparable products. But what is the right to use my brand worth? I therefore take the view that the container is worth 1 cent, that the brand is extremely expensive (€2.00 per litre sold) and that the design is worth €0.50. By applying this mechanism, what crosses the border has a derisory value, while the value of the brand will be huge and enable us to locate the lucrative item where we want. We have reached the point where some companies set themselves up with no factories, since manufacturing is no longer a problem once you are able to reap rich rewards from intangible assets. If I ask investors for cash, I need to pay them in return. I would be mad to ask them for capital to manufacture bottles that make me 0.5% while the brand makes me 100%. It is better for me to cut my business down to intangible assets and pay my investors.

Why is there not more of a clampdown on tax avoidance by multinational companies?

A finance director who is seeking to locate profits in a country with lower taxes is always one step ahead of any potential tax inspector. Analytical accounting allows me to work out the cost price of a product, to determine my transfer prices and to assign value to brands and rights. However, this accounting exercise is not compulsory, and is therefore not accessible to the tax inspector. Another difficulty faced by the tax inspector is borders. If the Indian tax authorities ask me to

DISJUNCTURE: INSTRUCTIONS FOR USE

How do you break up value?



1 YOU ARE A SINGLE COMPANY WANTING TO DESIGN AND SELL A PRODUCT? SET UP 10 SUBSIDIARIES (FACTORIES, PURCHASING, FINANCIAL SERVICES, LEGAL ADVICE, INSURANCE, MARKETING, ETC.).

2 RELOCATE THE SUBSIDIARIES THAT HANDLE INTANGIBLE ASSETS (THE EASIEST ONES TO MOVE), BY CHOOSING THE MOST ATTRACTIVE TAX OPTION: LUXEMBOURG FOR FINANCING COSTS, THE CAYMAN ISLANDS FOR THE PURCHASING DEPARTMENT, IRELAND FOR THE BRAND, ETC.



3 TAKE ADVANTAGE OF ALLOWANCES AND OF SPECIAL ECONOMIC ZONES, AND NEGOTIATE TAX BREAKS IN THE PLACES WHERE YOUR RAW MATERIALS, FACTORIES AND RETAIL MARKETS ARE LOCATED.

4 USE ARTIFICIAL MEANS TO MOVE CAPITAL GAINS TO OFFSHORE SUBSIDIARIES SPECIFICALLY THROUGH MAXIMISING INTANGIBLE ASSETS (VIA TRANSFER PRICING, DEBT TRANSFERS AND FALSE INVOICES).



justify the prices of products that I sell to India, I can justify them as I want: the Indian tax authorities are not going to come and start proceedings against me! And they will never receive any help from the French tax authorities, who obviously see the asymmetrical advantage. The Indian tax authorities can launch an enquiry regarding the Indian subsidiary, but they would need to have proof. However, it is not the Indian subsidiary that is being called into question, but me. I am the person who determines the yardsticks that enable me to justify my own prices.

Where is the line between legal and illegal practices?

The law is not well drafted. It is so flexible that you cannot criticise a tax optimisation consultancy for using it to its best advantage, or a company for looking out for its clients or shareholders. Undoubtedly, the differences between national standards enable companies to play on them and to optimise their net income. The result is pressure on governments to reduce taxation. Ultimately, it is their funding that is involved. However, if I do not overstep the wording of the law, if no one can prove that my behaviour is illegal, that's because it isn't. We are running virtually no criminal risk. Tax enquiries are frequent, but come down to negotiations based on much lower tax bases. When the amounts are significant, these issues are quickly escalated to the diplomatic level. It ends up fiscal horse-trading between governments.

Is publishing financial statements on a country-by-country basis technically feasible?

From a technical and administrative standpoint, 90% of the world's multinational companies could do it in five minutes. But it is pointless asking a company to do anything of the kind: it would never be in its interest to do so.

Interview by Jean Merckaert and Cécile Nelh
Our Translation

¹ The name has been changed as our interviewee preferred to remain anonymous.

DISCONNECTING STRATEGIES

MANIPULATING TRANSFER PRICES, RELOCATING DEBT AND PROFITS, BLACK BOXES AND OTHER KICKBACKS, ETC.

THERE IS NO SHORTAGE OF METHODS AND MOTIVES FOR MULTINATIONAL COMPANIES TO RELOCATE THEIR BUSINESS ACTIVITIES VIRTUALLY.

MANIPULATING TRANSFER PRICES

Transfer prices, which are set by the multinationals themselves, in order to invoice exchanges of goods or services between their subsidiaries, are the favourite disconnect channel.

When questioned about transfer pricing as he left the Elysée in 2009, Alain Joyandet (who was the French Secretary of State for Development Cooperation and Francophone Countries at the time), caught by surprise in front of the France 3 journalists: *"Isn't that money earned by migrants?"* was his comment. Bernard Kouchner (who was the French Minister for Foreign and European Affairs at the time), at least had the decency to hide his ignorance.¹ In defence of both men, the concept of transfer prices, which multinationals set for transactions between different entities within the same group, seems complicated, and the debate tends to be restricted to specialists, away from the public arena. However, as far as politicians are concerned, it has become a core issue for global trade and the world economy, since intra-group trade now represents between 50% and 60% of global goods and services transactions.² It is also a crucial issue for developing countries.

Eva Joly, a member of European parliament, reported, for example, that *"Zambia was using Mauritius to export its copper. The subsidiary located on the island was buying copper from Zambia at €2,000 per tonne, in order to resell*

¹ In the "Pièces à Conviction" [Incriminating Evidence] programme broadcast on France 3 on November 16th 2009.

² See footnote 1 p. 18.

... it at €6,000 per tonne. It could locate the €4,000 gain in the Mauritian subsidiary...as an untaxed profit. In this scenario, the Zambian Government did not receive a dollar in taxes.”³

Finally, Zambian copper exports were heading in the direction of Switzerland, which started to import over half of them in 2008, although it only accounted for 10% of the outlets four years earlier.⁴ It is also thanks to the transfer pricing method that the three largest banana trading companies in the world, namely Dole, Chiquita and Fresh Del Monte, were only taxed at a rate of 14% on their profits between 2002 and 2007, without any bother from the law, although their parent companies are actu-

KPMG :

“They [our team.] take a larger view and look beyond the present to help you establish policies to that can make your transfer pricing commercially viable and tax-efficient.”⁵

January 2008

ally registered in the United States, where the corporate tax rate is 35% (see p. 17). In the early 1990s, when Raymond Baker carried out a study on the differences between market prices and those practised between the entities of the same multinational company, based on 550 interviews with Chief Executives, managers and commercial directors in 11 countries,⁶ he arrived at some irrefutable conclusions: inconsistencies were recorded for between 45% to 50% of commercial transactions originating from Latin America. That proportion reached 60% for Africa. The average difference with the price that ought to be charged was over 10% in Latin America, and over 11% in Africa.⁷

OECD member countries have actually acknowledged the problem. *“Businesses of all sizes have created shell companies offshore to shift profits abroad often taking recourse to over or*

REFERENCE POINT

125 BILLION STOLEN FROM DEVELOPING COUNTRIES
Christian Aid, the British NGO, believes that transfer price manipulation and false invoicing by multinational companies cost developing countries around €125 million in tax revenues every year, or the equivalent of the amount required to save the life of roughly 350,000 children under five.⁸ The kickbacks and commissions that often go with these practices are hidden in anonymous bank accounts.

undervaluation of traded goods and services for related party transactions and some multinational enterprises (including financial institutions) have used more sophisticated cross-border schemes and/or investment structures involving the misuse of tax treaties, the manipulation of transfer pricing to artificially shift income into low tax jurisdictions and expenses into high tax jurisdictions which go beyond legitimate tax minimization arrangements.” (OECD Seoul Declaration, September 14th and 15th 2006).

THE LIMITS OF THE “ARM’S LENGTH” PRINCIPLE

Intra-group trade is governed by the principle known as the “arm’s length” principle, as defined by the OECD. In the event of a dispute between a multinational and a tax authority, the principle refers the parties to what the price would be if the transaction was being performed between two companies that are not subsidiaries of the same group (Article 9-1 of the OECD Model Tax Convention). The OECD regularly publishes a thick handbook intended for companies and tax authorities, in order to show how to calculate this arm’s length price (see box). However, these rules are hard to apply. When there is an international market that sets real-time prices, as is the case for raw materials, it is possible for tax authorities to identify major discrepancies in the invoices issued between subsidiaries. In contrast, when there is no such market, the methods recommended by the OECD can be interpreted very freely by multinational companies. For instance, the increased cost price (“cost plus” in financial speak) consists in calculating the cost price of the goods or service and adding a profit margin, defined according to “comparables” used in-house by the company or to external ones. Why, therefore, would the company not apply a “cost plus five” (5% margin) in cases where the real margin is 20%? In fact, Max de Chantérac, the finance director of a subsidiary within a French industrial group, believes, as does François d’Aubert, who chairs the Global Tax

³ Interview in *Libération*, May 18th 2009.

⁴ A. Cobham, *Tax Havens, Illicit Flows and Developing Countries*, during a conference at the World Bank, March 2010, p. 29.

⁵ <http://www.kpmg.com/Ca/en/WhatWeDo/Tax/InternationalTaxServices/Pages/TransferPricing.aspx>

⁶ United States, United Kingdom, France, the Netherlands, Germany, Italy, Brazil, India, South Korea, Taiwan and Hong Kong.

⁷ R. Baker, *Capitalism’s Achilles Heel*, 2005, Wiley, pp. 170-171.

⁸ Christian Aid, *Death and taxes: The True Toll of Tax Dodging*, May 2008, p. 3.

- Forum group non-cooperative territories assessment group, that “[the OECD rule] makes it easy for a multinational to put together all sorts of arguments, so as to limit competition to situations that suit it, and therefore exclude any comparable company, whose prices would invalidate its own transfer prices, from the concept of “arm’s length”.

Indeed, it is hard for the tax authorities to access a company’s analytical accounting records, which provide information on the way the company breaks down its fixed and variable costs, and determine the internal cost price of its products. Moreover, in France, for example, it is up to the authorities to prove that the transfer price charged is contentious under the OECD rules. The fact that international tax cooperation on transfer pricing is hard does not make matters easier. The problem is both practical (there is no means of investigating the financial statements of another subsidiary involved in the transaction) and political: the legal argument over transfer pricing is part of a heated battle between Governments regarding the location

of the tax base represented by a company’s profits.⁹

THE INTANGIBLES TANGLE

Finally, as Max de Chantérac explains “the practice of transfer pricing increasingly involves products that are not tangible, but intangible, like patents, technology and brands. However, it is extremely hard to gauge the price of these intangible concepts. Moreover, the law leaves a lot of room for interpretation in this area”.¹⁰ Among intangible assets, we can specifically identify the following:

Intellectual property rights

How much is a brand, a patent or a licence actually worth? What is much harder to work out is the value of the product that is “derived from an intangible asset”, according to Mr de Chantérac’s description, namely the right to dispose of or use a patent, a technology or a brand. In such an environment, it becomes very easy for a finance director to shift an important portion of the value generated to tax havens. The Italian press recently reported the fact that

Dolce&Gabbana’s practices were called into question at the High Court in Milan. The luxury brand would be suspected of having set up a shell company in Luxembourg (which is actually managed from Italy) in order to avoid the Italian tax authorities, and to have entrusted control of the group’s brands to that company. If you believe the various sources, the alleged fraud could amount to between €420 and €840 million.¹¹ One month later, there was still no reaction on the company’s website.¹²

Head office costs

The parent company usually houses the administrative, finance, marketing and technical departments under one roof. The cost of these departments, known as “head office” expenses, is among the items for which it is tempting to inflate prices when the head office, which is often a holding company, re-invoices these services to its subsidiaries from a low-tax territory. The aim is to escalate more of the profits on a tax-free basis while increasing the expenses of subsidiaries located in countries where the tax rate is higher. These expenses can easily amount to between 1% and 5% of major international groups’ revenues.

Captive insurance companies

Why do many multinational companies prefer to set up their own in-house insurance company rather than to take out a policy with an insurance company, like any SMC? For researchers R. Palan, R. Murphy and C. Chavagneux, there is no doubt that the main advantage of captive insurance companies and their offshore location is to minimise tax.¹³ Their location bears witness to that fact: we have worked out that 75% are registered in tax havens (see p. 20).¹⁴ ✱

FALSE INVOICING
Unlike manipulating transfer prices, false invoicing consists in falsifying the export and import prices for goods and services between two individual companies, specifically to avoid paying the corresponding taxes. This kind of tax fraud is very hard to detect, as it is often the subject of a verbal agreement between the parties.

REFERENCE POINT

THE FIVE METHODS THAT THE OECD USES TO WORK OUT A TRANSFER PRICE

a) traditional methods

- **the direct method**, known as the comparable free market price. This is the simplest method: the aim is to compare the price with the prices charged between independent companies. When there are no comparable transactions, the aim is to assess the transfer price based on indices like the profit margin generated;
- **the resale price method**, where the price is compared with the sale price that a group entity charges an independent customer;
- **the “cost plus” method**, where the price is set according to the production cost (a complicated calculation), plus a profit margin.

b) transactional methods

Used when the data are not reliable or available; these methods consist in comparing the profits generated by intra-group transactions with those generated by trade between independent companies:

- **the profit-sharing method**. This method is used when businesses within the group are too intertwined for a value to be determined for each transaction. The allocation of consolidated net income between subsidiaries is intended to be comparable to what it would have been in a fully competitive situation;
- **the gross margin method**, where the margin generated by the company on an intra-group transaction is compared with a similar transaction carried out by another, independent, company.

⁹ F. d’Aubert et M. de Chantérac, « Paradis fiscaux, fiscalité et multinationales », Notes d’*Oikonomia*, December 2009.

¹⁰ As quoted in *Oikonomia*, “Paradis fiscaux, fiscalité et multinationales [Tax havens, tax and multinationals]”, Notes on a meeting that took place on December 16th 2009.

¹¹ *AFP*, October 16th 2010, *TSR.ch*, October 16th 2010, *20minutes.fr*, October 16th 2010, *lbtimes.com*, October 18th 2010.

¹² Dolce & Gabbana website: <http://www.dolcegabbana.com/>. Last access on 16th of November 2010.

¹³ C. Chavagneux, R. Palan et R. Murphy, 2010, *op. cit.*

¹⁴ Our calculation is based on the top 20 countries in the rankings (96% of the global market) on the same list.

EXXON AND CHILEAN COPPER

Exxon, which purchased the Compañía Minera Disputada de Las Condes copper mine in the Andes for €64 million in 1979, reported losses on that investment for 23 years, which resulted in the company's de facto tax exemption. Exxon has therefore not paid the Chilean Government any tax on this operation. This situation is particularly surprising since we know that Chile, which is the world's leading copper exporter, has huge mines that provide the millions of tonnes required to manufacture electric cables for the whole world... In 2002, Exxon sold the company to Anglo American for €1.04 billion...

16 times the purchase price. In addition, at the time of the sale, the US company had accrued €460 million in tax credits to offset against future profits. How was such a conjuring trick possible? A Chilean parliamentary commission has enabled some light to be shed on this failure. According to the investigation,³ Exxon localised its costs in Chile and put its profits in a safe place by overburdening Disputada with debt issued by Exxon Financial Services, the Group's financial arm, which is registered in Bermuda. The interest payment cancelled out the profits generated in Chile, while inflating Exxon's profits in Bermuda. The US corporate giant was also under-invoicing the copper and copper derivatives sold to its subsidiaries or parent companies.⁴ Following its investigation into this scandal, the Chilean Parliament introduced a tax on companies' mining revenues (not their profits) that ranges between 0.5 and 5%.⁵

DEBT TRANSFERS

Can you transfer debt to countries that are not the ones for which the debt was incurred? This is a mechanism that multinational companies use to deduct interest expense from tax in an efficient way.

Can you transfer debt to countries that are not the ones for which the debt was incurred? This is a mechanism that multinational companies use to deduct interest expense from tax in an efficient way.

How do you sell a company that you bought twenty years ago for a higher price when it has never made a profit? A textbook case provided by Exxon in Chile (see box), highlights the way in which multinationals play on the tax laws of the countries where they operate. In fact, they shift losses to countries where profits are taxed at a high rate, while deducting interest expense, or even benefiting from tax credits along the way, and accrue profits in countries where taxes are low... This practice is called under-capitalisation. The debt transfer can be quite basic, as in the Chilean case. But there are also more elaborate techniques.

Companies are vying to outdo one another's ingenuity, riding the various systems in place in the countries where they own subsidiaries. The same goes for certain schemes aimed at accumulating interest expense deductions, which have been mentioned by Jim Flaherty, the Canadian Finance Minister. Company A takes out a loan – and can therefore deduct the interest expense on the loan from its tax charge – in order to inject capital into subsidiary B, which is part of the same group and is located in a tax haven. With that capital, subsidiary B agrees to extend a loan to subsidiary C, within the same group, which

is located in a different country and will also be able to deduct its interest expense from tax. Another example, as Mr Flaherty explains, is that a partnership is viewed as an US company in the United States, even if it is Canadian. The result is that this kind of vehicle can take out a loan in Canada to finance an investment in the United States: the interest is deductible in both countries.¹

People have only recently become aware of the gravity of this phenomenon: we had to wait until 2007 for Germany to introduce regulations in this area. From January 1st 2008 onwards, companies' interest expense deductions have been capped, regardless of their origin. The aim is to make transferring profits to lower-tax countries harder. Inspired by Germany, Italy voted to abolish the under-capitalisation rules in December 2007, and to replace them with a system that caps deductible interest expense, regardless of its origin. France is behind in this area, although “*according to the parameters used in Germany, such a measure would lead to an aggregate increase in profits [in France] of €41.6 billion, which corresponds to tax receipts of €11.35 billion over three years.*”²

Ultimately, Western countries are struggling to control the phenomenon. In Southern countries, most tax authorities are overwhelmed by the creativity demonstrated by the finance directors and tax advisors of trans-national groups in order to shift their tax bases.✱

¹ According to Deloitte : http://www.deloitte.com/view/fr_CA/ca/services/fiscalite/bfa18445881fb110V.gnVCM100000ba42f00aR.CRD.htm

² Council for Compulsory Tax Charges, *Companies and Tax and Corporate “Loopholes”: a large number of tax-exemption systems*, October 2010, p. 258.

³ Decreto Ley 600: http://www.cochilco.cl/normativa/decreto_ley_600.pdf

⁴ X. Harel, *op. cit.*, pp. 241-243.

⁵ Law 200-26: <http://www.leychile.cl/Navegar?idNorma=239219>

BLACK BOXES AND CORRUPTION

Another reason for the virtual relocation of the transactions performed by multinational companies is to avoid the law. This is a useful precaution, for example, in cases where obtaining a foreign government contract is often accompanied by the payment of commissions, or even kick-backs.

In 1996, anti-corruption judges joined together and launched the Geneva Appeal, in order to create a European judicial sphere. On that occasion, fingers were pointed at tax havens' involvement in money laundering and in the flight of funds originating from bribery. The fact remains that, to date, the scope of that appeal has not resulted in major changes: the proceeds from embezzling public funds and from the corrupt practices of senior officials, company executives and politicians in the Southern and Northern countries, which the latter try to keep untraceable, are multiplying thanks to tax havens.

Most tax havens are actually legal havens that guarantee secrecy. A large number of legal vehicles (trusts, *anstalts*, foundations, etc.) enable the real owner of the funds to be hidden and dirty money to be recycled. However, according to a Dow Jones report published in December 2009, one third of the 182 company directors questioned in 30 countries stated that they had lost a contract in an emerging market to competitors who had fewer scruples about bribery.¹ *

PROOF BY EXAMPLE

NIGERIA HAS BEEN STRIPPED

With €320 billion diverted or hidden in foreign countries, according to the numbers put forward by the Nigerian delegate at the 57th session of the General Assembly of the United Nations in 2002, the country figures prominently among those where acts of bribery and the illegal transfer of funds have made a significant contribution to capital flight.² In fact Technip, the French petroleum services group, was fined €270.4 million in accumulated fines by the US Criminal Court in June 2010, for corrupting Nigerian government officials over a period of around 10 years, in order to win contracts amounting to over €4.8 billion. Technip's US partners, KBR and Halliburton, its parent company, which had used accounts in Switzerland, were also collared by the law and paid a fine of €321.6 million for similar offences, involving contracts to build liquefied natural gas plants on the Bonny Island site in Nigeria.³

¹ The report was quoted in *La Lettre de Transparence*, Issue No 44, March 2010, p 11.

² United Nations, January 2002 "Global study on the transfer of funds of illicit origin, especially funds derived from acts of cor-

ruption" General Assembly, A/AC.261/12, Vienna.

³ *Les Échos*, "Technip condamné à une lourde amende pour corruption au Nigéria [Technip condemned to a heavy fine for bribery in Nigeria]", June 29th 2010; B. Neumann, "Technip passe

PROOF BY EXAMPLE

OUTLAW COMPANIES

Elf Aquitaine⁴. A huge bribery case, which implicated politicians and senior chief executives, compromised France's leading company – which subsequently became Total – amidst a media storm. Between 1989 and 1993, Elf's management used over-invoicing to pay hidden commissions. The aim was to win new markets and make some people richer. Tax havens were at the center of this €300 million game. For instance, to make sure that the French company gained control of Gabon's oil, Alfred Sirven and André Tarallo, two Elf managers, had opened bank accounts in Switzerland. The enquiry headed by Paul Perraudin, the Swiss examining magistrate, showed that the ultimate destination of that money was a bank account at the Canadian Imperial Bank of Commerce (CIBC) in Geneva, opened by Samuel Dossou, the adviser to the President of Gabon in the name of Kourtas Investment, a company based in the Bahamas. The judge came to the conclusion that President Bongo was the likely economic beneficiary. The background to this sordid affair of state is the monopolizing of African oil by a handful of insiders.

Siemens⁵. Between 2000 and 2006, the German company paid around €1.3 billion in backhanders, mainly to political officials, in order to win contracts in Russia and Nigeria. Michael Kutschenreuter, the former finance director of Siemens' telecommunications division, admitted that he had made "discreet" payments alongside major contracts through "dubious consulting agreements", false invoices and shell companies in Switzerland. Siemens was condemned to pay €2.5 billion in fines and tax arrears by the German courts and the US stock exchange authorities, in order to mop up the mess.

BAE Systems⁶. The law caught up with the British defence group in February 2010, when it was condemned to pay €320 million in fines by the US and United Kingdom authorities for paying backhanders on United States territory. The US Defence Ministry criticised BAE "for having paid several hundred million dollars to third parties, despite being aware that there was a high probability that this money would be forwarded to government decision-makers, so that they would favour BAE when awarding defence contracts."⁷ Using tax havens like Jersey and the British Virgin Islands was at the heart of the scheme.

à la caisse pour corruption au Nigéria [Technip pays up for corruption in Nigeria]", *L'Expansion*, June 28th 2010.

⁴ Verdict of the Criminal Chamber of the Supreme Court, January 31st 2007 p. 23.

⁵ Siemens press release on the subject, which

insists on its cooperation, <http://www.siemens.com/press/pool/de/events/corporate/2009-q4/2009-q4-legal-proceedings-e.pdf>

⁶ BAE posted a confirmation on its own website at: <http://www.baesystems.com/Newsroom/>

[NewsReleases/auto-Gen_1101517013.html](http://www.les-echos.com/NewsReleases/auto-Gen_1101517013.html)

⁷ *Le Monde*, "Pots-de-vin : forte amende pour le vendeur d'armes britannique BAE [Back-handers, Hefty fine for the British arms dealer]", February 8th 2010

THE SECRETS OF OPAQUENESS

What makes these practices even more effective is that some countries and territories are not very particular about the identity of the parties operating on their territory. This attitude leads to breaches into which the “Big Four” and other legal and financial advisors disappear – when they don’t open them.

The disjuncture that occurs in tax havens would not be possible without secrecy. It is this feature that allows multinational companies to create a virtual world where they can locate their business, away from tax and foreign tax authorities. This secrecy also allows less scrupulous financial players to bypass the prudential rules issued by the Basel Committee, like the shareholders’ equity ratios required in order to be able to lend money. Finally, it protects criminals and corrupt individuals against legal proceedings. Secrecy prevents the real beneficiaries of bank accounts or the owners of offshore companies from being identified. It usually goes hand in hand with the discretion of the authorities in tax havens, who rarely respond to requests for mutual legal or tax assistance expressed by the countries that have been robbed. Or else, like Luxembourg, Liechtenstein and the United Kingdom, they respond under conditions and within timeframes that allow plenty of time for the incriminated parties to move their loot elsewhere.¹ Bernard Bertossa, the former public prosecutor for the Canton of Geneva, who was involved in the Geneva Appeal (see p. 35) with Denis Robert, was already saying in 1998 *“that money could go round the world in 24 hours. We, the magistrates, would need twenty-four generations to follow it”*.² Tax inspectors could say roughly the same thing.

This is the reason why the Tax Justice Network (network of NGOs and researchers) classifies nations according to their opacity score.³ Its financial secrecy index (see p. 7) assesses the harmfulness of 60 financial centres according to 12 key financial secrecy indicators, including the existence of strict banking secrecy, the weakness of the cooperation with foreign tax authorities, the absence of a public register for legal vehicles like trusts (see p. 14 on Jersey), foundations or *anstalts*, or even the possibility of setting up the company without providing your own name.

In order to benefit from increasingly opaque schemes, companies can rely on financial and legal intermediaries who have particularly extensive experience of tax planning practices. The “Big Four” consulting and accountancy firms rank among the accused, along with corporate banks, legal experts and lawyers (see box). Their creativity knows no

bounds where guaranteeing their clients’ anonymity is concerned. A telling example is the invention of what we should call a company divided into protected cells (“protected cell company” or PCC in English), a solution which has since met with considerable success in the Seychelles and other “paradise” islands. TJN compares this structure to *“a house with a lock at the entrance and many rooms inside, each room locked separately with its own door, but also with an escape tunnel only accessible from inside the room. If an investigator seeks to find out what is going on in one room inside the house, she first needs to unlock the main outer door. But imagine that by opening that first door everybody inside the building is alerted to the fact that someone has entered the house. (...) While the investigator tries to unlock the second door (by filing a second costly information request), the perpetrator has enough time to erase all traces of guilt and escape through the secret tunnel.”*⁴ *

considerable success in the Seychelles and other “paradise” islands. TJN compares this structure to *“a house with a lock at the entrance and many rooms inside, each room locked separately with its own door, but also with an escape tunnel only accessible from inside the room. If an investigator seeks to find out what is going on in one room inside the house, she first needs to unlock the main outer door. But imagine that by opening that first door everybody inside the building is alerted to the fact that someone has entered the house. (...) While the investigator tries to unlock the second door (by filing a second costly information request), the perpetrator has enough time to erase all traces of guilt and escape through the secret tunnel.”*⁴ *

PROOF BY EXAMPLE

DELAWARE, AN IMPERIAL PARADISE

It is not a coincidence if the United States appears at the top of the tax haven ranking drawn up by TJN.

According to the Australian Taxation Office, entities operating in some US states, including multinational companies, benefit from the same advantages that they would enjoy if they were located in tax havens.⁵ Like Delaware, the 2nd smallest state in the US confederation, which has over 850,000 companies (roughly one per inhabitant), including 50% of listed companies and 60% of the “Fortune 500” companies. How do you explain its attraction? *“Delaware judges and legislators are generally well disposed towards company management in issues like shareholder complaints, takeovers and consumer rights protection cases.”*⁶ In terms of governance, Jason Sherman, the journalist, considers Delaware as even laxer than Liechtenstein or Somalia (see p. 16). This makes the state the location of choice for setting up offshore companies, according to one tax planning website: *“As long as you do no business there, the tax rate is equal to zero, both on the profits generated and on the directors’ income, on condition that you don’t live there either.”*⁷ In actual fact, profits generated outside the state’s borders are not taxed, and there is no local income tax or “sales tax” (a kind of VAT). Meanwhile, the company does not have to be physically present in the state to be registered there.

1 A. Dulin and J. Merckaert, « Biens mal acquis : à qui profite le crime ? », *CCFD-Terre Solidaire Report*, June 2009, p. 147.

2 P. Hazan, translated from french « Drogue: ‘l’argent sale arrive en Suisse quasiment blanchi’ », *Libération*, June 10th 1998. Our translation.

3 Including CCFD-Terre Solidaire.

4 Tax Justice Network *Key Financial Secrecy Indicators* <http://www.secretaryurisdictions.com/PDF/CellCompanies.pdf>

5 Australian Taxation Office, *Tax Office submission to US Senate Committee on Homeland Security and Governmental Affairs*, July 21st 2009

6 P. Y. Duga, « L’État du Delaware, le paradis fiscal américain qui irrite le Luxembourg », *Le Figaro*, April 2nd 2009. Our translation.

7 Website: <http://www.paradisfiscaux.com/>.

The resounding failure of Enron, which was then the seventh largest company in the US, in 2001, also marked the downfall of Arthur Andersen, one of the five major global advisory and accountancy firms, which was accused of having turned a blind eye to the 760 companies set up in the Cayman Islands and in the Turks and Caicos Islands to hide Enron's debts.⁸ Despite the adoption of new accounting and financial transparency rules (the Sarbanes-Oxley law) in the United States, the "Big Five" became the "Big Four", without clearing up any of the doubts regarding their conflicts of interest. Far from it.

Judges and juries. Through their various companies, Deloitte, Ernst & Young, KPMG and Price Waterhouse Coopers (PWC) provide advisory and "tax planning" services at the same time as checking the financial statements of multinational companies. Each of the Big Four operates in around 140 countries. However, the accountant's code of conduct states that the same chartered accountancy firm cannot advise a client on their tax strategy and audit their financial statements.⁹ The Big Four, however, are able to wear several hats, which borders on a conflict of interest. What multinational companies like about auditors is their perfect knowledge of the company and their ability to make tax optimisation strategies acceptable in the eyes of the law. According to C. Chavagneux and R. Palan, *"the Big Four are contributing less and less towards ensuring the security of global capitalism by checking that the practices of the business world are sound (...). They legitimise the version of the facts that is of most benefit to their paymasters in exchange for substantial commissions."*¹⁰ Tax optimisation therefore makes maximum use of all the potential loopholes in the legislation. Rather than acting in keeping with the spirit of the law, the Big Four promote all sorts of tax avoidance by juggling with the texts. For instance, PWC published an 837-page handbook on transfer pricing in 2009! Crossing the red line has resulted in the law catching up with some

firms. In 2009, a sensational scandal involving an accounting fraud of around €1.5 billion using Mauritius destroyed Satyam, an Indian IT giant. The SEBI, the Indian stock exchange regulator, accused PWC of having certified financial results that were overvalued and false.¹¹ In 2003, the US Senate demonstrated that the tax optimisation products promoted by KPMG were often against the law.¹²

The standard-setters. The Big Four provide most of the funding for the IASB (International Accounting Standards Board), the private body

responsible for drawing up accounting standards. They also sit on the IASB board, alongside investors and company directors, while most countries have gradually transferred their expertise in this area to the IASB.¹³ It is therefore the Big Four who determine, to a certain extent, the way in which multinational companies should account for their business, and, in passing, the guidelines of the audit process that they are paid to conduct.

Tax avoidance brokers. We know about insurance or mortgage brokers, who negotiate preferential prices and rates for their clients based on their large client base. The Big Four, the banks and other legal experts play a very similar role in the taxation field. They advise a significant portfolio of multinational companies on tax matters and simultaneously negotiate

advantageous legal arrangements with Governments – including tax havens – on their behalf. We owe most of the offshore legal innovations that allow the richest in society to optimise their tax to these specialist legal and finance experts, and not to the thinly-staffed administrative authorities in the islands. The central role played by Barclays, the British bank, in Ghana's recent emergence as an offshore financial centre bears witness to this trend.

Supported by a number of banks, legal experts and business experts, Ernst & Young has created a startling new language: *"whether it involves logistics management or transfer pricing, tax is a commercial strategy lever. If it is applied correctly, it enables you to boost your competitive advantage and create value."*¹⁴ Conversely, the British New Economics foundation, says that the Big Four auditors are the profession that destroys the most value: *"Every pound that is 'avoided' in tax is a pound that would otherwise have gone to HM Revenue. In our model we looked at how this lost revenue could have been better spent. For a salary of between £75,000 and £200,000 [between €84,500 and €225,400] tax accountants destroy £47 [€53.00] of value for every pound in value they generate."*¹⁵

BIG FOUR AT THE HEART!

8 In May 2005, the US Supreme Court cleared Arthur Andersen of the crime of obstructing justice, which it had been found guilty of in 2002, however the company had already filed for bankruptcy. See *Alternatives économiques*, July 2005.

9 Article 3, Point 6 of the Statutory Auditors' Professional Code of Conduct, Chapter II, Decree N° 2010-131 of February 10th 2010.

10 C. Chavagneux et R. Palan, « Les paradis fiscaux », Repères, La Découverte, 2009, p. 75. Our translation.

11 *The Indian Economic Times*, « Sebi can probe Price Waterhouse in Satyam fraud case, rules HC », August 26th 2010.

12 C. Levin, <http://levin.senate.gov/newsroom/supplementing/2003/111803TaxSheIterReport.pdf>

13 D. Baert et G. Yanno, « Rapport d'information relatif aux enjeux des nouvelles normes comptables », Commission des finances, de l'économie générale et du plan, Paris, 2009.

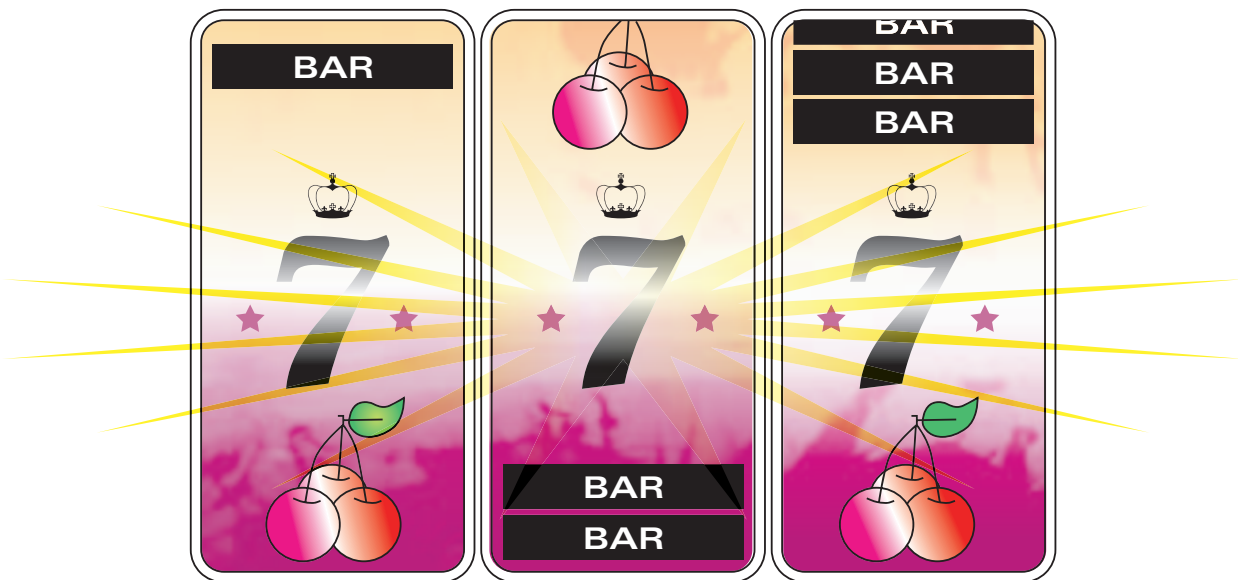
14 <http://www.ey-avocats.com/FT/fr/Services/Tax/International-Tax/Transfer-Pricing-and-Tax-Effective-Supply-Chain-Management> Our translation.

15 NEF, *A Bit Rich: Calculating the real value to society of different professions*, December 2009. <http://www.neweconomics.org/publications/bit-rich>

CHAPTER



WHEN THE REAL ECONOMY IS DOMINATED BY THE OFFSHORE ECONOMY A NEGATIVE SUM "GAME"



THE WORLD OF OFFSHORE FINANCE IS LIKE A GIANT CASINO.
EXCEPT THAT THE WHEEL OF FORTUNE ALWAYS TURNS IN THE SAME DIRECTION,
TO THE ADVANTAGE OF LARGE COMPANIES AND FINANCIAL
AND LEGAL INTERMEDIARIES, BUT AT THE EXPENSE OF CITIZENS
AND THEIR ACTUAL GOVERNMENTS. THE VERY SAME GOVERNMENTS
ARE SEEING THEIR ROOM FOR MANOEUVRE COME UNDER INCREASING
PRESSURE DUE TO THE WEIGHT OF TAX HAVENS
IN THE INTERNATIONAL ECONOMY.

WITNESSING RESOURCES FLIGHT

BETWEEN TAX AVOIDANCE AND EXPENDITURE, COUNTRIES ARE BEING ROBBED

Every year, between €600 and €800 billion escapes from developing countries, 65% of which is due to tax avoidance, between 30 and 35% to crime and 3% to corruption. These numbers amount to around 10 times the Official Development Assistance (ODA) granted by all wealthy countries put together. As an example, Nigeria receives €2.7 billion in ODA and experiences illicit capital flight of €12.8 billion per year. The reduction in the tax base is reflected in a fall in government revenue, since that €600 to €800 billion amounts to income that governments cannot tax. Tax avoidance by multinational companies alone is responsible for a shortfall of €125 billion in Southern countries' coffers.¹

PROOF BY EXAMPLE

WHEN COLGATE-PALMOLIVE PLAYS THE SWISS CARD

The CFDT Détergents trade union members, who were the victims of Colgate-Palmolive's decision to move its head offices from France to Geneva in January 2005, had to face an uphill battle to get a political response to what they claimed was tax offshoring. The US group chose to relocate to Switzerland, where it negotiated a 6.44% tax rate on its profits, compared with 33.3% in France. With the help of Ernst & Young, the company reorganised its French business, which was henceforth split into two entities: one responsible for manufacturing the products at its Compiègne plant, and the other for marketing them. The parent company sells the raw materials to the Compiègne plant from Geneva and buys the finished products back from it at cost price, plus a small margin (cost plus) of 6%. It then resells the finished products to the French marketing company, thereby locating the profits in the place where they are subject to the least tax. This process deprives the French Government and local authorities of €40 million in taxes, while French employees see profit-sharing and employee incentives, which are calculated on the basis of profits, disappear over the Alps...² The problem is that there is nothing in law to prevent such a stance. As Pascal Saint-Amans, who is the head of the OECD tax division, reminds us, "companies are free to domicile all the operations that relate to the brand, to research and development and to advertising in Geneva or Zurich (...). No one knows how to address the problem."³

SHRINKING TAX REVENUES,
EROSION OF AVAILABLE SAVINGS,
PUTTING WAGES UNDER PRESSURE...
THE COST FOR COUNTRIES AT THE ORIGIN
OF SIPHONED WEALTH TO TAX HAVENS
IS VERY HIGH.

Not satisfied with avoiding tax on part of their profits, unbeknownst to governments, companies are continually asking countries that want to host their operations to make increasing efforts on tax. Governments, which are competing with one another, are finding it harder and harder to resist this blackmail. What is more, international institutions do not encourage them to resist tax competition, when they specifically ask Southern countries to do everything necessary to attract foreign investors. The result is that the average corporate tax rate is continually falling on a world-wide basis. The rate has declined from 37% in 1993 to 32.7% in 1999 and to 25.5% in 2009, i.e. a decrease of around 7 percentage points in 10 years. Between 1999 and 2009, the corporate tax rate fell from 35% to 27.5% in Bangladesh and from 42% to 34.5% in South Africa. In Uruguay, it has fallen from 35% in 2003 to 25% in 2009.⁴ In France, the corporate tax rate was lowered from 50% to 33.33% during the 1990s. The income shortfall for governments is considerable. If they were taxed at the same rate as in 1993, the 50 leading European companies would have to pay an extra €17 billion in tax every year.⁵

As if the fall in tax rates was not enough, governments are also introducing a range of special tax regimes for the benefit of foreign investors. The number of export processing zones, which are generally characterised by low or nil tax rates, has increased from 79 world-wide in 1975 to 3,500 in 2006.⁶ In Southern countries, exemptions are frequently granted to all new investors for the first five years. Allowances are granted on a case-by-case basis, at the discretion of Finance Ministers or tax inspectors – whom investors know how to reward for their "notion of hospitality", if required. The accumulation of these special regimes represents a "tax expenditure" (or amount of potential revenues foregone) that can be huge. Since 2006, the Indian Government believes that these "gifts" (tax incentives and subsidies) have resulted in a €10.4 billion hole in India's budget every year.⁷ Morocco, meanwhile, has assessed its 2006 tax expenditure at 4.3% of GDP, i.e. 19% of its tax receipts.⁸ In Senegal, it is believed to amount to

1 Christian Aid, *op. cit.*, May 2008.

2 T. Fabre, « Multinationales : leurs plans secrets pour fuir le fisc », *Capital*, April 2006.

3 Quoted in X. Harel, *op. cit.*, pp. 204-205. Our translation.

4 KPMG International, *KPMG's Corporate and Indirect Tax Rate Survey 2009*.

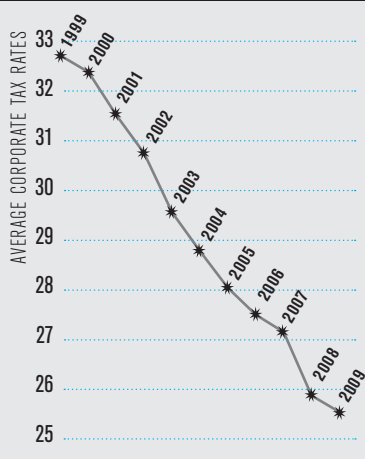
5 Calculations performed by the author based on data from *Fortune 500* and KPMG.

6 W. Milberg et M. Amengual, « Développement économique et conditions de travail dans les zones franches d'exportation : un examen des tendances », International Labour Organization, 2008, Geneva, p. 5.

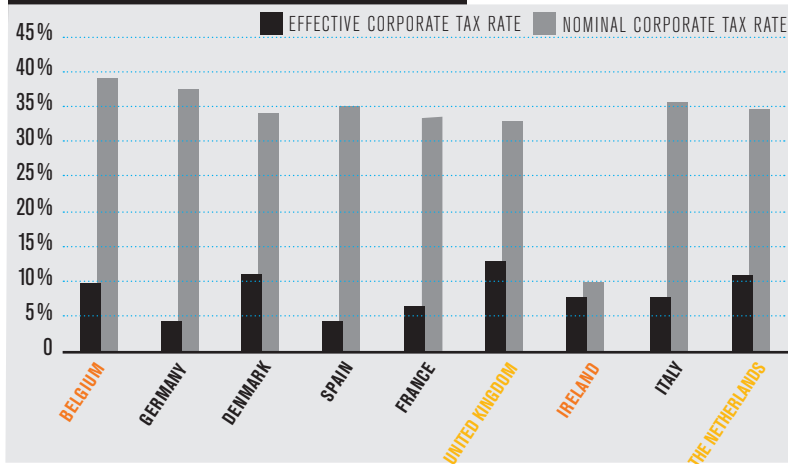
7 Actionaid, *Accounting for poverty*, September 2009, p. 43.

8 N. Jellouli (Moroccan Central Department of Taxes), *The Moroccan Experience of Tax Expenditure*, Presentation in Rabat, on November 23rd 2006.

WORLD-WIDE CORPORATE TAX RATES BETWEEN 1999 AND 2009



EFFECTIVE AND NOMINAL CORPORATE TAX RATES IN EUROPE IN 2009



••• €457 million, according to a government estimate relating to the 2008 budget,¹⁰ or 5% of GDP. By applying a levy of 3% for the extraction of its mineral resources, as specified in its tax code, and not the 0.6% levy that it has actually applied, Zambia could have obtained €50 million in additional tax receipts between 2004 and 2006! In 2008, the Government tried to force multinational companies in the mining sector to pay the 3% levy, but it soon backed down under pressure from the companies.¹¹

POPULATIONS ARE HARMED

The first victims of capital flight throughout the world are the middle classes and the poor. Capital flight of savings is a synonym for rising interest rates at local banks, which only lend to the wealthy, due to a lack of liquidity – or at prohibitive interest rates.

Low government receipts mean no funding for social services and public investment: indeed, how do you pay teachers and doctors' salaries, or extend the electricity grid and transport infrastructure when capital has flown to tax havens? In Sub-Saharan Africa, illegal capital flight represents over three times the budget allocated to agriculture, at a time when 30 % of the population is suffering from malnutrition.¹² As just one example among others, the hole in Southern countries' public finances due to tax avoidance by multinational companies alone amounts to five times the amount required to eradicate hunger in the world, according to the FAO (Food and Agriculture Organization of the United Nations).¹³ A large number of multinationals are therefore helping to splinter countries by sucking their

finances dry.

In France, tax evasion costs the government between €40 and €50 billion per year, including €15 to €20 billion resulting from abuse of tax havens, according to the information report on tax havens published in September 2009 by the Finance Commission of the French National Assembly (No 1902). This is the equivalent of the 2009 social security deficit.¹⁴

EMPLOYEES ARE IGNORED

What is less well known is that, beyond the cost to the government, and incidentally, to public service users and officials, the virtual shift of the wealth created by multinationals puts downward pressure on employment income in the private sector. As François d'Aubert and Max de Chantérac explain, "one practice that is open to large groups is to reduce profits in subsidiaries where they employ the most people, in order to reduce the profit-share paid to employees."¹⁵ What is more, the option available to a multinational company to shift part of its revenues to tax havens enables it to put pressure on employees, by keeping profits at a subsidiary low, or even non-existent, and by threatening to close it. This is an enormous challenge for trade unions: how can they be certain about the cost-cutting arguments put forward by management? The major unions do not seem to have realised the full extent of this issue, except in rare cases of mobilisation against "outsourcing for tax reasons" (see box on p. 40). In the long term, transferring gains offshore contributes towards capital yielding higher returns than work ☉

9 As a % of EBITDA, a gauge of the company's profitability. Source: *L'harmonisation fiscale en Europe [Tax Harmonisation in Europe]*, Amina Lahèche-Révil, CEPPI, 2002.

10 « Budget 2008 : les dépenses fiscales estimées provisoirement à 300 milliards », *Senegal Business*, October 14th 2009.

11 ActionAid, *op. cit.*

12 Calculation performed by the author based on data from the FAO,

African Economic Outlook (published by the OECD, the African Development Bank and the UN) and from the US *Global Financial Integrity* think-tank.

The budget allocated to agriculture in Sub-Saharan Africa amounts to €12.2 billion, while illegal capital outflows amounted to €41.9 billion on average per year between 2003 and 2008.

13 Figures from *Global Financial Integrity* December 2008; and Christian Aid, May 2008.

14 €20.3 billion according to *La Croix*, "Sécurité Sociale, un déficit plus faible que prévu [Social Security, a lower than expected deficit]", April 2nd 2010.

15 F. d'Aubert et M. De Chantérac, *op. cit.*, p. 2. Our translation.

16 M. Chevalier, « CAC 40 : les actionnaires d'abord », *Alternatives économiques*, n° 290, April 2010.

THE WINNERS

SHAREHOLDERS AND MANAGEMENT REAP RICH REWARDS

Over the past 30 years, shareholders have been capturing an increasing share of the wealth created by companies, both through the rise in share prices (capital gains) and through the increasing share of the profits awarded to them (dividends). This has been at the expense of the employees and reinvestment in the company. The key to this system is stock-options, which have turned company management into shareholders themselves, by linking an increasing portion of their income to the share price... The result is that in 2009, when the profits of the companies in the CAC 40 (French stock market index) decreased by 20% compared with 2008 (€47 billion in total profits), the level of shareholder awards was maintained (€35 billion). That number amounted to 56% of profits (excluding exceptional items) compared with an average of 40% in previous years. We can only regret that multinational companies do not pay more attention to those among their shareholders who refuse to sacrifice the company's social and ethical duties to the demands of profitability.¹⁶

UNDERMINING THE SOCIAL CONTRACT

THE WAY MULTINATIONALS BEHAVE DRAINS COUNTRIES OF RESOURCES THAT THE GOVERNMENTS HAVE TO FIND SOMEWHERE ELSE, TO THE DETRIMENT OF EQUITY, POLITICAL INDEPENDENCE AND SOMETIMES EVEN THE RULE OF LAW.

CONSUMERS ARE OVERTAXED

How can Southern countries offset the loss of €125 billion that is due to tax avoidance by multinational companies, especially when it occurs in parallel with a reduction in the corporate tax rate and with a rapid fall in customs duties as a result of the liberalisation imposed by the IMF?¹ The answer is simple: by transferring the tax onto local consumers and businessmen! In fact, this is the answer adopted by a large number of the governments concerned, which have raised VAT rates, among other measures. This unfair tax, which some analysts view as being the only effective one in countries where bribery is rife, weighs more heavily on the most vulnerable than on the wealthiest as a proportion of their income. The tax represents a much higher share of tax receipts in developing countries (40 %), than in developed ones (around 20 %).² In Niger, for example, VAT accounted for 50.1 %, on average, of internal tax receipts for the period between 1997 and 2005.³ In Brazil, according the Unafisco trade union, "over one third of the hours worked goes towards paying consumption tax (VAT).

(...) *Approximately two thirds of taxes come from consumption and barely a third from earned income and assets.*"⁶

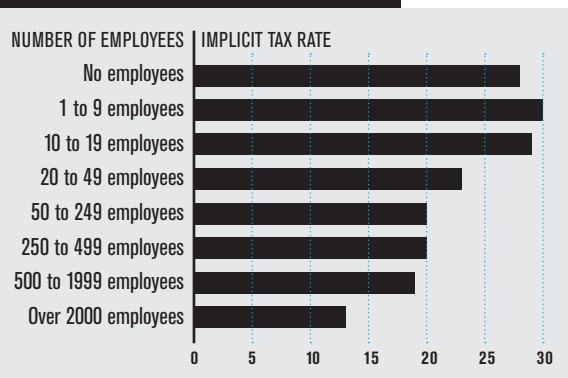
This results in a triple burden for the population: a fall in public spending, a decrease in earned income and an increase in the size of consumption levies!

THE RESULT IS A TRIPLE BURDEN FOR THE POPULATION, THROUGH THE FALL IN PUBLIC SPENDING, THE DECREASE IN EARNED INCOME AND THE INCREASE IN THE SIZE OF CONSUMPTION CHARGES!

SMALL AND MEDIUM-SIZED ENTERPRISES ARE FACING UNFAIR COMPETITION

Because they have no foreign subsidiaries or intermediaries well versed in tax avoidance strategies to advise them, most SMEs do not have the means to benefit from the same advantages as large companies. In fact, some are beginning take a stand. Business and Investors against tax havens, an SME grouping in the United States, has sent a petition to President Obama and to Congress, as well as a report asking them to limit the use of tax havens, and to abolish tax advantages for transactions that have no real commercial purpose. According to this organisation, the United States Government loses US\$ 30 billion every year because of these loopholes.⁷ In 2010, the US Office of Management and Budget estimated that the corporate tax levied on multinational companies represented only 7.2% of federal receipts, i.e. less than one sixth of the contribution that small businesses and individuals make to the Internal Revenue Service (IRS).⁸

IMPLICIT TAX RATE⁴ IN FRANCE BY SIZE OF COMPANY IN 2008⁵



1 J Marshall's "One Size Fits All? IMF Tax Policy in Sub-Saharan Africa", *Christian Aid Occasional Paper* N° 2, April 2009, provides a remarkable description of the policies imposed on Africa by the IMF between 1998 and 2008.

2 See M. Keen and M. Mansour, "Revenue Mobilization in Sub-Saharan Africa: Key Challenges from Globalization", *IMF*, 2008

3 Niger Ministry of Economics and Finance, "Analyse de la politique fiscale au Niger et ses impacts sur la pauvreté [Analysis of fiscal policy in Niger and its impact on poverty]", *Observatoire National de la Pauvreté et du développement humain* [National Observatory for Poverty and Human Development], 2008. http://www.pnud.ne/rap_eval/Rapport_Etude_fiscalite_%20pauvrete_Niger.pdf

4 The implicit tax rate represents the tax effectively paid as a proportion of net profits.

5 From the Compulsory Tax Council report, *Les prélèvements obligatoires des entreprises dans une économie globalisée* [Compulsory taxation of companies in a global economy], September 2009.

6 "Brésil - un système d'injustice fiscale à réformer", from the *Revue Alternatives Sud* in collaboration with the Tax Justice Network, "Évasion fiscale et pauvreté", Vol. XIV, p. 106, 2007. Our translation

7 Website: www.businessagainsttaxhavens.org

8 *Business Against Tax Havens*, "Unfair Advantages: The Business Case Against Overseas Tax Havens", July 20th 2010.

●●● In France, the Compulsory Tax Council has also showed its concern: “Large companies pay relatively less tax than SMEs (...) and companies in the intermediate bracket”, is what we read in its 2009 report. The CAC 40 companies (companies listed in the French stock market index), which generate around 30% of all French corporate profits, only pay 13% of the corporate tax bill, while SMEs with fewer than 250 employees, which account for 17% of corporate profits, pay 21% of the bill. Meanwhile, as stated by Eric Israelewicz in *La Tribune*,⁹ an SME pays three times as much tax as a large company on every €100 of profits. In developing countries, the fate of local entrepreneurs is hardly more enviable. As a share of internal savings has escaped offshore, access to credit is often prohibitive, and small and medium-sized company owners, even foreign ones, complain that they are subject to genuine “tax harassment”, especially in some African countries where tax inspectors sometimes abuse their powers, in order to conduct multiple tax investigations, make excessive tax demands or to threaten the company’s assets.¹⁰

A ONE-SIDED SOCIAL CONTRACT

By awarding themselves the lion’s share of the wealth generated, multinational companies are threatening to jeopardise political stability, as their behaviour weakens the foundations of the political systems in which they prosper.

When they resort to paying commissions offshore in order to obtain a government contract, or an exploration or operating licence, they subjugate the public decision-making process and often feed politicians’ interventionism – and even their authoritarian practices.

Furthermore, the proliferation of special tax schemes contributes towards supporting a culture where the law is avoided. The legal uncertainty facing entrepreneurs is sizeable: tax is perceived as a racket run by the government or tax collectors, and as a negotiable contribution... It is hard to seal a social contract on that basis. In order to pay the

bill that the multinationals have left unpaid, it is usually not enough for governments to fall back on consumers and SMEs. They need to run up debts and/or call on international financing – including development aid. This method of financing is very often synonymous with giving up part of their sovereignty, especially for developing countries. The structural adjustment plans that have accompanied the loans granted by the IMF and the World Bank have brought governments, farmers, and emerging industries in many countries to their knees, entirely for the benefit of their creditors and foreign investors. Today, European funding for Africa remains highly dependent on openness to trade as well as on measures to control migration flows. In the agricultural sector, international backers most often advocate an agro-export model at the expense of food crops, although those crops would be able to feed the population. In Burkina Faso, for example, 91% of the resources dedicated to agriculture come from external financing.¹¹ Even when donors are concerned about not dictating the policies to implement, the ministers and the handful of senior officials in the most vulnerable countries often spend more time complying with the formalities and anticipating the demands imposed by donors than developing policies that meet the aspirations of their own citizens.

Finally, taxation is the foundation of all political systems. Over time, it forms an integral part of getting the public to buy in to a collective project – the “social contract”, which the state is supposed to guarantee. However, that buy-in requires fairness. As Mick Moore, the British political scientist, reminds us, the political history of all major democratic countries shows a strong correlation between democratic progress and the development of a sophisticated tax system, quite simply because the public holds their lord, their sovereign or their government accountable for the use of the wealth that they receive... On the night of August 4th 1789, the French Revolution specifically abolished tax privileges, before arriving at the principle of “an indispensable common contribution (...) [being] equitably distributed among all the citizens in proportion to their means”.¹²

⁹ “Le CAC 40 paie moins d’impôt que les PME [CAC companies pay less tax than SMEs]”, *latribune.fr*, December 14th 2009.

¹⁰ The French Centre for Investment in Sub-Saharan Africa (Centre français des investissements en Afrique noire, or CIAN, specifically complains about this situation. See *Les Afriques*, “Carte 2008 du harcèlement fiscal en Afrique [2008 map of tax harassment in Africa]”, January 5th 2009.

¹¹ D. Crola, *Aide à l’agriculture : des promesses aux réalités de terrain*, Oxfam France, November 2009, p. 13.

¹² Article 13 of the French Declaration of the Rights of Man and of the Citizen.

¹³ C. Chavagneux et al., *op. cit.*, *L’Économie politique* n° 42, p. 30. Our translation.

¹⁴ €21.2 billion for Deloitte (2010 number), €21 billion for PWC (2009), €19.6 billion for E&Y (2008) and €16 billion for KPMG (2009). Source: Wikipedia.

¹⁵ Deloitte: http://www.deloitte.com/view/en_GX/global/press/global-press-releases-en/969f3f0550dfa210Vgn_VCM300001c56f00aR_CRD.htm

THE WINNERS

THE LEGAL AND FINANCIAL INTERMEDIARIES SHARE IN THE PROFITS

“Accountants, legal practitioners, bankers and other tax experts (...) have had a hand in all the legal innovations introduced to avoid tax and regulations. They have advised and influenced the politicians (...), [and even] drafted the legislation of the countries in which they had decided to set up operations themselves. (...) These are the same people who maintain that tax havens are a perfectly legitimate way to do business.”¹³ This unedifying picture has earned the Big Four the distinction of being awarded the *Alternative Tax Award* by Christian Aid, a British Charity. This award rewards the talent expended in depriving developing countries of their tax revenues... The Big Four’s aggregate revenues amount to around €80 billion.¹⁴ Deloitte, the leader, generates 28% of its revenues from consulting services and 44% from auditing services.¹⁵ By assisting and managing the way in which the disconnect is engineered, the Big Four retrieve part of the tax advantages gained by their client companies thanks to their advice. Under the pretext of complying with their clients’ demands, the banks act as an enlightened guide to the world of trusts, special purpose vehicles and other offshore delights. Wealth management is especially profitable.

••• The origin of the United States' Declaration of Independence was the British Parliament's decision to levy a tax on tea, and its refusal to grant the 13 American colonies the right to levy the tax. The Americans declared that there would be "no taxation without representation." A 6th Century priest, Salvian of Marseille, also saw tax inequalities as a core factor in the fall of the Roman Empire. That comment should be compared to the one made more recently by Christian Chavagneux, the journalist: "if we knew what the amount [of multinational companies' tax avoidance] was, we would be so horrified at seeing that the multinationals pay so little tax that it would create a dramatic political and public upheaval".¹⁶ ☉

*"Paying tax is tiresome, without a doubt, but it would be more bearable if all citizens were taxed equally. What is intolerable is that everyone does not share the common burden: the poor are paying for the wealthy. Even more, it is the wealthy, who from time to time, decide to increase the amount of tax, but it is the poor who pay the tax on their behalf. This is a scandalous misdemeanour! (...) The only thing that surprises me is that under these conditions, the poor and the destitute do not go off and join the Barbarians."*¹⁷

Salvian of Marseille, a 6th Century priest

16 Questioned during *Pièces à Conviction* [Damn-ing evidence], a television program shown on France 3 on November 16th 2009. Our translation.

17 Quoted in L. Jerphagnon's *Les Divins Césars. Idéologie et pouvoir dans la Rome impériale* [The Divine Caesars: Ideology and Power in Imperial Rome], Ed. Tallandier, 2004, Paris. Our translation.

GOVERNMENTS RENDERED IMPOTENT



Mired in their deficit and employment problems, Western governments repeat their unwavering conviction in the virtues of trade and investment without blinking an eye at every international jamboree, and with the benediction of the major emerging countries, without ceasing to create favourable conditions for the expansion of the private sector, in order to encourage growth and employment: "We reaffirm our commitment to free trade and investment recognizing its central importance for the global recovery." (G20 Seoul Summit Action Plan, November 2010). According to those governments, each country needs to adapt its legal and tax framework, or even its territory and its population, and reduce all forms of government intervention, in order to allow market forces to prosper for the supposed benefit of all. Although the 2008 financial crash rattled some certainties regarding the supposed good nature of the self-regulation of financial markets, this ideology has not learned its lessons.

STEERING WITH LIMITED EYE SIGHT

Aside from the actual fact that empirical analysis – particularly of the disastrous impact of these policies in the poorest countries – ought to lead its members to review, or at least to qualify, their judgment, the G20 injunction is based on shaky statistics. By dismantling the fiction of multiple offshore transactions, the Bank of France has shown that FDI inflows to France were, in reality, 85% lower than published (see p. 12). Such statistics ought to at least

bring the French Government to reassess the appropriateness of the sacrifices agreed to attract investors. Likewise, the diversion of a significant share of world trade by companies with no real economic purpose ought to lead the proponents of "commercial growth that benefits all" to call their beliefs into question.

In particular, the G20 countries do not seem able to see that the difficulty that they have in grasping the true nature of economic activities hides the evaporation of the value generated by international trade and investment, which is swallowed up by offshore subsidiaries, along the way. Of course, this value is not lost for everyone and lobbying by multinational companies and banks is a powerful tool. Should we, therefore, conclude that the G20 is deliberately turning a blind eye to the fact that a minority is capturing the world's wealth?

Without arguing against the cynicism expressed by some, we would rather assume that major world leaders are blind to this issue, and are duped by the offshore smoke-screen and soothed by the illusion that it is a phenomenon that takes place on the margin of the economy – and that just needs to be brought into line by forcing recalcitrant territories to cooperate.

Nonetheless, if they want to have an influence at the global level, or simply to have the tools to be able to debate the issue on an informed basis, they need to agree to look at the offshore phenomenon in broad daylight, in order to reveal its trickery. We are also betting that it will be easier and specifically, that it will be more efficient, to get a true picture of economic reality by pointing the spotlight at those who issue misleading data, rather than at those who receive inaccurate financial statements, albeit willingly, and who can be replaced (see chapter 4).

AT THE SOVEREIGNTY SUPERMARKET

Having organised a world where capital circulates freely, or almost freely, countries are now competing fiercely to attract that capital. The smallest among them have quickly understood that they needed to go further in giving up their sovereignty to attract financial inflows. They have done so to the point where they trade that sovereignty, by piggy-backing on the global economy.¹ In 2006, for example, the Jersey National Assembly

“Tax havens represent one of the most important political issues of our time.”

Christian Chavagneux³

community brings them, without it costing them anything at all.”² Because it lowers the quality of laws in other countries and hijacks those laws, this exploitation of legislation – whether regarding tax or regulations – is a direct challenge to countries’ sovereignty. The weakest countries – particularly developing countries – are the least capable of standing up to this “game”.

It is not so much the tax havens that are siphoning off the sovereign powers of countries or influencing the course of events. In the sovereignty supermarket, the customer is king. It is the bankers or the accountancy firms acting on behalf of their wealthy clients and of multinational companies who deter-

the invention of “*offshore sovereignty*”, where “*Coca-Cola is an economy, just like the George Forrest Group or Brazil.*”⁴

This being the case, it is easier to understand that the G20 countries are apparently finding it hard to solve the problem of tax havens. If it was David against Goliath, both the European Union and the G20 would have had no problem in getting the reluctant state lets to toe the line. However, behind the tax havens, which act as a kind of distorting two-way mirror for the real economy, we can detect the presence of industrial and financial groups whose revenues are often larger than countries’ budgets. The G20 has not involved itself in this arm-twisting competition.

However, is all the power that the G20 still has an illusion? The answer, in our view, is once again no. But there is an emergency. In order to fully recover their ability to change the course of history, and to meet the legitimate aspirations of their citizens, politicians will need to react quickly and with determination, by targeting the root of the evil (see chapter 4) this time ☺

THE HEADS OF THE G20 THEMSELVES, LIKE ALL ORGANISATIONS THAT ASPIRE TO MANAGE GLOBALISATION, HAVE LOST THEIR BEARINGS. BY CONFUSING THE COMPASS POINTS FOR THE GLOBAL ECONOMY, THE DISTORTING MIRRORS OF TAX HAVENS MARKEDLY REDUCE COUNTRIES’ ABILITY TO INFLUENCE THE COURSE OF HISTORY, AND EFFECTIVELY THEIR SOVEREIGNTY.

adopted a law regarding trusts that enabled the opaqueness of the system to be increased without anyone objecting. For Chavagneux et al., “*the legislators did exactly what the local financial services industry demanded (...). In exchange for legislation, tax havens receive an income from the business that the offshore*

mine the laws applicable to non-residents, by buying the sovereignty of such and such an island or other small country. What is in play offshore is actually the confiscation of countries’ sovereignty by multinational companies and their legal and financial intermediaries – or as Alain Deneault puts it,

THE WINNERS

TAX HAVENS ARE BETTER OFF, BUT ARE VULNERABLE

It is to tax havens’ advantage to attract multinational companies: Luxembourg, Bermuda and Liechtenstein are in the global top five in terms of GDP per inhabitant (Liechtenstein is in the lead with €97,680 per inhabitant in 2007).⁵

Receiving even 1% of the profits recorded on their territory in tax represents a significant amount for most of them, as their modest size and small population result in lower public expenditure than in large countries. However, these economies are vulnerable: those who use them have no ties to the territory, moving their fortune or their fictional subsidiaries at the slightest worry will matter very little to them. In fact, after the scandal of the client lists sold to the German tax authorities, the LGT-Bank in Liechtenstein saw cash inflows collapse by 95% compared with the previous year in the first six months of 2008. Likewise, the Cayman Islands found themselves on the brink of bankruptcy due to the impact of the financial crisis. Tax havens are also at the mercy of a scandal or a change in the political environment, like Nauru, an island in the Pacific that was bankrupted after it was sidelined at the turn of the 20th century, for example.

¹ In economic theory, this consists in extracting benefits from a processing without paying any of the costs.

² *Idem*, p. 31.

³ *Op. cit.*, *L’Économie politique* n° 42, p. 32. Our translation.

⁴ A. Deneault, *Offshore*, La Fabrique, Éditions, 2010, Paris, p. 117.

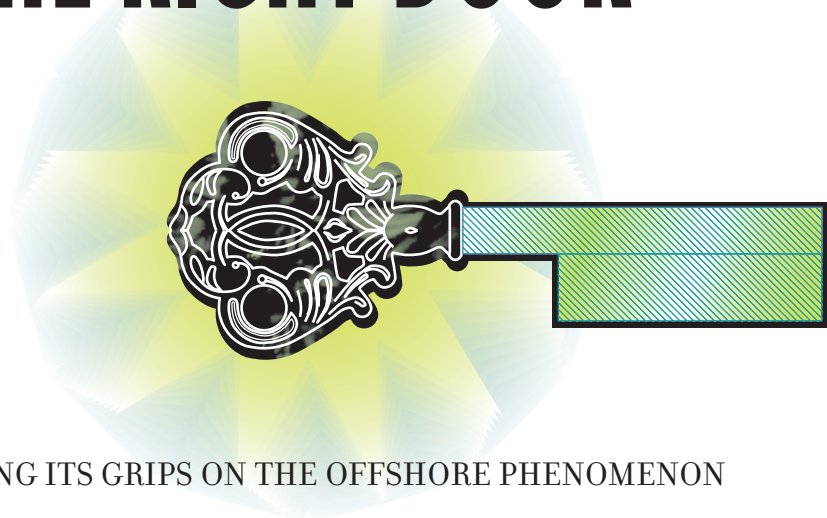
Our translation.

⁵ Source: *CIA World Factbook*.

CHAPTER



THE EU AND THE G20 HAVE THE H(E)AVEN'S KEYS THEY JUST NEED TO OPEN THE RIGHT DOOR



BY GETTING ITS GRIPS ON THE OFFSHORE PHENOMENON
AS IF IT WAS AN UNFAMILIAR ISSUE, THE EUROPEAN UNION, LIKE THE G20,
ARE CONFUSED OF WHAT TO TARGET. BREAKING THE MIRROR IS NOT ENOUGH:
THE DEFORMED REFLECTION OF THE ECONOMY SEEN IN THE TAX HAVEN
MIRROR IS PRODUCED BY THOSE BODIES' OWN BANKS
AND MULTINATIONAL COMPANIES.

Offshore finance is like air traffic, with its hubs¹ and transit zones. However, unlike human beings, capital has no borders. Most international efforts aimed at combating dirty money and tax evasion consist in putting pressure on certain hubs, which are known as “non-cooperative jurisdictions”. This amounts to misunderstanding the way offshore finance works. The tax havens are not the ones lying about where wealth is located: they are simply protecting the lie. At heart, the people who use them do not actually care about which secrecy jurisdiction their funds pass through. They are no more attached to them than air travellers are to one hub or another. Trying to find out the identity and the motives of those who use tax havens, and of their intermediaries would be a much more effective way of bringing hidden financial practices to light.

1 A hub is a transit platform that enables passengers to change flights quickly and easily (techno-science.net)

THE G20 AN INDETERMINATE STRATEGY



THE G20 IS ACCUSING TAX HAVENS OF HAVING PLAYED A PREDOMINANT ROLE IN THE FINANCIAL CRISIS, AND HAS CHOSEN TO POINT THE FINGER AT THEM TO BRING THEM BACK INTO LINE. THIS IS A CONVENIENT CHOICE, ALTHOUGH REAL PROGRESS IS IN DOUBT.

The OECD regularly reviews the progress accomplished since the London G20 Summit in April 2009, which declared an open season on tax havens. As at November 5th 2010, the black list was blank and the “grey” list only included nine countries, compared with 42 in April 2009. If we believe the OECD, this problem would be solved soon.

DEVELOPING COUNTRIES HAVE BEEN FORGOTTEN

In a report dated September 28th 2010,¹ the OECD highlighted the progress made in terms of tax cooperation, which included the signing of 397 tax information exchange agreements (TIEAs) compared with only 50 in 2009. However, that number is insignificant when compared with the potential number of such agreements, i.e. 58,000, inasmuch as there are 242 jurisdictions with a sovereign tax system.

Moreover, up until now, the initiative has not benefited developing countries at all. The *Convention on Mutual Administrative Assistance in Tax Matters*, which was amended in April 2010 in order to allow the exchange of tax information on request between all the signatory countries, and which is backed by the OECD and the Council of Europe, could benefit countries from the South. They still have to be asked to sign the Convention -and that tax havens required to do the same.

The OECD, which was criticised for being lax for “whitewashing” tax havens too quickly, introduced a “peer review” mechanism in March 2010, which is aimed at assessing the fulfilment of tax co-operation promises, under the guidance of the Global Tax Forum. This assessment is welcome. The first results of the review, conducted by individual Governments, should be ready by November 2011, when the G20 is meeting in Cannes. Moreover, it could lead to the publication of an updated list of tax havens by 2014.

THE OECD'S STRATEGY NEED TO BE CALLED INTO QUESTION

Is this enough? Apparently not. Undoubtedly, the assessment will measure the effectiveness of tax cooperation, by addressing the central issue of trusts and shell companies, which create an opaqueness that is largely comparable, strictly speaking, to bank secrecy. However, it raises important issues, such as

“We ask the Global Forum to enhance its work to counter the erosion of developing countries’ tax bases and, in particular, to highlight in its report the relationship between the work on non cooperative jurisdiction and development. The results will be reported at the Summit in France [November 2011]”.
Seoul Development Consensus for Shared Growth. November 12th 2010.

¹ http://www.oecd.org/site/0,3407,en_21571361_43854757_1_1_1_1_1_00.html

THE CRITERIA ARE TOO LAX

In April 2009, the OECD ranked tax havens according to their level of cooperation: on the “black” list were countries that had never declared themselves as prepared to cooperate with foreign tax authorities, while the “grey” list featured countries that had only committed to do so verbally and the “white” list countries that had signed tax information exchange agreements (TIEAs) with at least 12 countries.

This is a limited commitment, as there is nothing automatic about such cooperation (unlike the way in which the EU applies the Savings Directive). It is up to the tax authorities that have been cheated to ask for specific information, and then up to the authorities who have been called upon to assess the relevance of the request before responding to it. The secrecy jurisdiction that host companies, trusts or foundations most of the time doesn't know the beneficial ownership – that means it does not have the information that has been requested.

In addition, the 12-treaties hurdle enables territories to buy themselves good behaviour at a lower cost: in one year, Luxembourg, Switzerland, Liechtenstein, the Cayman Islands, Bermuda and even Singapore gained access to the “white” list... sometimes by signing treaties among themselves, or with Greenland and the Faroe Islands! Among the 33 tax havens that have been “white-washed” since April 2009, 17 are believed to have used this process to reach the 12-treaty hurdle.⁵ Finally, the OECD is only interested in tax issues, and not in the obstacles that tax havens put in the way of the law and financial regulatory authorities.

be ranked? Where will the black line and the grey line be drawn?

Finally, there is a political issue. At the G20 Summit in London, the OECD already spared a few big fish, including Jersey, Delaware, Mauritius, Barbados and even London.⁶ The Global Forum Assessment Group, which is chaired by François d'Aubert, is undoubtedly determined. However, will it be able to display total objectivity and avoid any diplomatic pressure with Singapore and Jersey as its vice-presidents?

There is a certain degree of incongruity in expecting the G20 to come up with such a list as if it was unaware of financial secrecy. On the contrary, the G20 creates financial secrecy, both in its midst and in territories that are dependent on its members. Based on the financial secrecy index established by the Tax Justice Network, we have calculated that the G20 countries accounted for 39% of global supply of financial secrecy services. That ratio rises to 88% if we add in the European Union and the countries under its influence ✨

●●● issues of priority, in the first instance.

Although exchanging information enables a greater clampdown on tax evasion by individuals, or obvious corporate evasion, it will be of no use whatsoever for tracking the manipulation of transfer prices and other complex tax avoidance strategies, which are nonetheless the most costly in terms of public funds.

Then there are operating issues. International bodies no longer draw up a list of tax havens worthy of that name. The Financial Stability Board (FSB) and the Financial Action Task Force (FATF), the inter-governmental body responsible for combating money-laundering and terrorist financing, were called upon by the G20 in Seoul, when it asked them respectively to produce a list between now and the Spring and between now and February 2011.² How can we still give any credit to the OECD list? Among the nine survivors that still feature on the grey list, there are only financial centres as “strategic” as Niue, Nauru, Montserrat or Vanuatu!³ Altogether, these centres only account for 0.17% of global offshore finance. This absence of a credible list destroys the sanction strategy issued by the G20. For example, what will be the scope of the French measure aimed at making the cost of transactions in non-cooperative territories more expensive?⁴

There is another strategic issue. Will the pressure exerted by the Global Forum on Transparency and Exchange of Information for Tax Purposes be as strong as that of stigmatising countries by putting them on a list? We would bet heavily against it. Although they are open to criticism, media coverage of the OECD lists undoubtedly forced the targeted territories to change. However, basing the entire international effort on an administrative assessment process, which is less transparent, means running the risk of restricting the debate to experts, without the targeted country worrying unduly.

There is obviously a technical issue. What will the criteria for the next list be? The ones selected in April 2009 were heavily criticised (see box). It is unlikely that any country will be considered as complying fully with the tax information availability and accessibility requirements expressed by the Global Forum. In this case, how will countries that have been assessed

2 The G20 asked them for this list in April 2009. In October 2010, the FATF published a list of «defaulting» States (Iran and North Korea), having claimed in June 2010 that it was closely monitoring the anti-money laundering efforts in 25 countries. Cf. <http://www.fatf-gafi.org/dataoecd/17/4/45540819.pdf>.

The FSB did not mention this in its action plan which was presented to the G20 in May 2010 – cf. http://www.financialstabilityboard.org/publications/r_100510.pdf.

3 Followed by Liberia, Uruguay, Guatemala, Costa Rica and Panama.

4 France has its own list of non-cooperative territories, which is very similar to that of the OECD.

5 Our calculation covers the tax information exchange agreements (TIEAs) identified by the OECD, but does not include double-taxation treaties.

6 Although China feature on the “white” list, a footnote reminds readers, without naming them, that Hong King and Macao are not yet considered as “cooperative”.





0 is the number of criminal sentences handed down in France for tax evasion in transfer mis-pricing cases.

PUTTING USERS UNDER PRESSURE

For the G20 and the European Union, putting pressure just on offshore finance transit zones to obtain a few pieces of information in the long-term and in the best case, would be a delaying tactic. In fact, it would be easy for them to obtain the information from offshore “fund carriers” or directly from the main travellers to offshore territories. A hard look at the tax authorities’ greatest victories over the past two years (see box p. 51) definitely argues for increasing the pressure on legal and financial intermediaries. Meanwhile, accounting secrecy, which allows companies to lie about where the value they produce is located, is likely to be the next logical step after banking secrecy in the combat launched by the G20 against tax havens. The major powers are timidly planning initiatives in both areas.

BANKS AND TAX ADVISERS

Between 2000 and 2007, the United States only asked Switzerland for information on 13 occasions, because the information exchange agreement between Bern and Washington (which is close to the model TIEA recommended by the OECD) was so restrictive. This number should be compared with the 14,700 US tax evaders with accounts in Switzerland who came clean following the UBS scandal in 2009! The Obama Administration seems to have fully understood that in order to track down tax evasion the point is asking banks for more information rather

than waiting for information from tax havens. On March 24th 2010, the United States Senate passed a bill (the Foreign Account Tax Compliance Act or FATCA), which will force foreign financial institutions to reveal their banking relationships with US taxpayers to the US tax authorities, from 2013.

France, meanwhile, has required all banks to disclose a list of financial transfers made by their clients in tax havens since 2009 - but its list of 18 territories avoids all the large offshore centres.

In the United Kingdom, the previous government headed by Gordon Brown adopted a law that requires companies and tax advisors to notify Her Majesty’s Customs and Excise of their tax planning schemes.

BREACHES IN ACCOUNTING SECRECY

Other initiatives will put direct pressure on multinational companies. What is their aim? To force multinational companies to account for their actions! The “revolution” enacted by the European Commission in a press release dated April 21st 2010 did not go unnoticed: it drew attention to the link between tax havens, multinationals and poverty for the first time, and asked companies to provide an overview of their results, on a country-by-country basis. On June 14th 2010, the European Council for Foreign Affairs, under the Spanish presidency, took up the proposal on its own account. The Commission crossed a new hurdle

PROOF BY EXAMPLE

THE DODD FRANK ACT, REPORTING ON A COUNTRY-BY-COUNTRY BASIS IS POSSIBLE!

The scope of this measure, which was adopted on July 21st 2010 in the United States, is decisive. Article 1504 includes a requirement for extractive sector companies listed in New York, i.e. around 90% of international oil and gas companies and 80% of major mining companies, to inform the US Stock Market watchdog (the SEC) of all payments made to foreign governments, on a project-by-project basis. If applied, this measure will enable people in developing countries to hold their government to account regarding the way in which oil, gas and mining revenues are spent. It will also enable people in Northern countries to question their national companies about their foreign business operations. This reform follows a similar measure introduced to the Hong Kong Stock Exchange in May 2010.

“[The European Parliament] calls on the Commission to ask the International Accounting Standards Board (IASB) to include among these international accounting standards a country-by-country reporting requirement on the activities of multinational companies in all sectors”.

European Parliament resolution of 23 September 2008¹

on October 26th, when it launched a consultation process that remained open until December 22nd, in order to gather stakeholders’ views on the idea of requiring multinational companies report on a “country-by-country” basis.²

This is a useful initiative that completes the tax and development initiative that was launched under the auspices of the OECD in April 2010, as part of a “taskforce” involving NGOs, companies, and developing

¹ European Parliament resolution of 23 September 2008 on the follow-up to the Monterrey Conference of 2002 on financing for Development (2008/2050(INI)).

² Cf. http://ec.europa.eu/internal_market/consultations/2010/financial-reporting_en.htm

THE TAX AUTHORITIES' GREATEST VICTORIES SINCE 2008⁶

In less than two years, the names of over 30,000 German, French and US taxpayers have been disclosed to the tax authorities in those three countries, unbeknownst to the banks.

The LGT Affair. In February 2008, Germany bought a list of 1,400 individuals and companies in 10 countries from one of the Liechtenstein bank's employees. The file enabled France to obtain €5.2 million in unpaid taxes from 64 families. Three files involving companies were referred to the public prosecutor in Paris.

The Credit Suisse Affair. In February 2010, Germany did it again, buying over 1,500 names of German taxpayers who held accounts in Switzerland for €2.5 million. Since then, 11,200 tax evaders have come clean to the tax authorities, which expect to retrieve over €1 billion in unpaid tax arrears.

The UBS Affair. UBS, which turned a deaf ear to the US tax authorities when they asked for the bank details of 250 US citizens, found itself threatened with the withdrawal of the licence that enabled the bank to operate in the United States. As it generates a third of its business in that country, its only option was to comply and pay US\$900 million in fines. This was too late for the US Government, which has already launched legal proceedings against UBS to obtain information on 52,000 accounts. Diplomatic negotiations between Washington and Bern allowed for the disclosure of 4,450 names, which ultimately prompted 14,700 taxpayers to voluntarily come clean with the tax authorities.

The HSBC Affair. France has got hold of a list of 130,000 clients of the bank's Swiss subsidiary, HSBC Private Banking, via a former employee of that company. There are at least 3,000 French taxpayers among those clients. Other tax evaders took fright and came clean to the "regularisation unit" for hidden capital.

³ <http://www.iasb.org/NR/rdonlyres/735F0CFC-2F50-43D3-B5A1-0D62EB50-DB99/0/DPExtractiveActivitiesApr10.pdf>

⁴ Jointly launched by CFDT, CGT, Solidaires, SNUI, Attac, Oxfam France and the "Plateforme Paradis Fiscaux et Judiciaires" in September 2009.

⁵ D. Baert et G. Yanno, *op. cit.*, 2009.

⁶ Jean Merckaert and Renaud Fossard, *op. cit.* 2010.

... and wealthy countries. A sub-group is examining the possibilities and limits of this country-by-country reporting initiative.

The current reform of the international accounting standard for the mining industry sector (IFRS 6) could show the way forward. The first draft of the revised standard that was submitted to the IASB for consultation suggests forcing companies in the sector to publish their financial statements on a country-by-country basis. However, the range of the information requested is very limited and, most importantly, this text enables companies to bypass this obligation when they take the view that the information is not significant or could be detrimental to them!³ A second text will be submitted for discussion in 2011. Pending this accounting reform, which will only be finalised in 2014 at the earliest, stock market regulation goalposts are shifting: on the Hong-Kong Stock Exchange in May 2010 and on Wall Street in July, listed companies in the mining sector have been forced to publish the payments that they make to the government in each country where they operate.

The idea of imposing an obligation of transparency on banks is also making progress in the financial sector. Since June 2009, French law has required banks to provide details of their offices and their business activities in the 18 "non-cooperative"

jurisdictions listed by Paris in an appendix to their annual reports. Local authorities, who were questioned by CCFD-Terre Solidaire as part of the "Stop Tax Havens" campaign,⁴ have gone further. On June 17th 2010, the Ile de France Regional Council unanimously passed a resolution asking its financial partners (banks and possibly insurance companies) "to provide a statement, on a country-by-country basis, regarding their business activities, their employees and the taxes and levies paid to local authorities". That information will be examined under the microscope before committing to any financial transaction. Since then, the initiative has spread like wildfire. Twelve French regional authorities out of 22 have expressed a similar desire which has been reflected in legally binding texts in four other cases (the Rhône-Alpes, Champagne-Ardenne, Alsace and Auvergne regions). Transparency on a country-by-country basis, which is now a requirement for financial partners, could involve other sectors of the economy in the future. In addition, towns (Villeurbanne, for example) are showing an interest in this approach. Will governments listen to the legitimate desire of local authorities to force multinational companies to be more transparent? As chair of the G20 in 2011, it would be an inspired move on the French Government's part to make that desire a priority. ✨

REFERENCE POINT

THE INTERNATIONAL ACCOUNTING STANDARDS BOARD (IASB)

The IASB is a private body responsible for setting the accounting standards in force in 110 countries, including the 27 members of the European Union. The IASB was founded in 2001 in response to a request made by investors to harmonise the standards in order to compare companies. Having abandoned their legislative powers in terms of accounting standards, governments now rely on a strictly private player, dominated by the Big Four, to say how companies should account for their business activities. The IASB, which meets in London, is governed by the IASC (International Accounting Standards Committee), a foundation based in Delaware (the main tax haven in the United States) that consist of 22 trustees⁵. The IASB Monitoring Board, which was set up in the wake of the 2008 financial crisis, no longer gives governments much say when defining standards, displeasing some countries, including France. The G20, meanwhile, regularly asks for convergence between accounting standards on a global basis, including between the IASB (IAS/IFRS) standards and the FASB standards that apply in the United States.

RE-ESTABLISHING THE ECONOMIC TRUTH OUR RECOMMENDATIONS

for the G20 countries and the European Union

THREE SETS OF PRIORITY MEASURES ARE CONSIDERED AS NECESSARY FOR ENDING THE CURRENT DISCONNECT BETWEEN THE GEOGRAPHY OF REAL ECONOMIC ACTIVITY AND ACCOUNTING GEOGRAPHY, AND THEREBY HELPING GLOBAL ECONOMIC BAROMETERS TO MAKE SENSE AGAIN.

1. REQUIRING MULTINATIONALS TO PUBLISH THEIR ACCOUNTS ON A COUNTRY-BY-COUNTRY BASIS, OR EVEN ON A SUBSIDIARY-BY-SUBSIDIARY BASIS

WHY?

The international community will never publish an exhaustive and objective list of tax havens: its government by consensus forbids it from blacklisting countries like the United Kingdom or the United States, for instance. Conversely, a company ought to be able to justify the reality of its economic activities everywhere it operates, regardless of whether the country where those activities are located is classified as a tax haven by one country or another. Confederations of Business and other employers groups ought not to be opposed to this move. In fact, in December 2009, the MEDEF (main French employers' association) protested against France including Chile on its tax haven list, which the government was contemplating at the time.¹ In their view, there was no reason to increase the costs for a French company, like Veolia in the transport sector, of developing a real economic business in Chile. The MEDEF is right on that point, but the quid pro quo is that the economic activity must be real. Only the company can testify to that, by providing a detailed explanation of the business conducted by each of its subsidiaries on a country-by-country basis. If its business operations correspond to a real business activity, it has nothing to hide. At present, however, the study conducted on 50 European companies (Chapter 2), shows that this information is not accessible to the general public, or even to shareholders and government bodies. Moreover, the data gathered do not enable us to distinguish between genuine subsidiaries and empty shells.

WHAT WE WANT

We are recommending that every company with international business activities be required to publish the following details for every country where they operate:

- the name of all its subsidiaries in the country in question;

- details of their financial performance, including
 - sales, both to third parties and to other group subsidiaries,
 - purchases, both third parties and with intra-group transactions,
 - labour costs and employee number,
 - financing costs, split between third parties and those paid to other group members,
 - and pre-tax profits;
- details of the tax payments included in its financial statements for the country in question;
- details of the cost and net book value of its tangible fixed assets;
- details of its gross and net assets.

HOW?

There are several ways of introducing this obligation to report on a country-by-country basis:

- Stock market regulation in each financial centre, for listed companies: in the mining sector, Hong Kong and the United States have tighter transparency requirements than European stock markets (see the "Dodd Frank act" box)!
- The European Union Transparency Directive (TD),² which is currently under review, provides an opportunity to extend this obligation to all listed companies at the European level.
- International accounting standards, which are mainly issued by the IASB for 110 countries, including the 27 EU Member States, and by the FASB for the United States. These standards apply to the vast majority of companies

1 « Paradis fiscaux : le patronat défend les entreprises de bonne foi », Les Échos, December 8th 2009.

2 <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CONSLEG:2004L0109:20080320:FR:PDF>

3 Conclusions on tax and development – Cooperating with developing countries to promote good governance on fiscal policy issues.

“The EU and its Member States should enhance the coherence of their development policies and move forwards by exploring [the option of] reporting on a country-by-country basis as the standard for multinational companies (...)”

Conclusions of the European Foreign Affairs Council Meeting of June 14th 2010³

- listed throughout the world and are expected to converge (a wish regularly expressed by the G20). Their modification would be a major leverage to force these companies to transparency: we propose revising,
 - IFRS 8 on the presentation of information on operating segments would be a powerful catalyst for requiring companies to be more transparent. The issue of reporting on a country-by-country basis is expected to feature in the European Commission's report to the European Parliament on the application of that standard, which is expected in late 2011 at the earliest;
 - IFRS 6, which applies to the mining sector. The standard is also under review, and the second version of the draft revised standard ought to be published in autumn 2011.
- The inclusion of such a requirement for multinational companies in the OECD guidelines, for which the results of the review process are expected in spring 2011, and in the OECD corporate governance guidelines would represent a very welcome development, but cannot be a substitute for a compulsory standard.

"Multinational companies must make a detailed break-down of their results on a country-by-country basis"

François d'Aubert, the French general representative in the campaign against non-cooperative countries and territories, 2nd April 2010⁴

2. PUTTING AN END TO SHELL COMPANIES

WHY?

Millions of companies, trusts and other secretive entities conduct economic activities throughout the world without any government authority being able to determine the beneficial ownership of said legal structures. This is an open door for off-balance sheet accounting, insider trading, money-laundering and even tax avoidance. It also guarantees a total refusal to cooperate on legal or tax matters.

WHAT WE WANT

We are asking the G20 and European Union countries to force all legal entities to register with a government authority in order to exist legally and to perform economic transactions. To this effect, each government or territory must undertake to:

- keep a register of the trusts and/or other secretive legal entities existing under its national laws. That register should specify the name of the real beneficiaries, the operators and the order givers;
- make the information available to the tax, customs and legal authorities in other countries on an ongoing basis;
- make sure that the trade registry imposes the same minimal requirements in terms of transparency.

Moreover, a register of bank accounts accessible to those same authorities should be drawn up in each country. Several European countries, including Spain and Germany, have such an instrument, for which the French tool (FICOBA, or the National Register for Bank and Related Accounts) serves as a benchmark. Jacques Barrot, who was

"I now call on the OECD to look at the feasibility of introducing multinational guidelines on Country-by-Country Reporting through a full and open consultation with governments, multinationals and civil society partners."

Stephen Timms, former Treasury Minister, 28th of January 2010,

OECD conference on tax and development in Paris.

the European Union's Commissioner for Justice, Freedom and Security, issued a press release in 2008 stating that the European Commission had contemplated this kind of obligation at the European Union level.

HOW?

For the time being, we expect the G20 and EU countries to:

- ask the Financial Action Task Force (FATF) to amend articles 33, 34 and VIII in its 40+9 Recommendations, in order to demand national registers and to make their creation one of the 16 key criteria for compliance with anti-money laundering standards;
- make the availability and accessibility of information regarding the effective ownership of financial assets a determining assessment factor in the Global Tax Forum Peer Review Group valuation reports.
- envisage heavy and coordinated sanctions against countries that do not comply with these specific recommendations within a given timeframe.

3. REINFORCING SANCTIONS AGAINST ECONOMIC AND FINANCIAL CRIME

WHY?

Economic and financial crime, especially in tax matters, would be much less attractiveness if it was no longer so easy to get away with. This is why countries must boost the level and the implementation of sanctions against tax evaders, and those who commit financial misdemeanours or crimes.

WHAT WE WANT

We are asking G20 and EU countries to:

- commit to entering into a multilateral agreement⁵ that would allow an effective exchange of tax information, and to ensuring that territories under their influence and financial black holes enter into the same agreement;
- extend the European Savings Directive, which is based on the automatic exchange of information, to a few developing countries, initially on an experimental basis;
- standardise the legal definition of tax evasion and to demand that the FATF make it an ancillary money laundering offence;
- seize and return the stolen assets from countries where they originate. This is a principle enshrined in the *United Nations Convention against Corruption* (known as the *Merida Convention*), and to adapt the internal legislation in each country in order to make it easier for the relevant non-governmental actors to prosecute those responsible with the purpose of restitution in case of failure of the state where stolen assets originate ✨

⁴ See the interview with *La Tribune* newspaper on April 2nd 2010. François d'Aubert, a former French Research and Budget minister, also chairs the Global Forum's peer review process.

⁵ The United Kingdom has made such a proposal. The updated version of the OECD-Council of Europe Convention on Mutual Financial Assistance could also contribute towards this process, under the condition that the Convention makes compliance with its terms easier for developing countries, puts pressure on non-cooperative companies to make them comply and enables the automation of information exchange.



This publication has been produced with the financial support of the European Union. The contents of this publication are the sole responsibility of the authors and can in no way be taken to reflect the views of the European Union.