



TAX HAVENS AND CAPITAL FLIGHT: *CLOSING THE FLOODGATES*

Moderator's Summary from the 6 February 2007 Roundtable Discussion at the Second Plenary Meeting of the Leading Group in Oslo

While taxation as such is not an “innovative mechanism”, some of the methods used both to evade and recover tax are certainly innovative. Input presented by the panel included most notably facts and recommendations from a report by the Tax Justice Network commissioned by the Norwegian Ministry of Foreign Affairs¹, and from ongoing work by the OECD. The scale of the problem prompted a change in the Roundtable title from “plugging the leaks” to “closing the floodgates”. These are some of the key points that were made:

What is a tax haven?

- A tax haven is characterised by financial transactions taking place without, or with a very low, tax being levied on the transactions and where there's no (or little) transparency or exchange of information.
- The tax havens themselves prefer being called “International Financial Centres”. A common term is “Offshore Financial Centres” (OFC), although being an island state is not a requirement.
- By one estimate traditional tax havens (small countries) represent only about 22 % of total offshore investments – the US, Netherlands, Switzerland and others being larger actors.

The scale of the problem

Measuring illicit flows of money is by nature difficult, but estimates have been made:

- USD 225 billion is lost annually in government revenue.
- USD 148 billion lost to corruption in Africa every year, and 80-90 % of the resulting illicit flows go outside the continent.
- (Italy) € 84 billion held abroad, (US) USD 40-70 billion in annual losses from tax evasion and USD 300 billion held in tax havens, (Ireland) €849 mill. recovered.
- The supply side of corruption has been neglected, as has the intermediary in corrupt deals; the facilitating third party, the tax haven. 53 % of the least corrupt countries are tax havens.
- Tax havens are a clear *symptom* of international corruption, and the geography of corruption must be redefined.
- Transparency International publishes a Bribe Payers Index (supply-side), but it is less well-known than the Corruption Perception Index (demand-side).
- The range and make-up of the tax evader is wider than before, and their numbers are growing.
- Access to tax havens and tax evasion possibilities broader than ever.

¹ “Closing the Floodgates: Collecting Tax to Pay for Development”, Tax Justice Network (John Christensen et. al.), February 2007.

The rationale for combating tax havens and capital flight

- Reducing the amount of tax evasion will have huge benefits, and more so for developing countries with volatile tax collection and a slimmer tax base, than for others.
- OFCs have incentives to improve their exchange of information; international pressure leads to a risk of reputational damage.

Suggested next steps for policy-makers

- The role of direct taxation should be reassessed. We are now seeing a shift of the tax burden from capital to labour. The economic consequences, particularly for poor countries, are bad, with cost of labour being one of their main competitive advantages.
- The playing field must be level, and ethical businesses protected from predatory tax behaviour.
- The demarcation line between harmful and benign practice should be made clear. A simplification and reform of tax regulations would simplify tax systems enormously and be valuable in itself. Regulation should not cost more than it brings in.
- There are mutual benefits from Exchange of Information Agreements. (In an EU agreement, Switzerland has been allowed to keep part of what is recovered from evaded tax).
- Some of the most important building blocks and prerequisites for combating tax evasion are common standards and codes, access to information, improved transparency and increased exchange of information, and international cooperation.
- To a certain extent the challenge is to enforce good practice and to sanction bad practice – which can also be interpreted as doing away with tax havens.
- The standards and the codes are, to a certain extent, in place, agreed and have broad international support. In some areas, such as financial reporting by multinational corporations, improvements are needed. Global fora, including representation from OFCs, are formally committed to model behaviour and to respecting the rules.
- Recommendations and good practice standards are not enough; examples show that even those OFCs that have signed up to this fail to comply when there's no risk of sanctions. Collective action is needed.
- Some specific proposals are; banning various types of secrecy – such as in relation to ownership; require financial intermediaries and professional associations (lawyers, bankers, accountants etc.) to report suspicious transactions; enhance the IMF's reviewing of standards and codes; identify the OFCs failing to cooperate; improve exchange of information such as tax information exchange agreements.
- The UN Tax Commission should be strengthened with developing countries taking greater interest in its affairs.
- Should a world tax authority be established, to tackle harmful practice and violations of rules?
- Investors such as the Norwegian Petroleum Fund should promote ethical investments and avoid utilizing tax havens.

THE PANEL:

Hege HERTZBERG, Deputy Director General, MFA, Norway (Moderator)

John CHRISTENSEN, Director, International Secretariat, Tax Justice Network (Lead Speaker)

Mr. Dónal GODFREY, Head, Harmful Tax Practices Unit, OECD Centre for Tax Policy and Administration (Co-lead Speaker)

Luis Eduardo ESCOBAR, Presidential Adviser to the Technical Group of the Initiative on Hunger and Poverty (GT-7), Chile (Commentator)

Jan BORGEN, Secretary General, Transparency International, Norway (Commentator)