

<b>Forum:</b>	Economic and Social Council
<b>Issue:</b>	The question of offshore banking and tax evasion
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<b>Position:</b>	Chair

## Introduction

Tax evasion and money laundering has always been a critical international issue since offshore banking conduces many obscure economic consequences. It is costing States vast amounts of money due to the fact that the assets owned by an individual or business indicate the level of taxes which they are obliged to pay and some people seek ways to refrain from paying those taxes. This renders people to look for alternative options such as offshore banking. The reason why people choose to open offshore accounts is because of the high interest rates, stricter secrecy laws and perhaps most importantly for paying fewer taxes compared to the country where they actually reside. This means that in countries such as Switzerland and Panama, governments have legislations that are created for attracting foreign customers therefore investment.

Some of the past incidents regarding money laundering includes the offshore banking in Nauru. When Nauru transformed into a tax haven in 1993, it became a viable location for the wealthy to launder their money. In 1998, Russian criminals laundered an estimated sum of £53.7 billion by exploiting shell banks in Nauru. The Naurian banks' operation without verifying the identities of their customers fostered the criminals choice of laundering their money into Nauru. The conspicuous activities of Naurian banks rendered the US to impose sanctions on them. Another example to illegal offshore banking would be the incident which the bank of BCCI is involved in. Dating back to the 1980s, the bank and its customers were founded in fraud for committing money laundering. The amount of money laundered was an estimated £17.6 billion. It was analyzed that the bank had relationships with suspicious and guilty officials from Zimbabwe and Argentina. The bank was later shut down due to its further fraud after an investigation conducted. As we can see, offshore banking not only cripples the budgets of governments but also makes way for the guilty and alleged.

It is the responsibility of ECOSOC to formulate reasonable methods of solving the issue since this is a worldwide problem that affects numerous States' economies.

## Definition of Key Terms

**Tax evasion:** This term covers the illegal methods of avoiding to pay or underpay the taxes of a government which is practised by some individuals, corporations and organizations. Such corporations and individuals who are convicted due to the evasion of taxes will be subject to criminal charges. Misrepresenting income, inflating deductions or expenses, hiding money and hiding interest in offshore accounts are schemes of tax evasion.

**Offshore banking:** Corporations and individuals may open new bank accounts in a jurisdiction other than their home country using a business entity. This is called offshore banking. Businesses which would do this would usually derive benefit from a certain advantage the country offers such as low taxes. This way that country gains the advantage of circulating the monetary assets of that business within the country.

**Tax liability:** Depending on the taxing laws of a State, a business gets taxed. The business is legally bound to pay the taxes to its government. The increase of progressive taxes are parallel to the increase of the income earned.

**Offshore account:** These are accounts opened by an individual in country which they usually do not reside. These bank accounts are used by corporations and individuals to evade their true tax liabilities. They launder a big sum of their capital to another country by establishing a shell company in that country and transferring that sum to that firm's bank account.

**Shell company:** Although a shell company's legitimate purpose is to raise funds before actually starting a business, shell companies can be set up by celebrities, wealthy individuals and also financially mediocre individuals or businesses to hide their true assets from their governments. So, shell companies are the address of illegitimate purposes too. Business entities obtain shell companies to avoid paying their true tax liabilities by registering to have access to offshore firm accounts.

**Criminal charge:** An accusation in a form of written complaint, information or indictment which becomes a prosecution. Those caught laundering money, evading taxes using offshore accounts are not tolerated and therefore are subject to criminal charges.

**Tax haven:** These are countries with very low tax rates and where many corporations choose to do offshore banking. Since there is lack of transparency, individuals too prefer to work with tax haven countries.

**Capital:** This term refers to the financial assets of an individual or business entity such as cash. However, it also refers to the machinery, production equipment and buildings used as industrial facilities such as factories and other manufacturing facilities. All in all, capitals are assets which are endured for keeping wealth instead of using that wealth to spend on purchasing goods.

## General Overview

### Tax evasion and its consequences

Tax evasion is a phenomenon that affects the social and economic stability of States around the globe. Usually, a vast majority of the citizens pay their taxes to the

government. So it is unjustifiable for others to not adhere to the laws and find a way of underpaying their taxes. It also significantly damages the revenues of governments. Funds that would normally be sufficient to enhance developmental projects are slipping away from governments due to tax evasion. This inevitably impacts the living standards of the citizens. Moreover, companies that do not pay their taxes have an inequitable advantage over their rivals that do pay the necessary taxes. This renders the cheating firms' capital possession to be greater. This reflects negatively upon business competitiveness since the firms that abide by the legal rules lose their share in the market.

### **Money laundering and tax havens**

In many parts of the world, such as the island of Jersey, governments do not raise tax revenue through income tax, therefore tax evasion is not considered a crime. Furthermore, according to international law one State cannot enforce its tax laws to another. In addition to this, tax havens such as Panama have high banking secrecy policies that attract a lot of foreign investment into the country. By hiding true identities individuals are able to hide their true ownerships. What is more is that some multinational corporations abuse the loopholes that exist within some of the countries which they do offshore banking by means of law. Corporations and individuals launder their funds to countries like these to avoid paying their true tax liabilities. Some examples for tax havens are British Virgin Islands, Bermuda, Luxembourg and Belgium.

### **Legitimate and illicit exploitation of offshore banking:**

#### **Legitimate use of offshore banking:**

Companies can be set up at offshore locations to be associated with building up finance, mergers and acquisitions and estate or tax planning according to Financial Action Task Force.

Furthermore, individuals may wish to transfer their money to offshore accounts if they do not want their assets to be monitored by their governments. It is perfectly legal to deposit money in another country for safety matters. This means that the individual's government may be in debt and have bills which demand paying. When this type of event occurs, governments have the privilege of confiscating your money. Asset confiscation has recently occurred in Cyprus, Hungary and Poland. This practise of freezing accounts and therefore not being able to access assets it becoming more common. In addition, depositing money to offshore accounts has another purpose; allocating assets to safer banks. Safer means banks that keep more of your money on hand. Also, offshore customers tend to enjoy benefits which may emerge from currency diversification.

#### **Illicit use of offshore banking:**

To conceal sources of ownership and funds, individuals, corporations and even terrorist organizations establish shell companies. They do this by not complying to reporting requirements, such as not reporting their incomes.

### **Panama Papers:**

These 11.5 million leaked documents which date back to 1977 are from the database

of Mossack Fonseca, world's fourth biggest offshore law firm. The German newspaper Süddeutsche Zeitung, the revealer(although the source is a mystery) of these files conveyed the files to the International Consortium of Investigative Journalists (ICIJ). The ICIJ then transmitted the files to the Guardian and BBC.

What is crucial to know about the incident is the detection of many public officials' secret attempts of evading taxes and international sanctions. Vladimir Putin, for instance had been hiding 2 billion dollars from Russian state banks, although the Kremlin spokesman has denied the allegations and claimed that the concept consists of speculations. Meanwhile, Pakistan's prime minister Nawaz Sharif, Ukrainian president Petro Poroshenko and former Iraqi vice-president Ayad Allawi are among the many politicians who have been hiding their assets, illegally. In fact, the former president of Iceland resigned after the release of the documents. The ICIJ also reports that 33 people and companies blacklisted by the US government is also a part of the scandal. The names are businesswise directly related to Mexican drug dealers, terrorist organizations and countries which the US has imposed sanctions.

## **Major Parties Involved and Their Views**

### **USA**

In the past USA did not really impose any strict regulations to individuals who desired to keep their assets at offshore accounts. Lately, the US government has changed its policy towards enforcing new laws that would help facilitate identifying which citizens are using offshore bank accounts to evade paying domestic taxes. The US has, since 2009, has rapidly began an investigation progress of identifying tax evaders and charge foreign banks that have allowed US citizens to deposit their funds. For instance, UBC admitted it allowed US citizens to use their bank as a tool of hiding their true assets.

### **Canada**

Although most Canadians pay their mandatory taxes they are legally obliged to, some do get away with paying their true tax liabilities. Canada seeks international collaboration with its partners by sharing data in order to tackle the issue of hidden assets thus tax evasion. Canada is working closely with the Joint International Taskforce on Shared Intelligence and Collaboration (JITSIC) to coordinate tax compliance activities.

### **Switzerland**

Swiss banks are famous for keeping foreign assets. Approximately, one-third of all worldwide funds located in offshore accounts are deposited in Switzerland. In 1934, Switzerland made its private banking laws formal with the Federal Act on Banks and Savings Banks. With this Act, no Bank in Switzerland was allowed to share the identities of account holders. In addition, Swiss laws are based on confidentiality when it comes to banking. Countries have previously complained that Switzerland is encouraging tax evasion due to their banking secrecy provisions. This was addressed at the Organisation for Economic Co-operation and Development (OECD) and the G20. As a result, nearly every country agreed to treaties that would insist on the exchange of banking information in cases of suspected tax evasion including Switzerland. ("The History of Secret Banking in Switzerland.")

## Panama:

Panama is one of the few countries that seems to be attracting mass foreign investment today. Strict banking secrecy laws along with no tax reporting requirements, no income tax, no capital gains tax, no interest income tax no sales tax, no tax on issuance of corporate shares, no tax to shareholders, no stock sale or transfer tax, no capital stock tax no property tax, no estate tax, no gift tax, no stamp tax, no succession tax and no inventory tax is what encourages foreign money to be deposited in Panama. A stable economy and government in charge also positively affects this.

## Organisation for Economic Cooperation and Development (OECD):

OECD is combating offshore tax evasion through international means. In 1996, the OECD States commenced their harmful tax practices initiative aimed to improve transparency and the exchange of tax information both within and outside the OECD. In 2000, with the report of Towards Global Tax Co-operation included 35 jurisdictions that met the criteria of being a tax haven. The process of these jurisdictions' improvement in transparency was also included in the report. Thanks to the efforts of OECD, 35 jurisdictions have committed to implement the standards of transparency. Andorra, Liechtenstein have not pledged to follow the principles of exchanging information and transparency.

## G20

This international forum consists of governments and central bank governors from the 20 well-developed economies. Its work is to ensure financial stability through means of promoting high-level discussion of policy issues. They hence study and review existing policies. In 2014, at Sydney, agreed upon a new standard of sharing tax information that was asserted and orchestrated by the OECD. This way, countries are automatically able to exchange tax informations.

## Timeline of Events

<b>1815</b>	Offshore banking is born at the Vienna Congress.
<b>1889</b>	The decline process of the British Empire and the relaxation of Business Incorporation Laws of Delaware facilitate the improvement of the pathway for offshore banking.
<b>1925</b>	UK passed a legislation that made it easier for its citizens to access financial trust services and to keep their financial dealings hidden.

<p><b>1929</b></p>	<p>Egyptian Delta Land and Investment, a company registered in London but had its headquarters in Cairo, according to the London courts did not have to pay taxes to the British government by making use of the offshore banking mechanism in the country.</p>
<p><b>1957</b></p>	<p>The Bank of England entered an agreement with British banks to create a temporary and informal allowance for banks in the UK to conduct unregulated deals with non-British clients provided they dealt in foreign currency. "History of Offshore Banking. Does It Really Have a Future?"<a href="http://www.worldoffshorebanks.com/history-of-offshore-banking-does-it-really-have-a-future.php">http://www.worldoffshorebanks.com/history-of-offshore-banking-does-it-really-have-a-future.php</a></p>
<p><b>1980</b></p>	<p>Treaty between Luxembourg and Italy put a cap on the tax rates that the citizens of both countries were required to pay "History of Offshore Banking. Does It Really Have a Future?" <a href="http://www.worldoffshorebanks.com/history-of-offshore-banking-does-it-really-have-a-future.php">http://www.worldoffshorebanks.com/history-of-offshore-banking-does-it-really-have-a-future.php</a></p>
<p><b>2005</b></p>	<p>Savings Tax Directive is introduced by European Union governments to remove cross-border interest payments.</p>
<p><b>2012</b></p>	<p>Cyprus's (a popular tax haven) near bankruptcy began to degrade the prominence of offshore banking.</p>
<p><b>2013</b></p>	<p>Bankers in the EU Member States are required to share their clients' transaction records and identities automatically since the EU Economic and Financial Affairs Council passed a new directive.</p>
<p><b>2015</b></p>	<p>A Protocol is signed between Switzerland and the EU making amendments to the country's existing savings laws to transform it into an automatic exchange of financial information agreement based on a global standard. "History of Offshore</p>

	Banking. Does It Really Have a Future?" <a href="http://www.worldoffshorebanks.com/history-of-offshore-banking-does-it-really-have-a-future.php">http://www.worldoffshorebanks.com/history-of-offshore-banking-does-it-really-have-a-future.php</a>
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## Relevant UN Documents

### **United Nations Practical Manual on Transfer Pricing for Developing Countries:**

The United Nations Practical Manual on Transfer Pricing for Developing Countries is a response to the need for clearer guidance on the policy and administrative aspects of applying transfer pricing analyses to the transactions of MNEs. Such guidance assists policy makers and administrators in dealing with complex transfer pricing issues, but also taxpayers in dealing with tax administrations.

"Transfer Pricing." <http://www.un.org/esa/ffd/tax/TransferPricing/index.htm>

### **United Nations Code of Conduct on International Cooperation in Combating International Tax Evasion and Avoidance:**

Putting an end to international tax evasion is obviously not an easy task, therefore requires international cooperation. International norms of conduct may facilitate the process of international cooperation. This document sets the ways for acting towards removing tax evasion.

### **UN Resolutions:**

ECOSOC resolution 2004/69 on "Committee of Experts on International Cooperation in Tax Matters", 11 November 2004

ECOSOC resolution 2006/48 on "Committee of Experts on International Cooperation in Tax Matters", 28 July 2006

## Treaties and Events

### **Multilateral Convention on Mutual Administrative Assistance in Tax Matters:**

This Convention was jointly developed by the Council of Europe and the OECD in 1988. The Convention is the most comprehensive multilateral instrument available for all forms of tax co-operation to tackle tax evasion and avoidance, a top priority for all countries. 108 jurisdictions currently participate in the Convention. "Convention on Mutual Administrative Assistance in Tax Matters." <http://www.oecd.org/ctp/exchange-of-tax-information/convention-on-mutual-administrative-assistance-in-tax-matters.htm>

## **The Standard for Automatic Exchange of Financial Account Information (AEOI):**

The Standard for Automatic Exchange of Financial Account Information, developed by the OECD with G20 countries, represents the international consensus on automatic exchange of financial account information for tax purposes, on a reciprocal basis. Over 60 jurisdictions have committed to implementing the Standard and all financial centres have been called to match those commitments, as of July 2014. "Standard for Automatic Exchange of Financial Account Information in Tax MattersEn."

### **Other Treaties and Events:**

The Manual for the Negotiation of Bilateral Tax Treaties between Developed and Developing Countries

OECD Model Convention on Income and on Capital

OECD Action Plan on Base Erosion and Profit Shifting

United Nations Code of Conduct on International Cooperation in Combating International Tax Evasion and Avoidance

The Exchange of Information on Request (EOIR)

## **Evaluation of Previous Attempts to Resolve the Issue**

Although the G20 has asked all countries to sign the Multilateral Convention on Mutual Administrative Assistance in Tax Matters, and although it has persuaded the OECD to compose short-term progress report pertaining transparency and the exposition of informations, tax evasion remains a great threat to the budgets of governments. Even though these contributions are a good stepping stone on examining and tackling the issue, they are not adequate since these steps do not actually directly deal with the perpetrators of crime.

## **Possible Solutions**

This issue can be examined in a variety of ways thus solutions can be provided for multiple platforms. The identification and prosecution of more individuals who are acting against the law by enforcing new and stricter regulations is perhaps the core of solving the issue at a national scale.

On the other hand, there seems to be lack of responsibility on the banks when it comes to tax evasion. So establishing new regulatory guides which the banks would legally have to be bound adhere to would help improve the situation. In addition, efficient cooperation between law enforcement authorities and tax administrators can be improved to crack down tax evasion.

Furthermore, international coordination needs more emphasis. Measures that will be taken at every country, especially tax havens, holds immense importance. Secrecy fosters money laundering, so more countries should be able to adapt laws towards transparency in regards to international collaboration.

Finally, exposing corporations that abuse the loopholes there are to the international community may be a sound step to tackle the issue. The deterioration of their reputation may result in considerable loss of revenues.

## Useful Links

[http://www.swlaw.edu/pdfs/lawjournal/17\\_1najera.pdf](http://www.swlaw.edu/pdfs/lawjournal/17_1najera.pdf)

<http://www.munish.nl/pages/downloader?code=ecosoc02&comcode=ecosoc&year=2015>

<http://www.oecd.org/general/oecdreportsprogressinfightingoffshoretaxevasionbutsaysmoreeffortsareneeded.htm>

<http://www.un.org/esa/ffd/documents/tax-committee-documents/tax-ecosoc-resolutions-and-decisions.html>

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