

# Tax Havens - The "Black Hole" of the International Finance

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## Abstract

*Tax evasion is a high interest topic, frequently approached both now and in the past because it is a very common phenomenon in all countries (either developed or emerging) and is particularly important. Tax evasion determines the occurrence of a set of creative accounting practices used in the context of what is considered to be right and what goes beyond the ethical limits.*

*The article presents, in general, tax evasion both theoretically and practically, examines the various ways in which evasion is interpreted by the laws and regulations adopted in the fiscal field, the ways that lead businessmen to perform and fraudulently register operations. Also, we aim at characterising the states that help the economic operators and the individuals, by means of tax havens and implicitly offshore companies, in order to avoid the payment of certain taxes that are higher than in the home country.*

**Key words:** tax haven, tax system, foreign capital

**J.E.L classification:** F38, F40

## 1. The background of the researched topic

The reason for choosing this widely debated issue derives from the desire to fathom the topic of tax havens, since it is very important, both for the EU and for all the Community countries, as well as internationally because fraud and tax evasion represent that phenomenon by means of which one or more taxpayers evade paying tax liabilities and the duties and taxes, or any other amounts owed to the state budget.

In the past twenty years, the ever growing liberalization of markets, products (goods and services) and productive factors, especially of the capital, has emphasized, both in the EU as well as internationally, the divergences between tax treatments and tax rates embraced by various countries in terms of income on their territory. From the various forms of tax planning both international, implemented in order to minimize the tax burden, as well as social, highly important being the use of tax structures residing in the countries with a privileged tax system, also called tax havens.

Often, the countries that implement a privileged tax system are also equipped with more simplified norms concerning the rights of the trading and banking entities. In general, tax havens are often corporate and banking havens and, in some cases, even penal havens in the sense that to the corporate and banking tax simplification it is added a penal system that does not include, for example, the tax evasion offense, false accounting, corruption and recycling.

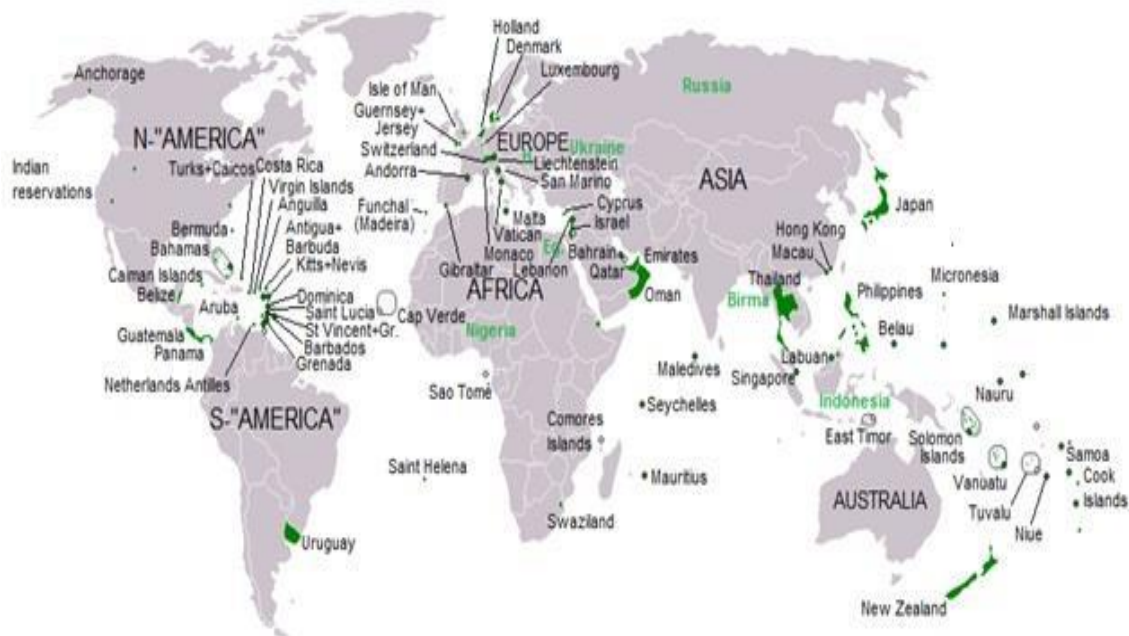
The fight against evasive practices that imply the transfer of the tax base to the countries with privileged tax regimes through ad hoc operations, without any valid economic reasons and aiming solely the obtaining of tax benefits, represents a priority for countries with high taxation. (Alonso *et al.* 2008, p.211)

The moment that stressed the development of the concept, but also of the phenomenon of tax havens occurred immediately after the Second World War, when the number of subsidiaries of

parent companies developed. Therefore, we can state that the former colonies, which have gained independence after the war, used a favourable tax legislation so as to be able to provide the funds necessary for development and functioning, because the phenomenon of liberty, although politically positive, showed drawbacks in the financial plan. As a result, the colonies have lost the financial aid from the metropolis and were forced to find other sources of income. Due to these economic conditions, the colonies were interested in creating a favourable environment for attracting foreign capital in the form of tax facilities, this leading to the emergence of tax havens mainly in these areas. (Buzan, 2012, p.19)

A tax haven is a country whose regulations concerning the tax base, the banking and/or financial sector allow the attraction of capital due to the extremely favourable conditions. Usually, in the tax havens, a very low or even absent tax regime is practiced, this making very convenient the establishing in these states of a company's headquarters (for example: an offshore company) or extremely rigid rules concerning bank secrecy, this allowing to carry out hidden transactions.

Figure no.1. The geographical location of tax havens



Source: (www.ziare.com, accessed on 16.05.2016)

Actually, the success of tax havens can be explained, both for individuals as well as for companies, through the need for a safety valve in an ever growing oppressive world. Tax havens are countries that have some odd characteristics, the most important being that is applied a minimum tax or none at all (zero tax) on foreign capital and on the foreign income of their own citizens and/or companies.

## 2. The comparative analysis of tax evasion between EU and Romania

It is well known the fact that tax evasion is nowadays a growing phenomenon, a continuous concern for the tax authorities, both in Romania and the European Union. Over the years, measures, laws and regulations have been taken against the evasion phenomenon, in order to reduce its high level of spread.

In order to accomplish an analysis that can determine whether all the laws in question had or not any effect on the taxpayers, whether they complied with the provisions and with the tax rates imposed by the state, both in the EU and in Romania, we will use the data concerning tax and budget revenues, as follows:

Table no. 1. Tax revenues and budget revenues

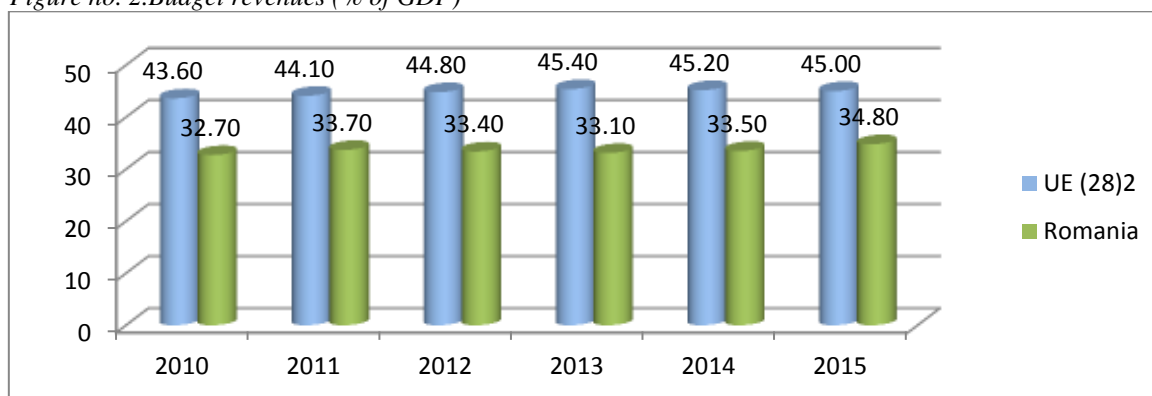
(% of GDP, ESA 2010)

No.	Year	European Union (28)		Romania	
		budget revenues	tax revenues	budget revenues	tax revenues
1.	2010	43,6	38,5	32,7	26,9
2.	2011	44,1	38,9	33,7	28,1
3.	2012	44,8	39,6	33,4	27,9
4.	2013	45,4	39,9	33,1	27,4
5.	2014	45,2	40,0	33,5	27,7
6.	2015	45,0	40,4	34,8	27,9

Source: EUROSTAT, 2015 (the contributions to social security are included in the tax revenues)

Analysing figure no. 2 and figure no.3, it can be easily observed a variable dynamic, with increases and reductions of budget revenues' level, but without significant changes. Since 2010, the EU recorded a revenues' increase in the general budget until 2013 and afterwards, these experienced a 0.04% decrease, until 2015.

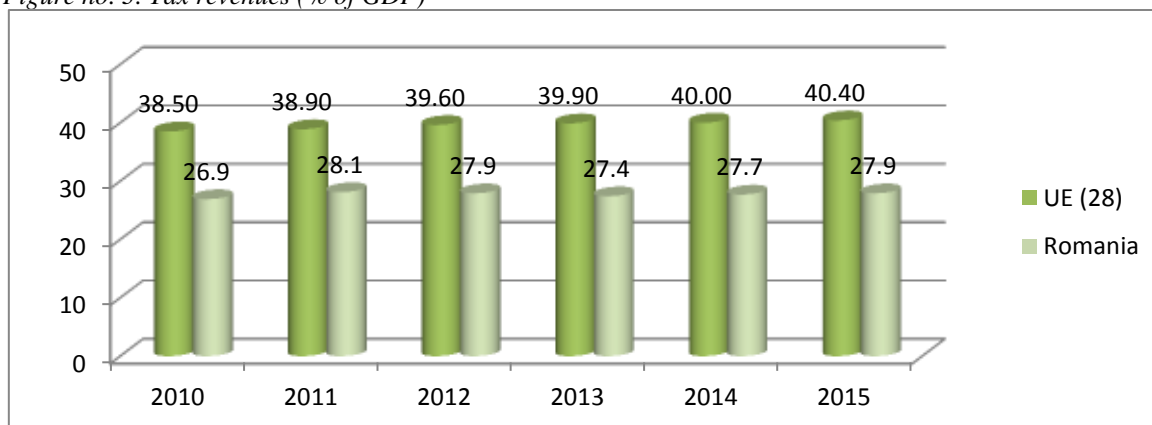
Figure no. 2. Budget revenues (% of GDP)



Source:(EUROSTAT, 2015)

It can also be observed a constant level of 45%. In opposition, tax revenues are growing continuously, but slowly, without significant changes, going from 38.5% in 2010 to 40.4% in 2015. Therefore, these recorded a 1.9% increase of the GDP value.

Figure no. 3. Tax revenues (% of GDP)

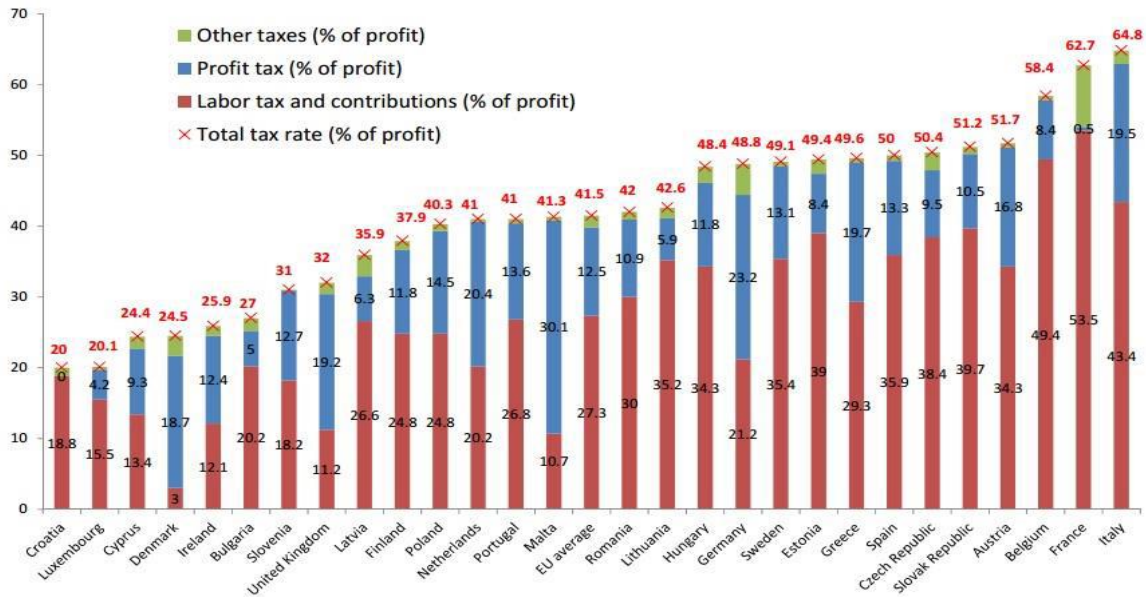


Source:(EUROSTAT, 2015)

As for Romania, it can be observed that budget revenues experience both a growth and a decrease in the analysed period. A significant increase of the level of these revenues in the GDP

can be noticed during 2014 - 2015, when the budget revenues were up 1.3%. However, the tax revenues experience a decrease of 0.7% from 2011 to 2013 and afterwards their levels start increasing.

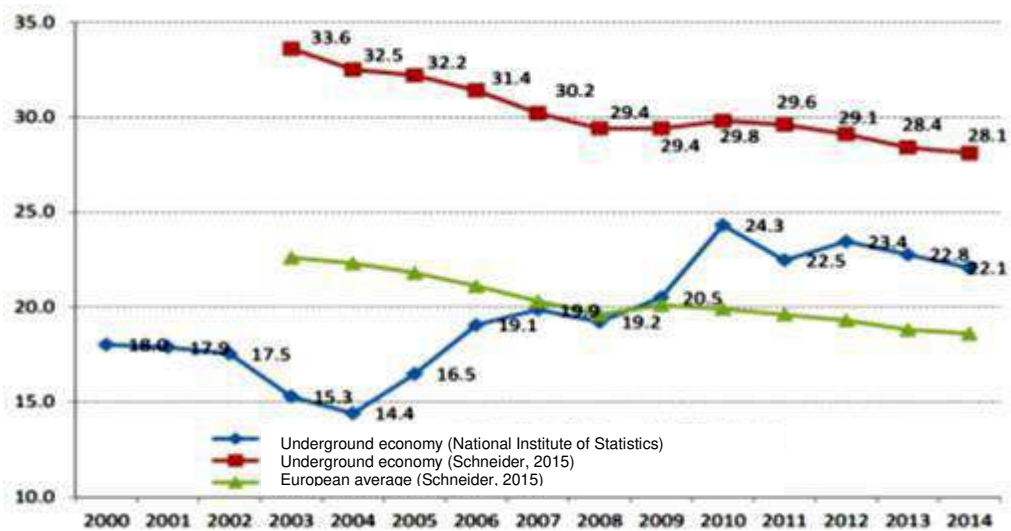
Figure no.4. The total tax contribution paid by companies to the state budget for 2014 – 2015



Source:(Fiscal Council, Annual Report,2015, 17)

It has been stated that if Romania had managed to collect taxes in a ratio of 100%, and if taxpayers didn't turn to various means to escape Tax Authorities, it would have a level of budgetary revenues in the GDP which would exceed the EU average because Romania is practicing a higher legal level of taxes than the EU average. A significant change in terms of managing taxes and duties in order to increase the efficiency of their collection, is compulsory. This change would also lead to a diminution of the tax burden on the dutiable subjects and thus for them tax evasion will not represent a path to follow anymore.

Figure no. 5. The share of underground economy in Romania and the EU (% of the GDP)



Source:(Fiscal Council, Annual Report, 2015, 35)

According to the Fiscal Council, the percentage of the underground economy in the GDP of Romania exceeds by far the EU average (Figure no. 4), this showing once again the inefficiency of

the legislative system but also the weakness of the tax collecting system. The average of the underground economy, namely the economy that operates legally but does not declare all revenues, reached, in 2014, 28.1% of the GDP, a 0.3% drop compared to 2013, this indicating a positive situation. Also, the average of EU 28 registered much lower values than the Romanian average, this being caused by the fact that the EU practices a lower level of taxes, but it also has effective laws and regulations that prevent taxpayers from seeking means of evasion.

Table no. 2. The underground economy of the European countries

Country	GDP (€ bn.)	Underground economy (€ bn.)	Share in GDP %
Bulgaria	41.2	12.8	31.2
<b>Romania</b>	<b>139.3</b>	<b>39.5</b>	<b>28.4</b>
Croatia	44.8	12.7	28.4
Lithuania	34.7	9.7	28
Estonia	18	4.9	27.6
Latvia	23.5	6	25.5
Cyprus	17.5	4.4	25.2
Malta	7	1.7	24.3
Poland	400.1	95.2	23.8
Greece	182.9	43.1	23.6
Slovenia	35.2	8.1	23.1
Hungary	102.7	22.7	22.1
Italy	1576	332.6	21.1
Spain	1051	195.6	18.6
Belgium	385.2	63.1	16.4
Czech Republic	154.3	23.9	15.5
Slovakia	73.9	11	15
Sweden	422.6	58.7	13.9
Norway	416.2	56.6	13.6
Denmark	249.7	32.4	13
Finland	198.7	25.8	13
Germany	2697	350	13
Ireland	167.4	20.4	12.2
France	2061	204	9.9
UK	1950	189.1	9.7
Netherlands	606.9	55.2	9.1
Luxembourg	45.6	3.6	8
Austria	319	23.9	7.5
Switzerland	507.4	36	7.1

Source: processing after A.T. Kearney, (A.T. Kearney's Global Business Policy Council (GBPC))

The willing acceptance to contribute of the taxable subject will increase only if this will be satisfied with the quality of the public services and will be treated fairly by the tax authorities.

The fight against tax evasion is getting more pronounced both nationally as well as globally. For this purpose, different specialized organizations have been designated to pursue this phenomenon and to operate in a manner as effective as possible, forces have been joined and financial and legislative decisions have been made in this regard. However, the legislation has shown to be in a very strict accordance with the dynamic evolution of the tax realities.

### 3. Conclusions

In the development of the proposed topic, it can be noticed that the tax evasion phenomenon is linked to numerous monetary factors such as rate, penalties and the probability of being subjected to controls by the authorities, and non-monetary factors, including the numerous social, ethical and moral norms.

Currently, by approaching the causes, it has been discovered that these influence in a significant manner the taxpayer's behaviour, and, implicitly, the evasion. By identifying the causes, we can

conclude that in order to deal with and combat the evasion problem it is necessary to act on it. It is essential to develop and implement contrasting actions that are thoughtful and decided at a group level. Some causes can and should be eliminated. These include: high tax rates, excessive regulations, and taxpayer's dissatisfaction concerning the offered public services, the knowledge that many subjects evade taxes and therefore evasion is widely seen as a common behaviour, therefore it can be considered normal. Thus, contrast actions are needed, these reducing the evasive behaviour. But, at the same time, it is essential to increase the taxpayers' possibility to spontaneously meet the social norm, and this can even be achieved by eliminating the causes listed above.

It is well known that the international monetary flows do not necessarily indicate the physical movement of the capital from one country to another, such mobility being achieved even through the accomplishment of financial transactions or direct investments of a multinational company. The capital movements are included, in this context, in the so-called tax haven, namely the states whose legal regime allows considerable limitations of taxes on the revenues generated by physical or juridical persons. These states, that have adopted a privileged tax system, have very simplified regulations concerning trading and banking entities. Under these circumstances, a decisive role rests on the offshore companies.

Throughout time, scandals such as the currently known #PanamaPaper existed previously worldwide, some very well-known examples being the disclosures made by Edward Snowden or the disclosures made by WikiLeaks on the Internet conversations or on the wiretaps of millions of Americans and not only.

The Panama Papers scandal of the year 2016 exceeds by far the scandal triggered by Snowden in 2013, especially in terms of the dimension of the data and information revealed to the public. If in 2013, Edward Snowden published about 1.7 million documents, in the #PanamaPapers" scandal we talk about a data and information leak of over 11.5 million records. That is, a 2.6GB archive, was e-mailed from an anonymous person to the newsroom of a German newspaper entitled *Süddeutsche Zeitung*. The amount of data published is huge when compared with the 1.7 GB of files made available to the WikiLeaks publication in 2010 by an American soldier.

Certainly, tax evasion represents a big problem for states all around the world and is now a complex economic and social phenomenon, that has been proven to be impossible to eradicate, with multiple effects on the macro or micro-economic level, starting from the diminution of the budgetary collection to the impairment of the income of each individual and even of the health of a company as a whole.

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