

# A Brief History of Tax Transparency

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## Abstract\*

This study describes progress on the international exchange of tax information from the end of the Second World War—a period marked by the complete absence of interinstitutional international collaboration—to more recent years, when there has been real awareness of taxation as an intrinsically global phenomenon. Thus the study analyzes the development of the new technical instruments and the institutional apparatus that have facilitated such progress, as well as matters that threaten their effectiveness and the critical factors in these processes.

**Keywords:** automatic exchange, global forum, information exchange, international tax transparency, standards, tax transparency

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## 1. The Beginnings: The Exchange of Tax Information up to 2009

The history of the international exchange of tax information is, until the onset of the twenty-first century, a history of opacity. There has been very little in the way of tangible results that show the contrary. We can record only a gradual—but always deficient—building of global awareness of the problem from 1989 onwards, when the European Community tried to “harmonize” taxation on savings as one of the challenges of its economic integration and, in general, of globalization. In any case, the historical-political context has not been conducive to progress.

The world emerged from the Second World War in a state of disintegration:<sup>1</sup> (i) there was little interdependence among national economies, high levels of mistrust among countries and/or blocs, and a relative dearth of multinational companies; (ii) there was no true world financial system as we know it today; (iii) the public mistrusted financial systems and banking; (iv) technology was ill-prepared for global interconnections in real time; (v) the focus was on reconstruction and economic recovery—which, in truth, was extensive and successful: “the thirty glorious years” period<sup>2</sup> that diminished concerns about tax fraud; (vi) in the tax field there was a complete absence of international, inter-institutional collaboration; and (vii) except perhaps in the advanced economies, the paradigm was one of banking secrecy.

In sum, there was no awareness that taxation was becoming an intrinsically global phenomenon and, even if there had been, there were no mechanisms to change the *status quo*. Tax havens began to develop in this period and the world-wide lack of tax solidarity became more marked. This caused a triple “misalignment”: country relative to country (or, if one prefers, opaque countries or jurisdictions relative to other countries); multinationals relative to local businesses; and large fortunes relative to the middle class and less advantaged citizens.

Albeit slowly, however, the seven phenomena mentioned above inexorably began to become blurred or disappear, and by the 1980s global circumstances had become very different. Growing awareness (academic, political, economic, financial) that the tax phenomenon is global, and that evasion is related to the financial system in at least two respects,<sup>3</sup> coincided with the end of the golden age of growth, economic crises (the oil crises of 1973 and 1981, and in Latin America the “lost decade” of the 1980s), the consequent increase in public deficits, and thus the urgent need for public resources.

At the end of the 1980s, therefore, the first political effort was made to associate the phenomenon of financial globalization with tax erosion: the failed European Directive on taxation of savings of 1989, the Scrivener Directive,<sup>4</sup> so named after the French minister who proposed

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<sup>1</sup> For example, the European Economic Community in its most elementary phase was a creature of 1957—that is, 12 years after the war. In Latin America, Mercosur originated in 1985 and the Andean Community only took steps towards economic integration in the 1990s.

<sup>2</sup> The term used to qualify the period 1945–1975, when there was very strong economic growth in the West (Piketty, 2014).

<sup>3</sup> One is the opacity of the financial system (it shelters evasion); the other is the unhindered movement of capital in the financial system (it fosters evasion, since it favors forms of planning that previously were unthinkable).

<sup>4</sup> This Directive was based on the understanding that the complete liberalization of capital movements that the then-European Economic Community (EEC, now EU) was moving towards, thanks to Directive 88/361/EEC, could distort tax systems: “the Commission shall submit to the Council ... proposals aimed at eliminating or reducing risks of

it. Germany's announcement that, on the basis of the Directive (which was not approved), it would withhold 15 percent on dividends and interests paid to other member states, caused capital flight amounting to US\$43 million between the end of 1988 and April 1989, when the measure had to be ruled out.<sup>5</sup>

The liberalization of capital movements has accelerated since the early 1990s, and there has been a worsening of the problem of tax resources lost to jurisdictions with low or no taxation for mobile sources of direct taxation. Hence the Organization for Economic Cooperation and Development (OECD) took steps on the matter from 1996 (transcending the European framework), and in 1998 managed to secure approval of a first study of harmful tax competition.<sup>6</sup> We should also mention the Inter-American Center of Tax Administrations' Model Agreement on the Exchange of Tax Information, which dates from 1990 and was revised in 1999.<sup>7</sup> Its merit lies mostly in its early identification of a conceptual problem and its provision of a solution whose practical application, as we know, was limited.

Viewed from a historical perspective, the OECD's studies between 1998 and 2008 were not effective in resolving the problem.<sup>8,9</sup> The European Union (EU) was somewhat more effective (though also with substantial limitations, as we shall see below):

- 1999–2000: Code of Conduct (also known as the Primarolo Report) to avoid harmful tax competition in the EU<sup>10</sup> (about 70 preferential tax regimes abolished in all member states, without exception). Nonetheless, see below for a critical review of the outcome of this exercise.
- 2003: approval of the EU Savings Directive, which entered into force in 2005 and was amended in 2014,<sup>11</sup> and which shares mass information on crossborder savings in the EU.
- 2006: the EU's Joint Transfer Pricing Forum. Apart from its concrete achievements,<sup>12</sup> its historical importance lies in the fact that for the first time, transfer pricing was put on the agenda of international and inter-institutional cooperation in the fight against tax evasion.<sup>13</sup> In other words, it identified a problem in how multinationals manage these operations.

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distortion, tax evasion and tax avoidance linked to the diversity of national systems for the taxation of savings and for controlling the application of these systems."

<sup>5</sup> Walter and Smith (2000).

<sup>6</sup> "Harmful Tax Competition: An Emerging Global Issue," OECD, 1998. [www.oecd.org/tax/transparency/44430243.pdf](http://www.oecd.org/tax/transparency/44430243.pdf)

<sup>7</sup> CIAT (1999).

<sup>8</sup> Nonetheless, some formal progress was made, such as the first OECD report on access to banking information (2000), the first lists of tax havens and preferential tax regimes, and the inclusive undertaking with the creation of the Global Forum, whose participants include non-members.

<sup>9</sup> The 1998 report on harmful tax competition was not approved by Switzerland or Luxembourg (the OECD operates by consensus). And the report on access to banking information, which these two countries did approve in 2000, does not contain timeframes for implementing the commitment. Additionally, at the start of 2001 the Bush administration took office and with that there was a radical change in the policy of the United States, which no longer wanted to move towards cooperation and caused the endeavor to founder (Maldonado, 2002).

<sup>10</sup> [http://ec.europa.eu/taxation\\_customs/resources/documents/primarolo\\_en.pdf](http://ec.europa.eu/taxation_customs/resources/documents/primarolo_en.pdf). For a history of this struggle and the "Code of Conduct," see [http://ec.europa.eu/taxation\\_customs/resources/documents/taxation/gen\\_info/economic\\_analysis/tax\\_papers/taxation\\_paper\\_10\\_history\\_en.pdf](http://ec.europa.eu/taxation_customs/resources/documents/taxation/gen_info/economic_analysis/tax_papers/taxation_paper_10_history_en.pdf).

<sup>11</sup> Directive 2003/48/EC, (<http://eur-lex.europa.eu/legal-content/ES/TXT/?uri=URISERV%3AI31050>).

<sup>12</sup> See [http://ec.europa.eu/taxation\\_customs/taxation/company\\_tax/transfer\\_pricing/forum/index\\_en.htm](http://ec.europa.eu/taxation_customs/taxation/company_tax/transfer_pricing/forum/index_en.htm).

<sup>13</sup> To that point, international cooperation had been confined (in the OECD) to highly technical discussions of the methodology used to set such prices.

Mention should also be made of other interesting regional exercises in this field, since there had been attempts (and some formal progress had even been made) at a Code of Conduct to avert the use of harmful tax practices among neighbors. For example, for Central America, Panama and the Dominican Republic—sponsored by the Council of Finance Ministers of Central America, Panama and the Dominican Republic and with the technical coordination of the International Monetary Fund and the Inter-American Development Bank—in 2008 a draft Code of Conduct was drawn up but it was never enacted because of a lack of political will. By contrast, the Caribbean Community did manage to approve a code in 1973.<sup>14</sup> Its practical results, however, are not clear.

It is also important to recognize the drive for transparency of the Financial Action Task Force on Money Laundering (FATF) process, which has sought to end banking secrecy and to promote the registration and control (beneficial owner) of ownership in businesses.

## **2. 2009, A Great Leap Forward: Exchange on Request (or the first standard)**

If something can be said of this panorama as a whole it is that it was disappointing: (i) the OECD exercises were ineffective; (ii) the EU's efforts, aside from the fact that they were not global in format or mission, suffered from significant technical limitations;<sup>15,16</sup>(iii) there was no other regional endeavor of any significance—especially none in Latin America, where in general the tax systems and administrations had only a modest degree of internationalization;<sup>17</sup> (iv) bilateral cooperation on information exchange, which existed on paper, was very rare in practice; and (v) perhaps the most fundamental factor, unlimited access to financial information on the part of tax administrations, which would require international consensus, was blocked by a minority of states or jurisdictions.<sup>18</sup> We can say that there was a “blocking minority.”

The situation changed, however, with the financial crisis of 2008. The drive emerged in the developed countries because of the fiscal requirements spurred by the crisis and the pressure of public opinion, which reacted to the bailouts of the financial sector and the revelations of aggressive planning on the part of big companies. In the large majority of developing countries it was the influence of the developed nations that impelled a move towards transparency, which

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<sup>14</sup> Agreement on the Harmonization of Fiscal Incentives to Industry ([http://www.caricom.org/jsp/secretariat/legal\\_instruments/agreement\\_fiscalincentives.jsp?menu=secretariat](http://www.caricom.org/jsp/secretariat/legal_instruments/agreement_fiscalincentives.jsp?menu=secretariat)). Also to be recalled, this time from outside the region, is the 2002 Memorandum of Understanding on Cooperation in Taxation Related Matters in the Southern African Development Community (SADC): [http://www.sadc.int/documents-publications/show/Memorandum\\_of\\_Understanding\\_in\\_Cooperation\\_in\\_Taxation\\_Related\\_Matters.pdf](http://www.sadc.int/documents-publications/show/Memorandum_of_Understanding_in_Cooperation_in_Taxation_Related_Matters.pdf).

<sup>15</sup> The three main failings of the Savings Directive—which were largely rectified with the amendment of 2014—were that it did not cover legal entities or “paying agents” located outside the EU; it did not cover all possible forms of (risk-free) saving, only interest and some investment funds; and the alternative system of withholding at source for Luxembourg, Belgium and Austria.

<sup>16</sup> The Code of Conduct (the Primarolo Report) did not define areas such as what constitutes passive income (for instance, it did not appraise international tax transparency regimes or CFC), and did not address the taxation of expatriates within the EU, thereby raising the possibility of migration for tax purposes, not only because of skilled and well paid work: HNWI regimes (tax regimes for high net worth individuals). Additionally, progress on transfer pricing in that period was timid and procedural.

<sup>17</sup> For a summary of the international tax situation in Latin America and the Caribbean, see Barreix et al., 2013.

<sup>18</sup> Switzerland, Luxembourg and, to a lesser extent, Singapore, Hong Kong and other financial centers.



still faces resistance from economic interests, including with appeals to sovereignty. First, the G20 made the earliest mention of tax issues in November 2008. The first G20 statement was followed by a much more detailed declaration in April 2009<sup>19</sup> and by the declaration of the G8 in L'Aquila in July 2009.<sup>20</sup> These statements immediately found expression in concrete events: (i) Switzerland, Luxembourg, Austria and Belgium withdrew their reservation to article 26 (exchange of information) in the OECD's Model Convention on Income and Capital; this implied the beginning of the end of banking secrecy world-wide, given that other jurisdictions, to avoid lifting their secrecy, had alleged that there was no level playing field if Switzerland and Luxembourg did not make the commitment; (ii) the commitment of other important financial centers, such as Singapore, Macao and Hong Kong, in favor of exchanging information on request; (iii) the publication of the list of the Global Forum on Transparency and Exchange of Information for Tax Purposes (GF), led by the OECD, of uncooperative jurisdictions in April 2009 (the Progress Report),<sup>21</sup> and the onset of efforts by many jurisdictions to be removed from the list. In Latin America and the Caribbean (LAC) this publication marked a turning point, because two Latin American countries (Costa Rica and Uruguay) appeared among the four listed in black, and 18 (especially in the Caribbean) were among the 39 listed in grey.<sup>22,23</sup> In other words, 46.5 percent of the jurisdictions listed throughout the world were in LAC. Today, only Guatemala and Trinidad and Tobago are unauthorized to advance to a Phase 2 review of effective information exchange,<sup>24</sup> and Anguilla, Antigua and Barbuda, Barbados, Costa Rica, Curaçao, St. Lucia and Sint Maarten appear as being only partially compliant with the standard.<sup>25</sup>

In any case, it is worth mentioning that other countries in the region have not joined the Global Forum, which now has 130 members. They are Bolivia, Cuba, Ecuador, Haiti, Honduras, Guyana, Nicaragua, Paraguay, Suriname and Venezuela. In the cases of Bolivia, Cuba, Ecuador, Nicaragua and Venezuela, this circumstance could be the result of a political decision (although not all of them could easily meet the standard), but in the cases of Haiti, Honduras and Paraguay there is a condition of historical, international financial and tax isolation (for example, this situation can be traced in the lists of the International Financial Action Task Force or FATF, where Honduras and Paraguay appeared until 2012).<sup>26</sup> Because of their tradition of scant transparency and institutional weakness, therefore, these countries will have to revise some aspects of their regulatory frameworks to enhance transparency and reach the international standard.

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<sup>19</sup> Of particular interest is the declaration of London on strengthening the financial system (April 2009): <http://www.oecd.org/g20/meetings/london/Annex-Declaration-Strengthening-Financial-System.pdf>.

<sup>20</sup> [http://www.g8italia2009.it/static/G8\\_Allegato/G8\\_Declaration\\_08\\_07\\_09\\_final%2c0.pdf](http://www.g8italia2009.it/static/G8_Allegato/G8_Declaration_08_07_09_final%2c0.pdf).

<sup>21</sup> <http://www.oecd.org/ctp/42497950.pdf>.

<sup>22</sup> Anguilla, Antigua and Barbuda, Aruba, Bahamas, Belize, British Virgin Islands, Cayman Islands, Dominica, Grenada, Montserrat, Panama, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines, Turks and Caicos Islands, and Netherlands Antilles, as well as Chile (the latter listed under "other financial centers").

<sup>23</sup> The jurisdictions on the grey list had committed to exchange of information but had not implemented the commitment effectively.

<sup>24</sup> Phase 1 reviews the country's legal framework.

<sup>25</sup> <http://www.oecd.org/tax/transparency/GFratings.pdf>.

<sup>26</sup> And certainly some others were or are, such as Nicaragua or Guyana, Ecuador or Panama.

Additionally, some that have decided to join the Global Forum could find themselves in difficulties because of their institutional framework as regards banking secrecy. Hence Peru faces a possible constitutional constraint (see below) and Panama faces difficulties in determining how to treat the financial statements of companies created in Panama that engage in no activity on Panamanian soil, as well as foundations and trusts.<sup>27</sup>

## **Two Speeds to Combat Fraud: EOIR and AEOI**

### 1. Exchange of information on request (EOIR):

Concept and use: this is the exchange of information on a concrete case, requested of one tax administration by another tax administration, when it is foreseeably relevant in applying the tax regulations of the requesting country. This information might be financial, accounting-related or concerning ownership (beneficial owners).

Once the relevance of the information has been justified to the requested administration, whether the requested country does or does not have a domestic interest in that request or its definition of tax fraud is irrelevant. It is also irrelevant whether the requested tax administration already has the information and, when it is in the possession of financial entities, in no circumstances can the request be denied on the grounds of banking secrecy. Full confidentiality in the handling of the information transmitted must also be guaranteed.

Legal basis: (i) article 26 (or equivalent) of the Bilateral Agreement on Double Taxation regarding the exchange of information; (ii) a tax information exchange agreement (TIEA); or (iii) article 5 of the OECD/Council of Europe Multilateral Convention on Mutual Administrative Assistance in Tax Matters (2011 amending protocol for its universal adoption and update).<sup>1</sup>

Statistics: see the mention of the Global Forum's 2015 Progress Report in this same document.

Final note: while the automatic exchange of information is gaining ground, technically EOIR remains the universal standard and is the option used by the Global Forum for its peer reviews of jurisdictions.<sup>2</sup>

### 2. Automatic exchange of information (AEOI)

Concept and use: this is the periodic and systematic transmission of non-preselected information from the State of the source to the State of residence, relative to a series of pre-established categories of income: dividends, interest, royalties, salaries, pensions and so on.

This information is gathered from paying persons or entities in the source, such as banks, employers and so forth, and is transmitted in line with standardized and secure protocols between tax administrations. Once the information has been filtered and processed, tax administrations can begin control actions towards their residents or request more information from the sending administration.

Legal basis: it can be: (i) article 26 (or equivalent) of the Bilateral Agreement on Double Taxation regarding the exchange of information, when thus provided for; (ii) a tax information exchange agreement (TIEA), when thus provided for; or (iii) article 6 of the OECD/Council of Europe Multilateral Convention on Mutual Administrative Assistance in Tax Matters (2011 amending protocol for its universal adoption and update).

Statistics: according to a survey carried out by the OECD (31 participating countries), the results are starting to be very significant: 17.8 million records exchanged. In some countries, such as Norway and Denmark, it was found that their residents were under-declaring or failing to declare about 40 percent of income abroad.

1. In the European Union there are specific additional instruments.

2. "Implementing the Tax Transparency Standards". OECD, 2010.

<sup>27</sup> See pages 28–29 of the report: [http://www.eoi-tax.org/peer\\_reviews/aa557ea9221d653369f4011848457bfc#default](http://www.eoi-tax.org/peer_reviews/aa557ea9221d653369f4011848457bfc#default).

### 3. 2014, The Missing Link: Automatic Exchange (or the second standard)

Very substantial progress has been made on exchange of information since 2009. Today there is a dense network of bilateral agreements<sup>28</sup> and a multilateral instrument has been ratified by almost 100 countries: the OECD/Council of Europe Multilateral Convention on Mutual Administrative Assistance in Tax Matters (2011 amending protocol for its universal adoption and update). Moreover, according to the Global Forum's 2015 progress report,<sup>29</sup> a survey of 32 jurisdictions revealed that taxes totaling US\$703 million had been recovered on average in the 2012–2014 tax periods, only as a result of the international exchange of information on request that these 32 countries have implemented.

There were also, however, voices that were critical of the achievements of the exchange of information on request. One of the most prominent was the Tax Justice Network, which called for the automatic exchange of information from a very early stage (2005) and repeated this call in 2012 when the Global Forum's success in information exchange on request had been achieved.<sup>30</sup> These criticisms were partly unfair because they ignored the huge progress entailed by the events of 2009 and the importance they could come to have in the medium term. Additionally, and this is particularly true in Latin America with its sorry history of banking secrecy, because of international pressure many countries lifted the domestic legal barriers to transparency. And in the end, the world divided into two groups: those that collaborate and those that do not. Today the former are a clear majority, though it is acknowledged that not all of those collaborating do so with the same eagerness.

To some extent, however, it should be said that the critical voices were right. Looking back, it is possible that the pressure of the activists, combined with the tax authorities' urgent need to find large-scale financial resources and the difficulty of implementing the exchange of information on request quickly and effectively,<sup>31</sup> triggered the most recent and most important change in the history of international tax transparency: the acceptance, which we can say is now widespread, of the new standard of automatic exchange. Together with the foregoing, moreover, the Foreign Account Tax Compliance Act (FATCA), which transformed the international landscape, must be accorded particular merit.

This law modifies Chapter 4 of the US Internal Revenue Code. It was enacted on March 18, 2010, although its full application has been delayed by the US government's practical difficulty in implementing a law with so many tax subjects that do not fall under US sovereignty. Under FATCA, foreign financial institutions (FFIs) must identify the accounts of US citizens or persons, and periodically or automatically they must report information on those accounts to the US

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<sup>28</sup> All the Tax Information Exchange Agreements (TIEAs) signed by the member countries of the global forum can be consulted interactively online at: <http://www.eoi-tax.org/#default>.

<sup>29</sup> <http://www.oecd.org/tax/transparency/global-forum-annual-report-2015.pdf>.

<sup>30</sup> The Tax Justice Network called for a move to the automatic exchange of information from a very early stage (2005): [http://www.taxjustice.net/cms/upload/pdf/TUIYC\\_2012\\_FINAL.pdf](http://www.taxjustice.net/cms/upload/pdf/TUIYC_2012_FINAL.pdf).

<sup>31</sup> For sophisticated tax administrations, with an appropriate system of risk control and audit selection, exchange on request was a very important step because the announcement effect was more powerful. For poorly organized tax administrations, however, the availability of this information was not real given that very few cases of fraud were uncovered in practice—simply because very few cases were investigated (in Latin America, no more than 2 percent of taxpayers are audited, on average!).

Internal Revenue Service (IRS). FFIs that do not report information face a 30 percent tax withholding on certain payments to them from US sources. Later, the Treasury decided to begin collaborating with various tax administrations throughout the world to ensure that FATCA was implemented better. To that end the United States offered some degree of information exchange—albeit not entirely reciprocal (see below)—or other advantages by signing Inter-Governmental Agreements (IGAs).

The act broadened and clarified the landscape of tax transparency only a few years after the progress made in 2009, since: (i) it showed that the automatic exchange of information was possible, both politically and technologically; (ii) it established very high standards of data transmission both in the objective sense (essentially, the bulk of the information held by banks, insurance companies and other financial institutions) and in the subjective sense (the concept of a “US person” is very broad, covering nationals, residents and a significant number of “interposed” or “shell” entities); (iii) it paved the way for certain countries, which did not comply with the transparency standards or did so with difficulty, to take advantage of FATCA to improve their legal frameworks and, in particular, their institutional arrangements for exchanging information. And this is very important for Latin America because several countries (Chile, Uruguay or Costa Rica), in order to meet the on-request standard and relieve themselves of internal political pressures against the lifting of bank secrecy, had used the Swiss system of a review judge or supervisory judge to oversee the exchange (as a guarantor of legal protection), and by definition this figure is incompatible with automatic exchange; and (iv) it creates a shared technological standard of data transmission among tax administrations, since the IRS took responsibility for standardizing the transmission technologies with the International Data Exchange Service.<sup>32</sup> In all, a revolution within the revolution that now operated with the information-on-request standard.<sup>33</sup>

Nonetheless, together with these clear advantages—which as we will see had an immediate and natural corollary in the Common Reporting Standard or CRS (see the box)—we must also record some weak points.

The first is the risk that this pace of change is too fast for some jurisdictions. By that we mean that forcing the financial centers, which have a more than extensive degree of legal, institutional and technological sophistication, to exchange information automatically and to start doing so in a short period is possible and salutary. But when certain States have sociopolitical and institutional constraints on moving quickly towards transparency (in Latin America there are clear examples), including doubts about the need for constitutional reform (as in Peru and Guatemala), the imposition of FATCA places the countries in the quandary of either being non-compliant or reforming at a dizzying speed, which is not always possible or desirable.

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<sup>32</sup> <https://www.irs.gov/Businesses/Corporations/International-Data-Exchange-Service>.

<sup>33</sup> In this sense the importance of the United States in the process is striking, first for being able to slow it down (see footnote 10) and later for acting as a catalyst. More significantly, this shows the importance of concerted action: if Switzerland and Luxembourg had not yielded it would not have been possible to get the other tax havens on board in this endeavor; without pressure from the OECD (with the United States in the lead), not as much progress would have been made.

The second question is the ambiguous position of the United States<sup>34</sup> in the global environment of automatic information exchange: on the one hand, it gets great credit for having helped surpass the on-request standard through FATCA, but on the other hand the country does not provide the same information as it requests. The main problem is that the United States requires foreign financial institutions (or countries, in the case of an intergovernmental agreement, IGA 1) to send information on balances, interest and dividends received and gross proceeds (amounts received for the sale of assets). On the other hand, in the United States and as regards payments to non-residents, the IRS has information on dividends (through withholding) and interest (since 2013, though interest remains exempt), but US banks still do not provide mass information to the IRS on the balances or gross proceeds<sup>35</sup> of non-residents.<sup>36</sup> Additionally, they do not demand transparency of offshore platforms.

This creates a competitive advantage for certain financial centers (several US states: see footnote 36) that fall under the sovereignty of the United States. International tax advisers are seeking to exploit that circumstance using new planning arrangements.<sup>37</sup>

Third, there are technical risks that automatic exchange will end up having little effect. It must be completely effective in three respects: (i) no jurisdiction can escape; (ii) it must cover all income streams, be they from business, capital or labor; and (iii) the stock variable must improve, making ownership transparent up to the ultimate beneficial owner of any entity. There are various means of meeting this basic objective. Our clear preference would be that the national registries should demand, on pain of severe penalties, to know each ownership chain up to the ultimate beneficial owners of all registered entities. This would allow each jurisdiction, consulting with a second jurisdiction (or more if desired), to verify the true sequence of ownership. This procedure was adopted by the Global Forum (Tax Transparency, 2015) in October 2015 and is similar to that recommended by the Financial Action Task Force to foster implementation and enhancement of policies to combat money laundering and the financing of terrorism. Complementarily, a global public registry could be created, building on the achievements of LEIROC ([www.leiroc.org](http://www.leiroc.org)), and its mandatory updating could be regarded as part of the standard of transparency. Access to this information must be justified. Furthermore, recently five EU

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<sup>34</sup> The United States, aside from its economic and political significance, has been a pioneer in international transparency and taxation, from its citizens' world income, set out in the Revenue Act of 1861 amid the Civil War, to the prosecution of criminals for tax offences in the 1930s, the professionalization of the IRS in the 1950s, and finally FATCA (automatic information exchange) more recently. Its leadership in international tax transparency is crucial—hence the need for it to secure legislative approval of the common standards and reports, and to eliminate opacity in its state regimes.

<sup>35</sup> The analytical outlooks for the US budget (the most recent in February 2015) always address this matter but Congress never agrees on anything:

*“The proposal would require certain financial institutions to report the account balance for US financial accounts held by foreign persons, expand the current reporting required with respect to US source income paid to accounts held by foreign persons to include similar non-US source payments, and provide the Secretary of the Treasury with authority to prescribe regulations that would require reporting of such other information that is necessary to enable the IRS to facilitate FATCA implementation by exchanging similar information with cooperative foreign governments in appropriate circumstances. The proposal would also require that this information, as well as information reported by foreign financial institutions to the IRS, be furnished to the account holders in order to encourage voluntary tax compliance. The proposal would be effective for returns required to be filed after December 31, 2016.”*

<sup>36</sup> There are also transparency problems with companies set up in some US states (Delaware, Nevada, South Dakota and Wyoming, especially in their “shell companies”), but that are in the process of adapting to the exchange standards of the Global Forum (Common Reporting Standard, CRS) and the OECD.

<sup>37</sup> [http://itep.org/itep\\_reports/2015/12/delaware-an-onshore-tax-haven.php#.VpK6TRXhC71](http://itep.org/itep_reports/2015/12/delaware-an-onshore-tax-haven.php#.VpK6TRXhC71).

member states demanded as a condition that the beneficial owner be made known: in April 2016, France, Germany, Italy, Spain and the United Kingdom announced a pilot initiative for the automatic exchange of information on beneficial owners (swiftly supported by another 35 jurisdictions), with a view to providing their tax and other relevant authorities with full knowledge of a wealth of information, and to fostering monitoring of the complex offshore routes used by criminals.<sup>38</sup>

All in all, this progress is phenomenal in historical terms, giving rise to the approval in 2014 of the OECD's CRS<sup>39</sup> and the later signing, by almost 100 jurisdictions, of the Multilateral Competent Authority Agreement that links the CRS to the Multilateral Convention on Mutual Economic Assistance in Tax Matters. The world is moving more decidedly towards the adoption in 2017 or 2018 of the automatic exchange of financial information as the new standard of universal tax transparency.<sup>40</sup> And although the undertaking is essentially designed for the control of the direct and asset taxes of multinationals and large fortunes, there is a spillover effect on the tax system as a whole—especially in developing countries where personal income tax is not so significant—because it also strengthens VAT and other taxes.

#### **4. ... And the Icing on the Cake in 2015: BEPS and its Importance in Transparency Endeavors**

The problem of harmful tax competition in its various forms and degrees is not solely a problem of those US states that comprise financial centers. What is worse, often the problems of low revenue do not stem from the non-disclosure of information. In reality, large corporations have used the differences of legal treatment between jurisdictions to optimize their tax bill without scruple. These are aggressive tax planning formulas that skillfully skirt the line separating fraud (avoidance) from licit practices (tax mitigation). In fact, there have been cases of aggressive planning in some countries of the EU, such as favorable treatment in Ireland (Apple, Fiat, Chrysler, and so forth); the Netherlands (Starbucks); Luxembourg, in a case known in the media as “LuxLeaks” (Pepsi, Ikea, AIG, Deutsche Bank, and so on); and more recently Belgium.<sup>41</sup> But according to Jean-Claude Juncker,<sup>42</sup> these and similar practices are present in as many as 22

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<sup>38</sup> On April 15, 2016, after a meeting of the G20 Finance Ministers and Central Bank governors, a statement was issued requiring that by July 2016 the OECD should publish objective criteria to identify jurisdictions regarded as uncooperative in matters of tax transparency. See also: <https://www.gov.uk/government/publications/beneficial-ownership-countries-that-have-pledged-to-exchange-information/countries-committed-to-sharing-beneficial-ownership-information>.

<sup>39</sup> See box.

<sup>40</sup> In Latin America, the following countries have made a commitment to adopt the new standard in 2017: Argentina, Brazil, Chile, Colombia, Costa Rica, Mexico, Uruguay and Panama (within certain limits). A total of 13 Latin American and Caribbean countries will have adopted the standard by 2018.

<sup>41</sup> For more information and as examples of the statement above, see the following files on state aid available on the European Commission website: Apple case: state aid SA.38373 (2014/C); or the Starbucks case: state aid SA.38374 (2014/C). Those interested can also visit the following site to analyze the “LuxLeaks” affair in greater depth: [http://www.icij.org/project/luxembourg-leaks?utm\\_campaign=lux\\_release&utm\\_source=email&utm\\_medium=button\\_middle&mc\\_cid=28019c7941&mc\\_eid=80ffe22bbd](http://www.icij.org/project/luxembourg-leaks?utm_campaign=lux_release&utm_source=email&utm_medium=button_middle&mc_cid=28019c7941&mc_eid=80ffe22bbd). Finally, the news on the Belgian case is more recent: <https://es.noticias.yahoo.com/la-ue-estima-ilegal-el-r%C3%A9gimen-exoneraci%C3%B3n-fiscal-111512708.html>.

<sup>42</sup> “LuxLeaks”: Juncker contre-attaque. *Le Figaro*, November 12, 2014: <http://www.lefigaro.fr/conjoncture/2014/11/12/20002-20141112ARTFIG00258-luxleaks-je-suis-politiquement-responsable-admet-jean-claude-juncker.php>.

EU member states and there is every indication that, if the cases in the EU have been brought to light, it is because there is a strong institution such as the European Commission that prosecutes such practices. In any case, a brief additional parenthesis on these matters seems opportune.

- 1) Multinational companies' web of international tax evasion involves sophisticated technical expertise (it does not consist, to be clear, of carrying the cash to a bank account in a briefcase and hiding it in the dark). The documents reveal various structures of fiscal engineering whose complexity is growing, such as the use of hybrid instruments—that is, those that receive a different tax treatment in two countries, which allows an income to avoid taxes; or the use of clauses that offset revenues and expenses by means of an accounting device that makes it possible to control the final benefit freely—that is, when there are revenues, a fictitious book expense is generated as an offsetting factor to leave the profit at zero; and when there are losses the reverse mechanism is set into motion by means of the “clawback provision”.
- 2) There is a necessary cooperation from tax advisory businesses, among them the biggest multinational companies engaged in accounting-legal-tax consultancy, and also various international law firms.
- 3) Much worse, there was (and there is?) an active complicity between various countries to foster such practices. Hence it is no longer simply a matter of there being a norm (banking secrecy, or a legal exemption) to shelter income: a country's authorities have to know the operation to perfection, and thus be aware of how another country's tax base is being eroded. This is explicitly or implicitly revealed in every consultation or ruling of “LuxLeaks,” but there are various means of achieving it and the EU is not the only transgressor.
- 4) What was said in the preceding point is even more serious if we keep in mind that, as we have seen, the fight against opaque tax practices in general has been continuing since at least 1997. In the European context (not hard to extrapolate, we fear), the initial success of the Code of Conduct has come to almost naught. It could even be said that the European Code was counter-productive because it left a sense of control and monitoring of harmful regimes on the part of the European Commission, and thus perhaps led to some loss of vigilance.

In this context, the works of the OECD and the G20 emerged in July 2013 to eliminate the base erosion and profit shifting (BEPS) carried out by multinationals. The BEPS project is a notable effort to deal with the maximum possible number of factors identified as potentially determinant of or contributory to international tax avoidance. It consists of a total of 15 actions that can be divided very schematically into four blocks:

1. Combating aggressive tax planning in general (actions 2 to 5, and 12).
2. Combating the abuse of double taxation agreements and improving their implementation (actions 6, 7 and 14).

3. Strengthening the regulation of transfer pricing (actions 8, 9, 10 and 13).<sup>43</sup>
4. Implementing the political agreements of the 14 preceding actions through a multilateral treaty (action 15).<sup>44</sup>

From the viewpoint of transparency, the BEPS project offers substantial progress on:

1. The obligation to measure and monitor the concrete results attained by countries after they have adopted some or all of the proposed measures.
2. The obligation of companies (and tax advisers) to reveal aggressive planning arrangements to the tax administrations before putting them into practice, or otherwise face a penalty.
3. The standardization, improvement and country-by-country reporting of tax information on multinationals' transfer pricing.
4. The establishment of flexible mechanisms to settle disputes related to double taxation between countries, including tax arbitration in the last instance.

The future success of BEPS will depend on:

1. The speed with which it is transposed into the corresponding legislation (political obstacle).
2. The coherence or symmetry of its regulation in all countries (technical-tax obstacle).<sup>45</sup>
3. Its enforcement (administrative obstacle).

Because of the institutional weaknesses of emerging countries (and several in LAC) in each of these levels, and because of the scant direct commitment to the process showed by some jurisdictions; this is a particularly daunting challenge for them. Moreover, skeptical opinions are being voiced about the usefulness of the exercise for emerging countries in general. Nonetheless, we believe that international cooperation between countries and multilaterals is very important in ensuring the global success of this initiative, given its crucial contribution and its complementarity with the tax transparency efforts fostered by the Global Forum on Transparency and Exchange of Information for Tax Purposes (banking secrecy, determination of ownership to the final beneficiary, and information exchange). Furthermore, the BEPS proposal has spurred discussions because of the new tax policy alternatives that are consequent on its future implementation.<sup>46</sup>

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<sup>43</sup> We should also mention other progress in the field of information technology such as electronic invoicing, which has now been implemented in seven Latin American countries; and electronic receipt of wages, which is underway in three jurisdictions. These are fundamental steps forward in tax control of domestic economic activity. It will also be very useful when there is international electronic billing, a control instrument with several applications such as the review of transfer pricing and combating "missing trader" fraud in the VAT on exports between EU countries.

<sup>44</sup> Action 1 on the digital economy is crosscutting in nature and makes quite general recommendations without concrete outcomes. All the material on BEPS can be consulted at <http://www.oecd.org/tax/beps.htm>.

<sup>45</sup> Thompson (2016) states that BEPS seeks to prioritize the elimination of international double non-taxation, even at the cost of causing international double taxation, which becomes tolerable collateral damage for the post-BEPS regime.

<sup>46</sup> As an example, we can cite the important discussion that has been prompted by the impact of the future implementation of BEPS—which will make it possible for the authorities to be informed about a taxpayer's global income, and better approximate the income that corresponds to each jurisdiction—on the application of allocation



The main criticisms of BEPS from emerging countries are as follows:

- BEPS is not a global process: the G8, G20 and OECD have not included all emerging countries and there have never been negotiations with this bloc as such. BEPS is a unilateral and hugely complicated package of recommendations on how international tax regulations should change.
- BEPS will not put an end to tax evasion. In several cases the proposals are tweaks to the prevailing tax system; it will be difficult for poor countries to put them into effect and curb tax evasion, which is organized today as an “industry” or structured system.
- BEPS does not really address the allocation of the fiscal sovereignty of the taxes among countries, but rather discusses the matter in a way that is either marginal (for example, broadening the definition of permanent establishment) or that speaks to the future (for example: Action 1 on the digital economy does attribute a tax to a source but the final policy decision is deferred because there is no “consensus”).
- BEPS does not end the race to the bottom, since the countries continue to engage in some form of tax competition. This means that corporate income tax, with its multiple exceptions and benefits, will continue to be eroded and to undermine tax revenues at the global level.<sup>47</sup>

Last but not least, corporate income tax has not undergone any great structural changes (income less costs) since it was conceived in the late nineteenth century, and BEPS might be its greatest historical transformation.<sup>48</sup> Barreix et al. (2016) proposes an adaptation of the income tax system to the changes of the twenty-first century, in which the drive for tax transparency is a crucial force. In other words, changes in tax administration and greater world-wide transparency will make possible new designs for tax policy in the area of direct taxation.

## 5. Conclusions

The forward march of transparency is a phenomenon with profound ramifications in many spheres: legal, political, ethical and so forth, with powerful global actors, and where not every formal legal or political agreement will have immediate effect. But it will have broad impacts on economic and social policies world-wide if it comes to prevail. Indeed, the big change is that tax transparency levels the playing field by offsetting the informational asymmetry between taxpayers and their advisers (operating at a global level) and national administrations for tax

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formulas to divide the income among the countries in which a multinational company operates. The discussion about the use of formulary apportionment for the unitary taxation of the multinational, as against the arm’s length principle, is involving academics (Picciotto, 2012), professionals (Spencer, 2014) multilaterals (IMF, 2014) and social organizations (Tax Justice Network, 2013), among other authors. The authors of this study, moreover, propose a new design for income tax (Barreix et al., 2016) based on this new international situation in which there is real knowledge of capital income flows and their ownership.

<sup>47</sup> In sum, according to the more prominent activists in the international tax field: “the measures [BEPS] recently announced by the OECD leave the fundamentals of a broken tax system intact and do not stop the race to the bottom in corporate taxation. G20 governments must do more and should strongly support further reforms” (joint agency briefing note from Oxfam, the Tax Justice Network, the Global Alliance for Tax Justice and PSI: <https://www.oxfam.de/system/files/still-broken.pdf>).

<sup>48</sup> While there have been occasional changes such as thin capitalization rules, transfer pricing or adjustments for inflation, in practice there have been no substantial structural changes. The proposals of Hall and Rabushka (1995), precursors of the “flat tax”, which proposed moving to a cash-flow type tax and disregarding interest in determining income (that is, ignoring the company’s financial structure), were not implemented.

and asset control. In short, capital (including information on its ownership and yield) remains mobile but now it cannot be hidden or distorted—it can run but it can't hide.

If progress on the international coordination of fiscal and financial transparency proves successful, it is very likely that it will spur changes in tax policy, especially as regards tax on income and capital. It will also pose new technical and ethical challenges to the management of the transparency process for taxpayers, tax advisors and tax administrators. The management of information will offer new opportunities in the areas of services (for companies) and controls (for tax administrations). Moreover, use of the data will impose new obligations on advisors and other public services (not only the tax administrations), and thus it will be necessary to draw up regulations governing the management and control of their activities.

Finally, a cultural perception is emerging that the informational asymmetry stemming from international tax opacity leads to inequality of treatment among citizens.<sup>49</sup> Lower-income taxpayers—who largely bear the austerity policies that followed the 2008 financial crisis in the advanced economies, and in the developing countries are suffering the demand adjustments attendant on the recent fall in commodities prices—are being affected by personal income tax, social security contributions, and all indirect levies, etc. While the wealthiest, with professional advisers and access to opaque jurisdictions, can reduce or hide their assets and income, to which is added the perception that they were not always acquired licitly. Lack of tax transparency, therefore, calls into question the market economy as a fair system, and even democracy itself as a competent regime.

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<sup>49</sup> The influence of capital mobility is evident in political economy models. A pertinent example is the additional condition to the Median Voter Theorem (which suggests that a majority-rule voting system will choose the outcome preferred by the median voter). This condition postulates that the richest sectors of a society avoid taxes and confiscation by means of capital flight, and thus the democratic process avoids opposition from a powerful pressure group and at the same time achieves the coexistence of formal democracy with tax regressiveness (Mahon, 2016). Additionally, the literature on the reactions of welfare states to globalization points out that governments respond with significant tax incentives to attract and retain multinational or multiregional companies, which are crucial economic agents in the mobility of corporate capital (Tanzi, 2000).

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