BUSINESSEUROPE

SPEAKING NOTES

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MADARIAGA – COLLEGE OF EUROPE FOUNDATION AND EUROPEAN ECONOMIC AND SOCIAL COMMITTEE
"HOW TO COPE WITH TAX HAVENS?"
24 JUNE

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Ladies and Gentlemen,

INTRODUCTION ON TAX HAVENS

- In an ideal world, tax havens would not exist. We would have one common global tax system. This would allow us to avoid all loopholes and prevent tax fraud.
- Yet, in reality countries use their tax system as a source of competitive strength. It allows them to attract capital and economic activity. This is legitimate and has been a source of growth for small and peripheral countries in Europe.
- But it should be very clear that this must not contribute to fraud, money or tax laundering or any other criminal activity. Such activity inflicts severe damage to our society.
- Tax havens are defined by four key factors according to the OECD:
  (1) No or nominal tax on the relevant income;
  (2) Lack of effective exchange of information;
  (3) Lack of transparency;
  (4) No substantial activity.
- The first criteria (no or nominal tax) is not sufficient to classify a country as tax haven.
- Jurisdictions need to make commitments on implementing principles of transparency and the exchange of information for tax purposes.
- Otherwise, they risk being listed as uncooperative jurisdictions by the OECD. This might entail sanctions.
- Over 40 jurisdictions were identified as meeting the tax haven criteria in 2000. Today all have committed to implementing transparency and effective exchange of information. There remains no single uncooperative jurisdiction on the OECD list.
- Now, countries need to implement these standards. It is crystal clear that a jurisdiction must control flows of money that enters and leaves its borders.

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CRISIS NOT BEHIND US

- We continue to face the consequences of a major financial and economic crisis. A lot still needs to be done to contain the credit crisis and its effect on the wider economy.
- Companies have a key interest in financial stability. Financing difficulties are taking critical proportions:
  - The real cost of financing for European companies has further increased since September 2008. It is too high to stimulate an economic recovery.
  - Access to finance has virtually dried up for the more indebted companies and those considered at higher risk.
  - International trade and supply chains have been considerably disrupted by the reduced coverage and increasing price of trade credit insurance.
- We have called upon EU institutions, national governments, financial regulators and Central Banks to take determined actions that relaunch growth and limit job losses.
- Their intervention consisted in the
  - recapitalization of banks;
  - guarantees on new debt emissions for the financial sector;
  - reduction of key interest rates;
  - fiscal stimulus plans in the order of 1.5% of GDP.
- This has been decisive in keeping the financial system alive and reducing systemic risks.
- However, we are not off the hook: rising corporate defaults and growing losses in the financial sector might lead to a further deterioration.

TAX HAVENS - ONE ELEMENT OF THE CRISIS RESPONSE

- The new approach to tax havens is one of the elements of the international policy reaction to the crisis.
- Stronger cooperation in this field can enhance the sustainability of the global financial system. It would reduce opacity and enhance traceability of funds.
- Last April, the **G20** agreed to take actions against non-cooperative jurisdictions. Tax havens are included. Countries might face sanctions if they do not adhere to international standards for exchange of tax information.
- The **ECOFIN Council** of 9 June announced its readiness to further discuss and promote the principles of good governance in the tax area internationally.
- Through the setting of internationally agreed standards for good governance, the **OECD** is very actively contributing to this agenda.
- The **European Commission** is supporting the process through setting up information sharing agreements within the EU and with third countries.

Let me elaborate on two points that we believe are key to address the issue of tax havens. They are also at the heart of the competitiveness of European companies. They aim at restoring the **functioning of financial markets** and **reforming tax systems.**

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TRANSPARENCY KEY TO RESTORE FINANCIAL MARKETS

- Enhanced transparency is needed to restore the functioning of global financial markets.
- This also requires cooperation from tax havens.
- The current political momentum now should to be used to enhance the transparency of international financial flows.
- This is important to reduce the scope for regulatory arbitrage that will arise upon strengthening the international financial supervision and regulation framework.
- At the same time, good governance in tax and regulatory matters must be promoted within the EU.
- It is important to distinguish issues of tax transparency and evasion from issues related to tax competition (in particular, low tax rates).
- Furthermore, tax policies and demand for exchange for information must not be used for protectionist purposes, hampering cross-border trade and investment.
- The **G8 business summit of December** last year made proposals:
  - for a “reasonable and appropriate” form of transparency of funds;
  - for appropriate levels of supervision and monitoring by financial regulators;
  - and warned that regulation should not stifle innovation in the market place.
- In a recent **BUSINESSEUROPE report on access to finance**, we call on the EU to take the lead by way of example in the G20 process.
- We should bring our international partners to advance balanced market reforms based on principles of:
  - transparency;
  - better risk management;
  - enhanced cross-border oversight;
  - and internationally comparable accounting and capital requirement rules.

BROADEN TAX BASE THROUGH TAX REFORMS

- Further to financial stability concerns, the erosion of tax bases is another reason for the renewed interest in tax havens. This will become an even greater concern in times of over-stretched public finances.
- Globalization has increased the possibility of cross-countries’ investments promoted by different tax treatment. It has also increased the impact of taxes on the international allocation of capital.
- At the same time, tax policy has affected the way companies finance their investment.
- Most tax systems favour debt over equity finance – interest is deductible against corporate tax but dividends are not.
- In practice, this has contributed to excessive leveraging according to a recent IMF study.
- This has also been accompanied by the development of complex financial instruments and structures. This in turn made it easier to channel funds through low or no-tax jurisdictions.
- Governments have reacted to this development by introducing complicated anti-abuse measures. Tax complexity has become a major problem in many European

countries and is a real threat to the Internal Market. This hits not only the fraudsters but all companies. Even those without any international operations.

- In a recent speech, Vito Tanzi – former director of the IMF 's Fiscal department – emphasized that economic growth may be affected as much by complexity as by higher rates of taxation.
- Currently, EU governments face huge pressure on public finances with a revenue shortfall of €600 billion in 2009 compared to 2008, according to the Commission's Spring forecast.
- It is now of outmost importance that the search for short-term revenue does not lead to aggressive protectionism that could hamper long-term economic growth.
- Instead, governments must set the right incentives for savings and investments to stay in Europe.
- It will be good to have the discussion on tax havens behind us to be ready to start working on more efficient and growth-oriented tax systems in Europe.
- We need to remove double taxation and double non-taxation – profit should be taxed once not twice.
- Furthermore, we must cut the compliance burden associated with tax payments for individuals and companies and prevent abuse in a well targeted manner, not influencing sound business practices.
- Ultimately, the best way to remove double taxation and reduce complexity remains a common consolidated corporate tax base (CCCTB) – and we continue to work on this project with the European Commission.

CONCLUSION

- Tackling tax havens will not get us out of the crisis.
- However, it should contribute to less opaque financial flows and facilitate detection of systemic risks in the future.
- We currently see an abrupt retrenchment of trade, investment and business activity in Europe and around the world.
- This is a direct consequence of a severely deteriorated environment for corporate finance and a heightened degree of risk aversions in financial markets.
- KPMG has recently undertaken a global survey of over 850 companies.
  - According to this survey, companies think the best way to help them through this recession is reducing costs.
  - Interestingly this is directly followed by better control of financial systems and better regulation in the finance sector.
- This illustrates that we must tackle the issue on a broader front.
- In our view, more efficient tax systems and strengthened financial transparency are key to tackle tax havens in a sustainable manner.
- These are also pre-conditions to restore growth and prosperity in Europe.
