TAX JUSTICE FOCUS

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TAX JUSTICE AND HUMAN RIGHTS: THE BEGINNING OF A BEAUTIFUL FRIENDSHIP?

Adrienne Margolis

Tax policy has wide-ranging implications for human rights throughout the world, not least because financial secrecy is indispensable to modern tyranny. Now law, accountancy and economics stand to be transformed as the public trace the connections.

Many anti poverty campaigners have already made the connection between tax justice and human rights, but the business community and the general public are only now starting to catch up. Governments all over the world are finding their coffers depleted as transnational corporations dodge taxes in the countries in which they operate, and wealthy individuals also move their money offshore. This makes government commitments to alleviating poverty increasingly difficult to achieve. In such circumstances it is becoming increasingly clear that wealthy countries can only make good on their stated commitment to universal human rights if they renounce the temptation to profit from illicit capital flows. Responsible democracies cannot moonlight as tax havens.

This edition of *Tax Justice Focus* brings together some of the strands of an emerging consensus in law and international affairs.

Magdalena Sepúlveda has been investigating the obstacles that governments face in alleviating poverty in her capacity as the United Nations special rapporteur on extreme poverty and human rights. Her report on the human rights impact of fiscal and tax policy has been submitted to the UN Human Rights Council for consideration in June. In her article for TJF, Sepúlveda spells out the connection between fiscal and tax policies and governments' human rights obligations,

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Eleanor Roosevelt, one of the architects of the Universal Declaration of Human Rights, photographed at the United Nations in 1947.

stressing that without the necessary funds to alleviate poverty, "realising human rights is rendered meaningless." Whether revenue is lost through illicit financial flows or austerity measures, she argues that states that do not take steps to collect all taxes owed are not meeting their obligations to realise economic, social and cultural rights.

The need is urgent. Yale philosophy and international affairs professor Thomas Pogge points out that about half of the world's population do not have adequate food, clothing, housing, medical care or access to social services that could protect them. Governments in the countries where many of the poorest people live have huge difficulty raising revenue through taxation, largely because corporations can easily shift profits to tax havens. Pogge notes that the funds lost through such tax abuse could go a long way to alleviating poverty and helping governments to meet human rights obligations. The key to solving the problem is global financial transparency.

Pogge recently chaired a task force set up by the International Bar Association's Human Rights Institute to investigate the links between illicit financial flows, tax and poverty. The task force published its report Tax Abuses, Poverty and Human Rights, in October last year. International human rights lawyer Lloyd Lipsett was the task force's rapporteur. He notes that a key finding in the report was that government action that facilitates tax abuse could violate state's international human rights obligations. The task force concluded that states have obligations to counter tax abuses and businesses have a responsibility to avoid tax planning that harms human rights. Lawyers have an important role to play - they must balance their obligation to their clients with an understanding of the impact of tax abuse on society.

Some commentators have seen the IBAHRI report as a starting point for further research into the impact of tax abuse on human rights.

"States have obligations to counter tax abuses and businesses have a responsibility to avoid tax planning that harms human rights."

More case studies are needed. A powerful example has been provided by Bill Black, campaigner and former banking regulator, whose actions helped uncover the US Savings and Loans scandal. He describes the experience of Ireland, where human rights have been harmed by severe austerity measures, as a result of economic policies encouraged by the country's tax haven status. Black warns that Irish tax policies have "spread the rot to other nations by inducing a race to the bottom."

It is time for the race to be halted.

Adrienne Margolis is founder and editor of Lawyers for Better Business (www.L4BB.org) a website and global network to keep lawyers one step ahead of developments in business and human rights. She is a director of Tax Justice Research.

"Responsible democracies cannot moonlight as tax havens."

TAXATION FOR HUMAN RIGHTS

feature

States have a self-imposed duty to deploy "the maximum available resources" to secure the human rights of their population. Fiscal policies mean that many of them are currently failing in that duty.

Magdalena Sepúlveda

What does tax have to do with human rights? Why is tackling tax evasion an ethical and legal obligation as well as a necessity for good governance? What do human rights obligations tell us about how States should design tax systems? How can good tax policies help us eradicate poverty and improve the enjoyment of human rights? These are all issues I hope to illuminate in my next report to the Human Rights Council.

Historically, human rights professionals and monitoring bodies have shown hesitation in addressing fiscal policies and their impact, but thankfully this is now beginning to change. During my country missions – for example to Paraguay and Ireland - I have seen firsthand the extremely unjust effects of taxation and spending policies that do not take human rights into account. It has become evident from the work of academics, practitioners, economists, NGOs and the UN, that examining fiscal and tax policies is a crucial component of assessing States' compliance with human rights obligations. In particular, recent work has illuminated the relevance of these policies with regard to tackling inequality and in providing for the realisation of human rights. Governments' rhetoric about eliminating poverty and realizing human rights is rendered meaningless without an effort to collect the funds necessary to pay for hospitals, piped water, schools, social security or legal aid. Without adequate tax revenue, the availability and quality of public services suffer, with a direct negative impact on the enjoyment of rights such as education and health of the poorest people in society. This in turn perpetuates inter-generational poverty.

A rights-based approach provides guidance on how, and from whom, States should collect taxes. Often, due to their limited political voice, people living in poverty are required to pay more than their fair share in taxes, while their needs are overlooked when resources are allocated. For example, on my mission to Paraguay, I found that there was no income tax and the government largely relied on sales tax for revenue. This had profoundly discriminatory effects: the poorest 10 per cent of the population was paying 18 per cent of their income in VAT while for the richest 10 per cent of the population, VAT represented only 4.6 per cent of their income.[1] As well as running afoul of the right to non-discrimination, by disproportionately cutting into their already small income, this also denied the poorest their rights to food, health and an adequate standard of living, among others.

The International Covenant on Economic, Social and Cultural Rights obliges its 161 signatory states to use the "maximum available resources" to secure the economic, social and cultural rights of its population. These maximum available resources include those that could *potentially be collected* through taxation. Therefore, if a State has a small tax base or overlooks widespread tax evasion while its people go hungry or homeless, it may in fact be in violation of this obligation.

Tax evasion, which is a particularly high-profile issue at the moment, has been estimated to result in annual revenue losses of USD $285 billion to developing countries,[2] and Africa loses twice as much in illicit financial outflows (including tax evasion) as it receives in aid. The problem is not just limited to the developing world; tax evasion in Spain is estimated to have resulted in a loss equivalent to EUR 88 billion in 2010. This greatly exceeds the total budget cuts made in 2012 as part of devastating austerity measures, which severely impacted human rights enjoyment in the country.[3] A state that does not take strong measures to collect all taxes owed cannot be said to be devoting the maximum available resources to the realisation of economic, social and cultural rights.

It is important, now more than ever, for human rights advocates to get ahead of the cost argument rather than avoiding it. The devastating spread of austerity measures - including taxation and fiscal policy reforms – is hitting the poorest people hardest and in many cases threatens their health, livelihood and very survival. Time and again, the poorest and most disadvantaged people (such as women, single parents or persons with disabilities) are being asked to pay more proportionally, while wealthy persons and corporations are escaping without paying their fair share. All too often, when governments face human rights bodies they use the defense of resource constraints; for instance claiming that the financial crisis leaves them no choice but to cut welfare benefits and services that those living in

" Human rights and tax justice advocates are strategic allies. "

"In nearly every country of the world it is not a question of lack of resources, but rather of a lack of political will to collect and marshal these resources in a manner that is compliant with human rights"

poverty rely on. Politicians, diplomats and policy-makers wheel out these excuses repeatedly, in media interviews and in reaction to the criticism of human rights bodies. In fact, in nearly every country of the world it is not a question of lack of resources, but rather of a lack of political will to collect and marshal these resources in a manner that is compliant with human rights - even though these states have voluntarily committed themselves, through international treaties, to precisely this responsibility.

Thankfully, more and more people are looking at tax through the lens of human rights. I warmly welcome this timely edition of *Tax Justice Focus* for bringing the human rights imperative to the fore, because there has never been a greater need to work together to demystify the idea that fiscal and macroeconomic policies are outside the reach of international human rights law. In the vital work of clarifying and communicating the social, economic and ethical imperative for a new global paradigm around tax, human rights and tax justice advocates are strategic allies.

Magdalena Sepúlveda served as the United Nations Special Rapporteur on extreme poverty and human rights between 2008 and 2014. She now reports to the General Assembly and the Human Rights Council on the obstacles that prevent people from enjoying their human rights.

Endnotes

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ILLICIT FINANCIAL FLOWS, POVERTY AND HUMAN RIGHTS

feature

Lloyd Lipsett

Lawyers have played an important role in creating the offshore system. Lloyd Lipsett argues that they cannot wash their hands of responsibility for its impact on fundamental human rights.

In October 2013, the International Bar Association's Human Rights Institute (IBAHRI) published an innovative new study, *Tax Abuses, Poverty and Human Rights*. The publication was the result of over a year of research and international consultations by a Task Force on Illicit Financial Flows, Poverty and Human Rights. Although tax abuses have been rising in prominence on the global political agenda in recent years, the issues have rarely been framed in terms of human rights. From the early feedback on the IBAHRI Task Force's work, an explicit human rights analysis is a welcome contribution to the global debates on tax justice, and further research and discussion is required in order to provide more practical guidance to policy-makers and practitioners.

The Task Force found that tax abuses have considerable negative impacts on the enjoyment of human rights. Simply put, tax abuses deprive governments of the resources required to provide the programmes that give effect to economic, social and cultural rights, and to create and strengthen the institutions that uphold civil and political rights. Actions of states that encourage or facilitate tax abuses, or that deliberately frustrate the efforts of other states to counter tax abuses, could constitute a violation of their international human rights obligations, particularly with respect to economic, social and cultural rights.

In the context of the developing world, the tax abuses of greatest concern to the Task Force included transfer-pricing and other cross-border intra-group transactions; the negotiation of tax holidays and incentives; the taxation of natural resources; and, the use of offshore investment accounts. Secrecy jurisdictions are also a concern because of their role in facilitating tax abuses.

> *"Practical guidance can help policy-makers and practitioners to think through the human rights implications of their actions and advice."*

The Task Force's human rights analysis also underscores the link between human rights and extreme poverty. For instance, the UN Human Rights Council had recently adopted *Guiding Principles on Extreme Poverty and Human Rights* that describe how poverty is connected as a cause or consequence of violations of 14 different human rights and all the key human rights principles—ranging from the right to food, the right to health, the right to education, the right to social security, to the principle of transparency.

Building on its review of international human rights law, the Task Force's report presents a number of conclusions and recommendations for governments, business enterprises and the legal profession:

Conclusion #1: States have obligations to counter tax abuses at the domestic and international level, including through cooperation in transnational institutions. While it must be recognized that international human rights treaties do not address tax abuses in an explicit manner, the Task Force concludes that States' legal obligations related to economic, social and cultural rights can be applied to the question of tax abuses, in terms of their actions at the domestic level, in their international cooperation efforts and in their participation in multilateral institutions.

Conclusion #2: Business enterprises have a responsibility to avoid negative impacts on human rights caused by tax abuses. The emerging human rights guidance for business enterprises suggests that all business enterprises, including corporate legal advisers and bankers, should exercise due diligence on the potential negative impacts of their operations—including with respect to the impacts of their tax planning strategies. Indeed, tax abuse is poised to become an important issue for business enterprises in terms of corporate social responsibility, reputational risk and human rights.

Furthermore, the estimated scale of corporate tax abuses also undermines some of the claims that foreign investment

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"Lawyers must balance their obligation to defend their client's interest with the underlying role of the tax system in society."

and private enterprise are major drivers of sustainable development. While there is undeniable evidence that foreign investment and private enterprise is—and can be—a powerful force for development and positive human rights impacts, evidence about the extent of tax abuses by transnational enterprises serves to reinforce criticism and cynicism about the role of the private sector in development.

Conclusion #3: The legal profession has an important role in assisting states and business enterprises in confronting the negative impacts of tax abuses on human rights. There was widespread agreement in the interviews that lawyers must balance their obligation to defend their client's interest with the underlying role of the tax system in society. One stakeholder stated that "we also need to encourage positive performance and the positive leadership role that lawyers can play in creating rules and regulations. Lawyers need to decide what is acceptable behaviour for their profession and to take the issue [of tax abuses] outside an individual decision for an individual lawyer."

Early Reactions and Next Steps

Not surprisingly, the early reaction to the Task Force's report has been varied. Tax justice advocates and human rights organisations have welcomed the linking of tax abuses and international human rights law—which provides an additional rationale for action on these important issues. Tax practitioners have raised valid questions about the need for more precise criteria to delineate legitimate tax planning and the tax abuses that fall afoul of human rights standards. Some commentators have stressed the need for additional research to better understand the magnitude of tax abuses and their impacts on developing countries.

The IBAHRI Task Force welcomes these comments and is also encouraged to see new initiatives and conferences that are delving into different aspects of the issues raised by the publication. While the Task Force's publication succeeded in providing a broad framing of issues and stakeholder feedback in terms of international human rights standards, the details of abusive tax schemes and practices also need to be analysed at a more microscopic level. The development of further case studies can help to provide concrete and nuanced illustration of the links between tax abuses and their negative impacts on human rights. The development of practical guidance can help policy-makers and practitioners to think through the human rights implications of their actions and advice.

The Task Force's publication on tax abuses and human rights therefore should be viewed as a starting-point for a global conversation between states, business enterprises, civil society organisations and the legal profession about ensuring that the human rights dimension of taxation is increasingly understood and more fully respected.

Lloyd Lipsett was the rapporteur for the International Bar Association Human Rights Institute Task Force on Illicit Financial Flows, Poverty and Human Rights. He is an international human rights lawyer with over 15 years of experience working with leading companies, governments, national human rights institutions, civil society organisations and indigenous peoples.

This article is based on an article entitled "The Six Trillion Dollar Question" that appeared in the IBA's Global Insights magazine in October 2013: **http://www.ibanet.org/Article/Detail.aspx?ArticleUid=E2915C5C-B70B-4A64-9D85-A0613827DF33.**

The IBAHRI Task Force's publication can be accessed at: **http://www.ibanet.org/Article/Detail.aspx?ArticleUid=4A0CF930-A0D1-4784-8D09-F588DCDDFEA4.**

HUMAN RIGHTS AND JUST TAXATION

feature

Thomas Pogge

Around half of the world's population is denied the right to an adequate standard of living. This will only be remedied if their governments can secure adequate tax revenues from large companies and wealthy individuals. Reform of the rules governing transnational financial flows turns out to be central to the cause of universal human rights.

The most widely underfulfilled human rights, by far, are social and economic ones, such as the right to a standard of living that is adequate for the health and well-being of oneself and one's family, including food, clothing, housing and medical care and necessary social services, and the right to security in the event of unemployment, sickness, disability, widowhood, old age or other lack of livelihood in circumstances beyond one's control.[1] About half of all human beings suffer serious deprivations of one such kind or another and have no access to the necessary social services that would protect them.

The first-line responsibility for these unfulfilled human rights lies with the governments of the countries in which the poorer half live. But these governments are also poor. While the industrialized states have annual revenues in the order of $20,000 to $50,000 per person, India has annual revenues of barely $200 per person and many other governments are poorer still. These large international discrepancies are due to two factors: the *per capita* gross domestic products of poor countries are much smaller; and they also raise a much smaller proportion of their GDPs as government revenues, typically under 20% as compared to an OECD average of well over 40%.

It is difficult for poor-country governments to raise income or consumption taxes from the poor majority of their population — such taxes are unpopular, costly to collect and aggravate the very human rights deficits they are supposed to alleviate. But such governments also encounter difficulties in imposing taxes on those who could pay. Through sophisticated efforts, wealthy citizens of these countries, and corporations operating within them, escape taxation to an extent that would be unthinkable in an affluent country with political clout and a highly sophisticated and well-funded tax administration. Boston Consulting Group estimates that 33.3% of all private financial wealth owned by people in Africa and the Middle East and 25.6% of such wealth owned by Latin Americans — some $2.6 trillion — is kept abroad; while the analogous estimates for North America and Europe are 1.8% and 7.9%, respectively.[2] To raise taxes on the income and capital gains produced by this wealth, poor countries must largely rely on the honesty of their taxpayers as they lack access to information about their citizens' overseas holdings.

Transnational corporations (TNCs) also massively escape taxation, typically by creating additional subsidiaries in tax havens and then instructing their poor-country subsidiaries to contract with their tax-haven subsidiaries into money-losing arrangements involving trade misinvoicing, abusive transfer prices as well as inflated consulting and trademark fees.[3] These arrangements diminish the taxed profits of the poor-country subsidiaries while increasing the untaxed profits of the tax-haven subsidiaries. Global Financial Integrity estimates that corporate tax abuse accounts for 80% of all illicit financial outflows from less developed countries, or about $4.7 trillion during the 2002–11 period and $760 billion in 2011 alone.[4] This is five or six times the sum total of all official development assistance flowing into these countries during the same periods.[5] Christian Aid calculates that, through these profit- and tax-diminishing capital outflows, governments of less developed countries have lost tax revenues in the order of $160 billion annually —

Article 25 of the Universal Declaration "Everyone has the right to a standard of living adequate for the health and well-being of himself and of his family, including food, clothing, housing and medical care and necessary social services, and the right to security in the event of unemployment, sickness, disability, widowhood, old age or other lack of livelihood in circumstances beyond his control ... Motherhood and childhood are entitled to special care and assistance. All children, whether born in or out of wedlock, shall enjoy the same social protection."

"The first-line responsibility for unfulfilled human rights lies with the governments of the countries in which the poorer half live. But these governments are also poor."

or about $2.5 trillion for the Millennium Development Goals period (2000–2015). "If that money was available to allocate according to current spending patterns, the amount going into health services could save the lives of 350,000 children under the age of five every year."[6]

Four groups of agents bear responsibility for the human rights deficit that results from poor countries' inability fully to collect reasonable taxes. First, the secrecy jurisdictions and tax haven countries (including Switzerland, Ireland, the UK and the US) which structure their tax and legal systems so as to encourage tax abuse and also typically protect bank secrecy against the tax authorities of less developed countries. Second, the individuals and corporations that erode the tax base of poor countries by using tax havens to hide their wealth and profits. Third, the bankers, lawyers, accountants and lobbyists who devise, implement and "legalize" these schemes. Fourth, powerful rich-country governments which facilitate the tax dodging of their TNCs abroad[7] and get tax havens to cooperate with their own tax enforcement efforts without ensuring that poor-country governments receive similar cooperation.[8]

The key to reducing the tax gap and consequent human rights deficit in the poor countries is global financial transparency: the abolition of shell companies and anonymous accounts, automatic exchange of tax information worldwide, and the requirement that, in their audited annual reports and tax returns, TNCs report their sales, profits and taxes paid country by country for each jurisdiction in which they operate. Such financial transparency would not merely advance tax justice but additionally protect human rights by also curtailing the activities of criminals such as terrorists, money-launderers, and traffickers in persons, drugs and weapons.

These changes must be implemented by the governments of tax havens and other rich countries, which will continue to move forward so long as there is sufficient pressure and support from their populations. Tax dodgers and their bankers, lawyers, accountants and lobbyists can help by not opposing or subverting the needed reforms and by collaborating toward the formulation and acceptance of ethical standards governing, for example, the conduct of TNCs or of international tax lawyers and accountants. A major break-through for financial transparency is now within reach. Let us ensure that the populations of the poor countries, whose basic human rights are at stake, participate fully.[9v]

Thomas Pogge is Leitner Professor of Philosophy and International Affairs and founding Director of the Global Justice Program at Yale, President of Academics Stand Against Poverty (ASAP) and of Incentives for Global Health. He chaired the International Bar Association's Human Rights Institute (IBAHRI) Task Force on Illicit Financial Flows, Poverty and Human Rights, which produced the report Tax Abuses, Poverty and Human Rights .

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5 **http://iff.gfintegrity.org/iff2013/2013report.html. http://mdgs.un.org/unsd/mdg/SeriesDetail.aspx?srid=569&crid=**

6 Christian Aid, False Profits: Robbing the Poor to Keep the Rich Tax-Free (Christian Aid, March 2009), p. 3. **https://www.christianaid.org.uk/Images/false-profits.pdf.** There are many pressures toward improving current government spending patterns in poor countries, which are often distorted by corruption, bloated security apparatuses and indifference to the poor. Insofar as such efforts are succeeding, additional revenues would have an even larger human rights impact than Christian Aid is calculating.

7 An example are the "tax holidays" periodically granted by the US Congress, such as the American Jobs Creation Act of 2004, which enabled US-based TNCs to repatriate profits accumulated in tax havens at a discounted 5.25% (instead of the usual 35%) tax rate. Without the prospect of such tax holidays, US TNCs have little to gain from shifting their profits from poor countries into tax havens.

8 Even the OECD's new landmark model agreement on automatic exchange of financial information is likely to exclude many less developed countries from its benefits because they lack the resources to set up the data collection arrangements required to qualify as a reciprocating partner.

9 For more on human rights and tax justice, see International Bar Association's Human Rights Institute (IBAHRI) Task Force on Illicit Financial Flows, Tax Abuses, Poverty and Human Rights, **www.ibanet.org/Human_Rights_Institute/TaskForce_IllicitFinancialFlows_Poverty_HumanRights.aspx**

"The key to reducing the tax gap and consequent human rights deficit in the poor countries is global financial transparency"

THE CELTIC CHIMERA: IRELAND'S TAX POLICIES STARVE THE PUBLIC SECTOR AND THE POOR

feature

William K. Black

Ireland has been at the forefront of moves to bring the offshore model into the heart of the onshore economic system. It is also suffering disproportionately from the impact of austerity. These two facts are connected.

Ireland adopted its distinctive corporate income tax policies as part of an integrated strategy based on the 'Washington Consensus' policies made infamous in Latin America. This neoliberal strategy restrained wage increases and starved the public sector of funds by sharply reducing revenue from taxes, particularly corporate income taxes. Ireland's policies appeared to work for some time and Ireland was hailed as the "Celtic Tiger."

In 2007 the Cato Institute's director of tax policy studies, Chris Edwards, explained that Ireland's success derived from 'a series of hard-headed decisions that shifted Ireland from big government stagnation to free market growth.' According to Edwards, the key to Ireland's success was 'its excellent tax climate for business'. And the benefits of this approach were spreading throughout the continent:

The Irish model of rock-bottom business taxation has been hugely influential. In recent years, corporate tax rates have been slashed across Europe. [T]he average rate in the EU has fallen from 38 percent in 1996 to 26 percent in 2006.

Inspired by the Celtic Tiger, many Eastern European nations have … installed both low corporate taxes and simple, flat-rate taxes on individuals.[1]

Edwards even argued that Ireland proved that there was no particular reason for a nation to educate its workers because it could import skilled workers that other nations had paid to educate:

It's become fashionable to argue that increased government spending on education is the key to success for countries like Ireland. I'm skeptical. For one thing, booming economies today can attract high-skill workers from global labor markets. In Ireland, brain drain has been replaced by brain gain as smart people from across Europe are drawn into the country's growing industries.[2]

"Irish tax policies have spread the rot to other nations by inducing a race to the bottom."

The Cato Institute wasn't alone in its enthusiasm for the Irish approach. In 2004 Jean-Claude Trichet, the President of the European Central Bank, cited Ireland as the "model" for nations entering the EU:

[T]he process of transformation that [Ireland] began over four decades ago has become a model for the millions of new citizens of the European Union. The new Member States of the EU have had to confront economic challenges whose magnitude and long-term importance are similar to those that faced Ireland when you began your work. Thanks to Ireland's economic success, to which you devoted your life, we can be confident that economic reform works.

Trichet cited Ireland as his definitive proof of the correctness of the two main points of his talk. The substance of these points is a staple of the stump speech of every

Jean-Claude Trichet, admirer of the Irish model. Here seen facing right. (CC by 3.0, Euku)

Republican candidate for the presidency in the U.S. The first priority is to deregulate and reduce worker's rights.

[O]ne has to consider the astonishing experience of Ireland, which recovered from poor economic and fiscal conditions in the mid-1980s to an impressive pace of economic activity and sound fiscal position in no more than a decade. In addition to a favourable macroeconomic environment and the benefits derived from participation in the European Union, the economic recovery was grounded on far-reaching home made structural reforms in the labour, capital and product markets.

The second priority is to cut government spending (Washington Consensus style austerity, which Trichet call "fiscal

"Ireland is a much smaller problem than the UK, but it has added materially to an already severe problem."

consolidation"). Trichet notes that Ireland has done both and is the Celtic Tiger because it has followed both policies.

In this respect, the dramatic acceleration of output in Ireland in the post 1987 period can be associated with a vigorous and successful project of fiscal consolidation starting in 1987. This programme was based on tight expenditure control via subsidy cuts, social security reform and a streamlining of the public sector and control of public expenditure.

Trichet further argued that Ireland provided proof that austerity could enhance growth, particularly if it were associated with large cuts in taxes:

Ireland's experience … clearly shows how policies geared to fiscal consolidation do not necessarily entail contractionary effects on real aggregate demand and economic activity. [I]in spite of the tightening policies undertaken, the rate of growth showed a significant increase in relation to previous years. [S]ignificant budget consolidation based on spending reduction enhanced the long term fiscal sustainability and increased the policy credibility of a more favourable tax regime.

Because Ireland adopted the euro it no longer has a sovereign currency, which exposes it to the extortion of the "bond vigilantes" if it runs a large budget deficit.

As a result, once the credit and property bubbles collapsed it was forced to cut expenditures on health and employment when they were most needed. If Ireland really collected corporate income tax at the stated rate of 12.5% the Irish economist David McWilliams estimates it would have 8 billion euros greater annual income and Irish suffering would be greatly reduced. Instead we have seen the return of wide scale Irish emigration, including recent university graduates – the nation's treasure. Far from importing talented workers as in the Cato Institute fantasy, the country is exporting them.

Irish tax policies have not only left Ireland unable to provide appropriate health services and provide the jobs that would keep Irish university graduates in Ireland – they have spread the rot to other nations by inducing a race to the bottom. Liechtenstein has recently announced plans for a 12.5% across-the-board corporation tax rate, explicitly to match Ireland's. More recently the United Kingdom has been offering reduced rates.

In fairness, the UK is among the greatest tax havens in the world given the notorious Channel Islands that epitomize the 'captured state'. Ireland is a much smaller problem than the UK, but it has added materially to an already severe problem.

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Endnotes

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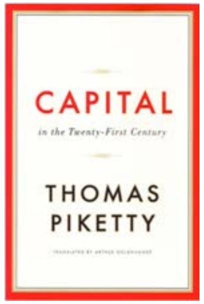
book review



Capital in the Twenty-First Century

Thomas Piketty, translated by Arthur Goldhammer
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Rent in the Twenty-First Century

Thomas Piketty's international publishing sensation is, in significant part, a manifesto for tax justice.

Thomas Piketty's book *Capital in the Twenty First Century* is first and foremost a voluminous and fascinating historical account of how unfettered capitalism tends towards extreme inequalities of income and wealth. Left unaddressed, these inequalities will threaten democratic nation states and their founding social values.

The book is replete with tax justice debate: the entirely avoidable rise of inequality, the case for progressive taxation, enforced transparency, and improved international cooperation. These are long-standing issues for us, which we have (albeit briefly) discussed with him.

Piketty's core argument is that for centuries returns to capital have been higher than rates of economic growth of output and income. The corollary of this argument is that without political interventions the share of national income going to labour declines. The inevitable outcome is that wealth becomes ever more concentrated in the hands of a tiny proportion of the population – the 0.1 per cent – who create rentier dynasties that dominate the political economy. Although tax havens are not a major feature of the book, the wealth management industry that operates from such places merely aggravates this situation by enabling rentiers to dodge attempts to tax wealth, for example through inheritance tax, wealth tax, capital gains tax, and of course, income tax.

Drawing on massive data sets for France, Germany, Sweden, the U.K. and the U.S.A., Piketty shows that brief periods of convergence towards greater equality in the mid-20th century were historical aberrations caused by war, financial crises, trade union power, advances in public education, and the rise of progressive income taxes. The Reagan-Thatcher reaction in the 1980s reversed this momentum, restoring capitalism to its pre-1914 trajectory. The future for Europe and North America, not to mention poorer countries elsewhere as they play catch-up, looks from his perspective like France's 19th Century *Belle Époque*. Barring a revolution, it seems, the American Dream is dead.

The book might have been more accurately titled *Rent in the Twenty-First Century*. It is essentially a study of how unearned incomes such as dividends, interest and property rents accumulate fastest in periods when growth rates stabilise at relatively low rates - 1.0 to 1.5% annually. Faced with ecological constraints and a huge demographic shift from population growth to decline, this may well be the bleak future facing those countries already out there on the technological frontier.

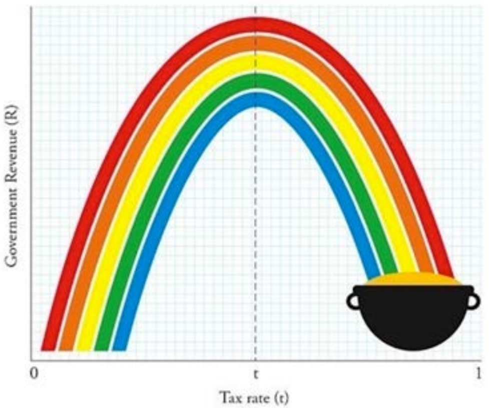
Piketty has a lot to say about tax. He calls progressive taxation "indispensable", argues for massive hikes in marginal income tax rates, and decries the "endless race to the bottom, leading, for example, to cuts in corporate tax rates and to the exemption of interest, dividends, and other financial revenues from the taxes to which labor incomes are subject." Piketty uses the language of "tax competition", or "fiscal competition" - though it's nothing to do with genuine competition: a far better term is "tax wars."

Faced with this and the closely related trend towards an "inegalitarian spiral", Piketty proposes a progressive annual tax on capital, supported by comprehensive and automatic exchange of information between countries. One suggestion certain to provoke the "supermanagerial" class and their acolytes is that the optimal top tax rate in developed countries is "probably above 80 percent." Right wing commentators have reacted predictably to this, claiming that high marginal tax rates reduce work and effort, and reduce productivity growth. To which Piketty responds robustly:

The reduction of top marginal income tax rates and the rise of top incomes do not seem to have stimulated productivity (contrary to the predictions of supply-side theory) or at any rate did not stimulate productivity enough to be detectable at macro level.

He demolishes American economist Arthur Laffer and his magical mystery curve, which claims – without empirical evidence - that tax cuts lead to higher tax revenues, through curbing avoidance and boosting economic growth. The fear that higher marginal tax rates on incomes above €500,000 would lead to a

book review (contd)



The Laffer Curve. Laffer's theory is that above a certain rate, higher taxes lead to lower revenues. Piketty estimates this rate is around 80 percent. (With thanks to www.and-smith.com.)

flight of top executives to Switzerland or Canada, says Piketty, is "*not only contradicted by historical experience and by all the firm-level data at our disposal; it is also devoid of common sense*." Indeed.

Despite the grandiose title, this is no rehash of Marx' *Das Kapital*. Marx argued there was an inexorable tendency for profits to decline, forcing the process of technological change and deeper exploitation of labour, and ultimately driving the system to its end. Capital was more than physical or financial assets; its essence lies in the power relations between owners of capital, land owners, the state, the managerial class and labour. Piketty, by contrast, looks at society through the lens of wealth and income, with power disproportionately held not by the top 1 percent targeted by the Occupy movement, but by the mostly rent-seeking multi-millionaires and billionaires in the top 0.1 percent.

Like John Maynard Keynes, Piketty wants to save capitalism from itself. Growing inequality is structurally embedded in capitalism, and the solution lies with democratising markets. "If we are to regain control of capitalism" he says, "we must bet everything on democracy." Indeed, again.

Piketty concludes that a tax on capital is the over-riding priority for tackling inequality. High marginal income taxes might partially redistribute the extraordinary incomes of the bonus-grabbers but will do little to redistribute inherited wealth. He suggests confiscatory annual capital taxes at 10 percent or higher on billionaires. Phew!

A tax on capital, he adds, might promote a necessary overhaul of accounting standards, leading us to transform how we define and value various types of assets, liabilities and net wealth. Current flaws in the system, he notes, "have contributed to the many financial scandals the world has seen since 2000." I can picture Prem Sikka and Richard Murphy nodding their vigorous agreement.

Piketty's data sets do not include developing countries in any meaningful way, though he does note that people in developing countries may be the biggest losers of the sweeping historical transformations that boost inequality. To help staunch the outflows of capital from Africa and other parts of the developing world – which outpace aid by a wide margin - he urges fiscal co-operation and data sharing to help poorer countries "root out the systematic pillage" that has emptied their treasuries. Foreign companies, their stockholders, and their enablers are, he says, "at least as guilty as African élites." I couldn't have said it better myself.

He also admits that the true wealth and inequality picture "is actually even larger than we estimated on the basis of official accounts" - because so much wealth is hidden behind offshore trusts and companies in tax havens. He cites our landmark study *The Price of Offshore, Revisited,* with its estimate of $21-32 trillion offshore, but settles on a substantially lower figure produced in a study by Gabriel Zucman, while admitting that could be merely a "lower bound". I'd argue strongly that ours is a far more robust estimate: we've not seen any serious effort to take down our numbers, though many would like to. In any case, despite the importance and sheer magnitude of this issue, this is in one sense a distraction

from Piketty's astonishing accomplishment with its vast historical and empirical sweep. The strength of his book lies elsewhere.

This book is a very, very rich pudding. I have read all of its 577 pages and it's clear that many of the reviews out there were written on the basis of a quick skim (at best) and a dusting-down of old ideological prejudices. Piketty calls his tax on capital proposal "utopian" and he's probably right, but he's on our side, folks, in wanting to open up a discussion about economic injustice and what can be done to tackle it.

There are many, many bag-carriers of the wealthy elites who will want to close down this debate. They will do whatever it takes to rubbish Piketty and his book. We should resist them. Read the book and draw from its strengths.

Review by John Christensen

news in brief...

Tax That

Take That front man Gary Barlow is one of almost a thousand wealthy individuals, including other pop stars, who will have to pay back money claimed as tax relief in the so-called Icebreaker scheme. According to the London *Independent*, Judge Colin Bishopp "ruled that Icebreaker was primarily a tax avoidance scheme, not a system of commercial investments". The British Prime Minister, David Cameron has defended the singer from calls for him to hand back his OBE. Cameron's father was a pioneer in Anglo-Panamanian financial services.

Gary Barlow, lead singer of Take That and tireless campaigner for charity.

Amazon in Trouble Again

Amazon employs 5,000 people in the UK and in 2012 it generated sales of £4.3 billion in the country. In the same year it paid £4 million in UK corporation tax. Amazon told the London *Sunday Times* that "[we pay] all applicable taxed in every jurisdiction [where we operate]. We have a single European headquarters in Luxembourg with hundreds of employees to manage this complex operation."

KPMG Netherlands Boss Quits

The head of accounting giant KPMG, Jurgen van Breukelen resigned last month in the midst of a controversy over the building of the company's new headquarters. According to Reuters, in April prosecutors said that "they suspected the joint venture set up to develop of the new Dutch HQ was used to boost costs in tax filings to Dutch authorities with the aim of reducing taxable income".

Singapore Edges Out Mauritius

Singapore has overtaken Mauritius as the main source of "foreign direct investment" into India. According to the *Times of India*, "during the last financial year, India attracted $5.98 billion in FDI from Singapore, whereas it was $4.85 billion from Mauritius". Much of the money invested in India comes from the "round tripping" of funds controlled by Indian nationals and in recent years the Indian government has put pressure on Mauritius to provide more information about investors using the island state as a tax haven. It seems that Singapore is eager to take up the slack.

Pharma, Heal Thyself

The pharmaceutical sector's tax planning has had more publicity in recent weeks than its core business of treating disease. First Pfizer sought to take over Astrazeneca. A "big benefit" of the deal, according to Pfizer's CFO, was the lower rate the merged company would have to pay (Reuters). Then the Chinese state-run newspaper *Legal Daily* accused British company GlaxoSmithKline of avoiding almost £10 million in taxes.

Drug companies receive enormous direct and indirect subsidies from the countries that host them. These subsidies are justified in terms of the contribution the sector makes to the public good. It is only a matter of time before the accumulated evidence of aggressive tax avoidance calls these subsidies into question. Why give taxpayers' money to companies that then seek to avoid paying tax on their handsome profits?

Lighting Up The Darkness

The indefatigable Richard Murphy, editor of *Tax Justice Focus: Country-by-Country Reporting* among many other things, has published a new report of the size of Britain's black economy. The report, *In The Shade*, estimates that around £1 in every £10 in sales goes unrecorded for tax purposes. These unrecorded sales are costing the government £40 billion a year in lost tax receipts.

Just What Would It Take?

Last month the banking transnational Credit Suisse pleaded guilty to criminal charges in the United States and agreed to pay $2.5 billion in penalties. The American attorney general Eric Holder said that hundreds of employees at the bank were involved in conspiring "to help tax cheats dodge US taxes".

news in brief (contd)

According to the *New York Times*, the Securities and Exchange Commission granted Credit Suisse a temporary exemption from a federal law that requires a bank to hand over its investment-adviser license in the event of a guilty plea. Meanwhile, Brady Dougan, Credit Suisse's CEO, has assured investors and analysts that the case makes "no material impact on our operational or business capabilities".

Business Among Friends

Oxfam's recent briefing paper *Business Among Friends: Why Corporate Tax Dodgers Are Not Yet Losing Sleep Over Global Tax Reform* explains how recent moves by the G20 and the OECD have left some of the worst problems of tax avoidance and evasion untouched. The report highlights the need for all countries affected by transfer pricing and other forms of abuse to be present at the negotiations on new standards for information exchange.

Hollande Eases Up On Penalties For Tax Evasion

According to *Reuters* the French government is planning to reduce the interest payments on late payments of tax by companies.

The irresistible François Hollande, back in the pages of the Tax Justice Focus. (CC by 3.0, Matthieu Riegler)

The government has already recovered just over a billion dollars after introducing similar reductions of fines and penalties for wealthy individuals. 80% of those who have so far come clean had money salted away in Switzerland. Last April the French President told reporters that he intended to "eradicate tax havens in Europe and the world" after a scandal involving a government minister, Jérome Cahuzac, left him "wounded, shocked and bruised". From eradication to accommodation in a little more than a year …

And Finally …

As this edition of the *Focus* went into production the *Telegraph* reported that the British tax authorities raised £1 billion more than expected "by targeting middle class professionals including accountants and barristers". Inquiries by campaigner Richard Murphy revealed that HMRC wasn't able to explain how it came up with the £1 billion figure. If the government is going to grab headlines it ought really to have more than wishful thinking to back up its claims.