TAX JUSTICE FOCUS

The newsletter of the tax justice network

THE ILLS OF FINANCIAL DOMINANCE

Doreen Massey

The power of the financial sector in Britain has worked a transformation on the country's 'common sense'. A successful challenge will require a radical change to the language we use to describe our shared life.

Societies take different shapes in different eras. They are framed by distinct forms of economy, specific social and political arrangements, and particular common understandings of how the world works. These are expressed too in distinct geographies, which in turn feed back into the way in which the country develops.

Since the undermining of the social-democratic settlement of the post-war years, UK economy and society has been framed by what we have come to call 'neoliberalism'. This was not inevitable; other alternatives were available; the victory of neoliberalism was an outcome of political and social contest.[1] And central to that victory, and to neoliberalism in its widest sense, was the triumph of finance. 'Finance', in the current era, is not just a sector of the economy; it is at the core of a new social settlement in which the fabric of our society and economy has been reworked. There is a long history in the UK of 'the City' having an important and often harmful role, but this time is different. Finance and financialisation now mould our economy, geography, ideology and politics to a degree that is not only astonishing but deeply negative.

Some of the dismal results of this dominance at national level are well documented: the vicious exacerbation of economic inequality; the crowding-out of other sectors of the economy (far from being the golden goose, the dominance by finance makes life

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Crowding out productive enterprise in the City of London. Threadneedle Street, once teeming with small businesses specialising in the garment trade, now home to a very different kind of stitch-up. Image: Chris P Dunn, some rights reserved.

much more difficult for other sectors); the pervasiveness of individualism and competitive greed. But the way these things work out on the ground in different places highlights even more the contradictions inherent in this social settlement.[2]

London itself, the pinnacle of finance's success, is riven with contradictions. A city once known for its variety of small industries is seeing that rich ecology erased, especially in the area around the City, by the power of finance as it either buys up, or simply has the effect of raising the price of, land and property. Small companies, perfectly viable in production terms, cannot survive – a real irony given the ritual political invocation of small businesses as the hope for the future.

London is also the most unequal city in the country, and this too produces problems. It exacerbates the poverty of the poor, especially through house prices. In its most bizarre recent manifestation local councils are 'decanting' their benefit-claiming poor to other regions. The whole social reproduction of the city is made more difficult.

"London, a city once known for its variety of small industries, is seeing that rich ecology erased"

Meanwhile 'the regions' also suffer from the dominance of finance. It is not only that this sector itself, and its wealth, are located in London. It is that its dominance of the national economy (and polity – see later) actively undermines regional growth.

Thus the City sucks in graduate labour from other regions, depriving them of a stratum from which economic growth might spring. (Meanwhile politicians castigate them for a lack of skills!) If the golden goose argument worked there'd be a geographical 'trickle-down' to the rest of the country. The truth is that the opposite happens. Meanwhile the degree of national inequality is exacerbated, through the regional dimension, as owner-occupiers in London and the South East 'make' more from increases in house-prices than they earn from their jobs.

One response from the London financial elite is that there is a fiscal transfer from London to the regions. Not only does this not address the dynamics of regional growth, it is a carefully calibrated fiction.[3] It is a political slogan based on very narrow criteria, which fails to take account of a host of ways in which London (and finance specifically) benefit from national policy. And it provokes damaging antagonisms, dividing the nation on regional lines when hostility should really be addressed to finance and the super-rich.

So we have a dysfunctional capital city, ferocious inequalities both within that city and between a vortex of growth in the South East and a land often referred to as 'the Rest of the Country', and an economic path that is detrimental to balanced growth. And all these are problems arising, not from the crisis of finance and the way that has been addressed, but from its growth, its dominance. It is imperative that we construct a different settlement.

One reason this bizarre arrangement exists is that finance dominates not only the economy but also politics and ideology. Its political influence is widely documented, yet somehow unseen or simply accepted (compare with the outrage at any hint of influence by trades unions). Yet in fact it is extremely active: it funds endless research projects that confirm its status as the golden goose, it is seen as a source of unbiased expertise, there are revolving doors with government and it doesn't even have to 'lobby' very explicitly, since it is cosily part and parcel of the social world of the elites. Policies across the range reflect the interests of finance, whose upper échelons are at the core of an elite whose spatial concentration in the South East consolidates their mutual support. There is a grossly unequal geography, as well as class configuration, of democracy and of voice in this country. And the City puts in a lot of work to keep it thus.

"In this society that celebrates choice we are told there is no alternative"

Less routinely recognised is how 'finance thinking' has become hegemonic ideologically. Finance may be a global industry but part of its power lies in the fact that it is intimate too – it gets inside our heads.[4] People from finance are interviewed as 'experts' in the media, as though they had no interests at stake. Economics is thus removed from political contestation. Competitive individualism is taken for granted. Distinctions are forgotten (erased) between earned and unearned, between value creation and value extraction (convenient, since finance's growth has depended so much on the latter – hence the burgeoning inequality from which we began this thumb-nail sketch of the state of the nation). In this society that celebrates choice we are told there is no alternative. This truly is hegemonic common sense, and it is at this level that social settlements are consolidated. It is at this level, therefore, that a challenge must be launched. This means not just contesting individual policies and issues (though that must be done) but even more importantly challenging the whole framework, the very language, that has become our society's common sense, and that both obscures the injustice that is being done and lulls us into acceptance that it is all inevitable.[5]

Moreover if this challenge is necessary because of the effects 'at home', it is equally so because of the UK's role in the wider world. As the Tax Justice Network has tirelessly pointed out, the existence of tax havens, and the practices of tax evasion and avoidance, are a means of redistribution from global poor to global rich and a key cause of world poverty. London's finance sector is a prime node in these arrangements. Could we develop what I have called 'a politics of place beyond place', addressing our responsibilities for the global effects of our economy?[6] Indeed the internal and external politics of place are linked – the poverty in London is an element in the same dynamics as the poverty in the global South. To take us back to the initial argument, London's finance sector was one of the crucial birthplaces of, and is now a key place of diffusion of, global neoliberalism, with its practices of cutting back state services, privatisation and deregulation. These are among our main exports.

We are living a strange situation – a populace guided by a hegemonic discourse that prevents escape from neoliberalism and yet a wide range of disparate groups whose interests potentially range them against the dominance of finance. There has been an economic (financial) crisis, but the ideological carapace has not cracked. Is it possible to build alliances, perhaps as suggested in the *Green New Deal*, and to break out of the common sense of this finance-dominated social settlement?

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Endnotes

1. See the Kilburn Manifesto: 'After neoliberalism?' by Stuart Hall, Doreen Massey and Michael Rustin. **http://www.lwbooks.co.uk/journals/soundings/manifesto**. Also in *Soundings*, 53, Spring 2013, pp. 8 – 22.
2. For a fuller analysis see Doreen Massey (2010) World City, Polity Press.
3. See World City (note 2) and Nicholas Shaxson and John Christensen (2013) *The Finance Curse*, Tax Justice Network.
4. See Kilburn Manifesto (note 1).
5. This is what I have begun to do in Doreen Massey (2013) 'Vocabularies of the Economy' at the Kilburn Manifesto site, and in *Soundings*, 54, Summer 2013, pp. 9 – 22.
6. See World City (note 2).

BE CAREFUL WHAT YOU WISH FOR

editorial

Nicholas Shaxson and Dan Hind

This edition of theTax Justice Focus explores the notion of the finance curse - the idea that countries hosting oversized financial centres suffer problems similar to those faced by countries rich in natural resources like oil. Rent-seeking, uneven development, asset price bubbles, industrial decline, heightened inequality, greater authoritarianism, grand corruption and deeper poverty have often followed hard on the heels of the discovery of oil and mineral wealth. Many of these countries are said to suffer from a 'Resource Curse', or from the 'Paradox of Poverty from Plenty'. An increasing body of work suggests that finance can have similar effects. Many of these harmful effects pre-date and go deeper than the economic and political crises that have become apparent since the collapse of Lehman Brothers in 2008.

This broad and heavily under-researched area of research is a work in progress for us at the Tax Justice Network, and the features in this edition build on and complement a short e-book we published recently entitled **The Finance Curse: how oversized financial centres attack democracy and corrupt economies**. Our main features and articles look in some detail at the United Kingdom, one of the world's largest and best-disguised offshore centres, and at one of its closest offshore satellites, the Channel Island of Jersey. Finance can be useful but beyond a peak size, it can turn bad. An oversized financial centre on your doorstep is the last thing you should wish for.

Despite this edition's fairly British focus, its messages have powerful implications for financially-dependent economies around the globe.

In our lead article, **Doreen Massey** explores the deep cultural and psychological effects of financial dominance. There is a long history of 'the City' having an important and often harmful role in the UK, she explains – but this time is different. Finance and financialisation now mould its economy, geography, ideology and politics to an astonishing degree and is at the core of a new social settlement in which the fabric of its society and economy has been thoroughly reworked. She argues for a campaign to change the 'common sense' about economics, as expressed in everyday language.

Adam Leaver of the Centre for Research on Socio-Cultural Change (CRESC) then offers a corrective to the idea, commonly heard in UK

Death Star now operational. *The new skyscraper at 20 Fenchurch Street in the City of London has an innovative design that helps maximise the office space available on the site. Unfortunately, the same design concentrates and reflects bright sunlight into a beam that melts the fittings of cars and bicycles parked outside. The Tax Justice Network awards it the Metaphor of the Month Prize, for embodying the finance curse in 37 storeys of cutting edge architecture.*

"In one sector, people appropriate vast economic rents from dangerous, valuable and potentially explosive substances that will, if not handled very carefully, leak out and pollute the surrounding environment. In the other, they dig mines and drill oil wells."

policy-making and opinion-forming circles, that London is the engine of Britain's prosperity. The reality is different: Britain is really two countries, where finance has ensured that London and its hinterland enjoys the 'metropolitanisation of gains' from economic activity in the whole country – while the rest of Britain suffers 'the nationalisation of losses' emanating from London's financial centre.

Next, **Tamasin Cave** of Spinwatch introduces us to the ways in which the financial and political elite in Britain merge and overlap, to the point where it no longer makes sense to talk about finance lobbying the government. The government is now a lobbyist for finance, to a degree that would have been unimaginable only a generation ago.

In the final feature in this edition **Nicholas Shaxson,** author of **a 2007 book** about oil in Africa and **another** about financial centres and tax havens, traces the similarities between mineral wealth and finance in greater detail. In one sector, people appropriate vast economic rents from dangerous, valuable and potentially explosive substances that will, if not handled very carefully, leak out and pollute the surrounding environment. In the other, they dig mines and drill oil wells.

These features are followed by an interview from the British tax haven of Jersey. **Mike Dun** describes the massive economic crowding-out that has occurred on his home island and explains how nationalist undercurrents in a small community can close down debate, entrenching political 'capture' by the financial sector. 'Thus "*Jersey Finance*" is tapped into a long-established mindset that has no relationship with analysis or discussion.'

It isn't all about the UK though. **David Officer** sends us a Letter from Cyprus, that brings the story of the crisis there up to date and flags up the imminent visit to the island's university of John Bruton, former Irish Prime Minister and current head of the International Financial Services Centre in Dublin. Will Bruton endorse proposals to cut corporation tax? Or will he finally break with the financial consensus? Our eyes are on Cyprus.

Finally, **Markus Meinzer** sets out the latest developments on automatic information exchange and FATCA. In amidst the bewildering detail, the outlines of new struggles are emerging.

A LETTER FROM CYPRUS

The economic crisis in Cyprus was long predicted. But the full extent of the problems in the country's financial sector did not become apparent until March, with the now infamous 'bail in' of depositors, the imposition of harsh austerity measures by the TROIKA, the collapse of one major bank and the near collapse of another. Since then the economy has slowed down and unemployment has risen rapidly. The anger of Greek Cypriots has many targets: the European Union; the Germans; their own political elites.

Most are unaware that the crisis derives in important respects from the country's status as a tax haven. The island's pre-crisis prosperity depended on attracting more or less illicit foreign capital, especially from the former Soviet Bloc. In order to do so Cyprus provided effective banking secrecy and low rates of corporation tax.

Billions of dollars left the island before March for the British Virgin Islands, St Kitts and elsewhere. Anxiety about the state of the Cypriot banks led to capital flight, which weakened the banks and turned anxiety into panic.

Cyprus now offers a stark warning of the dangers that small island states face if they try to develop by becoming tax havens. Not only does the strategy produce its own vulnerabilities in times of severe economic downturn, it seriously compromises the ability of an economy and society to grow in a stable and equitable way. Productive activities are crowded out, local elites become beholden to the financial services sector and the quality of governance deteriorates.

Later this month the former Irish Prime Minister (Taoiseach) John Bruton, now head of the International Financial Services Centre in Dublin, will visit the island and speak at the University of Cyprus. It will be fascinating to see if he joins prominent opinion formers on the island, including Professor Andreas Theophanos of the University of Nicosia, in calling for a reduction in the island's corporation tax to nine per cent.

Dr David Officer, University of Nicosia

THE METROPOLITANISATION OF GAINS, THE NATIONALISATION OF LOSSES

feature

Adam Leaver

The prosperous South East can no longer afford to subsidise the rest of the United Kingdom. Or so runs the conventional wisdom. The facts, on the other hand, are rushing headlong in the opposite direction.

A recent 800 page report highlighted just how unequal the UK regional economic landscape has become.[1] In ratio terms, the UK's largest 2nd tier city generates around 10% of the output of London – the second highest capital to 2nd tier city output inequality within the EU. In terms of the regional concentration of GDP creation, we have more in common with a Hungary, Bulgaria, Romania or Greece than a Germany, Netherlands or Sweden. And while there is evidence to show that the UK's 2nd tier cities were growing faster than the capital pre-crisis (from a lower base), that trend is now being undone as austerity cuts bite into the non-metropolitan North and West.

At one level it is no surprise that the UK coalition government's immediate post-election rhetoric about rebalancing has been abandoned, to be replaced by a new, morally-laden discourse about the unfair subsidies received by the regions and the rights of Londoners to keep more of 'their' income.[2] UK recessions encourage internecine squabbles over resources and London's position as both political and economic centre mean there was only ever likely to be one clear winner. But as Londoners and their informal representatives look on jealously as the bank notes seem to disappear to the non-metropolitan North and West, it is perhaps worth revisiting how we got here. This is a complex issue that requires balance and open-mindedness if we are to understand the diversity of flows in a national economy.

In terms of the UK national growth model, two processes have cemented London's dominance within the economy. First we now rely less on the manufacture of things and more on the manufacture of credit. We have bought into a growth model that depends on the ability of our banks to lend against assets, and for households (and businesses) to convert the capital gains from those rising asset prices into expenditure. It is a startling fact that the real value of housing equity withdrawal under Thatcher and Blair was marginally higher than the real value of GDP growth.[3] This national model significantly empowers London's form of 'gentlemanly capitalism': the historically entrenched culture and interests of land and finance within the UK which prioritise the making of money from money over the making of money from industrial enterprise. The political and economic spheres mutually reinforce each other: finance has access to the charmed circle of policy formation because of the great wealth and prestige bestowed upon them by a credit-fuelled, asset based growth regime.

Second, the broader process of privatisation and the extension of public-private partnerships disproportionately benefit a global city like London. London does attract capital, but it does so because it is a kind of conversion machine, taking national and international assets, converting them into revenue streams from which well-placed individuals skim high pay. In other words: London attracts capital because it is also extractive. Let's take the UK's Private Finance Initiative (PFI)[4] as an example. The PFI is a form of Public Private Partnership (PPP) where public infrastructure projects are funded, built and managed by the private sector to a public specification. Generally PFI contracts last

Is credit expansion driven by the City of London a drag on growth? Image: Jan van der Crabben, some rights reserved.

> *"The flipside to the revenue streams clipped by metropolitan elites is a series of costs and liabilities passed on to non-metropolitan areas."*

a minimum of 25 years, during which the private sector receive payments in exchange for bearing the project risk. Notionally private sector participants are paid only if services are delivered according to the negotiated concession agreement. The decomposition of activities around a contracted-out infrastructure project leads to a fragmentation of corporations around specialised functions, so that one company may provide the finance, another may build the school or hospital, another may manage the services. In theory some of these functions need not be located on the site of the project. And certainly the revenue streams do not all circulate regionally: the finance company probably has its operating office in London, as might the service management office. Even the building firm might be co-ordinated from London using local contractors on site. Overseas companies that invest in infrastructure funds are also likely to have an office in London, and those senior workers are likely to be extremely well paid.

Fragmentation has led to a concentration of certain functions like financing and asset management in London. This has diminished capacity in the regions through the withering of broad competences, the destruction of joined up supply chains, and skills drift as talent is forced to relocate down South to find a job. State-sponsored investment projects across the country have benefited private sector growth in London and the South. The obvious counterfactual – a publicly funded and organised infrastructure development programme – would result in a greater proportion of project revenue streams accruing to the region around the development site, kicking in multipliers that would further benefit the local economy.

These two developments tell us something about modern day capitalism in the UK. Contrary to the fantasies of free-market proponents, the success of London has much to do with an active UK state and its willingness to take on or underwrite private sector liabilities. The banking sector, for example, is a net recipient of state funds which the whole country must pay for, even though the private gains are largely realised in London. By our calculations, the Treasury received taxes of £203 billion over five years up to 2006/7; substantially less than the cost of the UK bank bailouts, estimated at between £289 billion to £1,183 billion by the IMF.[5] If we factor in the impact of government bailout guarantees on bank borrowing rates, then the longer term subsidies are even higher.[6] And all this is before we consider the costs of mis-selling and other predatory habits

Liabilities are also underwritten at public expense in the case of PFIs. Typically PFI consortia leave the maximum contractual risk with the local state or cost at a premium any risks that cannot be offloaded. So the flipside to the revenue streams clipped by metropolitan elites is a series of costs and liabilities passed on to non-metropolitan areas. There are also many hidden, contingent liabilities – as when NHS Trusts cannot repay their PFI loans, or unwieldy contracts produce inefficiencies and exorbitant penalty clauses which are costly to renegotiate. And this is before we discuss the many contracts that overshoot their original estimates.

All of these interventions should be thought of as State subsidies; received mainly by private subsidiaries operating in the capital, and paid for by taxpayers the length and breadth of the country. This quiet cross-subsidy from North and West to South East has been running un-noticed for a long period of time. Its unanticipated result is a kind of regional moral hazard: the metropolitanisation of gains, and the nationalisation of losses.

But we have arguably reached the limits of that model. Despite the current political spin that a three per cent rise in house prices (driven mainly by an eight per cent rise in the capital) marks the end of our problems, there is a limit to how far asset prices can rise when wages and growth are stagnant. We just aren't growing fast enough to take on the liabilities to fuel the asset price rises, and we aren't paying people enough to allow them to take on larger interest repayments. If debt is a claim on our future growth, there comes a tipping point where the scale of debt repayments acts as a drag on growth, crowding out investment and consumption.

From this perspective, a genuine rebalancing of the economy to a more sustainable model will involve a lot more than devolution. It will involve a lot more than encouraging private sector growth in the regions. It will require a fundamental rethink of the corporate welfare apparatus that has so benefitted the London area in recent years.

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3. Froud, J., Johal, S., Law, J., Leaver, A., Williams, K. (2011) Rebalancing the Economy (Or Buyer's Remorse), Centre for Research on Socio-Cultural Change (CRESC) working paper 87, p.22 [online] **http://www.cresc.ac.uk/sites/default/files/Rebalancing%20the%20Economy%20CRESC%20WP87.pdf**
4. The PFI is a form of Public Private Partnership (PPP) where public infrastructure projects are funded, built and managed by the private sector to a public specification. Generally PFI contracts last a minimum of 25 years, during which the private sector receive payments in exchange for bearing the project risk. Notionally private sector participants are paid only if services are delivered according to the negotiated concession agreement.
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6. For more detail on this, see Haldane, A. (2010) 'The $100 Billion Question', comments given at the Institute of Regulation & Risk, Hong Kong, 30 March 2010 [online] **http://www.bankofengland.co.uk/publications/Documents/speeches/2010/speech433.pdf**

IS FINANCE LIKE CRUDE OIL?

THE RESOURCE CURSE, OR THE PARADOX OF POVERTY FROM PLENTY.

feature

Nicholas Shaxson

Countries rich in minerals are often poverty-stricken, corrupt and violent. A relatively small rent-seeking elite captures vast wealth while the dominant sector crowds out the rest of the economy. The parallels with countries 'blessed' with large and powerful financial sectors are becoming too obvious to ignore.

While serving as the Reuters correspondent in oil-rich Angola in the mid 1990s, I wondered how such a 'rich' country could suffer such poverty. The shortest answer at the time was 'War'. Angola's conflict had many causes, but without the diamonds to fuel rebel leader Jonas Savimbi's army, not to mention the government's offshore oilfields, it would have been less bloody, and shorter.

As I arrived in Angola in 1993 a British academic, Richard Auty, was putting a name to a then poorly-understood phenomenon: what is now widely known as the 'Resource Curse'. Countries that depend heavily on natural resources like oil or diamonds often perform worse than their resource-poor peers in terms of human development, governance and long-term economic growth. Studies by renowned economists such as Jeffrey Sachs, Paul Collier, Terry Lynn Karl, Joseph Stiglitz and many others have now established the Resource Curse in the academic literature, and in the public mind too.

A weak version of this Curse, which few would disagree with, holds that resource-dependent countries tend to be bad at harnessing those resources to benefit their populations - as Figure 1 strongly suggests. The windfalls are squandered. A stronger version is more surprising: natural resources tend to make matters *even worse* than if they had been left in the ground, leading to higher rates of conflict, more corruption, steeper inequality, deeper absolute poverty, more authoritarian government, and lower long-term economic growth. I am in no doubt that the stronger version of the curse applied to Angola on all these metrics when I lived there.

To be fair, the wider cross-country evidence here is more complicated. Some countries like Norway that already have good governance in place before resources are discovered seem to fare relatively well – but being rich first is no guarantee of success either. Michael Edwardes, the former chairman of ailing British car manufacturer British Leyland, spoke of this with some prescience in 1980, following the OPEC oil price shocks: "If the cabinet does not have the wit and imagination to reconcile our industrial needs with the fact of North Sea oil, they would do better to leave the bloody stuff in the ground." Even if some rich countries can suffer from mineral windfalls, it is poor, badly governed countries that tend to suffer the most. The picture also varies with the global commodity price cycles: things look particularly bad during troughs in these cycles – as in the mid 1990s – and look less bad, at least on the surface, in the boom years.

How do we explain this 'curse?' The explanations fall into three main categories. First is the so-called "Dutch Disease." Large export revenues from oil, say, cause the real exchange rate to appreciate: that is, either the local currency gets stronger against other currencies, or local price levels rise, or both. Either way, this makes local manufactures or agriculture more expensive in foreign-currency terms, and so they lose competitiveness, and wither. Much higher salaries in the dominant sector also suck the best skills and talent out of other sectors, out of government, and out of civil society, to the detriment of all. Overall, the booming natural resource sector 'crowds out' these other sectors, as happened when many oil producers saw devastating falls in agricultural output during the 1970s oil price booms.

Finance-dependent economies, it turns out, suffer a rather similar Dutch Disease-like phenomenon, as large financial services export revenues in places like the United Kingdom or the tax haven of Jersey raise the cost of housing, of hiring educated professionals, and the general cost of living. A Bank for International Settlements (BIS) study last year found that finance-dependent economies tend to grow more slowly over time than more balanced ones, and noted that, by way of partial explanation, 'finance literally bids rocket scientists away from the satellite industry'. My short *Finance Curse*

> *"If the cabinet does not have the wit and imagination to reconcile our industrial needs with the fact of North Sea oil, they would do better to leave the bloody stuff in the ground."*
>
> *Michael Edwardes, chairman of carmaker British Leyland, 1983*

e-book, co-authored with John Christensen, provides plenty of detail on this.

A second standard explanation for the Resource Curse is revenue volatility. Booms and busts in world commodity prices and revenues can destabilise the economies of countries that depend on them, further worsening the crowding-out of alternative sectors. Gyrations in the world oil price – from below $10/barrel in the late 1990s to well over $100 within 10 years – has played havoc with budgeting in many oil-dependent countries, often with terrible effects on economic and political stability and broad governance. Those alternative sectors that were crowded-out during the booms aren't easily rebuilt when the bust comes: it is a ratchet effect. Again, there are close parallels with the financial sector, a source of great volatility, as the latest global financial crisis shows. Britain's industrial base, decimated by (among many other things) over-dependence on the financial sector, is proving slow to recover, post-boom.

The third category for explaining the Resource Curse – the biggest, most problematic, and the most complex – falls under the headline 'governance'.

Why do natural resources tend to make governments more wasteful, corrupt, and authoritarian?

A big part of the answer lies in the fact that minerals in the ground provide unproductive economic 'rents': easy, unearned money. As the Polish writer Ryszard Kapuscinski so brilliantly put it:

Oil is a resource that anaesthetises thought, blurs vision, corrupts. Oil is a fairy tale and, like every fairy tale, it is a bit of a lie. It does not replace thinking or wisdom.

When easy rents are available, rulers lose interest in the difficult challenges of state-building, or the need for a skilled, educated workforce, and instead spend their energies competing with each other for access to a slice of the mineral 'cake'. While those neglected sectors wither, this competition among 'godfathers' can lead to overt conflict, particularly in ethnically diverse societies, but it can also lead to great corruption, as each player or faction in a government knows that if it does not act fast to snaffle a particular mineral-sourced financial flow, another faction will. This is the recipe for an unseemly, corrupting scramble.

The financial sector, likewise, contains a multitude of potential sources of easy 'rents'. A secrecy law, for instance, has long been a source of rents for Swiss bankers, who haven't needed to do much else apart from watch the money roll in. More grandly, the network of British-linked secrecy jurisdictions scattered around the world, serving as 'feeders' for all kinds of questionable and dirty money into the City of London, is another big source of rents for the financial sector. Financial players' special access to information is another. Martin Berkeley, a former British banker, described one mechanism deployed by his bank as it sought to sell its customers dodgy derivatives:

On their client database they had in big letters written 'Client Has Screens' - meaning the client actually knows what the markets are doing: these tricks couldn't be played on them.

The Libor scandal provides another example of rent-seeking. One might reasonably also make a comparison between owning an oil well and having – as the banking system does – the ability to create money. Yet there is a difference too: rising credit creation – and the growing private debts that accompany it – generate fees for the financial sector that are extracted not from under the ground, as with oil, but from debtors, taxpayers and others: from the population itself.

Another source of the trouble in resource-rich states is that when rulers have easy rents available, they don't need their citizens so much to raise tax revenues. This top-down flow of money undermines the 'no taxation without representation' bargain that has underpinned the rise of modern, accountable states through the rise of a social contract based on bargaining around tax, and through the role that tax-gathering plays in stimulating the construction of effective state institutions. If the citizens complain, those resource rents pay for the armed force necessary to keep a lid on protests.

In economies dependent on finance we don't see the same kind of crude, swaggering petro-authoritarianism of Vladimir Putin's Russia or José Eduardo dos Santos' Angola, but we do see some surprisingly repressive responses to criticisms of the financial sector and the finance-dominated establishment, particularly in small tax havens like Jersey, as Mike Dun's article in this edition – along with the main *Finance Curse* e-book and my book *Treasure Islands* – repeatedly illustrate.

All these processes – the economic crowding-out of alternative economic sectors such as agriculture or tourism, plus the 'capture' of rulers and government by the dominant mineral sector, who become apathetic to the challenges posed by trying to stimulate other sectors – add up to a mortal threat not just to democracy, but also to the long-term prospects for a vibrant economy. Since Angola's long civil war ended 11 years ago, politicians have routinely called for a 'diversification' of the economy and a 'rebalancing' away from dependence on oil. The fact that petroleum still makes up over 97 percent of exports and contributes to 60 percent of GDP, is testament to the difficulty even the most well-meaning reformer faces. Similarly, calls for 'rebalancing' away from excessive dependence on the financial sector have tumbled from the mouths of politicians in the United Kingdom and Jersey. But these calls will prove equally empty if they do not actively work to shrink and contain the financial sector.

Nicholas Shaxson is author of Poisoned Wells, *a book about the resource curse in oil-rich countries in Africa, and of* Treasure Islands, *a book about financial centres and tax havens.*

MORE THAN A LOBBY: FINANCE IN THE UK

feature

Tamasin Cave

Finance and the British state are mutually embedded to the point that it can be hard to tell where one stops and the other starts. Here Tamasin Cave of Spinwatch gives us a brief tour of the tangled web that is public life in the UK.

Lord Sassoon, until January this year economic secretary to the Treasury in the UK government, is a man who bestrides the worlds of government and finance. In 2012 he delivered the inaugural summer lecture of the British Bankers Association. He began by thanking the outgoing head of the BBA, Angela Knight, for her services to Britain:[1] 'Angela, the country owes you a debt of gratitude', he said, praising her for her steady, calm presence during the Northern Rock crisis of 2007, for her masterful lobbying to defend the City in Brussels, and for rebuilding banking's relationship with the UK government and with the industry's customers.

Sassoon went on to explain how, as early as 2003, the Bank of England financial stability team had already identified 'some of the key issues that would be at the heart of the crisis, for example, the over reliance of Northern Rock on wholesale funding, the extent of Bradford and Bingley's exposure to the buy-to-let market, RBS's increasing exposures in Germany and elsewhere'.

He talked of how in 2005, Andrew Large, who was deputy governor of financial stability at the Bank, was 'ringing alarm bells', one of two people identified by Sassoon at 'the top global table that were standing out against the orthodoxy'. 'Sadly we all listened but took no action,' said Sassoon.

According to Lord Sassoon, this is a government 'utterly committed to ensuring the UK is open to business and that London continues to thrive as a global economic centre… A government with a number of bankers in its ranks, led by a Prime Minister who is proud to say he comes from a stock broking family'. Sassoon's remarks echo the sentiments of the Labour Party's Ed Balls a few years earlier. In 2006 Ed Balls, then the Economic Secretary to the UK Treasury, told an audience at the BBA that 'when the WorldCom accounting scandal broke in the US, we resisted pressures

Offshore dynasts, old and new.

from commentators for a regulatory crackdown'. He went on to say that the UK government had a 'specific and clear interest' in safeguarding 'the light touch and proportionate regulatory regime that has made London a magnet for international business'. Of course it was this same 'light touch' regulatory regime that allowed Northern Rock, Bradford and Bingley and RBS – finance as a whole – to engage in a frenzy of risky business.

Lord Sassoon is only one of many former bankers to have served in the current UK government. In the current Cabinet both David Laws, a Liberal Democrat Minister for Schools, and Oliver Letwin, a Conservative Minister at the Cabinet Office, worked in investment banking before they entered Parliament. In fact the UK comes second only to Switzerland for the number of people moving through the 'revolving door' between the finance sector and officialdom according to a report by the OECD.[2] Baron Green of Hurstpierpoint, previously Chairman of HSBC, is currently a Minister at both the Department for Business Enterprise and Skills and the Foreign and Commonwealth Office. In May 2013 the former Chairman of Goldman Sachs, Richard Sharp, joined the Bank of England's Financial Policy Committee, the new watchdog set up to protect the public from another financial meltdown.[3] Two months later another former Goldman Sachs banker, Mark Carney, became the governor of the same institution. Current and former employees of the investment bank also known as 'the vampire squid' have donated £8.8million to Britain's political parties in the last decade. Sharp himself donated £400,000 during that period. And this is only a fraction of what the sector gives. In 2011, hedge funds, financiers and private equity made up over a quarter of Conservative Party funding, with the City as a whole contributing more than half of its donated income.

The global accountancy firms – the so-called "Big Four", PWC, KPMG, Deloitte and Ernst & Young – are also deeply embedded in the

"The UK comes second only to Switzerland for the number of people moving through the 'revolving door' between the finance sector and officialdom according to a report by the OECD."

British state. They earn hundreds of millions of pounds a year from government business while loaning their staff to government departments and political parties, where they advise on everything from tax law to privatisation programmes.

All four companies insist that their involvement is limited to providing 'technical insight' into proposed polices. But at the same time some actively lobby government for changes in tax legislation. Ernst & Young's Tax Policy Development team, for example, says that it 'works with clients to develop proposals for changes in tax policy that can be taken to government'.

'Unlike a traditional lobbying service,' the pitch reads, Ernst & Young's team will work with its clients to develop 'technical policy options in a form that is used inside Government today'. Put simply, this means it uses its knowledge of the workings of government to lobby for clients. This, it says, means that tax changes can be 'implemented with the minimum of delay', and makes sure that 'the concerns of policy-makers are addressed'. This gives proposed tax breaks 'the maximum chance of adoption'. In this respect, the insider status of E&Y is clearly of benefit to its clients.

The advantages to clients of lobbying for tax policy changes – as opposed to tax planning – are clearly explained in Ernst & Young's pitch: 'In an era where the government is focusing on actively identifying and countering tax avoidance, and where there has been considerable media coverage on particular 'tax avoiders', policy development offers a low risk alternative.' In other words, 'policy development' – lobbying for changes in the law – offers its corporate clients a less risky way to reduce their tax bill.

Incidentally, Ernst & Young's lobbying team would not be covered by the government's proposed register of lobbyists, which is making its way through Parliament. If it passes in its current form, the register will include only a tiny fraction – 5 per cent on some estimates – of the £2 billion UK lobbying industry.[4]

Former politicians beat a well-trodden path in the other direction. Tony Blair took a job with JP Morgan when he left Downing Street. He joins a group of politicians-turned-financiers too numerous to name here. But some idea of the scale of what's happening can be grasped if we restrict ourselves to former Ministers in the Department of Health during the New Labour years. Alan Milburn is an advisor to Bridgepoint, a private equity firm and PWC. Norman Warner has been an adviser to Apax Partners, another private equity firm. And Patricia Hewitt has advised Cinven, yet another private equity group.

And then there is the current Prime Minister. As Lord Sassoon notes, David Cameron comes from a stock broking family. This underplays things a little. His father co-founded the Panamanian investment company Blairmore Holdings and was the chairman of Close International Asset Management, based in Jersey.[5] Unlike Tony Blair, the British Prime Minister from 1997 to 2007, who only began to make extensive use of tax havens on leaving office, Cameron is part of an offshore dynasty. Blairmore indeed.

Through the revolving door that takes politicians into lucrative employment and financiers into government, through party donations, and through the informal mechanisms of finance's lavish hospitality, the political class is integrated with the sector to the point where it can be difficult to see where one stops and the other starts. Ambitious politicians have been eager to associate with investment bankers and others from the sector. There's money to be made, of course, but also the seductive sense that they are in the room with the people who understand how the world really works, with the winners. Billions in taxpayers' money seems like a small price to pay for such company. And the pervasive secrecy and clannishness of British politics only compounds the problem. We do not know, for example, how much money finance contributes to the free market think tanks that enjoy such sympathetic coverage in the UK media.

Given the degree of overlap, and the shared commitment to London as a world financial centre, the organized lobbies for finance do not have to spend much time persuading the government to promote their interests. Instead, in the words of the then-Chancellor and later Prime Minister Gordon Brown, they work together to 'promote the City and its financial service expertise throughout the world'. It is hardly surprising that the few warnings that reached Sassoon's 'global top table' went unheeded. By then the British government no longer saw the financial sector as one lobby among others. It saw itself as a lobbyist for finance. This was, and is, a recipe for trouble.

Tamasin Cave is a director of SpinWatch **spinwatch.org** *and leads the* **Alliance for Lobbying Transparency** *coalition, which is campaigning for a statutory register of lobbyists in the UK. She is the co-author of* A Quiet Word: Lobbying, Crony Capitalism and Broken Politics in Britain, *which Random House will publish in April 2014.*

Endnotes

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"THE LOBSTERS WILL STILL BE HERE"

An Interview with Mike Dun, in the British Channel Island of Jersey

Mike Dun is a writer, political activist and citizen, based in Jersey. He blogs at **tomgruchy.blogspot.com**.

Nicholas Shaxson, the editor of this issue of the *Focus*, interviewed him about life on a small island with a large financial sector.

Shaxson: It has been said that many jurisdictions with large financial sectors suffer from 'state capture' by the sector. To what extent is this true of Jersey, if at all?

Dun: Communities – especially small ones – are liable to be 'captured' by a dominant economic activity such as mining, or making pots, and they will be vulnerable to downturns or failures. Jersey was 'captured' to some extent by the 'Newfoundland trade', a cod-fishing business that was the biggest economic sector for many years until it failed in the mid 19th century (bringing down Jersey's main bank in the process). The families involved were politically important, and intermixed with the remnants of the old feudal system and farming interests. There was diversification then.

Fishing has faded but the farming lobby is still important: not because it is economically significant now, but because of the 'countryside' lobby, which is tied up with Jersey's self-image as an old agricultural centre, its love of the Jersey cow, and so on. The big difference with the 'finance' sector is that the wealth [in finance] is not generated by Jersey-based hands, and is totally unrelated to the local population.

Political power rests with the finance houses through their local States [Jersey government] representatives. But the whole picture is complex. Powerful groups such as Jersey lawyers and their structures are in the net. The lawyers are the entrenched establishment here; they have control over everything: and they are, of course, manipulated by the bankers. The lawyers are the old established families. The bankers are mostly outsiders who come and go: they often get transferred. If you control the law, the courts, and which laws are implemented – then you don't have to do a great deal else.

Shaxson: A foreigner whom I interviewed in Jersey on my last visit described her new home as 'an island without morals.' Is this your feeling?

Dun: Finance has steamrollered morals and ethics and many other quaint things. The 'Methodist' Jersey Evening Post [the island's only regular newspaper,] for example, used to refuse even to publish horse racing results: they took their Methodist principles seriously. Now they promote the usual gambling pursuits, not to mention the gambling that takes place in the finance sector. It is totally captured and is still the only source of information for many within the Island.

Shaxson: Has finance crowded out other sectors? Can other sectors thrive?

Dun: Take farming, for instance. There were 1100-1200 dairy famers here in the 1950s; a few months ago this had dropped to 26, and it's probably down to 24 now (though the farmers that remain have much bigger herds than before.) A lot of those are coming up to retirement age, and there is nobody to carry on. They cannot compete: you cannot produce with your hands the sort of money, the millions, that run through these little offices. The country parishes are now owned by the people in the finance industry, to a large extent, and the farmers often rent their fields from the new wealthy.

Jersey's newly launched "Innovation Fund" is a good example of how the government merely pays lip service to economic diversification. The original intent was to encourage new start ups or new ideas, but the published rules showed that it was only designed to attract 'high return' activities. The only ones that could possibly reach the target were finance-based – unless it was to start a gold mine somewhere. It demonstrated the 'high net worth' thinking that dominates Jersey. Fortunately the **Scrutiny Report** [a body producing non-binding recommendations on government policies, which is one of few Jersey bodies that serve as any kind of check or balance to executive power] has focused on this, and the rules are now 'modified' to include charity groups and lesser activities needing start up funding – in theory! They will probably chuck a few thousand to charities to make it look good.

In reality, the thinking is not about encouraging small businesses that are just providing a living for a few people. Families with children and parents that get old are ultimately money- and resource-hungry. The game is wealth generation, and high net worth individuals.

Shaxson: How easy is it to criticise the financial sector?

Dun: All criticism that might include the word 'Jersey' is actively discouraged. At one level this is an emotional reaction with a 'nationalist' undertone: everything carrying the 'Jersey' word has to be the best in the world. Thus 'Jersey Finance' is tapped into a long-established mindset that has no relationship with analysis or discussion.

interview (cont)

At a political level this strange suppression of dissent has been honed to a level of perfection so that even people with no traditional family or business links with Jersey will mouth the same hostile and unthinking response of: 'if you don't like it, there's a boat off the island in the morning'. Such attitudes affect dissenters in their normal daily lives when seeking somewhere to live, or with respect to employment.

The 12,000 people employed in the finance sector have had their tongues removed, of course, as a condition of their jobs. In fact a very large number of workers with knowledge – that includes civil servants, say, or teachers – are effectively silenced. You cannot get lawyers to come out and say anything. They won't speak to you if you bump into them in the supermarket. They will not discuss anything that could be slightly contentious: only the very safest subjects. There are no human rights groups among the lawyers. If there is a finance case with a human rights angle, of course, they will argue it. But will they fight for the 10,000 people here with housing difficulties? There is no lawyer, ever, who spoke out for them. Not ever, ever.

Shaxson: Jersey has no general elections and no system of organised political parties. How easy is it more generally to criticise the powers that be?

Dun: Jersey has a mathematical barrier to reform insofar as it is very difficult to draw together enough people prepared to lobby on political issues. There is no unified or co-ordinated action at all. They are so gutless, the States [government] members, even the progressive ones: they all get so hung up on personal issues. The establishment don't even need to do anything right – because there's no challenge. When I heard on the radio that the Labour Party in the UK defeated the government [in August 2013 on taking military action in Syria], I found it extraordinary.

Environmental issues such as 'Line in the Sand' or "Saving Plemont" will attract large numbers of people here, because such are seen as 'non political'. Catching syphilis is more socially acceptable than supporting a political group in Jersey. Death is preferred to joining a political party.

Shaxson: Can one imagine a Jersey without a finance centre?

Dun: Just 20,000 people survived in Jersey during the 17th century. Many of them supplemented their income from fishing, farming and knitting with smuggling and piracy.

Nothing much has changed because finance is really only a development of the latter two.

The current world-wide attention [on tax havens] might stimulate reform at an international level, and Jersey is now being forced to face the 'Independence or bust' question that challenged the American Colonists in 1775. Taxation is of course still at the root of the problem.

A more balanced economy with a revitalised tourism sector must be a realistic possibility, because the Island has many natural attractions and exploitable characteristics. And the lobsters will still be here if the finance activity diminishes – though they might be available mostly for those prepared to catch them for themselves! Presumably the professional knowledge of those employed in the finance sector might be put to some more worthwhile use.

Finance has crowded out Jersey's once-vibrant music scene. The Beatles, for example, haven't played the Springfield Ballroom since 1963. Image courtesy of Tracks Memorabilia – **www.we-buy-beatles.com**

TOWARDS MULTILATERAL AUTOMATIC TAX INFORMATION EXCHANGE – IS FATCA THE FINAL WORD?

analysis

Markus Meinzer

The US Foreign Account Tax Compliance Act (FATCA) came into force on 1 January this year. So far, it has led nine other countries to sign bilateral treaties with the US to ease the compliance costs for their financial institutions. Many others are under negotiation.

However, even if partners choose the reciprocal model 1, the US will only deliver a trickle of information in exchange (See pages 41–43 of the TJN paper **'Bank account registries in selected countries**). While the US committed to improve their information disclosure in the future, the relatively slow pace of progress made in finalizing bilateral deals raises doubts as to whether promises alone from the US will suffice to convince other jurisdictions to engage with FATCA. Financial institutions in some countries may choose instead to close down US accounts and therefore achieve low compliance costs with the FATCA law without a bilateral deal.

In the meantime, however, the OECD is working on a multilateral system for automatic tax information exchange whose mechanics are informed by both FATCA and the powerful EUSTD-amendments (Chapter 5 of **'The UK-Swiss tax agreement : doomed to fail'**). More details are expected in 2014, but early layouts of the system are promising in terms of coverage and openness of the system.

In terms of coverage, the plans of the OECD appear to address **some problems** associated with the original FATCA regulations, while leaving others unremedied (e.g. safe deposit boxes). Most importantly, accounts held by trusts appear at the moment to include a reporting requirement to the respective countries of residence about all related parties of trusts. The settlors, trustees and beneficiaries of trusts (effectively defined as controlling natural persons) would need to be disclosed to their respective country of residence. While such a reporting requirement without proper public national registries of trusts could not guarantee proper enforcement, such a disclosure regime is far more demanding than the US FATCA regulations. The draft US-form to be signed by account holders with respect to trust accounts leaves those off the hook very easily. You only have to tick the box stating that there is no involved US person – that's it.

With respect to openness, the system is envisaged to be located at the CoE/OECD Convention on Administrative Assistance in Tax Matters. While the Convention comes with a **price tag to it** – of paying homage to the 'OECD – it has the great appeal that countries can quite easily join the Convention. However, surrendering to **Global Forum scrutiny** is a condition and for countries with limited domestic tax capacity this hurdle may be too high.

A key campaign goal therefore may be to demand that those countries are given the opportunity to participate in this new multilateral automatic exchange system without being required to fully submit to peer review, nor to reciprocate data input during a transition period.

An open question about the OECD model is: will it also require banks to search their paper records, and not only their electronic records? This would be very important to counter tendencies to engage in 'Stone Age Banking', whereby relevant identification files are no longer held electronically, but only on paper in order to avoid reporting and taxation. Also, British and Swiss accounts held since time immemorial, at least during the era of colonialism and apartheid, could be included if paper records were to be reviewed as well.

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book review

The Dynamics of Global Economic Governance: The Financial Crisis, the OECD and the Politics of International Tax Cooperation

Author: Richard Eccleston

Published: Edward Elgar, Cheltenham, U.K. 2012
ISBN 978 1 84980 279 6

Faced with a singularly tepid economic recovery, unprecedented levels of sovereign and household debt, and widespread political malaise, this book sets out to address what I (and I suspect most of us) regard as a key issue: "Does the system have the political capacity to devise and implement an effective governance response to the grave challenges facing the global economy?"

The grave challenges come in many forms, including climate change, macroeconomic imbalances, sharply rising inequality, and others. Eccleston focuses on the politics of international tax cooperation, partly because this issue has moved centre stage in the past decade, forcing world leaders, senior tax officials and, above all, the OECD, to proclaim success even when progress has been minimal or non-existent: remember Sarko's claim in 2009 that "the days of tax havens are over"?

In practice it has historically been notoriously hard to reach and enforce international agreements on tax cooperation. Confronted by powerful entrenched interests, political progress has, at best, been around lowest common denominator policies (e.g. on request tax information exchange agreements) and the radical measures needed to create a global framework for effective cooperation have been firmly kept off the agenda.

At the risk of dampening enthusiasm, the kindest thing we can say about progress since the 2009 G20 summit is that world leaders have come under some pressure from rising public anger directed at tax avoidance, but the pressure is geographically uneven and even within G20 there is little genuine appetite for the substantive reforms TJN has been promoting since 2003. Civil society will need to monitor diligently to ensure that the warm words uttered at the G8 summit in Enniskillen this June turn into something more than mere window-dressing.

And herein lies the major stumbling block: even within regional groupings like the European Union, states have been reluctant to cede their sovereign authority on tax affairs. But it is at the global level that the gap between stated aspirations and actions really yawns. There is nothing in the space marked 'International Tax Authority'. The OECD, of course, lays claim to this exalted position, but lacks legitimacy and understandably remains tied to the interests of its own member countries (as the BEPS action plan illustrates all too clearly). The UN Tax Committee remains woefully under-resourced and lacks political status.

As Ecclestone points out, however, the push for reform provided by the G20's endorsement of the OECD's agenda since 2009 runs a particular risk insofar as major non-OECD countries within the G20, China in particular, may be unwilling to endorse and promote policies that underpin western economic interests. So the G20 momentum for reform might have peaked, and could rapidly diminish. Ecclestone is far from optimistic in his conclusions:

> *The dilemma facing the international community is that the need for effective global governance is as acute now as at any time in recent history… Despite this acute need, the capacity of the international system to develop and deliver effective governance is arguably lower today than during the immediate post-war period. Not only is the United States less willing and able to provide global leadership . . . but many of the rules-based multilateral institutions that were created as part of the Bretton Woods settlement are also in decline.*

This declining authority also extends to the OECD, which is steadily losing its grip on the tax agenda. While the OECD's powers wane, however, there are few signs of a new leadership arising from within the ranks of the BRIC or other 'emerging' economies. As the credibility of the arm's length method diminishes across the world, the tendency is more towards fragmentation as Brazil, China, India and others adapt their policies to their own needs, and the OECD will exhaust both time and political effort into patching up a broken system. It is not impossible that the emerging powers – China and India above all – will act to shore up the global institutions. Indeed, China's signing of the OECD Multinational Convention on Mutual Administrative Assistance in late-August 2013 might signal a major change in the political dynamics, in which the G20 will have greater cohesion in its attempts to secure international cooperation.

But faced with what is likely to be an extended period of slow economic growth, austere fiscal

book review (cont)

policies and rising inequality, there is every risk that international cooperation will succumb to the finance-oriented mercantilism of countries like the U.K. The prospects for progress towards effective global governance, Eccleston concludes, have never been more challenging.

This is not a book for the fainthearted, but it covers a lot of ground and addresses a key issue of our times. If governments are unable to rapidly agree on how to tax capital, tax regimes will inevitably become more inequitable, with consequent undermining of the legitimacy of democratic governance. A new international tax settlement is therefore urgently required, but the existing institutional frameworks for negotiating and implementing such a settlement are not fit for purpose. We may be in for a bumpy ride.

Review by John Christensen

news in brief

Base Erosion and Profit Sharing

OECD chief Ángel Gurría, a convert to the cause of automatic information exchange.

On July 18th 2013 the OECD published its **Action Plan on Base Erosion and Profit Sharing** (BEPS). On September 6th the G20 leaders said that they 'fully endorse' the plan and **stated bluntly** in their communiqué that 'profits should be taxed where economic activities deriving the profits are performed and where value is created'.

Here at the Tax Justice Network we have always taken the view that brass nameplates, nominee directors and the rest of the offshore sector's bag of tricks do not create value. The effective tax rate on transnational corporations should, if the G20 leaders mean what they say, rise steadily in the years ahead.

China Signs Up to Automatic Information Exchange

On August 27th China signed the OECD's Multilateral Convention on Mutual Administrative Assistance in Tax Matters. China has previously been slow to sign up to international initiatives and this apparent reluctance has been a useful excuse for those resisting effective reform in Europe and the United States. By signing the Convention China has made life for offshore's lobbyists significantly more difficult.

Though the Convention is by no means perfect, it does establish automatic information exchange as the basis for international cooperation on tax. This is an extremely welcome change. As recently as two years ago the OECD was still pushing information exchange on request and dismissing its critics – the Tax Justice Network, the Financial Transparency Coalition, the EU Commission and others – as impractical daydreamers. Now the OECD's Secretary General Ángel Gurría is singing a very different tune: 'Today's signing is both timely and important, as the G20 has endorsed automatic exchange of information as the new global standard'.

While it is a little galling to see the OECD taking credit for a shift in global tax policy it long opposed, this has to be balanced against the fact that the case for tax justice is steadily gaining ground in the global institutions.

India Introduces Capital Controls

In August India introduced new restrictions on the movement of money out of the country. **According to the Economist**, the allowance for personal remittances has been reduced from $200,000 to $75,000 a year and companies can spend no more than their book value on investments abroad without permission from the central bank. Previously, they were able to spend four times their net worth.

The Indian government has ruled out further restrictions. On August 30th the Prime Minister, Manmohan Singh, **said that** 'the last two decades have seen India grow as an open economy and benefit from it … There is no question of reversing these policies just because there is some turbulence in capital and currency markets.' Nevertheless, the Indian rupee is vulnerable to movements in transnational capital. If interest rates in the United States finally start to edge upwards, the currencies of developing countries will come under intense pressure. Capital controls, long out of favour, might be making a more sustained comeback in the months ahead.

Trick or Treaty in Mongolia

Tax treaties are sold to the public as a means to prevent the double taxation of firms and individuals. But it is becoming increasingly clear that they can also be used a means of facilitating double non-taxation. That's the conclusion Mongolia seems to have drawn. In recent years it has torn up agreements with the Netherlands, as well as with Luxembourg, Kuwait and the United Arab Emirates.

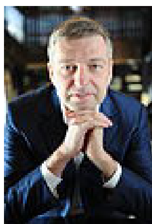
news in brief (contd)

The country is set to become a massive producer of copper. Rio Tinto, the Anglo-Australian mining group has a major stake in Mongolia mineral wealth, through its investment in the Oyu Tolgoi open mine cast in the Gobi Desert. **According to Reuters** the company believes that Mongolia's withdrawal from its tax treaty with the Netherlands will make no difference since 'the firm has a separate investment agreement with Mongolia which "stabilizes" treaties that were in force in 2009'.

Be that as it may, the Mongolians can take heart from the G20's recent communiqué on Base Erosion and Profit Sharing, which, as noted above, states that 'profits should be taxed where economic activities deriving the profits are performed and where value is created'. The Dutch government **has already signalled** its willingness to look again at the loopholes in its tax regime.

Perhaps the G20 leaders will look kindly on efforts of others to secure reasonable revenues from companies operating within their borders.

Injury Time for Monaco?



Dmitry Rybolovlev, the new owner of AS Monaco. Potash has never seemed so glamorous.

The recent purchase of football club AS Monaco by Russian potash magnate Dmitry Rybolovlev has drawn new attention to the massive tax advantages the tiny principality affords to its residents. Although French nationals working in Monaco are required to pay tax in France, the statelet itself has no income tax as such. Footballers from the rest of the world can keep all of their salaries.

Now that the club is owned by a billionaire this is becoming a major issue for other clubs in the French league. **The BBC reports** the president of the Ligue de Football Professionnel saying that, if left unchanged, the current arrangements will give AS Monaco a €50 million advantage over its competitors.

No Duty to Behave Badly

During debates about taxation in the UK defenders of the status quo like to point out that the managers of companies have a 'fiduciary duty' to minimise their tax bills. This in turn has led some to claim that directors are at legal risk if they do not do all they can to avoid tax.

The Tax Justice Network asked the law firm Farrer and Co to give its opinion on this widely used claim. The response, **available online here**, is unequivocal: 'It is not possible to construe a director's duty to promote the success of the company as constituting a positive duty to avoid tax'. Indeed, Farrer point out that the law in its current form gives ample protection to directors who choose to act responsibly and avoid aggressive tax avoidance and the opprobrium it attracts.

Alan MacDougall, who runs the pension investment adviser PIRC, told the *Guardian* that, 'we hope that directors, and their advisers, take careful note of this opinion. It is no longer acceptable for them to seek to justify tax avoidance through a misinterpretation of directors' duties'. Indeed, given the reputational risks associated with tax avoidance, due consideration to principles of equity and fair dealing might make more sense in simple business terms.

Papaconstantinou Set To Face Trial

According to the Financial Times, in August of this year Greek lawmakers voted by a large majority to send the country's former Finance Minister, George Papaconstantinou, to face trial. The charges relate to the so-called Lagarde List, the names of some two thousand Greek customers of HSBC Geneva.

In October 2010 France's then-Finance Minister Christine Lagarde handed the list to Constantinou. He is accused of removing the names of three family members, and of failing to hand any of the material to the police, charges he denies.

We already know that the widespread use of offshore jurisdictions contributed mightily to finance sector instability in the years running up to the crisis. It is becoming increasingly apparent that banking secrecy is at the heart of the current fiscal crisis in Europe.