TAX JUSTICE BRIEFING

# A TAX JUSTICE GLOSSARY

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| Affiliate | A related company or subsidiary |
| Aggressive tax avoidance | The use of complex schemes of uncertain legality to exploit taxation loopholes. |
| Arising basis | Treating income earned outside the country of residence as liable to tax in the year in which the income is earned, even if it is not remitted to the country where the tax is payable. Compare with the remittance basis. |
| Banking secrecy | Banking secrecy laws strengthen the normal contractual obligation of confidentiality between a bank and its customer by providing criminal penalties to prohibit banks from revealing the existence of an account or disclosing account information without the owner's consent. Can be used to block requests for information from foreign tax authorities. |
| Capital gains tax | A tax on the profits from the sale of capital assets such as stocks and shares, land and buildings, businesses and valuable assets such as works of art. |
| Capital flight | The process whereby wealth holders deposit their funds and other assets offshore rather than in the banks of their country of residence. The result is that assets and income are not declared in the country in which a person resides. |
| Charitable trust | A trust established for purposes accepted by law as charitable. |
| Citizenship basis of taxation | Tax is charged on the worldwide income of all citizens of the state irrespective of whether they are resident or not in the territory during the period for which the taxes are levied. The most obvious example is the USA. |
| Company or corporation | An entity treated as a separate legal person from those who set it up, established under the rules of the country in which it is registered. |
| Controlled foreign corporation (CFC) | A subsidiary company or corporation registered in a tax haven or other territory where little or no tax is charged on the profit the subsidiary makes. Profits declared by the subsidiary can in some cases be subject to |

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| | tax in the country of residence of the parent company if it has the appropriate controlled foreign company legislation to enable it to do so. |
| Coordination centres | A special form of company with taxation advantages, often used to attract corporate headquarters to a country. Most notably found in Belgium, the Netherlands and Ireland. |
| Corporation tax | A tax on the profits made by limited liability companies and other similar entities in some countries, but otherwise usually being similar in application to income tax. |
| Currency transaction tax | A tax levied by a country that issues a currency on all the trades in that currency worldwide at very low rates e.g. 0.005 percent. Considered the most likely form of the Tobin Tax to be effective in practice. |
| Deferred tax | A fictional tax which only exists in company accounts and is never paid. Deferred tax does not, as such, exist. But the rules of accountancy generally require that income be matched with expenses. If an expense is recognised for tax purposes more quickly than it is for accounting purposes (which is common with much plant and equipment) this means that the tax cost for the years when this happens are understated. Conversely, when all the tax allowances have been used on the assets there might still be accounting charges to make and the tax cost would then be overstated. To balance this equation a notional tax charge called deferred tax is charged to the profit and loss account in the earlier years and put on the company's balance sheet as a liability. The liability is released as a credit to profit and loss account in the later years and supposedly over the life of the asset all should balance out. |
| Discretionary trusts | Most offshore trusts permit payments to be made at the discretion of the trustees, which means that the identity of beneficiaries can remain a secret. In practice, trustees normally follow a 'letter of wishes', provided by the settlor, instructing them whom they are to pay money to, when and how. |
| Domicile | The country identified as a person's natural home, even if that person has not been resident there for extensive periods of time. |
| Double tax relief | Tax relief given by the country in which the taxpayer resides for tax paid in another country on a source of income arising in that other country. |
| Double tax treaty | An agreement between two sovereign states or territories to ensure, as far as possible, that income arising in one and received in the other is taxed only once. Includes rules to define Residence and Source, and limits on Withholding Taxes. Also usually includes provisions for cooperation to prevent avoidance, especially information exchange. |
| Effective tax rate | The percentage of tax actually paid in relation to the total income of the person paying the tax. |
| Export processing zones | Artificial enclaves within states where the usual rules relating to taxation and regulation are suspended to create what are, in effect, tax havens within larger countries. |

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| Flags of convenience | The flag of a country with easy or lax maritime regulations and low fees and taxes, flown by ships registered in such countries, even though they have no substantial connection with the country. |
| Flat tax | A tax system in which as income rises the amount of tax paid remains constant in proportion to total income. Compare with progressive taxes. |
| General anti-avoidance principle | A legal principle that seeks to prevent a tax payer from obtaining the taxation benefit arising from any transaction if they undertook it solely or mainly to obtain a tax benefit. It does so by looking at the motivation of the taxpayer at the time of entering into the transaction, for which reason the concept of tax compliance is important. If the person was seeking to be tax compliant then they should probably keep the benefit they obtained from the transaction. If they were tax non-compliant then they should not. Compare with a general anti-avoidance rule. |
| General anti-avoidance rule | A general anti-avoidance rule seeks to tackle those who try to break the rules of taxation through the use of further rules. Rather than considering intention, it lays downs ways of interpreting series of events to determine whether the benefit of tax legislation can be given to the tax payer. Rules are invariably open to interpretation, however, hence a general anti-avoidance rule runs the risk of increasing the opportunity for abuse. |
| Gift tax | Taxes charged on gifts either during life or on death. The charges may be on the donor or on the cumulative value of gifts received by the recipient. |
| Hedging | A strategy intended to reduce investment risk using call options, put options, short selling or futures contracts. Often refers to taking a futures position that is equal and opposite from a position in the cash market. A hedge can be used to lock in existing profits. It is often claimed that hedging is best done offshore, but there is no evidence to support this assertion and most hedging expertise is onshore. |
| High net-worth individuals | Otherwise known as HNWIs (pronounced hen-wees). Generally categorised as individuals with more than US$1 million of liquid financial assets available for investment. |
| Holding companies | A company that either wholly owns or owns more than 50 percent of another company, the latter being called a subsidiary. An intermediate holding company is a holding company which has one or more subsidiaries but is itself owned by another company. The term 'ultimate holding company' refers to the one that is finally not controlled by another company. |
| Income tax | A tax charged upon the income of individuals. It can also be extended to companies. The tax is usually charged upon both earned income from employment and self employment and unearned income e.g. from investments and property. |
| Inheritance tax | A form of gift tax charged upon the estates of people upon their death. |
| International Business | A type of company offered by many offshore finance centres and tax havens, |

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| Corporations (IBC) | usually one which receives all or most of its income from abroad. IBCs usually pay an annual registration fee but are subject to minimal or zero tax rates. |
| Inversion | The act of a parent company whose headquarters are located within one jurisdiction switching registration with an offshore subsidiary they own to secure location within that offshore jurisdiction in order to secure a tax advantage. Mainly occurring in the USA. |
| Land value taxation | A tax on the rental value of a site, assessed as if it were undeveloped and unimproved - in other words, as if it were bare land. |
| Licence. (Licensing) | A contract for the use or property, often intellectual property such as a patent, copyright or trademark. If ownership of the property is transferred to a holding company located in a tax haven, the licence fee income paid to the licensor may be exempt from tax, as well as reducing the taxable profits of the operating company (often a subsidiary) which is the licensee. |
| Limited liability partnerships (LLP) | A partnership that provides its non-corporate members with limited liability. LLPs are frequently based offshore for tax avoidance purposes. |
| Loophole | A technicality that allows a person or business to avoid the scope of a law without directly violating that law. |
| Money-laundering | The process of 'cleaning' money from criminal or illicit activities to give it the appearance of originating from a legitimate source. |
| National insurance contributions | See social security contributions. |
| Offshore | Offshore relates to any jurisdiction (regardless of whether they are islands) which provides tax and regulatory privileges or advantages, generally to companies, trusts and bank account holders on condition that they do not conduct active business affairs within that jurisdiction. The term is very broad and normally includes 'onshore' tax havens such as Andorra, Lichtenstein, etc. |
| Offshore financial centre | Although most tax havens are Offshore Finance Centres (OFCs) the terms are not synonymous. Tax havens are defined by their offering low or minimal rates of tax to non-residents but may or may not host a range of financial services providers. An OFC actually hosts a functional financial services centre, including branches or subsidiaries of major international banks. States and microstates that host tax havens and OFCs dislike both terms, preferring to use the term International Finance Centres. |
| Partnerships | Any arrangement where two or more people agree to work together and share the resulting profits or losses. |
| Payroll taxes | See social security contributions. |
| Permanent Establishment | An office, factory, or branch of a company or other non-resident. Under Double tax treaties business profits are taxable at source if attributable to a Permanent Establishment. May include construction sites or oil platforms in |

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| | place for over 6 months. |
| Poll tax | A tax that levies the same sum on each person irrespective of their means to make payment. |
| Preferential tax treatment | A situation in which individuals or companies can negotiate their tax treatment in the state in which they have a tax liability. Pioneered by Switzerland in the 1920s, the arrangement is commonplace in the offshore world. |
| Private company | A company not quoted on a stock exchange. Shares cannot usually be sold without the consent of the company or its owners; in many countries little or no information need be disclosed on the activities of such companies even though their members enjoy the benefit of limited liability. |
| Profit laundering | The process of transferring profits from a territory in which they would be taxed to another in which there is either no tax or a lower tax rate. Mechanisms for achieving this include transfer-pricing, re-invoicing, licensing, thin capitalisation, corporate restructurings and inversions. |
| Progressive taxes | A tax system in which as income rises the amount of tax paid increases in proportion to the income as well as in absolute amount i.e. the percentage tax rate increases as the income rises. Also referred to as Graduation. Compare with flat and regressive taxes. |
| Public company | A company whose shares are quoted on a recognised stock exchange and are available to be bought and sold by anyone who wishes without consent being required from the company itself. Generally required to be more transparent than private companies. |
| Quoted company | See public company. |
| Race to the bottom | The downwards trend of tax rates and regulatory requirements on capital arising from competition between sovereign states to attract and retain investment. |
| Regressive taxes | A tax system in which as a person's income from all sources rises the amount of tax they pay reduces in proportion to their income even if it increases in absolute amount i.e. their percentage tax rate falls as their income goes up. Compare with progressive taxes and flat taxes. |
| Reinsurance | Some large companies decide not to insure their risks with the conventional insurance markets but instead set up their own insurance companies. When insurance companies do this it is called reinsurance. By setting up a captive or reinsurance company offshore, a tax deduction for the premiums paid is available in the country where the risk is and the premium is received offshore where there is little or no tax. This can, therefore, be viewed as another form of transfer-pricing. |
| Re-invoicing | Re-invoicing involves invoicing a sale to an agent, typically based in a tax haven or OFC, who subsequently sells on to the final purchaser. In practice the agent pays part of their mark up to the original vendor or to the purchaser, |

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| | usually to an offshore account. This is a widely used process for laundering profits to a tax haven. The process is dependent upon secrecy for its success. |
| Remittance basis | Concerns income earned outside the country of residence. The remittance basis says that tax is only due in the year when income is remitted to the country in which the tax payer is resident and not when it arises. Enables a person to avoid tax indefinitely in their country of residence provided it is kept and spent abroad. Compare with the arising basis. Both have relevance within the context of the residence basis of taxation. |
| Residence | For an individual, the person's settled or usual home; for simplicity a presumption may be applied based on a rule-of-thumb, such as presence within the country for six months or 183 days in any tax year. It may be possible to be resident in more than one country at one time (though double tax treaties aim to prevent this). Some individuals may also try to avoid being resident anywhere. For companies, residence is usually based on the place of incorporation but can also be where the central management and control of the company is located, if they are different. Tax haven companies formed for non resident owners are usually defined not to be resident in their country of incorporation. |
| Residence basis | Taxation of residents of a territory on all their worldwide income wherever it arises, usually with a credit for tax already paid overseas. The aim is to discourage residents from investing abroad in lower tax countries, by ensuring that income is taxed at the residence country rate if it is higher. Compare with source and unitary basis. |
| Ring-fencing | Different and preferential tax and regulatory treatment given by tax havens to companies and trusts owned by non-residents as contrasted to companies and trusts owned by residents. |
| Sales tax | Taxes on sales can be levied in two ways. Firstly, as a general sales tax (GST) added to the value of all sales with no allowance for claiming a rebate on tax paid. Secondly, as a value added tax (VAT) charged by businesses on sales and services but which allows businesses to claim credit from the government for any tax they are charged by other businesses. The burden of VAT therefore falls almost entirely on the ultimate consumers. GST and VAT are both regressive taxes since lower income households always spend a higher proportion of their income on consumption and therefore invariably spend a greater proportion of their income on this tax than do the better off. VAT is the most widely used form of sales tax. |
| Social security contributions | Payments made towards a fund maintained by government usually used to pay pension and unemployment benefits. Health benefits are sometimes covered as well. Social security contributions are generally considered to be taxes. |
| Source basis | Taxation of income in the territory where it is earned. Under double tax treaty rules, income attributable to a Permanent Establishment is taxable at source. Some countries tax only on a source basis, and consider income earned outside the country exempt; but some tax on the basis of both source and residence (subject to a foreign tax credit). Compare with residence and unitary bases. |

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| Special purpose vehicles | Any company, trust, LLP, partnership or other legal entity set up to achieve a particular purpose in the course of completing a transaction, or series of transactions, typically with the principal or sole intent of obtaining a tax advantage. |
| Stamp duty | A tax on the value of contracts. Usually charged on contractual dealings on shares and other stocks and securities and on dealings in land and property. |
| Subsidiary company | A company 50% or more owned by another company which is its parent company. |
| Tax arbitrage | The process by which a sophisticated tax payer plays off the tax systems of two different countries to obtain a tax benefit as a result. |
| Tax avoidance | The term given to the practice of seeking to minimise a tax bill without deliberate deception (which would be tax evasion or fraud).<br><br>The term is sometimes used to describe the practice of claiming allowances and reliefs clearly provided for in national tax law. It is, however, now generally agreed that this is not tax avoidance. If the law provides that no tax is due on a transaction then no tax can have been avoided by undertaking it. This practice is now generally seen as being tax compliance. So what the term tax avoidance now usually refers to is the practice of seeking to not pay tax contrary to the spirit of the law. This is also called aggressive tax avoidance.<br><br>Aggressive tax avoidance is the practice of seeking to minimise a tax bill by attempting to comply with the letter of the law whilst avoiding its purpose or spirit. It usually entails setting up artificial transactions or entities to re-characterise the nature, recipient or timing of payments. Where the entity is located or the transaction routed through another country, it is international avoidance. Special, complex schemes are often created purely for this purpose. Since avoidance often entails concealment of information and it is hard to prove intention or deliberate deception, the dividing line between avoidance and evasion is often unclear, and depends on the standards of responsibility of the professionals and specialist tax advisers. An avoidance scheme which is found to be invalid entails repayment of the taxes due plus penalties for lateness. |
| Tax base | The range of transactions that a country chooses to tax. A broad base includes a wide range of transactions. A narrow base includes relatively few transactions. |
| Tax competition | The pressure on governments to reduce taxes usually to attract investment, either by way of reduction in declared tax rates, or through the granting of special allowances and reliefs such as tax holidays or the use of export processing zones. Applies mainly to mobile activities or business, but the competition to attract investment may result in an overall decline of corporation tax rates and in the amounts of corporation tax paid, often resulting in an increased burden on individuals. |
| Tax compliance | A term that is acquiring a new use. It can mean payment of tax due without engaging in tax avoidance or evasion. It is used in contrast to the terms tax |

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| | avoidance and tax evasion. Tax compliance in this context is used as a test of a person's intention before they undertake a transaction. It asks whether the person is seeking to comply with the spirit of the legislation concerning the transaction into which they are entering. If they are, then it should be presumed their intent was to be legal. If they are seeking to comply with the letter but not the spirit of the law (and it is usually possible to determine this from the form the transaction takes) then it should be presumed their intent was to break that law, the onus of proof otherwise falling upon them. This test is then used in connection with a general anti avoidance principle to determine whether that principle should be applied to a transaction, or not. A person who has used an appropriate motive is 'tax compliant'. |
| Tax efficiency | A term used by tax professionals to suggest getting away with paying as little tax as possible. |
| Tax evasion | The illegal non payment or under-payment of taxes, usually by making a false declaration or no declaration to tax authorities; it entails criminal or civil legal penalties. |
| Tax haven | Any country or territory whose laws may be used to avoid or evade taxes which may be due in another country under that country's laws.<br>The Organisation for Economic Cooperation and Development defines tax havens as jurisdictions where:<br>1. Non-residents undertaking activities pay little or no tax;<br>2. There is no effective exchange of taxation information with other countries;<br>3. A lack of transparency is legally guaranteed to the organisations based there;<br>4. There is no requirement that local corporations owned by non-residents carry out any substantial domestic (local) activity. Indeed, such corporations may be prohibited from doing business in the jurisdiction in which they are incorporated. .<br>Not all of these criteria need to apply for a territory to be a haven, but a majority must. |
| Tax holidays | A period during which a company investing in a country does not have to pay tax under an agreement with its government. |
| Tax mitigation | A phrase used by tax professionals when describing the desire to pay as little tax as possible. |
| Tax non-compliant | A person who is not seeking to be tax compliant. |
| Tax planning | A term used in two ways. It can be used as another term for tax mitigation. When, however, tax legislation allows more than one possible treatment of a proposed transaction the term might legitimately be used for comparing various means of complying with taxation law. |
| Tax shelter | An arrangement protecting part or all of a person's income from taxation. May result from pressures on government or a desire to encourage some types of behaviour or activity, or may be a commercial or legal ruse, often artificial in nature, used to assist tax planning. |

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| Thin capitalisation | Financing a company with a high proportion of loans rather than shares. Used by Transnational Corporations to reduce the business profits of a subsidiary, since the interest on loans is usually allowed as a deduction, but dividends on shares are paid out of after-tax income. The interest is usually paid to another subsidiary of the transnational corporation located in a tax haven where no tax is paid upon its receipt, resulting in an overall reduction in the tax charge of the group of companies. |
| Tobin tax | The Tobin Tax or Currency Transaction Tax (CTT) is a proposed tax on the foreign exchange market named after the late James Tobin, the Nobel Prize winning economist, who proposed the idea. |
| Transfer-pricing | A transfer pricing arrangement occurs whenever two or more businesses (whether corporations or not) which are owned or controlled directly or indirectly by the same people trade with each other. The term transfer pricing is used because if the entities are owned in common they might not fix prices at a market rate but might instead fix them at a rate which achieves another purpose, such as tax saving. If a transfer price can be shown to be the same as the market price then it is always acceptable for tax. What are not acceptable for tax purposes are transfer prices that increase the cost or reduce the sales value in states which charge higher tax rates and increase the sales value or reduce the costs in states with lower tax rates. The difficulty for many corporations at a time when over 50% of world trade is within rather than between corporations is that there is no market price for many of the goods or services that they trade across national boundaries. This situation arises because they are never sold to third parties in the form in which they are transferred across national boundaries within the corporation. This gives rise to complex models in which attempts are made to allocate value to various stages within the supply chain within a company, which process is open to potential abuse. For this reason it is argued that such firms should be taxed on a unitary basis. |
| Transnational corporations (TNCs) | A corporation with subsidiaries or divisions in two or more nations. Also known as multinational corporation (MNC). |
| Trusts | A trust is formed whenever a person (the trust settlor) gives legal ownership of an asset (the trust property) to another person (the trustee) on condition that they apply the income and gains arising from that asset for the benefit of a third person (the beneficiary). Trusts can be established verbally but typically take written form. Trustees are frequently professional people or firms charging fees. Trusts are usually of one of three types:<br>• discretionary trust<br>• charitable trust<br>• interest in possession trust. |
| Trustee | A person who holds the legal title to assets held in a trust and administers it. |
| Trust beneficiary | Anyone who may obtain a benefit from a trust. A person who has the right to a benefit has an ‘interest in possession’; a discretionary beneficiary can get income or benefits only when and if the trustees decide to pay it to them. |

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| Trust settlor | The person who establishes a trust by gifting assets to it. |
| Unitary basis | Treating the income of related entities within a single firm or corporate group on a combined or consolidated basis, and applying a formula to apportion it for taxation by the different countries or territories from which it derives. Each may apply the rate of tax it wishes. An alternative to the residence and source bases of taxation. It has been used in federal countries such as the USA, applying an allocation formula based on a ratio of sales, employment costs and assets employed within each state. It has been opposed by tax authorities (and TNCs) because they consider that it would be too difficult to reach international agreement especially on the formula. However, taxation of highly integrated TNCs may in practice entail a formula-based allocation of profits, due to the difficulty of finding appropriate arm's length transfer prices. |
| Value Added Tax | Known as VAT. See sales tax |
| Wealth tax | A tax on a person's declared wealth, typically imposed annually at a very low rate. Once commonplace in Europe these are now rarely used since they are thought to encourage people to hide assets offshore. |
| Withholding tax | Tax deducted from a payment made to a person outside the country. Generally applied to investment income, such as interest, dividends, royalties and licence fees. |