

The Professionals: Dealing with the enablers of tax avoidance and financial crime



Few individuals have the skills or the time to navigate the complex world of tax, financial regulation and offshore accounts. Instead, multinationals and wealthy individuals rely on professionals to manage their affairs.

To service the offshore economy, a large industry of administrators, accountants, bankers, lawyers and lobbyists has developed, employing hundreds of thousands of people around the globe. These are the people that set up the secret bank accounts, create the anonymous companies and draw up the trust documents that fuel financial secrecy. Day in, day out, they dream up new complex tax avoidance schemes which

can be marketed to institutional investors, multinationals and banks. Then they lobby politicians to make sure that they can carry on what they are doing.

The firms involved span from familiar household names, such as HSBC and the big four accountancy firms, to smaller firms which only operate in tax havens.

Amongst these the most important are the offshore magic circle, a group of offshore lawyers based in tax havens.

Many of these firms have found themselves entangled in well publicised scandals. The Panama Papers exposed the activities of Mossack Fonseca, an offshore law firm headquartered in Panama. Swissleaks exposed how HSBC assisted their clients to evade taxes by stashing their money in their Swiss branch. And there have been many more, but despite these scandals, there has been little noticeable improvement in the conduct of these firms. Revelations about how even 'respectable' firms assist in the perpetration, or covering up of financial crime, tax avoidance and other illicit financial flows continue to emerge regularly.

Issues

One factor behind the increasingly aggressive nature of these firms has been the abandonment of the partnership model. In years gone by most professional services firms, from architects to accountants, were partnerships. Under this model all of the partners were financially



The big four

A particular role in the world of tax avoidance is played by the big four accountancy firms: PwC, KPMG, Deloitte, and EY. These companies have become giants, responsible for a wide range of corporate services. From auditing to management consulting to tax advice.

They have also become the voice of business. Conducting classic public relations activities like advising clients on upcoming changes to legislation and representing the interests of their clients to government. At the same time they market themselves to government as technocratic advisors.

In the tax world, it is not uncommon for a big four accountancy firm to be advising the government on tax legislation, and then advising their clients how to avoid it.

It should be of little surprise that tax simplification is not a high priority for professionals who make their money advising clients on highly complex tax systems.

Most importantly, the big four firms have dominated the international accounting standard setting process through the IASB and the FASB.

responsible for the firm and there was no limitation on their liability if things went wrong. If a firm was fined by a regulator, or sued by a client, it was the partners who had to dig into their pockets. This rather focused their mind on staying on the right side of the law.

Today almost all professional services have become limited liability partnerships. This new form of company is a relatively recent innovation. It gives the partnership limited liability. Partners no longer have collective responsibility, and individual partners have a limited financial exposure in the event things go wrong.

In 2014 PwC were given a \$25 million fine for whitewashing a financial statement at the request of the Bank of Tokyo-Mitsubishi. The statement implicated the bank in \$100 billion worth of money laundering

Regulation of professional services firms is notoriously weak. The conduct of firms and their employees is usually in the hands of a self regulatory body, made up of other professionals from the same industry. In the UK, there are 21 membership bodies responsible for regulating financial professionals. These bodies rarely take any action against members of their own profession.

External regulators and law enforcement agencies, even in highly developed financial sectors like London, are under resourced.

There simply are not enough regulators to effectively police the sector.

The situation is much worse in secrecy jurisdictions, where the sheer volume of business means that the effective regulation is an almost impossible task.

Solutions

Governments should take action to regulate the professional services industry.

Like with the banks, the answer to the problems caused by a concentration of power is to break up institutions. For that reason, it should be government policy to break up the big four. This would have the added benefit of encouraging competition in the market for professional services.

The audit function of these firms would be a good place to start. Auditors play a particularly important role in the regulation of our economies. They are external whistle-blowers with wide ranging powers to investigate the internal affairs of companies. Governments should insist, through legislation, that firms doing this important work are independent companies who do not provide other services on the side. This will make sure that the management of auditors is focused on auditing, and not on winning their next contract for other services.



\$1.9BN

Amount HSBC fined in 2012 for their part in facilitating money laundering in Mexico

The regulation of lobbyists and public affairs professionals is an important part of setting up a more responsible financial system. Governments should introduce regulations to ensure that lobbyists publish who their clients are, how much they spend and a record of their meetings with government officials. Firms engaging in lobbying and public affairs should not be able to act as advisors to government.

A former partner of PwC told a UK Parliamentary Committee that they would sell a tax avoidance scheme if it had more than a 25% chance of surviving a challenge from the tax authority.

Financial and legal services should not be allowed to be marketed into a country from offshore locations. Instead, firms marketing services should be compelled to operate through a significant presence in the jurisdiction from which they are soliciting funds. This includes having management and directors

resident in the country where they operate. This will make sure that professional services companies are not able to escape regulation by acting offshore.

Regulators must be well funded and independent from those regulated. The regulation of the conduct of financial professionals should be taken out of the hands of their colleagues, and given to a statutory body.

Rules setting out appropriate conduct by professionals should be drawn up by regulators, which should include rules designed to end the revolving door in the financial industry. Auditors should not be able to be employed by a company they have previously audited for several years after they leave the audit profession. Regulators should be prevented from immediately taking higher paid jobs in the private sector when they leave their regulator. There should be a prohibition against professionals promoting artificial schemes one of whose main purposes is to create a tax advantage.

Finally, when a tax professional advises on a transaction they know how much tax their client will save if their client follows their advice. Tax Justice Network supports the adoption of legislation that would require tax advisors to report to tax authorities their estimate of the amount of tax avoided through the advice they have provided to companies and individuals. This would allow tax authorities to

\$134BN

Combined revenues of the big four auditing firms in 2016.

risk assess taxpayers based on how aggressive the advice they have taken is. Furthermore, there should be statutory rules adopted in each jurisdiction that forces both taxpayers and tax advisers to report full details about uncertain tax positions as declared in the annual group accounts, as well as full details on all tax avoidance schemes employed.

We are an independent international network launched in 2003. We conduct high-level research, analysis and advocacy on international tax; on the international aspects of financial regulation; on the role of tax in society; and on the impacts of tax evasion, tax avoidance, tax 'competition' and tax havens. We seek to create understanding and debate, and to promote reform, especially in poorer countries. We are not aligned to any political parties.

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Company number 05327824

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