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Secret structures, hidden crimes:

Urgent steps to address hidden ownership, money laundering and tax evasion from developing countries

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Acronyms

AML	Anti-money laundering
AMLD	(EU) Anti-Money Laundering Directive
BVI	British Virgin Islands
CDD	Customer due diligence
CI	Covered institutions
CSO	Civil society organisation
DFI	Development Finance Institution
DFID	Department for International Development (UK)
DNFBP	Designated non-financial businesses and professions
EBF	European Banking Federation
EEA	European Economic Area
EFTA	European Free Trade Association
EIB	European Investment Bank
ERBD	European Bank for Reconstruction and Development
ETS	Emissions Trading Scheme
EU	European Union
FATCA	Foreign Account Tax Compliance Act
FATF	Financial Action Task Force
FDI	Foreign direct investment
FIU	Financial intelligence unit
FSA	Financial Services Authority (UK)
GDP	Gross domestic product
GNP	Gross national product
IFI	International financial institution
MDGs	Millennium Development Goals
MNC	Multinational corporation
OECD	Organisation for Economic Co-operation and Development
OT	Overseas Territories
PEPS	Politically exposed persons
SAR	Suspicious activity report
STAR	Stolen Asset Recovery initiative
TCSPs	Trust and company service providers
TJN	Tax Justice Network
UNCAC	UN Convention Against Corruption
UNCTAD	UN Conference on Trade and Development
UNODOC	United Nations Office on Drugs and Crime

Acknowledgements

This report has been written by Alex Marriage with support from Jesse Griffiths and many valuable contributions especially from Markus Meinzer (Tax Justice Network), Mark Herkenrath (Alliance Sud), Robert Palmer (Global Witness), Mathilde Dupré (CCFD-terre-Solidaire), Stephanie Fried (Ulu Foundation), Paul Marshall (Barrister, No5 Chambers), Antonio Tricarico (Re:Common), Chris Halburd (Environmental Law Service) and Rodrigo Fernandez (SOMO). Vicky Anning edited the report.

Published 2013

Introduction

Tax evasion poses an acute challenge to development in the South and to well-functioning states in general. Companies and other legal structures that are anonymously owned and controlled are a key mechanism of tax evasion which is seriously undermining many countries' development efforts. Securing more disclosure about who owns and controls these vehicles would not only help to prevent capital flight in future but may also bring trillions of dollars of offshore wealth back into the tax net. From 2000 to 2010, illicit financial flows deprived developing countries of US$5.86 trillion.[1] For people in the developing world, the consequences of tax evasion can be a matter of life and death. Its effects on the debt-distressed developed economies in Europe are also now widely known.

Tax evaders use many of the same techniques to move their assets as criminals involved in corruption, terrorist financing, nuclear proliferation and arms smuggling and many other abuses. It follows, therefore, that many of the measures taken to tackle these activities, especially regarding transparency, are the same.

This report sets out how opaque ownership structures are a key tool for money launderers and facilitate many crimes. However the report will mainly focus on the abuse of legal structures and hidden ownership for the purpose of tax evasion. Anti-money laundering frameworks provide an opportunity to secure transparency by revealing the identity of beneficial owners, meaning the real people who own and control bank accounts and legal structures such as companies, trusts and foundations.

Money laundering means concealing the fact that money has been obtained illegally, or in the case of tax evasion kept illegally. Anti-money laundering frameworks could also address tax evasion by wealthy individuals, and to a lesser extent by corporations, by deterring and punishing the companies and professionals who facilitate these activities.

Developed countries with large financial markets are particularly attractive destinations for tax evaders and money launderers and so they must put in place more effective measures to keep out this dirty money and to stop some individuals and institutions from profiting by facilitating crime in other countries.

The frameworks to address money laundering, including tax evasion, have largely been developed. The Financial Action Task Force (FATF), the global anti-money laundering body, released its latest set of recommendations in February 2012. However, countries around the world must now transpose these frameworks into law and cooperate with their neighbours to enforce them. The European Union and countries world-wide will respond to this and update their money laundering laws. However, political pressure is needed to make sure that essential improvements are made.

Anti-money laundering frameworks provide an opportunity to secure transparency by revealing the identity of beneficial owners, meaning the real people who own and control bank accounts and legal structures such as companies, trusts and foundations.

Chapter 1 will outline the scale of the problem of tax evasion and money laundering for both developed and developing countries. It will also discuss other ways that undisclosed beneficial ownership and money laundering are undermining development.

Chapter 2 will discuss the ways that tax evaders abuse legal structures (such as shell companies, trusts and foundations) and use them to conceal, invest and utilise their ill-gotten gains. The chapter will also explain how nominee shareholders, nominee company officers, trustees and corporate company officers can hide ownership and control, making it much harder for authorities to prevent and punish tax evasion and to recover the taxes they are owed.

Chapter 3 will survey laws regarding ownership disclosure, looking at the best and worst practices across a large sample of jurisdictions based around 70 of the jurisdictions studied by the Mapping Financial Secrecy project.[2] All measures to increase transparency around ownership and control of legal structures are useful for law enforcement and tax authorities. However, a truly effective solution would be public registries of the owners and controllers of legal structures. We will see that, for the most part, existing rules are woefully inadequate.

Chapter 4 will discuss why it is crucial to make sure tax crimes are clearly covered by anti-money laundering measures and sanctions. The main way of doing this is by ensuring that tax crimes are included as a predicate offence of money laundering, which means making it a criminal offence to help someone to conceal tax-evaded money. It is important that all foreign and domestic tax crimes should be covered. Many, but by no means all, major jurisdictions explicitly seek to prevent people from laundering the proceeds of tax crimes, by making these crimes a money laundering predicate offence. In February 2012, FATF explicitly incorporated tax crimes as a predicate offence in the global anti-money laundering standards. This recommendation should be transposed to deter and punish the companies and professionals who facilitate tax evasion, especially financial service providers and their supply chain, including bankers, accountants, lawyers and trust and company service providers (TCSPs) that provide services in relation to the establishment and management of opaque corporate structures, legal entities such as foundations, and legal arrangements such as trusts.[3, 4] Tax evaders and their accomplices are robbing their neighbours who face cuts in essential services and job losses or have to shoulder a higher tax burden against a backdrop of mounting national debt in both developing and developed countries.

Chapter 5 will look at implementation including compliance, enforcement and international cooperation, concluding that this is often inadequate. In many jurisdictions, the previous FATF standards, released in 2003, were poorly transposed. In others, notably some EU member states, they were transposed and then not properly enforced. Jurisdictions must actively make sure that companies and professionals comply with the regulations, through effective monitoring and credible sanctions. Currently some governments do not cooperate sufficiently with other countries to root out money laundering, especially as far as tax evasion is concerned. Jurisdictions must work together and share information. The levels of cross-border money laundering and tax evasion are so vast that isolated efforts will be far less effective. Poor implementation partly reflects the fact that FATF, and the mutual evaluations it carries

out, focuses mostly on whether national laws are in place and do not pay enough attention to whether this is leading to compliance, deterrence and prosecutions.

This section will also consider the reasons why some governments tolerate these activities. Some countries are simply reluctant to commit resources to anti-money laundering (AML), despite the fact that the benefits of curbing tax evasion and money laundering would outweigh the cost of putting effective preventative measures into practice. A second reason that enforcement has been lacklustre is because some developed countries, especially those with a powerful financial sector, turn a blind eye to the inflows stemming from tax evasion and other dirty money for short-term financial gain and because of vested interests. This section will argue that in the long term, this does not contribute to sustainable growth and will prove self-defeating for those governments.

Chapter 6 will discuss the various political opportunities to put better rules about beneficial ownership disclosure and identification into practice and improve anti-money laundering standards. The key political moment is the transposition of FATF standards in many jurisdictions around the globe. The EU Anti-Money Laundering Directive is one of the biggest opportunities. The EU is the largest actor in the world economy and hosts the world's largest financial sector. The EU is also one of the most attractive destinations for tax evaders to store their money, and the largest destination for foreign privately held assets (see Appendix 1). Creating barriers to dirty money entering the EU would make tax evasion far more difficult and risky and much less attractive, not least in the South. A strong EU directive will also put pressure on many tax havens that are closely linked to the EU.

Chapter 7 will set out recommendations for how this can be addressed.
These recommendations fall under three main categories. Firstly that financial service professionals should always be compelled to verify the identity of the beneficial owners on whose instructions, or on whose behalf, transactions are made. To facilitate this, governments should also collect and check this information then make it available to the public. Secondly tax crimes should be made a predicate offence of money laundering. Tax crimes must be broadly interpreted to include offences that take place in other jurisdictions, and to include all deliberate illegal underpayment of tax. Thirdly the implementation of the legislation needs to be improved and international cooperation must be increased especially regarding fiscal matters.

> Anti-money laundering frameworks could also address tax evasion by wealthy individuals, and to a lesser extent by corporations, by deterring and punishing the companies and professionals who facilitate these activities.

Chapter 1

The Problem – Tax evasion, money laundering and hidden beneficial ownership

Tax evasion costs developing countries billions of dollars every year. A Christian Aid study found that – even using a very conservative estimate – developing countries lose the equivalent of US$160 billion per year to tax evasion by multinational companies using false invoicing and blatant transfer mispricing.[5] If this US$160 billion was supplemented to developing countries budgets with allocation unchanged it would be enough to save the lives of 1000 children every day.[6] This far outweighs the US$62 billion of extra money needed to reach the Millennium Development Goals (MDGs), designed to eradicate extreme poverty and hunger around the globe by 2015.[7] Another report using different methodology shows that the EU loses an estimated 2-2.5% of gross domestic product (GDP) every year to fiscal fraud; this has led to cuts in public services, job losses and higher taxes.[8]

According to an Oxfam report, tax losses to developing countries due to tax evasion by individuals amount to another US$124 billion.[9] Over the past decades, tax evasion by individuals has led to the accumulation of US$21-32 trillion of untaxed offshore wealth, according to recent research by the Tax Justice Network (TJN).[10] About 25-30% of this (US$5.3–9.6 trillion) is from developing countries. According to TJN, developing countries probably lose as much every year from the missing tax on the interest this produces as they lose to new capital flight. If countries could start to recover this untaxed wealth, it could have an enormous development impact. Tax evasion is not a victimless crime.

Tax evasion and money laundering go hand in hand. Money laundering is the process of concealing the source of money obtained by illegal means. It can be easier to hide tax-evaded income because, unlike other criminal proceeds, the money generally comes from a legitimate source initially. This money only becomes illegal later on, when the full amount of tax due is not paid. This generally involves the tax payer concealing or under-declaring their income.

Hidden ownership facilitates tax evasion

Secrecy of ownership and control is a key mechanism that allows money laundering and keeps money untaxed. Much of the untaxed capital identified by TJN is held in the name of opaquely-owned legal structures or, more likely, by a web of such legal structures spanning various countries. Money can then be shifted between these different vehicles using phoney invoices and loans. Opaque ownership structures are also a way to conceal tax evaded and other criminal income when gaining access to the banking system. The top 50 private banks hold $12.1 trillion of transnationally invested assets, much of it for trusts and foundations.[11]

Opaque legal structures also frustrate other transparency initiatives such as international cooperation through tax information exchange. The veil of corporate secrecy means the taxpayer cannot be identified, so then it is harder to identify which country to share the information with and the information shared is much less useful. This was the experience in the EU after it implemented a form of automatic information exchange on savings income, with the European Savings Tax Directive. According to the European Commission:

"The second review of the Savings Directive confirmed the widespread use of untaxed offshore structures interposed between the payer and the ultimate beneficiary in order to obscure the actual beneficial ownership: 35% of the non-bank deposits in Member States (65% for deposits in Savings Agreements countries) are held by such structures located in offshore jurisdictions."[12]

The prevalence of automatic information exchange between tax authorities is increasing, and there is momentum towards a global standard. Developing countries will benefit from this, but only where individual taxpayers – whether corporations or people – can be accurately identified.

Secrecy of ownership makes "round tripping", a major means of evading tax in developing countries, possible. Round tripping involves sending money out of your country, then disguising your identity to pose as a foreign investor and bringing the money back to your country, receiving the tax breaks that are designed to attract foreign direct investment. This seems to explain why Mauritius is the biggest foreign direct investor in India (accounting for 43.6% of foreign direct investment).[13] Revealing beneficial ownership would help to stem future outflows of tax evaded revenues from developing countries, and also could help to bring back some of the money that has been lost over previous decades.

Anti-money laundering rules are a key opportunity to remove that secrecy through forcing disclosure of who really owns or controls bank accounts, companies, trusts and the like, known as beneficial ownership disclosure.

Most money launderers will try to access the banking sector: banks in developed countries are a particularly attractive destination. Tax evaders and other money launderers will generally want to access the banking system to make it feasible to spend, move and invest money on a large scale. To keep their money safe, individuals generally want to get it into established banks with a good reputation, in a country with strong property rights and a well regulated banking system. As banking systems can fail, these individuals will also aim to get their money into banks in a country with the capacity to bail out the banks. This means that much of the proceeds of tax evasion and other illicit capital flight from the global South ends up in the North. If access to banks in the EU and other developed markets was cut off, tax evaders and other criminals would find it much harder to find low-risk investments.

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Shell companies undermine climate change prevention measures – the case of Indonesian oil palm and paper and pulp companies by Ulu Foundation[29]

EU member states have played a leading role in efforts to combat global climate change. This has included supporting steps taken by forest-rich countries such as Indonesia to prevent deforestation and forest degradation. However, these efforts may well be undermined by the services provided by EU-linked secrecy jurisdictions, which allow the laundering of proceeds from forest destruction, illegal logging and tax dodging using opaque legal structures. Shell companies have already been abused to undermine the EU's controversial Emission Trading System (ETS).[30 31] In 2009, the European law enforcement agency Europol estimated that VAT fraud linked to the EU ETS carbon credits was costing the EU €5 billion in lost taxes. A year later Rob Wainwright, Director of Europol, said: *"Organised VAT fraud remains a significant criminal activity in Europe. It is responsible for draining huge resources from central government revenues and undermining the objective of transforming Europe into a competitive and greener economy."*[32]

Indonesia has the third largest tropical forest area on earth, yet is the largest emitter of CO_2 from deforestation and "forest land use change". In 2009, Indonesian President Yudhoyono announced that Indonesia would cut greenhouse gas emissions by 26% by 2020 compared to the "business as usual" level. If sufficient international support were available, levels could be cut by up to 41%. This has served to place Indonesia at the heart of international climate finance efforts designed to provide support for a reduction in deforestation rates.

The World Bank has found that "forest loss and forest crime dominate the [Indonesian forestry] sector" and that *"Indonesia is losing forests at a remarkable rate, one of the fastest in the world"*. The Bank concluded that "industrial timber demand exceeds sustainable supply."[33] Illegal logging in Indonesia represents a substantial threat to national and international efforts to prevent and mitigate climate change.

Illegal logging is not just something that happens in the forest. According to the international police organisation INTERPOL, it is a profit-motivated global business that is likely *"best addressed with financial tools allowing the identification and seizure of assets."*[34]

"Timber is a commodity no different from narcotics, weapons, vehicles, or any other internationally traded goods that can generate profit. The illegal trade in timber is business-like in its structure with both provider and buyer companies."[35]

Two of the most significant drivers of deforestation and forest degradation in Indonesia are the paper and pulp sectors, as well as the palm oil sector. Yet, despite spending or pledging substantial sums to protect forests as part of efforts to reduce climate change, EU-linked secrecy jurisdictions provide anonymity for companies involved in Indonesia's forest sector, making it difficult to trace the proceeds of sophisticated illegal logging and tax dodging operations, including any that may allegedly be associated with the primary drivers of deforestation, the paper and pulp industry and the oil palm sector. The British Virgin Islands, Cayman Islands, Bermuda, The Netherlands, and to a small extent Luxembourg and Cyprus, appear to be the primary EU-linked jurisdictions used by Indonesian forest sector companies.

Oil palm expansion has had significant environmental and social impacts in Indonesia over the past decades. The Dutch not-for-profit organisation Aidenvironment estimates that, between 1996 and 2007, deforestation related to oil palm plantation development in Indonesia amounted to 4.2 million hectares. It is estimated that forest degradation during the same period amounted to as much as 5.4 million hectares.[36] Research by non-governmental organisations (NGOs) and other sources have alleged various illegal practices in the Indonesian palm oil industry, including:[37]

- land clearing without the necessary governmental approvals and permits;
- destruction of the natural habitat of endangered species, including the orangutan, the Sumatran tiger, the Sumatran elephant, the clouded leopard and the tapir;
- forest fires as a result of illegal burning;
- drainage of tropical peat lands;
- social conflicts with local communities, especially related to free, prior and informed consent.

In 2010, Indonesia's new anti-money laundering statute (Law 8, 2010) listed forestry and environmental crimes, as well as corruption, bribery, "criminal activities....in the tax field" and other crimes as predicate offences of money laundering. This means under the new statute, efforts to transfer the proceeds of such crimes overseas, or to change, hide or disguise the form of such proceeds, would be deemed as money laundering.

Major forest-related conglomerates active in Indonesia's paper and pulp and oil palm sectors often use complex structures with layers of "shell companies" domiciled in secrecy jurisdictions, including EU member states such as the Netherlands, or jurisdictions closely linked to the EU, such as the Cayman Islands and the British Virgin Islands (BVI).[38]

According to a recent INTERPOL report, *"some estimates suggest that the Indonesian government is losing one to two billion US dollars per annum in unpaid taxes and charges, others suggest that Indonesia loses $125 million a year due to the activities of just 18 illegal logging syndicates."*[39]

Ulu Foundation recommends that:

Given the high-risk nature of Indonesia's forest sector, all jurisdictions that provide domiciles for shell companies owned by forest conglomerates active in Indonesia should ensure the relevant professionals in their territory conduct robust in-depth due diligence in order to ensure that they are not facilitating the flow of criminal proceeds potentially associated with illegal or destructive logging, or tax crimes including illegal transfer pricing.

Simple due diligence steps, including requiring any forest-based company operating in Indonesia – especially in the paper and pulp, oil palm and logging sectors – to document publicly and post online for easy public scrutiny, independently verified and internationally credible proof that the supply chain for their timber is entirely legal. This should be required prior to providing incorporation or financial services to forest-based companies. Additionally, jurisdictions providing services for Indonesia-linked forestry companies could communicate with Indonesia's Financial Intelligence Unit.

Hidden ownership facilitates corruption and crime

The United Nations Office on Drugs and Crime (UNODOC) examined all existing studies, and estimated the total value of money laundering to be around US$2.1 trillion in 2009, which is equivalent to 3.6% of global GDP.

Beneficial ownership transparency would help to address illicit capital flight, which has been estimated to cost developing countries US$859 billion in 2010. These flows comprise proceeds of corruption, crime and tax evasion. The above estimates do not, however, capture losses resulting from the mispricing of cross-border services or the mispricing of merchandise trade via false invoicing or smuggling.[14] The long-term trend has been towards rising levels of illicit financial flows.

The United Nations Office on Drugs and Crime (UNODOC) examined all existing studies, and estimated the total value of money laundering to be around US$2.1 trillion in 2009, which is equivalent to 3.6% of global GDP.[15] Russia provides a particularly stark example, according to Ruslan Milchenko, a former Moscow tax official who now heads up Russian anti-corruption organisation the Federal Information Centre for Analysis and Security.

"Official figures from the Central Bank show that in 2011, 250,000 Russian firms paid no taxes and submitted annual reports reporting no activities. Simultaneously, the Central Bank found that more than 4 trillion rubles (US$130 billion) had been processed through accounts of these inactive companies.... This is almost half of the budget of Russia in 2011... And that is just the official accounting. Unofficially we believe that of the 5 million firms registered in Russia, 3 million or even more are phantom companies, which don't conduct any real commercial activities and are aimed only on money-laundering."[16]

Global Witness has produced a number of case studies about politicians and officials in developing countries acquiring vast amounts through corruption and then laundering the money abroad.[17, 18] The Grand Corruption Database lists 150 cases involving hidden ownership of a corporate vehicle.[19] This arose out of the World Bank and United Nations Office on Drugs and Crime (UNODOC) Stolen Asset Recovery (STAR) initiative as practitioners in the field of asset recovery were constantly encountering hidden beneficial ownership in their investigations. Often this secrecy formed an insurmountable barrier to returning the assets to government coffers.

Illicit outflows are a major explanation for developing country debt. Researchers James Boyce and Leonce Ndikumana found that sub-Saharan Africa has lost US$700 billion to illicit capital flight since 1970, which dwarfs its outstanding debt of US$175 billion. They wrote:

"For every dollar of foreign borrowing, on average more than 50 cents leaves the borrower country in the same year. This tight relationship suggests that Africa's public external debts and private external assets are connected by a financial revolving door."[20]

As well as being used to hide the proceeds of earlier graft, opaque legal structures are often used in initial corruption scams. Legal structures with undisclosed beneficial ownership can also be used to corrupt government tendering processes and the selling of concessions. In the example of procurement, a bidding company sometimes turns out to be a shell company controlled by an official who wins the tender for an inflated price, then pays a real sub-contractor to do the work for a much lower price. When selling natural resource extraction rights, a similar scam can be carried out. For example, the Democratic Republic of Congo's state-owned mining company, Gécamines, sold stakes in four large mines to offshore companies with hidden ownership, at prices well below their market value. Some of these stakes were then sold to large UK-listed companies at a much higher price. It is unclear who profited, but the Congolese government and people clearly lost out. Similarly, stakes in Nigerian oil blocks ended up being held by obscure companies. Some of these companies seem to be linked to individuals known in money laundering terms as politically exposed persons (PEPS): a senator and a businessman close to the country's then head of state.[21] In the extractive industries, opaque ownership can be used to get around the country-by-country and project-by-project reporting requirements set forth in recent US legislation, the Dodd Frank Act, which is likely to be adopted by the EU.

Hidden ownership masks accountability for human rights or environmental violations

When a human rights violation has taken place, the people affected can find it difficult to hold anyone to account. This includes taking legal action, as this is much more difficult to do if you cannot identify the parent company or management further up in the chain of ownership. The European Coalition for Corporate Justice has recommended that reporting obligations of companies should include: *"Data about the structure of the enterprise, its sphere of responsibility and its decision making process"*.[22] A court case alleging environmental damage brought against Shell by people from the Niger Delta highlights the importance of corporate accountability regarding human rights.[23] However, anonymity around ownership is part of a broader set of problems, around the corporate form and limited liability, including difficulties in holding parent companies responsible once they have been identified. Often liability for abuses can be limited to the national subsidiary, which is likely to have shifted profits out of the country already and therefore can be wound down rather than paying out compensation. The UN Guiding Principles on Business and Human Rights attempt to address these problems. UN Special Representative John Ruggie stated:

"far greater clarity is needed regarding the responsibility of corporate parents and groups for the purposes of remedy."[24]

In a later report, Ruggie made clear that, *"These guiding principles apply to all*

Local procurement

International aid effectiveness agreements state that country systems should be used to coordinate procurement for aid projects. Governments might then choose to procure these goods locally, to boost their own productive capacities, expertise, employment and to keep the money circulating in the local economy. In order to do this, it would help to establish that the beneficial owner of a contracting firm is actually a local, and that it is not a subsidiary of a multinational parent company.[40]

Development Finance Institutions (DFIs) and Money-laundering

An increasing amount of finance is provided to the private sector in developing countries by donor governments and multilateral institutions. In 2010, International Financial Institutions (IFIs) channelled $40 billion to the private sector in the South; this is estimated to rise to more than $100 billion in 2015.[41] Civil society organisations (CSOs) have raised serious concerns about accountability when Development Finance Institutions (DFIs) channel this aid through financial intermediaries. The European Investment Bank (EIB) and UK DFI CDC (formerly the Commonwealth Development Corporation), which is wholly owned by the UK's Department for International Development (DFID), were recently embroiled in a money laundering case that exemplifies this problem. They invested in a private equity firm that subsequently invested in Nigerian companies. These companies were reportedly "fronts"[42] for the laundering of money that had allegedly been obtained corruptly by the former Governor of Nigeria's oil rich Delta State, James Ibori. When whistleblower Dotun Oloko raised his concerns with DFID, his identity was revealed to the private equity firm in question, leading to intimidation that forced him to leave his native Nigeria fearing for his family's safety. DFID have since apologised and said it was an accident.[43] Eventually, in March 2012, James Ibori was tried for corruption. He was found to have used British banks to launder US$250 million looted from state coffers. At around the time, the questionable investments of other DFIs came to light.[44, 45] It seems that both the European Investment Bank (EIB) and CDC unwittingly invested in opaque shell companies that Ibori's associates controlled.

The fact that DFIs operate in a similar way to investment banks means they should be required to comply with the same AML standards and carry out Customer Due Diligence (CDD). They ought to then follow this down their supply chain to financial intermediaries that they use. It is not only important that DFIs carry out CDD, but also that they should be subjected to regulatory oversight for anti-money laundering compliance. It is not clear whether this is the case in many circumstances. It is a matter of concern that, even though the private equity firm is now under criminal investigations by the European Fraud Office (OLAF) and the Nigerian Economic and Financial Crimes Commission (EFCC) with regard to its Ibori linked investments, the DFI investors are still continuing to fulfil their commitments to the fund. These DFIs are now effectively beneficiaries from Ibori's corruption. This example shows that the EIB and CDC failed in their ongoing duty to monitor the activities of this fund manager. In the case of the EIB, there is the surreal situation whereby the bank has continued to back a fund manager that it has referred to OLAF on the basis of its own Inspector General concluding that fraud is likely to have occurred in the fund. It would therefore appear that DFIs do not have systems in place to monitor their fund managers effectively. As such, DFIs should avoid channelling their money through private equity firms,

states and to all business enterprises, both transnational and others, regardless of their size, sector, location and ownership structure." He adds, *"States should take appropriate steps to ensure the effectiveness of domestic judicial mechanisms when addressing business-related human rights abuse, including considering ways to reduce legal, practical and other relevant barriers that could lead to a denial of access to remedy."*[25] Greater beneficial ownership transparency would be a useful part of a package of measures to ensure corporate accountability for human rights and environmental abuses.

> Legal structures with undisclosed beneficial ownership can also be used to corrupt government tendering processes and the selling of concessions.

Use of complex structures to circumvent financial regulation

Many banks used complex and even illegal structures to hide losses before the financial crisis. One example is UK Bank Northern Rock, which used an investment vehicle registered in Guernsey to hide its losses (which would later be bailed out by taxpayers). The bank registered the beneficial owner as a Down's syndrome charity, without the knowledge of the charity's staff. This clearly raises questions as to whether the appropriate checks had been properly carried out. The example also supports the argument for public registries so people and institutions can know if their identity is being abused.[26] Strengthening transparency rules regarding beneficial ownership of legal structures can help prevent such destabilising activities being carried out at the expense of the majority of citizens and the broader economy.

Tax avoidance

Greater organisational transparency and beneficial ownership disclosure would make it easier to understand aggressive tax planning and avoidance schemes. Often tax avoidance schemes exploit the legal loopholes that can exist when transactions take place between jurisdictions with different rules. Many of these schemes exist in a contested grey area between what is legal and illegal. Therefore it is important to have absolute transparency about how such schemes work. The majority of tax dodging by multinationals exists in this grey area. It is legal or semi-legal but it is highly immoral. Transparency around beneficial ownership of legal structures would have the additional benefit of helping tax authorities to better understand aggressive tax avoidance schemes, amend tax laws and uphold the original intention of those laws.

One telling example of the impact of tax avoidance in developing countries is ActionAid's case study of the UK brewing company SAB Miller. ActionAid found that, if the tax loopholes the brewer used could be closed, the additional tax revenues in Africa from SAB Miller alone would likely allow another 250,000 children to go to school. In this instance, sufficient information was publically available to identify the ownership structure and the avoidance schemes used. This information allowed an informed public debate about tax policy, which, in many

Through the abuse of trusts and similar legal constructs, a person can legally dissociate themselves from ownership and therefore from taxes and other obligations.

cases, would not be possible because of opaque ownership structures.[27] Together with automatic tax information exchange, beneficial ownership transparency would not only lead to the detection of illegal tax evasion, but it would also help to uncover and repudiate legal forms of tax avoidance by multinational corporations (MNCs). Greater transparency would allow civil society and citizens to participate in a well-informed debate about appropriate tax laws.

Slicing and dicing ownership in complex legal structures is also a method of aggressive tax avoidance. A trust normally has three components: settlor(s) who put the money in; trustee(s) who are responsible for looking after the money and transferring it to the intended beneficiary or using it as instructed; and the beneficiary. Through the abuse of trusts and similar legal constructs, a person can legally dissociate themselves from ownership and therefore from taxes and other obligations, whilst retaining the option of the trust transferring the asset or income back to themselves later on. This is because the trustee has discretion to transfer the money back to the settlor. Often this is ensured in an agreement known as a letter of wishes where the trustee agrees to transfer the money back to the beneficiary. For this reason, the arrangement should not have legal weight unless the settlor, the trustee and any letter of wishes linked to the trust is registered with the authorities.

The same applies for similar constructions such as foundations and *Anstalten* a form of company with one secret shareholder which is permitted in Liechtenstein. For example, *Ermessensstiftungen* (discretionary foundations) based in Liechtenstein have been identified as a major challenge to AML compliance in Switzerland. *Ermessensstiftungen* do not have predetermined beneficiaries, but distribute their earnings on an ad hoc basis guided by the principles laid down in the original foundation charter. Swiss banks can accept money from these vehicles without having to identify owners and controllers because, in a legal sense, there is no beneficial owner.

In Liechtenstein, it is legal to establish a hidden agreement between the founder and the board, which gives the founder effective control over the foundation. The Swiss Bankers' Association has attempted to identify ways to distinguish "legitimate" from "illegitimate" or "fake" discretionary foundations and found the task almost impossible. The proposed revision of the European Savings Tax Directive would approach this issue in the following way: if the beneficiary will not reveal themselves the Directive obliges the effective manager of entities and legal arrangements within 44 EUSD jurisdictions to apply the savings tax. This would make the beneficial owner choose between paying the withholding tax or revealing their identity, even if they were from a third country, in the latter case the tax authority then might be obliged to share this information with their home country.[28]

Having discussed the damage caused by money laundering and hidden ownership, the next chapter will discuss in more detail how legal structures are abused and how this could be prevented.

The arrangement should not have legal weight unless the settlor, the trustee and any letter of wishes linked to the trust is registered with the authorities. The same applies for similar constructions.

Chapter 2

How are companies, trusts and other vehicles abused and what can be done about it?

Trust and Company Service Providers

The challenges posed by unaccountable owners and shell companies are illustrated by rogue Trust and Company Service Providers (TCSPs). TSCPs provide the following three key roles. First, they can be used to set up companies, equivalent legal persons (i.e. foundations), and legal arrangements such as trusts. Second, they can play a role in running these vehicles, for example, acting as trustees or as company officers. Third, they can provide an address and mailbox for the company, foundation or trust.[46] Often TCSP services are provided by lawyers or accountants, although some TCSPs are large companies specialising solely in these areas. These functions can all be legitimate and may be morally defensible, but under current rules they can also be corrosive for three reasons because they can:

1. Help provide opacity or even deception.
2. Set up shell companies and other opaque vehicles in various jurisdictions to take advantage of laxer anti-money laundering standards.
3. Set up structures that render the owners unaccountable for their actions and obligations, including to tax authorities, creditors and the victims of human rights violations.

Setting up and selling legal structures without adequate customer checks

Companies can be set up and sold on by a TCSP without them conducting any due diligence. TCSPs can also set up such opaque constructions as trusts and foundations, *Anstalten* and other legal constructs. These vehicles can then easily be used as fronts for money laundering.

FATF recommended that trust and company service providers should be one of the covered institutions (CIs), meaning the organisations and professions required to carry out customer due diligence (CDD) under anti-money laundering rules. The EU has already transposed this recommendation in the Third Anti-Money Laundering Directive (AMLD). However, there are significant problems with the interpretation of this in the UK, which suggests this provision may not be working in other member states either. In the, UK TCSPs are regulated by the tax authority. They do not have to carry out AML checks if they are setting up a company but have no further relationship with the customer. This is because setting up a company is viewed as a one-off event that would almost always be below the €15,000 transaction threshold above which AML CDD needs to be carried out. This means the beneficial owner does not need to be identified and there are no checks later to see if unusually large amounts of money start flowing through the company.

Global Witness's investigation into alleged money laundering in Kyrgyzstan found companies were set up by a UK company service provider but with nominee shareholders and directors in the Seychelles, Russia and Panama. The British TCSP that registered the company therefore did not have a legal obligation to do the checks: this was left to the nominees. It is not clear what checks the nominees carried out on these companies, and no checks were carried out within the EU. TCSPs should be required to carry out due diligence on their customers no matter the length of their relationship and should not be allowed to rely on checks in other jurisdictions.

However, there is a further loophole in the UK because firms can be incorporated with the UK corporate registry Companies House directly. Companies House does not carry out any customer due diligence itself. As part of the update of their AML standards, jurisdictions should require corporate registries such as Companies House to take an active role in anti-money laundering enforcement and to carry out due diligence to accurately establish beneficial ownership information. This should then be published online and should be available free of charge. The information can then be checked by CIs and investigators. Those setting up new companies could be asked to fill out an online form, which could be published online after incorporation. To complete the registration process, owners and company officers should be required to visit the registry with passports for identification. Company registration would become slightly more expensive, but companies could meet these costs, which would be a reasonable price to pay for limited liability.

As part of the update of their AML standards, jurisdictions should require corporate registries such as Companies House to take an active role in anti-money laundering enforcement and to carry out due diligence to accurately establish beneficial ownership information.

Lonestar used a holding company in Belgium to sell its stake in the Korean Exchange Bank, as Belgium does not claim capital gains on this kind of sale. Lonestar argue that this exempts them from US$342 million of capital gains tax in Korea. The Korean authorities argue that the holding company is merely a mailbox and the matter has now gone for international arbitration

Use of mailbox companies in laxer jurisdictions can help money launderers

TCSPs are currently allowed to set up and provide an address for firms with no real operations in a jurisdiction that can then be used to take advantage of its laws. One such form of "regulatory arbitrage" is the hunt for extremely low tax rates. The NGO CCFD Terre-Solidaire found that overall 21% of the subsidiaries of the 50 largest companies in Europe were located offshore (47 of the companies had offshore subsidiaries for the remaining three the data was not available).[47] An ActionAid investigation into the largest 100 companies on the UK stock exchange found that 98 had subsidiaries in tax havens and 38% of their subsidiaries were offshore. Retailers Sainsbury's and Morrisions do not have a single shop outside the UK yet have tax haven subsidiaries.[48]

One form of tax-related regulatory arbitrage is treaty shopping. Parent companies set up a mailbox company to give themselves a presence in a jurisdiction with a favourable double taxation treaty. For example, South Korea is in a dispute with the US-owned private equity firm Lonestar. In 2003, Lonestar used a holding company in Belgium to sell its stake in the Korean Exchange Bank, as Belgium does not claim capital gains on this kind of sale. Lonestar argue that this exempts them from US$342 million of capital gains tax in Korea. The Korean authorities argue that the holding company is merely a mailbox and the matter has now gone for international arbitration after a protracted dispute.[49] Treaty shopping is a problem that goes beyond taxation, according to The Centre for Research on Multinational Corporations (SOMO). *"Multinational corporations (MNCs) investing abroad have been using Dutch bilateral investment treaties (BITs) to sue host country governments for over 100 billion dollars for alleged damages to the profitability of their investments."* Often the countries in question are in the developing world.[50]

Mailbox companies allow companies to locate in a jurisdiction with laws in place to protect financial secrecy or with weak requirements to disclose ownership information. TSCPs provide the location for the infamous nameplate or mailbox companies. This practice has led to a building in the Cayman Islands where 18,000 US companies are based. US President Barack Obama called it *"either the biggest building in the world or the biggest tax scam in the world. I think the American people know which it is."*[51] Although he could have equally cited examples of the same thing within the USA, the premier locations for shell companies, there are various examples of premises that have squeezed in an impressive number of companies per square foot. One such building in Wyoming hosts more than 2,000 companies. There have been 12 civil lawsuits against these companies alleging unpaid taxes, fraud and trademark infringement since 2007. State and federal tax authorities have been pursuing more than US$300,000 in unpaid taxes owed by companies based there.[52] It is much easier to set up a front company if that company does not need to have any real operations. FATF has recommended that CIs identify if there is a separate address for the main place of business, if this is different from the official addresses to capture mailbox companies. This requirement would be made much easier if required as part of the registration process. Companies should only be allowed to incorporate in a jurisdiction if they have meaningful economic substance within that jurisdiction (for example, staff and sales). Holding companies should be required to operate in one of the countries where their subsidiaries carry out substantial operations.

An example from Latvia

Two Latvian TCSPs (nominally) presided over companies involved in many criminal activities. The majority of the alleged malpractice are believed to involve tax evasion from Ukraine, but they are also accused of presiding over companies involved in defrauding governments and investors, and even arms smuggling.[57] No one is saying the formation agents were engaged in these crimes, but they served as directors and shareholders for hundreds of companies in the British Virgin Islands, Panama, Cyprus, New Zealand, the USA, the UK and Ireland. The companies they were nominally in control of were used as shareholders of many other companies and as corporate company officers.

It is much easier to set up a front company if that company does not need to have any real operations.

Currently nominees' identities can also be sold on an industrial scale. Nominee shareholders can sign an agreement leaving profits to the real beneficial owners. After the initial transaction, nominee company officers often take no further role in the management of the company.

Nominees and corporate company officers are a means of hiding beneficial ownership

It is legal for nominees to charge a fee to record their name and pose as shareholders or company officers on official paperwork, obscuring the real beneficial owner(s). The nominee is then a legal owner or controller: one of the reasons the legal owners might be different from the beneficial owner. Sometimes nominees are also close associates who take a more active role in running the vehicle but are still acting on the instructions of the real beneficial owner. It is difficult to regulate this. However, currently nominees' identities can also be sold on an industrial scale. Nominee shareholders can sign an agreement leaving profits to the real beneficial owners. After the initial transaction, nominee company officers often take no further role in the management of the company. This advert shows how the real beneficial owners can be assured of control:

"With this package [Price tag £350] we will provide a private individual, who is a citizen of the EU, as the nominee director for your company. We will also provide a dully [sic] signed general power of attorney empowering you to run the business, and manage the company's activities, and you will take full legal and financial responsibility for the running of the company. This package also includes a pre-signed, undated letter of resignation from the nominee director."[53]

Why is this practice allowed? The Organisation for Economic Co-operation and Development (OECD) provides the following rationale:

"Nominee shareholders are utilised in most jurisdictions. With respect to publicly traded shares, nominees (e.g. registering shares in the names of stockbrokers) are commonly, and legitimately, used to facilitate the clearance and settlement of trades. The rationale for using nominee shareholders in other contexts, however, is less persuasive and may lead to abuse." [54]

This quote is from an OECD report suggesting that TCSPs and fiduciaries should be licensed (although weakly suggesting this is only necessary in a limited set of circumstances). In fact, this should always be the case, and TSCPs that fail to furnish authorities with beneficial ownership information during investigations or random checks should lose their licenses. The Global Witness report Grave Secrecy shows how these nominee arrangements frustrate investigations by obscuring who is really behind the companies and how the companies which nominees notionally oversee can engage in extremely dubious activities, in this case moving hundreds of millions of dollars of suspicious funds from Kyrgyzstan. Due to the laxity of its corporate registration rules, the UK is considered a secrecy jurisdiction by TJN, and the same applies to the USA.[55] The following passage highlights the absurdity of the UK's current system and its openness to abuse:

"To summarise, five UK-registered companies shared three nominee directors in the Seychelles, and had Russian owners who 'held' their annual meetings on the same days at the same location in London, despite one of them being dead. Three of the companies – Mediton, Novelta and Nedox – were also all dissolved on the same day. These facts taken together suggest that the same individual or individuals are behind these companies, individuals whose identities remain hidden. The above information does not suggest that the service providers and nominees who fronted for the real beneficial owners of these five companies have done anything illegal. Neither does it prove illegal behaviour by the real beneficial owners…"[56]

Nominees represent a key money laundering risk and should be flagged as such. People would be deterred from becoming nominee company officers if they expected to be held to account for the company's actions. For example, UK law states that nominees have the same responsibilities as any other director and are liable for the company's wrongdoing, but in reality this is rarely, if ever, enforced. In many places it is not necessary to be a human being (a natural person) to act as a company officer, such as a director because as a 'legal person' a company is allowed to fulfil this role, this is known as a corporate company officer, it provides another way to conceal information about the beneficial owners.

The Latvian case shows the dangerous loopholes created by corporate company officers and nominees. By allowing nominees and corporate company officers to be registered as corporate officers, a state is accepting legal ownership information that does not have to correspond with beneficial ownership information. Having considered some of the means that can be used to evade tax and launder money, and considering the fact that tax evaders and money launderers will often spread themselves across multiple jurisdictions, partly to take advantage of particular laws, the next chapter will look at the measures that jurisdictions are putting in place to prevent this kind of activity or sometimes to encourage it.

Companies should only be allowed to incorporate in a jurisdiction if they have meaningful economic substance within that jurisdiction (for example, staff and sales). Holding companies should be required to operate in one of the countries where their subsidiaries carry out substantial operations.

Chapter 3

Current standards around beneficial ownership identification and disclosure

Know your customer rules: beneficial owners' identities should always be verified when establishing a business relationship

There are two levels to beneficial ownership transparency.

1. **Are banks and professionals checking beneficial ownership information when setting up legal structures, bank accounts or transactions that could be used for money laundering?**

2. **A) What is the quality and detail of ownership information on public record?**

   B) Who can access it?

Money laundering has been criminalised in most places. Anti-money laundering standards create legal obligations for professionals and companies in sectors involved in making large financial transactions. Known as CIs, these professionals and companies are usually required to look out for suspected money laundering and report it to the authorities. AML rules make it harder for individuals to cross borders with large amounts of cash. 52 jurisdictions monitor transnational flows of currency and other instruments, but 18 make no such requirements. These include some significant tax havens such as Luxembourg, Switzerland and Mauritius (see Appendix 2 for full list). For this and other practical reasons, most money will be shifted across borders by electronic bank transfer. Anti-money laundering compliance was mainly designed with the banking sector in mind. This is reflected in FATF terminology, which refers to financial institutions and Designated Non-financial Businesses and Professions (DNFBPs). Accountants, lawyers and trust and company service providers (TCSPs) are the most crucial professions but dealers in high value assets, such as real estate, jewels and art also have a responsibility. If professionals suspect that money has been acquired illegally, they are required to reject the business and report it to the relevant authorities generally through a "Suspicious Activity Report (SAR)". In 69 out of 70 jurisdictions surveyed banks are required by law or regulation to record suspicious or unusual transactions to designated authorities in SARs. The exception is Liberia, where reporting is "permissible". Anti-money laundering rules make it harder for banks to just accept cash or deposits from suspect individuals. Instead, money launderers set up shell companies and other structures before opening bank accounts in the name of these vehicles to conceal their identity.

At the EU level, customer due diligence rules must be improved so that they cannot be circumvented by an opaquely owned vehicle or a web of such vehicles. A risk-based approach, as recommended by FATF, is meant to focus attention on the situations where money-laundering is most likely to happen. At the micro level, it means professionals should target risky cases with more thorough customer checks, known as enhanced due diligence. This is sensible. It helps target resources and prevents the government agencies tasked with tackling money laundering – known as financial intelligence units (FIUs) – from being swamped with overly cautious and irrelevant SARs. However, the EU uses a poorly transposed version of the risk-based approach, creating a loophole. EU rules, as they stand, mean that you only have to verify the beneficial owner in high-risk cases. This does not make sense, because if the beneficial ownership information is hard to find or unconvincing, this is a clear indicator of risk. To protect the banking system from abuse, customers should be rejected and SARs filed whenever the beneficial owner cannot be identified. There are several exceptions: in cases where suspicion of money laundering is very high, it can be preferable to accept the business whilst simultaneously tipping off authorities with a SAR, making it more likely that wrongdoers will be brought to justice. The current EU directive takes this approach.[58] Under the new FATF standards, CIs are permitted to identify the senior management if they have decided it is too difficult to identify a beneficial owner. This is a get out clause that provides an excuse for not carrying out sufficiently rigorous due diligence to establish beneficial ownership information. The exception is the case of listed companies and state-owned enterprises, where management information can be most relevant. Equally discretionary trusts and foundations pose a high money laundering risk because the beneficiary is not defined. However, they also play an important role in managing charitable funds. Banks should only be allowed to accept money from discretionary trusts, foundations and similar constructions if the individuals who fund and control the vehicles and also the legal agreements that govern them have been provided to the government. Equally banks should require a record of people and institutions that have received payments in the past (if such information is not already publically available).

If CIs were required to verify the beneficial owner's identity each time as part of CDD, this would mean tax evaders would find it harder to access 'safe' banking systems within the EU, whatever the secrecy laws in a tax haven through which an individual was channelling their illicit money.

It is important to verify not only that ownership information provided is comprehensive, but also that it is convincing. The new FATF recommendations state that overly complex corporate structures can be indications of a higher risk customer.[59] For example, when presented with a complex ownership structure, CIs should consider whether it seems normal for that type of business and whether there is a reasonable explanation for this structure. Equally, CIs should consider whether the beneficial ownership information they have been provided with is accurate, or if it appears that nominees are posing as the beneficial owner(s). They should also continue to monitor the customer to make sure that someone else has not started to exercise control. If information about the beneficial owners of legal structures was recorded, verified and updated by a government agency, then CIs could refer to this, making their due diligence easier to carry out.

Disclosure requirements for companies across 70 jurisdictions

Currently very few countries adequately record who owns and controls legal structures. Even fewer countries make this information public, leaving most jurisdictions wide open to tax evasion and money laundering. First, governments should not simply rely on CIs to collect beneficial ownership information, which makes it much more likely that wrong-doers will slip through the net. Second complex chains of opaque vehicles not only help to get around CDD when opening a bank account, they are also used to bamboozle law enforcement and tax authorities, frustrating prosecutions and asset recovery efforts. If information was collected in a central registry, it would be possible to find it more quickly and efficiently.

In both cases the standards add that "Countries should consider measures to facilitate access to beneficial ownership and control information by financial institutions and [other cis]". The most effective way to do this is through requiring such legal persons and legal arrangements to register beneficial ownership information with authorities. Equally, as authorities and the private sector need to be held to account for tax and AML compliance and enforcement, this kind of information should be publically available. This would also speed up the process of accessing information for foreign authorities.

Most jurisdictions rely on legal ownership. However, as the example of the two Latvian TSCPs highlights (see box on page 12) this is insufficient because legal owners and managers could be nominees or even other shell companies. Disclosure is generally more detailed about companies than it is about other legal arrangements such as trusts where there is usually no central government register. Some jurisdictions do not even require some types of companies to register. This is the case in the Marshall Islands, Vanuatu and Liberia, making it even harder for authorities to investigate tax evasion and money laundering cases. It is imperative for tax purposes that both ownership and control of assets and vehicles is established. Some jurisdictions are satisfied with either ownership or control. As a possession, a shell company is more of a tool than an investment. The purpose of owning it is to control it. Equally the destination of the income stream passing through a vehicle should also be established to ensure that the income stream is taxed. For anti-money laundering customer due diligence purposes, the EU considers the beneficial owner(s) to be all those with more than a 25% shareholding of a company. However, this is easy to circumvent. The 25% threshold does not do enough to determine who is in control, which is often more important when a legal structure is simply being used as a channel for money.This might be lowered. to the 10% stake recognised in the USA so that the EU does not fall foul of the Foreign Account Tax Compliance Act (FATCA), which would make it more difficult for EU banks to access the US market. However, this threshold should be dropped entirely except in specified cases, such as for the shares that are traded on a reputable exchange. Then senior managers could be identified instead. At a very minimum, to lay the foundations for beneficial ownership disclosure, a government legal ownership register should be set up. Equally the more information that is made available about legal structures, the easier it is for investigators to pursue the ultimate beneficial owners, so these intermediate steps are useful in the absence of beneficial ownership registers.

If ownership information is not updated, it is easy for a money launderer to simply assume control of a company after it has been incorporated. In some jurisdictions certain types of companies do not have to report changes, the reasons for this vary. For some jurisdictions, the updates are only needed in certain circumstances. In the Netherlands, changes in legal ownership only need be reported when the company is 100% owned. In Germany, changes that affect a controlling portion of shares must be reported. In other cases, some types of company – especially foreign-owned ones – are exempted from updating ownership information. This is the case with international business corporations in the Seychelles, for example. Countries that do require updates in legal shareholder

FATF recommendation 24 relates to transparency and beneficial ownership of legal persons:

"Countries should ensure that there is adequate, accurate and timely information on the beneficial ownership and control of legal persons that can be obtained or accessed in a timely fashion by competent authorities."

Recommendation 25 on transparency and beneficial ownership of legal arrangements states the following:

"...information on the settlor, trustee and beneficiaries, that can be obtained or accessed in a timely fashion by competent authorities. Countries should consider measures to facilitate access to beneficial ownership and control information by financial institutions."[60]

> Under the new FATF standards, CIs are permitted to identify the senior management if they have decided it is too difficult to identify a beneficial owner. This is a get out clause that provides an excuse for not carrying out sufficiently rigorous due diligence to establish beneficial ownership information.

Table 1. Do companies have to provide authorities with beneficial ownership information regarding shareholders?

All companies require recording of beneficial ownership (6)	Companies available where only legal ownership is recorded (36)		Companies available without recorded ownership information (27)
Andorra Bermuda Costa Rica India Jersey[61] Monaco	Bahrain Barbados Belgium Botswana Cyprus France Germany Ghana Gibraltar Guernsey Hong Kong Hungary Ireland Isle of Man Israel Italy Japan Korea	Luxembourg Macau Malaysia (Labuan) Maldives Malta Mauritius Netherlands Panama Philippines Portugal (Madeira) San Marino Singapore Spain Switzerland United Arab Emirates (Dubai) United Kingdom Uruguay	Anguilla Antigua & Barbuda Austria Bahamas Belize British Virgin Islands Brunei Canada Cayman Islands Cook Islands Denmark Dominica Grenada Guatemala Latvia Liberia Liechtenstein Marshall Islands Montserrat Nauru Samoa Seychelles St Kitts and Nevis St Lucia St Vincent & Grenadines US Virgin Islands USA

Table 2: Which jurisdictions require companies to report changes in legal ownership?

Changes in legal ownership must be reported:	Certain types of companies do not have to report changes or companies only have to update information in a limited set of circumstances:	No obligation to report changes:
Andorra Bahamas Bahrain Brunei Cyprus Hong Kong India Ireland Isle of Man Israel Italy Lebanon Liberia Macau Malta United Kingdom	Cayman Islands France Germany Japan Netherlands Seychelles Samoa	Belgium Bermuda Botswana Jersey Liechtenstein Luxembourg Marshall Islands Panama Philippines Portugal (Madeira) Singapore Spain Switzerland Uruguay USA Vanuatu

information often request this update in the annual returns of the company. For example, this is the case in the UK. In Jersey, beneficial ownership information has to be updated but only in certain circumstances.

No clear-cut cases[62] were found of a country that permits neither nominee nor corporate company offices. With the exception of Monaco, however, this seems to be because their banking system caters only to individuals but not to companies. In the bad cases, like Saint Lucia, there is no requirement for company officers to be registered; and in the British overseas dependency of Anguilla neither company officer nor shareholder names need to be reported to the government. Worse still, sometimes there are no requirements for some types of company to register with authorities at all. This is the case in Vanuatu, Liberia and the Marshall Islands. The concept of a nominee is not applicable in the French legal system and as a consequence "nominee" directors are not available. However, corporate bodies may be company directors. A foreign corporate body has to have a representative, who is a natural person. They can be held legally responsible and they are meant to provide the beneficial ownership information to authorities on request. This makes for stronger regulation than in the other countries studied, but is still sub-optimal. It does not seem that different from having a nominee. The effectiveness of this measure hinges on whether the representative is held accountable for the company's actions and for any failure to collect accurate beneficial ownership information.

Publication of company officer information

In our sample, there were no countries that made beneficial ownership information available online. However, in Canada, provinces all have their own rules, and in Quebec owners' and officers' identities are available online. There are various examples of countries where legal ownership information is online for free or at a low cost. However, in many EU states you have to pay for basic information on a company. This cost is likely to be prohibitive when an investigation might have to trawl through

If CIs were required to verify the beneficial owner's identity each time as part of CDD, this would mean tax evaders would find it harder to access 'safe' banking systems within the EU, whatever the secrecy laws in a tax haven through which an individual was channelling their illicit money.

Table 3: Are nominee or corporate company officers allowed (whether directors, secretaries, trustees, enforcers or otherwise)?

Both nominee and corporate company officers are allowed:	Both are permitted because there is no company registration requirement:	Nominees are allowed but not corporate company officers:	Nominees allowed unclear regarding corporate officers:	Corporate company officers are allowed but not nominees:	Corporate company officers are allowed (unclear regarding nominees):
Anguilla Bahamas Belgium British Virgin Islands Canada Costa Rica Cyprus Dominica Hong Kong Isle of Man Jersey Luxembourg Malaysia (Labuan) Mauritius Panama Portugal (Madeira) St Kitts and Nevis St Vincent & Gren-adines United Kingdom USA	Liberia Marshall Islands Vanuatu	Botswana Israel Singapore Switzerland	Belize Seychelles	France	Antigua & Barbuda Barbados Brunei Cayman Islands Cook Islands Gibraltar Grenada Guernsey Ireland Malta Netherlands Samoa Spain Uruguay

hundreds or thousands of records.

Disclosure requirements for legal arrangements

When it comes to registering legal arrangements, the problem is far more severe. The vast majority of countries do not require registration. This includes the USA, and within the EU: Germany, the United Kingdom, the Netherlands, Belgium, Austria, Denmark, Hungary, Ireland, Luxembourg, Portugal (Madeira), Malta and Cyprus. In Latvia, there is no such requirement but this is because domestic trusts are not recognised. However, it is not clear if foreign trusts are operable there. In Switzerland there is no provision for Swiss law trusts. However, foreign law trusts can be administered from Switzerland, although this is a recent development. The Canadian government collects information on the settlors and beneficiaries of all trusts that are resident in Canada.[63] Not having registered trusts has immense significance, as compliance with other aspects of trusts regulation is then considerably harder to monitor. Italy has a registration requirement that applies to resident and non-resident trusts. France has a registry for *Fiducie*, a recently introduced French version of trusts. Foreign law trusts are now also required to register if they have a tax implication in France. Requiring at the least that trusts must register with a central agency is a key step that the EU and other jurisdictions should take. Trust registration would make other requirements for trusts such as providing accounts more enforceable. Trusts that were not registered could be deemed to have no legal weight; therefore the arrangements would no longer protect the assets held.

Trusts are peculiar to common law countries. Many countries do not recognise them, so countries like the UK host many foreign controlled trusts. There is no trust registration requirement but domestic trusts should be known to the authorities as these are required to submit tax returns. This would generally not be the case with a foreign-owned trust. However, trusts are often used as conduits for tax evasion and in many types of crimes that foreign authorities would want to investigate, so foreign-owned and -controlled trusts should also be made to register. The same holds for foundations, *Anstalten* and other legal entities that play a similar role to trusts outside of common law countries.

Accounting requirements for trusts and other arrangements

Trusts and foundations often hold or transfer vast amounts of income. If they are made to submit accounts, it would be much easier for authorities to monitor their use and make sure it is legitimate. Twenty-two countries require trusts to keep accounting data including Italy, France, Spain, Austria, Malta, in the EU and other developed economies like South Korea, Canada, Singapore and even some traditional tax havens like Monaco. However there are loopholes that render this requirement useless in other countries. This can be exemplified by the situation in the USA, which requires data to be kept but does not got give a minimum retention period. This is almost meaningless.

Governments should not simply rely on CIs to collect beneficial ownership information, which makes it much more likely that wrong-doers will slip through the net.

For the majority of countries, the problem is that there is not a registration requirement for trusts. This means the rule that accounting data must be submitted cannot be upheld. Some states like Belgium and Demark give this treatment only to foreign law trusts that do not have to register. This is an example of a harmful tax practice where in order to attract business, preferential treatment is given to foreigners who may be evading taxes. In the case of St Kitts, for example, international trusts are required to keep such data but only because of AML rules.

Of the countries where data is available, Canada has a well-conceived requirement for trusts to submit accounting data to authorities. This applies as long as the trustee is based in Canada, even if the beneficiaries are not. In other countries such as a Britain and Austria trusts are required to submit accounts at least in certain circumstances. However, there is no obligation for trusts to be registered in the first place, rendering this requirement much harder to enforce. For this reason, trusts and other legal arrangements (with the exception of collective investment schemes) should be required to register with a central agency in the countries in which any participant in that arrangement resides or in which a bank account is held in the name of that arrangement. The responsibility to register would generally lie with the fiduciary – the person who is responsible for managing, or holding the assets on behalf of the beneficiary.

OECD research has found that various jurisdictions require fiduciaries of foreign law legal arrangements to provide information on the participants (for example, settlors, trustees and beneficiaries) to a government agency.[64] This is often to prove that the fiduciary is not the owner and therefore should not be taxed on the arrangement's income or assets. If a legal arrangement needed to be registered in order to have weight, it would create an incentive for the fiduciary to register to avoid the risk of being classified as the owner and taxed accordingly. Given the huge amounts of money that is held or channelled through trusts and all other such legal arrangements, fiduciaries should be required to submit annual reports to be published online in the residence country of each fiduciary who oversees a trust with overall payments either above €15,000 per year or with underlying assets valued at above €100,000 at any moment in the year. Annual reports should include the full names and birth dates and country of residence of each participant in the legal arrangement and of payees (those that receive payments from the trust). It is important to ask for information about payees because otherwise the real beneficiary can get around the requirement by disguising any payouts they receive as a disbursements for services provided to the trust such as consultancy fees. This is especially important for discretionary trusts and other similar such arrangements and entities that do not have a beneficial owner. The only way to find out who benefits is through the accounts.

To make registration of trusts and other constructions such as foundations truly effective trustees, foundation council members and fiduciaries should also submit all documents related to the legal arrangements to the registry in order for the arrangement to take effect. Information on all natural persons who are participants should be provided to the registry and updated annually. The registry would have a responsibility to verify the information provided and to apply sanctions for inaccurate reporting or failure to report. For more detailed recommendations see TJN *Bank account registries in selected countries: Lessons for registries of trusts and foundations and for improving automatic tax information exchange.*[65] In addition, the TJN report found that at least five countries have bank account registries that are managed by the tax authorities. This measure could also be useful for addressing money laundering more broadly. The report contains recommendations about how such registries should operate.

This survey of the rules in a large sample of jurisdictions has shown that most jurisdictions would have to change to live up to the global standard set down by FATF. If this is not done in the developed economies where so much dirty money ends up, tax evasion will continue to sap national budgets and impede development with devastating human consequences for the world's poorest people

The EU considers the beneficial owner(s) to be all those with more than a 25% shareholding of a company. However, this is easy to circumvent.

Chapter 4

Tax crimes as a "predicate offence" of money laundering

Foreign and domestic tax crimes should be recognised as a predicate offence of money laundering

In addition to undisclosed ownership, a further problem is the impunity with which people who commit tax evasion and the professionals who facilitate them are able to operate. This is aggravated because of the partial or complete failure of various jurisdictions to include foreign and domestic tax crimes within their money laundering frameworks. Most jurisdictions consider money laundering to have taken place once it is proved that the money was wholly or partially the proceeds of a crime known as a money laundering predicate offence. A predicate offence is a crime that, as a matter of logic or statutory provision, is or must be a part of another crime. To date, most countries' lists of offences that predicate money laundering include at least drug trafficking, organised crime, smuggling and terrorist activities. In many countries, all serious crimes count. Some countries take an "all crimes approach" which means they consider all criminal offences to predicate money laundering. Going still further, in some jurisdictions, if proof cannot be supplied that money was obtained legally then prosecution can be brought for money laundering.[66]

In the EU, money laundering rules require states to treat serious crimes that take place abroad, whether in the EU or a third country as a predicate offence, but only if the crime that took place abroad is also recognised as serious in domestic law. This is known as dual criminality. One problem with this is that even large-scale tax violations are only viewed as misdemeanours or as a civil matter in several member states. So for some jurisdictions within and outside the EU the first step is to make tax evasion a crime, or to widen the scope of tax offences that are viewed as serious.

If you conceal the proceeds of any serious crime, you are committing money laundering. The question is: what counts as a serious crime? A serious crime is often defined in relation to the severity of a jurisdiction's guideline jail sentence for that offence, with a one year guideline sentence frequently used as a cut-off point. However, to give extra guidance and tackle the most serious and common crimes, FATF proposes a list of specific predicate offences where those who conceal the proceeds should automatically be considered to have committed money laundering. This list initially focused on drug trafficking, and later on terrorism and corruption. Within the EU drug trafficking, terrorism and corruption are automatically considered as predicate offences of money laundering regardless of the guideline sentences.

In 2012, FATF recommended that tax crimes should be made a predicate offence of money laundering. This prompted Singapore, one of the world's largest financial centres, to reaffirm its commitment to making foreign and tax crimes a predicate offence; this is due to come into force in 2013.[67] Making tax evasion a predicate offence means that a jurisdiction has to consider it in CDD, and in AML enforcement and cooperation. The FATF transposition represents a chance to make sure that not only individuals and companies committing illegal tax evasion, but also the professionals facilitating it, are held to account for their insidious activities. Considering the grave consequences of tax crimes presented in Chapter 1, they must be regarded as a serious crime with real victims.

Deterring tax evasion by explicitly recognising it as a predicate offence will have immediate benefits. CIs would be incentivised to consider tax evasion risk in their due diligence and to turn down potential customers who put them at clear risk. This would immediately raise the cost and hassle involved in tax evasion. Tax evading individuals would have to choose between avoiding all investments and expenditure in jurisdictions that adopt this measure, or paying their taxes in the state where they were due. Higher risks would also decrease financial institutions' willingness to enable tax crimes.

In the EU and other important financial centres there is a gap. Within the EU under the Third Anti-Money Laundering Directive,[71] which has been in effect since 2005, tax evasion is only covered where there is a maximum sentence of above one year, or a minimum sentence of above six months. The EU is considering lowering the threshold to a maximum guideline sentence of six months, which might help to capture tax crimes in some jurisdictions where tax evasion is not a predicate offence. However, relying on a six month maximum sentencing guideline will almost certainly mean that tax evasion will not be covered in some member states.

Why a strong definition of tax crimes is crucial

FATF recommendations do not define "tax crimes" and the concept varies considerably between jurisdictions. This can obstruct cross-border cooperation and lead to certain

> Making tax evasion a predicate offence means that a jurisdiction has to consider it in CDD, and in AML enforcement and cooperation. The FATF transposition represents a chance to make sure that not only individuals and companies committing illegal tax evasion, but also the professionals facilitating it, are held to account for their insidious activities.

Table 4: Are Tax crimes a predicate offence and how are tax crimes treated under different AML legislation?[68]

Foreign and domestic tax crimes are a predicate offence:		Tax crimes are a predicate offence unclear about offences committed abroad:	Tax evasion is not a predicate offence, but specific tax-related offences are predicate crimes:	Neither foreign nor domestic tax evasion is a predicate offence:
Belgium	Malta	Poland	Austria [69]	Bulgaria
Botswana	Mexico		Cyprus	Hong Kong
Canada	Netherlands		Germany	Japan
Czech Republic	NewZealand		Switzerland	Luxembourg
Denmark	Norway		Turkey [70]	Macau
Estonia	Portugal			San Marino
Finland	(Madeira)			USA
France	Romania			
Greece	Singapore			
Hungary	Slovakia			
Italy	Slovenia			
Ireland	Spain			
Jersey	Sweden			
Korea	Ghana			
Latvia	St Vincent & Grenadines			
Lithuania	United Kingdom			

types of tax crime not being covered. The phrase "tax crimes" is used to avoid meaning being lost in translation, as different states have different terms and approaches.

In Germany, the third EU AMLD means that the following would be eligible to be considered as predicate offences: particularly serious tax evasion; professional, violent or organised smuggling and receiving; holding or selling goods obtained by tax evasion where this is deliberate rather than negligent. The overriding criteria for determining whether tax evasion should be considered as particularly serious depends on whether it involved "intense criminal effort". The following factors provide further guidance, but do not necessarily mean the offence will be viewed as serious: if more than €50,000 is evaded; forgery of documents; taking part in a group set up for this purpose; or abuse of an official position.[72]

In France, a much broader range of offences is covered. Tax fraud is the main tax offence, which covers any deliberate attempt to underpay taxes through wilful failure to pay or concealment:

"anyone fraudulently evading or attempting to evade the establishment or full or part payment of the taxes covered by this code, whether having willfully omitting to make his or her declaration within the time limits prescribed, or having willfully concealed a proportion of the sums subject to tax, or having willfully arranged his or her insolvency or obstructed by any other means the collection of tax, or by acting in any other fraudulent manner." [73]

This can result in a maximum sentence of up to five years. However, in France the threshold for a predicate offence of money laundering is stricter than the EU requires: an offence that results in imprisonment or a fine of above €3,750 is a predicate offence if it provides the offender with a direct or indirect profit.

In Switzerland 'tax evasion' and 'tax fraud' are separate concepts: fraud involves falsifying official documents or lying, whereas tax evasion involves underpayment of tax, which is considered to be accidental. There is a risk that, even under the new international AML regime, Switzerland will only share information with other countries in matters of tax fraud as defined by Swiss law, which is much harder to prove. A more likely outcome of the revised FATF recommendations is that Switzerland will also exchange information in matters of "severe tax evasion" (a new legal concept that will most probably include repeated evasion of large sums). Turkey shares the Swiss distinction of tax fraud and tax evasion, as Turkey based its commercial law on that of Switzerland.[74] Some countries have weaker definitions of tax crime, applying only civil sanction to tax evasion. In some countries it is a predicate offence to evade certain types of taxes and not others. For example, in Austria tax crimes are only considered a predicate crime when they involve evading import or export duties.

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In Austria tax crimes are only considered a predicate crime when they involve evading import or export duties.

During transposition, tax crimes should be interpreted to cover all intentional underpayment of tax, including all direct and indirect taxes. The definition based on deliberate underpayment is the more common definition and would allow for greater international cooperation. A strong common definition of tax crimes, recognising all intentional attempts to underpay on foreign or domestic tax obligations, is needed in the EU and elsewhere.

The European Commission has expressed an interest in standardised punishments and definitions for certain types of tax crime, and the draft EU-Liechtenstein tax fraud agreement provides a possible model. The customs and taxation arm of the EC, DG TAXUD, notes:[75]

"As tax fraud is often linked with other forms of criminal activity it is important to strengthen cooperation between tax administrations and other authorities, in particular anti-money laundering, social security and judicial authorities, both at national and international level."[76,77]

The EU has a precedent for implementing a definition based on all deliberate underpayment of tax. The draft EU-Liechtenstein tax fraud agreement provides a possible definition of tax fraud. This definition covers not only falsified tax returns, but also incomplete tax returns. It also covers both individuals and legal persons, and relates to both direct and indirect tax.[78]

Clear, broad definitions of tax crimes exist, and are necessary, given the global nature of the problem. For example, Richard Murphy of Tax Research UK defines tax crimes as follows:

"Any deliberate act that results in tax not being paid on an economic event whose substance occurs within a jurisdiction contrary to the law of the jurisdiction where that economic event either occurs or is recorded or that results in tax not being paid contrary to the laws of the jurisdiction in which a benefit of that economic event arises."

This might be politically feasible if combined with a financial materiality threshold to exclude very small cases. This definition recognises the cross-border nature of transactions, vital in a world where, in the words of Jeffrey Owens of the OECD, *"the creation of offshore financial accounts, shell companies and the like are just a click of a mouse away."*[79] This is even more necessary when you consider the increasingly artificial nature of modern tax reduction schemes, which are *"Nominal, hyperportable, multi-jurisdictional, often quite temporary location of networks of legal and quasi-legal entities and arrangements that manage and control private wealth"*.[80]

Making tax crimes a predicate offence would deter professionals from devising illegal tax evasion schemes and make it harder for tax evaders to use or invest their money in the jurisdictions that adopted this provision. Considering the large scale of cross-border tax evasion, this should recognise both foreign and domestic tax crimes. Many crucial jurisdictions do not consider tax crimes a predicate offence or do so in circumstances which are unjustifiably restricted. However in a considerable number of jurisdictions tax crimes are predicate offence but this does not seem to be creating sufficient deterrence. For legislation to be effective it needs to be combined with strong implementation including international cooperation and credible enforcement unfortunately as the next chapter will discuss this is often lacking.

Chapter 5

Putting anti-money laundering standards into practice: international cooperation, enforcement and private sector corporate compliance

Existing AML standards have been poorly enforced. The two main reasons appear to be: not enough focus on implementation of standards at the global and national levels; and vested interests that benefit from attracting laundered and tax evaded money from abroad.

Existing AML standards have been poorly enforced. Appendix 3 shows the amount of assets frozen as a result of AML in various jurisdictions are tiny compared to the estimated US$2.1 trillion that UNODOC estimate was laundered in 2009, or the estimated US$859 billion of illicit flows from developing countries in 2010.[81]

Appendix 4 shows the total number of suspicious activity reports that were filed in the surveyed countries in the year of their last mutual evaluation. The previous FATF standards – known as 40 + 9 and the EU's Third AMLD – are not being properly implemented because monitoring of CIs by authorities was inadequate to ensure proper compliance. For example, the United Kingdom's Financial Services Authority (FSA) produced a report in 2011 on AML compliance in the financial sector, which found that banks were not effectively implementing the regulations. Notably, more than 50% of the UK banks that the FSA studied did not carry out "meaningful enhanced due diligence" in risky circumstances.[82]

According to a study on implementation of the previous AMLD carried out for the EC by the accountancy firm Deloitte, the compliance situation was much worse outside the banking sector. Deloitte found:

"the latest statistics show that the frequency of AML reporting for most non-financial professions in most Member States is still very low, the inherent risk of launderers being tempted to use techniques which involve non-financial professions increases."[83]

Notably, more than 50% of the UK banks that the FSA studied did not carry out "meaningful enhanced due diligence" in risky circumstances.

A further problem is that prosecutions are not being brought with sufficient regularity, and sanctions are not tough enough to create a deterrent effect. In actual cases where money laundering is proven, the sanctions are not strong enough to deter such activity. For example, in the USA, the recent fine of $340 million to Standard Chartered for concealing illegal sanctions-busting transactions with Iran was ridiculously small when compared with the $250 billion worth of transactions the bank had handled as a result of this activity.[84] At least there was significant publicity around this case, which helps create deterrence by warning others and damaging the reputation of the company involved. Often in the EU, when companies face sanctions this tends to go unpublicised and unnoticed. In addition, in some countries in the EU, the administrative fine for non-compliance with the directive is ludicrously low: €32,000 in Estonia and €50,000 in Italy.

The possibility of revoking the licenses of institutions that are seriously implicated in money laundering should be considered. Equally, prosecutions should be brought against the individuals involved. At the EU level, the Commission has already discussed the possibility of minimum administrative sanctions for financial institutions, arguing that current sanctions are often not a deterrent. The EC Communication on reinforcing sanctioning regimes in the financial services sector points out that, as many cases almost certainly go undetected, fines should considerably exceed the profits made from a given activity in order to affect an actor's cost-benefit analysis. The communication notes that, in some countries, penalties are applied only to natural persons or only to legal persons. They argue, sensibly, that it should apply to both.[85]

Too little focus on implementation and effectiveness of standards in FATF mutual evaluations

The incomplete implementation of the FATF standard partly reflects the fact that mutual evaluations have focused most of their attention on whether FATF standards are transposed into national legislation, and too little on what happens next. FATF's mutual evaluations have been a crucial way to pressure countries to put AML standards into law. However, it is increasingly felt that, to date, the peer reviews do not do enough to investigate how effective these laws are proving to be. When looking at implementation, mutual evaluations mainly consider sectoral frameworks and compliance procedures. More in-depth studies of individual cases would be illuminating: it was this shift in approach that led the Financial Services Authority (FSA) to come to its damning conclusions about the compliance of UK banks.

"the latest statistics show that the frequency of AML reporting for most non-financial professions in most Member States is still very low."

Deloitte study on the application of the third Anti-Money Laundering Directive

Table 5: Overall Compliance with FATF 40+ 9

Ranking	Jurisdiction	Year of Assessment	Compliance
1	Guernsey	2011	82.31
2	Hungary	2005	77.78
3	Belgium	2005	75.69
4	United Kingdom	2007	72.11
5	Cyprus	2007	71.43
6	US Virgin Islands	2006	70.07
7	USA	2007	70.07
8	Malta	2008	68.71
9	Singapore	2007	68.71
10	Cayman Islands	2008	68.03
11	British Virgin Islands	2007	67.35
12	Panama	2009	67.35
13	Isle of Man	2006	65.99
14	Portugal (Madeira)	2009	65.97
15	Uruguay	2007	64.63
16	Gibraltar	2006	62.59
17	Italy	2007	62.59
18	Malaysia (Labuan)	2007	61.22
19	Switzerland	2006	61.11
20	Spain	2006	60.99
21	Ireland	2010	59.86
22	Anguilla	2009	58.5
23	Israel	2008	58.33
24	Hong Kong	2009	57.82
25	Cook Islands	2007	56.25
26	Latvia	2010	56.03
27	Guatemala	2007	55.78
28	Bahamas	2007	55.1
29	Macau	2009	55.1
30	Austria	2010	54.42
31	India	2010	53.47
32	Germany	2007	53.06
33	Bahrain	2008	52.08
34	Liechtenstein	2008	51.02
35	Canada	2008	51.02
36	Barbados	2006	50.34
37	Denmark	2008	49.66
38	Mauritius	2008	48.3
39	Monaco	2008	47.62
40	Japan	2009	45.14
41	Lebanon	2009	44.9
42	St Kitts and Nevis	2008	44.22
43	Bermuda	2005	42.86
44	Brunei	2008	42.86
45	United Arab Emirates (Dubai)	2009	42.86
46	Philippines	2009	42.18
47	Korea	2010	42.18
48	St Vincent & Grenadines	2007	41.5
49	Andorra	2010	39.01
50	Luxembourg	2008	34.69
51	Antigua & Barbuda	2008	34.01
53	Vanuatu	2006	33.33
54	Grenada	2009	28.57
55	Costa Rica	2007	28.47
56	Samoa	2006	27.89
57	Dominica	2009	25.85
58	San Marino	2008	24.31
59	Botswana	2007	23.61
60	Ghana	2009	23.13
61	Seychelles	2008	22.92
62	St Lucia	2008	13.61

FATF's member states are making some attempts to address weak implementation. In the latest review of the organisation's mandate in April, ministers from member states agreed that: "Future evaluations will move beyond technical compliance of the standards and aim to understand how resources and sanctions are being applied in practice to meet desired objectives".[86] One way to achieve this should be to subdivide each criterion into two parts, one looking at transposition of rules and the other looking at how thoroughly and effectively they are put into practice.

There are a number of problems with the way FATF mutual evaluations are undertaken that weaken their credibility. Table 5 shows an analysis of the compliance ratings from AML mutual evaluations. It was produced for 62 jurisdictions as part of the Tax Justice Network's Financial Secrecy Index.[87] For each of the 49 FATF recommendations, or all where a rating was available, a score is given as follows. Compliant gets a score of one, Largely Compliant two thirds, Partially Compliant one third and Non-Compliant gets zero. The total score is then calculated as a percentage. CCFD-Terre Solidaire applied a similar method to a different sample of jurisdictions.[88] Some tax havens and money laundering destinations score very well. Some smaller tax havens have transposed all the FATF criteria in order to perform well in the mutual evaluations. However, this will not help to address money laundering if they do not then properly enforce the regulations or cooperate with other jurisdictions including by sharing information. Their high scores could be due to the absence of tax crimes as a predicate offence in FATF 40+9. The fact that the recommendations relating to the abuse of legal persons and legal arrangements a key tool of money laundering are not given enough significance in the assessment criteria is another major

In the USA, the recent fine of $340 million to Standard Chartered for concealing illegal sanctions-busting transactions with Iran was ridiculously small when compared with the $250 billion worth of transactions the bank had handled as a result of this activity.

weakness of FATF's mutual evaluations. This could skew the results of mutual evaluations, as could the fact that major jurisdictions like the USA and UK have poorer ownership transparency standards than many of the smaller jurisdictions that are more traditionally viewed as tax havens. It could also reflect the fact that countries like the UK put standards into law and then enforce them poorly, which mutual evaluations in the current format underemphasise.

The other side of the coin is that jurisdictions with weak money laundering frameworks could be rated non-cooperative or high risk even if they do not have a severe problem with money laundering, but rather that they lack the resources to implement the framework recommended by FATF. For countries that were rated non-compliant, this means that foreign financial institutions are wary of doing business with any companies or individuals there. This can damage legitimate financial activity of businesses and individuals between these countries and the outside world. Whilst it is important that there are carrots and sticks, it also essential that these are applied in an objective and impartial way. The fact that this is not the case is highlighted by the example of Luxembourg and Turkey. CCFD-Terre Solidaire calculated that Turkey was 30% compliant with FATF recommendations whereas Luxembourg was 20% compliant. However, Turkey ended up on the FATF grey list and Luxembourg did not.[89]

The score that different countries get becomes a political issue, and it has been questioned whether FATF is as critical of its own member states as it is of third countries. As many top performers are FATF members and big players in the OECD, where FATF is based, or are dependent jurisdictions on such states, they can influence the standards and evaluations to improve their ratings.[90] Questions have been raised about the lack of democracy and accountability in FATF governance. The fact that FATF is not based on any treaty has meant that its mandate has never been the subject of public debate. It is not clear which seven countries make up FATF's steering committee.

It is important that FATF is subjected to public scrutiny and is transparent about its decision-making processes. For example, as the box on page 25 shows, the Transnational Institute (TNI) has criticised the FATF standards related to the abuse of non-profits for terrorist financing, finding that the standards have been exploited by repressive states to crack down on civil society. Clearly some non-profits may be used for financing terrorism and the sector must be transparent and accountable. However, TNI argues that problems could have been avoided if civil society had been more widely consulted in the formulation of the standards.

Removing obstacles to international cooperation

The new FATF standards seek to promote international cooperation, which is essential when dealing with cross-border money laundering and tax evasion. FATF recommends that FIUs should contact their foreign counterparts if they detect a crime involving that country, as well as responding to requests for assistance. Furthermore, FIUs should be properly financed and skilled, and should cooperate fully with foreign investigations, including supplying all required information quickly. FATF also recommend that banking secrecy should not impede information sharing.

Currently many jurisdictions cooperate less fully on tax crimes than on other matters, and dual criminality requirements are a considerable obstacle to AML cooperation. Even if a state does not consider tax crimes as a serious crime or a predicate offence, there is a chance their authorities will cooperate with others that do. However, many states do not do so because of dual criminality requirements, which mean a state will only help another state in the investigation of a crime if the offence would have also been considered a crime in their jurisdiction. This can be interpreted quite narrowly, as offences where both jurisdictions share similar wording. This is especially problematic when you consider the complexity of fiscal laws. This can obstruct collaboration against money laundering, and may be either a technical obstacle or a deliberate tactic by tax havens.

Within the EU, Austria, Belgium, France,[94] Germany and the Netherlands[95] do not fully cooperate in the absences of dual criminality and Luxembourg, puts in place measures to prevent effective cooperation in cases involving fiscal offences.

Countries should also refrain from making exemptions in regard to AML cooperation when it concerns fiscal crimes. This is the case with Luxembourg: *"The Law of 8 August 2000 on co-operation in criminal matters does not allow co-operation on accessory fiscal issues and, generally, the data exchanged may not be used for tax purposes, even accessory ones."*[96] It appears that CIs in Luxembourg are not even permitted to report suspicious activities that may involve fiscal issues in the absence of other predicate offences.[97]

CCFD-Terre Solidaire calculated that Turkey was 30% compliant with FATF recommendations whereas Luxembourg was 20% compliant. However, Turkey ended up on the FATF grey list and Luxembourg did not.

Unintended consequences: Authoritarian governments used FATF terrorist financing recommendations to crack down on critics

Previous global AML standards produced by FATF have been criticised for providing authoritarian regimes with an opportunity to crack down on non-profit organisations. Under these standards, there were 40 recommendations for the prevention of money laundering and nine special recommendations for combating the financing of terrorism: known as 40 + 9. The new standards merge the two sets of recommendations together into their latest 40 recommendations.

Special measure VIII for combating terrorist financing, from the old recommendations, has been completely incorporated into recommendation eight of the new standards, which covers measures to prevent the misuse of non-profit organisations.

This merging of terrorist financing and misuse of non-profits has allowed authoritarian regimes to conflate the two, with serious adverse consequences for non-profits in some cases. For example:

"In June 2010, EAG (Eurasian Group on money laundering and terrorist financing) found Uzbekistan 'partially compliant' with SR VIII…. EAG nevertheless recommended that Uzbekistan should 'review effectiveness of the established system of control and monitoring of the NPO sector' for AML/CFT purposes. The Uzbek NPO regulation system is seen by ICNL to have resulted in most foreign and international NGOs being 'closed and expelled from the country' and 'a process of re-registration, which led to a significant reduction in the number of non-governmental organizations' in Uzbekistan. Under the Administrative Liability Code it is illegal to participate in the activity of an unregistered organisation. One of the last international organisations in Uzbekistan – the representative office of the Institution of New Democracies in Uzbekistan – was closed by the courts in the spring of 2010'. Human Rights Watch's representative office in Uzbekistan was closed down by a court decision the following year."[91]

According to TNI, these unintended consequences could have been mitigated if civil society had been more widely consulted in the formulation of the standards. They point out:

"FATF's approach to the [non-profit] sector contrasts that taken toward the banking and financial services sectors, which have long had observer status at the FATF and play a very active role in the development and implementation of FATF Recommendations. It is difficult to understand why the recommendation, guidance and evaluation criteria for SR VIII have all been drawn-up by the FATF without any open consultation or structured input from concerned NPO. [Non Profit Organisation]"

They argue this contributes to a trend for *"principally, but not exclusively authoritarian or hybrid regimes" to put in place "legal or quasi-legal obstacles […] subtle governmental efforts to restrict the space in which civil society organizations (CSOs) – especially democracy assistance groups – operate."* FATF should also consider that CSOs can play a role not only as charitable organisations but also as watchdogs that can encourage good governance and stimulate public debate.

These rules have also made life much harder for bona fide international NGOs and donor organisations that work in conflict zones. TNI argues that human rights safeguards need to be incorporated into the FATF standards and also its mutual evaluations, especially regarding freedom of expression and association.

The new FATF recommendation 37 states that:

"Countries should render mutual legal assistance, notwithstanding the absence of dual criminality, if the assistance does not involve coercive actions. Countries should consider adopting such measures as may be necessary to enable them to provide a wide scope of assistance in the absence of dual criminality. Where dual criminality is required for mutual legal assistance, that requirement should be deemed to be satisfied regardless of whether both countries place the offence within the same category of offence, or denominate the offence by the same terminology, provided that both countries criminalise the conduct underlying the offence."[98]

Furthermore, jurisdictions must:

"(c) Not refuse to execute a request for mutual legal assistance on the sole ground that the offence is also considered to involve fiscal matters."

These principles would greatly help to address crossborder tax evasion and should be transposed.

Banking secrecy, data protection and group compliance

In some jurisdictions, banking secrecy laws prevent the sharing of information with other jurisdictions on tax evasion and other forms of money laundering. FATF's latest recommendations state that countries should:

"…not refuse to execute a request for mutual legal assistance on the grounds that laws require financial institutions to maintain secrecy or confidentiality."[99]

The EU has made some good steps in this direction, with the draft EU-Liechtenstein tax fraud agreement. The section on administrative cooperation in tax matters would require that information requests cannot be refused simply because the information is held by a bank or anonymous investment vehicle.[100]

Equally, data protection laws sometimes prohibit the sharing of information on customers transnationally within a multinational bank. Data protection laws should be amended so that information needed for money laundering checks can be shared within multinational groups. If CIs cannot access data from within their group that was collected in another jurisdiction, due to data protection laws, they should begin the CDD process from the beginning, rejecting the customer and filing a SAR if necessary. There is an issue when customers of multinational banks transfer their relationship from one jurisdiction to another: CIs should not be permitted to rely on due diligence conducted in laxer jurisdictions. Both individual national subsidiaries and parent companies should be held responsible separately for their AML compliance. At all these levels it should be ensured that adequate measures have been taken to prevent money laundering. This would guarantee proper accountability: both that checks are done at departmental or national level; and also that the group is properly overseeing that these requirements are upheld across all its subsidiaries.

Table 6: International cooperation: Does the Jurisdiction cooperate in the absence of dual criminality

Fully		Largely	Partially	Not at all
Anguilla	Liechtenstein	Andorra	Ghana	St Lucia
Antigua & Barbuda	Luxembourg	Austria	Japan	
Bahamas	Malta	Belgium	Macau	
Bahrain	Philippines	Botswana	Samoa	
Barbados	Portugal (Madeira)	Cook Islands		
Bermuda	Singapore	Costa Rica		
British Virgin Islands	St Kitts and Nevis	France		
Brunei	St Vincent & Grenadines	Germany		
Cayman Islands	United Kingdom	India		
Cyprus	Uruguay	Lebanon		
Dominica	US Virgin Islands	Malaysia (Labuan)		
Gibraltar	USA[92]	Mauritius		
Grenada	Canada	Monaco		
Guernsey	Denmark	Netherlands		
Hong Kong	Italy	Panama		
Hungary	South Korea	San Marino		
Ireland	Spain	Seychelles		
Isle of Man	Guatemala	Switzerland		
Israel	Marshall Islands[93]	United Arab Emirates		
Jersey		(Dubai)		
Latvia		Vanuatu		

Who benefits from the money laundering and tax evasion economy?

A light touch approach to regulation, and an 'anything goes' approach to attracting finance and customers can benefit the financial sector and bring money into an economy. However, it is not a sustainable way of boosting growth; it creates little employment and can create destabilising economic conditions beyond a government's control.

Banks in EU member states and other developed countries are targeted by tax evaders from developing countries because they are perceived as the safest place to invest. The safety of these large financial centres, and the fact that money generally arrives via a chain of arrangements in other smaller tax havens, has led researchers to term places like the City of London 'destination havens'. The fact that countries like the UK, Switzerland and the USA give preferential tax treatment for foreigners also makes them tax havens. These countries have cornered a huge proportion of the global market in handling business for foreign clients. In theory, the concentration of this industry among a few firms in destination havens provides the opportunity for much stricter regulation.

Many states have adopted 'beggar thy neighbour' tax competition policies, looking to attract illicit capital from abroad to swell their financial sectors. In the USA, it is legal to handle the proceeds of various crimes committed abroad.[105] The USA has previously tried to attract foreign tax evaders and others with illicit funds to bank in the USA to help its balance of payments problems and to bring business to Wall Street. This is demonstrated by the USA's qualified intermediary programme, and the initial conceptualisation of the Foreign Account Tax Compliance Act (FATCA), which sought to prevent US authorities from seeing information that they would be obliged to share with foreign tax authorities about deposits in the USA.

Tax competition includes not only competition on rates but also attempts to give preferential treatment to foreigners, including by providing financial secrecy

For smaller conduit havens, the benefits are even less clear, as simply being a nominal paper or electronic destination generates few jobs, skills or revenues.

Public institutions must also comply with AMLD regulations

Official bodies, including public banks at the national and especially multilateral level, might not be subject to effective oversight. There is a major question about whether EU institutions and multilateral banks are regulated under the current EU directive. This is especially important for the European Investment Bank (EIB), where the EU member states are the shareholders[101] and the European Bank for Reconstruction and Development (EBRD), in which the EU has shares."[102] Questions have been raised about the EBRD's due diligence following its funding of projects in Serbia and Slovenia, which have been the subject of corruption investigations.[103] The case detailed on page 9 of the EIB supporting a financial institution that was used as a money laundering vehicle, suggests the bank's due diligence was inadequate, and its disregard for whistleblowers and their concerns are also disturbing. Similar concerns have been raised in relation to EBRD subsidiaries.[104] The FATF and EU standards make clear that suspected customers should not be informed that they are at risk of detection: it would appear the EIB breached this duty. However, the FATF standards and EU directive should pay more attention to more sinister cases and explicitly set out whistle-blower protection measures.

Central Banks must also implement the AMLD framework, as they sometimes carry out key functions, including accepting deposits on behalf of foreign banks (known as correspondent banking). Global Witness found that the French Central Bank was used in this way to transfer money abroad for the son of Equatorial Guinea's President Obiang.

and not subjecting tax and financial crimes committed abroad to the same AML provisions, cross-border enforcement or information sharing with other jurisdictions.

Latecomers are still joining the race to the bottom; welcoming tax evaders from abroad, whilst at the same time clutching in the dark for their own lost billions and those that took them. This encourages financial imbalances and instability, whilst in the countries that are winning this race, finance grows mightier and less footloose parts of their economies whither.

However, existing financial centres have major comparative strengths, such as a strong rule of law, which would only be enhanced by stronger standards. New York, Switzerland and London have continued to attract vast amounts of business despite increased regulation following the financial crisis. If stronger due diligence standards were adopted, these centres would still be attractive to foreigners, but it would compel them to declare this income and be taxed on it in their home countries.

Conversely, comparative advantage gained through increasing secrecy or cutting regulations will not be permanent: the growth of offshore finance in other locations like Singapore, Macau and Mauritius could replace existing financial centres. Some Northern governments are concerned that they may speed up this process by putting in place rigorous standards.

The economic benefits of becoming a tax haven are likely to be small, and may be negative. The most recent World Investment Report by the UN Conference on Trade and Development (UNCTAD) – has found that countries gain little benefit from foreign direct investment (FDI) through being tax havens:

"...a group of economies with a significant presence of ... [trans-national corporations] ... receives a below-average contribution of FDI in terms of the Index indicators. This group includes a number of economies that attract investment largely owing to their fiscal or corporate governance regimes (including tax havens and countries that allow special-purpose vehicles or other corporate governance structures favoured by investors, such as Luxembourg and the Netherlands). Such regimes obviously lead to investment that has little impact in terms of local value added or employment." [106]

For smaller conduit havens, the benefits are even less clear, as simply being a nominal paper or electronic destination generates few jobs, skills or revenues. Equally, becoming a money laundering centre has its own risks. It encourages weak oversight and cultivated ignorance, meaning integrity breaks down, often leading to banking crises, up to and including the bank's own staff defrauding it to the point of bankruptcy.[107] Officials in developing countries like Ghana should note this when considering development as an offshore financial centre, and instead concentrate on adding value and winning customers through good regulation and a reputation for integrity.

A staggering example is the Dutch trust industry, which employs just 2,000 people. The conduit business in Holland creates inflows and corresponding outflows so large – 10 times the size of Gross National Product (GNP) in 2009 – that the central bank had to separate out such flows from trade that involves economic substance in the Netherlands in its public statistics.[108]

However, financial professions and firms form a powerful interest group within states, blocking reform. James Henry of the Tax Justice Network estimates the global tax evasion industry centred on private banking employs one million people worldwide. The hubs of this activity are private banks or private banking arms of financial groups. It also reflects vested interests in the tax evasion and money laundering economy from politicians and regulators who see themselves as champions of the service industries that they are supposed to be overseeing. Bureaucrats and legislators frequently come and go through the revolving door between government and these businesses.[109] Such industries regularly make large contributions to political parties.[110] However, the financial sector is not a monolithic entity: different actors and sections have different interests. Indeed, many banks support beneficial ownership registries to make compliance with customer due diligence easier.[111]

Countries that aim to attract these kinds of illicit inflows, or turn a blind eye to them, are undermining development by leaving their financial systems wide open to tax evaded income and other laundered money from the global South. This activity mainly benefits a small interest group, and is almost certainly detrimental to the broader public interest in these countries. Lax financial regulation, manipulation of chains of legal structures, and tax evasion has all played a significant role in the financial crisis. The effect of the crisis is still being felt in many of the destination tax havens of the developed world and the power of these interest groups is a major reason why this problem escalated and has not been satisfactorily addressed.

Chapter 6

Political processes and opportunities to tackle hidden ownership and tax-related money laundering

Opportunities related to anti-money laundering standards

The transposition of FATF anti-money laundering is the largest political opportunity for change. However, progress must be fought for.

FATF transposition is taking place in 180 jurisdictions around the globe.[112] FATF standards are non-binding and leave much leeway for interpretation. This often leads to weak standards at a national level, but it also means that countries can update and strengthen their interpretation of any aspect at any time.

However, FATF transposition provides a 'moment for change', as it creates international pressure on countries whose standards are lagging. It also helps to create momentum as countries see benefits when their good practices are reciprocated, and helps to assuage concerns about any perceived competitive disadvantage that could be created by strong standards.

This provides progressive governments, civil society advocates and responsible finance institutions with the opportunity to call for stronger standards: beneficial ownership disclosure; making tax crimes a predicate offence; and ensuring proper enforcement and cooperation. These key steps would help to prevent tax evasion and other illicit capital flight from developing countries committed by wealthy individuals and to a lesser extent corporations as well as deterring the accomplices – the tax planning professionals who enable this pernicious process.

The EU's approach is crucial

At the EU level, the Directorate General for Internal Market and Services (DG MARKT) is in charge of drafting a new proposed directive that is scheduled to come out in early 2013. This will first be agreed with heads of other commission departments who will also offer input, before being discussed by the European Parliament and member states.

The European Parliament has expressed a clear desire for tougher rules. A resolution in September 2011 on combatting corruption contained the following statement:

"[The parliament] calls on the Commission to make the fight against the abuse of anonymous shell companies in secrecy jurisdictions, enabling criminal financial flows, a key element of the upcoming reform of the *Anti-Money Laundering (AML) Directive."*[113]

In a further resolution on 19 April 2012 on tax dodging, the Parliament noted that:

"...strengthening the regulation of, and transparency as regards, company registries and registers of trust is a prerequisite for dealing with tax avoidance."[114]

In July 2012, the French Senate published a report based on the findings of the inquiry commission on tax avoidance, which recommended European registers for bank accounts and secrecy vehicles, it stated that the EU should *"Introduce a European register for trusts and other secrecy entities"* and "*Create a European list of bank accounts on the model of the French FICOBA"*. It is also worth noting that the AMLD sets a minimum standard but does not preclude countries from putting in place stricter measures including on beneficial ownership disclosure.

A strong EU directive would have clear implications for the European tax havens outside the EU, including the UK's crown dependencies and overseas territories (OTs).

The three European Economic Area (EEA) members Norway, Liechtenstein and Iceland, would generally be expected to transpose EU Internal Market regulations such as the AMLD. The UK's crown dependencies and overseas territories could also be pressured to implement the measures proposed in the next EU AMLD. There are three British Crown Dependencies: Jersey where trusts manage US$300-400 billion[115] as well as Guernsey and the Isle of Man. Of the 14 British Overseas Territories, seven are secrecy jurisdictions according to the FSI: Anguilla, Bermuda, British Virgin Islands, Cayman Islands, Gibraltar, Montserrat, and Turks and Caicos[116] [117]. These jurisdictions are also crucial players in global money laundering and tax dodging.

The idea that the UK has no control over them is simply untrue. Not only was the UK obliged to join the European Savings Tax Directive, which mandates automatic information exchange in certain contexts, but also self-rule in Turks and Caicos was suspended in August 2009 due to corruption.[118] Whilst this was a particularly stark case, this shows that the British government has the power to intervene to prevent corruption and other malpractice. According to the OECD:

"...the UK can and has extended international treaties to OTs [Overseas Territories] and enacted legislation in these territories over their objection. As recently as 2000, the UK exercised these powers to enact legislation in the OTs to ensure their compliance with international human rights conventions. The UK government intervened after the OTs were given an opportunity to adopt the necessary legislation themselves. After the Phase 3 on-site visit, the UK acknowledged that – from a constitutional perspective the UK has unlimited power to legislate for the OTs... the UK stated that it may be a matter of good policy and administration to consult the OTs rather than legislate directly."[119]

More recently it appears that the UK government's position is that it will not allow the Crown Dependencies to sign an information exchange agreement with the USA unless the same level of information exchange is provided to the UK, including information on those behind bank accounts owned for trusts or companies.[120]

The next review of these territories should consider harmonising their money laundering, financial regulation and accounting standards with the United Kingdom's. Considering the role they played in the financial crisis, it should also consider the costs and benefits to the UK, including the considerable indirect impact from their effects on global economic stability and global security, of the existing arrangements. Financial services and fiscal systems should be at the heart of this review. Thus far there has been no political will to do this in the UK context, but it will not necessarily be the case as public opinion is becoming more fully sensitised to this issue. Ultimately, if a territory disagrees with such reforms, they can hold a referendum with a choice between reform or secession.

The savings tax directive has shown the pressure that the EU can put on third countries, especially those in Western Europe that are closely linked to the EU. A strong revision of the anti-money laundering directive by the EU will put pressure on Switzerland, San Marino and Andorra to move towards better standards. There are also eight FATF style regional bodies.[121] Their role is limited to coordinating mutual

evaluations of their members. However, this is a process that would be worth improving.

Banks support public beneficial ownership registries as part of the AMLD

The European Banking Federation (EBF) who represent some 5000 European banks in the EU and European Free Trade Association (EFTA) countries support public registries of beneficial ownership information at least for companies. This quote from their submission to the EC consultation on the revision of the AMLD is worth quoting at length.

"The EBF [European Banking Federation] regards the inclusion of harmonized, reliable, transparent, detailed, updated and relevant shareholding as well as BO [Beneficial Ownership] information concerning non-listed companies in public registries as imperative if credit and financial institutions are expected to discharge their obligations concerning BO identification pursuant to the 3. Directive in a manner that ensures high standards of integrity of the CDD process of credit and financial institutions provides them with the required legal certainty and is truly consistent with the risk-based approach."

"The EBF furthermore suggests that the Commission should also explore options to introduce corresponding changes to the company law regime of the EU which would include formal cooperation and reporting obligations for non-listed companies to furnish/submit the relevant information mentioned above to the public registries and to keep them updated as a result of changes that may occur within the company from time to time. Moreover, the cooperation and reporting obligations should be valid for all companies and enforced irrespective of specific legal forms provided by the company law regimes of the Member States."[122]

Other opportunities in Europe and around the globe

Draft EU/Liechtenstein agreement on anti-fraud and tax cooperation matters

This agreement is currently languishing in the EU council after Luxembourg and Austria objected to it. The agreement also covers administrative cooperation in tax matters. It requires that information requests cannot be refused simply because the information is held by a bank or an anonymous investment vehicle. It also provides a good definition of tax crimes, recognising all intentional underpayment of tax.[123][124] As it is reciprocal, if this were passed it would amount to tacit acceptance of these standards within the EU, requiring internal reforms by member states, including Austria and Luxembourg. They also have forms of bank secrecy, which probably explains their opposition. If this deal is ratified, negotiations will begin with Andorra, Monaco, San Marino and Switzerland.[125]

USA – Money Laundering review and executive support for ownership transparency

On 12 November 2012 the US administration announced that it would undertake a holistic review of the USA's money laundering standards.[126] It is likely that this is partly a response to various high-profile money laundering scandals in the last year including scandals involving HSBC, JPMorgan Chase and Citibank.[127]

There is also a bipartisan bill, proposed by Senators Levin and Grassley, called the Incorporation Transparency and Law Enforcement Assistance Act, which would mandate beneficial ownership disclosure. This is especially important, as the USA hosts a vast number of shell companies, and the states of Delaware, Wyoming and Nevada have some of the weakest transparency standards.[128]

In some parts of the US government, there is a real appetite to tackle this issue. The US Treasury and Fincen (the USA's FIU) are developing a new rule requiring more thorough due diligence by banks when dealing with accounts held by opaque legal structures. They will also champion federal legislation to prevent shell companies being set up anonymously, and support similar reforms around the world. The new head of the FIU has named the use of anonymous entities by money launderers as the main challenge facing the unit.[129]

US President Obama agreed to advocate for beneficial ownership disclosure under the Open Government Initiative.[130] The initiative encourages governments to sign up to transparency commitments, with civil society groups reviewing their implementation. The USA's anti money laundering review will also be crucial, considering it does not recognise foreign tax crimes as a predicate offence.

G20: In Seoul in 2010 The G20 Anti-Corruption Working Group committed to:

"prevent corrupt officials from accessing the global financial system and from laundering their proceeds of corruption, we call upon the G20 to further strengthen its effort to prevent and combat money laundering, and invite the Financial Action Task Force (FATF) to continue to emphasize the anti-corruption agenda as we urged in Pittsburgh and report back to us in France on its work to: continue to identify and engage those jurisdictions with strategic Anti-Money Laundering/ Counter-Financing of Terrorism (AML/CFT) deficiencies; and update and implement the FATF standards calling for transparency of cross-border wires, beneficial ownership, customer due diligence, and due diligence for 'politically exposed persons'."[131]

The G20 states also committed to:

- implement whistle-blower protection rules by the end of 2012
- sign the UN Convention Against Corruption (UNCAC) convention (see below)
- improve mutual legal assistance
- Improve recovery and repatriation of assets.

UN Convention Against Corruption (UNCAC)

While FATF can only issue recommendations, and the G20 Action Plan is voluntary for its members, the UN Convention Against Corruption (UNCAC) is legally binding and has the force of international law. Therefore, states have an obligation to comply with various UNCAC articles on money laundering and proceeds of crime. Article 52 of UNCAC is based on the FATF recommendation. It mandates states to require financial institutions within its jurisdictions to identify beneficial owners. There is now a four-year review process of how countries comply with the UNCAC. This is likely to show that there has been practically no movement by states to require their financial institutions to identify beneficial owners. It also calls for full mutual legal assistance and proportionate and dissuasive sanctions for failure to comply with anti-corruption or accounting standards.[132]

"The EBF [European Banking Federation] regards the inclusion of harmonized, reliable, transparent, detailed, updated and relevant shareholding as well as BO [Beneficial Ownership] information concerning non-listed companies in public registries as imperative if credit and financial institutions are expected to discharge their obligations."

Conclusions and recommendations

Tax evasion has already cost developing countries trillions of dollars and has locked many in a debt trap. Every year, hundreds of billions more dollars go missing. Tax evasion is a collective actor problem, in which most states are simultaneously victims and abusers: international cooperation must break this destructive cycle.

Making sure that banks identify who they are doing business with in the EU and other developed countries would force individuals to choose between declaring their income properly or losing their access to invest, save or spend their money in these countries. Revealing the hidden owners and controllers of bank accounts, trusts, companies and other such structures would be a hugely important step towards addressing tax evasion and bringing offshore wealth back into the tax net. Transparency of beneficial ownership would remove a cloak that makes tax evasion and myriad other crimes possible and profitable.

However, beneficial ownership disclosure is not a silver bullet: it is a crucial part of the package of measures needed to reduce tax evasion at a global level. Momentum is building for two other measures, notably country-by-country reporting and automatic information exchange, but there would be many circumstances where information exchange could be undermined with opaque legal structures.

These concrete measures go hand in hand with a shift in philosophy, largely brought about by the financial crisis, which recognises that cut-throat tax competition and financial secrecy are major flaws in the global economy.

The transposition of the new FATF anti-money laundering standards into law provides opportunities which cannot be missed. This is a chance to regulate the tax planning industry as well as deterring individual tax evaders. Identification and disclosure of beneficial ownership and tax crimes as a predicate offence of money laundering must be set into concrete laws, which must be properly enforced and complied with. It is crucial that information sharing and judicial and administrative cooperation are improved to address cross border tax evasion.

The following comprehensive package of recommendations is realistic and in line with FATF standards. If implemented, they would strike a major blow against destructive tax evasion.

Recommendations

Ensure full beneficial ownership disclosure and prevent misuse of legal structures

Register all legal structures and their beneficial ownership information. Information about all forms of legal structure should be collected and verified by national authorities as a condition of establishing the structure in that jurisdiction. In the case of legal structures such as trusts and foundations, these should be required to register in any country where there is a bank account in the name of the arrangement. The names of fiduciaries and settlors should also be reported. This is especially important for discretionary structures with no predetermined beneficiary.

Publish all legal structure ownership and control records online, available without charge. The information should be published, for free, online, electronically tagged and in a searchable format.

Ensure definitions of beneficial ownership include both control and ownership. For taxation purposes, it is essential to know which taxpayer will receive the income or assets so they can be taxed accordingly. For anti-money laundering purposes, it is important to know who is in control. Identifying either ownership or control is not good enough.

There could be an exemption when it comes to identifying the beneficial owners for shares that are traded on a reputable exchange or state-owned enterprises. However, managers might be engaging in tax evasion or money laundering, so the managers of the relevant subsidiary should be identified. For the subsidiary of multinational companies, which can be part of a chain of companies, it is important to establish the direct parent company and also the ultimate parent company.

Legal structures such as trusts and foundations should be required to publish accounts in each country where they have a fiduciary or bank account. This is especially important for discretionary trusts and foundations. Accounts should disclose all payees. This should apply to trusts that either hold above €100,000 in assets or make aggregate annual payments of €15,000 or more.

Introduce substance requirements: companies with no meaningful staff or sales in a country should be made to close. To prevent the use of an artificial legal presence in lax jurisdictions to get around money laundering rules, moves should be made to close companies that have no staff or sales in a particular country. Countries could consider measures to preclude trade with conduit vehicles in other countries and require trade and transactions to take place directly between firms or subsidiaries where economic substance takes place. Holding companies should be based in a country where one of their subsidiaries has a substantial economic presence.

Disclose trading addresses. As a minimum, the actual place of doing business should be disclosed, because it is an indicator of AML risk and also useful for law enforcement and stolen asset recovery practitioners.

In the absence of public registries nominees should be compelled to always collect beneficial owner(s) details. TCSPs should be licensed and required to record beneficial ownership information. This information should ideally be put on public record and published. They should be subject to random checks to make sure that this is done, and lose their license to operate if they fail to do so, regardless of whether money laundering has occurred as a result of their negligence.

Additionally, nominees (whether shareholders or officers) should always be flagged as such in the company registration and other official documents as they are a key indicator of money laundering risk. Failing to declare that you are a nominee should result in sanctions. This would not prevent nominees from posing as the real owner but would make it much harder for anyone to provide nominee services on an industrial scale to hundreds of companies. Nominee officers must be held liable for their companies' conduct in the same way as other company officers. Corporate directors, whether nominees or not, should be held responsible if they fail to take adequate measures to prevent money laundering.

Corporate company officers should not be permitted. A real person, not a legally constructed person, is needed to perform the oversight functions that ensure good corporate governance.

Governments should consider limiting the number of circumstances where nominee company officers are permitted. Failing this, nominees should be held to account for their companies' activities.

Recommendations

Introduce effective due diligence standards

Ensure verification of beneficial ownership by covered institutions. CIs should always have to verify the identity of the beneficial owner(s) before making a decision about the degree of further due diligence needed. When the beneficial owner cannot be verified, the business should be rejected and authorities should be tipped off.

Make all due diligence requirements on-going for the duration of the business relationship rather than one-off.

Make tax crimes a predicate offence

Both foreign and domestic tax crimes should be made a predicate offence of money laundering.

Tax crimes should be framed so as to recognise all deliberate attempts by a taxpayer to pay less than their legal obligations. This should apply to all direct and indirect taxes. The following definition proposed by Tax Research UK would be particularly difficult to circumvent.

"Any deliberate act that results in tax not being paid on an economic event whose substance occurs within a jurisdiction contrary to the law of the jurisdiction where that economic event either occurs or is recorded or that results in tax not being paid contrary to the laws of the jurisdiction in which a benefit of that economic event arises."

Jurisdictions should cooperate on tax matters in the absence of dual criminality. For example this would involve Jurisdiction A cooperating with Jurisdiction B to address tax crimes that took place in Jurisdiction B but are laundered through Jurisdiction A, even if Jurisdiction A does not recognise those crimes under domestic law. At the very least jurisdictions should include crimes which are broadly similar in their interpretation of dual criminality. At the very least jurisdictions should include crimes which are broadly similar in their interpretation of dual criminality.

Ensure effective compliance, enforcement and cooperation

Tougher sanctions are needed, to influence CIs' cost benefit analysis. The possibility of revoking the licenses of institutions that are seriously implicated in money laundering should be considered. Equally, prosecutions should be brought against the individuals involved.

Regulators should study individual cases and carry out random undercover checks, as well as looking at actors' overall compliance procedures. More attention should be paid to accountants, lawyers and trust and company service providers.

Jurisdictions should actively detect the proceeds of foreign crimes, share information spontaneously, and cooperate with requests for assistance.

Improve FATF mutual evaluations. Recommendation 24, which relates to transparency and beneficial ownership of legal persons (companies), and Recommendation 25, which covers transparency and beneficial ownership of legal arrangements (for example trusts), should become main assessment criteria. Equally, peer reviews by other countries should be used to hold countries to account for their international cooperation. For each of the mutual evaluation criteria, separate consideration should be given to legal frameworks and to implementation and effectiveness.

Ensure oversight of multilateral organisations. International organisations, especially publicly owned banks, pose similar AML risk to other financial institutions. An independent regulator should monitor their compliance

Collection and publication of statistics

Make detailed and disaggregated official data on money laundering publicly available. Authorities should keep and publicise disaggregated records on SARs received, noting how many related to inter alia: fiscal crimes; corruption; organised crime; and terrorist financing. The same should apply to confiscated proceeds, including confiscated proceeds returned to other jurisdictions. Foreign and domestic crimes should be tagged to allow further disaggregation.

Make detailed and disaggregated official data on cross border flows and stocks publically available. At the macro level, countries and International Financial Institutions (IFIs) should record and publish more information on cross-border flows and bank and non-bank deposits.

Banks should describe their AML compliance measures in their annual reports and provide some detailed indicators including number of SARs filed, number of PEP clients, and amount of assets frozen (disaggregated for type of predicate offence).

Appendix 1: Global Financial Integrity estimates of privately held non-resident deposits in secrecy jurisdictions[133]

Rank	Secrecy Jurisdiction	2002	2003	2004	2005	2006	2007	2008*
1	United States	1,248,069	1,242,742	1,411,348	1,603,469	2,033,727	2,599,837	2,114,546
2	United Kingdom	692,745	769,367	998,932	1,033,344	1,419,931	1,938,743	1,433,926
3	Cayman Islands	533,204	754,002	962,317	898,190	1,264,978	1,341,012	1,684,780
4	Switzerland	176,151	219,580	196,954	199,125	301,777	543,136	235,166
5	Luxembourg	185,012	269,053	325,563	305,213	355,656	500,104	456,133
6	Germany	175,003	190,016	198,574	191,257	299,013	490,843	427,782
7	Jersey	185,067	224,551	251,724	264,075	350,463	408,174	367,103
8	Netherlands	184,164	233,837	226,506	214,685	330,643	398,342	347,575
9	Hong Kong SAR	158,065	175,893	221,804	214,021	259,064	343,262	315,974
10	Bahamas	165,089	176,366	236,842	242,855	268,035	261,354	367,369
11	Singapore	100,612	100,557	123,249	120,623	161,271	210,783	210,055
12	Russia	23,371	32,978	48,597	90,662	124,818	185,299	653
13	Japan†	77,113	93,865	130,394	92,193	114,888	182,215	...
14	Guernsey	53,512	72,571	77,835	99,944	124,660	129,240	147,677
15	Spain	39,571	50,177	45,138	52,430	86,885	117,979	71,714
16	Netherlands Antilles*	67,373	73,336	74,803	81,444	93,993	107,376	107,143
17	Belgium	45,600	55,360	62,180	51,077	76,653	90,021	72,055
18	Panama	36,538	39,726	50,346	56,047	69,100	85,198	96,786
19	Ireland	19,170	30,796	36,726	45,003	63,617	73,841	286,067
20	Bermuda	31,647	41,952	90,367	55,946	72,348	71,447	41,275
21	Isle of Man	27,367	35,326	40,611	41,204	58,972	66,994	76,490
22	Taiwan	33,624	44,333	52,045	48,208	51,340	65,394	65,091
23	Italy	52,988	42,986	49,762	38,225	56,554	57,307	32,337
24	United Arab Emirates	29,739	29,193	29,193	37,899	61,908	54,364	47,530
25	Portugal	12,671	15,601	15,634	17,281	30,129	34,497	19,982
26	Cyprus	7,258	9,695	18,173	18,576	22,871	32,860	37,192
27	Israel	12,348	14,817	17,124	19,814	29,040	29,610	16,649
28	Liechtenstein	17,670	18,534	19,137	19,242	23,980	28,064	25,508
29	South Africa	8,005	11,617	14,225	15,955	21,131	26,730	16,194
30	Malaysia	7,273	7,535	15,155	6,643	13,177	22,180	5,926
31	Lebanon	11,649	16,967	18,678	17,140	19,124	21,419	20,523
32	Monaco	15,414	15,414	15,414	14,495	20,500	20,500	...
33	Barbados	3,547	6,289	8,747	8,742	24,915	19,622	9,578

* Netherlands Antilles was dissolved in 2010

Secrecy Jurisdictions for which no data was available: Northern Mariana Islands, San Marino, Sao Tome e Principe, Somalia, Tonga and US Virgin Islands
*Represents preliminary data
†Japan is not defined as a secrecy jurisdiction
These countries are ranked by magnitude of deposits in 2007
http://www.gfintegrity.org/storage/gfip/documents/reports/gfi_privatelyheld_web.pdf

Rank	Secrecy Jurisdiction	2002	2003	2004	2005	2006	2007	2008*
34	Liberia	6,951	8,946	18,097	14,433	16,152	17,692	17,968
35	Gibraltar	5,342	6,375	6,900	9,608	23,046	17,020	12,324
36	Mauritius	2,577	3,654	5,374	5,192	11,140	16,651	11,095
37	Macao SAR	4,975	5,494	6,818	9,557	13,190	16,247	19,020
38	Uruguay	4,897	5,841	5,838	6,240	6,679	10,552	8,055
39	Marshall Islands	398	1,344	2,315	3,941	5,192	8,235	7,034
40	Malta	2,464	2,733	3,365	3,217	8,488	7,862	12,502
41	Dublin	6,554	6,429	7,697	9,282	6,861	7,821	–
42	Hungary	2,024	2,755	3,192	4,866	5,334	7,738	4,250
43	Belize	1,655	2,117	2,259	4,278	5,938	6,716	9,575
44	Antigua and Barbuda	1,497	2,421	3,344	4,267	5,190	6,113	–
45	Bahrain	1,735	3,002	6,135	4,051	6,358	5,427	4,674
46	Andorra	3,758	3,908	5,241	4,097	4,437	4,547	5,839
47	Costa Rica	2,593	1,177	1,643	1,773	4,059	4,456	3,460
48	Samoa	873	890	1,649	2,445	3,672	4,185	6,584
49	Iceland	259	475	707	1,609	4,672	3,565	-919
50	St. Vincent	932	839	1,336	1,446	3,803	3,246	3,089
51	Seychelles	198	301	432	1,315	2,000	2,721	4,330
52	Aruba	920	811	760	698	1,132	1,389	1,353
53	British Virgin Islands	3,357	2,937	2,517	2,097	1,677	1,257	–
54	St. Kitts and Nevis	143	372	387	755	845	1,036	–
55	Montserrat	765	765	805	805	805	805	–
56	Vanuatu	1,196	565	588	675	725	800	296
57	Anguilla	146	178	209	241	273	304	–
58	St. Lucia	71	56	314	217	278	291	468
59	Dominica	141	47	3	20	109	257	134
60	Turks and Caicos Islands	257	257	257	257	257	257	–
61	Maldives	39	31	54	58	100	123	88
62	Grenada	60	30	60	61	45	66	171
63	Niue	19	19	19	19	19	19	–
64	Cook Islands	19	19	19	19	19	19	–
65	Nauru	35	28	11	898	12	10	-5
66	Palau	1	0	0	1	7	6	–

Appendix 2: Does the Jurisdiction together with banks, control or monitor the flow of currency and monetary instruments crossing its borders?

Yes				No	
Antigua & Barbuda	Costa Rica	Israel	Samoa	Andorra	Macau
Austria	Cyprus	Italy	San Marino	Anguilla	Maldives
Bahamas	Denmark	Japan	Singapore	Brunei	Marshall Islands
Bahrain	Dominica	Korea	Spain	Gibraltar	Mauritius
Barbados	France	Latvia	St Kitts and Nevis	Grenada	Montserrat
Belgium	Germany	Liberia	St Lucia	Hong Kong	Nauru
Belize	Ghana	Malaysia (Labuan)	St Vincent & Grenadines	Jersey	Seychelles
Bermuda	Guatemala	Malta	United Arab Emirates (Dubai)	Lebanon	Switzerland
Botswana	Guernsey	Monaco	United Kingdom	Liechtenstein	
British Virgin Islands	Hungary	Netherlands	Uruguay	Luxembourg	
Canada	India	Panama	US Virgin Islands		
Cayman Islands	Ireland	Philippines	USA		
Cook Islands	Isle of Man	Portugal (Madeira)	Vanuatu		

Appendix 3: Amount of assets frozen as a result of money laundering investigations

Country	Amount in Local currency or US Dollars	Currency and Year	In US$[134]
USA	2,000,000,000	2006	2,000,000,000
Hong Kong	324,200,000	USD (2009)	324,200,000
Germany	304,479,701	2007 (USD)	304,479,701
United Kingdom	250,000,000	2006 (USD)	250,000,000
Korea	163,562,900,000	2007 (KRW)	181,569,620
Austria	100,000,000	2007 (EUR)	144,606,069
Italy	112,030,844	2003 (EUR)	130,121,262
Belgium	56,039,846	2003 (EUR)	65,088,999
Macau	456,000,000	2007 (MOP)	57,119,448
Spain	35,791,444	2004 (EUR)	45,587,698
Jersey	27,434,989	2009 (GBP)	45,322,797
Panama	41,000,000	2010 (USD)	41,000,000
Luxembourg	26,800,000	2010 (EUR)	37,372,600
Japan	33,000,000	2009 (USD)	33,000,000
Netherlands	23,500,000	2008 (EUR)	29,796,896
Canada	31,400,000	2006-7 (CAD)	26,936,605
Monaco	11,700,000	2006 (EUR)	14,942,898
Latvia	6,500,000	2007 (LVL)	13,374,133
Denmark	9,800,000	2005 (EUR)	11,754,019
Singapore	10,962,377	2008 (USD)	10,962,377
Israel	9,000,000	2007 (USD)	9,000,000
India	424,400,000	2008/09 (INR)	8,704,492
Cyprus	5,500,000	2009 (EUR)	8,140,000
St Vincent & Grenadines	7,744,109	2009 (USD)	7,744,109
Cayman Islands	6,000,000	2010 (USD)	6,000,000
Hungary	5,500,000	2007 (USD)	5,500,000
Malta	2,670,811	2009 (EUR)	3,952,800
Malaysia (Labuan)	10,776,000	2006 (Ringgit - MYR)	2,950,149
Portugal (Madeira)	2,390,000	2010 (USD)	2,390,000
Ireland	1,350,000	2009 (EUR)	1,998,000
Uruguay	1,400,000	2007 (USD)	1,400,000
San Marino	685,441	2008 (EUR)	869,107
Bermuda	350,000	2010 (USD)	350,000
Antigua & Barbuda	14,753	2007 (USD)	14,753

Appendix 4: Number of Suspicious Activity Reports (SARS) received in a selection of jurisdictions

Jurisdiction	Number of SARs	Year
USA	600000	2006
Japan	272325	2009
United Kingdom	213561	2006
Netherlands	54605	2008
Korea	52474	2007
Latvia	27000	2006
France	17310	2009
Belgium	15554	2008
Ireland	14500	2009
Italy	14241	2008
Hong Kong	13553	2009
Singapore	11004	2009
Israel	10597	2007
Portugal (Madeira)	8470	2010
Germany	7349	2008
Malaysia (Labuan)	4186	2006
Spain	2904	2008
Denmark	2095	2009
Jersey	1859	2009
Isle of Man	1561	2007
Austria	1385	2009

Jurisdiction	Number of SARs	Year
Panama	944	2009
Switzerland	896	2009
Luxembourg	754	2006
Macau	725	2007
Guernsey	539	2007
Cyprus	428	2009
Monaco	395	2006
Guatemala	330	2008
Costa Rica	280	2007
British Virgin Islands	191	2010
Uruguay	174	2007
Liechtenstein	163	2006
San Marino	110	2008
Gibraltar	100	2007
Botswana	99	2006
St Kitts and Nevis	96	2007
Antigua & Barbuda	52	2006
Belize	38	2007
Grenada	25	2007
Dominica	17	2007
Montserrat	2	2007

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