



The world of Offshore Financial Centers

And the role of the EU in it

Giacomo Rigon

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<p>Abstract: The subject of the thesis is the world of the offshore financial centers in the global economy, understanding which services are offered by main OFCs and the kind and size of the business relationship they have established with companies and individuals all around the world. However, the main issue is the role that the EU plays in the OFCs world, both concerning policymaking and concerning involvement as active player. This is achieved by the thesis based on what is available in the current academic literature, on the raw data published by influential institutions and on the estimates made by professional and experts of the subject. The material used is mainly academic textbooks for the basic concepts and secondary data sources like academic publications, financial and economic journals and statistical data, but also EU institutional papers, IMF reports, the Panama Papers and other thesis, in order to get legal, political, financial and overview information. The main result and conclusion is expected to be giving complete a panoramic outline of services and financial estimates but mainly to confirm the deeply rooted participation of the EU in the phenomenon.</p>	
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1 RESEARCH TOPIC

1.1 Introduction

An offshore financial center (OFC) can't be defined through a single characteristic but it involves a sum of aspects: starting from a primary orientation of business towards nonresidents, a favorable regulatory environment, a low or zero taxation scheme but also a disproportion between the size of the financial sector and the domestic needs, the dealing in currencies that are not the currency of the country where the center is located, the fact of being a center separated from major regulating units (states) and last but not least the offshore banking activities are essentially an entrepot business.

Basically there are four essential uses for OFCs locations. To start with, they are utilized by those wishing to avoid or dodge their commitment to pay taxes. Tax avoidance is legal, however outside the soul of tax assessment law, while tax evasion is dependably an illegal action including the non-exposure of a financial gain to a fiscal authority that has a lawful right to be informed about it.

Second, they are utilized to conceal criminal exercises from view. That criminal action may be tax evasion itself, however may likewise be money laundering or wrongdoings producing money that should be cleaned up like burglary, extortion, defilement, insider trading, robbery, financing of terrorism, drugs dealing, human trafficking, frauds, kidnapping and blackmailing.

Third, they are utilized by the individuals who need their exercises to be unknown, regardless of the possibility that they are totally within the legitimate borders. A few people wish to conceal their wealth from their partners, for instance; others might need to hide businesses which, however legal, may ruin their public image.

Fourth, they are utilized by those looking for some place less expensive to do business; in these areas they can often keep away from the exorbitant commitment and expenses connected to regulations and laws that would be applied if the exchange were attempted on onshore territories.

Offshore finance is a significant theme since it is a sector that has expanded extensively since the 1970s and it has become of common interest lately thanks to new sources of information in the matter like Panama Papers and LuxLeaks, that will both be used later on in this thesis. Anyway for the lion's share of banks and an increasing number of organizations, the utilization of offshore jurisdictions has a tendency to be the habit instead of the special case. Offshore economies are not just huge on account of their size; they exemplify a parallel arrangement of economic principles utilized by business and financial elites to dodge rules on money related laws and the ripartition of capitals.

1.2 Research aim

This thesis is revolving around two main research aims: the first is to synthetize the services offered by the main OFCs and the financial consequences that are generated from them. The second instead, is to investigate the relationship between the European Union and the offshore finance phenomenon.

1.3 Research questions

The research questions of the thesis are two as the aims, the first is: what are the services offered by the main OFCs and what kind of financial impact they have on the world? The second instead: what is the role played by the European Union in the offshore finance phenomenon?

1.4 Demarcation

The scope of the research is to understand the world of the OFCs and the role that the European Union has in it. The research includes an overview of which are the main tax havens, the locations and main features of the top four, according to the Panama Papers, but without getting into details in the other ones. It will face the topic of which are the services offered by OFCs to private individuals and corporations. It will also give an insight into info and data about the size of financial flows going from and through OFCs even if limited to what is available in the current academic literature and to the estimates made by professional and experts of the subject.

This paper has also a focus on the level of involvement of the EU in the offshore business and it analyses aspects such as: the advance tax ruling practices, the level of intermediation established toward OFCs, the amount of European wealth held offshore and the capital flows related, but also how some European countries can be considered OFCs based on the concept of “conduit” jurisdiction. The thesis offers a general outline on EU countries policy making related to OFCs, not getting too deep into each EU country specific regulation, instead being more a summary of the mutual aspects shared by onshore EU countries or general attitude towards the industry.

2 RESEARCH DESIGN

2.1 Material

The elements of the research that provided the data that I analyzed are mainly academic textbooks for the basic concepts that are supporting my explanations and the further information; the secondary data sources (due to the topic collecting primary data would be almost impossible for me) are mainly academic publications, financial and economic journals, statistical data and the leaking material like the Panama Papers and the Lux Leaks in order to get numerical attainments; EU institutional papers, IMF reports, ECB papers and other thesis involving the same or a similar topic to get legal, political and overview information.

2.2 Approach

The approach that it is used to answer the research questions is a descriptive desktop research with analytical and numerical foundations of pre-existing statistics, estimates and academic studies. The thesis is not based on a field research or on primary data this because it resulted to be impossible as a private individual due to the specific matter of the thesis. The innate nature of offshore finance pushes towards the use of pre-existing leaks of information or on estimates and values put together by influential institutions or professionals in the field.

The possible problems and bias regarding this approach are to be connected with the scarcity of reliable data on the topic. For example, the leaks from a single company like Mossack Fonseca (Panama Papers) can't be an accurate representation of the whole

panorama of firms worldwide working in the offshore finance field. But also in overall the total secrecy, in fact Murphy (2011) states that *“an offshore company owned by an offshore trust creates an almost impermeable barrier to inquiry”*, and non-cooperative status of some jurisdictions forces professionals to make estimates based on little information, increasing so the risk of inaccuracy of the output. Even considering these issues, the approach selected is to be regarded as the best possible since there are no other legal and reasonable ways of obtaining data on offshore finance.

2.3 Data collection

All the data comes from secondary sources so they aren't collected personally, as explained in the previous paragraph. Consequently, there was no way of influencing what kind of instruments, methods and procedures have been used in the collection. For the same reasons the data analysis techniques don't appear to be relevant as no quantitative data are involved. The main duty was to choose trustworthy and reliable data from relevant academic or institutional sources that are exactly related to be subject investigated in the research questions.

3 REVIEW OF EXISTING RESEARCH

Various researches have been produced and shared regarding the field of this thesis. Both on the OFCs world financial flows aspect and on the European Union role on it the academic community has been prolific, even if a lot of info and data is coming from the financial industry itself or from institutions like the EU or the OECD. The following part gives a brief overview of both aspects in the overlying order, with the aim of giving the reader a support in better understanding the following parts of the paper.

Regarding the type of services and financial flows generated by offshore jurisdictions there are strongly contrasting opinions. Palan, Murphy and Chavagneux (2010) clarify that while, individually tax havens may appear insignificant, together they strongly affect the world's economy. They also claim that tax havens are fundamental to the global economy, they don't just operate at their margins. OFCs are a vital part of the financial industry, especially the wealth management and investment sectors, not only conduits for tax avoidance and evasion.

Zhixiang (2008) on the other hand focuses more on the type of activities rather than the volume of financial flows. He finds a strong difference between OFCs and money laundering centers, even if sometimes the two collide, since the first attract more asset investment but on the other hand, the second scares potential investors away. This has evidence in a higher value of financial intermediation in OFCs and a lower one in the money laundering centers. The paper shows that the role of offshore havens in facilitating illegal activities has been overestimated in the previous studies. In addition, it claims that the competitive advantages in the matter have been reducing in the recent years due to global action against it.

Other authors like Henry (2012) are more number and data oriented, giving an outlook of the offshore economy as *"large enough to have a major impact on estimates of inequality of wealth and income; on estimates of national income and debt ratios; and most importantly to have very significant negative impacts on the domestic tax bases of key source countries"*, giving so a clear idea of the size of the phenomenon. The economist claims the results proposed to be only related to the financial wealth since all the other sources and forms of wealth are impossible to quantify.

Early research focused on the implications of the European Union in the offshore finance shows quite concurring opinions. For example, according to Palan (2012) the EU has a great degree of involvement in the OFCs world, and his conclusions are based on the

data from the Bank for International Settlements (2010). He argues that more than half of all international assets and liabilities are to be connected to EU countries or jurisdictions related to it.

Also Mügge (2013) considers the EU to be highly involved in the OFCs world, to a point where he argues it is the biggest player worldwide even considering the policy efforts implemented to control and avoid its negative sides. He identifies the root of the problem in different strategies from different EU countries and in the way the EU is structured and functioning.

Zucman (2013) proposes a very interesting concept according to which the western world does not really have a negative net foreign asset position, but that this deception is simply caused by tax havens. Based on his assumptions this discovery “*turns the Eurozone, officially the world’s second largest net debtor, into a net creditor*”, underlining so the massive size of the European wealth held offshore.

Fernandez (2015) while trying to address the issue of shadow banking in Europe, and in particular securitization, widely calls multiple EU countries OFCs based on the concept of conduit jurisdiction. The same word is used by Garcia-Bernardo, Fichtner, Heemskerk and Takes (2017) whose work basically demonstrate the active and main role of the EU in the offshore environment by using a data-driven approach.

Therefore, from the previous literature appears that the EU is strongly involved in the world of OFCs in multiple ways, both as a provider of offshore finance services and as the source of extremely big amounts of wealth stored in other OFCs.

4 THE MAIN OFCS AND THEIR LOCATIONS

Since there are so many OFCs and they are spread out all around the world, it might be sometimes difficult to know exactly which one of them are the most important in terms of business volume and where to locate them in a map.

Based on the Panama Papers, out of the companies that appear in Mossack Fonseca's leaks almost half of the companies, more than 113000, were incorporated in the British Virgin Islands. Instead the actual HQs location of the firm, Panama, was only second in the list (ICIJ 2016).

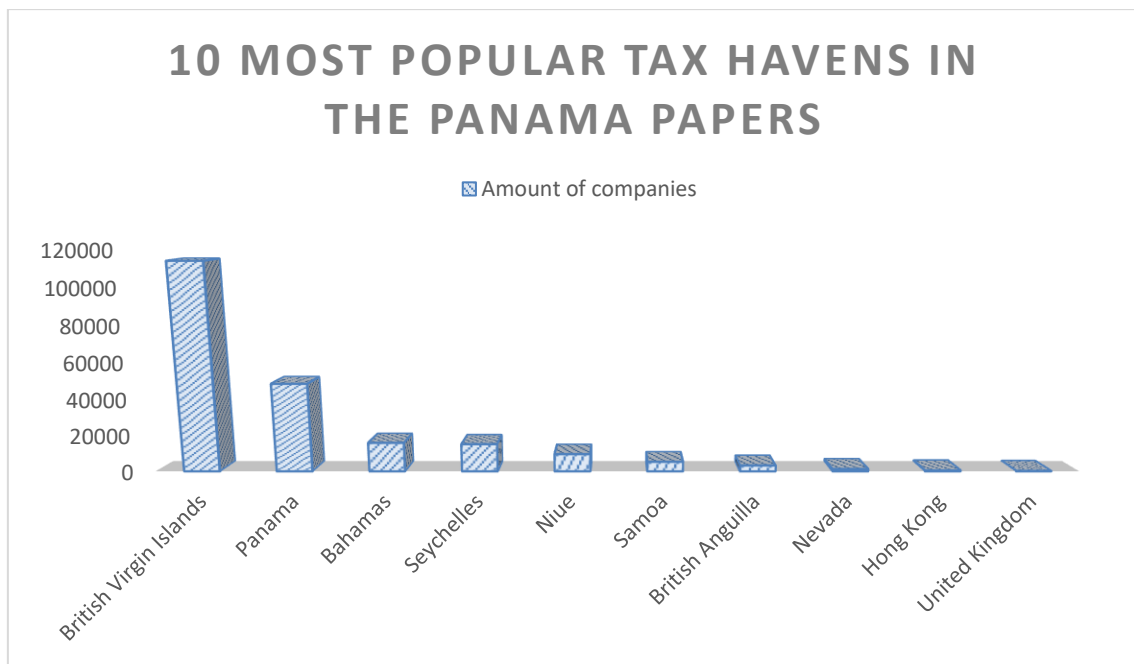


Figure 2. The 10 most popular tax havens in the Panama Papers, Source: The Panama Papers

In this part of the thesis the author is going to describe more in depth the four jurisdictions that according to the Panama Papers that had more incorporations occurring within their financial sector.

4.1 The British Virgin Islands

The British Virgin Islands are one of the best and most respected financial sectors not only in the Caribbean (they are located to the east of Puerto Rico), but on a global scale. Apart from being a modern and efficient banking system, it is also a country where the government has placed considerable focus on developing strict money laundering and tax evasion laws. Thanks to this attitude towards transparency they earned an amazing reputation in the financial community and even a spot on the OECD's white list. Since 2004, when the BVI Business Companies Act has been adopted, more than half a million firms have been incorporated on the island (Wolters Kluver 2016).

4.2 Panama

Secrecy and position, its nearness both to the homonym Canal and to the USA, are the key that sealed the success of Panama among international tax havens. The Latin jurisdiction remains a "black hole" because it does not participate in the agreements for the exchange of tax information, although it has recently expressed its intention to improve, it has a similarity to the Swiss legislation, which punishes violation of banking and financial secrecy (ISole24Ore 2016).

Significant progress has been made to strengthen financial integrity, the authorities have adopted several legislative reforms to address weaknesses in the framework for Anti-Money Laundering and Combating the Financing of Terrorism. But there is the need to continue to energetically enhance the effectiveness of the AML/CFT regime, particularly on issues of tax transparency (IMF 2016).

4.3 Bahamas

This country made of small islands is located in the Atlantic Ocean north of Cuba and southeast of the US state of Florida. It was the first nation in the Caribbean with a IOSCO

A status (“signifying the highest level of compliance with international standards for the jurisdiction’s securities regime”) that was obtained after reaching the Signatory A status under the MMoU (“an international benchmark for cross-border co-operation [...] provided securities regulators with the tools for combating cross-border fraud and misconduct that can weaken global markets and undermine investor confidence”). In addition, the country can offer complete anonymity and confidentiality to investors, exemption from local taxes and stamp duties, ease of company incorporation and the minimum requirement of just one shareholder and one director (Wolters Kluver 2016).

4.4 Seychelles

The group of islands has risen as an undeniably prominent OFC and its turning point was the boost in the 1990s with the fall of the Soviet Union. Seychelles, which is located in an archipelago in the Indian Ocean, east of mainland East Africa nearby Madagascar, is basically in the same time zone as most of the Eastern Europe, was a popular choice among the soviet elite that wanted to move capital outside the region (Sharman 2011).

The jurisdiction is strong on mutual and hedge funds, which can be created as a society, a global trust or a limited partnership. A key aspect that supported the country in becoming a relevant OFC is the position on bank secrecy. The info of people related to accounts or funds are not publicly disclosed. Furthermore, a Seychelles based international company profits of favorable starting-up expenses, the lack of local duties and no exposure of the minimum capital. It might seem that Seychelles haven't been doing what's necessary to fight money laundering. Anyway, they have expressed the will to change by attempting to enhance its legal and fiscal structure (Wolters Kluver 2016).

5 SERVICES AND LEGAL FORMS IN THE OFCS

The OFCs offer many different types of services and legal forms that attract investors in moving their capitals and businesses in one of the jurisdiction providing them. Different ones will of course be of interest to different investors according to their needs. Due to the very wide range of services offered by offshore jurisdictions, the thesis will focus in the next part simply on the main ones or the main categories, giving an explanation about what they consist of, what they are used for and other relevant aspects.

5.1 Limited liability vehicles

There are mainly two types of limited liability vehicles used in the OFCs:

1. International Business Companies (IBCs) that basically are corporations formed under the corporate legislation of a tax haven (such as Bahamas, Panama, Turks & Caicos). IBCs are not authorized to do business in the country of formation (incorporation) but can have offices that manage global operations.
2. Limited Liability Companies (LLC) that are *“a business structure allowed by state statute. Each state may use different regulations [...] Owners of an LLC are called members. Most states do not restrict ownership, and so members may include individuals, corporations, other LLCs and foreign entities. There is no maximum number of members. Most states also permit “single-member” LLCs, those having only one owner”* (IRS 2017).

5.2 Tax planning for companies and individuals

OFCs are additionally destinations for the organizations and individuals interested in tax planning. In fact, offshore jurisdictions offer structures that permit to camouflage the ownership and to stay away from property, inheritance or capital gain taxes, all within the law. In addition, the creditor's claims in the event of default are limited when an organization is located in the OFC.

There is another possible reason for the usage of OFCs regarding asset management matters, a situation when *“wealthy individuals and enterprises in countries with weak economies and fragile banking systems may want to keep assets overseas to protect them against the collapse of their domestic currencies and domestic banks, and outside the reach of existing or potential exchange controls. If these individuals also seek confidentiality, then an account in an OFC is often the vehicle of choice”* as stated by FSF’s Working Group on Offshore Financial Centers Report (2000).

5.3 Trusts and foundations

There are certain legal forms used to protect the ownership, two of the most important are trust and foundations. Trust in general is a relation between two individuals concerning ownership management. Trusts cannot be considered as companies, they can’t be sold or bought. The IRS states that *“a trust is a relationship in which one person holds title to property, subject to an obligation to keep or use the property for the benefit of another”* (IRS 2016). Instead foundations have a bit different meaning in an offshore context compared to an onshore context as they are used mainly for estate planning purposes. Quoting McCann *“although a foundation is a distinct legal entity, it has no shareholders and it is administered in accordance with contractual principles – not fiduciary principles. [...] A founder may be a real person or a corporation or a trust [...] that endows the foundation with assets, and it is then called ‘the patrimony’. Foundations may hold assets in their own name, for the purposes described in the constitutive documents. The founder is not the legal owner of the assets, and it is this separation which protects assets from potential creditors.”*

5.4 Banks and insurances

Most of the most important banking institutions have their HQs or if nothing else their branches in an OFC providing also the typical services. For example, on Cayman Islands, one of the main jurisdictions in the Caribbean, there are *“over 40 of the top 50 banks*

holding licenses here” (Cayman Islands Monetary Authority 2017). There are many reasons why it is attractive to banks and insurance companies to be offshore: obviously there are huge advantages due to no or low corporate tax, but also capital gains tax, withholding tax on dividends or interest.

Usually anyway the most relevant factor for the banking and insurance industry is the regulatory environment, as OFCs are usually way more lenient compared to onshore jurisdictions. This attitude is also often the same regarding supervision and reporting. Finally, offshore banks are as limited as if they would be onshore concerning trading.

Regarding insurance companies usually MNCs establish them in OFCs in order to protect against risk within their group or holding. Basically, the concept is that an onshore insurance company establishes a subsidiary in an OFC to reinsure certain risks underwritten by the parent and to reduce overall reserve and capital requirements, with also the goal to reinsure against catastrophic risks (Financial Stability Forum, 2000).

5.5 Investment funds

This type of services can vary considerably considering the different sub-categories but in overall *“an investment fund is a supply of capital belonging to numerous investors used to collectively purchase securities while each investor retains ownership and control of his own shares. An investment fund provides a broader selection of investment opportunities, greater management expertise and lower investment fees than investors might be able to obtain on their own”* (Investopedia 2017).

Regarding collective investment schemes the OFCs are preferred because of their low or non-existent income tax. In the table below, there are the top five countries in the Euro Area according to their amount of assets and the percentage of the total assets held by investment funds in the Euro Area in the year 2016:

Euro Area Member States		
Aggregated B/S Investment Funds EUR Billions December '16		
Country	Total Assets	% of tot € area
LU	3804,6	34,27%
IE	1938,4	17,46%
FR	1356,6	12,22%
DE	2046,2	18,43%
NL	830,80	7,48%

Table 1. The 5 most relevant countries in the Euro area according to their number of assets held by investment funds, Source: European Central Bank 2016

It can clearly be noticed how Luxembourg even if it is one of the smallest countries in the Euro Area it is by far the biggest player in the investment funds industry, accounting for more than one third of the whole area. It is worth mentioning also the very relevant role of Ireland, which as Luxembourg is one of the offshore jurisdictions part of the EU.

5.6 Ships registration

Another important line of business for some OFCs is the ship registration.

As an example, “about 8,600 ships fly the Panamanian flag. By comparison, the US has around 3,400 registered vessels and China just over 3,700” (BBC 2014). By law the country under whom flag is the ship cruising must practice the administrative control over it. Some of the OFCs have very favorable legal and fiscal environments for ship registration and that’s why they are so frequently used for this kind of operations. The international infrastructure of the OFCs is organized for non-residents and that is the motivation behind why such a hefty portion of them offers this kind of services. This is particularly common for example in Panama as mentioned before, but also in Liberia, Cayman Islands, Cyprus, Gibraltar, Malta, Bahamas, and some others.

5.7 Other services and products

Apart from the services mentioned in the overlaying part, many OFCs offer also general corporate services, provision of directors, company secretarial services, movies, IT, estate planning and stock brokerage. Of course, an individual or a company will find a wider or smaller offer of these depending on the jurisdiction selected.

6 THE FINANCIAL IMPACT ON WORLD'S ECONOMY

The presence and size of OFCs have different effects. First of all, tax havens that are utilized for tax avoidance and tax evasion obviously correspond to decreased tax income for the onshore nations. There is little information about the amount of cash diverted through OFCs. Since 2003 when, as indicated by Palan, Murphy and Chavagneux (2010), not by any means real data on these activities were accessible, researchers have embraced different ways to deal with in order to get solid figures (Zucman, 2014; Henry, 2012; Palan, Murphy and Chavagneux, 2010).

The loss generated by tax evasion and avoidance of enterprises is evaluated to be between 2% to 2,5% of the world's GDP (Palan, Murphy and Chavagneux, 2010). Those percentages can be translate into a yearly loss of 270 to 335 billion dollars in the European union. James Henry (2012) computed that up to 32 trillion dollars (around 26 trillion euros) of unreported private money was held offshore toward the end of 2010 by extremely wealthy people. These figures just incorporate financial wealth and hence avoid lands, yachts and other non-monetary resources. Zucman (2013) assessed that 8% of the private financial wealth (around 5,8 trillion dollars) of rich people is being buried in OFCs, prompting a yearly expense loss of 130 billion euros under the supposition that 75% of the amounts is untaxed.

As huge as it may seem, the figures just allude to private financial wealth, but the unpaid tax revenue generated by MNCs are excluded. As indicated by Troost (2013) the tax losses that are experienced through the tax avoidance methodologies of MNCs are twenty times higher than those connected with duty avoidance of well off individuals. More than 80% of the 100 biggest public traded US companies have subsidiaries in OFCs (GAO, 2008)

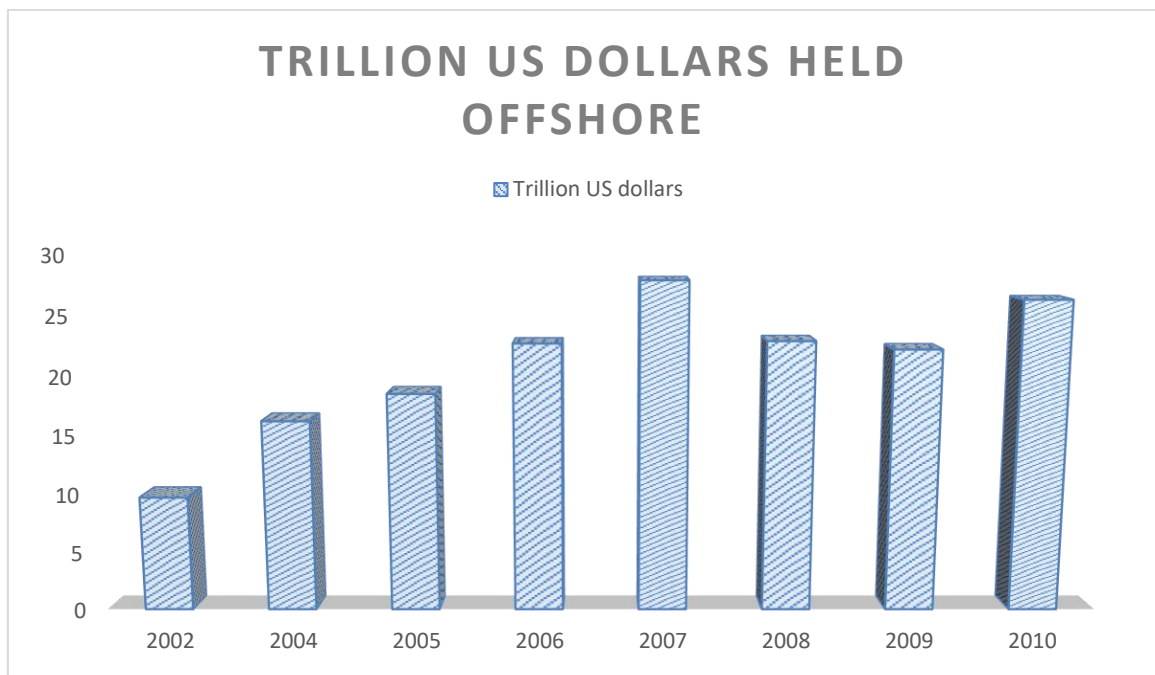


Figure 1. The estimated amount in offshore financial assets in trillion U.S. dollars from 2002 to 2010, Source: statista.com

7 EU POLICIES AND ATTITUDE

The taxing power is one of the pillars of the sovereignty of the Member States Union, which in fact have given only limited powers to the Union. The development of tax provisions at EU level aims at a correct functioning of the single market. In an initial phase,

it begun with the harmonization of indirect taxes in more depth than they did for direct taxes.

This because EU's power to create and implement fiscal policies has always been reduced to indirect taxes such as VAT and excise duties. The fundamental issue is that any maneuver regarding direct taxes requires unanimity at the Council of Ministers, basically being a revision of the treaties. Considering these aspects and adding others like the fact that the single currency gives total stability to the exchange rates in the internal market, but also that the four freedoms that generated a marketplace where individuals and companies can shop around or that the presence of a strong collective action problem is undeniable, the EU is hardly expected to succeed in its fight against cross-border tax avoidance and evasion (Mügge, 2014).

Regarding also the political stand point Mügge (2014) states that *"the EU contains within it multiple and opposed interests; many of its member states follow an offshore strategy, making the EU itself the host to the largest tax evasion industry in the world. If we include EU member state dependencies such as the former Dutch Antilles and the UK Channel Islands, Bermuda, and the Caymans, the EU hosts approximately 60 per cent of the world's tax havens"*.

Discrepancies between tax regimes of different countries allow certain companies to implement an "aggressive tax planning" to minimize their tax burden. The aim of the close coordination and exchange of information between tax administrations is to avoid this happening. The governments of the European countries should also ensure that their systems of taxation on corporate income are transparent and equitable, and not structured to attract undue companies from other EU countries or at least erode the tax base. Therefore, they signed a Code of Conduct that invites you to avoid it.

Anyway, the fight against tax avoidance and aggressive tax planning is a key challenge. Increased cooperation, coordination and transparency between the EU Member States in the matter of tax policies would help in reducing significant tax losses incurred by the Member States and to ensure greater fairness across the EU. In addition to the progress already achieved and ongoing activities, the Commission proposed a series of new initiatives contained in a notice published in June 2016. The Commission will try this year to revive its proposal for a common consolidated corporate tax base for companies and to prepare, by the end of 2017, an EU list of tax havens or the so called “EU list of non-cooperative tax jurisdictions” (KPMG 2016).

About the topic Pierre Moscovici, Commissioner for Economic and Financial Affairs, Taxation and Customs stated that *"The EU takes its international tax good governance commitments seriously. It is reasonable for us to expect the same from our international partners. We want to have fair and open discussions with our partners on tax issues that concern us all in the global community. The EU list will be our tool to deal with third countries that refuse to play fair."*

On the other hand, it might be argued that the blacklists have become a tool to divert the attention from jurisdictions that would have tax haven features like for example, focusing just inside the European Union, the UK and its dependencies and overseas territories, the Netherlands, Ireland and others (Gravelle 2013).

7.1 Consequences of the policies

The EU's most relevant tax policy concerning the OFCs world is the 2005 Tax and Savings Directive, that for the first time forced cooperative jurisdictions to tax or report the income deriving from interest earned by EU residents (or whose beneficial owner is). This kind of regulation left open space to non-EU residents and companies, or suggested as a solution also the possibility of moving the entity to a non-cooperative jurisdiction. Based on a data from two leaks that took place in 2013 it is clear how, immediately after

the implementation of the Directive, the growth of EU-owned entities declined while the one of the non-EU-owned entities remained stable. The leaks highlighted a replacement of EU ownership with non-EU ownership and of cooperative jurisdictions with non-cooperative ones (P.Caruana-Galizia & M.Caruana-Galizia, 2016).

This phenomenon proves how fast the market reacts and finds a solution to any policy change regarding offshore finance and how the EU finds difficulties in implementing efficient and hard to elude measures. There is a need of more comprehensive policies that would regulate in a more productive way the subject. On the other hand, the last decade of tax and financial regulations deprived tax havens of some of their attractive assets and four former OFCs have permanently closed: Nauru, Niue, Marshall Islands and Tonga (Hampton and Christensen, 2011).

8 EU'S INVOLVEMENT IN THE OFFSHORE WORLD

8.1 Advance tax ruling

Tax ruling is a general term used for any kind of arrangement between the tax authorities and an individual or a company but for this thesis is more interesting the concept of advance tax ruling since it is a behavior that could be theoretically connected to OFCs but that happens widely also within the EU. Basically, the difference is that *“an advance tax ruling is a statement provided by the tax authorities, or an independent council, regarding the tax treatment of a taxpayer with respect to his future transactions and on which he is – to a certain extent – entitled to rely”* (European Parliament 2015). Based on it multinationals (with subsidiaries in several countries) choose the most advantageous destination from a fiscal point of view.

The problem is that the secret tax agreements signed by the European Union countries with multinational companies are growing exponentially. The report "Survival of the

Richest" (Eurodad, 2016), which uses the data provided by the EU Commission, found out that starting from the 547 tax-ruling signed in 2013, the number grew to 972 in 2014, reaching 1,444 in the Union at the end of 2015. The report conducted a comparative analysis on the progress regarding specific tax justice measures in 18 European countries. The analysis shows an overall increase of over 160% in just two years (2013-2015) and an increase of almost 50% from 2014 to 2015.

Sifting through the member countries, it is clear that Luxembourg, even after Lux Leaks scandal, has not changed direction and remained at the top of the standings having granted 172 other multinational secret agreements. Even Belgium is at the top of the EU countries with the highest number of tax-ruling into force at the end of 2015 according to the Commission's accounting model. According to the report of the NGO the tendency does not seem to have been the least tarnished by the Lux Leak scandal detonated in November 2014.

Since the agreements are secret between companies and tax authorities the public cannot know their content. However, the study points out that the Lux Leaks scandal and the investigation of cases of aid was conducted by the Commission with some sensational decisions already made public, like for example the decision in the case of the Irish ruling in favor of Apple group in August 2016 gave clear evidence of how these agreements allow corporations to obtain favorable tax treatment, as well as a real competitive advantage compared to small and medium-sized domestic enterprises (ISole24Ore 2016).

8.2 Intermediation in the EU countries

A relevant issue is not only tax ruling and having a common policy as European Union regarding offshore jurisdictions, but also the intermediation made from EU countries to OFCs should be taken into consideration as a key factor.

As appeared from the Panama Papers, Mossack Fonseca worked with intermediaries in more than 100 countries all around the world, also in the EU. Their most active clients by number of offshore company incorporations were from Hong Kong and Switzerland, but also the United Kingdom (that should still be considered part of the EU since Brexit hasn't been implemented yet), Luxembourg and Cyprus (ICIJ 2016).

This places three EU countries in the list of the jurisdictions with the most active intermediaries, as can be seen from the following chart:

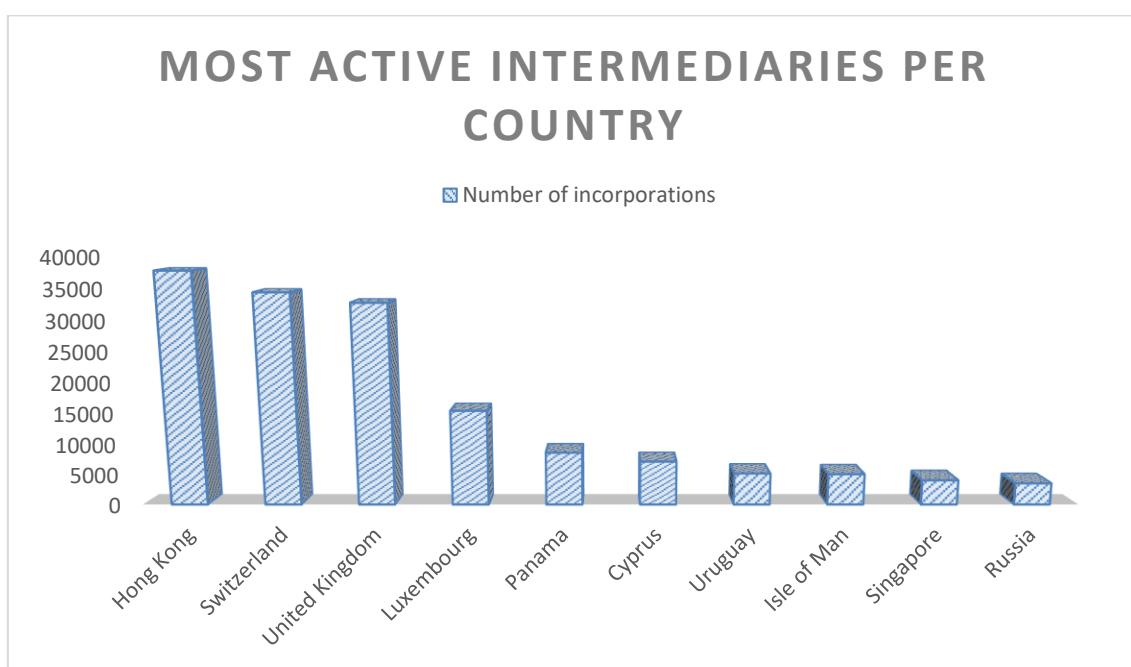


Figure 3. The 10 most active intermediaries per country in the Panama Papers, Source: The Panama Papers

The very high number of incorporations attributed to the UK can easily be explained by referring to an indicator such as "offshore intensity" that is basically the foreign financial assets divided by the GDP of the jurisdiction. This ratio intuitively shows how inten-

sively the country acts as an OFC and concerning the year 2011 the top ten of is dominated by jurisdictions that are under the sovereignty of the UK or that are (formally independent) Commonwealth realms (Fichtner 2011).

The same highlighting of the role of some countries is expressed also by Fernandez (2015) that referring to the size of the other financial institution sector in the EU claims it is “disproportionately concentrated in the UK (29%), Luxembourg (17%), the Netherlands (15%) and Ireland (8%). The largest economies of the Eurozone, Germany (7%), France (7%), and Italy (4%) are small players”.

Also Palan (2012) in the matter of international capitals focuses on the same countries by identifying two agglomerations of OFCs: the British Imperial pole (London, British Crown dependencies, British Overseas Territories and recently independent colonies) accounting for 38,3% and the Mid-size European pole (Benelux countries, Ireland and Switzerland) accounting for 14,9%. Basically, in March 2010 the 53,3% (that was 58,4% the previous year) of all international assets and liabilities are to be connected to EU countries or jurisdictions related to it, giving an even stronger image if compared to the 14,9% of the USA.

8.3 Capital flows from the EU to the OFCs

In nowadays world it is quite normal having capitals flowing across borders of different countries and continents, so being the OFCs one of the main players in this phenomenon. In order to give a clearer overview of the situation, the following table shows the holdings, in percentage, of the Euro Area residents in jurisdictions outside the Euro Area according to the European Commission:

	FDI Assets	FDI Liabilities	Port. Equity Assets	Port. Debt Assets	Other Assets	Other liabilities
Other Europe	37,1	38,3	26,1	39,8	49,6	54,2
North America	22,8	26	34,8	34,8	16,2	14,4
China	1,5	0,3	2,9	0,1	0,9	1,2
Japan	1,3	2,2	5,3	3,8	2,0	1,7
Offshore Financial Centers	8,8	14,4	12,7	5,5	10,4	11,5
Rest of the world	28,5	18,8	18,3	15,9	20,9	17,1

Table 3. Extra-Area Holdings of Euro Area Residents: Per cent of Total Holdings, Source: European Commission 2013

It can easily be noticed that the OFCs, even being fiscally small countries, are one of the main players, with way larger percentages than bigger and more industrially developed markets such as China and Japan. This can definitely showcase the high level of involvement of the EU countries in practices linked to offshore jurisdictions.

8.4 The difference between “sink” and “conduit” OFC

If the whole idea of OFC is based on the findings of the Panama Papers, it might be easily understood by the reader that these jurisdictions are small island tax havens rather than large and economically relevant countries. But a new data-driven approach for identifying OFCs based on the global corporate ownership network, in which over 40 million firms (nodes) are connected through 71 million ownership relations (lines), has just been developed by Garcia-Bernardo, Fichtner, Heemskerk and Takes (European Parliament 2017).

This concept is based on the difference between “sink” OFCs and “conduit” OFCs: the first ones “*attract and retain foreign capital*”, instead the second ones are “*attractive intermediate destinations in the routing of international investments and enable the*

transfer of capital without taxation” (Garcia-Bernardo, Fichtner, Heemskerk and Takes 2017).

In this work 23 jurisdictions are identified as sink OFCs and 5 as conduit OFCs. The latter ones “*canalize the majority of corporate offshore investment*” and they are the Netherlands, the United Kingdom, Ireland, Switzerland and Singapore.

This underlines that 4 out of 5 of the main players are on European soil and 3 out of 5 are part of the EU (counting the UK since Brexit hasn’t been implemented yet).

These countries facilitate the transfer of value from and to sink OFCs and because of these their services are used by companies and individuals all around the world.

Each one of the 5 conduit OFCs is specialized in a geographical area: The United Kingdom serves as a conduit between European countries and Luxembourg, Bermuda, Jersey, British Virgin Islands and Cayman Islands. The Netherlands is the principal conduit between European companies and Luxembourg, Curacao, Cyprus and Bermuda. Luxembourg and Hong Kong companies invest directly in European countries and China, without using a conduit OFC. In contrast, investments from countries typically identified as small tax havens (e.g., Bermuda, British Virgin Islands, or Cayman Islands) do use conduit OFC, and thus companies located in these jurisdictions invest in other OFCs (Garcia-Bernardo, Fichtner, Heemskerk and Takes 2017).

Basically, the overall picture is that the Netherlands and Luxembourg serve the European countries, Hong Kong (and some other sink OFCs) serves the Asian countries, and instead the United Kingdom serves as an integrator between Europe and Asia. But also, the study shows how every country is specialized in a particular line of business: activities of head offices for Ireland and the UK, mining and quarrying in Jersey for Switzerland, manufacturers of electronics and computers for Hong Kong, holding companies for the Netherlands and Luxembourg, other financial sectors for Ireland, business support service activities for the Netherlands (concentrated in Luxembourg). Apart from

those lines of business Luxembourg, Hong Kong, Singapore and Ireland work strongly with unknown sectors that end up in sink OFCs (Garcia-Bernardo, Fichtner, Heemskerk and Takes 2017).

The concept of conduit OFC was already used by Fernandez (2015) to underline the importance of the role played by some EU countries in the offshore financial flows. In his work referring to the Netherlands, Luxembourg and Ireland, he stated that *“these locations do not harbor the higher value added services of shadow banking found in first-tier financial centers such as New York and London, but instead provide a specialized service industry that facilitates pass-through entities processing large capital flows”*.

8.5 The EU as a source of Offshore wealth

In 2015, the largest source of wealth for the OFCs was Western Europe, with references to the United Kingdom, Germany and France, even after declining 3% compared to the previous year. It is also very relevant that the United Kingdom was in the top three source countries together with China and the United States, but being the one with the highest ratio of offshore shares compared to the total wealth of the country, with an astonishing 6%. This number might seem small compared to areas like MEA and Latin America with around 25% of total private wealth held offshore, but it should be kept into consideration that in these regions, economic and political tensions (as well as access to financial products not available onshore) create a totally different environment than the one in the UK (BCG 2015).

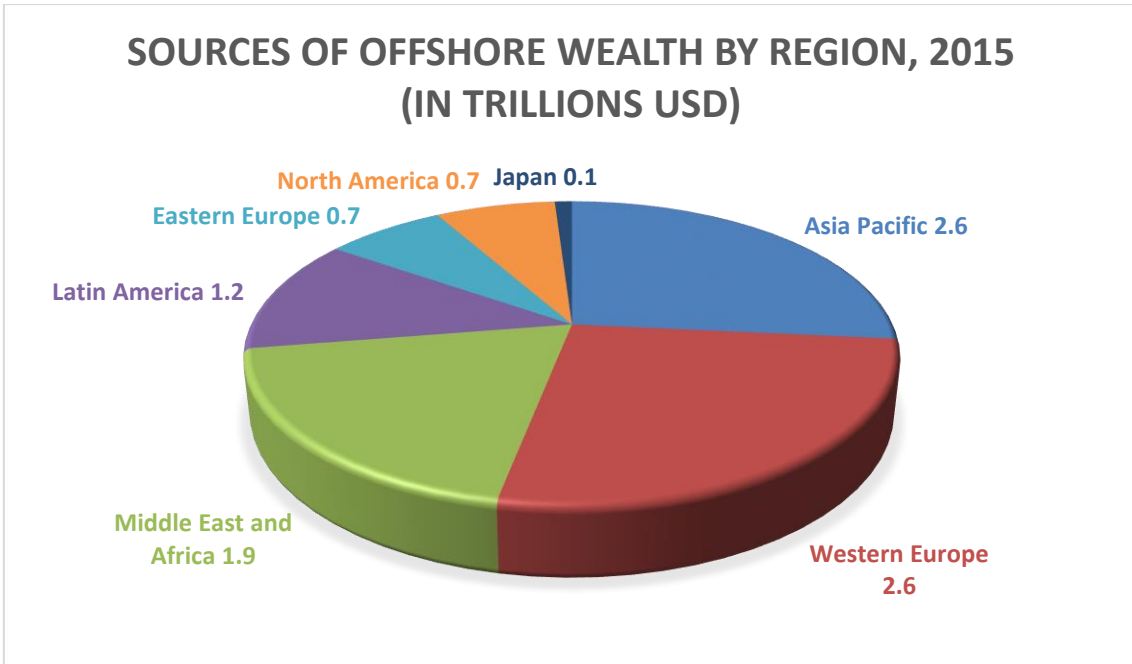


Figure 4. Source of Offshore wealth by region in 2015, Source: BCG Global Wealth Market-Sizing Database 2016

In general, in the years between 2010 and 2015 the percentage of the offshore wealth coming from the old world (the developed regions) has been constantly decreasing in favor of the new world (developing regions) that grew from 57% in 2010 to 65% in 2015. This was influenced also by the regulatory measures against tax evasion and money laundering that are being implemented in the EU, pushing them to bring back the capitals onshore. Despite this the offshore wealth generated in the developed countries is forecasted to grow 2% annually until 2020, showing still a trend even if a less remarkable one compared to the annual 6% forecasted for the developing countries (BCG 2015).

9 DISCUSSION

9.1 The services offered by the OFCs and their financial impact

The findings of this thesis regarding the offshore world were multiple and mainly based on three areas: locations, services and financial impact.

The OFCs market defined according to the “traditional” concept, being the so-called sink jurisdictions where the wealth is stored, have in The British Virgin Islands, Panama, the Bahamas and the Seychelles the four main players. The first has a fully dominant role in terms of incorporations, considering that the jurisdiction basically is responsible for half of the companies incorporated worldwide.

The main attraction of the OFCs are the services or service providers they offer. The key ones like the limited liability vehicles, the possibility of implementing tax planning for companies and individuals, trusts and foundations, but also the more traditional ones like banks, insurances and investment funds, or more leisure related ones like ship registration, in which Panama is the main provider widely surpassing China and the US together, can offer huge benefits to all the parts involved (except the onshore countries treasuries) even operating in the total legality. Therefore, for the individuals or organizations willing to have a higher degree of risk and with no ethical bond to legality, operating borderline or fully illegally with the OFCs, brings even bigger competitive advantages than those that are working within the borders of the law.

The consequential financial flows are simply the representation of the advantages they can guarantee to their clients and partners. These activities can be legal like tax planning or illegal like tax evasion but in both case, they have an enormous financial impact on the onshore jurisdictions from individuals and even exponentially bigger ones from

MNCs. The yearly tax loss from individuals of 130 billion euro and of 2,6 trillion from
MNCs add up to an astonishing 2,73 trillion euro every year. A proof of how established
are these practices is that 80 out of the US top 100 companies have subsidiaries in an
OFC.

Considering the fact that those are just a part of the business practices of the OFCs, the
offshore world plays a key role in nowadays economy and financial industry. Looking at
the issue from an economic point of view and business volume it is no wonder that so
many jurisdictions and main countries take part in this environment as active players
rather than as barriers against it.

9.2 The role of the EU in the offshore finance phenomenon

In the second part about the role of the EU in the offshore finance industry the focus
was on the policy approach regarding the subject and on the level of involvement as
capital source or service provider.

In the matter of policy making the EU has two main issues, its structure doesn't support
an effective fiscal environment concerning cross border taxation and on the other hand
the interest of some member countries is more oriented towards an offshore strategy
than against it. Even when the EU is able to implement some laws to control the flows
the market is very fast at adapting and changing its best practices. Some results have
been achieved but the overall view on the topic is rather pessimistic.

The Western European area is nowadays the biggest source of offshore wealth in the
world and in particular the UK is in the top three countries and has a relevant off-

shore/GDP ratio considering the fact that it is a strongly developed economy. If we extend the idea of UK to British Imperial Pole (with all dependencies and recent colonies) the group accounts for 38,3% of the international assets, giving a very clear idea of how relevant and central its role is in the global economy. Also from the point of view of FDIs one of the main destination of European capitals is the offshore world. So, the overall picture shows the EU (and the UK as leader) as a great utilizer of OFCs and offshore services in order to manage and enlarge wealth or to do various businesses.

From the opposite point of view providing services related to the offshore industry is a business in which the EU plays the role of the lion too. Advanced tax ruling, intermediation and other financial services connected see a group of EU countries (essentially UK, Luxembourg, Netherlands and Ireland) as main global players. The phenomenon is even more relevant if we consider the concept of conduit-OFC, where the UK is the absolute leader, like in most of the aspects bonded with offshore finance. Also, considering as a factor the offshore intensity, the top ten is dominated by commonwealth realms, proving once again the centrality of the UK in the industry and consequently of the EU, at least up to the final implementation of the Brexit.

In overall it is very clear from the literature taken into consideration earlier that the EU is highly involved and has a central role in the world of OFCs. Despite some policy making that is trying to limit the phenomenon and regulate more the industry the situation is hardly expected to change in the short term. Both the aspects of capital source and services provider proved to be deeply rooted in the European economy and business environment, showing the pivotal position of the EU (or at least of some EU countries) in almost every data set or piece of literature.

10 CONCLUSIONS

The relevance of this paper is to be connected to a more conscious understanding of the world of the OFCs and to the fact that it is usually seen in the collective imagination as detached from the EU and relegated in minor countries in exotic locations held “ethically” and politically totally accountable for it. Instead the centrality of the EU and consequently of us, Europeans, forces the acknowledgement of the situation and pushes towards a shift in the perception of the phenomenon.

The work might appear to give more relevance to the aspect of the role of the EU instead of being well balanced also with the aspect of the overview about the world of the OFCs. This is due to the fact that the latter serves as a tool to enrich, contextualize and make more meaningful the part related to the EU but also to make the reader understand the reasons behind the common mistake in the perception of the offshore finance environment. It might be correct to consider the second research question (what is the role played by the European Union in the offshore finance phenomenon?) more relevant from an academic point of view and more central to the paper itself but also the first (what are the services offered by the main OFCs and what kind of financial impact they have on the world?) has its importance and works as a support in order to create a well-rounded and decently exhaustive thesis.

For the future, it could be interesting to re-evaluate the pivotality of the EU in the world of the OFCs once the UK will finally implement the Brexit in its totality. This because of its leading role in most of the data sets and pieces of literature regarding the topic. A new union without the UK might end up with a lot smaller degree of involvement in the offshore finance world, twisting so totally the output of this thesis and the considerations of the author.

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