

## **Escaping the Certainty of (Death and) Taxes: Governance of Tax Havens.**

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**Abstract:** This working paper argues that any arrangement in the international effort to prevent tax evasion should maintain privacy as its core value. Conflating tax evasion and tax avoidance entails risks to individual freedom. Perhaps it is better to search for insights from behavioral economics to devise more effective incentives than punishment to pay taxes. Likewise, blockchain technology may be an additional tool for enhancing both corporate transparency and privacy.

**Keywords:** Tax evasion, tax avoidance, behavioral economics, blockchain, transparency

**Resumen:** Este documento de trabajo argumenta que cualquier arreglo en el esfuerzo internacional para prevenir la evasión fiscal debe mantener la privacidad como su valor central. Confundir evasión fiscal y elusión fiscal entraña riesgos para la libertad individual. Tal vez sea mejor buscar ideas de la economía del comportamiento para diseñar incentivos más efectivos que castigos para pagar impuestos. Asimismo, la tecnología blockchain puede ser una herramienta adicional para mejorar tanto la transparencia como la privacidad corporativa.

**Palabras clave:** Evasión fiscal, elusión fiscal, economía conductual, blockchain, transparencia

This working paper argues that any arrangement in the international effort to prevent tax evasion should maintain privacy as its core value. Conflating tax evasion and tax avoidance entails risks to individual freedom. Perhaps it is better to search for insights from behavioral economics to devise more effective incentives than punishment to pay taxes. Likewise, blockchain technology may be an additional tool for enhancing both corporate transparency and privacy.

*Despite the force of patriotism... and the indispensability ... of law and order, no major state in modern history has been able to support itself through voluntary dues or contributions ... Taxes, compulsory payments by definition, are needed... their necessity is as certain as death itself.*

*M. Olson, the Logic of Collective Action.*

### **Individuals, not governments should have the final word.**

A tax haven is a set of institutions and practices designed to facilitate tax avoidance;<sup>1</sup> as different from tax evasion, a criminal activity. Transactions using tax havens resulting in tax savings might be legal from the perspective of one legal order, but the aggregated impact of those transactions yields corrupting effects.

Tax avoidance, for example, incentivizes solely tax-savings transactions devoid of underlying real wealth-producing value in a community, perpetuating societal inequalities;<sup>2</sup> It solidifies the impression that taxes are unfairly collected because savvy actors can take advantages of 'loopholes' unavailable to the common taxpayers; it encourages professional (legal,

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<sup>1</sup> See *generally* Tax Justice Network, Inequality & Tax Havens, <http://www.taxjustice.net/topics/inequality-democracy/inequality-tax-havens/> (last visited, January 7, 2015). See also *generally* Jacques Leslie, The True Cost of Hidden Money: A Piketty Protégé's Theory on Tax Havens, N. Y. TIMES, June 15, 2014, <http://goo.gl/V0jK1w>; Laura Bowen, International Tax Havens: Are Multinationals Gaming the System? Chicago Policy Review (online), Jan. 28, 2014, <http://chicago-policyreview.org/2014/01/28/international-tax-havens-are-multinationals-gaming-the-system/>.

<sup>2</sup> See, e.g. Gillian Brock, *Taxation and Global Justice: Closing the Gap between Theory and Practice*, 39 *Journal of Social Philosophy*, 161 (2008) at 162 ("Our current arrangements contribute greatly to the global poverty problem and allow vast amounts of taxable income to escape taxation." *Id.*).

accounting, and business) cultures in which duties to clients is paramount, regardless of societal costs; it raises the costs of keeping institutions safe from criminal actors; and it reinforces a strict separation between legal and ethical duties in rendering professional advice.

A tax haven is a network designed to facilitate tax avoidance strategies. It thrives from opacity in corporate, financial, and accounting transactions; from professional advice identifying the tax avoidance strategies resulting in tax savings; and from jurisdictional differences in tax and corporate policies.<sup>3</sup>

Opacity can be addressed with more transparency, abusive professional advice with more specific regulations of professional actors, and the jurisdictional differences with more coordination.<sup>4</sup> All of these remedies

<sup>3</sup> See generally Staff of S. Permanent Subcommittee on Investigations, Comm. on Homeland Security and Governmental Affairs, *Abuse of Structured Financial Products: Misusing Basket Options to Avoid Taxes and Leverage Limits*, Majority and Minority Staff Report (July 22, 2014), <http://www.hsgac.senate.gov/subcommittees/investigations/media/subcommittee-finds-basket-options-misused-to-dodge-billions-in-taxes-and-bypass-federal-leverage-limits>, July 21, 2014, REPORT-Abuse of Structured Financial Products (Basket Options) (7-22-14, updated 9-30-14).

<sup>4</sup> For instance, see M. González Marcos, B. Zagaris and L. Shirley, *Panama Adopts Banking Regulations Requiring Immobilization of Bearer Shares*, 31 *International Enforcement Law Reporter*\_\_ (Jan. 2015), fn. 8, indicating that [t]he official theme of the 39th G-8 summit held on 17–18 June 2013 in Northern Ireland was tax evasion and transparency. Agreements were also reached on global tax evasion and data sharing. The G8 nations agreed to tighten rules on corporate taxes that sometimes allow companies to shift income from one nation to another to avoid taxes. They agreed that shell companies should have to disclose their true owners, and that it should be easy for any G8 nation to obtain this information. Going forward, corporate and individual tax information will be shared automatically to help detect tax fraud and evasion. The OECD was assigned to gather data on how multinationals evade taxes.

See, e.g., *The Lough Erne Declaration* (the summit communiqué), [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/207543/180613\\_LOUGH\\_ERNE\\_DECLARATION.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/207543/180613_LOUGH_ERNE_DECLARATION.pdf).

Also, the Foreign Account Tax Compliance Act (FATCA) of 2010 requires that foreign financial institutions share financial information of certain customers with the U.S. Treasury Department, raising thereby privacy concerns in certain countries. An additional tool for tax compliance, FATCA aims ultimately to fight tax evasion by enhancing the self-reporting systems in place – such as the Foreign Bank and Financial Accounts (FBAR) Report. FATCA expects to bring to light underreported tax liabilities of those U.S. taxpayers using “investment-based assets held in offshore accounts” (Lawrence A. Kogan, *U.S. FATCA Information Reporting: A Pretext for Fishing with Like-Minded European and OECD Nations for Long Forsaken Tax Revenues at Exotic*

are welcomed methods for curtailing the abusive use of tax havens, although they leave some unanswered questions.

How to justify shifting the balance in favor of governments asking from individuals not only to self-report activities, but also to abstain from taking advantage of loopholes in a politically-driven tax legislation and enforcement? In certain capacities and contexts, e.g. corporate officers, individuals may deem they have a duty to take advantage of loopholes.

Also, a pure economic analysis of tax-avoidance strategies may show that they make more sense as alternative or complementary devices of wealth-distribution. If this practice were deplorable only for the loss of revenues, then showing an economic gain elsewhere in society would make this criticism less persuasive.<sup>5</sup>

A tax avoidance mindset fits better with the liberal conception of the state that the right of individuals should prevail over governmental goals. It is not a coincidence that arguments in libertarian circles against taxation are adduced as justifications among professionals catering to clients who benefit from tax avoidance strategies.

It assumes that governments have equal legitimacy regardless of the democratic quality of their respective policy decision processes. It does not leave the door ajar in case singled-out people may need to protect their wealth from an authoritarian government.<sup>6</sup>

It assumes that certain professional cultures should become mindful

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*Offshore Locations, 2012 EMERGING ISSUES 6831, at 1). In essence, FATCA allows the Internal Revenue Service (IRS) to authorize foreign financial institutions (FFIs) to become its extraterritorial agents, so they may report and withhold taxes from “many different types of U.S. source payment destined for the offshore accounts of U.S. individuals and certain U.S. beneficially owned non-financial foreign entities (NFFEs)” (Id. at 6-7). To comply with FATCA, a FFI must reach a compliance agreement with the IRS to conduct due diligence in order to identify and obtain information from U.S. accounts holders or, alternatively, it must withhold a 30 percent tax from U.S. sources.*

<sup>5</sup> See generally, e.g., Qing Hong and Michael Smart, *In Praise of Tax Havens: International Tax Planning and Foreign Direct Investment*, 54 *European Economic Review* 82-95 (2010) (arguing, “the investment-enhancing effects of international tax planning can dominate the revenue-erosion effects. The implications of this view are strong: an increase in international tax avoidance can lead to an increase in both statutory and effective tax rates on capital, if initial tax rates are not too high, and an increase in the welfare of citizens of high- tax countries.” *Id.* at 83).

<sup>6</sup> See generally, e.g. Robert T. Pennock, *Death and Taxes: On the Justice of Conscientious War Tax Resistance*, 1 *Journal of Accounting, Ethics & Public Policy* 124 (1998) (arguing that “resistance to paying war taxes that stems from a principled pacifism is not the same as tax-dodging.” *Id.*); Götz Aly, *Hitler’s Beneficiaries: Plunder, Racial War, and the Nazi Welfare State*, 2008.

of the spillover effects of domestic policy decisions.<sup>7</sup> While this awareness of spillover effects is basic for ensuring public goods, e.g. security, certain jurisdictions will prioritize their own policy goals, regardless of spillover effects.<sup>8</sup>

Knowing that multinational corporations, individuals seeking privacy, and criminal organizations have all used tax havens suggests that their corrupting impact might be better analyzed using the notion of institutional corruption as advanced by Lawrence Lessig.<sup>9</sup> “Institutional corruption is manifest when there is a systemic and strategic influence which is legal, or even currently ethical, that undermines the institution’s effectiveness by diverting it from its purpose or weakening its ability to achieve its purpose, including...weakening either the public’s trust in that institution or the institution’s inherent trustworthiness.” - from “Institutional Corruption, Defined” by Lawrence Lessig, (<https://ethics.harvard.edu/lab>).

Given the enormous tax enforcement costs, it might be useful to explore insights from behavioral economics developed by the Behavioral Science & Policy Association (<https://behavioralpolicy.org/>) to increase compliance with tax obligations.

Also, accepting that privacy is paramount for free individuals in a democratic society, using technologies like blockchain in corporate matters could ensure privacy, transparency, and traceability. Neither governmental surveillance nor surveillance capitalism must be our alternatives. The choice about the timing of dying in the hands of the individual hints to the existence of the hypothetical social contract justifying the only legitimate purpose of state power: to ensure liberty. This ultimate choice should be kept perhaps as a safety valve against the overbearing bio-power of the State. Also, ethical tax-avoidance structures should be kept in the hands of individuals to remind such overbearing state bio-power that although death and taxes are certain, only free individuals in a democratic society should decide ‘when’ to die and ‘how much’ taxes to pay.

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<sup>7</sup> See generally, e.g. IMF Policy Paper, *Spillovers in International Corporate Taxation*, May 9, 2014, <http://www.imf.org/external/np/pp/eng/2014/050914.pdf>.

<sup>8</sup> See, e.g., Kent Greenfield, *Democracy and the Dominance of Delaware in Corporate Law*, 67 *Law and Contemporary Problems* 135 and ff. (2004) (addressing the illegitimacy of the Delaware dominance in corporate law).

<sup>9</sup> See Lawrence Lessig, *Memorandum re Request for Proposals for the Lab “Project on Institutional Corruption,”* Nov. 12, 2010 (v3.0), at 3.

## A failure of governance

With a vile assassination, an indictment, and two massive leaks (namely, the Paradise and Panama Papers, respectively), the necessity of corporate and tax transparency worldwide has been established.

Daphne Caruana Galizia, the leading journalist from Malta who was part of the investigative efforts of the Panama Papers, was killed in October 2017. An explosive device demolished her car. This ‘mafia-style murder’ sent a chilling message to the people of Malta and to the world.

The indictment against Paul Manafort, Jr. and Richard W. Gates III for conspiracy to launder money and failure to report Foreign Bank and Financial accounts, among others, lists 17 entities from the U.S., 12 from Cyprus, two from the Grenadines, and one from the United Kingdom. Through these entities they advanced “a scheme and artifice to defraud, and to obtain money and property by means of false and fraudulent pretenses, representations, and promises from the United States, banks, and other financial institutions.” (<https://goo.gl/Sqd7pF>). The allegedly artful scheme could have passed undetected, but for Manafort’s involvement in the future President Trump’s election campaign.

In the Paradise Papers, the ICIJ (<https://www.icij.org/>) published the leak of 13.4 million documents revealing transactions of the Bermudan law firm Appleby (Millions of Leaked Files Shine Light on Where the Elite Keep Their Money, NYT, <https://goo.gl/JWzf7N>). This leak includes evidence of transactions from world leaders such as Queen Elizabeth II, “advisors, donors and members of U.S. President Donald J. Trump’s administration”; multinational corporations such as Apple, Nike, and Allergan (<https://goo.gl/fgWuTT>).

Also, the German newspaper *Süddeutsche Zeitung* in coordination with the ICIJ announced a leak on 4.3.16 of a 2.6 terabyte database containing 11.5 million documents of 40 years of records from the Panama-based firm Mossack Fonseca (<https://panamapapers.icij.org/>). At its best, the documents reveal individuals and companies legally attempting to avoid taxes or hiding their wealth from prying eyes, and, at its worst, it shows them criminally attempting to evade taxes or launder money.

Politicians, athletes, artists, celebrities and wealthy individuals and companies around the world are cast as members of a callous elite stealing from their respective countries tax-revenues and thus the basis for the ostensive provision of public goods.<sup>10</sup> Their greed drives an endemic inequality

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<sup>10</sup> See, e.g. *Hamish Boland-Rudder, Martha M. Hamilton, Pakistani PM disqualified by court over Panama Papers links: The Supreme Court of Pakistan has voted unan-*



and contributes to the decline of the welfare state. The culprits are tax dodgers, and most importantly; the lawyers, accountants, bankers, and 'poaching' governments of tax havens that enable the functioning of the so-called offshore asset protection industry to function are the culprit.

All of the sudden, regardless of the motivation, legality, or legitimacy of using offshore companies, they are suspicious. And, once again, shaming was inflicted on the brand of entire countries and their peoples to signal that the international community won't tolerate secrecy jurisdictions.<sup>11</sup>

The cast seems to have been perfectly selected. The founders and main partners of Mossack Fonseca had influential positions in the Panamanian government. Fonseca, was minister counselor of the President of Panama and Secretary General of the Political Party in power, while Mossack was a member of the Council on Foreign Relations. The case for influential members of elites colluding across borders to steal from their respective societies resulting in endemic inequality was easy to show with the Panama Papers revelation confirming old biases against, well, the well-to-do. They are richer than they deserve because they do not pay their fair share of taxes. Most importantly, the need of transparency was obvious as the "law firm at the heart of the 'Panama Paper's leak [was] owned by a Nazi's son,"<sup>12</sup> who happens to have a CIA connection from when his father offered to spy on the communists when escaping to Panama after World War II.

John Doe, the anonymous and heroic whistleblower of the Panama Papers, said in 'The Revolution Will Be Digitized', that he gave the information to newspapers because he was upset by witnessing the corruption that keeps income inequality, "one of the defining issues of our time."<sup>13</sup> Mossack Fonseca, said John Doe in his statement, intentionally "used its influence to

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*imously to disqualify Nawaz Sharif from the prime ministership over offshore assets, The Center for Public Integrity, 2017, <https://goo.gl/1q9AuY>.*

<sup>11</sup> "U.S. Comes Up Short on Corporate Transparency." *The New York Times*. December 21, 2017. Accessed May 20, 2018, <https://www.nytimes.com/2016/04/19/world/europe/us-comes-up-short-on-corporate-transparency.html>. <https://www.nytimes.com/2016/04/19/world/europe/us-comes-up-short-on-corporate-transparency.html>.

<sup>12</sup> Toi, and Eric Cortellessa. "Law Firm at Heart of 'Panama Papers' Leak Owned by Nazi's Son." *The Times of Israel*. Accessed May 20, 2018. <http://www.timesofisrael.com/law-firm-at-heart-of-panama-papers-leak-owned-by-nazis-son/>.

<sup>13</sup> Kim, Susanna. "Panama Papers' Source Explains Motivation Behind Leak." *ABC News*. May 06, 2016. Accessed May 20, 2018, <http://abcnews.go.com/Business/panama-papers-source-explains-motivation-leak/story?id=38929713>. <http://abcnews.go.com/Business/panama-papers-source-explains-motivation-leak/story?id=38929713>.

write and bend laws worldwide to favour the interests of criminals over a period of decades.”<sup>14</sup> John Doe called for “the European Commission, the British Parliament, the United States Congress and all nations to take swift action not only to protect whistleblowers, but to put an end to the global abuse of corporate registers.”<sup>15</sup> John Doe knew about the economic criticism against capitalism in creating unfair income inequalities. Also, he was aware of the neglect of the U.S. Congress to adopt policies to combat tax evasions as its members depend greatly on the money raised from those elite persons “who have the strongest incentives to avoid taxes.”<sup>16</sup> John Doe’s understood that the flourishing of tax havens is not only “a glaring symptom of our society’s progressively diseased and decaying moral fabric,” but an utter failure of governance.<sup>17</sup> Banks, regulators, tax authorities, legislatures, judiciaries, the media, and above all, “the legal profession has failed.”<sup>18</sup> “Democratic governance depends upon responsible individuals throughout the entire system who understand and uphold the law, not who understand and exploit it.”<sup>19</sup> Mossack Fonseca, however, “found allies and clients at major law firms in virtually every nation,”<sup>20</sup> who were more than willing to exploit the law. Finally, John Doe recognizes a global lack of ethics in the system we still call capitalism but suggests furthermore that it is a failure of governance that serves actually to mask “economic slavery.”<sup>21</sup>

## Appeals for reforms of the global tax regime complex

Alliances and organizations with old and new proposals to govern international taxation rushed to take advantage of the policy window created by one of the largest leaks in history. To name a few:

The Organization for Economic Cooperation and Development called for an emergency meeting to address how governments may cooperate using leaked information; Christine Lagarde of the International Monetary Fund stressed that international cooperation on taxation needs to be significantly

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<sup>14</sup> ICIJ, *The Panama Papers, Panama Papers Source Offers Documents to Governments, Hints at More to Come*, May 06, 2016. Accessed May 20, 2018. <https://panamapapers.icij.org/20160506-john-doe-statement.html>.

<sup>15</sup> *Id.*

<sup>16</sup> *Id.*

<sup>17</sup> *Id.*

<sup>18</sup> *Id.*

<sup>19</sup> *Id.*

<sup>20</sup> *Id.*

<sup>21</sup> *Id.*



improved since taxes are not global, but rather an attribute of sovereignty par excellence;<sup>22</sup> Oxfam called for action to “End the Era of Tax Havens”;<sup>23</sup> the Panamanian government appointed an Independent Committee with the participation of Joseph Stiglitz and Mark Pieth to propose changes in the financial system;<sup>24</sup> the Obama White House adopted an executive measure “to close loopholes used by foreigners in the US and called on Congress to pass legislation”;<sup>25</sup> the G-20 insisted in transparency threatening tax havens with penalties;<sup>26</sup> 300 economists published a letter against offshore tax havens;<sup>27</sup> The “Treasury Announces Key Regulations and Legislation to Counter Money Laundering and Corruption, Combat Tax Evasion”<sup>28</sup> and also pressures Congress to adopt beneficial ownership legislation;<sup>29</sup> Congress

<sup>22</sup> Smith, David. “IMF Chief Talks Panama Papers Fallout: Time to ‘think outside Box’ on Global Tax.” *The Guardian*. April 11, 2016. Accessed May 20, 2018. <https://www.theguardian.com/business/2016/apr/11/panama-papers-imf-christine-lagarde-global-tax> <https://www.theguardian.com/news/2016/may/06/panama-papers-us-launches-crackdown-on-international-tax-evasion>.

<sup>23</sup> “End the era of tax havens”, Accessed May 27, 2018. [www.oxfam.org.uk/get-involved/campaign-with-us/our-campaigns/inequality-and-poverty/end-the-era-of-tax-havens](http://www.oxfam.org.uk/get-involved/campaign-with-us/our-campaigns/inequality-and-poverty/end-the-era-of-tax-havens).

<sup>24</sup> Ap. “Panama Papers: Govt Set up Independent Committee to Recommend Financial System Cleanup.” *The Indian Express*. April 30, 2016. Accessed May 20, 2018. <http://indianexpress.com/article/world/world-news/panama-papers-probe-govt-recommendation-committee-mossack-fonseca-2777303/>.

<sup>25</sup> Roberts, Dan, and Jana Kasperkevic. “Panama Papers: US Launches Crackdown on International Tax Evasion.” *The Guardian*. May 06, 2016. Accessed May 20, 2018. <https://www.theguardian.com/news/2016/may/06/panama-papers-us-launches-crackdown-on-international-tax-evasion>.

<sup>26</sup> Mayeda, Andrew, and Mark Deen. “G-20 Threatens Penalties on Tax Havens After Panama Papers.” *Bloomberg.com*. April 15, 2016. Accessed May 20, 2018. <http://www.bloomberg.com/news/articles/2016-04-15/g-20-threatens-penalties-against-tax-havens-after-panama-papers-in1zhqaf>.

<sup>27</sup> Dewast, Louise. “300 Economists Sign Open Letter Against Offshore Tax Havens After ‘Panama Papers’.” *ABC News*. May 09, 2016. Accessed May 20, 2018. <http://abcnews.go.com/International/300-economists-sign-open-letter-offshore-tax-havens/story?id=38980820>.

<sup>28</sup> “U.S. Department of the Treasury.” *Ukraine-/Russia-related Designations and Identification Update; Syria Designations; Kingpin Act Designations; Issuance of Ukraine-/Russia-related General Licenses 12 and 13; Publication of New FAQs and Updated FAQ*. Accessed May 21, 2018. <https://www.treasury.gov/press-center/press-releases/Pages/jl0451.aspx>.

<sup>29</sup> “US Treasury Presses Congress for Beneficial Ownership Legislation.” *Reflection*

launched its anti-tax havens proposal;<sup>30</sup> and, most dramatically, the tax loophole that allow corporate inversions was curtailed by federal regulations and President Obama asked Congress “to close the loophole “for good”.<sup>31</sup>

Some proposals supplement other components of the global taxation regime complex already in place, namely, the Foreign Account Tax Compliance Act (FATCA) of 2010. (<https://www.treasury.gov/resource-center/tax-policy/treaties/Pages/FATCA.aspx>).

The questioning and dismantling of some tax havens fits well with the recent research by Thomas Piketty in *Capital in the Twenty-First Century* (2014) demonstrating that unregulated capitalism breeds inequality. Piketty’s assessment is groundbreaking for the following reasons: It restates that economic arrangements are not natural, but the result of social-political decisions; It shows that capitalism inherently generates inequality and therefore regulation is essential to keep inequality at bay; It shows that deregulation should be handled with care on a case-by-case basis and never as an overall conception of an ideal economic system, as the classical 19th century insights about capitalism of the classical economics were correct, but lacked the data to demonstrate them; It articulates what the Occupy Wall Street Movement expressed as political maladies; and it supports the rationale of tax transparency initiatives, such as FATCA, as necessary fiscal tools for cross-border tax cooperation. While Marx welcomed the advancement of capitalism as a progressive form against feudal relationships, hoping to see its own collapse, Piketty demonstrates that that the advancement of capitalism must be tamed in order to be perfected. Instead of waiting for the collapse of the system, Piketty proposes a global solution: information and taxes.

The piece connecting John Doe’s whistleblowing with Piketty’s work is Gabriel Zucman’s, *The Hidden Wealth of Nations: The Scourge of Tax Havens* (2015) (with a foreword by Thomas Piketty). The policy proposal

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- a Tool for Your Organisation’s Success | STEP. Accessed May 22, 2018. <http://www.step.org/news/us-treasury-presses-congress-beneficial-ownership-legislation>.

<sup>30</sup> “Tax Reform Should Close Offshore Loopholes, End Tax Haven Abuse.” FACT Coalition. February 24, 2016. Accessed May 21, 2018. <http://thefactcoalition.org/tax-reform-should-close-offshore-loopholes-end-tax-haven-abuse/>.

<sup>31</sup> “President Barack Obama on Tuesday Championed New Federal Steps to Discourage Corporate Tax Dodging through a Practice Known as “inversions” and Called on Congress to Close the Loophole “for Good”.” U.S. News & World Report. Accessed May 21, 2018. <http://www.usnews.com/news/business/articles/2016-04-05/obama-to-address-new-rules-to-deter-tax-inversions>.

advanced in this book is a “worldwide register of financial wealth recording who owns what in stocks and bonds.” Zucman’s normative assumption is correct: “Each country has the right to choose its forms of taxation.”<sup>32</sup> But no country should have the right to craft laws, policies and institutions with the purpose of poaching on the tax bases of other countries. Zucman is aware that multinationals are within the boundaries of the law, if not the purpose of the law, when using tax avoidance strategies. Yet, he estimates that for US firms alone the costs of tax avoidance are 130 billion “and since equity ownership is very concentrated, it essentially benefits only the wealthiest among us.”<sup>33</sup> A worldwide register of financial wealth, recording who owns stocks and bonds, may begin by consolidating the fragmentary, private financial registries that already exist —such as the Depository Trust Company in the United States and the Luxembourg bank Clearstream. And also, by transferring “ownership of the data to the public.” “Combined with an automatic exchange of information between the banks of all tax havens and foreign tax authorities, a financial register would deal a fatal blow to financial secrecy.”<sup>34</sup> Also, we should consolidate worldwide the taxation of multinationals.<sup>35</sup>

Briefly, the Paradise Papers and Panama Papers leaks showed that eliminating secrecy jurisdictions is necessary to begin healing capitalism’s illnesses: If tax havens were eliminated, most of our income inequality problems would be ameliorated; if tax havens were eliminated, revenue would flow to governmental coffers to finance social needs; if tax havens were eliminated or at least all the transactions conducted through them were transparent, the world would be a better place. Out of shame of being caught, wealthy people, and most importantly, lawyers, accountants, and financial advisors worldwide would stop abusing loopholes for the benefit of their respective clients or taking advantage of the lack of cooperation on taxation matters among countries. It is first and foremost an ethical issue, as the professionals, endowed with special licenses to practice their professions for the benefit of society, should realize that the tax laws are adopted through a democratic deliberative process, and therefore they should advise their clients to fulfill the law’s objectives.

Following the revelations of the Paradise and Panama Papers, there are tax dodgers, governments and lawyers with questionable ethics helping

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<sup>32</sup> Gabriel Zucman, *The Hidden Wealth of Nations, The Scourge of Tax Havens* (2015) (with a foreword of Thomas Piketty) at 1.

<sup>33</sup> *Id.*

<sup>34</sup> *Id.* at 5.

<sup>35</sup> *Id.* at 116.

the tax dodgers, and what is needed is more transparency and more penalties to deter the abuses. In this inglorious narrative, there are heroes, evil-doers, victims and bystanders.<sup>36</sup> We wish it were this simple.

The truth is murkier. The narrative of bad and good players soothes us and makes us look away from other explanations of how the rigged global tax regime complex exposed by the Paradise and Panama Papers was possible. It leads to mainly symbolic policy solutions that would leave unanswered John Doe's calls for restoring good governance on taxation matters.

### **Yes, to transparency but the default should be the privacy of citizens: Neither government surveillance nor surveillance capitalism!**

The tax haven debate and their revelations of the Swiss, Lux, and most recently, the Paradise and the Panama Papers shows that the state system is maturing toward a more coordination on taxation and its enforcement. This is good news.<sup>37</sup> But we must remain vigilant before moving irreversibly towards total transparency on taxation matters. Governments cannot be trusted completely nor should individuals be left completely to their own devices. By default, in liberal democratic societies, or in good societies, we should give the individuals the upper-hand. Governments have to justify their actions, not their citizens.

As part of the power of the sovereign, fiscal policies should consider spillover effect and tax systems should not be purposely designed to facilitate circumvention of foreign tax laws. This principle should be unquestionable. But a degree of confidentiality is paramount for protecting privacy. For that purpose, a weak version of transparency would suffice and self-regulation mechanisms for professionals such as lawyers, accountants, and financial advisors, coordinated globally, could be more effective in managing tax abusive schemes while preserving privacy. Even accepting at face value John

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<sup>36</sup> "The Panama Papers: Exposing the Rogue Offshore Finance Industry." ICIJ. Accessed May 22, 2018. <https://www.icij.org/investigations/panama-papers/>.

<sup>37</sup> If we take into account that the era of artificial intelligence is already here and its social impact can be sustained only through, e.g., a universal basic income that most likely will be funded through taxation, transparency among jurisdictions in taxation matters is a must. [To ameliorate the social impact of artificial intelligence world we may want to consider a basic universal income. To finance universal basic income is a must of a new economy based more and more on AI. "This means that tax rates will have to be high." And it means also that tax systems among nations need to be coordinated as well as social security systems (<https://goo.gl/bJUBkg>)].

Doe's arguments about a failure of governance, certain principles need to be kept in place in order to protect individual privacy, or a new governance arrangement must be devised to correct that failure; otherwise, the reform efforts could maintain power imbalances among countries.

Also, international reform proposals for more transparency assume that there are other corrupt societies in which the 'offshore' business can take place, and that players in these societies, also members of the elite, accept the role of gatekeepers of an insidious asset protection industry. This is inaccurate and unfair. We should move past facile prejudices. Some people believe that the corrupt are 'the other', while they are not or are less corrupt. It is not a coincidence that Stieglitz and Pieth, after renouncing the Panama Commission, called for America and Europe to close guards against tax heavens, a recommendation that echoes John Doe's. Somehow, they seem oblivious to acknowledge the cradles of the offshore industry. It is Wall Street and London, and, yes, it is also Panama, and Grand Cayman, among others, where by lack of institutions, deliberately or unintentionally, the conditions are propitious for playing "the role of elsewhere" for financial transactions.<sup>38</sup> But, if we do not explain these power imbalances and the role that the 'us vs. them' mentality plays in the tax heavens debate, the digitized revolution begun by John Doe with the leak of the Panama Papers will be betrayed or, worse, forgotten.

We should explore whether the notion of tax avoidance —different from tax evasion— is and should be a necessary corollary of using taxation to influence behavior. Both tax avoidance and tax evasion are a by-product of taxation's in-built disparities. We should devise governance arrangements that presume the honesty of taxpayers/citizens. The global tax regime complex should not render entire categories of citizens and countries suspect just because they try to minimize their tax bills using corporate entities. It is not a coincidence that some U.S. Senators opposed FATCA precisely because it "turns the 4th Amendment on its head, it presumes that every American with money overseas is a criminal." *The Unintended Consequences of FATCA, Part*

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<sup>38</sup> Nicholas Shaxson explained clearly what tax heavens are in his book, *Treasure Islands, Uncovering the Damage of Offshore Banking and Tax Havens*, 2011. It is elsewhere that becomes nowhere. Or better, it is a place that operates "in the gaps between jurisdictions. Elsewhere becomes nowhere." at 6. More importantly, the institutional design is driving by centers, London, Wall Street, benefiting the financial institutions and the elites in both center and peripheral jurisdictions. "Offshore connects the criminal underworld with financial elites and binds them together with multinational corporations and the diplomatic and intelligence establishments." *Id.* at 10. See also Nicholas Shaxson, *How to Crack Down on Tax Havens: Start With the Banks*, *Foreign Affairs*, March/April, 97, No. 2 (2018), at 94-107.

I, Senator Paul (<https://goo.gl/xbtNaa>).

Similarly, to the point that governments need some degree of confidentiality in order to operate efficiently, private citizens also need some degree of confidentiality to make decisions as free individuals in a democratic society. More importantly, the social contract underlying the justification of a government requires it.

## **Of Spillovers, tax avoidance and transparency.**

John Doe's revelations signal the strengthening of a norm essential for an effective global taxation regime complex: No jurisdictions should design, adopt, or implement fiscal and corporate policies that intentionally create opportunities to negatively impact the tax base of other countries. A reliable test for determining potential negative spillover effects should be developed. Luisa R. Blanco & Cynthia L Rogers, found "evidence of positive spillovers from tax havens to nearby developing countries, but not to nearby developed countries." (Are Tax Havens Good Neighbor's? FDI Spillovers and Developing Countries, 50 Journal of Development Studies 530 (2014), <https://goo.gl/GsaRwn>).

Yet, the distinction between tax avoidance and tax evasion should be maintained as a way of giving the benefit of the doubt to the citizens taxpayers. However, with the Panama Papers' revelations, the difference between tax avoidance and tax evasion has been blurred. This change is taking place in several ways:

a. using tax avoidance as a general category under which tax evasion is subsumed; b. adding the distinction of "abusive" to the notion of avoidance; and c. creating a presumption of abusive (illegal, criminal) tax avoidance when corporate entities conducting transactions across jurisdictions are involved. These conceptual strategies distinguish between legal and illegal behavior and between legal and unethical behavior. More importantly, they strategies shift the assumption of avoidance as a legal, legitimate activity of taxpayers to assuming avoidance as suspicious, in principle, of being either illegal in the same terms as tax evasion; or ethically illegitimate in terms of selfish disregard of socially responsible objectives. Let's look at some of these strategies. Traditionally, tax avoidance is defined as "[A]n action taken to lessen tax liability and maximize after-tax income"; while tax evasion is "the failure to pay or a deliberate underpayment of taxes."<sup>39</sup> Tax avoidance is considered a "right

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<sup>39</sup> Internal Revenue Service, U.S. Department of the Treasury, *Worksheets Solutions, The Difference Between Tax Avoidance and Tax Evasion... Part 25. Special Topics*,



of taxpayers”. They may “reduce, avoid, or minimize their taxes by legitimate means.” Concealment or misrepresentation are not allowed, but “shaping and pre-planning events to reduce or eliminate tax liability within the parameters of the law” is allowed.<sup>40</sup>

Conversely, evasion involves “some affirmative act to evade or defeat a tax, or payment of tax. One of the most relevant acts in relation to the Panama Papers is the use of corporations to conceal or camouflage actions” or make things seem other than they are.” Taxpayers have the right to minimize taxes using legal means and the corollary obligation to report income voluntarily. Using, for instance, sham corporations may indicate concealment or camouflaged actions. In such cases, accountants and lawyers go beyond the exercising of a right of taxpayers to avoid taxes to “making things seem other than they are.”<sup>41</sup>

Now, the use of a corporate entities and trusts would call for additional justification from the taxpayer to show that they are not using them either separately or in the aggregate for concealment purposes across several jurisdictions. The traditionally required disclaimer of tax consequences and compliance with the laws of other countries used in those jurisdictions that provide incorporation services no longer suffices. Lawyers may now have an affirmative duty to verify the role played by an entity in the overall structure of a transaction. This conceptual shift calls for the professional advising on tax, corporate, and financial matters to discharge their respective professional duties with an eye to the impact of their advice on the integrity of several tax systems, even if it is not legally required.

An example of conflating tax avoidance with tax evasion and using the abusive tax avoidance category to call for a professional ethical duty is found in the work of Gillian Brock and Hamish Russell. They said in *Abusive Tax Avoidance and Institutional Corruption: The Responsibilities of Tax Professionals*,<sup>42</sup> that revering the letter of the law does not suffice for professionals, accountants, lawyers, and financial advisors in discharging their

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*Chapter 1. Fraud Handbook, Section 1. Overview/Definitions, 25.1.1.24 (01-23-2014), Avoidance vs. Evasion, [https://www.irs.gov/irm/part25/irm\\_25-001-001.html#d0e80](https://www.irs.gov/irm/part25/irm_25-001-001.html#d0e80).*

<sup>40</sup> *Part 25...Special Topics.*

<sup>41</sup> *Cf. generally Tanina Rostain and Milton C. Regan, Jr. Confidence Games: lawyers, accountants, and the tax shelter industry (2014) (explaining the abusive tax shelter industry in the U.S. from 1994 to 2004, the authors stated that “[t]o focus on the wrongdoing of individual participants is to miss the institutional factors that contributed to the tax shelter episode.” Id. at 7).*

<sup>42</sup> *Edmond J. Safra Working Papers, No.56, Feb. 17, 2015, [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2566281](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2566281).*

duties vis-à-vis their clients. Even in the ideal situation in which the letter of the law is respected, advice given and service rendered that shape transactions in a way that limit the tax authorities to collect tax revenues efficiently and equitably is not morally permissible. Brock and Russell, however, use the notion of abusive tax avoidance as an umbrella term to refer to an “explicit tax reduction that is contrary to the spirit or intent of the law”.<sup>43</sup> In their view, using abusive tax avoidance as a general category comports better with a purposive reading of tax law over a literalist reading of tax law. After conflating tax evasion and avoidance in one category, Brock and Russell, rely on an estimated by Christian Aid, stated that developing countries lose \$160 billion year. The estimated losses for developed countries, according to Brock and Russell, was \$385 billion for 2006, based on IRS numbers. If these estimates are accurate, the consequences for governments and inhabitants in some jurisdictions are dire: there are fewer revenues to finance for instance public projects, healthcare, education, and security; and the less well-off people are worse off as they lack the savvy and means “to reduce their effective tax burdens.” “Multinational corporations and wealthy individuals — who are best positioned to contribute revenue to public coffers and who consequently should bear the greatest responsibilities to contribute— are able to avoid an alarming proportion of their tax obligations through complex and contrive arrangements.”<sup>44</sup> According to Brock and Russell, this additional imbalance between rich and poor is again the result of the rich being able to pay for sophisticated and complex legal, financial, and accounting arrangements, while the poor cannot.

Yet, governments and taxpayers have responsibilities in the tax avoidance market: demand by corporations and high net worth individuals to

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<sup>43</sup> *Id.* at 1 and 11. Cite also Russell and Brock in the Human Journal... To cite this article: Hamish Russell & Gillian Brock (2016) Abusive Tax Avoidance and Responsibilities of Tax Professionals, *Journal of Human Development and Capabilities*, 17:2, 278-294, DOI: 10.1080/19452829.2015.1091810. To link to this article: <http://dx.doi.org/10.1080/19452829.2015.1091810>.

<sup>44</sup> *Id.* at 5. See also Brock, *Abusive Tax Avoidance and Responsibilities of Tax Professionals*, on file with author, including within *Abusive Tax Avoidance ‘Tax Evasion’* “that directly violate the letter of the law’s spirit or intent. Abusive tax avoidance is thus a broader category than tax evasion. By focusing on abusive tax avoidance, we are following the approach of tax enforcement authorities in the United States, United Kingdom, Canada and several other countries.” (relying on “See, for example, US Government Accountability Office (GAO), *Abusive Tax Avoidance Transactions: IRS Needs Better Data to Inform Decisions About Transactions* (Washington D.C.: GAO, 2011), p. 1; HM Revenue and Customs, “HMRC’s GAAR Guidance,” (HMRC, 2013), available at: <http://www.hmrc.gov.uk/avoidance/gaar-part-abc.pdf>).

minimize their tax bill (supply) and supply-side that professionals (accountants, lawyers, and financier) providing the know-how. For instance, technology facilitates communication for instance for 'transfer mispricing', weakening even further the arm-length condition to consider these types of transactions legal; Tax havens jurisdictions offering minimal or zero tax rates design their laws to facilitate infringement of the laws of other jurisdictions, involving complex tax laws and an abundance of loopholes.

A developing country playing the role of tax haven sees its own domestic institutions weakened as it consolidates the international perception of corruption by catering to external players circumventing laws in foreign countries by exploiting lack of coordination among them vis-à-vis paying taxes. Brock and Russell remind us that these intermediaries have duties to maintain the integrity of the system. The large accounting firms facilitate the tax-avoidance of the corporations. Deloitte, PricewaterhouseCoopers and Ernst & Young, and KPMG (The Big Four).

Similar arguments apply to law firms. As they are an integral part of the tax shelter industry, they should have the responsibility to remedy it, for instance, by advising legislatures on the design of better tax laws. The problem with this suggestion is that accountants and lawyers represent private interests and cannot be put in the role of correcting defective legislation, which could have intentionally created the loopholes to benefit certain interests in a society. Brock and Russell mentioned a test adopted in Canada to determine whether there is abusive tax avoidance: "In moving to a purposive reading of tax law, some countries have adopted a general anti-avoidance rule (GAAR)," which basically is a version of the economic substance test. Applying the anti-avoidance rule, the Canadian Supreme Court asks "1. Was there a tax benefit? 2. Was the transaction arranged for any bona fide purpose other than to avoid taxes? 3. Was the tax benefit obtained consistent with the object, spirit or purpose of the provisions relied upon?" Private professional advising clients should not be put in a position of deciding where the line is drawn for the overall benefit of the tax base of a country, however (See generally Brian Arnold, A comparison of statutory general anti-avoidance rules and judicial general anti-avoidance doctrines as a means of controlling tax avoidance. Which is better? (What would John Tiley think?), <https://goo.gl/e6dzzi>).

Individuals may try to push the boundaries of the avoidance and of course let the authorities decide. What it should not be allowed, of course, is blatantly deceiving the authorities among jurisdictions. But there should be no responsibility by private players to inform tax authorities of loopholes.

Using incentives beyond punishments to nudge players to include public, systemic goods, into their actions is a different matter, and could

actually be more effective, as recent studies suggest.<sup>45</sup> Also, affirming how corporate social responsibility adds value may be a more effective way to discourage tax avoidance, even when legal, but may have a negative systemic impact.<sup>46</sup>

To ask practitioners to pay attention to the purpose of the law of several jurisdictions is challenging because the corrupting impact may be found in the aggregation of the discrete transactions. In this case, each transaction may be legal in-and-of itself, but the overall outcome of the transactions is abusive. How should these standards be determined? Obviously, we could begin by saying that the authority in charge of regulating the professions in the respective jurisdictions providing the services should be the one setting those standards. For instance, the impact of the aggregated transactions may be abusive as a result of unintended consequences of a loophole in one jurisdiction in combination with others and therefore it should not be disavowed. Yet, if the impact is the result of policies intentionally designed to take advantage of the loopholes elsewhere, then the transaction should be considered abusive and therefore voidable.

To require practitioners to assess the tax consequences of multi-jurisdictional transactions would be daunting. It might be necessary to institute a recognized transnational certification scheme provided by bar associations or by an agreed upon authority. This certification scheme would attest that the outcome of a particular transaction using corporate entities or trusts is legal in light of laws of the requesting client subject to a particular jurisdiction and that as a whole does not result in tax evasion. But again, this implies that tax avoidance strategies should be allowed.

Another example of blurring the distinction between tax avoidance and tax evasion is found in Australia. Since 2008, John McLaren pointed out that the Australian government blurred the distinction between tax avoidance and tax evasion for purposes of the Australian taxpayers using tax havens to minimize taxes.<sup>47</sup> Some Australian statutes for instance disregard the

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<sup>45</sup> Kristina Bott, Alexander W. Cappelen, Erik Erik Ø. Sørensen, and Bertil Tungodden, *Research: Moral Appeals Can Help Reduce Tax Evasion*, *Harvard Business Review*, July 20, 2017, <https://hbr.org/2017/07/research-moral-appeals-can-help-reduce-tax-evasion>.

<sup>46</sup> See *Does Corporate Social Responsibility Add Value? Evidence from Capital Structure and Product Markets Interactions*, "Http://journal.ru/wp-content/uploads/2016/08/d-2016-154.pdf." 2016. Accessed May 21, 2018. doi:10.18411/d-2016-154.

<sup>47</sup> *Journal of the Australasian Tax Teachers Association 2008 Vol.3 No.2, The Distinction Between Tax Avoidance and Tax Evasion has become blurred in Australia: Why has it Happened? John McLaren.*

distinction and address instead ‘tax exploitation schemes’ or require attorneys, accountants and financial advisors to report suspicious transactions in which the transfer of money take place between tax havens. The presumption here is that if taxpayers use tax havens they are suspected of tax evasion, unless they can show otherwise. The professionals providing tax advice in this area have an additional duty of first not furthering avoidance structures, and secondly of reporting when the activities are suspicious. In other words, the distinction between tax avoidance (legal) and tax evasion (illegal) is kept, unless tax havens are involved. Domestically, the presumption is that it is used for tax avoidance unless proven otherwise. If tax avoidance amount to tax evasion or a presumption of tax evasion, then the need to verify that it is not rests upon the shoulders of the taxpayers and their advisors. In addition, financial institutions can be required to disclose information about the transactions in question to the relevant authorities. For domestic taxation issues the differentiation between tax avoidance and tax evasion still holds; but the difference does not hold for taxation issues involving tax havens or OFC. “The AML/CTF Act would appear to designate that all measures to reduce and minimise income tax through the use of tax havens constitutes criminal activity.”

Joseph E. Stiglitz and Mark Pieth, in their report “Overcoming the Shadow Economy,” argued that a positive globalization must deal with secrecy jurisdictions. They wrote the report after resigning from a Panamanian Committee addressing the aftermath of the Panama Papers leak. These secrecy jurisdictions “facilitate both money laundering and tax avoidance and evasion, contributing to crime and unacceptably high levels of global inequality.”<sup>48</sup> This was, recall, John Doe’s motivation for becoming a whistleblower. Notice that Stiglitz and Pieth put together tax evasion and tax avoidance based on the authority of the Black’s Law Dictionary (2nd. Ed. 2001). In a footnote, they write, “Tax evasion is defined as reducing tax payable by fraudulent (i.e. illegal) means while tax avoidance is defined as lawful tax liability minimization.”<sup>49</sup> The arguments advanced by Stiglitz and Pieth to justify full transparency on taxation matters are well-known: privacy is a matter of cultural attitudes ranging from Norway, Sweden, and Finland publishing tax returns online to the Philippines considering disclosure of tax returns as an invasion of privacy punishable as a crime.<sup>50</sup> Given the fact that there are free riders taking advantage of public goods without paying their fair share by making use of secrecy jurisdictions, there is no place for secrecy on

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<sup>48</sup> *Overcoming the Shadow Economy*, at 4, 2016.

<sup>49</sup> *Id.* at 4.

<sup>50</sup> *See id.* at 5.

tax matters. Secrecy jurisdictions exist because Europe and America allow them. Yet, growing inequality within these societies is rendering the upholding of secrecy jurisdictions more difficult to justify. Transparency must be global to be effective.<sup>51</sup> Keeping the conceptual differentiation between tax avoidance and tax evasion, Stiglitz and Pieth pointed out that a reading of the data from the Panama Papers reveals legitimate uses of corporations, but also blatant tax fraud by individuals and companies. “These structures have enabled and in fact incentivized such heinous abuses of the most vulnerable.

At the same time, these structures are developed and used by respected global corporations to avoid taxation on massive wealth, in the trillions of dollars.” They affirm that institutions in place to allow for this to happen are the following: transfer pricing manipulations, existence of “tax-free special economic zones and preferential tax treatment for incorporating entities”. All of these institutions are legal, independently, but result in undesirable corrupting results: they affect the tax base of countries, leaving less revenues for social programs, and investments in infrastructure, technology, and education. Briefly, they facilitate what Lawrence Lessing calls institutional corruption.

Stiglitz and Pieth ask rhetorically “[W]hat, if any, are the social benefits of these complex and opaque arrangements? It is increasingly apparent that there are huge social costs.” “From a global perspective, this form of competition is destructive...Indeed, tax competition leads to higher inequality and poorer public services.” More problematic, is the connection to secrecy; money laundering for example: “illicit profits to do both conceal origins, but also to avoid taxation.” Only the elite in a country service provider that benefits from those secrecy-havens. Stiglitz and Pieth put forward an interesting proposal. Given the existence of institutions that are open to both legal, illegal, legitimate and illegitimate traffic, if a country wishes to continue providing these services, then “fuller transparency, strengthened monitoring, and consistent enforcement is required.”

This sound proposal should be complemented by methods of protecting the privacy and bolstering the default position of having governments to demonstrate the need for access to otherwise private information rather than the other way around.

In general, according to William B. Barker, the problem lies in an ideology that supports tax avoidance as a matter of enhancing liberty. “Up to 2009, the US federal courts have favored a strict or literal interpretation of tax law that facilitates tax avoidance buttressed “by an ideology of liberty.” Baker argues that “tax avoidance justifying ideology is anti-democratic. The

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<sup>51</sup> See *id.* at 6.



persons/tax payers have a right to avoid, instead of a duty to pay. This is the ideology that needs to be eradicated from taxation matters.” And this is precisely the norm that the Paradise Papers and the Panama papers revelations set out to change. Supported by Judge Learned Hand’s famous words stating that tax avoidance is legal and legitimate; today tax avoidance might be legal, but it certainly seems less legitimate. As President Obama’s said about using transfer-pricing and taking advantages of loopholes, the actors may be acting legally, but certainly not ethically.

A bar association could play a role here by self-regulating the activity of the professions and their respective specializations. For instance, lawyers could be restricted from entering into certain investment arrangements and to have stricter responsibilities vis-à-vis the whole system when dealing with taxation matters.

Tax avoidance should be maintained as long as taxation is used to induce certain kinds of individual behavior. Certainly, the payment of taxes presents a classical Olsonian problem of free riders enjoying public goods and also a classical “philosopher king model’s problem of how politicians and government officials act. In contrast to domestic tax policy, “[t]he same philosopher king model of government behavior remains relatively influential in the international tax policy context.” (S. Dean, *Philosopher Kings and International Tax: A New Approach to Tax Haven, Tax Flight, and International Tax Cooperation*, <https://goo.gl/3pRJ5z>). “The standard explanation for cross-border tax cooperation embraces the most improbable form of the model by assuming that cooperation occurs simply because it is economically efficient and increases the GDPs of both participating nations.” Id.

Perhaps it is possible to find insights from behavioral economics in devising incentives to pay taxes beyond the compulsory tools of criminal law. Such insights could help reduce enforcement costs and would enhance social trust in and across societies. In the end, the Paradise Papers and Panama Papers leaks are acts of political expression of another component in the struggle against global inequality. We should all welcome this, but we should not be naïve regarding the methods and risks involved. To have chosen ‘Panama Papers’ as the name of the leak serves to conceal the reality that users and services are usually located in wealthy countries rather than Panama. It is common knowledge that there are lawyers in the US or Europe that would go to great lengths to ask Panamanian lawyers confidentially to organize corporations and to open bank accounts as long their names remain anonymous in the documentation.

At any rate, transparency on tax matters should be coupled with strong privacy protections for taxpayers since the default should be trusting taxpayers against the potential abuses of governments.

## **Keeping the door ajar**

Tax havens are partly the result of using taxes for inducing individuals' behavior by governments. When citizens have the right to arrange their affairs to minimize taxes, they remind governments that they are the principals in the social contract. Government should not have the upper-hand vis-à-vis its citizens. For instance, profit opportunities in environmental crime stem from the same structures that benefit all criminal activities —the rules, restrictions, regulations— governments put up to control behavior. Organized crime makes money by circumventing these structures. Furthermore, when an activity or product is made illegal, criminals necessarily capture a monopoly on that activity or product. Regulation and law creates a form of scarcity for the product or activity, thus raising its price for those willing to pay and the potential for significant profits in exploiting the commodity. Governments establish environmental protection regimes for a variety of legitimate and illegitimate reasons, usually to prevent total exhaustion of resources or to allow politicians to maintain webs of patronage. Enforcement of such regimes is vulnerable to corruption, which becomes an avenue to control the flow of illegal rents and ensure patronage. Taxes on legal goods create incentives to pursue unregulated and untaxed sources of supply, such as high prices to legally recycle electronics in industrialized countries that, as a result, create incentives to illegally dispose of such goods in developing countries. Perhaps it is time to think about other ways of having individuals and corporations make better decisions on taxation matters beyond putting all conduct under the umbrella of tax evasion as a crime. Again, insights from the field of behavioral economics may be useful here.

When tax havens facilitate illegal activity in general (e.g. migration, tax evasion, human trafficking, prostitution, smuggling, but also serve other legitimate purpose, should policy solutions try to eliminate them or keep their use within certain acceptable levels?

Would it be more effective to give ethical training to key players in the operation of tax havens such as lawyers and accountants so that they become aware of the consequences of their role in sustaining tax havens? This is what Gillian Brock and Hamish Russell propose.

Would it be better to look for ways of preserving tax havens, but with heightened scrutiny? This is what Joseph Stiglitz and Mark Pieth propose. Specialized, trained lawyers, accountants, and other professionals involved in the operation of tax havens will be apt to account not only for the national, but also the transnational consequences of their advice. And this would foster institutional and social trust while preserving individual privacy.

Technological capability is available to identify non-compliance, making our lives completely transparent, as suggested in the movie *The Circle* (<https://goo.gl/ATZSo2>) or to put ourselves under constant surveillance of the sort denounced by Snowden (<https://citizenfourfilm.com/>). But the fact that is feasible, does not mean that it should be done. As it is well-known, Facebook connects not only family and friends but also foreign hackers and ‘troll farms’ that can influence election results (<https://www.nytimes.com/2018/03/22/opinion/democracy-survive-data.html>). Thus, technology should be an instrument to protect essential values (e.g. privacy), and not to shift the onus to citizens in favor of the ostensive needs of governments. It should be the other way around. We need a ‘trust but verify’ mechanism.

### **Would ‘Bitcoin Jesus’ save us? And let’s go all the way to Delaware: Ensuring both transparency and privacy with delayed traceability**

“Bitcoin Jesus” is a good example of trying to escape the certainty of taxes. The U.S. has a universal taxation system. “Roger Ver, an ex-U.S. citizen, ex-convict, millionaire investor, self-describe libertarian and founder for Passports for Bitcoin... [is promoting] the right to live in the Federation of St. Kitts and Nevis, two sun-kissed islands a three-hour flight from Miami.”<sup>52</sup> There are no taxes on personal income or capital gains, and secrecy about financial affairs. Bitcoin, a currency that so far can be used without government oversight, has been furthered by libertarians, such as “Peter Thiel, who plans also to build an artificial island where people can do whatever they want.”<sup>53</sup> Bitcoin can also be used by people who trade in illicit commodities

<sup>52</sup> Jason Clenfield and Pavel Alpeyev, ‘Bitcoin Jesus’ promises a virtual paradise, *the Washington Post*, June 23, 2014, [https://www.washingtonpost.com/business/bitcoin-jesus-promises-a-virtual-paradise/2014/06/19/c050eb38-f59a-11e3-a606-946fd632f9f1\\_story.html](https://www.washingtonpost.com/business/bitcoin-jesus-promises-a-virtual-paradise/2014/06/19/c050eb38-f59a-11e3-a606-946fd632f9f1_story.html). “Roger Ver.” Wikipedia. May 25, 2018. Accessed May 27, 2018. [https://en.wikipedia.org/wiki/Roger\\_Ver.](https://en.wikipedia.org/wiki/Roger_Ver;); “St Kitts Nevis Citizenship Program.” St Kitts Nevis – Citizenship by Investment. Accessed May 27, 2018. <http://stkitts-citizenship.com/visa-free-travel/>.

and services. People who go to St. Kitts try to escape responsibilities, according to John Christensen of the Tax Justice Network.<sup>54</sup> Yet, the underlying blockchain technology of bitcoin can also be used to enhance the transparency of corporations while preserving individual privacy. When cryptocurrency wallets become big enough they have the potential to become “super tax havens” as described by University of California-Irvine law professor Omri Marian.<sup>55</sup>

Since cryptocurrencies, including bitcoin, are only taxed when they are converted into fiat currencies, they have become an alluring venture for not just trading cryptocurrencies but also storage as assets. Cryptocurrencies possess characteristics that resemble tax havens such as earnings not being subject to taxation and the anonymity of users or potential taxpayers being upheld. Authorities across many countries are scrambling for solutions to prevent cryptocurrencies from turning into tax havens. However, they might be late since an increasing number of people are exchanging their fiat currencies into cryptocurrencies, indicated by the rise in market cap and surge in the price of bitcoin<sup>56</sup> and other cryptocurrencies.<sup>57</sup>

Yet, offshore tax havens are still going strong, as indicated by the Financial Secrecy Index. Switzerland still occupies the first place with the USA improving its ranking to stand second in 2018 (from 3rd in 2015).<sup>58</sup> There are still trillions of dollars that are stashed in these traditional tax havens despite media reports announcing their decline. Also, these offshore markets are regulated with deep financial roots backed by governments which enable easier transactions albeit saving few transparency laws that put their customers identity in jeopardy. In addition, tax havens are relatively nonvolatile and stable, with millionaire clientele across the world who not only invest but also expand and diversify these assets that are not yet fully accounted for.<sup>59</sup>

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<sup>53</sup> *Id.*

<sup>54</sup> *Id.*

<sup>55</sup> Marian, Omri Y., *Are Cryptocurrencies ‘Super’ Tax Havens?* (October 1, 2013). 112 *Michigan Law Review First Impressions* 38 (2013). Available at SSRN: <https://ssrn.com/abstract=2305863>.

<sup>56</sup> Verhage, Julie. “Bitcoin’s Epic Rise Leaves Late-1990s Tech Bubble in the Dust.” *Bloomberg.com*. August 29, 2017. Accessed May 23, 2018. <https://www.bloomberg.com/news/articles/2017-08-29/bitcoin-s-epic-rise-leaves-late-1990s-tech-bubble-in-the-dust>.

<sup>57</sup> “Crypto - Bloomberg.” *Bloomberg.com*. Accessed May 23, 2018. <https://www.bloomberg.com/crypto>.

<sup>58</sup> *View 2018 Results*. Accessed May 20, 2018. <https://www.financialsecrecyindex.com/introduction/fsi-2018-results>.

<sup>59</sup> “A New Study Details the Wealth Hidden in Tax Havens.” *The Economist*. October

Comparatively, crypto currencies are not regulated thoroughly and the few or underdeveloped laws and regulations are still under-developed, financially and otherwise, concerning cryptocurrency usage and storage.<sup>60</sup> Cryptocurrencies are extremely volatile, particularly in recently during which prices have fluctuated wildly resulting in overnight millionaires. However, with the burgeoning number of Initial Coin Offerings (ICOs), fraudsters are arriving in the market with Ponzi schemes and scrupulous designs as seen in the case of Gnosis ICO, which was incongruously valued at 300 million dollars.<sup>61</sup> As a result, currencies are now facing continuous challenges from regulators across the world who are actively clamping down on these markets and companies.<sup>62</sup> Governments have intensified actions such as banning transactions, raiding offices and even curtailing mining operations for the currencies.

In addition, technology companies are taking sides, with Google and Twitter to ban advertisements for cryptocurrencies in order to prevent the spread of malicious promotional activities.<sup>63</sup> Notwithstanding these constraints, cryptocurrencies are gaining an audience across the world. One particular instance is the Venezuelan government, which recently issued its own cryptocurrency, named the “petro”.<sup>64</sup> Venezuela is promoting this currency through its fossil fuel transactions and backing it by oil reserves, gold and other minerals. Venezuela offered India, which is facing high crude oil

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07, 2017. Accessed May 23, 2018. <https://www.economist.com/finance-and-economics/2017/10/07/a-new-study-details-the-wealth-hidden-in-tax-havens>.

<sup>60</sup> Magazine, Bitcoin. “Cryptocurrency Regulation in 2018: Where the World Stands Right Now.” *The Next Web*. April 27, 2018. Accessed May 23, 2018. <https://thenextweb.com/hardfork/2018/04/27/cryptocurrency-regulation-2018-world-stands-right-now/>.

<sup>61</sup> Morris, David Z. “The Rise of Cryptocurrency Ponzi Schemes.” *The Atlantic*. May 31, 2017. Accessed May 19, 2018. <https://www.theatlantic.com/technology/archive/2017/05/cryptocurrency-ponzi-schemes/528624/>.

<sup>62</sup> Drousseau, Ryan. “All The Places Cracking Down on Bitcoin and Cryptocurrency | Money.” *Time*. March 19, 2018. Accessed May 20, 2018. <http://time.com/money/5198439/all-the-places-now-cracking-down-on-bitcoin-and-cryptocurrencies/>.

<sup>63</sup> Rooney, Kate. “Twitter Bans Cryptocurrency Advertising, Joining Other Tech Giants in Crackdown.” *CNBC*. March 26, 2018. Accessed May 20, 2018. <https://www.cnn.com/2018/03/26/twitter-bans-cryptocurrency-advertising-joining-other-tech-giants-in-crackdown.html>.

<sup>64</sup> Karsten, Jack, and Darrell M. West. “Venezuela’s “petro” Undermines Other Cryptocurrencies – and International Sanctions.” *Brookings*. March 09, 2018. Accessed May 20, 2018. <https://www.brookings.edu/blog/techtank/2018/03/09/venezuelas-petro-undermines-other-cryptocurrencies-and-international-sanctions/>.

prices, a 30% reduction on the price of oil if the transaction is made using the petro.<sup>65</sup> However, major economies have denounced the petro and banned all petro transactions. Furthermore, the Venezuelan parliament declared the petro illegal as a fraud perpetrated by President Nicolás Maduro.<sup>66</sup> While the petro signifies the entry of crypto currencies into mainstream macro transactions as the World's first government-backed cryptocurrency, its fall reminds us of its inherent problems. Whether tax havens get a new (virtual) address remains to be seen.

Cryptocurrencies, particularly bitcoin, are just one of many varied applications enabled by the blockchain technology.<sup>67</sup> Any process that depends on middlemen or third parties for verification, from financial services (e.g. insurance and asset management) to governance (e.g. elections) to trade, is a prime candidate for blockchain application. In a blockchain world, contracts are embedded in digital code and stored in transparent, integrated databases that are immutable and not tamperable, by design, also called smart contracts. In this world, every agreement, process, task and payment has a digital record and signature that can be identified, validated, stored, and shared. Intermediaries such as lawyers, brokers, and bankers become obsolete. Individuals, organizations, machines, and algorithms freely transact and interact with one another with hardly any friction. The issues of trust that hound so many collective action problems become less salient. This is the immense transformative potential of blockchain.

Corporate governance is undergoing this transformation through blockchain. The major areas include voting and shareholding in the companies, compliance to various regulators, and recordkeeping. While voting inside boardrooms and shareholders voting under blockchain would be more reliable and transparent, companies can also ease the auditing process through real-time accounting and compliance enforcement through algorithms. Institutional investors would arguably have a difficult time disguising their trades due to greater transparency of blockchain technology,

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<sup>65</sup> Anand, Nupur. "India Must Decide If It Hates Cryptocurrencies More than a Good Oil Deal." *Quartz*. May 02, 2018. Accessed May 20, 2018.

<https://qz.com/1267691/venezuela-woos-india-with-30-discount-on-crude-oil-if-paid-in-its-cryptocurrency-petro/>.

<sup>66</sup> "A Fraud: Venezuela's National Assembly Declares Petro Unconstitutional." *CCN*. March 07, 2018. Accessed May 23, 2018. <https://www.ccn.com/venezuelas-national-assembly-declares-petro-unconstitutional/>.

<sup>67</sup> *Blockchain is a distributed ledger technology(DLT), originally devised to underpin cryptocurrencies such as Bitcoin. Heralded as revolutionary, blockchain radically increases trust among participants in an accounting system by adopting an inherently democratic and transparent verification process without compromising privacy.*



but the technology would allow them to purchase shares at a lower cost and trade in the market with greater liquidity. Together these have a profound impact that could rearrange the power dynamics of stakeholders in corporate governance such as managers, shareholders, lenders, regulators, and third-party experts.

Delaware, home of about two-thirds of Fortune 500 companies, has been at the forefront of experimentation and adoption of technology in corporate governance. In response to disputes in Delaware-based corporations such as inconsistent stock ledgers, stock ownership issues, delayed transfers and settlements, Delaware Blockchain Initiative (DBI) was launched in 2016.<sup>68</sup>

DBI aims to promote blockchain startups and encourage companies to use blockchain applications that make them future-ready. As a part of DBI, effective on the first of August 2017, amendments made to the Delaware General Corporation Law (“DGCL”) allow companies to use DLTs for the creation and maintenance of corporate records, including the corporation’s stock ledger.<sup>69</sup> This move is more significant than a mere record keeping upgrade as the shares are now in a blockchain which are authorized and filed by the Division of Corporations. Cryptographically signed, these shares have a perfect record and all actions on it are automated, accurate, and accountable, thereby eliminating the inconsistencies in records. Importantly, DLT shares aim to remove the discrepancies between corporate and securities laws that have a strong impact on the companies as seen in the case of Dole Food Inc.<sup>70</sup> Proxy voting in the companies is expected to be streamlined through blockchain voting to avoid errors such as in the case of T. Rowe.<sup>71</sup>

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<sup>68</sup> Delaware Office. “Governor Markell Launches Delaware Blockchain Initiative.” PR Newswire: News Distribution, Targeting and Monitoring. May 02, 2016. Accessed May 20, 2018. <https://www.prnewswire.com/news-releases/governor-markell-launches-delaware-blockchain-initiative-300260672.html>.

<sup>69</sup> Legislature, Delaware. “Delaware General Assembly.” Legislator Detail - Delaware General Assembly. Accessed May 20, 2018. <https://legis.delaware.gov/BillDetail/25730>.

<sup>70</sup> Say, My. “Why the Delaware Blockchain Initiative Matters To All Dealmakers.” Forbes. September 20, 2017. Accessed May 20, 2018. <https://www.forbes.com/sites/grouphink/2017/09/20/why-the-delaware-blockchain-initiative-matters-to-all-dealmakers/#42cc099e7550>.

<sup>71</sup> “Bullish on Blockchain: Examining Delaware’s Approach to Distributed Ledger Technology in Corporate Governance Law and Beyond.” Harvard Business Law Review (HBLR). January 04, 2018. Accessed May 20, 2018. [http://www.hblr.org/2018/01/bullish-on-blockchain-examining-delawares-approach-to-distributed-ledger-technology-in-corporate-governance-law-and-beyond/#\\_edn26](http://www.hblr.org/2018/01/bullish-on-blockchain-examining-delawares-approach-to-distributed-ledger-technology-in-corporate-governance-law-and-beyond/#_edn26).

Smart contracts are self-executing contracts automated through software programs with conditions that are determined by all parties involved. The combination of smart contracts placed on top of distributed ledgers is powerful enough to automate a range of corporate services including automation of compliance with laws among various agencies and regulators.

DBI is mulling introduction of “smart UCC” filings, to replace the current UCC (Uniform Commercial Code) filing process, which is paper-based, error-prone and sluggish.<sup>72</sup> UCC filings on a distributed ledger will automate UCC filings and related collateral, expedite review of UCC records, and reduce errors and costs. It will allow UCC filings to be an important tool to manage risk and compliance. However, the actual rewards of this digitization through DLT can only be seen when layers of processes are hammered down to a simple process where securities issuers and investors can interact directly. Delaware took the initiative to begin the revolution in corporate governance within companies but the potential of DLT goes further.<sup>73</sup> The principal of digital identity can be extended from shares and shareholders to the identity of companies on a blockchain. Assigning digital identity does not just eliminate duplicates but also provides a transparent monitoring mechanism that benefits both regulators and investors in terms of conducting hassle-free business. In addition, a digital identity is easily verifiable across borders to prove compliance to various regulations, thus increasing ease of movement for business across various regulation regimes. Although there are companies already venturing into digital identity and identity management for people,<sup>74</sup> corporate digital identity is yet to be seen.

This vision enables companies that are incorporated globally and given digital identities to reap increased transparency among the host of benefits

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<sup>72</sup> Tinianow, Andrea, Caitlin Long, and Delaware Blockchain Initiative. “Delaware Blockchain Initiative: Transforming the Foundational Infrastructure of Corporate Finance.” *The Harvard Law School Forum on Corporate Governance and Financial Regulation Firm Age Corporate Governance and Capital Structure Comments*. Accessed May 20, 2018. <https://corpgov.law.harvard.edu/2017/03/16/delaware-blockchain-initiative-transforming-the-foundational-infrastructure-of-corporate-finance/>.

<sup>73</sup> The 2017 Amendments to Delaware’s Business Entity Laws.” S Corp (S Corporation) Advantages & Disadvantages | CT Corporation. Accessed May 27, 2018. <https://ct.wolterskluwer.com/resource-center/articles/2017-delaware-business-entity-law-amendments>.

<sup>74</sup> Goel, Amit. “12 Companies Leveraging Blockchain for Identification and Authentication.” *MEDICI*. March 28, 2016. Accessed May 20, 2018. <https://gomedici.com/12-companies-leveraging-blockchain-for-identification-and-authentication/>.

as detailed, albeit at a global scale. Having all companies and their shares incorporated in a blockchain that is embedded with stipulated regulations according to the law of land would result in a seamless integration of regulations, such as is being implemented in Delaware.

In the current legal and political environment in which jurisdictions are working on taking advantage of persistent lack of coordination among them, there are some like South Dakota or Wyoming that are promoting themselves aggressively as the corporate and trust-friendliest jurisdictions. Yet, for those who put a premium on certainty, Delaware offers a proven, reliable track-record of dealing on corporate matters. The overall Delaware legal and tax environment is, of course, designed to make it always an attractive alternative. The Delaware Blockchain Initiative (DBI) continues to place Delaware at the corporate governance forefront leveraging both experience and innovation. In fact, it is no coincidence that the back cover of the classical Foreign Affairs magazine for November/December 2017 displays an advertisement of Wilmington Trust emphasizing that “Delaware is a trust-friendly state, with more than 100 years of favorable tax laws.”

If Panama’s Law 32 of 1927 was inspired by the corporation law of Delaware, then perhaps it is time that yet again Panama follows through Delaware’s benchmark. Correcting failures of governance via institutional, legal, societal, and technological means, private actors could still offer financial and corporate services that ensure both privacy, and timely accountability. There should be a way for individuals to create all the corporations they want using blockchain technology disclosing the minimal information. If and when an authority wants to inspect the data of a particular citizen then there are the records of his or her transactions, including in which and how many corporations he or she is a shareholder. Every individual is the owner of his/her data and controls who has access to it. Transactions are confidential and traceable, if and when necessary. This would give the individual some degree of protection from both government surveillance and surveillance capitalism. Neither the IRS nor Facebook nor AT&T should have access to the data of individuals without a good reason. As Attossa Araxia Abrahamian points out, one of the General Data Protection Regulation “more touching lines [is]: The processing of personal data should be designed to serve mankind”, (Data Subjects of the World, United! NYT, 5.28/18, <https://goo.gl/yTdLaH>).

As it is unquestionable that death and taxes are certain, we need to recall that part of being a free human being is constantly trying to escape these certainties. Perhaps it’s no coincidence that in Freeport, Bahamas, in Beachway Dr., an office of Deloitte sits cater-cornered to the St. Paul’s Methodist Church.