LEGAL COMMITTEE

Topic: Actions designed to create a global legal framework in order to tackle corporate tax fraud

Research report by Daniela Sannino and Valeria Pasquarelli

INDEX

1. Definition of key terms

Framework: a system of rules, ideas, or beliefs used both to plan or make decisions and in order to deal with problems;

Corporate fraud: it refers to activities undertaken by an individual or a company that are done in an illegal or dishonest manner. They are designed to increase the profits of the perpetrating individual or company and to mislead the public;

Tax fraud: it refers to the intentional forgery of information on a tax return by an individual or business entity in order to limit the amount of tax liability;

Tax evasion: it is the process whereby a person, through commission of Fraud, unlawfully pays less tax than the law mandates or avoids paying a true tax liability;

Trust: Coalition of enterprises or industrial unions by means of which enterprises, united by analogies of production or by an instrumental relationship, come to constitute an economic complex to unitary direction, in order to reduce production costs and limit domestic or foreign competition;

Informal economy: it is the diversified set of economic activities, enterprises, jobs and workers that are not regulated or protected by the state ;

Tax gap: it is the difference between total amounts of taxes owed to the government versus the amount they actually receive;

Tax avoidance: it is the arrangement of one's financial affairs to minimize tax liability within the law;

Tax burden: it refers to the total amount of tax paid by groups, industries, etc., especially as compared to what a particular group, company, etc., pays;

OECD: Organisation for Economic Co-operation and Development;

VAT fraud: Value Added Tax fraud.

2. Introduction

Taxes stand for the common involvement of the population given over to the administration costs. Taxation system is vitally important for a collectivity, consequently to a State, in order to work normally. On the contrary, tax treatment lies upon the concept of equality. Tax fraud, also called tax evasion, as it aspires to evade the payment of tax, is made up of benefitting from the State's advantages and frameworks without bearing this primary citizen's responsibility.

Tax fraud often entails taxpayers purposely misrepresenting their real state of affairs to the tax authorities in order to decrease their tax liability by including dishonest tax reporting, such as declaring less income, profits or gains than the amount effectively earned.

Moreover, this activity is commonly linked to the informal economy. Furthermore, tax fraud is known to be one of the most powerful implement for supporting financially crime syndicate or terrorism. As a matter of fact, the resources implicated are concealed from the management, which makes them terribly useful to finance illegal activities without being spotted by governments authorities. The amount of unreported income , that is to say the difference between the amount of earnings that should be referred to the tax authorities and the actual one, is considered as a measure of the extent of tax evasion. On the other hand, tax avoidance is the legal use of tax laws to reduce one's burden of taxation. The first case as well as the second one can be viewed as forms of tax noncompliance, as they identify a range of acts that intent to sabotage a state's tax system.

3. Major countries involved

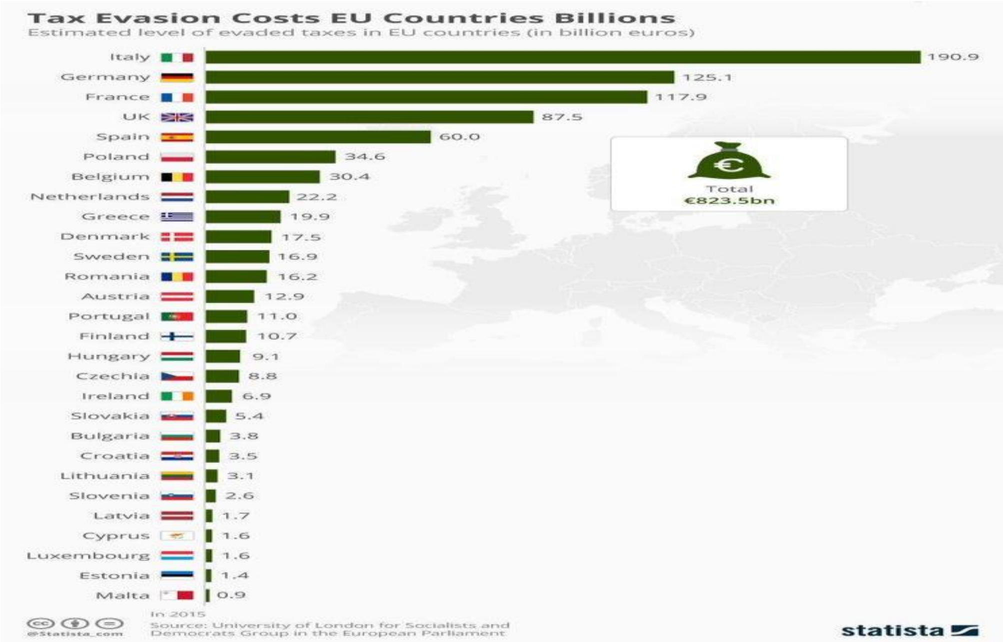
Nowadays in many countries there is the lack of an institutionalized and systematized estimation of the evasion, with adequate periodicity. As regards the causes of this phenomenon it is important to underline that they vary from one country to another and at the same time, within the same state throughout its history and time. Some of the reasons of tax evasion, among others are:

- The structure of the country's tax system;
- Anarchic distribution of powers among the different government levels, in particular in federal countries;
- Population's lack of education;
- Tax pressure (high rates);
- Digital economy, with the significant technological development.

As a symbol of national supremacy, tax rules is submitted to an undivided vote when it comes to European rulings. Every member state has it own delineation of the concept of tax fraud, which turns it into an even more complicated things to address for the authorities. Two cases in point of these differences are France and Luxembourg.

- **France**
  Tax evasion is outlawed by the article number 1741 in the French General Tax Code. The counterfeit behavior can take various forms such as a misrepresentation of a person's affairs or a willful action of hiding income or profits, all aiming to reduce or suppress their tax liability. The text prohibiting tax fraud is not in the Criminal Code and the procedure that has to be tracked during the inquiries cannot be found in the Code of Penal Procedure.

- **Luxembourg**
  As a country with an exceptional tax scheme, it is prohibited by paragraph 396 in the General Tax Law, from May 21st, 1931. In order to give a demonstration of fraud, Luxembourg authorities demand a noteworthy amount of unpaid taxes, and the methodical use of fraudulent operations in order to hide facts or profits to the administration. Each year, calculated €1 trillion in public funds is lost in European Union, due to tax evasion:



The graphic shows the level of evaded taxes in EU countries.

4. UN involvement

The 2017 revision of the United Nations Model Double Taxation Convention between Developed and Developing countries was expected to bring a version which should have been revised especially for what concerns exchanging information, making sure that the new United Nations Code of Conduct is respected. In 2016 a proposal aimed at creating a United Nations Code of Conduct dealing with the fight against International Tax Evasion was approved. The Code mentioned above sustains information automatically exchanged for tax purposes as the way forward for countries generally, yet, simultaneously, fully realizes that exchange of information is vital for developing countries. In 2016 thanks to the approved Code of Conduct, automatic exchange of information was set as the new universal standard. This happened after ECOSOC had relied on such a Code including it in a Resolution in 2017, during an ECOSOC Special Meeting about International Cooperation regarding Tax Matters.

Moreover, the OECD (Organization for Economic Cooperation and Development) model convention and commentaries is supposed to broaden the spread of information to allow triangular, or multi-party exchange of information requests.

The UN has continuously been dealing with this issue throughout the years, above all focusing on transparency and on the development of multi-stakeholder reporting standards. This topic was widely discussed in the Multilateral Convention, which was developed by the OECD and the Council of Europe in 1988 in order to tackle tax evasion and avoidance. The amendment of 2010 gave particularly to the developing countries the possibility to benefit for the new, more transparent environment.

The CBCR (Country by Country Reports) Agreement, which is multilateral, was implemented to entertain automatic exchange of country-by-country reports. It should start work in most of the 57 jurisdictions that have agreed to it in 2017. The Committee has approved, and in 2017 has been issuing, the following innovative products: a new revised United Nations Model Convention and Commentaries, with a new provision on fees for technical services; a version of the Transfer Pricing Manual, which has been modified and then officially launched, which gives guidelines on transfer pricing operations of countries that are currently emerging; finally a new handbook on selected issues in the taxation of extractive industries by developing countries.

No Member States has donated to The Trust Fund in Tax Matters, in spite of the fact that ECOSOC encouraged them. Nevertheless, some donor agencies have voluntarily sponsored some of the Committee's actions.

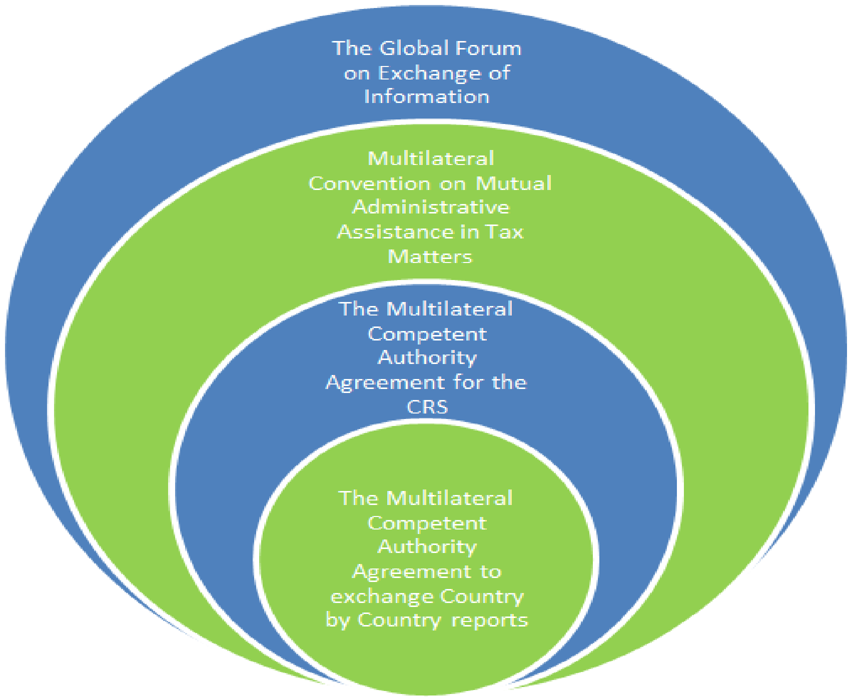
Before starting by naming the various treaties that had been signed on the considered topic, it should be remarked that in many cases, treaties do not provide an adequate basis for a decent tax information exchange among developing and developed countries, and in particular with secrecy jurisdictions. Some, such as Switzerland, have forced developing countries into making large tax concessions in their treaties, in exchange for information exchange that is, too often, minimal. Double Tax Treaties or Double Tax Agreements (DTAs). These treaties aim at eliminating double taxation where the same income is taxable in two States.

Report with recommendations on anti-abuse measures: BEPS (Base Erosion and Profit Shifting). Its action plan includes: establishing international coherence of corporate income taxation, ensuring transparency while promoting certainty and predictability and, more in general, underlines the need for a swift implementation of the measures. St. Petersburg Tax Declaration: it was signed on 20 September 2013 at the occasion of the General Assembly of the CFE in Saint Petersburg, Russia, with the purpose of further enhancing better structuring and operation of the tax systems worldwide, making sure that tax advisers continue playing a role throughout the world. The OECD also launched in 2011 The Oslo Dialogue, which aims at promoting a whole-of-government approach in order to tackle financial crimes by stimulating inter-agency and cooperation on an international scale.

The UN has proven remarkable dedication to reinforce the effectiveness and operational faculty of the United Nations Committee of Experts on International Cooperation regarding Tax Matters, that plays a key role in guiding by and for developing countries. In 2016 the Committee held two meetings and, both in 2016 and 2017, ECOSOC held a special meeting on tax refund, which consists in the difference between the taxes paid and taxes owed. The Committee approved, and in 2017 has been issuing, the following innovative products: a new revised United Nations Model Convention and Commentaries, with a new provision on fees for technical services; a version, which has been revised, of the Transfer Pricing Manual, launched both in a digital format and then officially, giving guidance on transfer pricing systems of developing countries and a recently-released handbook on selected issues in the taxation of extractive industries by developing countries.

Being this issue extremely spread worldwide, involving all aspects of daily life, solutions have to be found as soon as possible, since the implementation of new legal frameworks and systems to tackle corporate tax fraud would prove crucial in the abolition of criminality in this field and consequently would benefit each individual. Measures have already been identified and, among them, there are very appealing ones. For instance, partnerships should be chosen carefully, awareness should be spread regarding irregular practices and the use of social security numbers belonging to the deceased, monitoring any communication is received from the IRS or Tax Agencies, making sure tax records are secure; if they are electronic, they should be encrypted with strong passwords.

Four main initiatives are now being adopted and implemented and can be seen in the picture below:



The United Nations Secretary-General in 2017 appointed as members of the Committee a new group of experts, after having consulted with the Member States. Such States, in particular developing countries, should consider nominating qualified tax experts. It is crucial to provide further guidance to developing countries when it comes to draft their domestic tax policies and while dealing with complex transactions, such as those that involve the search of natural resources and the implementation of an arm's length price to a cross border transaction between related parties. Member States should as well support the Committee and its subsidiary bodies using the voluntary trust fund, so that the Committee could fulfill its mandate, which includes supporting larger participation of developing country experts and an increase in the participation of Least Developed Countries for what concerns the Committee's actions.

Despite the fact that the Committee meets now rarely, there has been no additional funding to support the secretariat which assists the Committee yet.

No Member State has donated to The Trust Fund regarding Tax Matters, even if ECOSOC strongly encouraged to do so. Nevertheless, a few donor agencies have spontaneously sponsored some of the Committee's actions.

Furthermore, technological innovations offer a clear path through which tax evasion and tax fraud could be efficiently reduced, prevented the Government from spending billions due to the issue. In the document "Technology Tools to Tackle Tax Evasion and Tax Fraud" are illustrated the current uses of technology by tax administrations in countries all around the world in order to avoid, recognize and fight tax evasion and tax fraud. Basing on the experience of 21 countries, the report gives examples which are real and already ready to be applied to achieve effective use of technology in the fight against tax crimes:

- In Rwanda, points of sale technology have been introduced to address electronic sales suppression, which resulted in a 20% increase in VAT (Value-Added Tax) collected on sales.
- In Quebec, Canada, similar technology was introduced in the restaurant sector and has led to the restoration of approximately EUR 822 million in taxes.
- In Hungary, electronic cash registers increased VAT revenue by 15% in the sectors that are concerned.

5. Useful links

http://taxadviserseurope.org

www.oecd.org

https://tax.findlaw.com

https://developmentfinance.un.org

https://www.jstor.org/stable/40972114?seq=1

https://www.ciat.org/which-are-the-causes-of-tax-evasion/?lang=en

https://www.weforum.org/agenda/2017/04/which-countries-are-worst-affected-by-tax-avoidance/

http://www.ejtn.eu/Documents/THEMIS%202016/Semi%20A/France2_TH_2016_01.pdf