

FEATURES AND ADVANTAGES OF USING TAX HAVENS

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Abstract: *The appearance of tax havens is tied to illicit money laundering process, evolving later under various illegal forms and currently they operate under the protective umbrella of beneficial jurisdictions belonging to some political protected States worldwide. For them to be capable of functioning, special conditions to attract investors have been created. The purpose of this study is to highlight the main features of the tax havens, their operating mechanism and peculiarities of their tax laws, offshore entities regime. The article concludes on the reason of the occurrence, the existence and proliferation of tax havens, as well as legislative efforts that are submitted worldwide to eradicate them in the perspective of future global economic and financial developments.*

Key words: *tax haven, tax system, taxation, offshore companies.*

1. Introduction

In the general context of globalization of the economy, a significant obstacle to Governments concerned with the increase in tax revenues, is the tendency of the transferability of the results arising from the productive activity by the contributors, in areas with low taxation, known as tax havens, the phrase that tends to be replaced by the name of international financial center or a financial haven.

Although associated with terms such as “immoral” and “illegal”, the existence of international tax havens, had in recent decades, the effect of a progressive growth of the economic activity, more than two-thirds of the international broad money being performed in their shadow.

There are many definitions for the tax haven term: according to the report to the International Service for Gordon Revenue

of the United States of America (IRSI in the 1981, by the Gordon Committee which investigated the use of tax havens by the U.S. taxpayers, a tax haven is any country which is regarded as such and which wants this”. [5]

Roger Brunet defines tax havens as follows: “It is called tax haven a territory where individuals and companies have the sensation that are less taxed than somewhere else”. [2]

Tax havens are those States that offer a variety of tax privileges to offshore companies registered in their territory. Any offshore company can operate in favourable tax conditions, provided registration in a tax haven, the company must conduct business outside of the record.

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tax conditions, provided registration in a tax haven and the company must conduct business outside of the registration territory.

The operation of these companies in the traditional tax havens, is aided by the legislative mechanism, which means in that States the law provides tax advantageous conditions for offshore companies. You have highlighted the fact that, through the non-payment of tax, the company does not violate the law, but under the legislation is partially or fully exempted from payment of taxes.

The lightness of the legislation of those States or territories, encouraged foreign investors to set up companies in their territories. In these areas, operation of companies, the security of foreign investment and of information are guaranteed by the law.

The first law relating to the international companies, was adopted in 1982 by the Legislative Assembly of the British Virgin Islands, to make a competitive legislation relating to offshore companies registered in this area.[6] The law was implemented in 1984 and allowed the establishment of offshore companies exempt from taxes, demanding minimal requirements for conformity, providing full confidentiality of the details.[1] The British Virgin Islands have the most successful legislative system that supports the offshore companies. Also here, in 2005, came into force the New Act concerning the establishment of offshore companies, representing a continuing development of the existing legislation concerning the operation of these companies. This Act removes any distinction between a local company and an offshore entity, thus promoting a single type of company, the international business company from the British Virgin Island being exempted from the taxes payment and still enjoying the benefits of previous legislation.

Worldwide there are currently about 68 financial havens. Some have disappeared, such as Lebanon, but some of them have subsequently reborn, others like Switzerland, are disappearing or even failed as it happened to Cyprus. At the same time, in certain areas there may appear new havens. These tax havens are some excellent hot topics, because they are known and used by tourists and some businessmen. For example, famous for banking secrecy are Austria, Andorra, Monaco, Gibraltar. They also are havens vacation: for example the Caribbean area holds a multitude of Islands with independent status, which have a taxation system more permissive than allowed elsewhere.

According to statistics of the Organization of Economic Cooperation and Development (OECD), through financial havens were conducted the businesses of huge size. Approximately 65% of the total international monetary expansion was run under the umbrella of such unimaginable havens. Thus, the large corporations in the U.S. have moved in the 1980s to tax havens, under various forms of major foreign investment, about 22 billion U.S. dollars, while other Western European corporations held financial resources of about 160 billion U.S. dollars.

All banking transactions conducted through tax havens have been evaluated at the beginning of the 21st century at about 1,600 billion U.S. dollars. According to studies conducted by economists in the U.S., 25 years ago it ran through tax havens 5% of the world economy, compared to 50% today.[4]

Thus, tax havens represent a highly used way to making international tax evasion, tax avoidance schemes with privileged tax regime offered by the developed countries. At the origin of privileged tax regimes are contradictory economic interests. Those countries that encourage them, obtain

collateral economic benefits, even though tax revenues are reduced, and those who reject and limit them, are trying in fact, to protect their tax revenues.

2. Characteristics and classification of tax havens

Starting from Roger Brunet definition of tax havens, there can be highlighted a number of features, such as:

- reduced taxation
- protection of information
- encouraging the development of banking sector
- modern media holding
- the absence of currency control
- the promotional advertising
- favorable tax treaties

Some of the countries considered tax havens, have charges only for certain on income or only specific taxes, much reduced compared to those applied in the countries of origin of those companies that use financial havens. Thus, they make available to customers all the tax benefits which they cannot obtain in their residence countries. By acquiring the country's residence considered as a tax haven, or by installing the registered office of the company or other legal entity, they enjoy that country's own taxation, such revenues and profits will be taxed far less than in their countries of origin. In conclusion, the tax haven countries, through this reduced taxation, ensure their capital resources used in economic expansion.

For example, the Government of the Cayman Islands, Bermuda, Bahamas and other not tax income or personal wealth- in these cases, the absence of the income taxes, is part of the nearby policy of the banks and the economic-financial corporation from abroad, and there are cases in which that country has considered that there is no need to apply a revenue tax. The majority of financial havens in the

Caribbean are small, economically weak countries, with generally poor inhabitants. That country, can get a considerable income, with a lower cost, through the collection of customs duties, taxes for permits and fees.

All tax haven countries provide some protection to bank or commercial information. In the case of a legal inquiry from a foreign Government, most countries will not protect this information when the investigation is made under treaties. Otherwise, tax havens refuse to disclose the offered banking secrecy, although, it is a violation of the laws of another country.

The distinction is made by exaggerated restriction rules on classified bank information, that may encourage tax offences have been carried out, as well as legislation that pertains to the protections of personal privacy, but that in some cases allow legitimate research.

The security level and the size of the measures that limit access, varies from one country to another. Thus, some countries make a distinction between tax evasion and other criminal activities, cooperating when criminal cases are being investigated, other than fees, but instead they not cooperate when there is question of tax evasion.

So, the fact of having a secret safe, protected by law, with regard to financial and commercial operations in these countries by persons or corporations participating in economic operations, also contributes to ensuring sources of capital.

The banking business has tended to play a more important role in the economy of fiscal paradise, compared with the economy of country which is not a financial haven.

Most countries financial havens are pursuing policies to support the Bank's activities outside the State's borders. This achieved through the implementation of a distinction between the banking business of the inhabitants of the country and that of foreigners.

In general, the activity of foreign companies is not subject to reserve funds requirements, it is taxed differently (if will be taxable) and will not be exposed to scrutiny regarding currency conversions or other economic activities. In addition, this activity enjoys the guarantees relative to the maintenance of banking secrecy.

Tax havens, are thriving largely thanks to the presence of foreign banks. One of the important requirements of an effective banking activity is an optimal relationship between the volume of foreign goods, in the form of bank deposits and the total foreign trade volume of the country in question.

Capital deposits in foreign banks in financial havens are much higher compared to foreign bank accounts located in the countries that are not financial havens.

Ensuring the necessary capital resources for economic growth and maintaining the social local balance is achieved by the existence of a developed banking system that allows quick and easy operations outside the borders without restrictions.

As a general rule, the citizens are not subject to the controls on the currency, but this rule is not available for the inhabitants of that country. A company established in a tax haven and whose owner is a foreigner

who carries out the majority of activities beyond paradise, is generally regarded as a person with a foreign regime in terms of exchange controls. Thus, in the tax haven, a foreign can register a company in order to carry out activities in other jurisdictions. As long as a company's activity is carried out in the currency of other countries and do not execute financial transactions in financial paradise, the company is not controlled about the exchange transactions made in the tax haven.

One of the advantages of tax havens is the absence of the trade verification for both nonresidents and transactions in foreign currencies as well.

These countries see in financial activity a relatively stable source of income and seek to promote it. A promotional campaign for the paradise country is achieved through the linear aggression which means the adaptation of the legal framework in order to attract financial resources.

Financial havens are classified according to their importance, in main financial havens and secondary financial havens.[1]

As we can see in Table 1, the main seven financial havens and their characteristics are:

The countries considered main tax havens and their characteristics Table 1

Crt. nr.	Features	State
1.	The income and capital gains are not taxed. They are known as "zero havens" or "pure havens".	The islands of Bermude, Bahamas, Bahrain, Nauru, Cayman, Turks, Caicos, Saint-Vincent, The Republic of Vanuatu and Monaco;
2.	The tax rates have a low value as they are approved by the state or as a result of the application of the quota reductions, due to the implementation of tax agreements between different states concerning double taxation;	The British Virgin Islands, Liechtenstein, Switzerland, Neterlands Antilles, Man Islands, Guernesey and Jersey Islands, The Republic of Ireland;

Crt. nr.	Features	State
3.	The taxation of income or benefits is determined locally base. The taxpayers from these states are exempt from taxation of profits made by trading across borders;	Liberia, Costa Rica, The Philippines, Venezuela, Malaysia, Panama;
4.	Countries with preferential treatment for offshore and holding companies;	Hungary, Austria, Netherlands, Luxemburg, Thailand, Singapore;
5.	Offers tax exemptions for industries that have been made for the development of exports;	Ireland for the companies created before 1 January 1981, Madeira;
6.	Provides financial benefits for international business companies, that are focused on investment or not, but instead are classified as offshore finance companies with certain privileges;	The Islands of Bahamas, Antigua, Bermude, The British Virgin Islands, Montserrat and Nevis Islands in the Caribbean;
7.	Provides specific tax advantages to other banking companies or other financial institutions with offshore activities;	Antigua, Island-British territory in the Caribbean, Anguilla, Grenada, Barbados Islands and Jamaica;

Source: the table is created by the author using dates from Finante.ideaplussolutions.net/.../51725386828_BUZINESCU_RO... [accessed September 12, 2014]

Secondary financial havens include the small countries and the industrialized countries, where certain income tax is high, but where at the same time there are legislative provisions which have particular character, being used by investors in certain tax planning operations.

From the small territorial class, as well as tax havens, the following are relevant examples:

- small states such as the Vatican, French Polynesia, the Republic of Malta, Maurice Islands, Tonga Inlands, Haiti, Taiwan, Jamaica, the British Virgin Islands. They have a reduced area and have a numerically small population, without having to carry out all the features of the main tax havens. Therefore, they often do not practice any taxation or not tax all income obtained by individuals or companies,

- or providing exemptions from taxes for the activities carried out by certain companies or set very low odds;

- powerful industrialized states which have the possibility of becoming attraction for certain economic sectors. These are: Italy, Austria, Belgium, France. These powerful industrialised countries tend to grant reliefs appealing, offering tax exemptions or tax reductions, in order to expand exports and attract foreign capital.

3. Elements of taxation in Cyprus

Cyprus became a tax haven in 1975 by Act No.37 that regulated the offshore entities regime, allowing the country to become an attractive tax haven. According to its, offshore entities are joint stock companies or individuals, belonging entirely to foreigners holding Cypriot resource revenue. In relation to this

definition, it differentiates the following circumstances:[3]

- If the unit is directed and controlled from outside Cyprus, it is not subject to income taxation in Cyprus;
- If the entity is ruled and controlled in Cyprus, it is subject to a tax with a lower fee of 10% of the common law duty that is in most cases a fee of 4.25%;

The same law regulates the status of the offshore companies and foreign branches. According to it, a branch is considered an offshore company if it belongs entirely to foreigners and in terms of fiscal if the company that made the branch registration is controlled from abroad it is not subject to taxation and if the company is managed and controlled in Cyprus, it is subject to the tax on benefits with a rate of 4.25%;

Societies people offshore(offshore partnership) are not taxed either on behalf or in the name of members of society. The conditions to benefit from this exemption are as follows: all associates must be foreigners and whether they are offshore partnerships, business object must be exercised outside of Cyprus.

In terms of the tax regime of offshore banking units(OBU), they are exempt from all taxes in Cyprus, if they are not controlled from Cyprus, as well as all offshore branches of foreign companies. If they are headed and controlled from Cyprus, are subject to an income tax benefit of 4.25 percent in the country and must pay an annual fee of \$15,000.

Foreign employees of an offshore company have discounts or tax exemptions even the companies operating in the free zone of Larnaca, they are subject to personal income tax at the rate of 50% of the resulting from the common law.

Foreign employees who work outside of Cyprus and receive wages in Cyprus, are taxed at a rate equal to one tenth of the common tax.

Concerning the tax facilities of the

foreign trade companies (Foreign Sales Corporation), Cyprus was on the list of countries where F.S.C. can be created through application of the US laws in force since 1985. Cyprus offered to FSC a reduction of 90% of the tax rate, an exemption from 90% on the income foreigners from these companies.

Stimulating investment in Cyprus is made by into force of various decisions, whose objective is to stimulate the growth and expansion of its economy, to facilitate the exports. For example, a temporary tax exemption for 10 years is granted to foreign investors in the free zone.

The fall of the Cypriot banking system is due to the wrong election of Laiki Bank and Bank of Cyprus made by the managers and by the European System of Supervision and Regulation. According to official documents, have the following result:[6]

- In July 2010, Laiki Bank and Bank of Cyprus pass the stress test carried out by the EU, with 582 million euros capital surplus, to the satisfaction of the Cyprus Central Bank;

- At the end of 2010, they were about 6 billion euros invested in bonds issued by Greek banks, accounting for one third of GDP achieved;

- Also at the end of 2010, Laiki Bank pays dividends for 67 million euros and the Bank of Cyprus pays dividends for 27 million euros plus another 47 million in 2011. Through these payments has been transferred an important part of the capital;

- In 2011 were made other stress tests to those banks which have been passed , and a week after that, European leaders have agreed a new deal to rescue Greece, which consisted in debts restructuring;

- In August 2011 Laiki Bank expands its business in Greece with mortgages, hoping to achieve a positive asset portofolio, but after three month, the Bank's management begin to reduce the Greek sovereign bonds;

- In November 2011, some Bank Laiki customers begin to withdraw their deposits due to the Greek crisis;

- In 2011 the banks experienced a loss because of Greek debts. Bank of Cyprus has reduced the lending portfolio for Greece. As a result of economic analyses have been classified as non-performing 10% of total loans;

- The stress tests carried out in December 2011, revealed a capital deficit of 2 billion euros for the Laiki Bank and 1.6 billion euros for the Bank of Cyprus;

- The Cypriot Government has called for international aid because it cannot cover such losses;

In conclusion, because of Greece's debt rescheduling, the Cyprus banks have realized the historical loss of 4.3 billion euros.

The European Union and the International Monetary Fund pledged an aid of 10 billion euro capital infusion for the strengthening and restructuring of the banking system, highlighting that the Cyprus problem solving will be achieved through long-term banking reforms. Thus, Cyprus requires the acceptance of the loss of 80% for deposits holders of over 100,000 euros at Laiki Bank and approximately 60% for Bank of Cyprus. At the same time, the Cypriot State had accepted the liquidation of Laiki Bank, which in Romania was represented by Marfin Bank.

The European Commission has proposed that the depositors of the bankrupt banks which are not insured, be obliged to bearing the losses, but just after 2018. For this proposal to be applied, must be obtain the approval from the European Parliament.

According to the assessments made by the Moody's rating agency, whether Cyprus would no longer be able to pay its debts, this cause losses to Russian banks and companies of over \$50 billion.

In March 2013, Cyprus received a \$13 billion financial rescue, from the UE, as a support for its banking sector's massive restructuring. In this way, its role as an international tax shelter is ending.

4. Conclusions

The appearance of tax havens is tied to illicit money laundering process, evolving later under various illegal forms, and currently, they operate under the protective umbrella of beneficial jurisdictions belonging to some political protected States worldwide. For them to be capable of functioning have been created special conditions to attract investors.

Due to the large number of tax obligations imposed on taxpayers, they're trying to find ways to avoid or reduce tax liabilities. The main concern of businesses is to mitigate the impact of high taxes and controls, and this justifies the use of tax havens as a refuge from the increasingly high taxes. The objective of use of tax havens is obvious, the maximum gain with the minimum state payments. Any individual will seek countries, where the tax is minimal.

The development of offshore companies is growing ever larger and this is due to the development of tax havens. The offshore phenomenon gets widespread at the international level, and the access to them is more easily achieved. The establishment of offshore companies is in a continuous development. The significant of the offshore world is highlighted by the fact that most major international banks and bank branches were created and are present in offshore financial centers, the largest investment foundations in the world and trust companies also operate through the offshore subsidiaries. At the international level there is a struggle against tax havens development, promoted in particular by the developed countries. Tax evasion was, is and will be a phenomenon present everywhere in social

and economic area as well. Its development is alarming because of the absence of the control measures, that can affect the stability of the world economy, already globalized. The fight against evasion is especially necessary, firstly must be adopted an affective system and after that, a rigorous fiscal control and a tax education of the citizens in the same time.

Although official statement and positions taken by the political leaders, financial and tax havens continues to be the most hospitable territories for money laundering and practicing the most sophisticated combinations for hiding large scale fraud.

The credibility and strength of the attraction of these territories is given by the fact that in those areas there are branches of the great majority of major European and American banks, the biggest law firms are up to date with every dollar or euro going through their clients' accounts, and large companies and audit firms control the conduct of such operations, which they consider be perfectly legal but refuse to comment on the questionable business of the major global corporations.

Regarding the attitude of international organizations and the developed economies against the proposal recommended by the Transparency International Organization and approved by the Organization of Economic Cooperation and Development (O.C.D.E), to suspend all financial dealings with the uncooperative off-shore centres, both the European Union and the United States are

less willing to implement and enforce this recommendation.

In fact, the policy makers at European level and worldwide, "search" legal modalities for the abolition of tax havens and tax evasion while owners of big companies that benefit from the advantages of these havens are part of the same political class, who lived together during the years and have sought not to disturb each other.

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