Committee: Economic and Financial

Issue: Limiting money laundering and tax evasion through enhancing transparency in the Banking Sector

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INTRODUCTION

Our era will, as everything shows, remain in the history books characterized by one of the worst and most acute economic crisis that mankind has ever witnessed. The GDP[1] of almost every country is falling off cliffs and everyday life becomes more and more difficult for the majority of people not only in the Less Economically Developed Countries but in the European Union as well. While the number of people living in inhumane conditions rises every day, little seems to have changed ever since the economic crisis hit Europe back in 2008. Austerity measures and high taxation is the common practice followed by the vast majority of the most affected countries. The real problem though which needs to be combated is corruption. Money laundering and tax evasion are two of the most damaging practices for a given economy and cost billions of dollars every year.

A great step towards combating money laundering and tax evasion has been taken within the states of the European Union. The keystone of the European system remains the Third Anti-Money Laundering Directive, adopted in 2005, which requires financial operators to report any suspicious or unusual transactions or activities. The Directive incorporates into EU law the revised Forty Recommendations of the Financial Action Task Force (FATF), which is the international standard setter in the fight against money laundering and terrorist financing. Financial Intelligence Units (FIUs) play a key role in the fight against money laundering and terrorist financing. These units are responsible for receiving, requesting, analyzing and disseminating information to the competent authorities on potential money laundering or terrorist financing activities. They are usually placed within law enforcement agencies or administrative bodies reporting to Ministries of Finance in EU States.

The European Commission has made significant efforts to improve coordination and cooperation between FIUs and to harmonize criminal penalties for money laundering. The operational cooperation and exchange of information among EU FIUs has been reinforced

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[1] Gross domestic product (GDP) is a monetary measure of the market value of all final goods and services produced in a period

by the FIU-NET project. Funded by the Commission since its beginning, this project aims to establish a secure computer network for the exchange of financial intelligence.

That being said, it is now more imperative than ever that the biggest and most important Intergovernmental Organization, the United Nations step up following the path that the European Union has paved and solve the issue once for all. The lack of transparency in the trades in the banking sector especially in some countries makes it possible for people to hide their actual income or to hide their interest in offshore accounts thus avoiding paying the correct amount of taxes depending on their true income and obviously damaging the economy creating deficit. Our committee needs to find a way to combat the problem of tax havens, to establish a possible framework based on which countrys' banks should run, a framework that is clearly going to aim at l transparency during every legal activity.

DEFINITION OF KEY TERMS

Tax-Evasion

According to the OECD glossary tax-evasion is a term generally used when referring to illegal practices in order for liability to tax to be hidden.[2]

Money Laundering

According to the Article 1 of the 1990 European Communities Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime, money laundering is "*The conversion or transfer of property, knowing that such property is derived from serious crime, for the purpose of concealing or disguising the illicit origin of the property or of assisting any person who is involved in committing such an offence or offences to evade the legal consequences of his action, and the concealment or disguise of the true nature, source, location, disposition, movement, rights with respect to, or ownership of property, knowing that such property is derived from serious crime"*

On the other hand, the United Nations define it *as "a process which disguises illegal profits without compromising the criminals who wish to benefit from the proceeds. It is a dynamic three-stage process that requires: first, moving the funds from direct association with the crime; second, disguising the trail to foil pursuit; and third, making the money available to the criminal once again with the occupational and geographic origins hidden from view."*

[2] http://www.oecd.org/ctp/glossaryoftaxterms.htm

In simple words money laundering is a term used to describe the process by which the profits gained from corruption and illegal practices appear to have derived from a legitimate source.[3]

Transparency

Transparency[4] in economic terms is the extent to which investors have access to required financial information about a company, such as ,but not limited to, price levels and financial reports.

Offshore

The term offshore identifies any item that is located or based outside one's national boundaries. The term " " is used to describe foreign banks, corporations, investments and deposits. An offshore bank is a bank located outside the country of residence of its depositors and especially when the given bank is in a country which is considered a tax haven; its accounts are referred to as offshore accounts. A company may legitimately move offshore for the purpose of tax avoidance or to enjoy relaxed regulations. However offshore financial institutions can also be used for illicit purposes such as money laundering and tax evasion.

Tax havens[5]

A tax haven is a country that offers foreign individuals and businesses a minimal tax liability in a politically and economically stable environment, with little or no financial information shared with foreign tax authorities. Tax haven status benefits the host country as well as the companies and individuals maintaining accounts in them. Tax haven countries benefit by drawing capital to their banks and financial institutions, which can form the foundation of a thriving financial sector. Individuals and corporations benefit through tax savings resulting from tax rates ranging from zero to the low single digits versus relatively high taxes in their countries of citizenship or domicile. Some tax haven countries are Andorra, Panama, Hong Kong, Mauritius and Monaco.

[3] https://www.int-comp.org/careers/a-career-in-aml/what-is-money-laundering/
[4] http://www.investopedia.com/terms/t/transparency.asp
[5] Investopedia. "Tax Haven." *Investopedia*. N.p., 24 Nov. 2003. Web. 08 July 2017

BACKGROUND INFORMATION

Tax evasion a step further than tax avoidance

A common misconception that is often made even by media reporters is between the terms tax evasion and tax avoidance and whether each of these given practices are legal or not. Tax avoidance is the practice through which individuals or companies follow legitimate methods approved by the I.R.S[6] in order to minimize taxes. Some prime examples of tax avoidance would be moving once company to a country with lower tax rates such as Monaco. These are called offshore companies . Nevertheless, there are countries such as the United States that prevent such practices as they tax their citizens on their worldwide income regardless of their leaving in the States or abroad. Tax avoidance practices go back to the early 17th century where in England people used to have one or two windows per hundreds of square meters in order to avoid the so called "window tax" which as the name indicates, the more windows you had the higher the price. However impressive the fact that people use techniques to avoid taxes from the very first steps of the taxation system may sound , practices have been updated even further. Obviously, these ways of avoiding taxes will be beneficial for your company or enterprise but may be harmful for a given state thus it is a very controversial issue when it comes to the ethical aspect of using tax avoidance practices. Nevertheless, as our issue is not about money loss due to tax avoidance but rather due to tax evasion and money laundering I will not comment further on this issue but I believe that this distinction regarding these two terms should be made. On the other hand, tax evasion is an illegal practice which aims to hide the real income of a given employee or company from the state. Being an illegal practice as already mentioned, tax evasion is considered a very serious offense, thus some tax evasion cases are even turned over to the IRS criminal division for prosecution.

[6] The Internal Revenue Service (IRS) is the revenue service of the United States federal government

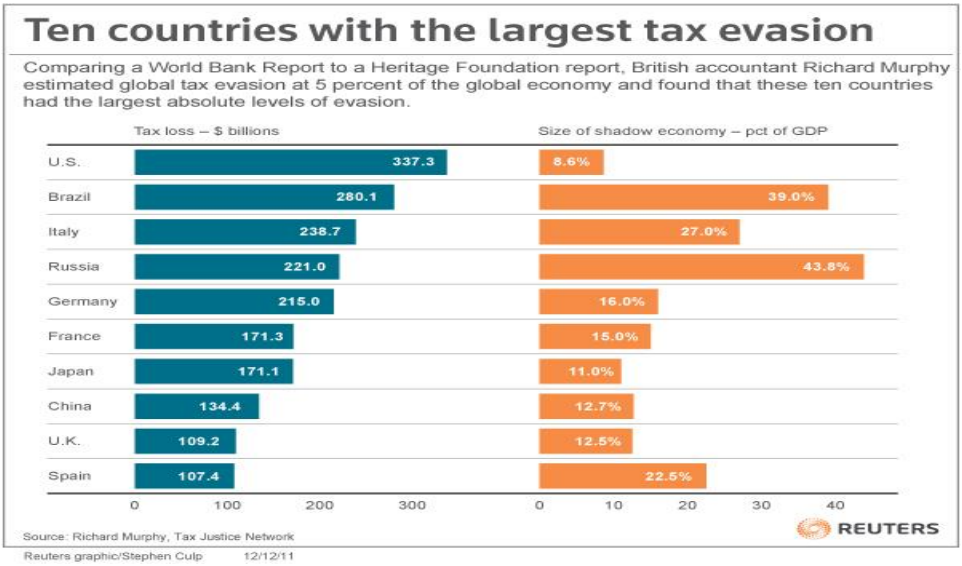


Figure 1: The ten countries with the largest tax evasion

How does tax evasion work?

Tax evasion has already been included as a term in this study guide several times, but it is not until now that the ways that this can be done will be discussed upon and as the text flows you will be able to learn the impact of tax evasion on global economy and thus why it worries the United Nations and all the states. The "underreport of income" and hiding money from your reports to the state is the most common and easier way that comes to mind when talking about tax evasion. Unfortunately, though the aforementioned are not the most harmful practices that one can use in order to get away with paying taxes. Practices that mostly are going to be discussed during our sessions and that concern the global economy the most are the following.

- Hiding interest in offshore accounts
- Tax Havens

Seizing the given opportunity I consider it mandatory to highlight the differences between these two practices and clarifying common misconceptions concerning both of them. In order to start with, offshore accounts although igniting great ethical debate and controversy are not illegal, however hiding once interest in these given accounts is highly illegal and is a tactic often used as it is difficult for a given state to examine offshore accounts due to problems that arise from bureaucracy, thus if an individual or corporation used an offshore bank to hide a certain type of income from the government, then it crosses the line of evasion. For example, possessing offshore accounts in Canada is not that suspicious for a given individual, but offshore accounts in Cayman Islands is a way different story. The difference in these two cases arises from the difference in laws of the aforementioned countries and their taxation systems. The latter is considered a tax haven, because according to OECD reports tax havens have characteristics as the following;

- Lack of effective exchange of information,
- Nor or only nominal taxes,
- Lack of transparency in the operation of the legislative or administrative provisions.

The impact of tax evasion on global economy

It easily goes without saying that tax evasion needs to be combated as it devastates the global economy. Tax havens, which is the most common strategy people employ when evading taxation is shifting income to a country whose tax policies provide for lower rates or even no income tax at all, is the one that has the most interest as more and more scientists get to concern themselves with it, thus ringing the alarm to the world that this problem is

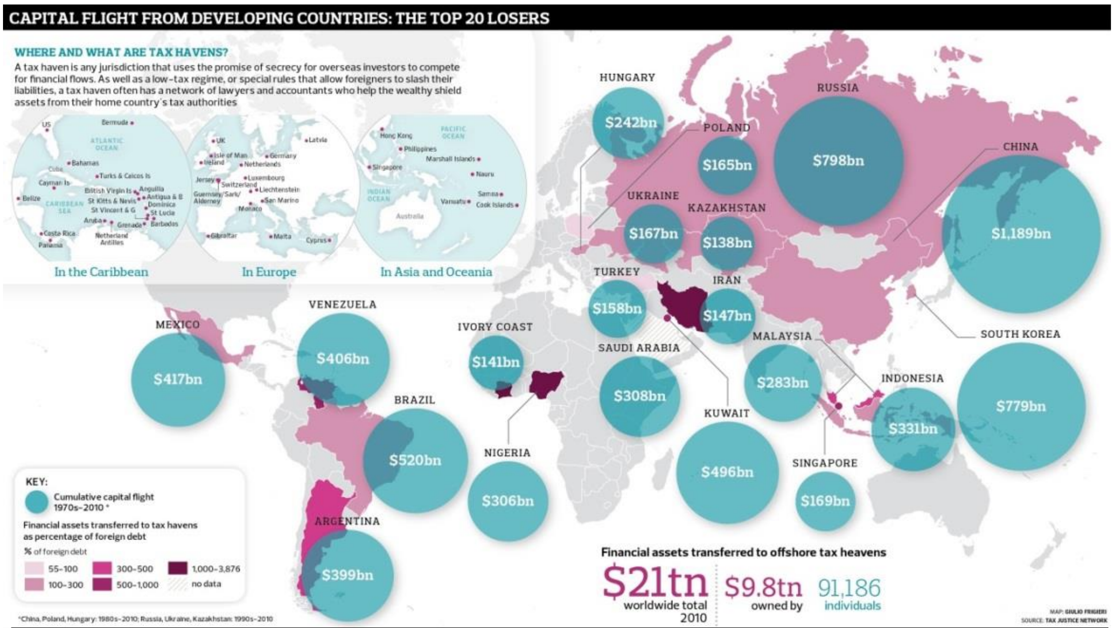
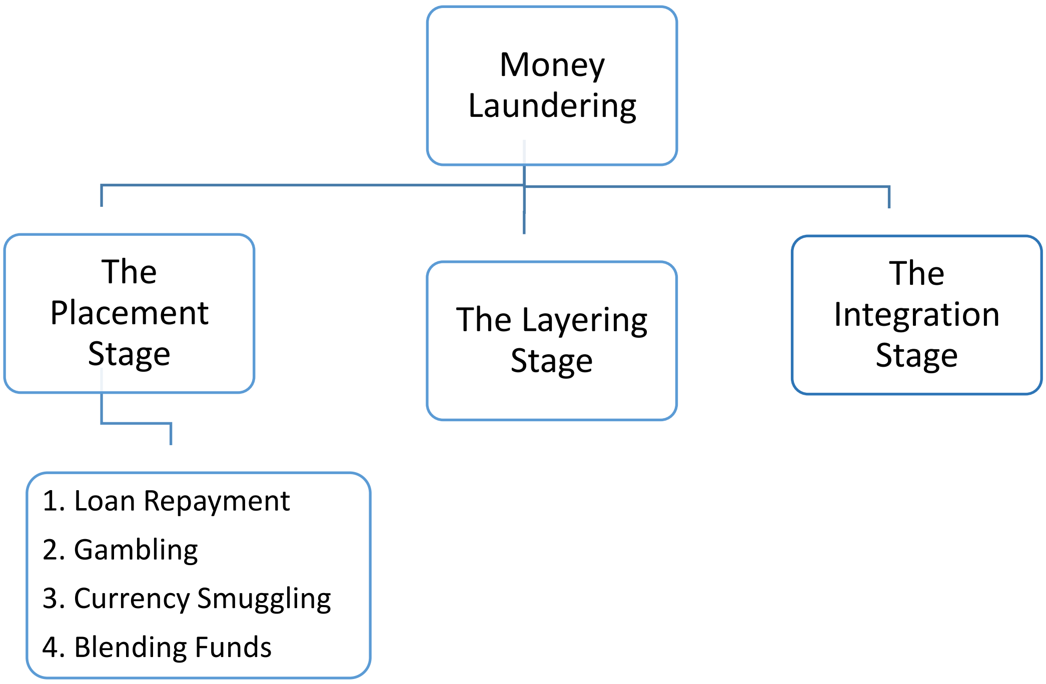


Figure 2: A map showing tax havens and their impact in global economy

not an insignificant one. A certain study by "Joseph Guttentag" and "Reuven Avi-Yonah" from the University of Michigan Law School, shows the effect of the given study. More specifically it is estimated that the use of tax havens by individuals has an economical reduction of $40 to $70 billion year which is about 5 to 6 times the Gross Domestic Product of the United States which ranks first among all countries including the European Union when it comes to their G.D.P. according to the International Monetary Fund for its study in 2016. Tax Havens allow individuals to escape income that would be taxed at regular rates by withholding the information from their returns filed for the United States government.

Money laundering

Money laundering could be divided into three main phases each of which has some distinctive methods through which each phase works. As shown in the following diagram the first process is described as "The Placement Stage" during which the financial proceeds of crime "enter" the financial system. This stage is the most dangerous one when it comes to get caught due to the fact that placing large amounts of money into the legitimate financial system is highly suspicious. Often used ways in order to do that, especially when speaking about large amounts of money would be, gambling or blending funds which is when an individual uses a legitimate business and mixes illegal money with legal sales receipts. After placements comes the "Layering Stage" or the "Structure Phase" as often called. In this stage, the aim is to separate the illicit money from its source thus usually by moving funds electronically, dividing them into investments, most frequently overseas, so as to elude being detected. The final and decisive stage of money laundering is "The Integration Stage". Its objective is to reunite the money with the criminal without drawing attention of the state or the officials. Common practices are purchasing property or expensive jewelry and cars thus not drawing attention into the illegal cash. Potential macroeconomic consequences of



unchecked money laundering have been cited by the International Monetary Fund as inexplicable changes in money demand, contamination effects on legal financial transactions and increased volatility of international capital flow and exchange rates owed to unanticipated cross-border asset transfers. The latter point is especially important and poses a big risk to the EU financial system as money laundering has a direct effect on the Foreign Exchange Market of the economy of the Union.

Transparency in practice

As our topic states transparency is the best weapon that the banking sector has in order to solve ones for all the problem of tax evasion and money laundering. Some countries have tried to put transparency into practice; some have made big steps towards succeeding while others not so much. More specifically in 2014, the Bank of England unveiled proposals that would lead to the disclosure of minutes of rate-setting deliberations, as well as making transcripts and audio recording of policy makers' decisions available to the public. This approach has already been adopted in the US, where the Federal Reserve publishes minutes of its policy meetings within three weeks while the Bank of Japan publishes minutes after a month has elapsed. As we can infer the public is the worst enemy of the potential tax evaders, thus these prime examples show that transparency is already in practice and also has a significant impact. One of the most typical examples is that of the United States and their taxation system, which is being elaborated on in a following sector of this paper. In this case, after implementing the aforementioned policy, one of the biggest declines in their losses due to tax evasion was achieved , whereas before putting the aforementioned into practice lost an estimated 337 Billions of dollars according to a report from the World Bank.

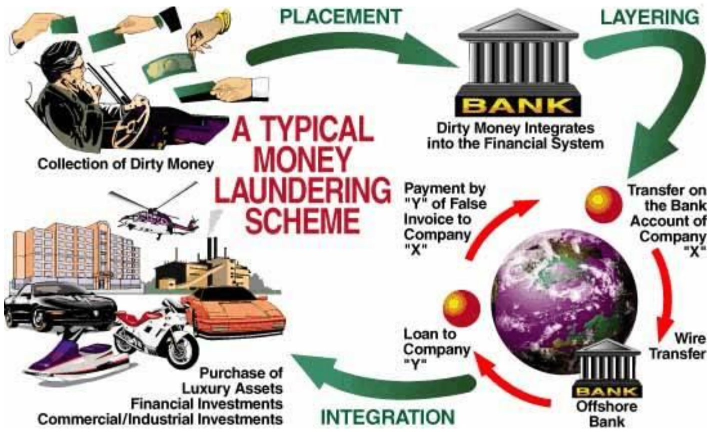


Figure 3: A typical Money Laundering Scheme

MAJOR COUNTRIES AND ORGANISATIONS INVOLVED

Cayman Islands

Cayman is a British Overseas Territory in the western Caribbean Sea and comprises of three main islands. The interesting fact about Cayman Islands is that they are one of the very few countries that do not levy corporation tax, capital gains tax or any other direct taxes on companies located on the islands thus no direct taxation is imposed on residents and companies. The government receives the majority of its income from indirect taxation. Duty is levied against most imported goods, which is typically in the range of 22% to 25%.

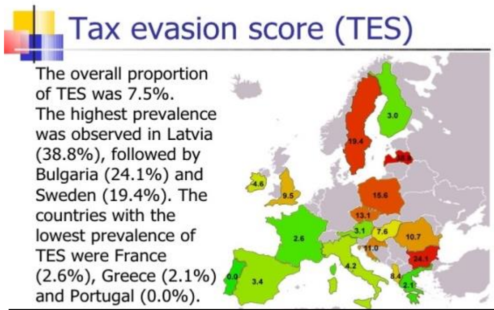


Figure 4 Tax evasion score in Europe

Latvia

Latvia ranks first as the country with the highest tax evasion prevalence in Europe with 38.8%.

Portugal

The state of Portugal ranks first while scoring a staggering (0,0)%, amongst the countries with the lowest tax evasion prevalence in Europe, although it would be safe to say that it holds the top, of the given list even when we speak about the whole world.

Switzerland

Switzerland is considered a tax haven due to its 85 year strict policy when it comes to the secrecy in money related trades in its banking sector, but less than four months after the country refused to sign a very important treaty in 2014 aiming to combat tax evasion, found itself embroiled in the biggest banking scandal in history. The alleged systematic involvement of the bank's Swiss-arm put mounting international pressure on the country's strict 85-year financial secrecy laws and sent ripples through the banking world, highlighting the need for improvements in transparency.

United Kingdom (UK)

According to the HMRC 4.4 billion pounds were lost due to tax evasion only in the United Kingdom during the years 2013-2014. In 2014 though, the Bank of England unveiled proposals that would lead to the disclosure of minutes of rate-setting deliberations, as well as making transcripts and audio recording of policy makers' decisions available to the public.

United States of America (U.S.A)

The United States' taxation system taxes every American citizen the same no matter if you are a resident of the United States or anywhere else in the world. This way the system cannot be "tricked" by offshore accounts and thus making it one of the most effective in the world alongside the one of Eritrea which follows the given tactic as well.

The G20

The G20 is an international forum for the governments and central bank governors from 20 major economies such as but not limited to the United States and the United Kingdom. More specifically the G20 have warned tax havens that if they fail to co-operate with new transparency standards they will face "defensive measures" from countries which represent 85 per cent of the global economy. Furthermore at the spring meetings of the International Monetary Fund and World Bank on April 2016, the G20 finance ministers and central bank governors repeated their commitment to "internationally agreed standards on transparency". The move steps up the pressure on Panama, since it is the only country along with Bahrain that has refused to commit to the new standards, after the release of the Panama Papers showing efforts of the rich to hide their tax affairs from their home countries.

International Monetary Fund (I.M.F)

The International Monetary Fund (IMF) is an international organization formed in 1944 and is consisted of 189 countries working to foster global monetary cooperation, secure financial stability, facilitate international trade, promote high employment and sustainable economic growth, and reduce poverty around the world. In 2000, the IMF responded to calls from the international community to expand its work on anti-money laundering (AML) extending them to include combating the financing of terrorism. The IMF is especially concerned about the possible consequences of money laundering, and related crimes for the integrity and stability of the financial sector and the broader economy. These activities can discourage foreign investment and distort international capital flows. They may also result in welfare losses, draining resources from more productive economic activities, and even have destabilizing effects on other countries.

Financial Action Task Force (F.A.T.F.)

The FATF is an inter-governmental body whose purpose is the development and promotion of national and international policies to combat money laundering and terrorist financing.

Organization for Economic Co-operation and Development (OECD)

The Organization for Economic Co-operation and Development (OECD) is an intergovernmental economic organization with 35 member countries, founded in 1960 to stimulate economic progress and world trade. It provides a platform to compare policy experiences, seeking answers to common problems, identify good practices and coordinate domestic and international policies of its members. OECD is an official United Nations Observer.

Figure 5: The logo of OECD

TIMELINE OF EVENTS

Date	Description of Event
1998	The Vienna Convention
December 14,2005	UN Convention against Corruption
October 30 2014	Global Forum in Berlin on Transparency
April 2015	The first leak of the “panama papers” was made, the biggest data leak in history as there are 11.5m documents and 2.6 terabytes of information

UN INVOLVEMENT: RELEVANT RESOLUTIONS, TREATIES AND EVENTS.

The United Nations Office on Drugs and Crime (UNODC) on money-laundering and countering the financing of terrorism

Law enforcement, organized crime and anti-money-laundering unit of UNODC is responsible for carrying out the Global Program against Money-Laundering, Proceeds of Crime and the Financing of Terrorism. It was established in 1997 in response to the mandate given to UNODC through the United Nations Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances of 1988. The objective of the Global Program is to strengthen the ability of Member States to implement measures against money-laundering and to assist them in detecting and seizing illicit proceeds.

United Nations Convention against Corruption

The United Nations Convention against Corruption was adopted by the General Assembly of the United Nations on the 31st of October 2003 and was entered to force in December 14th 2005. It is the only legally binding universal anti-corruption instrument. The Convention's far-reaching approach and the mandatory character of many of its provisions make it a unique tool for developing a comprehensive response to a global problem. The Convention covers five main areas: preventive measures, criminalization and law enforcement, international cooperation, asset recovery, and technical assistance and information exchange.

PREVIOUS ATTEMPTS TO SOLVE THE ISSUE

World Forum on Transparency in Berlin

On October 30 2014, an agreement was signed by finance ministers from 51 countries in a Global Forum in Berlin which called for the immediate exchange of information among the countries which have singed when it comes to the Banking Sector, who joined forces to ensure the end of tax evasion and money laundering, with Switzerland deferring until 2017.

The Warsaw Convention

The Warsaw Convention was signed by the Council of Europe and its official name is Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime and on the Financing of Terrorism. It was signed on May 16, 2005 and its aim is to combat money laundering in Europe.

The Vienna Convention

The Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances also known as "the Vienna Convention" was signed in 1988 under the auspices of the United Nations. The signatories, agreed to join to cooperate in order to combat the laundering of the proceeds of drug trafficking. The measures included the criminalization of money laundering and enhanced international cooperation together with the commitment of signatories to procure that the laws of their jurisdictions should be amended to bring this about. Much of the success of the Convention depends on enhanced mutual legal assistance, transparency and extradition processes. Given the variety of legal systems, languages and political interests in the world such matters are not simply resolve.

The 1990 Council of Europe Convention

Adopted in November 1990, the Council of Europe Convention establishes a common criminal policy on money laundering. It sets out a common definition of money laundering and common measures for dealing with it. Its scope is not limited to money from drug trafficking but rather to generally eliminate money laundering in Europe.

POSSIBLE SOLUTIONS

"We can't keep relying on the next Lux Leaks or Swiss Leaks to reveal the billions hidden away in the shadow banking system.[…] Banks should be required to disclose information to authorities and the public on a regular basis, like the country by country financial reports now required in the EU, to keep these scandals from happening in the first place." These are the words of the Director of the Financial Transparency Coalition Ms. McConnell when asked about her views on transparency in the Banking Sector and exchange of information between nations in order to combat corruption and illicit actions. As you can

infer the most important part of McConnell's speech is the highlighted one, which underlines the importance of sharing information among nations. This exchange of data could lead to more efficient researches and investigations so as to accelerate the procedures of arresting the criminals thus leading to saving money for the state. In conclusion open communication should be the byword and information-sharing should become second nature to ensure a more stable and secure banking system this could be done through a potential open data base, a framework of cooperation that could be monitored by the United Nations or another Intergovernmental Organization in order to avoid corruption and leaks.

Something that goes along with information sharing but is much more efficient is the mandatory introduction of country reports on a global scale when it comes to details relating to its profits, costs and taxes. In this way everybody would be able to check his or her country's financial whereabouts thus making it almost impossible for corruption to appear within ones nation government. This measure could be voted for by the United Nation's General Assembly or it could be a form of a deal between countries that share common interests although a law or agreement that would be voted on a global scale via the United Nation's G.A, although not legally binding, would be much more efficient.

Last but not least what helps criminals avoid facing the consequences of their actions are the big differences between the legal systems of its country thus being able to exploit different articles to get away with paying taxes. In order for this to be combated the harmonization and codification of money-laundering laws within countries would be a huge step towards solving the problem.

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