The End of Bank Secrecy?

An Evaluation of the G20 Tax Haven Crackdown

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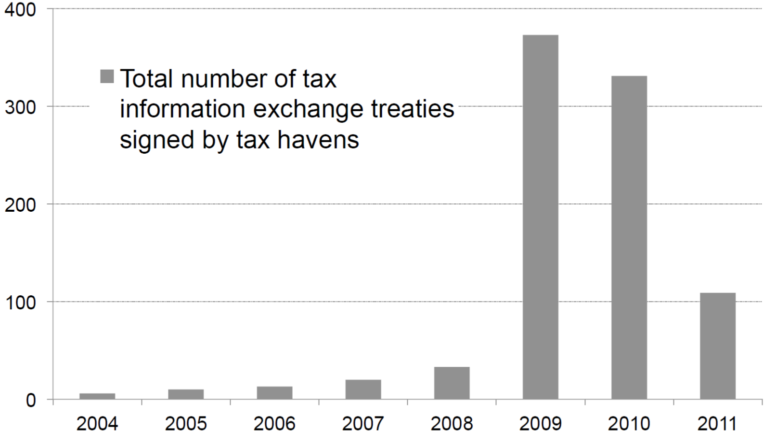
Introduction

- Households hold 8% of their global financial wealth in tax havens (Zucman, 2011)
- Widely held view that household wealth in tax havens is largely untaxed
  - tax authorities have no systematic information about offshore income
  - tax havens do not give this information away
  - detecting tax evasion is very difficult
- Policy agenda: bring capital income subject to effective taxation in residence countries

The G20 tax haven crackdown

- OECD has urged tax havens to conclude information exchange treaties since 1998
  - most important tax havens opposed this initiative
  - very few treaties concluded
- G20 summit in April 2009:
  - OECD draws up list of non-compliant tax havens (12 treaty threshold)
  - G20 countries threaten with economic sanctions
  - all havens commit to comply and start signing treaties

The G20 tax haven crackdown



Does it work?

- The effectiveness subject to controversy:
  - "The era of bank secrecy is over" (OECD, 2011)
  - "Whitewashing of tax havens" (Shaxson and Christensen, 2011)
- Limitations of the G20 approach:
  - information exchange on request - not automatic
  - imperfect treaty networks
  - treaties between havens (e.g. Liechtenstein-Andorra) and between havens and micro states (e.g. Greenland-Samoa)
  - actual implementation
- No fact-based knowledge about the economic effect of the treaties

What do we do?

- Use a unique dataset on bank deposits in tax havens
- Study how and how much treaties changed patterns of offshore bank deposits

What do we find?

- Estimated responses to the treaties
  - shifting of wealth to tax havens with no treaty
  - no signs of repatriation of wealth
  - no signs of increased self-reporting of wealth
- The G20 tax haven crackdown does not seem to have significantly improved tax collection

Data

- Locational Banking Statistics of the Bank for International Settlements
  - bilateral deposit data for 14 havens (e.g. Switzerland, Luxembourg, Cayman Islands)
  - aggregate deposit data for 5 additional havens (e.g. Bahamas, Hong Kong, Singapore)

- Limitations:
  - includes deposits owned by corporations and funds
  - includes only bank deposits (around 25% of total offshore wealth)
  - immediate ownership rather than ultimate ownership basis

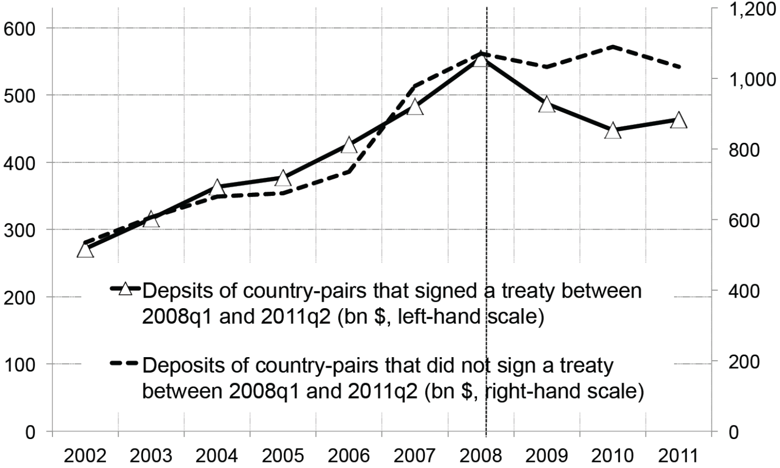
Analytical approaches

- Regression analysis: standard panel techniques
- Graphical analysis

Result #1: Minority of households responded to treaties

- **Result #1**: A treaty between a country and a haven causes a 15% drop in the bank deposits held by the country in the haven
- Interpretation:
  - assume that the behavioral response comes from households
  - assume that 50% of deposits in havens belong to households
  - 30% of households moved their deposits in response to treaties

Result #1: Minority of households responded to treaties

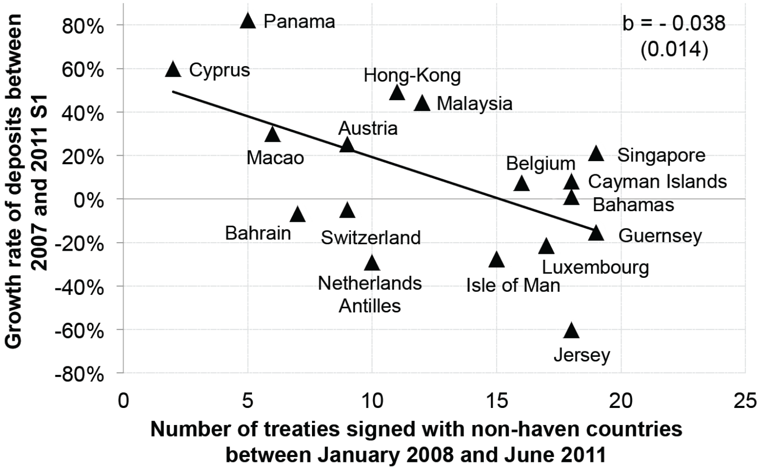


Result #2: Deposit shifting to havens with no treaty

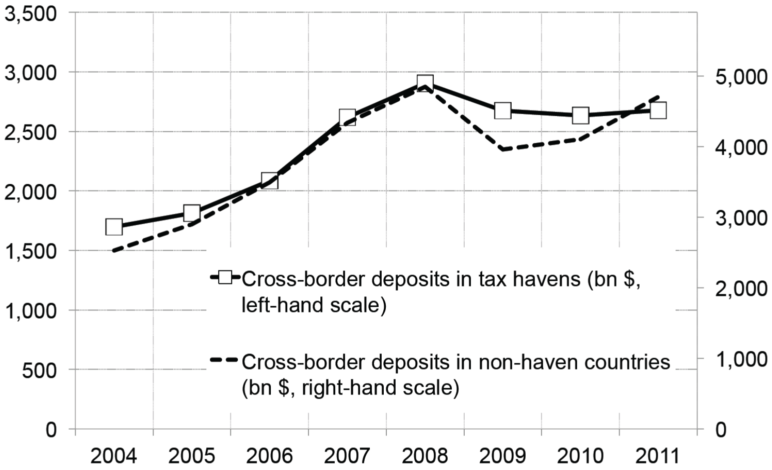
- **Result #2a**: A treaty between a country and a haven causes a 0.6% increase in the bank deposits held by the country in each of the other havens

- **Result #2b**: A treaty between a country and a haven causes:
  - a 1.2% increase in the bank deposits held by the country in each of the havens that have no treaty with the country
  - no change in the bank deposits held by the country in havens that have a treaty with the country

Result #2: Deposit shifting to havens with no treaty



Result #3: No repatriation of offshore deposits



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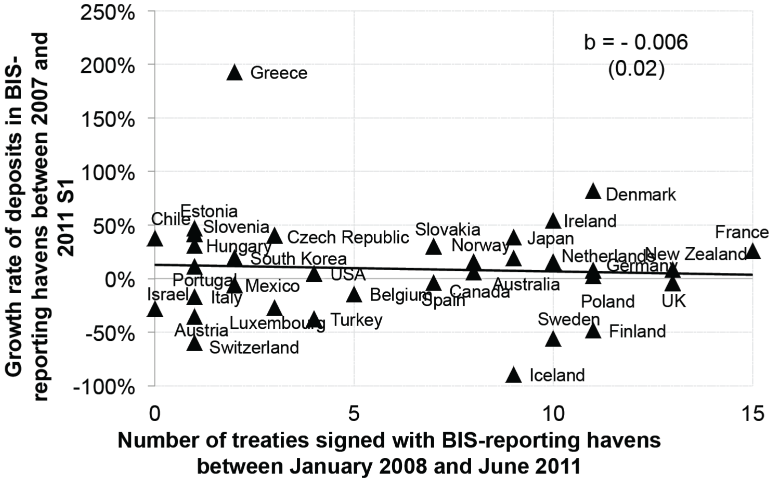
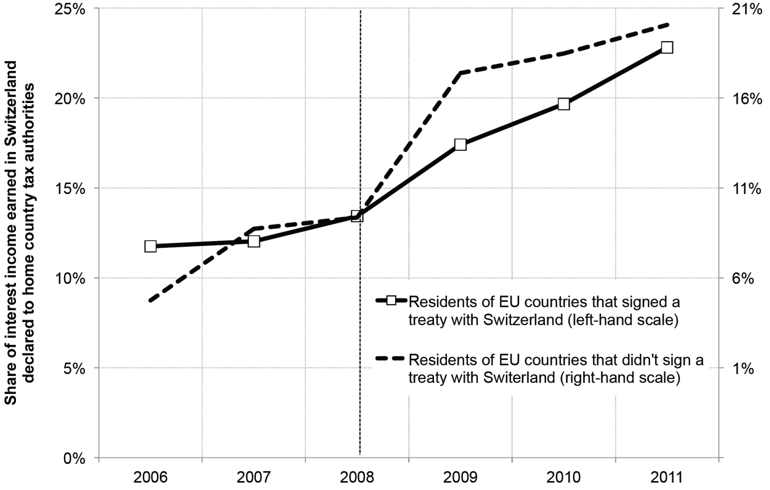


Result #4: No increase in compliance

- The main dataset has no information about self-reporting
- We use a Swiss dataset with direct information on voluntary disclosure of interest income
    - European Savings Directive: Switzerland applies a 35% withholding tax to the interest income of EU households
    - EU households can escape the withholding tax by disclosing their interest income to their home country
    - we can compute the *fraction of Swiss interest income which is voluntarily disclosed* for each of the 27 EU countries

Result #4: No increase in compliance



Result #5: Evaders with sham corporations may have responded strongly

- Around 25% of the bank deposits in havens are recorded as belonging to other havens in the BIS statistics
- This most likely reflects the use of sham corporations

Result #5: Evaders with sham corporations may have responded strongly

- **Result #5a**: A treaty between a country and a haven causes a 1% drop in the bank deposits held in the haven through other havens

- **Result #5b**: A treaty between a haven and another haven causes no change in the bank deposits in one haven assigned to the other haven

Conclusion

- Main findings:
  - significant but most likely modestly sized response to treaties
  - response was deposit shifting rather than repatriation/self-reporting
- Policy agenda:
  - complete treaty networks
  - make treaties more demanding