

The fight against tax evasion in Europe

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by

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1. Background

- Most people do not realise what the structure of the tax gap is:
 - Few realise that offshore is not the biggest part of the problem;
 - And nor are big companies
 - But that domestic tax evasion is the big issue

2. The tax gap

- Three components:
 - Tax avoidance
 - Tax evasion
 - Unpaid tax

3. What we know about the tax gap

- At most country levels, very little indeed, the UK excepted - who do it annually, but in my opinion not very well - plus some sporadic country studies, some of which are already out of date
- At the official EU level, only VAT is assessed, but nothing else. The EU VAT gap estimate is €160bn
- At an unofficial level there is my data for the S&D group on the EU tax gap that has attracted a lot of attention – I estimate the total EU loss at €1trn - consistent with the EU VAT estimate VAT given that VAT is maybe one sixth of government revenues on average in many EU countries

- What we can say with certainty that we do not know enough.

4. What the tax gap data suggests

- Avoidance may be 15% of the tax gap
- Unpaid tax may be up to 20% of the tax gap
- Tax evasion may be 65%, at least, of the tax gap

5. Offshore is not nearly as important in all this as may be thought.

- Data suggests that offshore:
 - may be 5% of the 15% tax avoidance total (or one third of avoidance)
 - may be 10% of the total 65% for tax evasion, so maybe 15% or so of that

6. The consequences of the tax gap data that we have

- I still believe we may be losing at least €1 trillion of loss across the EU to the tax gap, excluding unpaid tax
- More than €800 billion of this may be evasion
- The vast majority of this is domestic, onshore, abuse

7. Why the tax gap is important

- Wherever we are on the political issue of organisation of the economy we always end up with a mixed economy
- All we argue about is how the mix should be made up:
 - The right wing want more private sector
 - The left wing see a bigger role for government
- But no one is seriously saying we should get rid of:
 - The private sector

- The role of markets in allocating some resources
 - The importance of choice
- The need, therefore, is for a level playing field on which all businesses can compete fairly
- Tax abuse undermines the level playing field:
 - Tax avoidance largely impacts big business
 - Tax evasion and unpaid tax impacts smaller businesses and the self employed more
- But in both cases tax abusers:
 - have a lower cost of capital and so an unfair competitive advantage
 - a larger source of capital as their retained profits are higher
 - or a price advantage because they can undercut their honest rivals to make the same return
- And in all cases tax abuse:
 - distorts competition in favour of the tax abuser
 - penalises the honest business
 - undermines the efficient operation of markets by the introduction of an artificial and unfair factor of production
 - reduces the resources available for growth in honest businesses which are also those most likely to invest in capital, R&D and employees for the long term
 - reduces stable employment prospects
 - reduces long term growth rates as a result, largely because cheating businesses tend to be 'fly by night' i.e. transient by their very nature as they seek to stay one step ahead of authorities
- In this case if we are to deliver
 - long term growth
 - a stable small business environment
 - sure employment prospects
 - reliable capital markets
 - a vibrant mixed economy

then we have to tackle the tax gap.

- This is not just about tax though: it's also about the whole of our economic policy as well and the chance that it is properly regulated and managed to ensure long term well-being

8. The steps needed to address tax evasion

- First we need to drastically improve tax gap estimation methodology, practice and publication intervals
 - City, University of London is working on this over the next four years

- Then we need to have data driven approaches to this problem
- The focus on large company offshore tax avoidance has been useful for raising awareness - and as someone who has been instrumental in doing that I offer no apology - but it is not the really big issue now
- The focus on evasion has to be increased
- The focus on domestic abuse has to grow
- This is not a problem that is 'over there in tax havens' but is instead 'here' and 'onshore'
- Technical solutions to tackling domestic tax evasion have to be developed
- Offshore is now being beaten by technical developments such as
 - country-by-country reporting
 - automatic information exchange
 - beneficial ownership data and exchange
- There is less awareness of what the necessary technical developments are to deal with this issue domestically and more work is required on this
 - Again, City, University of London will be working on this

9. The question of resourcing tax authorities is critical to addressing this issue

- Some but not all EU countries are substantially reducing resources for their tax authorities as part of austerity programmes
 - Computerisation has clearly had an impact in this area but that cannot be used to explain all the cuts
- But if the tax gap is to be beaten then resources are needed
- And we must also move beyond purely technical solutions
- Technical solutions on evasion rely on data being available on:
 - Accounts
 - Beneficial ownership
- But in countries like the UK tax returns are not file by at least 1 million companies a year who might have obligation to submit them (based on my research) whilst at least 400,000 companies a year fail to file accounts of any sort
- And there is no evidence that any resources are beg made available to tackle this issue

- The result is that there is massive risk that the data that will be exchanged soon will be quite good for the companies who are honest (about whom few questions will be asked by authorities) and will be very poor or non-existent for companies where there may be wrong doing about which enquiry might be desirable
- There is massive risk in this of total waste of effort on creating systems that yield no benefit because the data exchanged will be incorrect or simply absent
- Vitally, we have no way of knowing which data is incorrect as almost none of it is checked right now

10. Solving the data quality issue

- The best way to do this by far is require that banks in each country be required to submit an annual report on all limited liability entities to which they have supplied services noting:
 - Company name
 - Company number
 - Registered office address
 - Contact address at which the bank corresponds
 - Phone and email contact details
 - The names and addresses of those who the bank thinks are
 - Shareholders
 - Directors
 - Others with whom they have regular contact on the instruction of the company or its shareholders
 - The total sums deposited into and paid from the company's bank account in a year as an indication of the scale of its operation for risk assessment purposes
- Tax authorities then must have the right to estimate tax owing by companies who have not complied and make this the personal responsibility of the directors and others if they cannot be traced
- Limited liability was never meant to be a licence to commit tax fraud but that is what it has become
- The political will to create domestic automatic information exchange of this sort is vital if evasion is to be beaten.

11. More information

More information on the issues noted plus references to other materials to back up the points made and details of the research work now being undertaken on these issues at City, University of London, is available from:

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