Publish What You Pay NORWAY

- Sustainable development goals are wishful thinking unless we finance them.
- Financial transparency and taxes are the keys to finance development.
- Did you know that one mechanism that can fight financial secrecy already exists? It is low cost, effective, and targeted to use. It will show where the money is built up. The only thing missing is politicians willing to use it.

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Ignoring the elephant in the room?

Why financial transparency is necessary to finance development.

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We welcome any questions or clarification needs in writing to post@pwyp.no

Content

1 What is the problem?

- Any discussion about *sustainable development* goals risk becoming wishful thinking unless we discuss how we shall finance the goals and target a root cause behind the problem, not just the symptom.

> ***Sustainable development** goals (SDGs) are a new, universal set of goals, targets, and indicators that UN member states will be expected to use to frame their agendas and political policies over the next 15 years. The SDGs follow and expand on the millennium development goals (MDGs) which were agreed by governments in 2000 and are due to expire at the end of 2015.*
>
> *Source: Ford, L., Sustainable development goals: all you need to know, The Guardian*

- We cannot ignore that between 2003 and 2012, more than $6.6 trillion flowed out of developing nations. This is illicit money that comes from crimes like tax evasion, money laundering, and bribery. These illicit financial flows (IFFs) are increasing at a staggering rate of 9.4% per year.[1] That is twice as fast as global *gross domestic product (GDP)* is increasing. The latest data reveal that IFFs peaked in 2012, totalling more than $991.2 billion.

> ***GDP** is the standard measure of the value of final goods and services produced by a country during a period minus the value of imports.*
>
> *Source: OECD data: Domestic product, https://data.oecd.org/gdp/gross-domestic-product-gdp.htm*

- For every official development aid dollar coming into developing countries, more than $10 left countries in IFFs in 2012.[2] No matter how you look at it, developing nations are losing more financial resources than they are gaining.

- IFFs are destructive to the prospect of *sustainable development*. No country is protected against IFFs; they just hurt developing countries so much more. They undermine the taxbase and thereby hinder mobilising of a country's own resources. Imagine how many education budgets, vaccine programmes, healthcare centres, teachers, and schools IFFs amounts to.

> ***Sustainable development;** Development that meets the needs of the present without compromising the ability of future generations to meet their own needs.*
>
> *Source: World Commission on Environment and Development (WCED). Our common future. Oxford: Oxford University Press, 1987*

- The fact that many large multinational companies and the super-rich hardly pay any income tax at all ,has created an intense and international debate about whether paying taxes has, in practice, become a "voluntary thing".

- This can happen because *multinational companies* and the super-rich have access to a big toolbox of secrecy mechanisms that they can use in order to avoid paying taxes. This toolbox of secrecy is useful for everyone that has something to hide, whether they are multinational companies, super-rich, drug dealers or terrorist networks.

> ***The multinational corporation** is a business organisation whose activities are located in more than two countries and is the organisational form that defines foreign direct investment.*
>
> *Source: B. Kogut: Multinational Corporations, International Encyclopedia for Social & Behaviorial Sciences, Elsevier Ltd*

- One major problem is *secrecy jurisdictions* (tax havens). A common feature of legislation in tax havens is that they do not have an informative public-company registry, no or very limited statutory obligations, no obligation to preserve, no audit requirements, and no duty to disclose who the real owners are. It is quite possible to be anonymous if you wish. It is possible to set up trusts to hide what is happening and hide where the value creation actually takes place.

> ***Secrecy jurisdictions;** Places that intentionally create regulation for the primary benefit and use of those not resident in their geographical domain. That regulation is designed to undermine the legislation or regulation of another jurisdiction. To facilitate its use, secrecy jurisdictions also create a deliberate, legally backed veil of secrecy that ensures that those from outside the jurisdiction making use of its regulation cannot be identified to be doing so.*
>
> *Source: The Tax Justice Network: Secrecy Jurisdictions, Research Briefing, Tax Research UK.*

- The *extractive industry* is a powerful industry with huge profits. Exports of oil, gas, and minerals alone were equivalent to approximately nine times the value of international aid to Africa in 2008. This is important, as 2/3 of the worlds poorest people live in the most resource-rich countries in the world but have seen little income. PWYP Norway has revealed that ten of the largest oil and mining companies in the world, use over 6,000 subsidiaries and that 1/3 of those are registered in tax havens. Natural resources have the largest value-creation potential to mobilise tax revenue, but profit often ends up elsewhere.

1 http://www.gfintegrity.org/press-release/new-study-crime-corruption-tax-evasion-drained-a-record-us991-2-billion-in-illicit-financial-flows-from-developing-economies-in-2012/

2 Kar, D., Spanjers, J., (2014). Illicit Financial Flows from Developing Countries: 2003-2012, Global Financial Integrity.

> ***Extractive industry;** An industry where materials such as oil and coal are obtained from under the ground in drilling, mining, and quarrying.*
>
> *Source: Longman Business English Dictionary*

- The consequence is that profits that should have translated into, and invested in, the common good (such as education, healthcare and jobs) are drained out of the country instead, and transferred to companies and tax havens where little or no tax is paid. Costs are moved to where a company has to pay its taxes or to corrupt leaders, which can lead to maintaining corrupt and irresponsible regimes.

- Countries offering such secrecy claim that this is an exercise of sovereignty. However, rather than an exercise of sovereignty, it is a non-acceptable intervention affecting the sovereignty of other countries that are losing their revenues. Tax havens assure that this capital, which should be given to the developing countries (resource capital) or the developed countries (financial capital), is transferred and placed in jurisdictions without transparency.

- Because of all the secrecy, it is difficult to single out and reveal the difference between tax evasion and organised crime and corruption, both in politics and elsewhere in society. The secrecy that surrounds both the information and the profits.

- It is a paradox that multinational companies and the super-rich seem to expect to use society's infrastructure, have the advantage of a society's rule of law and order, use its effective communication services, and have access to well-educated people, good health services, and a market but seem unwilling to contribute to finance all of this by paying their fair share in taxes.

- This creates a global increase in the income for those who do not pay taxes, but also increases the cost for ordinary citizens who are left to pay for upholding a functioning civilisation.

- This allows gaps in wealth to arise both between and within nation-states to the benefit of a small minority, and to the detriment of the rest of the citizens. The consequence is greater inequality in the world. The global economic system and global world leaders are failing developing countries, and they are failing ordinary citizens.

- It is difficult for citizens to try to unravel layers upon layers of secrecy when multinational companies intensively use secret jurisdictions, *anonymous shell companies*, anonymous *beneficial owners*, and fake companies to cover their tracks.

- Those who try to investigate or announce what is going on are often met with threats, violence, and ruinous lawsuits; they are sometimes even killed. This is done deliberately in some countries in order to scare citizens from holding both companies and governments accountable so that multinationals can continue with their abuse. What if information could instead be public, so that people did not have to risk their lives to reveal abuses of power, corruption, and tax evasion?

> ***Anonymous shell companies;** Companies which only exist on paper, with no real employees or offices.*
>
> *Source: The Economist, Shell companies: Launderers Anonymous, September 2012*
>
> ***Beneficial owners;** A beneficial owner in respect of a company means the natural person(s) who directly or indirectly ultimately owns or controls the corporate entity.*
>
> *Source: EITI: Pilot project: Beneficial ownership, https://eiti.org/pilot-project-beneficial-ownership*

- With this briefing, Ignoring the Elephant in the Room, we present an argument for why financial transparency is necessary to finance sustainable development. We would like to contribute to strengthening young people's competence, attitude, and vigour to meet one of the most dangerous challenges of our time: *financial secrecy*.

> ***Financial secrecy** occurs when there is a refusal to share financial information with the legitimate authorities and bodies that need it - for example to tax citizens appropriately, or to enforce criminal laws.*
>
> *Source: Financial secrecy index: What is financial secrecy? Tax Justice Network, http://www.financialsecrecyindex.com/faq/whatisfinancialsecrecy*

- Financial secrecy is not an inevitable force of nature. It is only politics, and it is very possible to do something about politics. Mechanisms and solutions that can significantly hinder financial secrecy do exist.

- Political root causes can be unpleasant and difficult to tackle, but obviously, this is a relationship between politics, power, the market, and inequality. However, a race to the bottom will leave everyone at the bottom. Society has solved inequality in two ways over the course of history: conflict and war or preventative redistribution. A more transparent economic system is the only sustainable solution in the long term.

- We believe that an informed and demanding youth culture can grasp the attention and interest of people, politicians and the media. Youth can offer insight and knowledge on financial secrecy and how it harms societies and show that there are existing policy measures that can significantly hinder it, if only politicians were willing to use them.

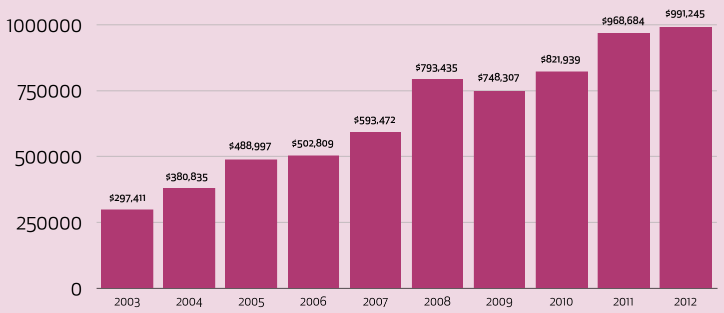
2 What do we know about IFFs?

What are IFFs?

IFFs are illegal movements of money or capital from one country to another. It is called illicit flow when the funds are illegally earned, transferred, and/or used.

Illicit Financial Flows from Developing Countries: 2003 - 2012

(In millions of U.S. dollars, nominal)



Source: Global Financial Integrity

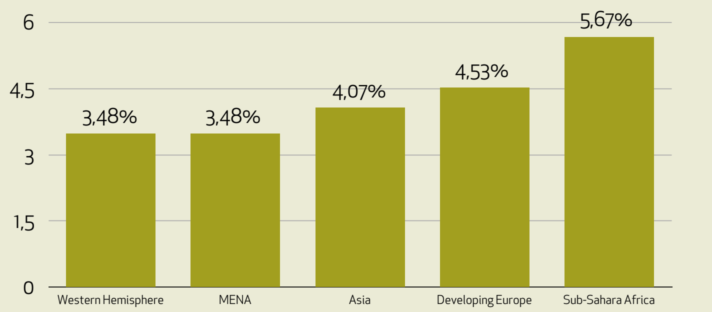
How much do the regions of the world really lose?

A part of the problem is that IFFS are increasing at a staggering rate of 9.4% per year.[3] That is twice as fast as global GDP is increasing. This graph shows IFFs to GDP per region.

3 http://www.gfintegrity.org/press-release/new-study-crime-corruption-tax-evasion-drained-a-record-us991-2-billion-in-illicit-financial-flows-from-developing-economies-in-2012/

Illicit Finacial Outflows to GDP by Region: 2002-2011

(Average annual illicit outflows from developing countries as % of GDP)



Source: Global Financial Integrity

What do IFFs consist of?

There are three different types of unrecorded money moving between countries.

The first includes corruption, the proceeds of bribery, and theft by government officials. When we think about what the problem is, we often think about corruption in a developing country. We also think about leaders who are living their lives in extreme luxury while the rest of the citizens in the country are being held as hostages in poverty and even dying because of lack of access to basic healthcare. This is an important part of the problem, and corruption is destructive for development.

However, on a global scale, this corruption only accounts for 5% of the problem.

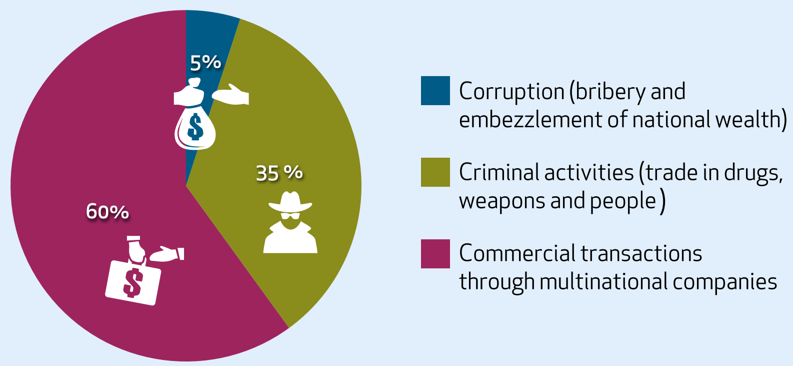
The second part of the problem is criminality, such as drug trafficking, human trafficking, trafficking of endangered animals or parts of animals, and all types of criminal networks, including terrorist networks. The secrecy offered in tax havens is very useful for anyone who has something to hide.
On a global scale, this amounts to 35% of the problem.

The third part of the problem is commercial transactions being routed through multinational companies with intensive use of tax havens. This part of the problem has to do with multinational companies organising themselves in such a way that they can trade through their own structures, and across countries in order to manipulate many types of taxes in order to avoid paying taxes. This amounts to 60% of the problem ,and is the major problem.

For all three types of problems, the only remedy is transparency.

Even though different types of IFFs have been categorised, it is difficult to single out and reveal the difference between tax evasion and organised crime or corruption. This is because of the secrecy that surrounds both the information and the profits. Because of all the secrecy, money from drug trafficking, for example, can easily be invested in the legitimate economy.

What compose illicit financial flows?



Source: Global Financial Integrity

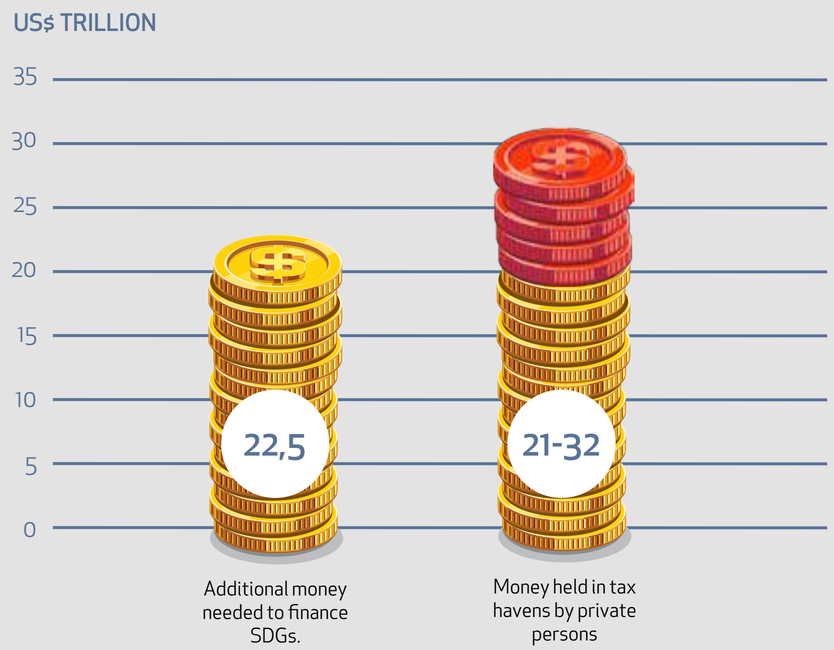
Can all this money just be reversed and put directly into development?

No, of course not. The point is that huge profits end up in places other than in developing countries. We can compare different, relevant data and information to each other in order to get a picture of what may hinder countries from mobilising their own resources, and which resources may be available for sustainable development.[4]

Governments may need to find as much as $1.5 trillion a year to finance sustainable-development goals. It means that politicians have to mobilise about $22.5 trillion over the next 15 years of implementing the sustainable development goals.[5]

This graph shows a comparison of how much money we need to finance development and how much money rich people have hidden in tax havens:

- The first stack of money shows how much additional money is needed to finance SDGs.
- The second stack of money shows how much money private people hide in tax havens. According to a study by James S. Henry[6], wealthy people hold between $21–32 trillion in tax havens.



4 For example domestic resources (which include domestic investment and government revenue), "lost resources", (such as including illicit financial flows, profits taken out by foreign investors, including interest payments on foreign debt and lending by developing countries to rich countries), and inflows of external resources, including international public resources (aid and other official flows), private flows for profit (such as foreign direct investment and investments in stocks and shares) and private flows which are not-for-profit (such as charitable flows and remittances from migrant workers) and debt-creating flows (which are both public and private borrowing by developing countries). See: http://www.eurodad.org/finance_for_developing_countries

5 According to the Government Spending Watch report

6 Henry S., J., (2012), The Price of Offshore Revisited, Tax Justice Network.

This is how the companies are avoiding taxes:

- **They're hiding to build financial muscles**

  PWYP Norway revealed that ten of the world's most powerful extractive industry giants own at least 6,038 separate companies, and a minimum of 1/3 of these separate companies are located in secrecy jurisdictions (tax havens). In PWYP Norway's investigation, Delaware was the favourite place for multinational oil companies to register. The Netherlands came in second place [7].

- **They get a fancy address at, for example, 1209 North Orange Street, Delaware, CT, USA:**

  At least 285,000 companies are registered at a single address in Delaware in the United States. More than 50% of all US publicly traded companies are incorporated in Delaware. Among them are Google, Apple, Coca-Cola, Bank of America, Ford, General Electric, JP Morgan Chase, Wal-Mart, American Airlines, and many more. The secrecy for sale is used by big multinational corporations, small businesses, and private individuals to minimise taxes, avoid regulations. And their own governments conceal information, and cover their tracks, but smugglers, drug traffickers, criminals, and money launderers are also here. Delaware is the state that requires the least amount of information. It's easy to set up shell companies in Dalaware, no questions asked [8].

- **Companies say they are just following the law, so try to tax them if you can:**

  Wealthy people have placed between $21–32 trillion in tax havens; this amount is roughly similar to the US and Japanese economies combined [9].

- **They are using secrecy as a business model:**

  $1 of every $2 of large corporate investment in developing countries is channelled through tax havens[10]. The key features of a tax haven are that it is a state, country, or territory where the legal system favours secrecy over transparency, and which requires little or no information for taxes. Such rules do not apply to residents who live there, only to those who do not live there so that they can avoid obligations in their home countries. The business model is to sell secrecy. Tax havens have, in effect, declared war on honest taxpayers by giving those who avoid taxes the means to do as long as they can pay for it, which leaves others to finance society back home.

12 Pak J., S. (2012), Lost billions. Transfer pricing in the extractive industries, Publish What You Pay Norway

13 Kar, D., Spanjers, J., (2014). Illicit Financial Flows from Developing Countries: 2003-2012, Global Financial Integrity.

14 van der Does de Willebois, E., et al., (2011), The Puppet Masters: How the Corrupt Use Legal Structures to Hide Stolen Assets and What to Do About it, Stolen Asset Recovery Initiative, The World Bank, UNODC.

- **Trading with themselves:**

  More than 60% of world trade takes place within a multinational companies[11].

- **Transfer mispricing their billions:**

  A study by PWYP Norway estimates that over $110 billion disappeared through mispricing of crude oil in the United States and the EU between 2000 and 2010[12].

- **Leaking like a fish net:**

  IFFs from developing countries peaked at $991 billion in 2012[13].

- **Give themself shelter:**

  World Bank showed that 70% of corrupt politicians used anonymous companies in 200 major corruption cases to conceal their identity. When money first was stolen, the reversal rate was only 0.2%. Money from corruption, crime, and tax evasion can be easily laundered into our economy through concealment, secrecy, and anonymity[14].

- **Profits or proceeds of avoiding tax?:**

  56% of US companies' foreign profits are attributed to tax-friendly sites[15].

- **They borrow to pay dividends:**

  Apple has the biggest build-up of cash in corporate history (around $200 billion) stashed away in tax havens. So in order to pay **dividends** to their investors, Apple decided not to take the money out of tax havens because this would require them to pay taxes to the authorities. Instead, they borrowed money in order to pay dividends[16].

? **Dividends** are a sum of money that is paid regularly (mostly annually), from a companys profits to the company ' s shareholders.

11 Source: Neighbour, J.,Transfer pricing: Keeping it at arm's length, OECD Observer, January 2002.

12 Pak J., S. (2012), Lost billions. Transfer pricing in the extractive industries, Publish What You Pay Norway

13 Kar, D., Spanjers, J., (2014). Illicit Financial Flows from Developing Countries: 2003-2012, Global Financial Integrity.

14 van der Does de Willebois, E., et al., (2011), The Puppet Masters: How the Corrupt Use Legal Structures to Hide Stolen Assets and What to Do About it, Stolen Asset Recovery Initiative, The World Bank, UNODC.

15 Drucker, J., Inversions Are Often Last Stop for Avoiding U.S. Taxes, Bloomberg Business, December 12, 2014.

16 West, M., Tax Avoiders: Apple joins other multinationals in sinking to the bottom of the ocean, Brisbane times

10 reactions

-"You've got a building in the Cayman Islands[17] that supposedly houses 12,000 corporations. That's either the biggest building or the biggest tax scam on record.[18]"

Barack Obama,
president of the United States.

"Inevitably, when we talk about tax avoidance, the spotlight falls on the high-profile cases. But tax avoidance is not confined to a small number of wealthy companies and individuals – it is a whole, grubby industry from which shameless tax advisers and promoters are making big bucks. That is simply unacceptable. We cannot have an industry in this country based solely on ripping off the public purse."

Margareth Hogde,
labour MP, UK

"We have created a system which ensures that billions of dollars are placed outside our control. It is an international system, and countries, including Great Britain, have contributed to creating this system. This is a legal but terrible system. In combination with globalisation, it constitutes a death trap for tax."

Dr. Jeffrey D. Sachs, professor in Economics at the Earth Institute, Columbia University and a Special Adviser to UN Secretary General Ban Ki-moon.

17 In 2010 Forbes included the Cayman Islands in the list of World's "best tax havens". Source: http://www.forbes.com/2010/07/06/tax-havens-delaware-bermuda-markets-singapore-belgium.html

18 Democrat Primary Debate, Manchester, N.H., 1/5/08

"We often say: how do you spell development? T A X. We need to allow countries to gather their own domestic revenues in order to finance their own development.[19]"

Grace Perez-Navarro, deputy Director, Tax Policy Administration, OECD

"No one has the right to set his own tax rates. It is not right for individuals to grow wealth from free trade and economic integration only to take off profits at the expense of their neighbours. That is outright theft."

Thomas Piketty - French Professor of Economics at the Paris School of Economics who works on wealth and income inequality. He wrote the book Capital in the Twenty-First Century

"Tax havens are indeed heavens for tax evaders and fraudsters, but they are hell for the law-abiding citizen and responsible tax-payer."

José Manuel Barroso,
former European Commission President

"While the poor and middle class fight for us in Afghanistan, and while most Americans struggle to make ends meet, we mega-rich continue to get our extraordinary tax breaks."[20]

Warren E. Buffett,
american businessman and philanthropist

"There would be more revenue for all if countries resisted the temptation to compete with each other on taxes to attract business. By definition – a race to the bottom leaves everybody at the bottom."

Christine Lagarde, managing director, International Monetary Fund

19 S0ource: Speech in the seminar «The Industry of Tax Avoidance», organized by PWYP Norway, Oslo.

20 Warren E. Buffett, Stop Coddling the Super-Rich, The New York Times, 14 August 2011

3

What are the consequences for society?

We have achieved much in our global world. But, amidst progress for some; billions of people across the world still lack access to basic food, water, health services, energy, security, education, and jobs. Corruption, capital flight, and financial secrecy are preventing us from addressing the most urgent problems.

Our forests, water, and biological diversity are threatened in the name of profit, often through companies where the real owners are hidden. We see environmental destruction, and there is no one to hold accountable.

Millions of citizens across the globe experience the effect of armed conflict, crime, terrorism, and persecution daily when challenging their government on transparency and breaches of human rights, corruption, impunity, exploitation, injustice, and the erosion of the rule of law. We already know that natural resources create a fertile ground for conflict. It is obvious that when financial resources are not benefitting all of society and people do not have access to education, food, water, and having their basic needs covered, they become vulnerable and desperate. We see that human displacement is at its highest level since the Second World War.

Citizens across the planet are deeply concerned about the consequences of climate change, and that we are only seeing the beginning of the problems that we will be facing. It is one of the most pressing moral questions of our time, and it is urgent that we make capital flows more transparent so that we can finance our common global challenges. The problems we are facing are truly global, and we must all strive to do our part and inspire others to accept their responsibility.

We see increasing and widening income inequality. This widening gap is one of the defining problems of our time. If a goal is to spark economic activity, we cannot ignore the lower-income social strata because income inequality is harming the potential for economic growth[21].

Today, more than 7 billion people are living on our planet. One billion of the world's citizens receive 80% of global income. One billion barely survive on less than a dollar a day. This is an inequality that is not sustainable, and which urgently needs to be addressed. In countries where inequality and poverty levels are high, illicit financial flows also are high.

Global inequality seems to be slightly decreasing and inequality within nations is increasing. But a small decrease in overall inequality may not be true because available national data regularly underestimate the top 1% of incomes, and because global tax havens conceal the reality of those incomes.

We will not be able to address our global challenges with the current economic system, which allows the richest to get richer. By increasing the income share of the poor and the middle class we can see an increase in growth. Increasing income share in the top 20% results in lower growth—this means that when the rich get richer, the benefits do not trickle down[22]. Excessive inequality does not enable sustainable growth, so if you increase the income share of the poorest, you get a manifold effect that you do not get if you increase the income share of the richest.

An economic system where multinational companies and the super rich are allowed to not pay taxes, and where national companies and ordinary citizens must pay taxes, is effectively undermining both competition and the market.

Today, over half of the world's 100 largest economies are multinational companies. Which means that 75 percent of the world's states have a GDP below the annual profit in each of the 50 biggest companies[23].

Multinational companies and the super rich are able to pay for legal and accounting advice on how to avoid rules and laws, and how to get rid of rules and laws. Through lobbying and litigation, companies are able to get rid of regulations they do not like, such as environmental protection, and to try to get politicians to shift the tax burden away from capital and onto labour. Such advice has developed into an industry in itself. We used to see oil companies pushing contracts on countries that had clauses that said their contracts should be above any national and international laws. Today, we see that multinational companies and the super rich are getting richer and increasingly more able to control political power.

Multinational companies are spending billions on lobbying governments (in some countries, they even are financing political campaigns), and they are pushing and lobbying to create trade agreements that contain clauses say they shall be allowed to make money exactly the way that they want to, and if the government interferes, they will sue them.

The multinational companies and the super rich may claim it's all legal. It may be legal, but it is not right. And it is not sustainable!

21 http://www.imf.org/external/pubs/cat/longres.aspx?sk=42986.0

22 Increasing the income share of the poor and the middle class actually increases growth while a rising income share of the top 20 percent results in lower growth—that is, when the rich get richer, benefits do not trickle down.

23 compiled by Sarah Anderson and John Cavanagh of the of the Institute for Policy Studies in their Report on the Top 200 corporations released in December 2000. http://www.corporations.org/system/top100.html

4

What has been said and done about the problem?

What does the UN do about financial secrecy?

With the eight Millennium Development Goals (MDGs) derived from the Millennium Declaration and adopted by all United Nations Member States in 2000, world leaders made a commitment to time-bound goals to combat poverty, hunger, and diseases, provide education to all children and equal opportunities to both women and men, protect the environment, and establish a global partnership for development. They pledged to achieve all of these goals by 2015.

These goals focused mostly on the difference between rich and poor countries, not the inequality within countries.

There has been important progress in achieving universal primary education, gender equality, and safe drinking water in rural areas, but there have also been shortfalls, most notably on human development goals such as reducing child mortality, improving maternal health, and on environmental goals such as on CO2 emissions and protecting forests. So we have achieved much, but financing is still needed for the remaining goals.

Likewise, by 2015, a global debate on what is to come after the Millennium Development Goals (MDGs) has been undertaken. The UN released a report that set up six essential elements to frame and reinforce the sustainable development agenda, which again formed the basis for 17 sustainable development goals (SDGs). The discussion about how we can finance such development has been held within many countries and is called the 'financing for development' debate.

This discussion comes after the world has experienced a global financial and economic crisis. Many countries were hit hard and each faced different challenges. The more interconnected a country has been with the world economy, the more seriously the country has been hit. This has had an impact on the willingness of industrialised countries to fund development in other countries because they are struggling with their own problems. At the same time, we know that financial secrecy is one core aspect of the financial crisis.

The 193 UN member countries are being criticized for not having sufficiently addressed illicit financial flows. A global community is pushing the UN to stop illicit financial flows.

What does the *EITI* do on financial secrecy?

The EITI *is a voluntary standard and process with requirements for improving the governance of natural resources, and it is a voluntary tripartite transparency process that brings together stakeholders from government, civil society, oil, gas, and mining companies and investors.*

The goal is to produce an EITI report, which discloses company payments to the government and government's receipts. The purpose is to allow citizens to see how much their government is receiving from their country's natural resources, and thereby strengthen government and company systems, informing a public debate, and enhancing trust. Some countries have put the EITI requirements of payments to governments into their law system.

The information in an EITI report is not accounting reporting, so it is not possible to use this as statistical financial information across countries, and different countries also contribute differently to the EITI process. The EITI is a mechanism established because other mechanisms were lacking.

Historically, the EITI has focussed on payment of taxes and other payments, which may reveal discrepancies and potential corruption. More recently, the EITI is arguing for transparency of beneficial owners, which can reveal who owns a company.

What do the USA and the EU do about financial secrecy?

A minimum requirement for transparency has been introduced in the USA and the EU. The law requires publicly traded companies in the extractive industries to disclose what they paid in taxes to foreign governments. The EU has also included forestry. The intention is that it should be possible to compare payments from companies with the state authorities, with what the government says it receives for all countries from which it extracts resources.

These are the same principles as the EITI, but it has been established as a requirement in law. This minimum reporting on tax payments is called 'country-by-country reporting'. The US law is called the "Dodd-Frank Act" and the EU law is called the "EU Transparency Directive". What they have in common is that they are laws that demand oil companies to publish information on tax payments.

23 compiled by Sarah Anderson and John Cavanagh of the of the Institute for Policy Studies in their Report on the Top 200 corporations released in December 2000. http://www.corporations.org/system/top100.html

Although these laws are milestones for transparency, they are still a minimum standard for country-by-country reporting because this is information about tax payments. Information on tax payments may reveal possible discrepancies that can be investigated further in order to see if corruption has happened. It is necessary and relevant, but it cannot address illicit financial flows.

What does Norway do about financial transparency?

Norway has implemented the same law as in the EU.
But, since companies transfer significant profits out of the source country before it's taxed, it is not enough to know only which tax payments a company has paid.

That is why Norway is moving in the direction of an extended country-by-county reporting standard which, when correctly implemented, can show where the capital has been built up. An extended country-by-country reporting standard is, therefore, a relevant tool if governments would like to investigate possible tax avoidance.

What does the African Union (AU) say about financial secrecy?

The African Union (AU) and United Nations Economic Commission for Africa (UNECA) released a report in 2015 on illicit financial flows called 'Why Africa needs to track it, stop it and get it[24]', and showed that Sub-Saharan Africa lost an annual average of $52.9 billion—about 5.5% of GDP in illicit financial outflows—from 2003-2012. The former South African President Thabo Mbeki led the process and launched the report, which recommended curtailing trade-related illicit flows, which is the largest part of measurable illicit financial flows (IFFs). This is an important first step in showing the magnitude of the problem. It remains to be seen what the countries in the African Union will do about it and which mechanisms they will use to hinder it. This is ultimately a political matter.

The African Union (AU) *is a continental union consisting of 54 countries in Africa, which was established in 2001. Its purpose is to lead Africans' integration and development.*

What does the IMF say about financial secrecy?

The International Monetary Fund (IMF) showed that international companies have managed to push the income tax down to zero, and the countries lose up to 15 percent in tax revenue. They said that the more countries that yield to investors' demands
when it comes to taxes, the more the international society will suffer. The fact that international companies reduce the tax they pay and legally review tax claims has major implications for national economies, as well as for undermining its ability to finance government expenditure.

The International Monetary Fund (IMF) *is an organisation of 188 countries. It was conceived at a UN conference in 1944 to build a framework for economic cooperation. The IMF's main task is to ensure stability in the economic system.*

What does the OECD say about financial secrecy?

The process *OECD* has had to address financial secrecy is its process on 'base erosion and profit shifting', called BEPS. The OECD addressed the problem by saying that the country-by-country information should only be intended for, and accessed by, tax authorities, which will have to collect the information themselves through formal processes—and only in order to address possible transfer pricing purposes and with high exclusion thresholds.

The companies do not have to publish annual accounts in the public domain.

It is very unlikely that this mechanism will have any effect for issues related to base erosion and profit shifting out of developing countries.

The Organization for Economic Co-operation and Development (OECD) *has 34 members and was established in 1961. They claim to promote policies that will improve the economic and social well-being of people around the world.*

What does the International Bar Association's (IBA) say about financial secrecy?

The International Bar Association (IBA), the world's largest legal organisation, sees tax avoidance from a human-rights perspective. When an increasing number of multinational companies use legal advice and other mechanisms to avoid paying taxes, the effect is that the companies are removing the resources that nations need to realise human rights.

This can be a breach on human rights, says IBA, who connected tax abuse, poverty, and human rights[25].

24 http://www.uneca.org/iff

25 http://www.ibanet.org/Article/Detail.aspx?ArticleUid=4A0CF930-A0D1-4784-8D09-F588DCDDFEA4

5

Enough talking! What needs to be done?

- PWYP Norway says that it is not enough to know which tax payments a company has paid. The problem is that companies can transfer significant profits out of the source country before they are taxed by using many types of secrecy mechanisms. We call all these different ways of avoiding tax as the 'secrecy toolbox'. The consequence is that a country loses its potential tax revenue and cannot finance its development.

- PWYP Norway proposes mechanisms that are low-cost, effective, and targeted so that they can significantly hinder such leakages. We encourage governments, tax authorities, academics, journalists, and others to discuss these mechanisms when they analyse and discuss their resource tax systems and the need to design an optimal tax system in general. Neglect can cost a country deeply in tax loss.

- The problems and the solutions are so interlinked that it is almost impossible to discuss one without the other. To act, we need knowledge. Lack of transparency and standardised information has become a global as well as a national democratic challenge that requires financial, legal, and political measures. At the same time, we see there is very little knowledge on the techniques used by the extractive industry to channel profits away before they become taxable. There is also little understanding of what can be done to solve the problem.

- It is necessary to understand where the leaks are happening, which techniques are being used, and which mechanisms work together in order to comprehend which solutions can work for which problem. In the same way that there is no medicine that can cure all diseases in the world, there is not one policy measure that can fix all tax systems in the world. This is about creating the optimal mix of different policies.

- PWYP Norway has produced knowledge and written reports that discuss some of the problems, and some of the secrecy mechanisms used by the extractive industry to avoid taxes and what can be done about these mechanisms. We also show which mechanisms can be enacted upon unilaterally, and which mechanisms that must be harmonized with another to have full effect.

- Our reports cover various aspects of financial secrecy in the extractive industries. To make this information available for all, we highlight the most important information from the reports in a briefing. The briefing is short and explains the problem, the consequences, and the solution we suggest. In this part, we will present the short versions of some of the reports we have published.

- To illustrate the situation we see today, we have worked with professional illustrators to try to capture—in one picture—what this problem is about. You will find this picture on the front side of each report and briefing. We hope this picture can be of help when trying to understand the different problems addressed in the different reports, and also in discussing what the reports are addressing.

PWYP Norway has written several reports that explain how finacial leakages can happen and present mechanisms that can stop it.
On the next pages you can read brief summaries of these reports.

An extended country-by-country reporting standard

In the report "An extended country-by-country reporting standard. A policy proposal to the EU. Volume 2", Publish What You Pay Norway provides a policy proposal requiring multinational extractive companies to be transparent about their operations in every country.

THE PROBLEM

2/3 of the world's poor live in countries rich on natural resources. Extraction of these resources is a great opportunity to mobilize capital that can be invested in poverty reduction. Still, the money often ends up elsewhere. Multinational oil and mining companies have been given access to profit on the extraction of natural resources from many of the world's poorest countries. The extractive industry has been under increasing criticism for corruption, tax evasion, human rights violations and for shifting profits from source countries to other parts of their corporate structure, often in tax havens. All this is done under a shield of opacity: contracts are secret, parts of the corporate structures are undisclosed and the financial statement information is so aggregated and condensed that even the most interested reader is left uneducated. These companies are extracting resources that are owned by the countries they operate in, and the companies sell their products in transparent markets provided by other countries. The demand is rising on these companies to be transparent about their operations in return.

THE CONSEQUENCES

Until today, multinational companies have not been required to provide key information about their actions in the countries they operate. Instead, the companies are able to build large fortunes from the extraction of natural resources and hide them in tax havens, where information about ownership, accounts and transactions are kept secret. The lack of international regulation has made financial secrecy possible and lucrative. For over 50 years, this financial secrecy has contributed to rob generations of citizens in resource-rich developing countries of the financial basis that could have aided sustainable development. When governments, investors, journalists or citizens ask the companies for information about where the money has gone, they meet a wall of silence and secrecy.

A SOLUTION

An extended country-by-country reporting standard is one of the best, most targeted and inexpensive tools to hinder corruption and capital flight in the extractive industries. In addition, it will create a more level playing field for the companies worldwide. The policy proposal will require the companies to report eight key accounting figures for every country that they operate in. These few figures will provide governments, investors and citizens with the information they need to assess how the companies manage the resources, where the money flows and whether the countries get their fair share of the revenues. Only with such reporting are citizens able to hold their governments and the companies accountable, and investors able to know the true value of their holdings.

Q&A

What does the "extended" in country-by-country reporting stand for?

The European Union and the United States have both introduced country-by-country reporting for the extractive industries, requiring companies to report tax payments in each country in which they operate. This is a great step in the right direction, but PWYP Norway has demanded that Norway takes the legislation further by introducing "extended" country-by-country reporting. This involves developing the reporting standard after two important criteria . The first concerns the content: Tax payments need to be presented in context. No figure presented in isolation gives much meaning. Unless the reporting includes key accounting figures, it will not be meaningful. The second concerns the form: The reporting must be linked to the consolidated financial accounts of companies and take the form of notes to the consolidated financial accounts, at least with respect to the key accounting numbers. The financial accounts are already audited and therefore trustworthy and would not need additional and costly auditing and verification. If companies are not required to present the reporting from their audited financial accounts, they will have a considerable scope for circumvention. Any country-by-country reporting that fails to meet these two core requirements will automatically entail less confidence in the reporting and/or have higher costs. The reporting requirements in the US and the EU do not include these two criteria yet, but this could be about to change. France has already demanded country-by-country reporting for banks based on financial accounts. The proposal from PWYP Norway is supported by investors, tax authorities, the ministry of Foreign Affairs, the central unit for prosecution for investigation of economic and environmental crime, the Association of Norwegian editors and organizations at large in Norwegian civil society. The proposal has also been presented for the EU commission in 2012.

How close are we to extended country-by-country reporting in Norway? What remains?

- Natural resources have not helped citizens of poor countries to escape poverty.
- Cash flows often end up elsewhere, in the accounts of multinational companies in tax havens.
- The Norwegian Ministry of Finance has issued regulations on extended country-by-country reporting, which will show where cash flows end up.

15 out of 18 elements have already been implemented in the extended country-by-country reporting. However, 3 critical elements are still missing for the legislation to work as intended and prevent companies

How YOU can ensure that we rectify the last few omissions.

- Investors can trace their money and assess how companies manage assets.
- Lawmakers can treat companies equally and create a level playing field.
- Citizens can hold their governments and companies accountable.

How close are we to extended country-by-country reporting in Norway? What remains?

15 of 18 elements of the extended country-by-country reporting are already in place!

Only 3 elements remain for the objective to be realised

RED FLAG 1 is about CONTENT:

What is the problem?
The regulations issued by the Norwegian Ministry of Finance refer to the «purchase of goods and services» instead of costs.

What is the implication?
The implication of the regulations requiring reporting of the purchase of goods and services only, and not of total costs, is that reporting is not credible because it becomes difficult to identify the real profits of companies, i.e. total revenues less costs, and thus to establish a link to the tax figures.

What is the solution?
The regulations must require specification of the full costs on a country-by-country basis, thus implying that both revenues and costs are disclosed through country-by-country reporting. If the «purchase of goods and service» is of special interest to the Ministry of Finance, such reporting should take the form of a sub-group of costs.

RED FLAG 2 is about FORM:

What is the problem?
The regulations do not require country-by-country reporting to match the accounting figures of the companies from extraction activities, i.e. audited figures.

What is the implication?
The implication is that the wording is not in line with developments elsewhere in the world. France has, for example, already incorporated the EU provisions into French law, with a requirement that country-by-country reporting shall also apply to banks and that the information shall be disclosed in notes to the annual financial statement on a country-by-county basis (Art. 89, CRD IV of 26 June '13; Capital Requirements Directive).

What is the solution?
The information must be disclosed in notes to the annual financial statement because the most logical and effective place from which to obtain financial information is the audited financial statement of a company. This means that the reporting of accounting figures does not entail any additional costs, because such figures have already been audited.

RED FLAG 3 is about FORM:

What is the problem?
The regulations only require companies to disclose these details from producer countries, and allow for exemptions.

What is the implication?
The implication of the regulation being limited to producer countries only is that we ignore all company subsidiaries in tax havens. PWYP Norway showed that ten of the largest companies operate with at least 6,000 subsidiaries and that 1/3 of these are registered in tax havens. (This is only the information that companies were comfortable with disclosing. We did not have access). These countries are of key importance when seeking to get an overview of the total revenues and costs of extraction companies, which are not limited to the countries in which production is taking place, in addition to the fact that these are the exact jurisdictions that serve as the main conduits for capital flight, tax evasion and corruption.

What is the solution?
The information must be disclosed for all countries. No exemptions must be granted. The regulations must also exclude the scope for exempting subsidiaries from reporting, with the regulations being amended to ensure that all activities included in upstream reporting are also reported on a country-by-country basis, in line with similar legislation in other countries.

2010

2014

- TYPE AND TOTAL AMOUNT OF PAYMENT FOR EACH PROJECT
- TYPE AND TOTAL AMOUNT OF PAYMENT MADE TO EACH GOVERNMENT
- TOTAL AMOUNTS OF PAYMENTS, BY CATEGORY
- THE GOVERNMENTS THAT RECEIVED THE PAYMENTS, AND THE COUNTRY THE GOVERNMENT IS LOCATED
- THE PROJECT TO WHICH THE PAYMENTS RELATE
- CURRENCY USED TO MAKE THE PAYMENT
- FINANCIAL PERIOD IN WHICH THE PAYMENT WAS MADE
- BUSINESS SEGMENT OF HTE RESOURCE EXTRACTION ISSUER THAT MADE THE PAYMENT

Basic country-by-country reporting

Tax payments to governments can indicate corruption if these do not match what governments claim to have received. (Dodd-Frank/EU)

- PRODUCTION (per type)
- # EMPLOYEES 31.12.
- INVESTMENTS (mill USD)
- REVENUES (mill USD)
- COSTS (mill USD)
- CASH TAX IN THE P&L
- PAYABLE TAX DEBT 1.1.
- PAYABLE TAX DEBT 31.12.
- IN NOTES TO THE ACCOUNTS
- NO EXEMPTIONS, ALL COUNTRIES INCLUDED

Extended country-by-country reporting

Tax payments to governments reported in context can show which countries cash flows end up in.

Downstream pollution of upstream numbers

in Statoil's first country by country report

The Norwegian regulation is clear: It is the production activities (upstream) that should be reported on for each country. Publish What You Pay Norway's analyses show that Statoil in its reporting has allowed numbers from downstream operations to be mixed with, and pollute, the numbers from upstream operations.

If Statoil also wants to report on its downstream business, that is fine. But upstream operations must still be reported separately, and in accordance with the regulation.

The Norwegian country-by-country regulation has the same definition as the EU directive of what constitutes upstream activities: …undertaking activity in the extractive industry' means an undertaking with any activity involving the exploration, prospection, discovery, development, and extraction of minerals, oil, natural gas deposits or other materials. This is what is called upstream activities in extractive industries. Downstream activities are refining, trading and marketing / selling final production. Downstream activities are not part of the definition of the current country-by-country reporting under the EU directive, nor under the Norwegian regulation.

The way Statoil has reported is detrimental to the work being done to promote more transparent reporting by the extractive industries worldwide. That is because there is no clear correlation between the taxes paid in upstream activities and the context in which taxes are paid (upstream activities). Therefore Statoil should publish a new report that is in line with the regulations, and report upstream activities country-by-country. If downstream activities are reported (separately), then revenues and cost associated with downstream should be reported in the country where income is actually earned or costs added.

Norwegian politicians and bureaucrats should take some of the blame for Statoil not getting it complete in the first country-by-country reporting in the world.

When regulations only require companies to report purchases of goods and services, the full cost of upstream is not shown. This means that it seems as if profits in individual countries are higher than it actually is, which in turn have the effect that taxes reported seem relatively lower than they actually are. That means that the company can attract criticism for paying to little tax relative to the apparent profits. Norwegian authorities therefore expose Statoil and other companies for unnecessary and unfair criticism when they have made a regulation containing such weaknesses. Publish What You Pay Norway has worked intensely since long before the regulation came out that Norwegian authorities must rectify weaknesses in the reporting to ensure that the reporting is as accurate as possible. We have come far, but regulation is missing three key elements to function as intended. Politicians have a responsibility to make a good law, and that it is the relevant figures reported: Only upstream activities or upstream activities that are separated out, and with all upstream costs included.

Tax in context is the employees, the investments, the production, the revenues, the costs and the taxes for extractive activities (that is upstream) in every country around the world – nothing more, nothing less.

On page 5 of its country-by-country report, Statoil showed its value chain and the scope of the reporting, which is exploration and production (upstream). How the reporting have been polluted by numbers from transportation, refining and processing, and marketing and trading we do not understand. The figure shows that Statoil understands the scope of the report.

Civil Society and others have waited many years for the first country-by-country reporting in the world. We expect that Statoil will set the gold standard for how to do this. Statoil should do this, and Statoil can do this. But then Statoil need to publish a new country-by-country report with the correct numbers. Publish What You Pay Norway has in the table below tried to distinguish upstream information from the total numbers in the country-by-country report using information from the company's annual report (!). This is what Publish What You Norway found (exchange rate 2014 USD / NOK = 6.304116):

What we can read on the basis of this table is that Statoil would have created very good results for the resource rich countries if they were able to reach upstream revenues of $ 136.87 per boe (oil equivalent).

But that is not the case, and this is due to two factors:
(1) Statoil sells a lot of gas in Norway, the US and elsewhere, and thus the expectation is that the realized price per boe should be significantly lower than the Brent oil price. Publish What You Pay Norway's analysis above shows that the realized price upstream is $ 66.90 in Norway and an average of $ 49.82 internationally. (But it is impossible to check that country-by-country before Statoil has published a correct country-by-country report)

ABC for CBC reporting	Revenues (mill NOK) A	Production volume (mill BOE) B	Revenue per BOE (USD) (A / B) / 6,304116 = C
Upstream Norway	182200	432,0	$ 66,90 per boe
Upstream international	85.200	271,3	$ 49,82 per boe
Downstream	339.450		
Total	606.850	703,3	$ 136,87 per boe
Brent oil price 2014 as per Statoil			$ 98,90 per boe
Brent oil price 2014 as per external sources (EIA and Statista)			$ 99,02 per boe

(2) Downstream figures have been allowed to contaminate the upstream country-by-country reporting.
It is positive that Statoil has made a comprehensive report and also added an independent, but limited assurance report. But even if the assurance report is limited it should have captured the above problems. The issue, and the fact that PWYP Norway has used financial statements to correct the error at the overall level, shows that this is financial figures and belong in notes to the financial statements. It should have been covered by the quality control of the external audit of the financial statements.

Transparency Agreement
- A tool for multinational transactions

How to expand and fix the toolbox used by tax administrations

A recurring problem in the global market is a number of asymmetries between the multinational companies and the host countries. In this report, Publish What You Pay Norway, gives a complete overview of transparency initiatives in the world today, and introduces a less known transparency instrument- The Transparency Agreement – which is a unilateral contractual arrangement between a company and a government, whereby the company guarantees that in exchange for its "license to operate" within a country, it will be transparent when the authorities wants insight.

THE PROBLEM

PWYP Norway's main focus is to ensure that extended country-by-country reporting (CBC) is legislated in as many countries as possible, to enhance the public oversight of extractive industries by investors, governments, media and civil society. The extended CBC reporting is a simple, low-cost and effective tool to get broad insight into multinationals.

However, one institution has deeper needs for insight into multinational companies and their transactions than the rest of society, and this is the tax administration. The reason is that the tax administration is the institution that is responsible for assessing the correct tax base and collecting the taxes from the multinational's representative company in the country. Tax administrations have limited insight and ability to follow transactions through the value chain within multinationals.

Automatic Exchanges of Information (AEOIs) has been promoted as a solution, but this instrument is mostly effective for individual tax payers with bank accounts in tax havens. AEIOs are ineffective at giving tax administrations the insight into the chain of transactions that occur within a multinational.

THE CONSEQUENCES

The consequence of tax administrations not having insight into the full chain of transactions of multinational companies, particularly multinational companies within extractive industries, is that the tax administrations lack the proper information to do a correct assessment. The reason is that the tax administrations only are looking at a very small part of the value chain, the part that occurs within the country where the tax administration has jurisdiction. The court system in the country is facing the same problem when a tax case is brought to the court by a company.

The result is that tax administrations and courts of law lack the insight to distinguish a tax scam from a bona fide transaction. This may have two consequences: (1) tax scams are not discovered and reassessed, leading to taxes that are too low taxes; and (2) bona fide transactions may incorrectly be assessed as tax scams.

A SOLUTION

One very low-cost, simple and effective solution is to give the tax administration (and thus also the court system) the necessary insight into the chain of transactions that occurs within a multinational company. It is important that this insight is based on sampling, so that the burden on the company does not become too high while retaining the intention of the instrument – to give insight into the full chain of transactions within a multinational company.

The transparency agreement (or guarantee) has been designed to give tax administrations insight on a sampling basis into the chains of transactions within multinationals. In order for it to work, a transparency agreement or guarantee has to be demanded, either by law or by model agreement, before a multinational is given a licence to operate or establish a presence within a country. Failure to agree to be open and transparent – on a sampling basis, shows a non-cooperative behaviour.

Q&A

Does PWYP Norway promote the transparency agreement?

PWYP Norway has investigated and found that a transparency agreement would be a good idea for tax administrations, but we do not promote it as such. Countries and tax administrations should be able to assess this to be a good idea by themselves. PWYP Norway 's main concern is to secure the release of the public, which is why PWYP Norway promotes extended CBC reporting.

The Ministry has stated that the purpose of the bill is to draw a line between the lawyers' duty of confidentiality and the tax authorities' right to information about income and wealth that is important for tax estimation. You can read more about the draft bill and the different consultative statements from relevant actors at the Government's webpages: www.regjeringen.no.

Is it dangerous for a country to demand a transparency agreement from multinational companies?

No, it is not dangerous, but it may be that some multinational companies will say no to entering the country if they have to sign on to a transparency agreement. However, a country needs to think through whether that multinational company is the one that it would invite into the country, or whether it is better to invite those that are willing to sign the transparency agreement.

Why is the transparency agreement not public, but only for tax administrations? Because the transparency agreement allows insight into individual documents, and these are regarded as private papers only relevant for the company itself, and the tax administration that is going to assess the company.

Why should I read this report?

Most people think tax administrations have too much information about personal tax payers. They would be shocked to know how little tax administrations know about multinational companies. This is why you should read this report.

"All sensible politicians favor growth, just as we all favor sound public finances. Both can be achieved if we rationalize spending, invest available resources wisely, and clamp down on tax evasion," says Victor Ponta, Romanian jurist and politician who was confronted with allegations of money laundering, tax evasion and conflict of interest in 2015.

Protection from derivative abuse

In the report "Protection from derivative abuse", Publish What You Pay Norway reveals the harmful use of the financial instrument called derivatives in the extractive industries.

THE PROBLEM

Today, trade with non-renewable natural resources like oil or minerals does not have to be connected to the physical and geographical extraction of them. Rather, much of today's trade is made through the use of financial instruments. Some of the most complicated financial instruments are derivatives, which are used extensively by companies in the extractive industries. The use is legal and can have positive effects. Unfortunately, derivatives can also be abused in order to move capital across countries and thereby evade tax. Most often these instruments are used for the companies' own benefit and at the expense of poor host countries where the resources are being extracted. By using derivatives, companies can transfer revenues out of the host countries before the revenues are taxed. This harmful use of the financial instrument of derivatives has up until now been underexposed. Yet, to illustrate the size of the problem, the global value behind all derivatives was more than ten times the world's gross domestic product in 2011.

THE CONSEQUENCES

The well-known investor Warren Buffet has termed derivatives as "financial weapons of mass destruction" that can harm the whole economic system. Extractive companies' abuse of derivatives harms both rich and poor countries. Derivatives are used to transfer untaxed money out of host countries (where the companies extract resources) and keep this money circulating within a multinational corporation without taxation, or without taking the money back to the home country (parent company jurisdiction). Poor developing countries are particularly vulnerable to this abuse: Tax revenues from the extraction of their natural resources might be the only financial basis of such a size that it can help fight poverty. Tax evasion, made possible by amongst other abuse of derivatives, taps host countries of their legitimate and strongly needed resources. Furthermore, few developing countries have the resources or capacity to uncover abuse of derivatives, as they are very complicated instruments. Lack of transparency in the extractive industries makes this task even more difficult.

A SOLUTION

PWYP Norway outlines an effective policy proposal to hinder the abuse of derivatives and their harmful consequences: Countries can single out derivatives in a separate tax base. We call this "the separation method". The companies' income from derivative activities would thus be taxed separately from their income from extractive activities. This means that gains are taxed based on the general tax rate in the country, and losses can be used against current gains or carried forward and taken against future gains. This would limit the abuse of derivatives for transferring un-taxed funds from poor countries.

The method can be implemented unilaterally and is in line with how most countries have set up their tax systems, and with legislative systems in general. It fixes the market failure created by derivative abuse; while at the same time it does not discourage the proper use of these instruments.

Q&A

What is a derivative?

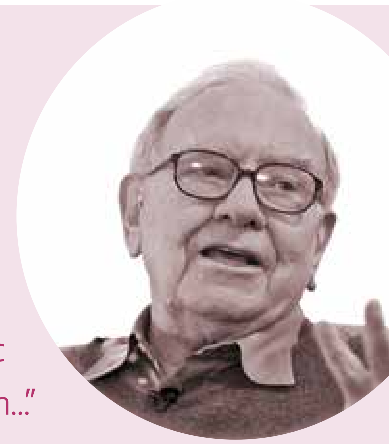
A derivative is a financial instrument that allows speculation on the future price of a product - without buying the actual product. The price is linked to the market place the product is derived from, but there is no physical delivery to back the transactions, only settlement of derivative contracts. A derivative has thus no value of its own.

How does it work?

Derivatives (like futures, options and swaps) were developed to allow investors "hedge" risks in financial markets - in effect buy insurance against market movements. Used correctly, hedging is a good instrument for securing profits in an uncertain world. Yet derivatives are unfortunately also an ideal instrument to move large amounts of pretax earnings from one tax jurisdiction to another. By entering into opposite derivative instruments at the "wrong" timing, it is possible for companies to create huge losses in jurisdictions with high tax, and equivalent profits in jurisdictions with low tax - thus being able to transfer huge amounts of untaxed funds legally out of a country.

"Derivatives are financial weapons of mass destruction that can harm the whole economic system..."

- Warren Buffet.



Lost billions.

Transfer pricing in the extractive industries

In the report "Lost Billions. Transfer pricing in the extractive industries", Publish What You Pay Norway investigates the potential trade mispricing in imports of crude oil in the European Union (EU) and the United States (US) between 2000 and 2010.

THE PROBLEM

The report finds that at least 110 billion US dollars have "disappeared" during import of crude oil to the EU and the US during 2000-2010. To understand how and why, we need to look closer at "transfer pricing" – which happens when two related companies trade with each other and set a price for this transaction. This is not in itself abusive or illegal. But it becomes so when the price is deliberately set too high or low in order to avoid paying taxes or to shift profits across borders. This is called transfer mispricing. Today, over 60% of world trade is taking place within multinational companies. Transfer mispricing is one of the most used techniques for extractive companies to transfer profits from host and home country to the company itself.

THE CONSEQUENCES

Transfer mispricing minimizes the overall tax bill for the company, and helps the company move much of its profits to tax havens with low or zero taxes. As a result, tax dollars that should accrue to tax authorities in the home and host countries, are converted into higher profits for the multinational company. It is nearly impossible for national tax authorities to determine whether they are collecting their fair share of taxes. Developing countries in particular often lack access to the necessary information, as well as the capacity to verify the prices set by companies and their related entities outside their own jurisdictions. This is even more difficult, if not impossible, when entities are located in secrecy jurisdictions or tax havens, where company accounts are not required or available.

A SOLUTION

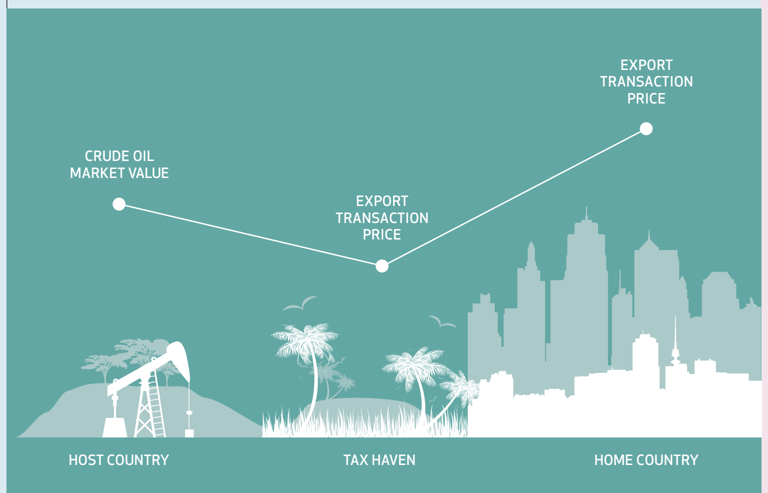
To avoid abusive transfer mispricing, the OECD suggests the use of the principles of "arm's length prices". This implies that companies should set prices as if they traded with a company outside the company structure. However, there is no mechanism in place today to ensure that companies really do this. PWYP Norway has proposed one very simple and effective reporting mechanism called "An extended country by country reporting standard for the extractive industries". It will not directly target transfer pricing, but it is a significant step in the right direction of getting necessary information about key accounting figures and the distribution of these between operating countries, tax havens and home-bases. It will allow investors to follow their money and governments to access valuable and standardized information across all jurisdictions where the companies operate. Only through such reporting can governments be certain that they are collecting their fair share of revenues and taxes.

Q&A

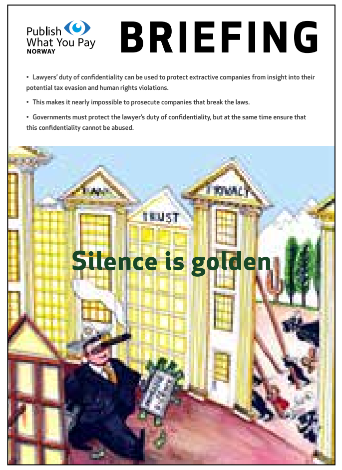
How does transfer mispricing work?

Take for example a company that extracts gold in Tanzania and then processes it and sells it in the United States. The company does this through three subsidiaries: one in Tanzania (host country), one in a tax haven (with zero taxes) and one in the United States (home country). The subsidiary in Tanzania sells the produce to the subsidiary in the tax haven at an artificially low price, creating artificially high profits for the latter. The subsidiary in the tax haven then sells the produce to the subsidiary in the US for a very high price, creating artificially low profits in the US and consequently a lower tax bill. Notice that the intermediary subsidiary has bought at a low price and sold at a high price, and thus created artificially high profits – without any costs. As it is located in a tax haven, it pays no or little taxes on this profit. In this example, the profits are effectively moved to the company itself, while the cost is picked up in Tanzania and the US.

In our report "Piping Profits", we show that ten of the world's most powerful extractive companies operate with at least 6038 subsidiaries, where more than 1/3 are located in secrecy jurisdictions. Consequently, a lot of their trade is within their own corporate structure and the potential for transfer mispricing is great. This report, "Lost Billions", will give you insight into a tax abusive practice that concerns citizens in poor and rich nations alike.



Silence is golden



In the report "Silence is golden", Publish What You Pay Norway sheds light on an unintended and concerning consequence of lawyers' duty to maintain client confidentiality.

THE PROBLEM

To plan and facilitate tax evasion for multinational companies has become a global and lucrative business – and lawyers play an important role in it. This practice is evident in the extractive industries, where many poor, resource-rich countries are tapped for tax revenues from their natural resources. Capital that should accrue to these host countries, or to the home country of the company, is instead moved within the company structure and transferred to tax havens. Companies often use lawyers to structure these transactions. Lawyers have a duty of confidentiality, which obliges them to respect the confidentiality of their clients' affairs. The noble purpose of this principle is to protect an individual's ability to access the justice system, and safeguard rule of law in the society. Yet it is necessary to shed light on the unintended consequence of this confidentiality: companies can use it to claim client confidentiality to protect themselves against government insight into activities, transactions and company structures. It also protects the lawyers from having to disclose their own contributions to tax evasion.

THE CONSEQUENCES

Multinational companies have, with the help of lawyers, built complex corporate structures that make it nearly impossible to prosecute companies for human rights violations, or for illicit tax evasion from both rich and poor countries. The global financial integration has developed much faster than the national governments' capacity to get an overview over the implications for their legislations and economies. Poor countries with non-renewable and finite natural resources are in a particularly vulnerable position. Developing countries are being drained of nearly 1000 billion US dollars each year through illicit financial flows. That equals ten times the value of total international aid to poor countries. Tax evasion from commercial companies constitutes the largest share of illicit financial flows. Complex corporate structures and lack of transparency makes it nearly impossible for tax authorities to prosecute the companies.

A SOLUTION

Lawyers' duty of confidentiality is vital, noble and necessary for a free and civilized society. Yet it is important to separate lawyers' passive protection of clients, from active contribution to crimes like illicit tax evasion. Publish What You Pay Norway sees no contradiction in seeking to protect the lawyers' duty of confidentiality on the one hand, and at the same time ensure that this confidentiality cannot be abused. It is vital to make this distinction, as the abuse of the privilege of confidentiality can undermine the privilege itself. One potential solution is to remove the duty of confidentiality on a specific and limited area concerning client accounts, in order to ensure tax authorities' ability to access and collect their fair share of tax and revenues. This possibility has been discussed in Norway and is supported by PWYP Norway.

Q&A

Will Norway lead the way?

In January 2012, the Norwegian Ministry of Finance published a draft bill proposing an exception from lawyers' duty of confidentiality in the tax area. The proposal involves new provisions of the Assessment Act and the VAT Act, which will oblige lawyers to provide information on deposits and debt, money transfers and other balances on clients' bank accounts and other accounts in the lawyer's name. This obligation will also apply to others who have a statutory duty of confidentiality regarding such information. The backdrop is a Supreme Court ruling from 2010, which concluded that the names of clients who transfer money through lawyers' client accounts should be kept secret.
The Ministry has stated that the purpose of the bill is to draw a line between the lawyers' duty of confidentiality and the tax authorities' right to information about income and wealth that is important for tax estimation. You can read more about the draft bill and the different consultative statements from relevant actors at the Government's webpages: www.regjeringen.no.

"The essential purpose of the global shadow financial system is the shift of money from poor to rich. This is about getting rich secretly and not having to account for such riches locally",
writes Raymond Baker, Director of the think-tank Global Financial Integrity (taken from another of our reports, "Piping Profits")

6 What can young people do to make financial transparency possible?

Volunteers from KFUK-KFUM Global has this spring travelled around to tell about the importance of financial secrecy to youth all over Norway. Photo: Iselin Marøy

Young people are an important force of change in the world. Several times, history has proven that when young people mobilise, they can accomplish extraordinary things and change unjust structures. The abolishment of slavery and apartheid are examples of big changes that would not have happened without global movements of young people.

Today, the world is facing new challenges. Poverty and climate change are challenges that are causing human suffering. 1–2 billion people live in extreme poverty and are not able to live their life to its fullest potential. Financial secrecy is one of the main causes of poverty and increasing inequality in the world. Illicit capital flows drain resources from people who need it the most and are making the challenge of poverty and inequality more severe.

However, there is good news! Illicit capital flows happen because of politics. It is because of the systems being built that companies and individuals are able to evade tax and drain money away from important development. This is good news because we can change politics!

This is why KFUK-KFUM Global is working to mobilise young people to influence decision-makers. Through KFUK-KFUM Global, young volunteers are coming together to work against financial secrecy in order to stop poverty. During the spring of 2015, they worked to influence the negotiations on financing for development in the UN. Through campaigns, meetings with politicians, inputs to the foreign ministry in Norway, and workshops, they have communicated the importance of changing legislation to fight secrecy. Volunteers have spoken to young people all over Norway in order to get more people involved in the fight against injustice. They have met the prime minister of Norway and told her to remember the importance of fighting poverty in top-level meetings that she is attending internationally. Our volunteers have challenged youth politicians to get involved in fighting financial secrecy. This work is important. Only by mobilising the force of change that young people all over the world represent, we can change the unjust structures that are causing poverty and inequality.

You can find out more about how to become part of KFUK-KFUM Global's voluntary network at www.kmglobal.no or by sending an email to global@kfuk-kfum.no.

KFUK-KFUM Global is a member organisation of PWYP Norway.

How can young people fight financial secrecy?

Ingebrikt Kvam (25 years old)

Member of the political committee of debt and capital flight, Changemaker

How are you engaged in the fight against financial secrecy?

I am engaged by volunteering for Changemaker. This is important to me because financial secrecy permits capital flight, and it affects the weakest in the society. Poor countries loose big incomes because of the tax cheating from multinational companies. This affects the poorest people, who lose their opportunity to go to school and have good health care.

Why is it important to be involved in the fight against financial secrecy?

It needs a lot of effort to fight selfishness. According to my experience there are strong forces in the financial sector that are fighting for secrecy. Therefore it is important that a lot of people work for transparency. Huge amount of money disappear from developing countries every year, therefore it is important to stop the capital flight.

Iselin V. Marøy (23 years old)

Participant Young Peace Performers, KFUK-KFUM Global

How are you engaged in the fight against financial secrecy?

I have been part of Young Peace Performers the last year, which is an exchange programme run by KFUK-KFUM Global. We have worked a lot with illegal capital flight. It is very clear that we need more transparency around companies and tax, and it is important that we can share information and have discussions about this topic. I was in Addis Ababa in July, as a representative for KFUK-KFUM Global. There I took part in the Financing for Development negotiations. We fought to get an agreement for more transparency and more attention to illegal capital flight.

Why is it important to be involved in the fight against financial secrecy?

Financial secrecy makes bigger gaps in the world, especially in developing countries. We cannot accept this. If you want more justice in the world, you have to fight for greater transparency regarding companies´ activities and work against illegal capital flight.

Martin Giset (25 years old)

Leader of Follo/NMBU, Attac

How are you engaged in the fight against financial secrecy?

Through our work in Attac we have figured out that known and "beloved" Norwegian companies as Freia, Statoil and ISS use tax havens. We have used the result to create consciousness about the problem. We wanted that self-proclaimed "tax haven free zones" should require transparency of companies in the bidding process.

Why is it important to be involved in the fight against financial secrecy?

Big multinational companies and the "economic elite" are today enjoying the secrecy that is offered by tax havens. They are avoiding tax and hiding corruption. To build a more democratic and justice world we need to put the spotlight on the "black holes in the world economy".

Which small steps can you take to fight financial secrecy?

The following are three different steps you can take to help fight financial secrecy:

Representatives from civil society in the South demanded financial transparency when they were in Norway to participate in PWYP Norway's capacity building program in 2014. Photo: Eline Helledal

1) **Spread the message on social media:**
- Participate in the fight against financial secrecy on social media. Follow PWYP Norway on social media, participate in the debate, and sign up for PWYP Norway's newsletter on the webpage: www.pwyp.no.
- Invite your friends to take part in the debate on social media and share posts and tweets.

2) **Become a volunteer:**
- Contact an organisation for which you want to volunteer. Your voice, time, and energy are crucial for the fight against financial secrecy!
- Take part in a political committee or a local group in your organization that focuses on the fight against financial secrecy.

3) **Talk about it:**
- Tell your friends why it is important to fight financial secrecy. PWYP Norway has developed material that can be used to present the facts to your friends or your organization. Go to www.pwyp.no to find the material or send an email to post@pwyp.no
- Write an opinion piece in the local newspaper on why it is important to fight financial secrecy. Contact post@pwyp.no for support in contacting the newspaper and writing the text.

If you have any questions about how you can get engaged, please send an email to **post@pwyp.no.**

HELP US CONTINUE OUR WORK:

Do you think our work is important?
Do you want to see financial transparency and accountability in the extractive industries?

You can support PWYP NORWAY by sending a text message

Text PWYPNORWAY to 09316
followed by (donation amount)
e.g. pwypnorway 500
(donations in NOK, international users must use +47 417 16 016)

YOUR SUPPORT MAKES OUR WORK POSSIBLE

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PWYP Norway is the Norwegian chapter in a network of 800 organisations from more than 70 countries worldwide. We work for financial transparency in the extractive industry to promote sustainable societies.

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