

Offshore Financial Centers and Tax Evasion in World Bank Operations

The World Bank Group (WBG) is committed to the integrity and transparency of global markets, and shares international concerns, including those expressed by the G20, about illegal financial practices that undermine such integrity and transparency. In the pursuit of its development mandate, the WBG is concerned about the issue of offshore financial centers (OFCs) and about the potential risk of tax abuse and the threat to good governance that they present.

The WBG addresses the issue of OFCs and tax evasion in its engagement with its member countries and in coordination with other international organizations and civil society. The key avenues for this engagement are support for strengthening tax systems and domestic resource mobilization and due diligence in private sector investment operations.

Strengthening tax systems and anti-corruption efforts in developing countries is at the center of the WBG's strategy for curbing tax evasion and appropriate use of public resources. This is now being expanded to include support for countries to meet the internationally agreed standard for tax transparency, which enables them effectively to participate in international efforts to combat illegal tax practices.

Tax evasion is unacceptable in any part of a transaction in which the World Bank Group is involved. Therefore, the WBG exercises due diligence to confirm that the structures in which it invests are chosen for legitimate reasons and are not being used for tax evasion, tax abuse, or other illegitimate purposes.

Support for tax systems and anti-corruption

The development impact of the WBG investments cannot be attained if client countries fail to receive adequate tax revenues for delivering essential services or allow unequal treatment of taxpayers. The WBG traditionally supports countries in establishing effective tax administrations which are transparent and which apply tax laws evenly and fairly. This support focuses on the removal of discretionary fiscal incentives which attract firms wishing to evade or avoid tax liabilities and on streamlining tax administration procedures and practices. The WBG also helps client countries to enhance transparency and integrity in their tax systems and strengthen control and tax enforcement mechanisms. The WBG coordinates its technical assistance for tax issues with other international organizations, such as the IMF and OECD, including through the OECD-led Global Forum on Transparency and Exchange of Information.

The WBG is also committed to the notion that, once tax revenues are collected, they must be employed properly, and not for the personal benefits of political or other government leaders or other corrupt purposes. The WBG's wide-ranging efforts to combat corruption include the joint UN-WBG Stolen Asset Recovery (StAR) Initiative, which seeks the timely return of assets stolen by acts of public corruption. This and other WBG programs are directed at maximizing the proper use of government revenues, by stigmatizing and penalizing corrupt practices.

Most recently, the WBG has provided assistance to several Caribbean jurisdictions in the negotiation of tax treaties that meet the OECD's internationally agreed standard for tax transparency. Efforts are also underway elsewhere in the Bank to help countries meet their commitments under the internationally agreed tax standard.

Due diligence in private sector investment operations

Private sector projects in which the WBG invests through the IFC and MIGA should be subject to appropriate and transparent taxation by host countries. Similarly, sponsor home countries need to be able to collect proper taxes, and sponsors must comply with their obligations to report income arising out of the proceeds from any project. Strengthened safeguards have now been put in place with the goal of ensuring that this is the case.

The involvement of offshore financial centers in transactions backed by IFC and MIGA may be for legitimate purposes when partners and sponsors act with integrity. For example, jurisdictions may be used to avoid double taxation of investments in developing countries, or may provide legal infrastructure that a given host country lacks. However, a lack of transparency and inability to exchange information on the part of some jurisdictions can provide an environment that facilitates cross-border tax evasion, fraud, money laundering, and other illegal activities. To address these issues, IFC and MIGA apply heightened scrutiny of projects involving off-shore financial centers, in order to assess the legitimacy of the proposed structures.

Before making any investment, IFC and MIGA carry out broad due diligence, including integrity due diligence on the sponsors and principals, to ensure that the project meets all WBG standards in a number of areas, including social and environmental, anti-money laundering and combating the financing of terrorism, anti-corruption, corporate governance and tax transparency. Such broad due diligence has long been standard for WBG private sector projects.

IFC and MIGA now also apply heightened due diligence to all transactions involving any intermediate jurisdiction (that is, the jurisdiction of organization of an investee company in a proposed transaction which is other than the project country or the jurisdiction of the principal sponsor or shareholder), including OFCs. The structure of the proposed transaction is examined carefully, including the domicile of the investee company, to ensure that the structure has been chosen for legitimate reasons and is not being used for tax evasion, tax abuse, or other illegitimate purpose. In performing its due diligence, IFC and MIGA look at many factors, which may include the fiscal benefit of the project to the host country; the effect of tax treaties and withholding regimes; the context of applicable tax laws and any regulatory framework; and the transparency of the jurisdictions involved with reference to the OECD's internationally agreed tax standard. As is the case with World Bank Group standards in other areas, specific measures may be required to mitigate any potential risks of tax abuse in a particular structure, such as requiring representations and covenants of tax compliance from sponsors, or requiring a change of domicile in the structure, where appropriate. When presenting a new investment transaction for approval to the WBG's Executive Board, IFC and MIGA disclose the structure of each transaction involving an OFC and provide an assessment of the structure.

The Way Forward

The WBG would like to acknowledge the valuable input and guidance provided by members of its Board of Directors and external stakeholders, and will continue to monitor international developments in this area and engage with stakeholders concerned about this issue. The WBG will be discussing with its Board of Directors within the coming months additional ways to strengthen internal safeguards against tax evasion and tax abuse, in furtherance of its commitment to the integrity and transparency of global markets and its developmental mandate.