Forum: Legal Committee

Issue: Addressing tax evasion and profit shifting practices in multinational corporations

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Introduction

Tax evasion is also referred to as avoiding paying taxes, an illegal activity. Those who are caught evading taxes are commonly sentenced for criminal charges and substantial penalties. Tax evasion consists of two parts, one which is nonpayment of tax or underpayment of tax which is both illegal. For example, by declaring less income or by overstating deductions. In simpler terms tax evasion is the action of avoiding paying tax by not following the law. Profit shifting is the action when companies or other businesses avoid paying taxes or minimize the tax payment.

Definition of Key Terms

Tax avoidance: An action taken to lessen tax liability and maximize after tax income. This process also includes minimizing tax liability within the boundaries of the law.

Tax evasion: A variety of practices including manipulation of financial records and evading rightful tax obligations.

Underground economy: This economy is referred to illegal transactions which may not follow the government's law, or the trade is unlawful.

Tax: A certain amount of money that is paid to the government regarding your income state.

Tax outflow: Tax outflow is when money is spent on fixed assets, salaries etc.

Profit shifting: Is a technique that involves companies paying less tax than they should

Tax Haven: A country or area where tax rates are at a low rate

Tax jurisdiction: Tax jurisdictions are building block of your company they determine which rules and policies you must follow.

Money Laundering: Disguising financial assets so that they can be used without detection of illegal activity that produces them.

Background Information

What qualifies tax evasion?

Tax evasion involves numerous deceptive illegal activities regarding the manipulation of financial records and evading tax obligations.

A) Hiding income

Hiding income is a fundamental form of tax evasion where individuals or businesses concealing sources from the government, or the tax authorizes. This can include unreported cash transactions, underreported sales or illegal activities. By keeping income hidden, evaders ensure the tax authorities are unaware of the income and outcomes of the accounts.

B) Inaccurate financial statement

Inaccurate financial statements are a serious offense where individuals or companies manipulate accounting records to understate their expenses. By representing misleading information which leads to the advantage of the company or individual to lower their tax payments.

C) Creating fake deductions

Creating fake deductions or simply faking events or charities for the company to generate receipts regarding the event or payment record, which leads to artificially lowering their taxable income. This action aims to lower tax liability, allowing companies to keep their income unlawfully (illegally).

D) Expanded expenses

This is when companies or individuals exaggerate the legitimate business costs such as supplies, salaries or other expenses to reduce taxable income. In summary, when companies expand their expenses, they are essentially lowering the profits on paper therefore avoiding tax payments. Regarding these actions the government has financial setbacks and the companies or business have an edge in the market.

E) Using small companies to hide assets

Also referred to as shell companies means that these businesses nearly have no active business operations. Which leads to taking advantage of the company by moving their money throughout them to hide who owns certain assets. For example, using offshore accounts or complicated transactions can lead to tax authorities having a hardship being able to locate the location of the account which can cause the companies to go unrecognizable with no trace. This action is usually related to money laundering schemes.

Types of tax evasion

A) Evasion of evaluation

In this method tax evaders knowingly file false reports concealing income and making illegitimate guesses. This action results in an inaccurate tax assessment. Generally, tax evaders can go as far as transferring taxable assets in their books to mislead the International Revenue System (IRS).

B) Evasion of payment

Evasion of payment occurs when business or individuals hide their assets in family member accounts or foreign institutions. If the business or individual deliberately evades paying taxes which can lead to money charges or depending on the severeness of the chase they may end up in jail.

Differences between tax avoidance and tax evasion

While tax evasion and tax avoidance involve efforts to minimize tax payments, they are opposite from each other.Here are key distinctions:

Legality: Tax evasion is illegal and consist of misrepresenting tax authorities whereas tax avoidance operates within the legal frameworks, using methods to minimize tax liability

Transparency: Tax avoidance involves the use of legitimate tax reliefs and allowances and is also transparent when in process in contrast tax evasion is dishonest tactics like false information on reports.

Penalties: Tax evasion can lead to prison or can be charged with severe penalties whereas tax avoidance doesn't charge penalties, but the case may vary depending on the individual and the crime which in conclusion officers may have the right to charge the suspect.

Ethics: Tax avoidance is often seen as a smart intellectual planning thought from time to time it can raise ethical questions, when in fact Tax evasion is condemned to be fraud.

Impact on public finance: While tax avoidance is legal, overuse of high earns or shares can strain governments finance, like tax evasion, by minimizing the tax base needed to fund public support, business or services.

Tax evasion and money laundering

Tax evasion and money laundering are combined with the world of crime. The reason for this is when tax evaders often turn money laundering technics make their illegally earned money to seem as though it is legal. These actions can lead to even more severe damage such as sharing large amounts of money into smaller accounts to go undetected, or these individuals may go as far as creating fake websites to earn the money and transfer it to offshore accounts. The alliance between tax evasion and money laundering presents a substantial hardship for law enforcement.

Global offshore accounts

The action of activating an offshore account outside of your country isn't illegal, however it might depend on the bank you are working with. Although individuals who tend to open an offshore account to simply not pay tax is when the action is illegal. The foreign account tax compliance act (FACTA) helps monitor offshore and onshore bank balances so that they can identify any illegal activity. Recently the office on drugs and crimes estimates around 2-5% of global GDP which is around 2 trillion us dollars on money laundering. In conclusion some countries may not comply with clients having offshore bank accounts, this varies from country's policies.

How does profit shifting occur

Profit shifting occurs when the tax rate in two or more countries differs which leads companies to profit shift. Business will likely shift profits generated by Internet protocol (IP) to lower tax jurisdictions. The most common method for shifting profit is for a multinational corporation to use a subsidiary it has in a tax haven to charge cost to the individuals it has in other countries. Multinational countries are estimated to shift $1.38 trillion worth of profit into tax havens every year, costing countries $245 billion in lost corporate tax every year.

Major Countries and Organizations Involved

The United States of America

The United States holds the world's highest percentage for tax evasion. President Biden had made an announcement regarding the tax evasion rates to be equal throughout the company's income and outcomes. The USA has also tax avoidance and tax evasion departments that only specialize in criminal activities. Such as the

Internal revenue service (IRS)is a Breau of department of the treasury and iso one of the most efficient tax administrators. Also to bring justice to the individuals of the government regarding the topic of tax or tax related cases is generally discussed in United states department of justice. The United States sentencing committee has also played an important role in making decision regarding tax fraud. Regarding the seriousness of the tax related topics, if turned internationally the FBI will be on the case. In conclusion, the USA government is trying to decrease tax-related crime.

India

14;597 cases were found regarding tax related issues throughout April to December in 2023. India losses around 10.3 billion every year due to tax invaders. Which is why India is cooperating with organizations business and other organization in order to minimize tax evasion in the country. Some of the organization in the country are the Indian revenue service (IRS). The citizens of the country can also report any kind of tax evasion through filling out a form online.

Netherlands

"Every year, governments would miss out on up to €427 billion due to tax avoidance. However, Kavelaar's doubts whether that amount is correct. 'The researchers assume commercial profits. However, taxes are calculated on the fiscal profit. That is a lot lower and therefore gives quite a distorted picture,' the professor said. Still, he believes companies and individuals are still evading too much tax." The organization willing to monitor and help develop tax Evison in the country are the fiscal information and investigation service (FIOD)

France

France has a high percentage in terms of tax it ranked the first out of 38 OECD countries in 2022. This according to French news reports the reason the taxes are higher is because the French benefit from services that have a higher quality then other country. The penalty system in France for tax evasion can start from 500.000 euros or you can be fined to go to jail for 5 years. The French also have specialized agencies that keep track of tax related activities such as the council of France or the European parliament which keeps updated on the headlines.

Luxembourg

The average single worker faces 32.1% tax rate in 2022 whereas the OECD average is 24.6%" In response to the tax-related CSR, Luxembourg's recovery plan included the adoption of a law prohibiting the making of corporate tax deductions based on interest and royalty payments (outbound payments) to related undertakings located in countries on the EU list of non-cooperative jurisdictions for tax purposes;

This law came into force in March 2021. According to the plan, this law would be subjected to an impact assessment that would inform a discussion on the possible extension of the law's scope towards jurisdictions other than those on the EU list. Furthermore, Luxembourg underlined its willingness to participate constructively in the discussions on the OECD's international corporate tax reform and upcoming EU initiatives such as BE-FIT (Businesses in Europe – Framework for Income Taxation".

Timeline of Events

The timeline of events regarding tax started throughout the Middle Ages. However, the chart below will indicate the most recent events of tax related topics.

Date	Description of event
Tijuana,2006	**The individuals voted on paying their taxes in an oversize account to protest the inability the government had to provide adequate security.**

Delhi lawyers,2009	The lawyers in India went on strike regarding the government wanting more money to cover legal services
Protest against European austerity	Some governments raised taxes to bring down the government's budget and satisfy international creditors. No table of contents entries found.
Spanish autonomists,2012	This event redirected taxes from Spanish government to locally organized projects.
Madagascar,2013	Business in Madagascar refused to pay taxes to the government, depositing their money in an offshore account which contained the government's money.
Apatzingan,2014	Finding the government wasn't giving business protection they stopped paying taxes.

Relevant UN Resolutions and Other Documents

1996	G7 makes the problems of tax evasion and avoidance a priority
1998	OECD report on harmful tax competition an emergency global issue
2000-2007	Development on international standards on tax transparency and securing commitments to a global level

2008-2009	**G20 pledged to end bank secrecy and establish the global forum on transparency and exchange of information of the economy**
July 2013	**G20 identifies tax avoidance as priority**
October 2015	**Adoption of the base erosion and profit shifting package of 15 actions to counter tax avoidance**
June 2016	**Establishment of the OECD/G20 inclusive framework on BEPS now 140 members**
2017-2020	**Activate discussion in the inclusive framework on how to address the tax challenges on the deglaciation of the economy cumulating with the release of blueprints for a two-pillar solution in October 2020**
July 2021	**Over 130 countries and jurisdictions join the statement on the two-pillar solution to address the tax challenges arising from the deglaciation of the economy**
October 2021	**136 members of the inclusive framework join the statement on the two-pillar solution to address the tax challenges arising from the deglaciation of the economy with a detailed implementation plan**
2022	**Target dates for development of model legislation, a multilateral convention and a multilateral instrument for the two-pillar solution**
2023	**Target date for implementation of the two-pillar solution**

Possible Solutions

"Where tax crime is facilitated by technology, a technology response is needed. The most common counter-suppression tool used to address electronic sales suppression is data recording technology. This tool records and secures the sales data immediately as the transaction occurs and stores it in a manner that means it is tamper proof. This means it cannot be manipulated by phantom ware or zappers, or if tampering has occurred, it is traceable and detectable. The data should be stored securely and preserved even if there is loss of power. There are different types of tools that are being used to perform this function, which are referred to in different countries and by different service providers as a fiscal control unit, electronic fiscal device, fiscal memory device, sales data controller or sales recording module. This type of technology should be able to be used in any type of cash register, such as traditional electronic cash registers (ECRs), computer-based point of sales systems, or those that are tablet or smartphone-based. Different solutions are available which can either be included as an integrated part of a cash register, or as an add-on installed with an existing cash register. As an additional feature, these types of tools are also being used to send data automatically to the tax authority, connecting cash registers online to their data server systems. This can occur either in real time or in bulk scheduled transfers, such as at the end of the day or each month. The tax authority then has the opportunity to access the data remotely for compliance and audit purposes."

Laws to prevent tax evasion

"Government agencies play a pivotal role in enforcing tax laws and ensuring compliance. The IRS in the U.S. and in India, the Income Tax Department, are key in this effort.

Income Tax Act 1961: This act in India is a comprehensive legal framework for tax collection. It includes various sections, like Section 139, which mandates accurate income declaration in tax returns.

Enforcing Accurate Income Declaration: Agencies ensure that all income, whether from a regular salary or investments in tax shelters, is correctly declared. This helps in identifying and preventing tax evasion.

Audit and Compliance: Regular tax audits is conducted to ensure compliance with financial regulations. These audits help detect any illicit financial flows or fiscal fraud.

Combating Evasion Tactics: Agencies focus on uncovering common methods of tax evasion, such as concealing income, using offshore accounts, or engaging in money laundering through shell companies.

Addressing Incorrect Information: Providing false information on income tax returns is a major focus area. This includes misreporting tax-deductible expenses or income sources.

Dealing with Tax Havens and Black Money: Efforts are made to trace funds hidden in tax havens or as black money, ensuring they are brought under the tax net.

Whistleblower Programs: Many agencies encourage whistleblowers to report evasion tactics, playing a crucial role in uncovering complex tax evasion schemes.

Regulating Tax Benefits: While tax benefits are legal, agencies monitor them to prevent their misuse for evading taxes.

Financial Secrecy Laws: Laws are in place to combat financial secrecy, making it harder for individuals and businesses to hide illicit income.

Retirement Account Regulations: Proper use of retirement accounts is monitored to prevent their misuse as a tax evasion method.

Paying the Taxes: Ensuring that all taxpayers, regardless of income source, pay their due taxes is a primary function of these agencies".

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