

Death and taxes: the true toll of tax dodging

A Christian Aid report
May 2008



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We believe in life before death

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Introduction

At a time of switchback stockmarkets and fears of global meltdown, the world economy in 2008 is an uncertain and nervous place. Will more banks collapse? Will the housing market crash? Can recession, or depression, be avoided?

In the world's poorest countries, the concerns are less about lifestyle and more about life and death. What will be the impact on growth in developing economies? Will the hope of a better, and longer, life for poor people be negated?

This debate is increasingly focused on the progress, or otherwise, towards the Millennium Development Goals (MDGs) set by the United Nations, which aim to halve world poverty by 2015. How will the money now be found to realise this ambition?

Christian Aid has concluded that the necessary money, and more, is already available – if only those who owe it would pay up. We are talking about tax. This report seeks to expose the scandal of a global taxation system that allows the world's richest to duck their responsibilities while condemning the poorest to stunted development, even premature death.

This is in part to do with super-rich individuals. It is also to do with governments, including the UK government, who have let this situation develop and persist. But it is mostly about the world's transnational corporations wielding their enormous power to avoid the attentions of the tax man – with devastating results.

The situation is stark and urgent. We predict that illegal, trade-related tax evasion alone will be responsible for some **5.6 million deaths** of young children in the developing world between 2000 and 2015. That is almost 1,000 a day. Half are already dead.

Tax and tax havens received much attention in the early months of 2008. Stories of German bankers salting away cash in Liechtenstein, HM Revenue and Customs pursuing bank accounts in Jersey and UK ‘non doms’ crying foul at having to pay anything, all bubbled away in the media.

Such scrutiny is long overdue. But it doesn’t even scratch the surface of an international industry that has grown up specifically to maximise ‘tax efficiency’ or, in other words, to deny sovereign governments their income. For governments in the developing world, this amounts to being robbed of their ability to improve their economies and the lives of their poorest people.

It is important to clarify what we are talking about here. Most people in Britain, for instance, engage in some level of ‘tax planning’ – be that claiming their various allowances or investing in a tax-free ISA. This activity is entirely legitimate in that it is enacting the intentions of relevant legislation.

Then there is the huge grey area of ‘tax avoidance’, which is legal but has, we maintain, a sliding scale of legitimacy. In the corporate world, avoidance often involves the use of tax havens to shelter and boost profits. This gets increasingly aggressive as ever more ingenious and complex instruments are peddled by the tax industry, with the sole purpose of getting around laws and regulations. Some idea of the size of this activity can be grasped by considering an astonishing fact: **a full 50 per cent** of world trade is reported to take place through tax havens.

The secrecy underpinning this system can also enable illegal activity on the part of criminal individuals and corporations – ‘tax evasion’. Our figures deal with just two of the most common forms of corporate evasion. The first of these is known as ‘transfer mispricing’, where different parts of the companies sell goods or services to each other at manipulated prices. Again, the potential scope of this practice can be seen from the staggering fact that some 60 per cent of all world trade is now thought to take place between global corporations and their subsidiaries. The other, ‘false invoicing’, is where similar transactions take place between unrelated companies.

We calculate, from just these two activities, that the loss of corporate taxes to the developing world is currently running at **US\$160bn a year** (£80bn). That is more than one-and-a-half times the combined aid budgets of the whole rich world – US\$103.7bn in 2007.

We are not suggesting that all of this money would be channelled to priority areas such as health and education. Even at current rates of expenditure, however, the lives and prospects for poor people in the developing world could be transformed. If,

for example, the same proportion of tax revenues were spent on healthcare in these countries as has been since 2000, then the lives of **350,000 children under the age of five** would be saved every year – including 250,000 babies (see Technical appendix page 51).

Between 2000, when the MDGs were set, and 2015 when they are supposed to be realised, the amount lost by these two specific methods will total US\$2.5 trillion. Taking into account additional sums from aggressive tax avoidance and other forms of trade abuse, the total loss is likely to be several times that amount.

Our figures are derived from the work of Raymond Baker, a senior fellow at the US Center for International Policy. To arrive at his findings on transfer mispricing, he and his researchers conducted 550 interviews with heads of trading companies in 11 countries – all on condition of anonymity.

Baker sees corporate tax evasion as part of a global process by which the wealth of the developing world is being steadily shifted to the world’s richest countries. He condemns this as ‘the ugliest chapter in global economic affairs since slavery’.

The World Bank estimates that it would cost US\$40-60bn a year to reach all of the UN’s MDGs, providing that policies and institutions are improved in the developing world. If the missing tax identified here were paid, there would be enough cash to meet this bill several times over.

This report examines the different methods, licit and illicit, through which transnational corporations and other businesses dodge tax in order to pay as little as possible. Lost tax revenue affects all countries, rich and poor, but the impact on the developing world is demonstrably much greater.

We look at the tax havens where the missing money goes, examining their history and the attractions they offer – paramount among which is trading secrecy. We ask how industrialised countries with their much-vaunted regard for the rule of law can have connived in the creation of a fiscal system so open to serious abuse?

And we look at the facilitators – including the giant accountancy firms such as KPMG, PricewaterhouseCoopers, Ernst & Young and Deloitte – who specialise in exploiting the existence of havens to minimise the tax liability of their clients, impervious to the social consequences. All of these ‘big four’ firms have in recent years paid massive sums to settle allegations of lawbreaking or the breaching of financial regulations. And yet they retain their status as the auditors of the world’s financial system.

The case studies in this report show the different impacts that tax dodging by companies can have. In **Zambia** and **Tanzania**, we show how poor deals in the past on copper and gold respectively have left these countries’ exchequers unable to capitalise on the recent huge surges in commodity prices. Yet when they have tried to renegotiate, they find themselves threatened with legal action. A more robust negotiating stance in **Malawi** illustrates how better deals can be reached.

In **India**, the government is giving some of that country’s biggest and richest companies a tax-free ride under the programme of Special Economic Zones, which were designed to bring more foreign investment into the country. Meanwhile, these developments are displacing tens of thousands of poor people – thrown off their land with scant compensation and denied the opportunity even to grow their own food. Life for them is getting worse, not better.

Rapid economic growth in **Peru** is also failing to deliver benefits for that country’s poor people. Preferential tax rates for asparagus producers, supplying most of the UK’s consumption, join those already enjoyed by mining companies. In **Bolivia**, on the other hand, raised royalty rates on gas extraction have enabled better healthcare and care for the elderly.

Britain has a particular responsibility in this situation. Of the 72 tax havens that exist as homes for fugitive money, no fewer than 30 are in Commonwealth countries and Crown Dependencies. Even in the financial hub of the City of London, a range of international initiatives to increase transparency of transactions has been routinely resisted. The International Monetary Fund recently identified the UK itself as a tax haven.

Gordon Brown, the UK prime minister, has consistently championed increases in aid to the developing world. He is committed to the UK reaching one important MDG – that of devoting 0.7 per cent of the country’s GDP to aid – two years early. We applaud this effort, and will be supporting the government to push other nations to fulfil their commitments.

But we also urge Mr Brown to look at another huge, and untapped, source of funds – the tax that companies are artfully avoiding paying around the world. Mr Brown has recruited some very high-profile corporations to help him in his quest to realise the other MDGs. Some of the same companies are named in this report for serial tax dodging.

The case of CDC plc, formally the Commonwealth Development Corporation, is instructive. This company, owned by the Department for International Development (DFID), was set up to channel taxpayers’ money to projects in the developing

world. Its latest accounts show that it made worldwide pre-tax profits of £365m, and yet paid no tax either in Britain or abroad. Many of its 78 subsidiaries are based in tax havens such as Mauritius, Bermuda and the British Virgin Islands.

Indeed, it can be seen that UK taxpayers are effectively subsidising company profits through the aid budget. Companies use their muscle to get the best tax deals possible in developing countries, in some cases with diplomatic pressure from their home countries, including the UK. These same governments then pour tens of millions of pounds of aid into the same countries to support basic services.

Christian Aid is not suggesting that DFID should be cutting back on its aid budget. Quite the opposite. But this money would surely be better used to target the poorest and most marginalised people, with the basics of state provision financed by in-country taxation.

The government of Ireland has in recent years laudably increased its aid budget. Yet at the same time it has adopted many of the characteristics of a tax haven, thus helping to facilitate tax losses in developing countries.

There is much to do if the pernicious global tax system is to be made to work for the world’s poor people, not just the rich. But there is a lot that can be done. Christian Aid calls on the UK and Irish governments to join together in taking a lead in reforming this system and in questioning the assumptions on which it is based. Primarily, they should support international moves to curtail and regulate the secrecy of tax havens, thereby lifting the lid on the tax industry and its machinations.

A common accounting standard should be promoted, to make the hiding of profits impossible by requiring companies to report what they do on a country-by-country basis. The creative abuse of the tax system by accountants, lawyers and bankers should also be challenged. This should be preceded by a thorough assessment of the scale of illicit capital flows, in particular tax evasion, facilitated by banks and corporations operating through the City of London or Dublin. Once identified, illicit wealth from the developing world must be repatriated.

The stakes could not be higher. Again, 1,000 children a day are currently dying in the developing world – denied basic healthcare because their governments in turn are denied their rightful revenues by illegal tax evasion. The full, shameful, picture undoubtedly encompasses millions more.

Secrecy can be used as an excuse for inaction. If we don’t know about something, how can we do anything about it? But now we do know. **So no more secrecy.** And no more excuses.

‘Currently there is both an agency problem – ministerial corruption – and an information asymmetry: companies know better than governments what rights are worth. The consequences are often grotesque... In 2006 the Democratic Republic of Congo received a mere US\$86,000 from mineral rights.’

Paul Collier, professor of economics, Oxford University, and Michael Spence, 2001 Nobel Laureate in economics

Stripping the riches

Gold bullion: a bulwark against financial insecurity, it's also in demand as jewellery for the world's emerging middle classes. In March 2008 it reached a record price of US\$1,000 an ounce



The past decade has seen record prices for commodities caused by rampant demand from fast-growing economies such as China and India.¹ The boom should herald a great future for resource-rich developing countries. They own much of the copper, nickel, platinum and iron ore on which the new economic power houses of the twenty-first century are being built.

They also own large reserves of gold, that most precious of commodities, which is now more valuable than ever as a bulwark against economic uncertainty and a source of jewellery for the world's newly emerging middle classes.²

For decades it has been a common refrain that many developing economies, particularly in Africa, have been static, or even in decline, since colonial times. Their problem is that while they produce the raw materials, all the value-added processing takes place elsewhere. But with the price of nickel rising six fold over the past 10 years,³ platinum five fold,⁴ copper quadrupling in value⁵ and iron ore⁶ and gold trebling⁷, surely things should be changing? Aid donors could be forgiven for thinking that the need for their help will soon start diminishing.

Surely the countries where the minerals are extracted are sharing in their value, not least through taxes and royalties on what is produced? Aren't the proceeds from the boom enough to give countries a chance to alleviate their poverty themselves – and invest in the future with well-funded health programmes and improved education systems?

Unfortunately, the depressing truth is that there is nothing remotely resembling an economic bonanza in many of the countries that should be benefiting from these soaring prices.

That is not because ravenous dictators are siphoning off a fortune while their people starve. Some corruption exists, but the greater culprits by far are those companies from wealthier countries that have been invited in to extract the minerals.

By measures both legal and illegal, these companies have too frequently shown themselves to have just one priority: taking as much wealth as possible from the countries where they operate, while putting as little back in as possible by paying as few taxes as they can.

Their defence is that they have a duty to ensure a maximum return for their owners and shareholders. This may well be justifiable for the legal means used to increase returns but when measured against the suffering they ignore in the process, that reasoning amounts to a new colonialism. Illegal means of increasing returns, however, cannot ever be justified in this way as no company is required to operate illegally. Christian Aid

has estimated that the cost to the developing world in lost tax revenue of just two forms of tax evasion – mispricing transfers and false invoicing – amounts to US\$160bn a year. In one year alone that money at current spending patterns in poor countries could save the lives of 350,000 children under five, 250,000 of them babies.

Extracting the cash

There are numerous ways for the transnational corporations (TNCs) and home-grown businesses in the developing world to avoid tax.

Legitimate ways include:

- using tax-avoidance schemes
- demanding tax concessions
- negotiating low royalty rates on output.

Illicit ways of evading tax in countries of production, which generally involve false accounting, include:

- falsifying invoices
- mispricing the transfer of goods and services
- mispricing financial transfers
- illicit transfers of cash.

Even the legitimate methods, however, may not always be what they seem. Given the rewards to be made, particularly from extracting natural resources such as oil and gold, concessionary rates might have been obtained by bribing corrupt ministers and officials. And some ostensibly legal tax-avoidance schemes have, in recent years, been deemed by revenue authorities to amount to tax evasion, and are therefore illegal.

How poor countries lose out

Many developing countries anxious to bring in big business to develop their natural resources have found themselves in a 'race to the bottom' in terms of offering financial inducements. In virtually every sector where such countries need outside help, be it mineral extraction, agriculture, manufacturing or even tourism, countries will compete with each other in offering to slash taxes, and royalty rates where appropriate, to win the necessary investment. In many cases, they see scant return for their efforts.

George Soros, the global financier and philanthropist, helps fund the Revenue Watch Institute, which promotes 'the responsible management of oil, gas and mineral resources for the public good'. He identifies three key problems facing resource-rich developing countries.

These he calls 'asymmetric information', 'asymmetric

bargaining power’ and ‘asymmetric agency’.⁸ They are common across the board, from tourism to agriculture, from telecommunications to consumer goods. In all cases, the power lies with the rich countries and the poor pay the price. It is in the industries extracting oil and minerals, however, that the asymmetry is perhaps most clearly defined.

‘Asymmetric information’ occurs when TNCs with platoons of lawyers, accountants and other experts arrive in a country to negotiate the tax regime under which they will operate. In the extractive industries, such experts will in many cases know far more about the value of the resources under discussion than the government selling them, and have long experience of devising hugely complicated tax formulas to their advantage.

The country representatives they come up against will be unable to match their knowledge, not least because in many developing countries, those with the requisite ability will in all likelihood be working in the private sector.

‘Asymmetric information’ also refers to the fact that the citizens of resource-rich countries are frequently kept completely in the dark about the deals that their governments have struck with TNCs. In Tanzania for instance, mineral development agreements made with gold companies remain confidential. After one agreement was leaked to the press, Commissioner for Minerals Peter Kafumu warned that possession of the document was ‘illegal’.⁹

In Gabon earlier this year the government temporarily closed down 22 local non-governmental organisations (NGOs), accusing them of interfering in politics after they issued a joint statement criticising the authorities on a range of issues from spending to unemployment.¹⁰ One of their key concerns was the secrecy surrounding a US\$3bn iron-ore mining deal with China’s state-owned National Machinery & Equipment Import & Export Corp in the Belinga mountains of the country’s remote north-east province.

‘We demand immediate publication of the contract... This way, Gabonese will know if their interests are being protected,’ says Marc Ona Essangui, who heads a coalition of environmental groups. He told a news conference it was thought the Chinese consortium had been exempted from all taxes for 25 years.¹¹

‘Asymmetric bargaining power’ today often involves TNCs threatening to take their business elsewhere unless the operating terms offered by the host country are as advantageous as possible – a particularly acute threat in the mining industry before the commodity boom.

‘Asymmetric agency’, meanwhile, rests on the principle that

ownership of natural resources is an attribute of sovereignty. This sovereignty, according to modern political theory, belongs to the people. Government ministers and officials therefore negotiate with foreign oil and mining companies as ‘agents’ of the people, while the managers of the companies act as ‘agents’ of the owners and shareholders. If the ministers and officials accept bribes, however, they clearly abandon any pretence of acting for the people.

‘Asymmetric agency’ may also occur if international institutions advising the governments of developing countries fail to act in the best interests of those countries.

In a 2006 World Bank study of mining royalties in developing countries financed by mining giant BHP Billiton, the governments that were surveyed overwhelmingly opted for royalties based on the quantity of ore mined. Mining investors, however, preferred profit or income-based taxes arrived at after operating costs had been deducted. When the study was published it concluded that taxing profits was the preferable option.¹² A World Bank official later said that the organisation did not see itself as duty-bound to act solely in the interests of the developing countries. Its role was to ensure a share-out of wealth between the companies and the countries with resources, said the official.

Paul Collier, a professor of economics at Oxford University, and Michael Spence, a 2001 Nobel Laureate in economics, have highlighted the problems resource-rich developing countries face in negotiations.

‘Currently there is both an agency problem – ministerial corruption – and an information asymmetry: companies know better than governments what rights are worth,’ they say. ‘The consequences are often grotesque... In 2006 the Democratic Republic of Congo received a mere US\$86,000 from mineral rights.’¹³

Incentives and allowances

The most common form of direct taxation for companies is corporate tax, paid as a percentage of profits. There is usually a standard rate for all businesses, though companies operating in sectors such as mining and the oil industry are frequently offered a wide range of incentives and allowances that reduce their liability.

In Tanzania, for instance, two of the largest companies are reported to have inflated their losses for years to ensure they fell outside the threshold (see story page 10).¹⁴

Companies may also be subject to taxes on imports and exports, on dividends they pay to shareholders (known as

‘withholding taxes’ when they are used), capital gains tax and VAT. But once again, these are often greatly reduced, or waived altogether, as an incentive to companies to invest.

The practice of offering tax breaks, however, is now under attack as economically unviable. Research has shown that lost revenue exceeded the benefits of increased investment, international tax expert Susan Himes, a consultant to the Organisation for Economic Co-operation and Development (OECD), told a conference in Ghana in February this year.¹⁵

Hard bargaining: Zambia

In the late 1990s, mines and smelters in the Zambian copperbelt were losing £500,000 a week after years of underinvestment and low commodity prices. Burdened with a large international debt, Zambia was forced by international pressure to privatise the mining industry.¹⁸

Two London-based firms, banker Rothschild and international law firm Clifford Chance, parcelled the mining works into seven separate entities, which were then sold. The agreements with the mines’ new owners, which run to more than 20 volumes, were negotiated by the government over a three-year period with the aid of Clifford Chance, without the involvement of parliament, trade unions or any of the affected communities.¹⁹

Over the past year Christian Aid and its partner organisations in Zambia have played a key role in bringing these development agreements to light. They show that the general royalty rate was set at 0.6 per cent (with even that figure left negotiable) rather than the 3 per cent set in the 1995 Mines and Minerals Act. The agreements are binding for up to 20 years.

The deal meant that in 2004 mining companies contributed only about 12 per cent of all corporate tax revenues, though they accounted for nearly 70 per cent of export revenues. In 2006, the Zambian exchequer received just £12m against £2bn of copper production.

Now, with copper quadrupling in value to about £4,000 a tonne in recent years, a newly elected Zambian government wants a better return. President

Royalties

Royalties are payments to governments of a fixed percentage of whatever is being extracted. An International Monetary Fund (IMF) survey in 2001 found royalty rates vary from 2 to 30 per cent, with most between 5 and 10 per cent.¹⁶

IMF and World Bank pressure on Zambia to privatise its copper-mining industry at the end of the 1990s led to the setting of what is believed to be one of the lowest royalty rates ever charged: 0.6 per cent.¹⁷

Levy Mwanawasa in early 2008 cancelled all tax concessions for the copper-mining companies in the country, saying they were ‘unfair and unbalanced’, and raised the royalty rate to 30 per cent.²⁰ He also announced that ‘windfall taxes’ would be introduced as the price of copper rose.

Zambia’s mine-owning companies, which include Canada’s First Quantum Minerals, Glencore International – the firm founded by controversial American commodity trader Marc Rich – and Vedanta Resources – the UK-quoted mining firm run by Indian billionaire Anil Agarwal – rejected the new arrangements.²¹ They want the matter adjudicated by the World Bank’s International Centre for Settlement of Investor Disputes.

In 2005 it looked as though even Zambia’s

paltry copper royalty rate would be eclipsed by an iron-ore deal between the Liberian government and Mittal Steel, at the time the world’s second-largest steel company. The company, owned by London-based billionaire Lakshmi Mittal, who in 2004 spent more than £30m on his daughter’s wedding, was able to retain complete freedom to set the sales price of the ore – giving it ultimate control over the amount of royalties due.

The deal was signed with the national transitional government that had been established at the end of Liberia’s devastating civil war, just three months before democratic elections.²² After an NGO revealed the contents of the deal in 2006, however, a new, elected government insisted on a revised contract.

‘All international oil companies have used kick-backs since the first oil shock of the 1970s to guarantee the companies’ access to oil.’

Testimony to French magistrates by the former Africa manager of Elf Aquitaine, André Tarallo

Tax avoidance and evasion

There are main two ways for a TNC – or an individual for that matter – to get around paying tax. One is illegal – tax evasion – and one legal – tax avoidance. Both often involve the manipulation of profits and revenues through tax havens, where little or no tax is required to be paid on monies held there.

Without facilitators in the developed world, those seeking to avoid paying their dues in the developing world would be unable to operate. But there are plenty of people willing to help: well-paid lawyers and accountants designing aggressive tax-avoidance strategies; bankers; and the administrators of tax havens where the proceeds can be hidden in complex offshore structures of trusts and front companies.

The main techniques of evading tax are well known but hard to prove.

Falsified invoicing

Often those in the developing world who are importing goods will inflate the price they say they have to pay to the foreign supplier so that they can report lower profits and hence pay less tax. The reverse can also happen. A person exporting goods from a developing country will deliberately undervalue what is being sold, on paper at least, so that profits are once again depleted.

Falsified invoicing is difficult to detect in official statistics, as it is often based purely on verbal agreements between buyers and sellers, but it is widespread. It is estimated that around 45 to 50 per cent of trade transactions in Latin America are falsely priced by an average of more than 10 per cent; while 60 per cent of trade transactions in Africa are mispriced by an average of more than 11 per cent.²³

Transfer mispricing

A transfer price is the price paid for an exchange of goods and services between related affiliates of the same TNC. In most instances this involves either the parent firm trading with a subsidiary, or two subsidiaries of the same TNC trading with each other.

As deals between related TNC affiliates account for 60 per cent of global trade, there is ample scope for mispricing.²⁴ Tax authorities say for a transaction to be legitimate, an ‘arm’s-length principle’ should be followed by paying the open-market price. This requirement is often flouted, however, with transactions mispriced to enable the parent company to move money around to minimise tax.

Developing countries are particularly vulnerable to transfer mispricing. Typically, they lack sufficient information from the parent company and the local company to be able to challenge the prices involved. It is notoriously hard, anyway, to establish what the arm’s-length price would be within the highly complex international production networks that exist today.

Ironically, many companies that claim to be socially responsible find nothing wrong in the practice of transfer mispricing, and appear wilfully blind to the fact that they are helping deprive the citizens of the countries they are operating in of revenues that could be used to build a future.

Mispriced financial transfers

These involve exaggerating the costs entailed in intra-corporate financial transactions in order to move capital around illicitly. This could, for instance, involve exaggerating the interest rates payable on a loan from a parent to a subsidiary company.

Round-tripping

This practice involves local businesses taking advantage of the tax breaks offered to foreigners in countries where the government is eager for foreign investment. They do this by sending their own money offshore, either legally or, more commonly, illegally, then bringing it back disguised as foreign investment, which then qualifies for preferential tax treatment.

In China, for instance, foreign investors enjoy low tax rates, favourable land-use rights and financial services from domestic and foreign financial institutions, and superior property-rights protection.²⁵ Companies registered in the British Virgin Islands are among today’s biggest investors in China, with much of the money believed to have originated from within China itself.²⁶

Bribery and kickbacks

Oil drilling and mining concessions have been most closely associated with the payment of bribes to obtain advantageous mineral development agreements.²⁷

‘All international oil companies have used kick-backs since the first oil shock of the 1970s to guarantee the companies’ access to oil.’ Testimony before French magistrates by the former Africa manager of Elf Aquitaine, André Tarallo.²⁸

This often results in the citizens of poor countries ending up with an unfair deal, and being under-compensated for the removal of their finite natural resources.

Capital flight

The deprivation of rightful tax revenues from developing country governments is part of a wider phenomenon known as ‘capital flight’. This is where companies and individuals illicitly export enormous amounts of capital that could otherwise be used to stimulate these economies.

Raymond Baker, a senior fellow at the US Center for International Policy and an internationally respected authority on money laundering, calls it ‘the ugliest chapter in global economic affairs since slavery’.²⁹ As with slavery, it is the poor and vulnerable who suffer.

Baker describes capital flight as ‘the most damaging economic condition hurting the poor in developing and transitional economies. It drains hard-currency reserves, heightens inflation, reduces tax collection, worsens income gaps, cancels investment, hurts competition, and undermines trade.’ He says it also ‘leads to shortened lives for millions of people and deprived existences for billions more’.³⁰

The flow of illicit money from developing countries, says Baker, is based on shifting the wealth out of the countries where 80 per cent of the world’s population live into countries where 20 per cent live.

It often involves TNCs seeking to evade taxes in the developing world and to maximise profits for their shareholders. They may also want to recoup rapidly capital expenditure they have incurred in a country they regard as politically unstable.

Other culprits include business accomplices, and corrupt politicians and officials anxious to bank the bribes they have taken in offshore tax havens.

Baker estimates that between US\$1 trillion and US\$1.6 trillion of illicit money moves across borders annually. Of that, he says, half – some US\$500bn to US\$800bn – comes out of developing and transitional economies.³¹ Between 60 to 65 per cent of that money has been moved to evade tax, criminal activity accounts for between 30 and 35 per cent, and bribery and theft by government officials, he estimates, another 3 per cent.

Money removed to evade tax through transfer mispricing and false invoicing alone, says Baker, accounts conservatively for 7 per cent of global trade transactions each year.³² Christian Aid (see Technical appendix page 51) estimates that the amount of tax revenue lost to developing countries annually through these two techniques amounts to US\$160bn.

‘For the first time in the 200-year run of the free-market system, we have built and expanded an entire integrated global financial structure the basic purpose of which is to shift money from poor to rich,’ Baker says.

Exporting a diamond worth US\$1,000 for US\$100, for example, includes a capital flight component of US\$900, which will then more often than not end up in an offshore account belonging to the exporter once it has been sold at the market price.

The quantity, quality or grade of whatever is being traded may also be misrepresented to justify the movement of large amounts of money out of the developing country. An invoice may state, for instance, that a jewel-quality diamond is an industrial cutting diamond to justify a lower price per carat, or conversely that 200 units of machinery have been bought when the true figure is only 150.

Other reported examples have included a shipment of cashew nuts from Nigeria that would usually have fetched nearly US\$5 a kilo being sold to the US for just under 50 US cents a kilo, and optic fibres needed to fuel Nigeria’s digital revolution being bought for US\$1,372 per unit when at source the cost was precisely US\$6.³³ In

both instances, the difference between the market price and the alleged prices paid was said to be the amount that those involved in the transactions managed to take out of Nigeria.

In some cases, illicit transactions will be disguised by being interwoven with genuine transactions. In other, more blatant instances, no transaction takes place – the imported goods or services that have been paid for simply fail to materialise.

As trade expands in services such as management expertise, the problem has increased: unlike goods, which require a customs or bill-of-lading record, services do not leave an equivalent paper trail. Services are intangible; it is hard to assess their fair value. Who can say whether or not US\$10,000 paid to a foreign contractor for ‘engineering consultancy services’ is a fair price or not?

In many cases, the removal of capital can, in fact, only be identified through a thorough transaction-by-transaction analysis that is far beyond the resources of most financial authorities.

'We hear every day that there is no money for development projects, for building schools and dispensaries. Yet people hear of billions of shillings lost in tax revenue... How do we explain this to people who we tell there is no money for basic services?'

John Cheyo, chairman, Parliamentary Public Accounts Committee, Tanzania¹

Tanzania: the sharp end of the panga

Clouds of dust rise from the huge open-cast gold mine in Geita



Christian Aid/Evelyn Hookstein

Tanzania is one of the fastest-emerging gold producers in Africa. It is thought to have the continent's largest gold reserves after South Africa. Since 1998 a new gold mine has been opened every year.

Gold is just one of one of Tanzania's mineral riches; it also has vast resources of rubies, sapphires, diamonds and emeralds. But it is gold that predominates. It accounts for more than 90 per cent of the country's mineral exports – in 2007 gold exports were worth more than £500m. The recent jitters in the global financial markets saw gold soar to US\$1,000 an ounce, the highest price in history.

Tanzania's 39 million citizens, however, have gained few benefits from this huge natural coffer. Its UN development ranking puts it at 159 out of 177 countries, more than half the population live on less than US\$1 a day, life expectancy is just 51 years, 140,000 people died of HIV-related illnesses in 2007, and 44 per cent of the population is classified as undernourished.

Instead of reaping the rewards of a bonanza, the country has lost hundreds of millions of pounds because the royalties levied on extracted gold are so low and mining companies have

reportedly minimised their tax liability by inflating their losses.²

Geita, in the heart of Tanzania's mining region, illustrates the massive disparity between the country's mineral wealth and its abject poverty. The drive from Lake Victoria to the mine is a bone-shattering two hours. Mine officials don't use it; they fly into an airstrip inside the mine site.

AngloGold Ashanti (AGA), which runs the Geita mine that opened in 2000, says it wants to leave the community better off than it was when it arrived, yet the pot-holed roads and shacks have shown little sign of improvement over the past decade. A young miner, who shares a house with two families, says the company should be doing more: 'Look at this place! Geita should be doing more for us. We have to hope that there will be changes in the future, but we should have seen changes for the better already.'

Mbaraka Islam, a journalist who has investigated the contracts signed by the big mining companies that entered the country in the late 1990s with the Tanzanian government, has spent time in Geita: 'Back in the late 1980s I thought Tanzania would be in heaven like Botswana and South Africa, with tarmac roads, and good education and health systems. But

The concessions

- The right to deduct 100 per cent of capital expenditure from taxable income in the year in which it is incurred, even though this means no tax will be paid in early years of mining operations because losses can be carried forward and offset against future liabilities.
- The right to increase the claim for capital expenditure by 15 per cent a year if they declare a taxable loss. This inflated expenditure is then carried forward for offset against income in future years. Under this scheme the chances of taxable income

arising are significantly reduced.

- A royalty rate of 3 per cent on gold exports. Other gold-exporting countries in Africa, such as South Africa and Ghana, charge similar amounts: Ghana a minimum of 3 per cent and South Africa 2.1 per cent, although in both cases more profitable companies pay more. The figure also compares badly to the 10 per cent Botswana charges for diamond extraction.
- Payment of the royalty can be deferred if the 'cash operating margin' (that is, revenue minus operating costs such as capital expenditure and interest on

loans) falls below zero.

- Exemption from corporation tax of 30 per cent of profits, if operating at a cash loss.
- Zero per cent import duty on capital goods and fuel.
- Five per cent import duty on spare parts for first year but then zero thereafter. Similar arrangement for mining exploration equipment such as explosives and lubricants.
- Exemption from capital gains tax.
- Exemption from VAT on imports and local supplies of goods and services.
- Stamp duty on buying property or shares reduced from standard 4 per cent to

a maximum of 0.3 per cent.

- Right to keep accounts in US dollars, which offers protection from currency exchange costs.
- The right to repatriate 100 per cent of profits.
- Foreign firms guaranteed 100 per cent ownership of mines.
- The right to employ unlimited numbers of foreign nationals.
- Losses are not 'ring-fenced' within the country, which allows companies to combine costs and income from one mine with those of other mines when calculating tax liability.

'The financial institutions lied to Tanzania. We have every right to state we have been lied to and we have every right to demand redress.'

Tundu Lissu, lawyer and activist

now nothing has changed and we are still begging.'

The contracts with the mining companies clearly do not have the interests of the country at heart. At the time they were signed, the World Bank was urging Tanzania to develop private investment in mining and attract foreign capital. The government's Mineral Sector Policy 1997 emphasises the primary role of companies in mining, with the government acting as regulator.

Commissioner for Minerals Peter Kafumu says negotiating with the mining companies was an intimidating experience, much like being faced with a traditional weapon: 'The companies are holding a panga by the handle and we are getting the sharp end.'

Lawyer and activist Tundu Lissu says the outflow of Tanzania's wealth was predictable: 'The financial institutions lied to Tanzania. We have every right to state we have been lied to and we have every right to demand redress.'

Mr Lissu has been at the forefront of the struggle by communities affected by large-scale mining for more than a decade. He is the co-author of *A Golden Opportunity?*, a report co-funded by Christian Aid, which documents how Tanzania is failing to benefit from its gold resources.

His report spells out how the two foreign mining companies that run the six biggest mines – Barrick, from Canada, and AGA, based in South Africa but listed on the London stock exchange – say they are running at a loss.

Thanks to the very generous financial concessions they were able to obtain when setting up in business in east Africa, this has meant that government revenues have seriously lost out. Royalties from the gold extracted have averaged £8.8m a year and all other taxes have amounted to less than £3m. Local media have reported allegations of tax evasion.

Company figures show AGA paid US\$96.8m in taxes and royalties between 2000 and 2006, averaging US\$13.8m a year. Yet over the same period it produced three million ounces of gold worth US\$1.43bn. Company reports say AGA made operating profits totalling US\$93m from 2002 until mid-2007.

Barrick does not reveal how much it pays to the Tanzanian government in taxes and royalties. Company reports, however, show its Tanzanian mines provided 'income' (defined as sales less cost of sales, that is, gross profits) of US\$97m since 2004.³

Tanzania is estimated to possess about 45 million ounces of gold. At the current gold price, that translates into a potential fortune of about US\$39bn.⁴

An inspector calls

In 2003 the Tanzanian government contracted US company Alex Stewart Assayers Government Business Corporation (ASA) to conduct an audit of the large gold mines in the country, to check if their declared production and financial positions were correct. ASA's report was kept secret, with the government refusing to publish. It was leaked to the *Sunday Citizen* newspaper in 2006.

It said that four gold mining companies, including Barrick and AGA, over-declared losses by US\$502m (AGA US\$158m and Barrick US\$236m) between 1999 and 2003. This means the government potentially lost revenues of US\$132m. The audit noted that thousands of documents were missing that would have shown whether royalties of US\$25m had been paid.

The ASA report stated: 'The huge tax losses declared by the mining companies are startling. The tax losses, comprised of their investments, operating cost and tax exemptions, are carried forward by the mining companies, which then will not pay corporate taxes unless they have very large incomes.'

The audit's analysis states that AGA managed to exaggerate its losses by 'early charging' of a tax incentive providing for 15 per cent additional capital allowance on unredeemed capital expenditure, and also by 'improper calculation of the [tax] allowance base by not deducting taxable profit/gain'. ASA also stated that 'a long list of documentation' substantiating the amount of investment and production costs claimed was 'missing'.

Work at the bottom of the open-cast gold mine in Geita



ASA noted that it was hindered by 'the persistent reluctance of the mining companies to cooperate with the Auditor' and the companies' failure to keep adequate documentation of their financial records in Tanzania. This meant that 'these mining companies are in default of the law, and failure to cooperate could be interpreted as a strong desire to hide faulty declarations'.⁵

In February 2007 the parliamentary Public Accounts Committee (PAC) in Dar es Salaam produced a report which found that the mining companies had declared losses estimated at US\$1.045bn between 1998 and 2005, equivalent to a quarter of national budget for 2006-07. The PAC regarded the 'losses' as suspect because mining companies were making heavy capital investments at the time.⁶

The report *A Golden Opportunity?* estimates that Tanzania has lost out on at least US\$400m over the past seven years from low royalties and lost taxes from mining companies. The amount would have provided a 'huge boost to tackling poverty in Tanzania'.⁷

The report says the government's budget for 2007-08 envisaged spending US\$48 per person on development expenditure such as education, health, infrastructure and water. The lost revenue could have paid for more than 8.3 million people to receive such services. The amount, the report adds, was equivalent to more than 1.5 times Tanzania's entire health budget for 2007. It could have funded the building of more than 66,000 secondary-school classrooms.

The authors arrived at their figure by working out what Tanzania would have received had a royalty rate of 7.5 per cent been levied and adding that figure to unpaid corporation tax, tax lost if mining companies had inflated their losses, and money they had failed to set aside for environmental rehabilitation.

In March this year, Tanzania's Chamber of Minerals and Energy responded to allegations of tax evasion with a two-page newspaper advertisement claiming that 'none of the mining companies audited has ever seen an ASA report'.

The advert continues: 'It is an essential element of audit procedure that an auditee be given the opportunity to explain any apparent anomalies found during an audit. This has unfortunately never happened and has given rise to a lot of speculation on the subject. The report is still a subject of discussion between the Government and respective mining companies...'

'Mining companies have invested in excess of US\$2bn in Tanzania over the last decade. As a result, total mineral exports

in the year 2005 amounted to US\$692.8 [million] compared to just US\$16.1m in 1997 – with gold alone rising from US\$13.1m in 1999 to US\$639.2m in 2005.'

Geita

The Geita gold mine is AGA's only mine in Tanzania. It is one of Africa's biggest open-cast mines and in 2006, according to its annual report, it produced 308,000 ounces of gold.⁸ It has been widely reported in the Tanzanian media that it will only start paying corporation tax in 2011, 11 years after starting operations.⁹ Yet its own annual reports show the company has made operating profits of US\$93m from Geita between 2002 and mid-2007.

The town of Geita does not have much to show for the fact that it is sitting on some of Tanzania's richest gold seams. Mining has seen the population increase six fold from 20,000 to 120,000 as men flock to Geita for jobs.

But the roads are in a lamentable state and water has to be fetched from wells as the main water-pipe goes direct from Lake Victoria to the mine camp, with no outlets for the local residents.

Geita District Hospital was built in 1956 and probably has not seen much upgrading since. It is busy, with about 250 outpatients a day and some 160 inpatients. Many of the wards have two patients to a bed. The busiest place is the HIV clinic, with an average of 150 patients a day. Doctors are concerned about the incidence of HIV; as with all mining sites, the gold mine attracts a lot of young single men.

But malaria is the greatest concern for the medical staff. They say mining has greatly increased its prevalence. Activities such as trenching, drilling and excavations tend to increase water run-off, which in turn increases breeding sites for mosquitoes. Dr Johannes Lukumay, the hospital's medical officer, says: 'We simply do not have sufficient stocks of anti-malarials.'

Geita employs 2,381 men, with a further 1,021 contractors. Basic annual salary is 350,000 shillings (US\$300), which is the minimum wage introduced by the government in January 2008. In addition they receive a 15 per cent housing allowance, free medical care for themselves and their families, and 28 days' holiday.

Peter, a young miner who asked us not to use his real name, complained that his salary was not enough. He says that TAMICO, the miners' trade union, has done little to improve wages. According to AGA only 3.1 per cent of the workforce

is unionised. It is difficult to know whether it is the union's reputation or a company dislike of unions that is responsible for this.

Peter is alarmed at the treatment of the local populations displaced by the mine. 'There is a lot of mistreatment of locals. They are chased from their homes and not compensated. They just live in camps and have lost their livestock,' he says.

Not far from the dingy two rooms Peter rents is an abandoned courthouse bearing the grand name of Environment and Mined Land Rehabilitation Group, Orphans and Services. In July 2007 86 families found themselves dumped here after being evicted from their homes.

They were from the village of Mtakuja, which now lies inside the mine site. Emmanuel Balitazali, 53, vividly remembers that night.

'Officers from the district came at three in the morning when we were all asleep. They had machine guns and a court order evicting us. We didn't have a chance to pack; they put us in a vehicle and dumped us here.'

Village leaders say they had already won a case against Geita and that the company's appeal was pending. Others claim that the company is in the clear as it had paid compensation to the district commission, which did not then pass it on to the residents.

Whatever the rights and wrongs, it is clear that Emmanuel and his wife Venerranda now have no home, few belongings and little hope of redress.

'We had to leave home, where we had our livelihood and where we had raised our children,' says Emmanuel standing in the middle of the courtroom with its two rows of raised benches.

Venerranda points to their meagre pile of pots, bags and flip-flops: 'It was very difficult. I couldn't stop crying. We could do nothing. I had lived there all my married life. I was not happy to be taken from my home and to lose all my belongings.'

Time for a change

There is pressure in Tanzania for change. In his inaugural address in December 2005, President Jakaya Mrisho Kikwete promised to review all mining contracts to ensure that 'the nation is benefiting from the richest minerals available in most parts of the country.'¹⁰ In November 2007 the president announced the formation of a committee to investigate the nature of the mining laws and contracts.

There have been four such previous committees; none have

ever been made public. The fourth review, *Review of Mining Development Agreements and Fiscal Regime for the Mineral Sector*, has been seen by Christian Aid. It recommends sweeping changes to mining and fiscal laws, and the renegotiation of various mineral development agreements with the mining companies. Yet, apart from minor changes to a recent agreement, none of the recommendations have been implemented.

Mr Lissu, the co-author of *A Golden Opportunity?*, was impressed by the recommendations in the fourth review: 'I was surprised. For a government which always maintains that all is well in the mining sector, it was a very candid examination of the mining problems.'

'But if you live in Tanzania and a report is not made public you can be sure it is not good for the government. They set it up with a big flourish and then it peters out.'

MP for Kigoma North Zitto Kabwe is a member of the latest review committee and is determined that, should the president refuse to make the report public, he will do so anyway. In August 2007 he was suspended from parliament when he introduced a private motion to investigate the government after it had signed a new mining agreement even though it had promised not to do so until the review had been completed.

Mr Kabwe is concerned that the donor countries have remained so silent on the issue of low gold-mining taxes. 'The donors do not speak out at all about the mining sector,' he says. He finds this surprising in light of the fact that donor countries contribute 40 per cent of Tanzania's budget.

This silence has been highlighted in the local press. An editorial in the *Sunday Citizen* says: 'They [the donors] remain tellingly silent on environmental rape committed by foreign mining companies. We don't hear strong words from them when artisanal miners or villagers in mining areas are undermined... When the mining law was being passed, or even now when there is a big debate on its contents, conspicuously missing is the voice of the donors... With such a stance, won't one be forgiven to conclude that development partners are guilty of condoning corruption by their kith and kin, the big western mining companies?'¹¹

There is some evidence for the collusion suggested in the editorial. A letter dated 3 December 2007 to the chairman of the Mineral Sector Regulatory System Review Committee from Basil Mramba, the Minister for Industries, Trade and Marketing, relates what happened when, in 2004, the government repealed the Income Tax Act of 1973 and replaced it with the 2004 Income Tax Act.

'What the donors give is peanuts compared to the wealth that goes out. The taxes ordinary citizens are paying just allow multinationals to make huge profits. You give money to your government, which gives that money to Africa with strings attached.'

Professor Issa Shivji, legal scholar



Emmanuel Balitazali, 53, and his wife Venerranda Thomas, both displaced from Mtakuja by the Geita gold mine

Mr Mramba states: 'During preparations of the new law a number of foreign diplomats in the country formed a committee to study the recommendations relating to the relevant tax bill, a measure which was unusual. Being the then Minister for Finance, I met them twice to listen and respond to their objections, especially to the manner in which mines were to be made to pay income tax, as had then been proposed by an expert from Oxford University in England. Eventually, the Cabinet decided to postpone the incorporation into the new law of the entire section of that bill which dealt with minerals so that it would be re-examined when the time was right.'

The expert was not named and nor were the diplomats, although it is alleged they represented the UK, Norway, South Africa and Canada. The UK, Canada and South Africa have a particular responsibility when it comes to gold mining in Tanzania. AGA and Barrick are based in South Africa and Canada respectively. One of AGA's major shareholders is the British corporation Anglo American. None of these governments,

however, appear to have raised concerns about how mining companies declare their revenues or about the favourable treatment they receive.

The UK is Tanzania's largest bilateral donor, spending £120m on aid in 2007-08, and one of the largest overall investors in the country, with investments worth about 1.4 trillion Tanzanian shillings (US\$1.1bn). It is also a major international proponent of the Extractive Industry Transparency Initiative – which sets global standards for companies to 'publish what they pay' in oil, gas and mining contracts, and for governments to disclose in full what they receive for them.

Dr Kafumu, the Commissioner for Minerals, believes that Tanzania is at a great disadvantage when sitting across the table from mining companies and their lawyers. 'We have no capacity to look at their books. They can write the books so



Athman Omari working at an artisanal mining site near the Geita gold mine. These small-scale miners are increasingly being displaced by the large mining companies. The World Bank estimates there are now 170,000 small-scale miners in Tanzania; in 1995 there were 550,000

that third-world countries cannot regulate properly. Even the contracts are difficult. I think the mining companies exploit our weaknesses in law and capacity,' he says.

'Globalisation is a disadvantage to third-world countries. Donor countries are protecting their industries. I have seen several times ambassadors accompanied by mining officials speaking to ministers.'

Professor Issa Shivji is one of Tanzania's most respected legal scholars. He says that the government should have taken a tougher negotiating position. 'The mining legislature was framed so that it was full of loopholes. The state could have demanded a 51 per cent share,' he says.

He disputes the allegation that there is no in-country expertise: 'We have the expertise, the university here has a long-established faculty of law, but we were never consulted.'

Professor Shivji thinks it is more important that Tanzania regains its rightful revenues to correct the relationship with the donors. 'What the donors give is peanuts compared to the wealth that goes out. The taxes ordinary UK citizens are paying just allow multinationals to make huge profits. You give money to your government, which gives that money to Africa with strings attached.'

Mr Kabwe, the MP who is currently on the review commission, spells out the implications: 'Under normal circumstances, if all taxes were paid, if no gold was undervalued

and if there were no over-declaration of total cost, this year we should get slightly more than what the donors give us.'

Mr Lissu thinks taxpayers in the donor countries should insist their countries stop picking up the bill for the mining companies: 'It is just common sense for citizens to demand their governments stop subsidising African countries when these countries have the resources to lead them out of the deep poverty in which they exist.'

In Geita, Emmanuel Balitazali ruefully surveys his few belongings in his corner of the abandoned courthouse.

'I am terribly disappointed as there is a lot of wealth. Other people are enjoying the wealth and we struggle to survive,' he says.

'My government inflicts a lot of pain on me because the government does not seek our interests. There is a lot of uncertainty in my life.'

The reason for that uncertainty is not hard to find. It is created by the companies mining gold in Tanzania, all of them large transnational companies based in the developed world and part of the financial establishment of those countries.

Yet reports in Tanzania allege that their local operations cannot keep proper accounts, cannot produce these records for government auditors, and have overstated their losses to dodge tax.

From green gold to yellow cake

Malawi

Malawi, a tiny landlocked country, is surrounded by countries with mining history: copper in Zambia and gold in Tanzania. It has long been solely dependent on agriculture, with fertile soil and plentiful rainfall. The late President for Life Hastings Kamuzu Banda, 'Dr Hastings', urged Malawians to grow more maize – what he called their 'green gold'.

Soaring oil prices and concern over climate change have led to increased interest in Malawi's uranium reserves. Malawi is now poised for its first modern mining project, undertaken by the Australian-based Paladin Resources, at Kayelekera in Karonga in the far north of the country.

It is estimated the exploitation of Malawi's uranium reserves will generate an annual income of up to US\$250m. Tobacco is currently the country's main foreign exchange earner at US\$19m. It needs to benefit from its mineral resources; it is the fourteenth poorest country in the world, with life expectancy of 46 years.

The Malawi government took a hard look at the mining contracts in surrounding countries before sitting down to the negotiating table.

Acting director at the Department of Mines Ellason

Kaseko says: 'We knew the uranium deposits were there, but it was better to leave it there rather than get a raw deal. We saw how our neighbouring countries had blundered and we decided to learn from them.'

The government says it is now satisfied with the fiscal deal it has negotiated. One key aspect was that it felt it was important to be a shareholder in Paladin Malawi, given public concerns about uranium.

It has a 15 per cent equity in the mine. The royalty rate was set at 1.5 per cent for the first three years' production and 3 per cent after that; the corporate tax was set at 27.5 per cent. In addition, any profit or loss is ring-fenced so can only be attributed to the mine at Kayelekera and not to wider Paladin operations.

'We believe Malawi was able to secure a good outcome from the negotiations, particularly given that this was the first mining investment of this scale to be made in the country,' says an official close to the negotiations.

The mining licence was granted in April 2007, but controversy dogged the project following the leak of the Environmental Impact Assessment. A group of six influential civil-society organisations (CSOs) swung into action. It set the scene for

an extraordinary journey – from the courtroom to an unusual alliance of company, government and CSOs.

The eventual outcome illustrates how a developing country government, working together with its concerned citizens, can negotiate better deals on mineral extraction for the benefit of its people.

'We were concerned about the manner in which the agreement was signed and we believed the government was not acting in the best interests of Malawians,' says Rafiq Hajat, executive director of The Institute for Policy Interaction.

There were a number of issues that concerned the group. Namely, the lack of legislation regulating the mining of uranium, the lack of consultation, threats to health from radiation, threats to water resources (Kayelekera lies within a catchment of a river flowing directly into Lake Malawi, Africa's third-largest freshwater lake), secrecy, and the lack of guaranteed benefits for surrounding community.

The group also wanted assurances that the International Atomic Energy Agency was fully involved in drawing up safety standards and guidelines for transport of the uranium. The mine is located close to Lake Malawi and the Rift Valley fault line.

The processed 'yellow cake' will be transported by lorry to the port of Dar es Salaam in Tanzania.

With little response forthcoming from either Paladin or the government – Mr Hajat says the government called the CSOs 'anti-development demons' – the CSOs decided on drastic action. They took the government to court for 'betraying the interests of the country', alleging unconstitutionality and breaches of environment laws.

Undule Mwakasungula, executive director of the Centre for Human Rights and Rehabilitation, defended the action saying: 'Regulatory legislation has to be in place in order to control the mining of uranium. Malawi as a sovereign country is required to introduce its own legislation to control and regulate companies such as Paladin.'

Things seemed set for a long, drawn-out, expensive court case until news of the court action leaked in Australia and Paladin shares started to slide. An out-of-court settlement was suggested.

The three parties sat down for some hard bargaining that took three days. In November 2007 Paladin announced that the company, the government of Malawi and the CSOs had settled their action on a 'positive and amicable basis'.

The terms of settlement stated that the government of Malawi would establish a working group involving the CSOs to amend the Mines and Minerals Act and to develop legislation to deal with the handling and transport of radioactive substances. The CSOs would participate in the team monitoring Paladin's environmental and health obligations.

At the request of the Karonga community, the government and Paladin agreed to upgrade the community water supply at Karonga. The company also pledged to upgrade the local airport in Karonga to international standards (it had planned to build an airstrip inside the mine site).

The agreement marked a sea change in the relationship between the government and the CSOs. As part of the monitoring committee, the CSOs have a permanent role overseeing the mining operation and ensuring all parties keep to the agreement.

Deputy Minister of Water and Irrigation Frank Mwenefumbo was one of those who initiated the dialogue: 'We recognised the role of CSOs in Malawi. Even the Minister of Finance says we have learnt from them. We had started with the perception that the CSOs

were determined to derail the negotiations.'

Mr Hajat agrees: 'We were not against mining per se. We were interested in the best interests of the people. That is the role of government and we wanted to make sure it was fulfilling its responsibilities.'

Mr Mwakasungula says it was a good deal for Malawi and issues this warning: 'These agreements are legally binding and if the government or Paladin violates the agreements, that would be a case of contempt, so we can go back to court.'

Karonga lies at the northern tip of Malawi, hard up against the border with Tanzania. The uranium mine is another 50km from the town; a risky drive in the rainy season with the possibility of collapsed bridges and washed-out roads.

The start date of mining depends on the condition of the road and has now been put off until the end of 2008. Construction of the road was initially funded by Taiwan but was abandoned after Malawi severed ties with Taiwan in January 2008 and recognised mainland China. China has promised to complete the road and Chinese surveyors are already at work, their conical straw hats the only protection against the tropical rain.

The mine itself is buzzing. In full operation it will employ



Kayelekera uranium mine, Karonga, Malawi

some 300 workers, now there are 500 people busy constructing the mine and the processing plant. Demolition of the hill containing the uranium seam is under way.

People in Karonga are pleased at the prospect of economic development in a region that has historically suffered from neglect. But there is a lot of suspicion about the company and the perceived health dangers of uranium.

Although Paladin claims already to be spending US\$11,000 a week on local produce, the business community complains it is bypassing them and buying direct from wholesalers.

There are also rumours about the effects of radioactivity and contamination of the waterways. Apart from the health implications, this would also affect the livelihood of the fishing community.

At the Bar Marina on the edge of the lake, most people are willing to take time out from watching the English Premiership football match and talk, but they are less keen to give their names.

Says one local businessman: 'It's a good thing, it will have an effect because there will be more jobs. But the big challenge will be to monitor the company. We are worried about pollution and the transport of the uranium.'

Says another: 'I am very happy to have the mine here, but we are all worried about the effects. We have heard a lot of bad things. Uranium is dangerous.'

The action by the Malawi CSOs, and the government's determination to learn from its neighbours, has ushered in a new era for extractive contracts. Observers say the contract drawn up in this tiny country will have repercussions far beyond its borders.

For more than a century there has been an inherent contradiction in the attitude of Western legislators towards tax havens. Despite their much-vaunted regard for the rule of law (and more recent concern for human rights plus the desire to help the developing world) they have allowed a financial system to develop that is wide open to abuse.

The secret shore

St John's Harbour, Antigua – one of the Caribbean's many tax havens



Christian Aid/Judy Rogers

Getting one up on the tax authorities has undoubtedly been a feature of human society since the first-known system of taxation was introduced by the pharaohs of Ancient Egypt. The paying of tax has generally been viewed unfavourably by those who are liable – an antagonism that has seen monarchies overthrown and governments brought to a violent end.

Today's dissenters, however, have no need to make their protest in blood. Celebrities such as Formula One racing champion Lewis Hamilton and pop star Phil Collins simply jet off to the balmy tax climes of Switzerland, while U2 lead singer Bono relocates his recording rights in a Netherlands-based tax structure.

The fortunes of these three are a small part of the truly vast amounts of money that are now held in the world's 70-plus tax havens. Estimates by the Organisation for Economic Co-operation and Development (OECD) in 2007 suggested that the sums then parked 'offshore' totalled anything from US\$5 trillion to US\$7 trillion (£2.5-£3.5 million million – at least twice the amount of Britain's gross domestic product).¹

The Tax Justice Network is an international campaign group with headquarters in London that promotes transparency in international finance and opposes secrecy. It has spent the past five years investigating tax havens. It estimates that the true figure held offshore is around US\$11 trillion. This includes the value of houses, yachts, works of art and other tangible assets whose ownership is registered in tax havens.

Even that estimate tells only part of the story: with tax havens now involved in an estimated half of all global trade, the sums passing through will be even greater.²

Firmly entrenched in today's fiscal thinking, tax havens are accepted as a fact of life. But there is a moral ambivalence surrounding them. Their purpose is to enable businesses and individuals to trade unencumbered by taxes and financial regulations, no matter what the merit of those taxes or regulations might be.

To guarantee that freedom, they have to guarantee secrecy for their customers too. But therein lies a problem. For that secrecy, which is usually enshrined in the haven's judicial code, can serve as a cover for tax evasion, bribery, corruption and money laundering.

Some efforts are being made to lift the veil. US financial regulators have taken determined steps to curb the activities of accountants, lawyers and banks engaging in tax-haven practices they judge 'abusive'. The German authorities are clamping down hard on some 750 wealthy citizens discovered

to have hidden hundreds of millions of euros in secret bank accounts in the small Alpine principality of Liechtenstein. In the UK, HM Revenue and Customs recently forced the big five high-street banks to hand over details of customers with offshore accounts. These customers are now being pursued for tax, with a further 170 financial institutions and organisations facing similar requests for disclosure.

Tax havens certainly deprive the exchequers of rich countries, but they have an immeasurably greater impact on developing countries that can ill afford the losses. Rich country governments should do a great deal more to curb their activities.

Havens enable businesses, particularly transnational corporations (TNCs), to deprive poorer countries of vast amounts of money that is rightfully theirs. In some cases it can also be the haven that provides a hiding place for bribes paid to the corrupt.

The UK has a particular responsibility for the system now in place. More than 30 Commonwealth countries and Crown Dependencies have taken their place alongside states such as Monaco, Luxembourg and Switzerland as tax havens of note.³ Measures that have transformed Crown dependencies into places that can aid and abet crime must have had the explicit approval of the UK government, because changes of legislation in such places have to be passed by the UK's Privy Council.

There are other ways that the UK government colludes with the havens. The EU Savings Tax Directive was introduced to target funds held by EU residents in tax havens on which interest earned was not being declared. But this has been largely neutered by the UK insisting it cannot apply to trusts and limited companies.

Huge profits made by offshore companies trading on the London markets can be sent straight into offshore accounts, with no questions asked about the ownership of the companies, and no tax paid. The absence of such a 'withholding tax' is another cause for concern.

The UK's tax laws for 'non domicile' residents were modified, under protest, in 2008 so that annual payments of £30,000 are now required in lieu of tax. But the changes failed to bring into the tax net assets held in offshore trusts and companies. People with a country of origin other than the UK, or with a parent from abroad, who say that they plan to leave the UK at some indeterminate date in the future will still only be taxed on income made in the UK.

The UK government was only reluctantly persuaded to accept into British law the provisions of an OECD treaty that

prohibits paying bribes to foreign officials. For years it said no new law was necessary, until peer review by other signatories determined that it was. Provision was made in the Anti-terrorism, Crime and Security Act of 2001.

If there are any doubts left as to the UK's active support of tax havens, then the operation of CDC plc, formerly the Commonwealth Development Corporation, is enough to allay them.

The company was set up to channel funds on behalf of the British government to projects in the developing world. Latest company accounts show that on worldwide pre-tax profits of £365m, the company paid no tax either in Britain or abroad – in fact it qualified for tax refunds.⁴ Many of its 78 subsidiaries are based in holding companies in tax havens such as Mauritius, Bermuda, the British Virgin Islands and the Cayman Islands.

Richard Murphy, a chartered accountant and senior adviser to the Tax Justice Network, says: 'These tax rates are just about the lowest I have ever seen. They make the most advanced tax planners look like amateurs.'

'They are the result of statutory tax exemption for CDC in the UK and negotiated exemptions overseas. It sets the most appalling precedent that companies investing in developing countries should not expect to pay tax.'

The Irish government does not appear to be concerned about the global financial impact of tax havens either. Since the 1970s, Ireland has built its economic growth on foreign direct investment, manipulating its tax system to attract TNCs aggressively. By 2004, it was the most profitable global location for US firms to invest, its position bolstered by broad political support for maintaining corporate tax at just 12.5 per cent. This puts Ireland in direct competition with some tax havens for the investment of transnational corporations.

Yet even in this low-tax climate, companies like US software giant Adobe's two Irish subsidiaries had a combined turnover of US\$2.6bn (€1.66bn/£1.31bn) last year yet paid just US\$5m (€3.19m/£2.53m) in Irish corporate tax, an effective rate of 0.5 per cent. The company trades extensively within itself and, as it doesn't report a geographical breakdown, it is very difficult to see exactly where profits are made and what taxes are paid.⁵

Recent research shows that TNCs investing in Ireland have, on average, more than twice the yield on their investments compared to Irish firms investing overseas.⁶ This is, in part, attributable to the profitability of foreign-owned capital in Ireland being overstated. In practice, this is because TNCs 'export' profits from other countries to Ireland, to avoid paying

tax overseas and to take advantage of Ireland's low corporate tax rate: evidence that Ireland's corporate taxation policy undermines the tax structures of other countries.

What tax havens offer

The inescapable fact is there are only four reasons for banking 'offshore':

- to avoid tax (which is legal)
- to evade tax (which isn't)
- to function in secret
- to sidestep regulations controlling financial services or monopolistic practices.

In each scenario, the pursuit of profit outweighs all other considerations, including good citizenship and social responsibility.

The world's more prominent tax havens, such as the British Virgin Islands, the Cayman Islands, Singapore, and Jersey and Guernsey, operate as follows:

- non-residents can register companies and pay little or no tax on the profits attributed to them
- tax information is either not exchanged with other states or it is made very hard for them to obtain
- the identities of the real owners or beneficiaries of bank accounts, companies and trusts can be kept secret
- no public disclosure of accounts is required.

The secrecy ensures that it is easy for those who want to use companies registered in these tax havens to avoid or even evade tax liabilities due elsewhere.

In many tax havens, hundreds of banks are on hand to facilitate business. Some 270 have a presence in the Cayman Islands alone.⁷ Accountancy firms are also very much in evidence (the 'big four' – KPMG, PricewaterhouseCoopers, Deloitte and Ernst & Young are present in virtually every major haven), along with tax and corporation lawyers. These experts in international finance also play an active part in helping the havens' governments dream up new schemes and services to pull in ever more customers, and to devise changes in the law that may add to a haven's attraction.

This is a cut-throat business where havens vie with each other for the trade while trying to stay ahead of the world's tax authorities and regulators. Because many havens are relatively small, geographically and in terms of population, laws and regulations can be introduced or amended rapidly, resulting in continual change.

The Cayman Islands, for instance, are now the world's

The inescapable fact is there are only four reasons for banking ‘offshore’: to avoid tax (which is legal), to evade tax (which isn’t), to function in secret, to sidestep regulations controlling financial services or monopolistic practices. In each scenario, the pursuit of profit outweighs all other considerations, including good citizenship and social responsibility.

fifth-largest banking centre where an estimated US\$2 trillion is believed to be held. Within months of a local banker being served with a subpoena to appear before a grand jury in the US investigating tax evasion, the Cayman Islands brought in bank secrecy with the Confidential Relationships (Preservation) Law.⁸ They also became a firm favourite with US healthcare companies after representatives of a US healthcare group arrived wanting to insure their clients against medical malpractice suits and helped to write the Cayman Islands’ insurance laws.⁹

Businesses and individuals who decide to use a tax haven are encouraged to:

- open bank accounts to receive income earned elsewhere and to settle bills incurred elsewhere, often using a credit card registered in the tax haven

- set up companies that do no real trade in the haven itself
 - set up trusts to own and manage assets located elsewhere.
- Regulations against money-laundering require tax-haven financial services companies to enquire where the funds they manage come from. But there is little evidence that these regulations are used in any effective way, as a UK government audit of the British Crown Dependencies found in 2008.¹⁰ The report comments on the low number of suspicious-activity reports in a number of smaller financial institutions, saying this low number indicated that ‘some financial institutions either do not know or monitor their customers sufficiently, or are unaware of their obligations to report.’

Vaduz, capital of Liechtenstein, a tax haven where financial secrecy was penetrated after a former bank employee sold a list of account-holders



Argentina

Argentina knows only too well the damaging effect tax havens can have on a country’s economy. In the late 1990s corrupt officials used tax havens to hide the huge amounts of money they were looting from the nation’s coffers.

In 2001 a client of Citibank in Buenos Aires secretly filmed a meeting at which a bank official offered to help him take money out of the country illegally. After all, said the official, he did the same for many customers.¹²

The video was shown on TV as an economic crisis

began gathering speed that was to lead to soaring unemployment and the country defaulting on its bonds, but it took an overwhelming tragedy several years later to goad the authorities into action.

After 200 people died in a fire at a Buenos Aires disco, survivors revealed that emergency exits had been sealed shut. As crowds took to the streets in January 2005 to demand justice for the dead, the hundreds of injured and the bereaved, manslaughter proceedings were started against the man who appeared to be the club’s owner.

When investigators began probing, however, they discovered that in all the documents relating to the club, the alleged owner was merely listed as the club’s ‘administrator’.

The real owners of the club and the disco company, on paper at least, were corporations registered in neighbouring Uruguay, a tax haven, under the name of a 70-year-old local frontman who had no money of his own.

The Inspector General of Justice for Buenos Aires, Ricardo Nissen, decided it was time to act. Directives were issued banning any company registered offshore

from trading in Buenos Aires unless it could be proved it was genuinely engaged in business activity in the country where it was registered.¹³ Absolute transparency was also demanded as to the identity of the real owners and beneficiaries.

It is thought that the Buenos Aires authorities are the first worldwide to have attempted to tackle comprehensively the principle of secrecy that underpins tax havens.

Many havens do not regard tax evasion as a criminal offence in the first place. Most have finance intelligence units that are supposed to be called in if money laundering is suspected. But they are not very busy. In 2007 just two cases of money laundering were detected in Jersey, according to the island’s annual police report.¹¹

Financial centres such as London, New York and Frankfurt also qualify as havens because they offer special facilities to non-residents. But their terms and conditions can be more exacting.

Many tax havens are microstates with little or no other resources, and some of them make most of their annual revenue through charging fees for their services. Such fees can be hefty – they account for half the annual revenue of the British Virgin Islands for instance – but are modest compared to the tax savings made by their clients. The cost of tax lost to governments, especially those in the developing world, is enormous.

How tax havens are used

One of the most common uses to which havens are put by TNCs is to ‘hold’ huge sums of money that in other jurisdictions would attract tax. Hence the large number of ‘holding companies’ based offshore. Havens also allow TNCs and wealthy individuals to set up ‘trusts’ into which money is paid. The identity of those paying in the money is hidden, as is the identity of those with access to it.

Holding companies

Most TNCs pay tax if profits from their subsidiaries are passed to them directly. This is because if the TNC is quoted on a major stockmarket, it will need to be incorporated in a major financial centre such as London, New York or Frankfurt, and subject to the tax laws of those jurisdictions.

To reduce their tax liability, the TNC will set up in a tax haven an intermediate ‘holding company’ owned by the parent company, but which in turn owns some or all of the parent’s subsidiaries.

All profits from the global subsidiaries will go to the holding company. In turn, the holding company will make any money the parent company needs available in the form of intra-

company loans. The parent company then pays interest on the money it has borrowed from the offshore holding company, obtaining tax relief where it is based.

Large amounts of capital in the tax haven are then at the disposal of the parent company – usually beyond the challenge of tax authorities – to invest anywhere or anyhow they like.

William Brittain-Catlin, author of *Offshore – The Dark Side of the Global Economy*, says: ‘In 2002 BP had more than US\$500m in offshore capital invested in various financial instruments to speculate on the money markets, making it as much a bank as an oil producer.’

Every TNC uses holding companies. BP uses them in the Cayman Islands for ownership of many of its subsidiaries, as does Wal-Mart Stores, the world’s largest TNC. Royal Dutch Shell has a number of companies in Bermuda; General Motors has companies both in the Cayman Islands and Barbados; ExxonMobil has holding companies in the Bahamas and the Cayman Islands; and Ford Motor Company’s reinsurance group is based in the Cayman Islands and Bermuda.

A holding company may also serve as a depository for the TNC’s intellectual property rights. These comprise patents, for which royalties must be paid, and copyrights, for which licence fees must be paid. They have either been bought by the TNC or, in most cases, have been taken out on products the TNC has itself developed.

The holding company will then charge the rest of the TNC for their use. Virgin, for instance, licenses the use of its logo to all other parts of the Virgin empire from the British Virgin Islands. Microsoft holds the copyright on most of its products for sale outside the US in Ireland.

Trusts

A trust is the mechanism through which some companies and many individuals keep their money offshore. In essence, a trust is a legal entity in which a person or entity owning wealth places it in the care of a trustee, who agrees to manage it for the benefit of other people, called the beneficiaries.

Trusts date back to the time of the Crusades, when knights wanted to ensure that their dependants were looked after while they were at war. Today, they are widely used for tax planning and to disguise where the wealth has come from, and where it goes.

Throughout the world trusts can be managed almost entirely without public scrutiny. Their existence does not have to be declared, nor do the names of the trustees have to be

on record nor do their accounts have to be published – an exception being charitable trusts in some countries, such as the UK. As a result they are the perfect mechanism for secret tax planning.

The road to ruin

For more than a century there has been an inherent contradiction in the attitude of western legislators towards tax havens. Despite their much-vaunted regard for the rule of law (and more recent concern for human rights plus the desire to help the developing world) they have allowed a financial system to develop that is wide open to abuse.

The tax havens central to the abuse did not emerge on to the world’s financial stage as a fully formed grand design that could be put to immediate use. Instead, their development was piecemeal, and they continue to evolve.

The first tax haven in recent history is believed to have been the US state of Delaware. In the late nineteenth century it offered companies that had hitherto been incorporated in New York a number of tax benefits, and regulatory advantages, if they incorporated in Delaware. One benefit was that directors and shareholders did not have to be listed.

It was the ‘Gilded Age’. With the civil war over, the population was growing and industry was expanding, and a generation of super-rich entrepreneurs, known as the Robber Barons, had emerged.

Companies flocked to Delaware, and have stayed there ever since. Today many of the world’s largest corporations have their homes in this small Atlantic seaboard state – Wal-Mart, General Motors, Ford, Boeing, Citigroup, ChevronTexaco and Coca-Cola. Those that don’t, such as ExxonMobil, IBM and General Electric, tend to have their main subsidiary holding companies there.

The use of offshore facilities by companies trading in Britain began early in the twentieth century when de Beers, the mining concern formed by Cecil Rhodes in South Africa, and the Vestey family, owner of the Dewhurst butchers chain, won legal rulings that the place of taxation for any UK company was the country in which its directors met. This paved the way for directors of British companies to meet in such places as the Channel Islands, thereby avoiding UK taxes. This situation persisted until the 1990s when it was ruled that a UK company was always taxable in this country.

The Great Depression at the end of the 1920s, which was accompanied by personal and corporate tax rises in the US, saw US capital pour into banks in the Bahamas and Panama. At the

same time, Liechtenstein emerged as a tax haven after passing a trust law designed to attract foreign investors in 1926.

Switzerland had by then emerged as a place where the wealthy of a number of European countries chose to hide their money from the tax hikes imposed by many governments after World War One to pay for reconstruction. A bank secrecy law was introduced in 1934 in Switzerland making it a criminal offence to divulge details of account holders and what they owned. The Swiss were later to claim that this was to protect the interests of wealthy Jews who were starting to suffer persecution under the Nazis. More recent research has suggested that the Swiss secrecy law was in fact drawn up to protect the great and the good of France after scandals broke about their use of Swiss bank accounts.¹⁴

According to Ronen Palan, author of *The Offshore World: Sovereign Markets, Virtual Places, and Nomad Millionaires*, it was the Suez crisis of 1956 that really set the stage for the emergence of a large number of British Crown Dependencies as tax havens, and established London as the world’s biggest financial market in the process.

The attack on Egypt by Britain, France and Israel after Colonel Gamal Nasser nationalised the Suez Canal was opposed by the US. In order to bring pressure to bear on the British government, the US immediately began selling sterling.

With the pound depreciating in value, the UK government went on the defensive, raising interest rates and temporarily restricting all sterling investments overseas. At that time the City of London was dominated by small merchant and investment banks, which were there to serve the British Empire. Unable to trade overseas, they were threatened with going out of business.

Sometime in September 1957 a new type of financial market emerged, says Palan. It became clear that the Bank of England did not regard non-residents dealing in foreign currency in London as subject to UK financial regulations.

‘It threw a life-line to the British banks, but it was also seized upon by American banks, which in the US were heavily regulated, and they started invading London,’ says Palan. ‘Then those that were not so wealthy found they could do the same thing in places like the Cayman Islands and Bermuda, which not only were under British jurisdiction, but were closer to their time zone too.’

By the early 1960s offshore havens became the ideal place to trade US dollars, which were in high demand in Europe but which could not be bought directly from the US because of

restrictions designed to limit the US external trade deficit.

The election of Harold Wilson’s Labour government in the UK in 1964 saw yet more money leave Britain’s shores. More recently, the elimination of exchange controls, the deregulation of financial markets and the internet revolution have all contributed to greater finance mobility, trebling the number of tax havens and vastly increasing the amount of money poured into them.

The way forward

Those campaigning for an end to tax havens have a long list of suggestions for ways to curb the abuse.

The key, though, is transparency. If the veil of secrecy around tax havens were lifted, many of the abuses would simply stop.

Christian Aid is joining with the campaign group Tax Justice Network in calling on governments to insist that tax havens publish full details about the owners, beneficiaries and officials of the companies, charities and trusts registered in their jurisdiction, as well as requiring that these entities’ accounts be made available for public inspection.

TNCs should be required to make country-by-country disclosure about the taxes they have paid. Only then can the developing world be sure of a fair deal.

'It's nothing short of a scandal that firms known to have either participated in crime or to have committed major breaches of financial regulations can play a part in determining how the global accountancy profession is operated and regulated.'

John Christensen, former economic adviser to the States of Jersey, who now heads the international secretariat of the Tax Justice Network

The haven experts

Headquarters of the International Accounting Standards Board, in the City of London



Every month, in a 1970s City of London office block built on the site of a Wren church destroyed in the Blitz, an august group of businessmen and women gather from around the world. Although largely unknown outside their profession – accountancy – those present wield immense power and influence.

They form the International Accounting Standards Board (IASB), a self-appointed body that devises the rules covering how companies should produce their annual accounts. More than 100 governments worldwide, including those of the UK and all other member nations of the EU, tend to rubber-stamp their findings into law.

Given the board's standing, it is pertinent to ask why it typically includes among its members former employees of accountancy firms that have in recent years paid massive sums to settle allegations of lawbreaking or the breaching of financial regulations.

The firms in question are not shady backstreet operators known only to their clients and the tax authorities. They are the 'big four' accountancy firms: PricewaterhouseCoopers, Deloitte, Ernst & Young and KPMG, which together help fund the IASB through a foundation registered in the US tax haven of Delaware.

Recent cases in which the firms have been involved include:

- KPMG forced to pay a regulatory fine of US\$456m in the US after admitting criminal wrongdoing by 'designing, marketing and implementing illegal tax shelters'.¹ It was the 'largest tax case ever filed' in US history.² As recently as March 2008 prosecutors were trying to bring charges against 13 former KPMG executives in connection with the case.³ The firm avoided indictment as prosecutors did not want to see it share the same fate as accountancy giant Arthur Andersen, which stopped trading and shed 80,000 jobs when linked to a previous tax-haven scandal.⁴
- Deloitte agreed to pay US\$50m in the US after the US Securities and Exchange Commission (SEC) found it had committed 'improper professional conduct' by failing to detect a massive fraud perpetrated by a company it audited. Deloitte neither admitted nor denied the finding.⁵ In the UK, Deloitte's financial advice business was fined £750,000 by the Financial Services Authority (FSA) for mis-selling financial products and failing to keep proper records. The FSA said the business's approach to compliance was 'wholly unacceptable'.⁶
- PricewaterhouseCoopers paid the US government US\$41.9m to 'resolve allegations' that it defrauded numerous federal

government agencies over a 13-year period.⁷ It also paid US\$2.3m to 'settle allegations' that it helped IBM pay bribes to secure US government contracts.⁸

- Ernst & Young paid the US government US\$15m for failing to register tax shelters or properly maintain lists of people who bought them.⁹ It paid a further US\$1.7m after entering into a business relationship with a software firm it was auditing, an arrangement the SEC said was 'reckless, highly unreasonable and negligent'.¹⁰ The company was banned in the US from taking on new corporate clients for six months. It was also censured by the SEC and paid US\$1.6m to settle charges that it had compromised its independence and contributed to faulty accounting by a client.¹¹
- In the UK, a tax scheme sold by Ernst & Young to retailers was called by a Treasury spokesman 'one of the most blatantly abusive avoidance scams of recent years'. He added: 'If unchecked, it would have cost our public services at least £300m per year'. It encouraged retailers to avoid paying VAT on a 2.5 per cent handling fee paid by credit- and debit-card customers.¹²
- In Italy, all four firms were fined for 'concluding agreements to substantially restrict competition on the auditing services market'.¹³

The preponderance of US cases reflects the tighter regulatory regime in the US and the greater power, and determination, of fiscal investigators to bring offenders to book.

'It's nothing short of a scandal that firms known to have either participated in crime or to have committed major breaches of financial regulations can play a part in determining how the global accountancy profession is operated and regulated,' says John Christensen, a former economic adviser to the States of Jersey, who now heads the international secretariat of the Tax Justice Network, which campaigns for transparency in international tax.

'There is an accountants' club making the rules by which they play where there should be an impartial body exercising proper scrutiny,' he says. 'Surely, given the scope for abuse within this rule-setting process, and the known practices of some of the companies involved, we are beyond the self-regulatory phase?'¹⁴

The board itself includes three members with close associations with currently three of the 'big four' accountancy firms. Its standards advisory council, which is 'committed to pursuing high-quality international financial reporting standards', includes representatives of the 'big four', as well as

Microsoft's chief accounting officer.

Microsoft was shown in a *Wall Street Journal* report in 2005 to have shifted patents and licences out of the US to its Irish subsidiary, which supplies the company's software to most of the world.¹⁵ Ireland only charges tax of 12.5 per cent on the profits to be made, while most other countries would charge more. At the time, the Irish subsidiary, based in a law firm's offices, was said to control US\$16bn of the company's assets, enabling it to avoid taxes on economic activities in many other countries.

Chartered accountant Richard Murphy, an adviser to the Tax Justice Network, says: 'After Microsoft's activities in Ireland were exposed, the company reregistered its subsidiary there as an unlimited company so they will never again have to publish their accounts.

'That's a poor commitment to transparency and accountability from a company of its size, and hardly a qualification for sitting on a body setting the rules for worldwide accounting.'¹⁶

The IASB says that in drawing up highly technical accounting standards, it wants the best technicians, and says it is not surprising that some of these are found in the biggest firms. Board members, on joining, have to sever their links with the commercial sector.

It adds that it is committed to transparency. There is a prolonged public consultation period before new standards, or changes to existing ones, are introduced, while any technical discussion involving five or more board members has to be open to the public.

It is also considering setting up a monitoring body on which representatives of organisations such as the European Commission, the Securities and Exchange Commission in the US, the International Organization of Securities Commissions and other financial regulatory bodies will be invited to serve. One of the body's duties would be to endorse trustee appointments.

Cultural differences

Christian Aid is not suggesting that the half-million people worldwide who work for the 'big four', or the many thousands of employees of smaller accountancy firms, are all by nature lawbreakers. Far from it.

But with the ease of global financial transfers today, a culture has grown up in which accountants have pushed the boundaries of what is and what is not permissible with aggressive 'tax planning'. In recent years, ever more complex

schemes have been developed and touted for sale in the business world.

A clamp down by the US and, to some extent, the UK has helped curb some of the more blatantly abusive 'schemes', but minimising tax on behalf of wealthy clients remains an integral part of accountancy, with firms dismissing any suggestion that the stratagems they devise may be socially irresponsible.

A KPMG partner writing recently in a financial magazine spelled out today's accountancy realities. 'A worrying tendency seems to have emerged among external stakeholders to make "moral" judgements about tax planning and to expect companies to manage their tax affairs in a "moral" way,' he writes.

'Let's be clear about this. Tax is a cost to business. As with any other cost, the board members owe their shareholders a duty to manage that cost by the legal means afforded to them. Where a company's tax philosophy is heavily influenced by a duty to shareholders, the focus should be on responsible management of tax cost.'

The author adds that it seems to have become fashionable to use terms such as 'aggressive tax planning' and 'unacceptable tax minimisation' synonymously with 'tax avoidance', while arguing that such practices demonstrate a lack of morality in tax matters. He argues that as 'there is no agreement on what constitutes morality either within or outside the sphere of tax' the term cannot be used to determine whether tax planning 'has crossed some illusory line'.¹⁷

Christian Aid disputes this analysis. It is fatuous to suggest that simply because different people have different views of morality, any moral critique is somehow invalidated.

Contrary to the KPMG partner's understanding, tax is not a cost for a business but rather a distribution of profit and, as such, should have no impact on the economic efficiency of firms. But it will affect the dividends a shareholder receives. Therein lies the crux of the problem. Company directors have a legal responsibility to maximise what shareholders receive.

They can therefore argue that in fact they have a legal responsibility to ensure tax liabilities are as low as possible. If other competing companies are using offshore secrecy or trade mispricing to avoid tax, the pressures on a company director or accountant to advise doing the same will be considerable.

One recent instance of KPMG planning for its clients saw it advising former US telecoms giant WorldCom that to avoid paying hundreds of millions of dollars in state taxes, it should classify the 'foresight of top management' as an intangible asset that the parent company could license to subsidiaries in

'Accountancy firms too are engaged in price-fixing cartels, tax avoidance/evasion, bribery and corruption, and money laundering...'

Professor Prem Sikka, University of Essex

return for massive royalty charges. This previously unheard-of definition led to the firm accruing more than US\$20bn in royalty charges and making huge tax savings.

KPMG collected some US\$6m for its efforts but the foresight of WorldCom's top management was clearly not that good, for the company then went bust.¹⁸ Richard L Thornburgh, a former US attorney general, who was appointed to investigate the subsequent bankruptcy, concluded that KPMG 'likely rendered negligent and incorrect tax advice' to the company, for which, he believed, the accountancy firm could be held liable.¹⁹

It wasn't the only criticism KPMG has attracted. In October 2002, the US Senate Permanent Subcommittee on Investigations of the Committee on Governmental Affairs began an investigation into 'the development, marketing, and implementation of abusive tax shelters by accountants, lawyers, financial advisors and bankers'.²⁰ The investigation included an in-depth look at four schemes run by KPMG.

Senator Carl Levin, who headed the inquiry, said when the findings were published: 'Our investigations revealed a culture of deception inside KPMG's tax practice.'²¹

An email his team obtained showed that a KPMG tax adviser had engaged in cost-benefit analysis of a potential breach of the rules, and decided that the financial rewards outweighed the penalties. The executive had noted that even if the regulators took action against their sales strategies over a tax shelter known as the Offshore Portfolio Investment Strategy (OPIS), the 'average deal... would result in KPMG fees of US\$360,000 with a maximum penalty exposure of only US\$31,000'.²²

In the UK, the company was found to have cold-called firms in an attempt to sell a tax-shelter scheme it knew would be disallowed. In its marketing prospectus, it said it believed HM Customs and Excise would challenge the arrangement as 'unacceptable tax avoidance'. However, the prospectus said, a similar scheme for telecommunications 'ran for nearly four years... before the EU amended primary legislation and stopped the concept'. In 2005 the European Court of Justice described the new scheme as 'unacceptable'.²³

The giant E, insignia of US energy group Enron, outside its headquarters in Houston, Texas. Its lopsided appearance was prescient – the company went bankrupt when it was discovered that huge losses had been hidden offshore

A critic writes

Prem Sikka is professor of accounting at the University of Essex and an acknowledged expert on accountancy firms' abuses. He says it is the rewards to be made from TNCs that have caused many of the problems.

More than 50 of the 100 largest economies in the world are corporations, not countries, with the five largest having combined sales greater than the gross domestic product (GDP) of the poorest 46 nations. The combined sales of the top 200 corporations, meanwhile, are bigger than the combined economies of all countries other than the ten most economically successful, and account for more than a quarter of world economic activity.²⁴

The accountancy firms that have helped engineer the emergence of the major corporations have grown into major players themselves in the process, and are now so large and powerful that the US\$80bn combined global income of the 'big four' alone is exceeded by the GDP of only 54 nations.²⁵

'Elected governments and host communities may be interested in eradicating poverty, promoting education, healthcare and human rights, but corporations may not necessarily share those goals,' says Professor Sikka.

'In the search for competitive advantage, they have shown that they are willing to indulge in price-fixing, bribery, corruption, money laundering, tax avoidance/evasion and a variety of antisocial activities that affect the lives of millions of citizens.

'Accountancy firms too are engaged in price-fixing cartels, tax avoidance/evasion, bribery and corruption, and money laundering,' he says.²⁶



Despite their social power, he adds, accountancy firms are generally not subjected to 'the disclosure requirements applicable to equivalent companies or public-sector bodies'.

He warns that looking to standard-setting agencies such as the IASB to provide benchmarks for their accountability is unlikely to be productive as 'major firms often provide finance and personnel to such agencies and are able to stymie threatening developments'.

Domestic and international auditing standards, meanwhile, are currently silent on the social obligations of accountancy firms.

'Against the background of comparative secrecy, relatively weak liability, accountability, regulatory, moral and ethical pressures, accountancy firms have become key players in the contemporary enterprise culture and have shown a willingness to indulge in questionable practices not only to increase their clients' but also their own profits,' says Professor Sikka.²⁷

Clearly, accountancy has come a long way from the days when the Monty Python team lampooned it as 'desperately dull and tedious and stuffy and boring and des-per-ate-ly DULL'.²⁸

The other facilitators

It is not only the accountancy firms, however, that facilitate aggressive tax planning. Banks are also key players, as was noted in a report earlier this year by the Organisation for Economic Co-operation and Development (OECD), which states: 'Much aggressive tax planning involves the use of financial instruments...The more sophisticated the transaction, the more sophisticated the financing may need to be. Those instruments are largely obtained from banks.'²⁹

In late 2001 US company Enron, one of the world's leading suppliers of electricity and natural gas, went bankrupt after shares plummeted when a leading financial analyst questioned the reliability of its reported earnings. It was subsequently discovered that the company had lied about its profits, and concealed debts and losses offshore so they did not show up in the company accounts.

An inquiry by the US Senate Joint Committee on Taxation into what happened stated that Enron 'excelled at making complexity an ally'.³⁰ Many transactions used 'exceedingly complicated structures' drawn up on the advice of 'sophisticated and experienced lawyers, investment bankers, and accountants'. Banks named as having provided their services included Chase Manhattan, Deutsche Bank, Citigroup and JP Morgan Chase and Co.

The US Senate Permanent Subcommittee on Investigations of the Committee on Governmental Affairs looked into abusive tax shelters, examining four KPMG schemes.³¹ It concluded that they could not have worked without the participation of banks.

Deutsche Bank, HVB Bank and UBS Bank were named as providing 'billions of dollars in lending critical to transactions which the banks knew were tax-motivated, involved little or no credit risk, and facilitated potentially abusive or illegal tax shelters'. NatWest was named in the same report as providing credit lines totalling more than US\$1bn.³²

Lawyers, too, were identified in the report as key players in the tax-haven industry.

The activities of 'some large, respected [US] law firms' were also highlighted, with one found to have 'provided legal services that facilitated the development and sale of potentially abusive or illegal tax shelters'.³³

'The real issue is that these tax concessions are obscene. Why should companies in SEZs pay no tax, while in India we still don't have money for universal schooling?'

Jayati Ghosh, professor of economics, Jawaharlal Nehru University, New Delhi

India: tax-break winners and losers

Landless labourers work in the fields in Jhajjar district in Haryana state, where Reliance Industries plans to develop a Special Economic Zone (SEZ). Landless labourers will get no compensation for losing their source of income



'This foregone tax revenue would be enough to feed each year the 55 million people who go to bed hungry in India every day.'

Aseem Shrivastava, economist

Bhagaban Soy, a 25-year-old Indian farmer, died trying to prevent his land from being taken over for a huge steel works.

He was shot by police when they fired into a crowd of local farmers protesting against the building of the plant by Tata, one of India's biggest companies, in the poor east Indian state of Orissa in January 2006.

He was taken to hospital by the police, where his mother alleges his hands were chopped off. He died later the same day.

'When we got his body back, both his hands were missing,' says his mother Sini Soy, 50. 'I am so angry at what happened. My son laid down his life for a cause and that must be honoured. My house and small piece of land are in the area where Tata wants to build its factory. But we will not sell – we will not dishonour his memory.'

Villagers in the area echo her feelings against Tata, which wants to build a 3,000-acre steel plant in the Kalinga Nagar industrial area.

A total of 14 people died in the shootings, after which the plan was put on hold. But locals believe the steel plant will go ahead.

Rabindra Jarika, a farmer and head of the local association opposing the plant, says they do not want to end up like other tribal people displaced by nearby factories and Special Economic Zones (SEZs) – areas governed by special rules to facilitate investment (including foreign direct investment) for export-oriented production. SEZs are free-trade zones owned and operated by private companies that are given generous tax holidays and unlimited duty-free imports of raw, intermediate and final goods.

Orissa is India's poorest state.¹ Says Mr Jarika: 'Tribal people (known in India as *adivasis*) are very attached to their land. It cannot be bought with money or gold. We have seen the situation of the people displaced by eight other factories and SEZs near here and it is very bad. They have become beggars after being driven out. We are sure the government will apply force to snatch our land and property but we are prepared to fight them. Even if they kill 14,000 people we will not succumb.'

Biggest profit-makers get tax holidays

SEZs are new to India (although Export Processing Zones existed previously) but have quickly caused controversy partly because of the kind of violence seen in Kalinga Nagar, as well as in Nandigram in the state of West Bengal, where at least 40 people reportedly died in 2007 during protests against a planned chemical industry SEZ.² One state – Goa – has even banned SEZs because of large-scale protests.

Activists say farmers are being forced off their land with little or no compensation to make way for big corporates building factories and industrial parks. Displacement is not a new phenomenon in India: as many as 60 million people have had to leave their homes since 1950 because of development projects, including huge dams such as the controversial Narmada dam project in central India. Many have been 'simply left to fend for themselves without assistance from the state that displaced them'.³

Many activists who support farmers fighting to keep their land concede that development will inevitably involve switching land from agricultural to industrial use. They campaign for better policies on resettlement and rehabilitation for those who lose their land or income.

Meanwhile, the companies operating within SEZs are given huge tax breaks. Those doing so, or planning to do so, include some of the biggest profit-making firms in India – such as Reliance, Jindal Steel, Infosys and Tata – as well as big international names such as Nokia. Tata's revenues in 2006-07, for instance, were £14bn – equivalent to some 3.2 per cent of India's gross domestic product (GDP).⁴

These companies get total tax exemption for the first five years, 50 per cent for the next two years and up to 50 per cent exemptions on profits that are reinvested for another three years.⁵

The tax exemptions also apply to activities in the non-processing area of the SEZs, which could be up to 50 per cent of the area of large zones. This implies that if shopping malls, amusement parks, residential homes or other luxury amenities are created in the non-processing part of the SEZs, they will not be taxed.

It is not only activists who believe that the tax breaks within the SEZs are an outrageous kick in the face to the poorest people in India, where, according to the UK's Department for International Development (DFID), up to 400 million people live in extreme poverty on less than US\$1 a day and more than 900 million on less than US\$2 a day.⁶

The Indian Finance Ministry has estimated SEZs will contribute a loss of 1,600bn rupees (£20bn) in tax revenue until 2010, thanks to exemptions from customs duties, income tax, sales tax, excise duties and service tax. This foregone tax revenue would be enough to feed each year the 55 million people who go to bed hungry in India every day, according to Aseem Shrivastava, an independent economist researching SEZs.

The current Finance Minister P Chidambaram has said the tax concessions should be scrapped, and has other reservations about SEZs. He wrote to cabinet colleagues outlining his concerns. 'SEZs per se will distort land, capital, and labour cost, which will encourage relocation or shifting of industries in clever ways that can't be stopped. This will be further aggravated by the proliferation of a large number of SEZs in and around metros [India's main urban areas];⁷ he said.

But India is pressing ahead with the SEZ policy, which was passed by Parliament in 2005, with 439 zones formally approved and 138 approved in principle.⁸ In contrast China now has only six large export-oriented industrial areas. Unlike in China, SEZs in India are privately owned and operated.

Commerce and Industries Minister Kamal Nath says the SEZs will create four million jobs,⁹ badly needed in India, which has high rates of unemployment (7.2 per cent in 2007¹⁰) and a fast-growing population. He believes SEZs will attract foreign direct investment (FDI), enable the transfer of modern technology and create incentives for infrastructure. The tax issue is an unjustified fear, he adds, as the income that is not taxed would not be generated in the first place without the attraction of the SEZs.

But others do not see the need for SEZs in India's already booming economy.

'India had high rates of growth before the SEZs were introduced, so why do we need them? In any case, much of the investment in SEZs is likely to be at the expense of investment in the rest of the economy,' says Arun Kumar, professor of economics at Jawaharlal Nehru University (JNU) in New Delhi. 'Some companies may even close down in other parts of the country to reinvest in an SEZ where they get the tax concessions. Why would any company want to work outside an SEZ now?'

Professor Kumar also believes there will be an increase in smuggling of cheaper goods from the SEZs to the rest of the country, resulting in further tax revenue losses. 'The resultant revenue losses will aggravate the deficit in the budget and result in cutback in expenditure. Most of these cuts tend to be in the social sectors, which will worsen the situation for the poor.'

Some companies have been able to get SEZ status for an existing plant, negating the argument that the purpose of an SEZ is to attract investment and create employment. This has been the case for the Essar and Adani SEZs, in Gujarat, among others, according to Manshi Asher, an independent researcher and activist documenting the impacts of SEZs. A large number of tax

Sini Soy, whose son was killed by police firing during protests against Tata's plan to build a steel plant in Jajpur district in Orissa



concessions for the software industry are due to expire in 2009 and many IT companies are trying to get SEZ status to continue their tax holidays. Mr Shrivastava asks: 'What is the point of retroactive SEZ status apart from solely to give the company tax concessions? It cannot possibly be to generate jobs.'

Only seven MPs took part in the debate when the SEZ Act was passed on May 9 2005, and some activists believe the law is unconstitutional. 'The legislation is very clever. All the laws of the land apply, but Clause 49 empowers government to suspend the application of the constitution should it get in the way of the SEZ,' says Mr Shrivastava. 'In effect the Act is unconstitutional and is being challenged in the courts by a number of farmers' groups.'

India's booming economy leaves many behind

The Indian economy is booming, with a growth rate of 8.7 per cent last year (2007-08), against 9.6 per cent and 9.4 per cent in the previous two years respectively. If these rates of growth are sustained, India will be the world's fourth-largest economy within 20 years.

Indians are justifiably proud that their country is now being talked of in the same breath as China as an emerging world economic superpower. Newspapers are filled with reports of the soaring stockmarket, Indian companies taking over western rivals, and the massive success of the hi-tech sector in creating jobs for the emerging middle classes.

But levels of poverty in India are staggering. One in three of

the world's poorest people live in India.¹¹ A quarter of global child deaths, one fifth of global maternal deaths and one fifth of all new cases of tuberculosis occur in India.¹² The child malnutrition rate in India is double the African average.¹³

The progress made by India will have a significant effect on whether the world as a whole is able to meet the eight United Nations Millennium Development Goals (MDGs). These range from halving extreme poverty to halting the spread of HIV/AIDS and providing universal primary education, all by the target date of 2015. The proportion of people living on less than US\$1 a day has been decreasing, but not fast enough to meet the MDGs target, according to DFID. Even meeting the target would still leave around 250 million people in poverty by 2015. India is likely to meet the primary education targets, but is lagging behind on health-related MDGs.

The poverty rate among the most marginalised communities – such as dalits, those at the bottom of India's caste system, and tribal people – remains very high. Activists, including Christian Aid, are concerned that even if India were to realise its MDGs, the plight of these people will not be addressed.

Some economists claim that India's rapid economic growth will eventually trickle down to help to lift millions out of poverty. However, others believe that while the upper and middle classes are reaping the benefits of the economic boom the poor are becoming poorer.

'People are much poorer than the government statistics indicate,' says Professor Kumar. 'Incomes may be rising, but many services are proportionately more expensive, so net poverty is increasing. Take healthcare for example. A study in Kerala (a southern Indian state) showed that between 1987 and 1996 there was a 326 per cent rise in health costs for the richest, but the rise for the poorest was 768 per cent.¹⁴ The nature of poverty is also changing. The poor are moving from rural to urban areas. So what they used to be able to get from the land is not available to them now. Urban poverty is much harsher.'

Jayati Ghosh, also a professor of economics at JNU and director of Christian Aid partner organisation International Development Economics Associates (IDEAs), says the tax concessions in SEZs amount to huge subsidies to big industrial companies.

'People are rightly upset about the land-grabbing going on for SEZs. But we have to face the reality that there is going to be change in land use as India develops. What is important is how you compensate and rehabilitate those people who were on the

land and what you do with that land,' says Professor Ghosh.

'The real issue is that these tax concessions are obscene. Why should companies in SEZs pay no tax, while in India we still don't have money for universal schooling? We spend only 4 per cent of GDP on education, instead of the aimed-for 6 per cent. If we had full payment of existing taxes we would have enough money to properly educate our children or for a public health centre in every village.

'To give up such a huge amount of government resources is of course a major crime given the needs of Indian society today and in future. But once again, what is at stake is more than the revenue losses, enormous as they are. Providing such massive tax giveaways encourages investors to shift their production from other locations to SEZs, in order to benefit from the tax holiday. This means no net benefit to the economy from additional investment, since it is simply moving from other areas.'

Professor Ghosh concedes there is no guarantee that greater tax revenues will automatically benefit the poorest. 'In terms of getting more tax revenue, there are two questions that need asking: will the regime allocate it and will the money reach those it is intended for? These are good questions. But if we do not have the resources in the first place then we don't have the money to allocate. There is a strong lobby for SEZs in government and from corporations. We are told India has no choice because China is doing this. But China is not giving these kinds of concessions.'

India is biggest recipient of UK aid

During a visit to India in January 2008, UK Prime Minister Gordon Brown announced a new package of aid for India worth more than £825m over three years, with £500m of that dedicated to health and education. The money will train 300,000 new teachers and build 300,000 new classrooms, meaning four million more children will receive an education.

India is the largest recipient of aid from the UK with £234m from DFID in 2006-07 and about £1.04bn given over the past five years (more than 90 per cent of this goes to the national or state governments). However, these figures pale into insignificance when compared to tax revenues lost through the SEZs of £20bn to 2010.

While Christian Aid welcomes the vital British aid to India, activists say it would be better if India could use funds generated by taxes from its own profit-making companies to help people out of poverty. The Indian government in 2004



Christian Aid/Stuart Freedman

pledged to raise public spending in education to at least 6 per cent of GDP, but this has not yet been achieved.

'The Indian government is giving away to companies, both Indian and multinational, amounts in foregone taxes that are many times the amount in aid that the British government is presenting to India,' says Professor Ghosh.

For example Reliance Industries, India's largest private-sector company with profits of US\$2bn (£1.1bn) in 2006, will get away with contributing nothing to the exchequer wherever it operates within an SEZ.¹⁵ In the Jhajjar district of Haryana state, close to New Delhi, Reliance Industries has permission for a 'multi-product' SEZ in the district that will displace 20-25,000 people. It is thought it will be the largest SEZ in the country at 25,000 acres (10,121 hectares).

In 2007 the government made changes to the SEZ policy in response to criticism, including limiting the area to 5,000 hectares, and formulated a comprehensive resettlement

A steel works dominates the skyline in Jajpur district in Orissa where Tata wants to build a new steel plant on the land of local farmers

and rehabilitation policy, according to which one person from each displaced family should be given a job. The necessary legislation, however, has yet to be passed, while recent newspaper reports indicate that the government will lift the 5,000 hectare limit.¹⁶ Reliance has anyway got around the size limit by splitting its SEZ into two parts.

Satpal Numbardar, 55, from the village of Badli, which is in the Reliance SEZ area, grows wheat and mustard on his 12 acres of land, which have been handed down through the generations. 'Reliance wants to buy this land, but I don't want to part with it,' he says. 'What would be the benefit for me? What is the benefit of the SEZ? The corporates get tax rebates but the common man won't get anything. Even if the government and Reliance try to make us leave, we will not. We will protest

'Big business is grabbing the land from the farming community, and farmers are becoming landless and poor.'

Ramesh Sharma from Ekta Parishad, a Christian Aid partner

the same way as others have done. We will do anything to protect our land. What else can I do apart from farming?'

Fellow farmer Azad Singh, 70, from nearby Nimana village, has 26 acres of land. 'This is the most fertile land in Haryana. If farming land is gone there will be grave shortages of food. You can't eat money. Farming is my ancestral profession and I will hand it down to my sons. Reliance came to see me but I told them to leave. These people are lying. They might give us work for one or two years then they will throw us out. People from outside will get the jobs. We are ready to protest and we are ready to die for this.'

Of great concern is the fact that landless labourers, who will lose their income if the SEZ is built, will receive no compensation at all. Even Indian government officials admit (off the record) that it is outrageous that those who do not own land – already the most vulnerable and often tribal people and dalits – get no compensation.

Birmati, 50, from the village of Pelpa, earns about 100 rupees (£1.25) a day as a labourer in the fields. 'If the SEZ comes we will have nothing. We have no land so we do not get any compensation. Reliance will not employ us. At least now we have work and we get paid.'

Christian Aid partner organisations work to help the rural poor, particularly the landless, in their struggle to acquire or keep their small pieces of land from being taken by big business. In 2007 Christian Aid partner Ekta Parishad organised a 200-mile march of 25,000 people from central India to New Delhi to demand the government give land to the landless and form a land plan for the country.

'Eighty per cent of SEZs are located on prime agricultural land and this is directly affecting the food security of the country, which can only get worse as more SEZs open,' says Ramesh Sharma of Ekta Parishad. 'Big business is grabbing the land from the farming community, and farmers are becoming landless and poor.'

Subsidies for the rich

India's policy of a favourable tax regime for corporates continued in the 2008 budget, with Professor Kumar estimating that subsidies given to the corporate sector through concessions on income tax, corporate tax, excise duty and customs duty now equal 2,780bn rupees (£34.7bn) each year.

'In contrast, the direct subsidies to the poor, like on food, employment guarantee schemes and housing, do not amount to 500bn rupees (£6bn). The disparity is glaring considering that the

subsidy to the corporate sector will benefit about 1 per cent of the population while the subsidy to the poor is shared by about 50 per cent of the population. Continuing with the SEZ policy and not announcing any changes in it is also continuing the massive concessions granted to the corporate sector,' he says.

'Given the situation of the poor, a lot more needs to be done but the government is not even able to fulfil its own expenditure targets. For instance, we are far from the goal of 6 per cent of GDP on education. We are not close to achieving at least 3 per cent of GDP on health.

'This year, rather than garner more resources for substantially increasing the help to the marginalised, the government continues to give up resources by giving (or continuing) tax concessions to the well-off.'

Tax holiday on the beach

SEZs and corporate tax subsidies are not the only way that companies in India avoid paying tax. Many companies turn to the tiny Indian Ocean island of Mauritius.

It is hard to believe that Mauritius, with a population of just 1.3 million and best known for its lagoons and palm-fringed beaches, is the biggest foreign investor in India. It accounts for nearly half of all FDI inflows to India.¹⁷ From April 2000 to December 2007, FDI inflows from the island republic stood at US\$20.1bn (£10bn), nearly 45 per cent of total inflows of nearly US\$51bn (£26bn) during the period.¹⁸

This is not because Mauritius in itself is an overpowering economy, rather because the island is an ideal route for investments into India. Most of the money flowing through Mauritius is from companies operating in India, who register an office on the island precisely in order to avoid paying tax.

The Double Taxation Avoidance Act (DTAA) between India and Mauritius means Mauritian tax residents without a permanent establishment in India are not taxed in India on capital gains from the sale of shares of an Indian company. This allows Mauritian tax residents to avoid capital gains tax of between 10 and 40 per cent, which would be payable under domestic Indian tax laws.

Companies can establish Mauritian tax residency under the DTAA simply by obtaining a tax residence certificate from the government of Mauritius, which requires that at least two directors are resident in Mauritius, a bank account is maintained in Mauritius and a Mauritius auditor is appointed.

Indian tax officials say the treaty costs the exchequer more than 40bn rupees (£500m) each year in foregone revenue.¹⁹

Ahead of the Indian budget in February 2008, officials from both countries met in the Mauritian capital, Port Louis, to look at changing the terms of the treaty. India is pushing to move from a residence-based system of taxation to a source-based system, meaning that investors from Mauritius would need more than a pro forma registered office on the island to qualify for tax breaks.

India has offered to compensate Mauritius for the losses if the treaty were to be renegotiated, with some newspaper reports saying it offered 5bn rupees (£62m). Analysts believe India would find it politically difficult to end the treaty.

Vodafone goes to court

However, the Indian government is fighting back in other ways against what it sees as a charade of offshore tax avoidance. It has demanded that Britain's Vodafone, the world's largest mobile phone company, should pay what lawyers estimate could be US\$2bn (£1bn) in capital gains tax on its US\$11bn (£5.6bn) acquisition of Indian mobile phone operator Hutchison Essar last year, from the Hong Kong-based group Hutchison.

Vodafone argues the transaction took place between offshore entities owned by itself and Hutchison and was outside India's jurisdiction. It also argues any tax liability lies with the Hong Kong group as the seller, not with Vodafone as the buyer.

The Indian tax department is seeking to show that since most of the assets were in India, the deal is liable for Indian capital gains tax. It also argues that under Indian law, the buyer is required to withhold any capital gains tax liability and to pay it to the treasury if the seller cannot be taxed.

In essence, India is arguing for a source-based rather than residence-based capital gains tax system, which means that a transaction is taxed where it happens rather than where the person undertaking it is located. India is arguing that the value of the deal was made in India by Indian consumers buying and using mobile phones, and that India should get a return on this through capital gains tax.

Vodafone has appealed to the Bombay High Court against the tax demand. According to court papers seen by Christian Aid, the Indian government argues that: '...the contention that [the] transaction took place outside of India by a non-resident with another non-resident in respect of the transfer of shares of a company which is also a non-resident and consideration is paid and received outside India is too simplistic [an] assertion... It may also be noted that the companies located in the Cayman Islands and Mauritius were primarily incorporated to hold the

shares of HEL [Hutchison Essar Limited]... these companies are no more than fictional entities.'

On 11 March 2008 the case was adjourned by the Bombay High Court until 23 June this year, because the Indian government has introduced an amendment to the Finance Bill in its annual budget. Once passed by Parliament, this would allow it to demand capital gains tax from the buyer rather than the seller if the seller cannot be taxed. Vodafone argues that this amendment shows it was not liable as the buyer under existing Indian law.

India's case against Vodafone is particularly ironic as Gordon Brown has included Vodafone on a list of 20 of the world's biggest multinational companies recruited to help him put the international community back on course to achieve the UN MDGs by 2015.

Richard Murphy, an adviser to the Tax Justice Network, says the case has massive implications, not only for India.

'Companies are watching this closely and will not like what the Indian government is doing at all. But India is counting on the fact that companies cannot afford to ignore the massive Indian market,' he says.

'Vodafone may win on a technicality to do with the new amendment but if the Indian government wins, it could bring about a radical shift away from tax avoidance. Why should it be that because a company is registered in the Cayman Islands or Mauritius no tax is due?'



Farmer Rabindra Jarika is refusing to sell his land to Tata, which wants to build a steel plant in Orissa. He says: 'Even if they kill 14,000 people we will not succumb'

‘Broad taxation, to a far greater extent than either aid or natural-resource revenues, obliges the state to invest in the creation of a relatively reliable, uncorrupt, professional-career public service to assess and collect dues and then hand them over to the state treasury.’

Mick Moore, professorial fellow at UK-based independent research charity the Institute of Development Studies

Why paying tax is good for you



Christian Aldi/Paul Boes

Out of reach: Angola's oil riches, lying just offshore, fail to benefit most of the population

Secrecy and bribes are the twin curses of countries in the developing world that are rich in natural resources. Together they ensure most citizens see precious little benefit from the oil or minerals extracted.

The lack of transparency about the deals struck between the transnational corporations (TNCs) and the politicians and government officials responsible for the country's natural wealth serves the interests of both parties at the negotiating table.

The mining or drilling companies do not have to reveal publicly the price they are paying for commodities extracted. The state representatives they deal with – their goodwill bought by bribes – can without fear of exposure agree terms that may be greatly disadvantageous to their country.

The corruption goes far beyond the payment of a few backhanders. All too often it ends up corroding the country's entire body politic. It is no accident that developing countries with the greatest abundance of natural resources have the worst forms of governments: tyrannical and corrupt.

Governments that are able to function thanks to monies made from natural resources, without having to look elsewhere for funds, are effectively accountable to no one but themselves, and will often use their unearned wealth to keep matters that way.

The states most susceptible to what has been called the 'resource curse' are those that lack the institutions necessary to counter endemic corruption, such as an apolitical police force, independent judiciary, free and fair electoral process and an unfettered press.

Mick Moore, professorial fellow at UK-based independent research charity the Institute of Development Studies, says that cross-national statistical analysis shows that natural resource wealth tends 'consistently' to depress the level of democracy.¹

'Governments sitting on large mineral wealth want to stay in power and naturally assume that plenty of other people are keen to displace them, probably by force,' he says. 'That motivates high expenditures on military, police, intelligence services, the general militarisation of politics and exclusionary governance.'

Impoverished countries, of course, attract aid, but research has shown that aid can also damage the social fabric, making states more accountable to donors than to their citizens.

The money means that recipient governments are under much less pressure to maintain popular legitimacy and are therefore less likely to cultivate and invest in effective public institutions. A 'strong president, weak parliament' syndrome

can develop, political accountability is distorted and patronage practices reinforced.

Tax revenues can and should be used to benefit the population as a whole. Norway, for instance, pays revenue from its North Sea oil into a social fund for the future from which old-age pensions will be met. Alaska routinely pays its citizens dividends from money paid by oil and gas companies.

Such schemes may be inappropriate in poorer countries where capital is scarce, but if companies paid royalties and taxes in a transparent manner, civil-society organisations could bring pressure to bear on governments for money to be properly invested in infrastructure, health and education.

In a bid to counter the unholy alliance of big business and corrupt officialdom in the developing world, the Extractive Industries Transparency Initiative was launched in 2002 to encourage companies to be open about the payments they make to governments.

Its aim is to allow a country's population to monitor the benefits supposedly accruing from the extractive industries and enable civil-society organisations to uncover any corruption in the use of the revenues. Crucially, however, companies still do not have to reveal how much profit they make or how much they pay in taxes.

No taxation without representation

The political landscape changes in countries where government revenues are largely derived from the taxing of citizens in a fair and equitable way.

Rulers dependent on taxes have a direct stake in the prosperity of some or most of their citizens, and 'therefore have incentives to promote that prosperity', says Moore.²

He adds: 'Broad taxation, to a far greater extent than either aid or natural-resource revenues, obliges the state to invest in the creation of a relatively reliable, uncorrupt, professional-career public service to assess and collect dues and then hand them over to the state treasury.'

Citizens being taxed, meanwhile, will engage politically, either by organising to resist taxation or to ensure their tax money is well used. Unless the sole response of the state is to crush resistance 'these reactions tend to increase the accountability of governments'.³

Recent research pooling data from 113 countries between 1971 and 1997 found evidence that it was the need for greater tax revenue that forced governments (even authoritarian ones) to democratise.⁴

The finding that citizens who are taxed become more engaged politically does not take account of those who, once wealthy, seek to protect their fortunes through tax minimisation. But it does underline one of the most important characteristics of what a tax system can and should deliver. These are known as the four Rs.⁵

- **Representation:** by paying taxes, people not only contribute to building a strong state that can deliver development but they also become agents in the process of development – holding governments to account for the way the money is spent and, over time, supporting the emergence and strengthening of democratic structures. Direct taxation of incomes and profits has been shown to be the major channel in this process.

- **Revenue:** governments need taxes to provide systems of health, education and social security. They are also necessary as the basis for a successful economy through regulation, administration and investments in infrastructure.
- **Redistribution:** taxes should reduce poverty and inequality, and ensure that the benefits of development are felt by all.
- **'Re-pricing':** taxes can be used to deal with related social problems, for example, taxing carbon emissions to tackle climate change or taxing tobacco to limit damage to health.

Democratic Republic of Congo: an abundance of mineral riches has led to years of conflict and corruption. In 2006, the government reportedly received just US\$86,000 from mineral rights



Lisney Adenro/Corbis

Systemic failings

It is not solely the activities of TNCs and corrupt governments that are denying the developing world a future.

Rich governments and international financial institutions lending or donating money are also playing their part in keeping poorer countries trapped in a cycle of poverty. In their case, however, it is not through the search for profits or criminality but rather through a lack of understanding about the workings of the economies in which they dabble.

Developed countries have a long history of seeking to influence the way taxes are raised in nations that owe them money. In Egypt in 1878, when the country was saddled with enormous foreign debt, a British tax expert was imposed as Minister of Finance.

Within two years, British companies had grabbed 70 per cent of the country's trade.⁶

So it has been ever since, with the experts on hand generally reflecting the economic hue of whichever country they happen to come from. In the early 1980s, with Britain and the US championing the open market, those countries to which they were providing loans and assistance were told that money was conditional on them, too, embracing free enterprise.

The economics of wealthy countries do not suit all economies. Nonetheless, there is a consensus among richer nations as to how the developing world should levy tax. The three main components of this consensus are:⁷

1. **Tax neutrality.** The tax system should not distort production or consumption decisions, a doctrine that leads inexorably to trade liberalisation, which can be inappropriate in vulnerable economies.
2. **Tax expenditure.** Low-income countries have been advised to impose VAT on expenditure rather than raise income. This has resulted in deepening inequality. For example, it is estimated that the poorest in Brazil spend 26.5 per cent of their income on VAT, while the richest spend 7.3 per cent.⁸ International Monetary Fund (IMF) researchers have shown that countries advised to use VAT to recoup revenues lost through the lifting of trade tariffs were only able to replace around 30 per cent.⁹ Furthermore, a just use of VAT presupposes that governments will use financial transfers, such as benefits, to compensate the poor for the new levies. Low-income countries, however, notably much of sub-Saharan Africa, simply do not have the wherewithal to provide such support to their poorest citizens.

3. **Set an unambitious target for tax revenues.** The consensus says that governments should aim to raise 15-20 per cent of their gross domestic product (GDP) through tax, although revenues in the EU-15 average in excess of 30 per cent.¹⁰ By setting the bar so low, there has been little pressure on the rich elites in poor countries to contribute more to the economy, and little incentive for governments to bring that pressure to bear. Revenues have failed to climb above around 10 per cent of GDP in many low-income countries compared to more than 40 per cent in the UK.

Christian Aid believes there should be a fundamental reassessment of tax policy by donors, including the World Bank and IMF, if there is to be any chance of the United Nations Millennium Development Goals being met.

Governments in the developing world must be allowed to implement tax regimes appropriate to their circumstances if they are to achieve the protection, infrastructure and basic services needed to create the right kind of environment for sustained development.

In the words of the campaign group Tax Justice Network: 'The whole range of issues referred to in the Millennium Development Goals cannot be tackled unless developing countries secure their own tax revenues.'

'This will free them from aid dependence, and help countries determine their own futures and chart their own route out of poverty. Securing the revenues might at the same time create the political accountability that is the other essential component in this process.'¹¹

'The price of minerals is very high at the moment, but the country is basically giving away gold, copper and silver, as it did in previous centuries.'

Father Miranda of Health Houses, a local health and education non-governmental organisation in Peru

Peru and Bolivia: a tale of two tax systems

A worker stoops to pick asparagus in Ica, Peru. Despite the heat, she is completely covered, to protect herself from sunburn and from skin irritation caused by insecticides



Christian Aid/Ana Cecilia Gonzalez-Vigil

'Sometimes my children cry when I go in the morning, and I feel so bad. But what can I do? There just isn't enough money if I don't go out to the fields,' says Wilma Tarqui. She is describing the daily 4am ritual of leaving her two small children with the neighbour who looks after them until she returns from the asparagus fields 12 hours later.

Like many of her neighbours, Wilma came to the coastal region of Ica, in Peru, from the mountains of Ayacucho, where the civil war with Maoist rebels in the 1980s and '90s was at its most intense. Thousands of people fled to the coast to build a new life.

This influx of people coincided with a decision in the US to subsidise the fledgling asparagus industry in Ica, ostensibly to encourage alternatives to the cultivation of coca, the raw material for cocaine. In 1991, the US lifted the tariff on asparagus imports, opening an enormous new market for the premium vegetable, which local entrepreneurs have now effectively cornered.¹

In 2000, legislation was passed in Peru to encourage the asparagus industry even more. Law number 27360 stipulates a profits tax rate of just 15 per cent for agricultural exporters, which is half the national average paid by other industries. Agrokasa, the largest Peruvian asparagus company, has seen its asparagus exports grow rapidly over the past ten years. In 1998, it exported 67,163 boxes weighing 5kg each, compared to 2.67 million in 2007.²

Nearly all the asparagus sold in Britain, apart from the produce of a very short English growing season in May and June, is now flown in from Peru.³ This year-round supply and relatively cheap production costs have made asparagus one of Peru's most successful agricultural exports. The Ica region, the centre of the country's asparagus industry, now accounts for 40 per cent of Peru's total agricultural production.⁴

This expansion helped increase Peru's economic growth by 10 per cent last year.⁵ But tax breaks, combined with a lack of political will to redistribute wealth, mean that very little of this new prosperity reaches the poorest people in Ica, those who need it most. In fact, some health indicators in Ica linked to poverty indicate a worsening situation. The number of children with chronic malnutrition has doubled since 2002 to 15 per cent, and Ica now has the second-highest incidence of tuberculosis in the country.⁶

Throughout the developing world, affordable healthcare and education are among the most pressing needs of the poor. The UK government is prioritising aid in these areas as

part of its commitment to the Millennium Development Goals. The prevailing view among donor governments and lending institutions has been that private-sector development is the best way to fuel improvements in these areas.

Campaigners in Peru point out, however, that strong growth and export figures do not necessarily mean improved living conditions for the poor. The asparagus boom in Ica is a case in point. In Ica, the positive macroeconomic figures hide the fact that the exports boom is not improving the lives of the poorest: they are forced to work in sub-standard conditions.

Labour Programme of Development is a local non-governmental organisation that has carried out a detailed study of the asparagus industry. Spokesman Jorge Choqueneira says: 'Extreme poverty is far from being eradicated and the region is even further from achieving the Millennium Development Goals.'

Health crisis

Victoria Sardon runs the government health centre for the district of Señor de Luren, where Wilma and her family live. Children are often left alone in their houses to fend for themselves while their parents work in the fields, she says. 'When children are left alone, sometimes they simply don't eat. It is the biggest health concern we have in this area.'

In the shantytown near the clinic, a group of three children ranging in age from two to nine years, sit on a piece of carpet laid down on the bare earth. Their 'house' is a flimsy structure of canvas pieces stretched across an insubstantial wooden frame. They are sharing a bowl of watery soup. The eldest, Luz Marina Chacoca, says both their parents work in the fields picking grapes until six in the evening. She is at school in the mornings, but comes home at lunchtime to keep her siblings company.

In the nearby town of Huánuco, there are more than 500 families, but just four nursery schools catering for a mere 36 children.

In August 2007 the region of Ica was struck by an 8.0 magnitude earthquake. More than six months on thousands of families are still living in makeshift shelters constructed out of donated canvas and straw mats. The government's rebuilding efforts have been extremely patchy.

Father Jose Manuel Miranda, who runs a medical charity called Health Houses, which is supported by Christian Aid, says: 'There is very little thought given here to the most marginalised people. Public investment in roads and services rarely reaches the poorest.'

Health Houses provides dispensaries and laboratories to test for common illnesses. It has also helped with building materials for more nurseries and play parks in the poorest communities.

Elizabeth Patcheco lives near Wilma in the San Martin settlement in the Señor de Luren district. Sitting on her bed, which rests on bare earth inside the ubiquitous temporary canvas structure, she says: 'We don't really have enough money, even with both of us working. I try to buy milk for the children when I can, but we cannot afford red meat, only chicken occasionally.'

Now 26, Elizabeth had her first child aged 17 and has had two more since. Her youngest is two. Between them she and her husband each earn 120 soles (£22) a week. Paying a neighbour to look after her children costs 25 soles (£4.50) a week.

'We have to struggle to keep going. I'd like to start over in Chile, but I cannot leave my children until they are older,' she adds. Things are even tighter at the moment because her husband has tuberculosis and is not able to work.

Monica Misayco also works in the asparagus fields. She is 23 and has two sons aged three years and eight months. She had to stop working for the birth of her second son and returned

when he was six months old. Like nearly everyone else in the community, she leaves her children with neighbours from 4am until she returns at about 4pm.

Apart from the back-breaking work, the conditions in which the family live are far from healthy. 'When the rain falls, it makes the bed wet,' says Monica. She has gallstones and doctors say she should have them removed. But the operation costs 500 soles (£91), which is about a month's wages – far more than she can afford. She also has problems with her appendix. 'The doctor says if it ruptures, I could die,' she adds.

A rich seam

Peru's mining industry is less visible to UK consumers than its asparagus exports, but in economic terms it is far more important. The country is the world's second-largest producer of silver and the sixth-largest producer of gold and copper. It is also a major producer of zinc and lead.⁷

Elizabeth Patcheco has just returned to her makeshift house in an earthquake-damaged shanty town after 12 hours, working in the asparagus fields of Ica, Peru. Her wages are vital as her husband can't work because he has tuberculosis



Christian Aid / Ana Cecilia Gonzalez-Vigil

'The tax regime is terribly generous to the mining companies. If you are paying no royalties, then basically you are getting the sub-soil and its materials for free.'

Professor Anthony Bebbington, Manchester University

The mining industry now accounts for more than half the country's export revenues and, especially as the world price of minerals soars, it has the potential to contribute hugely to Peru's economic development. World prices of copper have roughly quadrupled over the past ten years, while those of gold and silver have trebled.⁸

However, there is a growing sense that the country is not getting a fair share of the rapidly rising value of its mineral wealth. Critics argue that foreign mining companies are doing extraordinarily well out of Peru's mineral deposits, while a large proportion of Peruvians remain in extreme poverty.

Grupo Propuesta Ciudadana (Citizen's Advocacy Group) is a Peruvian pressure group that this year published an extensive study into the mining industry. It says that the country is allowing itself to be seriously short-changed. 'We have proved that the companies are getting the largest benefit from the extraordinary profits and the state must find a way of taking a larger share of these revenues,' says the report.⁹

In 2007, Peru's total mineral production was worth some £11bn. The tax revenue from mineral production was £2bn.¹⁰ At 17 per cent, this was significantly less than Peru's standard profit tax rate of 30 per cent.

An analysis of the profits from the Yanacocha mine – the second-largest gold mine in the world – shows the kind of money the mining companies have been making. In 2007 it cost US\$345 to produce an ounce of gold,¹¹ which by March this year was worth US\$1,000.¹² With costs of 35 per cent, and taxes of 17 per cent, it would appear that the company's after-tax profits amounted to 48 per cent of total mining revenue.

Richard Murphy, a chartered accountant and senior adviser to the campaign group Tax Justice Network, says: 'It is obvious that there is something seriously wrong [in Peru]. No mine should be getting a 48 per cent after-tax profit rate. If they are, the balance of rewards in Peru is inappropriate.'

Many countries in the developing world would rather obtain revenues from the mining industry by imposing royalties on the market value of a company's production. Profit taxes are more difficult to collect because profit figures can be easily manipulated.

But unlike other countries in Latin America that have successfully secured royalty rates of 50 per cent and more, Peru has allowed mining companies to pay between 1 and 3 per cent, with most companies negotiating exemptions from even that low rate.

Professor Anthony Bebbington of Manchester University worked with the Peru Support Group, a Christian Aid partner organisation, in 2007 to compile a report into mining and development. The report warns that 'Peru is essentially giving away its resources.'¹³

'The tax regime is terribly generous to the mining companies,' says Professor Bebbington. 'If you are paying no royalties, then basically you are getting the sub-soil and its materials for free.'

Mining profits became an issue in Peru's 2006 presidential election campaign, when candidate Alan Garcia pledged to renegotiate the government's contracts with mining companies. However, after becoming president, he argued that any renegotiation would cause legal problems for the country.

Most of the biggest mining firms operating in Peru are thought to have 'legal stability contracts' with the government, which effectively exempt them from paying any further royalties for at least ten years. Instead of renegotiating the contracts, President Garcia announced that mining companies would be asked for a 'voluntary contribution' of 3 per cent of their after-tax profits while mineral prices remain high. It will generate some revenue for the government – an estimated US\$175m in 2007.¹⁴

But this 3 per cent seems like a drop in the ocean given that the market value of Peru's mineral production has soared by several hundred per cent over the past few years. Mineral prices will not remain high forever and the deposits are finite – they will eventually be fully exploited.

'The price of minerals is very high at the moment, but the country is basically giving away gold, copper and silver, as it did in previous centuries,' says Father Miranda of Health Houses.

The problem of relying too heavily on profits tax is further highlighted by two lengthy disputes between Peru's tax authorities and Barrick Gold Corporation, a Canada-based company, which runs two gold mines in Peru. In September 2004, the company won its appeal in the Tax Court of Peru against a tax demand of US\$32m. However, Barrick is now involved in a new dispute with SUNAT, Peru's tax authority, which is demanding US\$49m in taxes it claims are owed for the years 2001 to 2003, plus interest and penalties of US\$116m. The company is appealing against the demand to the Tax Court.¹⁵

If world mineral prices remain at an historic high, then questions about whether Peru is getting a fair deal from mining companies are not going to go away.

'We have been sitting on a throne of gold and putting our hands out for charity. Charging a fair price to extract our natural resources is a lot fairer.'

Pastora Condorena Ticona, a community worker in El Alto, Bolivia

Bolivia: a different way

Next door to Peru, Bolivia had adopted a much more aggressive approach to tax collection after it was discovered that there were 24 trillion cubic feet of natural gas reserves under the soil.¹⁶ The estimated value of this resource in the current market is US\$228bn (£114bn). In 2006, Bolivia exported US\$2.03bn (£1.03bn) worth of gas.¹⁷

After centuries of seeing its tin, silver and gold reserves mined by foreign concerns that took most of the profits abroad, the discovery of yet another extremely valuable commodity in the poorest country in South America sparked a political movement for change. A groundswell of Bolivian public opinion was mobilised by Evo Morales, who was elected president in December 2005 with a mandate to renegotiate contracts with the hydrocarbons industry.

The most significant change was the increase in the percentage of royalty charged on gas exports. Previously, oil companies operating in Bolivia, including British Gas and BP, were charged royalties under a complicated system. The average amount paid was 25 per cent of the value of gas pumped, though this percentage was falling every year.¹⁸

Morales signed decree number 28701 to the Hydrocarbons Law, creating a new system requiring nearly every field to pay a 50 per cent royalty. By raising the royalties charged, the total amount of tax collected in Bolivia rose from 15bn bolivianos (roughly £1bn) in 2005 to 23bn bolivianos (roughly £1.5bn) in 2007. The amount coming into the treasury from gas royalties rose from 15 per cent to 26 per cent of total revenues.¹⁹

Roberto Ugarte, vice-minister in charge of taxation in the Bolivian finance ministry, says it was a conscious decision to increase the level of royalties in comparison with profits taxes. He agrees that oil and gas companies generally favour profits taxes because it is relatively easy to disguise profits. It is not so easy to disguise the amount of a commodity that is being pumped, explains Mr Ugarte. 'Before we passed the new tax law, almost all the companies were declaring losses,' he says.

The profits tax charged to the hydrocarbons sector has remained unchanged, at 25 per cent.

In the Bolivian mining sector, which has also seen enormous windfalls as the prices of precious metals climb ever higher on the world market, the government adopted a different approach. Instead of raising the royalties, since December 2007 the government has imposed a windfall-profits tax of 12.5 per cent on top of the existing profits tax of 25 per cent, to garner some more revenue from the most productive mines.

Clearly, the extra revenue from hydrocarbons and minerals taxes has given the fledgling Morales government more resources to address social problems. As its electoral base was largely drawn from the poorest sections of society, it had a strong political incentive too.

Progress on poverty

Bolivia is South America's poorest country with 70 per cent of its 8.4 million inhabitants living in poverty and 25 per cent malnourished.²⁰ It is too early for United Nations statistics to reflect improvements in rates of tuberculosis and malnutrition across Bolivia. But Martha Mejia, a paediatrician working for a branch of the UN World Health Organization in the Bolivian capital of La Paz, says there has definitely been a paradigm shift in the way local authorities are addressing the health needs of the population. Local health posts are now handing out nutrient packs to families, containing vitamin and mineral supplements, to combat malnutrition.

'The government definitely seems to be on the right track. It is better than many other countries where I have worked,' says Dr Mejia. Statistics for La Paz show that both chronic and acute malnutrition have fallen since the year 2000.²¹

The new gas tax revenue is also paying for a new form of child benefit to those attending primary school. At 200 bolivianos (£13.50) a year, the Juancito Pinto payment does not seem like a great deal of money, but for the poorest it makes a difference. Albertina Quispe has four children aged between 6 and 17. She says it means she can buy better-quality notebooks for her younger children and put something away for Christmas presents. Living in El Alto, the sprawling slum above La Paz where many migrants from the countryside have settled, is not easy. At nearly 4,000 metres above sea level, it is a forbidding place. Albertina has two nieces aged six and nine who were orphaned at a young age and now live with their grandmother, her mother. At first the family could not afford any furniture for the girls, but the Juancito Pinto gave them enough money to buy a bed.

Government figures suggest that primary-school enrolment rose by nearly 10 per cent between 2006 and 2007 as a result of the cash incentive.²²

On the brink

The Bolivian approach to oil and gas taxation is not universally popular, however. Affluent Bolivians, who are not so reliant on state benefits, fear that higher taxation will deter overseas

investors. Because of the huge investment involved in exploration, there is a great deal of foreign involvement in the sector. Along with Brazilian and Spanish companies, British Gas and BP have substantial investments in Bolivian fields.

The oil companies warn that it is becoming less profitable to invest in exploration, so production is likely to fall in the medium term. It is certainly the case that production is falling short of demand already, says Carlos Arze, a gas-industry expert at the Research Centre for Agrarian and Labour Development, a La Paz thinktank that Christian Aid supports.

But this is mainly because of a game of brinkmanship being played by the transnational companies, he adds. Although it would be highly profitable for them to pump more oil, they are in no hurry to do so. They believe that if they wait long enough, it will put pressure on the government to negotiate more favourable terms.

Reluctantly, at the eleventh hour, most of the companies signed operating contracts with the Bolivian state company Yacimientos Petroliferos Fiscales Bolivianos (YPFB). But the transnational companies operating in Bolivia are highly critical of the regulatory and distribution role now played by YPFB.

Ronald Fessy Malaga, spokesman for the Camera Boliviana de Hidrocarburos (a professional body representing drilling companies), sums up the prevailing attitude: 'To fly a plane you need a pilot, not a gardener. If this problem can be solved, the industry will fly like a plane again in five years' time.'

There is some justification for this attitude: a series of forced resignations at high levels in YPFB in the early days of the Morales government seriously held up crucial exploration projects.

But the political will to improve the lives of the poorest cannot be denied. Another significant innovation paid for with the new gas revenues is a much-improved state pension. The Morales government introduced La Renta Dignidad, which was paid monthly from age 60 and amounted to 2,400 bolivianos a year (£160).

Previously, the state pension was 1,800 bolivianos (£120) a year, payable in a lump sum annually from age 65. With average life expectancy in Bolivia also standing at 65, significantly more people are able to claim the new benefit. There are currently 676,009 Bolivians receiving La Renta Dignidad, compared with the 488,561 who received the previous pension.

The difference of £40 a year may seem insignificant, but the Bolivian minimum wage is 550 bolivianos (£38) a month and many of the poorest subsistence farmers earn much less than that. It is also much easier to budget when you get a monthly payout.

Miguel Querta Callegas used to be a builder. But at 78 years, he found it hard to get work. So he turned to shoe-shining in El Alto. As a builder, Miguel earned about 1,200 bolivianos (£80) a month. Shining shoes, he can earn little more than 80 bolivianos (£5) a month, or £60 a year. So the £160 he gets annually from La Renta Dignidad, instead of £120 from the previous benefit, makes a significant difference. His 80-year-old wife is at home. The couple could not survive independently without La Renta Dignidad. The burden of looking after them would fall on their children.

Tula Cordova, 64, lives with her granddaughter and has just started receiving the pension. As her husband died three years ago, it is very important, allowing her to pay her way. Under the previous system, she would have received nothing until she reached 65.

Before the government revised the state pension, it was not uncommon for families to abandon their elderly relatives, says Pastora Condorena Ticona, a community worker in El Alto.

'We have had a long struggle to get back the rights to our natural resources. Many people have died along the way. But it is finally being recognised that Bolivia is a rich country.'

She speaks for many of the poorest when she says: 'We have been sitting on a throne of gold and putting our hands out for charity. Charging a fair price to extract our natural resources is a lot fairer.'



Miguel Querta Callegas, 78, used to be a builder, but no one will hire him now. He shines shoes in El Alto, the shanty town above La Paz, Bolivia, to earn what he can. The new pension, made possible by the rise in gas revenues, helps him and his 80-year-old wife to survive

Until international steps are taken to curtail these aspects of global finance, poorer countries will remain stuck in the poverty trap, unable to pursue effective tax policies that would help them break free.

Recommendations



The City of London. The International Monetary Fund identifies it as a tax haven

Massive amounts of money are leeching from the developing world each year by businesses engaged in aggressive tax avoidance schemes and tax evasion. Two methods of evasion alone – transfer mispricing and falsifying invoices – involve sums that, if taxed, would raise US\$160bn a year in revenue.

This is several times larger than the extra US\$40-60bn the World Bank estimates poor countries will need annually to meet all the United Nations Millennium Development Goals (MDGs), which aim to halve poverty by 2015.¹

The sum is also more than one-and-a-half times the amount the developing world receives each year in aid. In healthcare alone, at current spending patterns in poor countries, the revenue would save the lives of an estimated 350,000 children under the age of five each year, 250,000 of them babies.

This draining of money is allowed to go unchallenged because of the permissive regulatory climate surrounding global transfers of cash into jurisdictions offering financial secrecy ('tax havens'), and the ability of international businesses to exploit the limited capacity of domestic tax authorities.

Until international steps are taken to curtail these aspects of global finance, poorer countries will remain stuck in the poverty trap, unable to pursue effective tax policies that would help them break free.

It will take considerable political will on the part of the UK and Irish governments to address the range of ways in which corporate tax evasion drains the resources of the developing world, but we believe both countries are ideally placed to take a lead in rectifying a situation that has been described as tantamount to a modern slave trade.

The UK itself, recently identified as a tax haven by the International Monetary Fund (IMF), must cease to be an obstacle to international financial transparency. It is directly or indirectly responsible for around half of the world's tax havens. As such, it must lead multilateral action to require automatic exchange of information between tax havens, countries from where the money has originated, and the countries where the companies and individuals who use tax havens are resident.

Ireland has in recent years stepped up its development contribution through aid. While this is welcome, it highlights an inconsistency in that country's development policy because, at the same time, Ireland has transformed itself into an international structure that facilitates tax dodging. To resolve this contradiction, Ireland should also now take a lead in addressing the disastrous effects of this structure on poorer countries.

The loss of cash that should be taxed is not the only

obstacle to the economic development of poor countries. Donor governments and international financial institutions have in recent years imposed a highly restrictive 'tax consensus' that has prevented countries from choosing tax systems most appropriate to their needs.

This consensus includes trade liberalisation, lower taxation for foreign investors and the imposition of VAT, which latter feature hurts the poor most. It has demonstrably failed to deliver revenues, wealth sharing or an improved political climate.

Christian Aid believes that the creation of effective and fair taxation systems in the developing world is the only way that poor countries can end their dependence on aid and stand on their own feet economically. Tax revenue, compared to monies from all other quarters, including profits from finite natural resources, is recognised as the only sustainable way of funding development.

Effective taxation is also key to raising the sums of money necessary to achieve the MDGs. And fair (as opposed to coercive) taxation has a fundamental part to play in building a strong state and making it accountable to its citizens, thereby helping ensure genuine political representation and good governance.

In this area too Christian Aid calls on the UK and Irish governments to lead the way in calling for a comprehensive reassessment of the 'tax consensus'. For our part, we will continue to work with civil-society organisations in poor countries in supporting effective taxation systems, and in demanding greater accountability from governments and greater transparency about commercial transactions. We will support their efforts to resist the tax consensus.

Action by the UK and Irish governments to be taken unilaterally

- Assess the problem: both governments to commission their own studies into the scale of illicit capital flows in general and of those due to tax evasion in particular, with a special emphasis on the role played by their own jurisdictions and institutions in facilitating capital flight and tax evasion from the developing world.
- Make the hiding of profits impossible: to promote an international accounting standard that requires companies to report what they do on a country-by-country basis. Their published accounts must show a breakdown of economic activity, including profits made and taxes paid, in every jurisdiction where they operate, without exception.

- Repatriate illicit wealth: the UK and Ireland should lead efforts to ensure the repatriation of existing illicit wealth, the handling of which is corrupt in itself. A system must be put in place – as called for by both the Commission for Africa and the UN Convention Against Corruption – to ensure that all assets held by banks in Britain and Ireland are scrutinised for origin, and that information on those found to be owned by the residents of developing countries is conveyed to the respective governments. UK and Irish financial institutions must be required to disclose the relevant information and cooperate in the repatriation of these assets, or face prosecution.
- Require banks to disclose the ownership of all foreign entities to which they supply services so that this information might be exchanged with the countries in question.
- Promote the use of ‘general anti-avoidance principles’ in tax to challenge the creative abuse of the tax system by lawyers, accountants and bankers, nationally and internationally.
- Require individuals to sign all import and export invoices to say they are correctly priced – with risk of personal prosecution if they are not.
- Press for reform of the International Accounting Standards Board so that it is taken out of private control and given international agency status, and so that it includes members who do not represent the interests of the financial community.

Action by the UK and Irish governments to be taken multilaterally

- Both governments should support the Organisation for Economic Co-operation and Development in its efforts to regulate tax havens, demanding automatic exchange of relevant information. All havens must be required to participate and sanctions must be imposed on those that do not actively cooperate.
- Action at a European Union level could also make an important contribution to the development of an international order of financial transparency. One possibility, alongside other measures to promote global transparency, would be to extend the EU Savings Tax Directive in three ways: so that it includes not only individuals but also companies and trusts; so that it includes all forms of income, not only interest; and so that it applies to secrecy jurisdictions outside the EU as well.
- Technical assistance should be provided to developing countries, where requested, to help them address trade mispricing problems.

Action the UK and Irish governments should take to challenge the tax consensus

The UK’s Department for International Development and Irish Aid should lead a reassessment of tax policy by donors, including the World Bank and IMF, to which both governments generously provide funds.

- The reliance on VAT that has been forced on countries must be revisited immediately.
- The failure to consider revenue effects of trade liberalisation must also be addressed, with low-income countries able to replace only 30 per cent of their lost revenues. The continuing negotiation of Economic Partnership Agreements must explicitly take this into consideration.
- The uniform demand by donors for reduced business taxation (especially for foreign businesses) should stop.
- The principle of self-determination of tax policy for poor countries should be established and respected by donors, reflecting the fundamental importance of this to the strengthening of state-citizen relationships and effective political representation.

Technical appendix

Every year some 10 million children under five die in the developing world, seven million of them babies. They die because of disease, malnutrition and lack of safe drinking water, but ultimately because of poverty and the absence of an effective state that can provide the type of healthcare and other services that the western world takes for granted.

The ability of governments in the developing world to tackle high infant mortality rates and other poverty indicators is extremely limited without the economic resources to implement beneficial change.

The fact that so many economies remain on their knees is due in no small part to a lack of tax revenue. This is a state of affairs for which tax evaders in the business world, who leech money that could otherwise have been used to save lives, bear much of the blame.

Christian Aid estimates that since the United Nations Millennium Development Goals (MDGs) were set in 2000, the developing world has lost an estimated US\$160bn a year in tax revenues as a result of transfer mispricing within transnational corporations and false invoicing between business accomplices. That is significantly more than the amount of development aid given each year during the same period.

If current levels of tax evasion continue unchecked, by 2015 – the deadline for the delivery of the MDGs – the tax-revenue losses will total US\$2.5 trillion. This figure is based on the value of the dollar in the year 2000, adjusted for inflation, and only covers money lost through transfer mispricing and false invoicing.

We cannot assume that if this tax had been paid, the revenue would have been devoted entirely to saving children’s lives. However, we can estimate the approximate effect of changes in tax revenue on mortality, using data from developing countries. In other words, we can estimate the relationship between taxes and death.

If we look at the data for 1960-2006, we gain a conservative estimate of the long-term relationship between the two factors. A higher estimate of the association between death and taxes emerges from the 2000-2006 figures.

By applying the estimates to the period 2000-2007 we can show that the revenues lost to transfer mispricing and false invoicing could have prevented an estimated 350,000 children under five from dying each year, including up to 250,000 infants.

This appendix briefly sets out the methodology used to measure the association between tax revenues and under-five and infant mortality rates, and shows how we reached an

estimate of US\$160bn of revenues lost each year to transfer mispricing and false invoicing.

Table 1 shows the calculation of tax losses due to commercial tax evasion, using transfer mispricing and false invoicing. These two forms of evasion are estimated to account for about 7 per cent of global trade transactions each year. We combine this figure with World Bank figures about the volume of trade and corporate tax rates in order to calculate the implied loss of tax revenues. As Table 1 shows, the losses are highest in the poorest countries, and range from around 14 per cent of existing tax revenues in low-income countries, to 10 per cent in upper-middle-income countries.

Table 2 shows the regression results used to obtain the tax-mortality associations, and the regression analysis is discussed in detail below. Finally, Tables 3a and 3b show the calculations of mortality impact, using the estimated tax loss and tax-mortality associations. Data on total mortality rates is added to see how our estimates imply they would fall if the taxes evaded by companies through trade were both (i) available to governments and (ii) spent in similar proportion and with similar association with outcomes to those observed during 1960-2006, and during 2000-06.

The implied potential reductions in infant and under-five mortality range is as high as 6.5 per cent and 7.1 per cent respectively. From the high-end estimates we show that 250,000 infant deaths a year are potentially avoidable by stopping abusive transfer pricing and false invoicing. Looking at all children under the age of five, a total of 350,000 deaths a year are potentially avoidable on this basis. Scaled up for the full MDGs period (2000-15) and assuming no change, this implies that 5.6 million children under five – four million of them infants – will die unnecessarily as a result of tax evasion through trade alone.

Mortality is highly complex. A full analysis would necessarily contain a wide range of variables, including disease factors (such as HIV prevalence), economic performance, inequality, weather and harvest conditions, governance indicators, measures of government expenditure patterns (for example, on public healthcare) and health-related outcomes (for example, level of medical skill of those present at births). Such an analysis is beyond the scope of this piece of work.

Instead, we estimate a simpler model that allows for the effects of income levels (GDP per capita) and of the ratios to GDP of aid flows and of tax revenues. In this way we aim to capture the approximate relationships of national income and of the main components of development finance. We use data

from the World Bank's World Development Indicators (WDI) throughout.

Our goal is to gain some insight into likely effects, all else being equal, of increasing tax revenues. Rather than take a simple correlation between these and mortality rates, we use a panel of data to carry out a simple regression to distinguish more clearly between the associations in countries at different income levels.

We use fixed-effects regressions to emphasise associations within particular countries, rather than the differences between countries. In this way we hope to get closer to seeing the associations that might hold if revenues were increased in particular individual countries – with their existing standards of governance, political preferences for expenditure and so on.

We expect to find that income level is strongly (negatively) associated with mortality rates, both directly and by acting as a proxy for broader aspects of development. No clear association is expected for aid; while it may have an impact in reducing mortality it may also have been targeted at those countries with higher existing mortality rates, which will complicate the relationship. Finally, we expect a strong negative relationship with tax/GDP, both as a direct indicator of the finance available for revenues and as an indicator of the general capacity of the state to meet basic requirements.

Regressions (1a) and (2a) in Table 2 confirm these hypotheses for infant and under-five mortality respectively. The results for GDP per capita and for the tax/GDP ratio are significant at the 2 per cent and 5 per cent levels respectively.

Given that the relationships may work more fully over time – that is, current period revenues may not have an immediate effect on mortality, but rather build over time as investments in, for example, healthcare capacity work have a delayed impact – we re-estimate the model with five-year lags of each variable. Regressions (1b) and (2b) show the results for infant and under-five mortality respectively, which are reassuringly similar in each case. The importance of the tax/GDP ratio is stronger relative to that of GDP per capita in this specification compared to the previous one.

To obtain the low-end estimates for mortality impact (see Tables 3a and 3b), we use the coefficient on the tax/GDP ratio in regressions (1b) and (2b) to calculate the implied marginal sensitivity of mortality rates.

To obtain high-end estimates we examine data for only the MDGs period (2000-06), and, rather than estimate the full model, we test only the association between mortality and tax/

GDP ratio. We divide the countries into one group of low- and lower-middle-income countries, and another of upper-middle-income countries, to address income differences, and obtain the results in the last four columns of Table 2.

By regressing such a simple model only, and for the short period, we are not addressing issues of causality but rather – by using fixed-effects regressions again – drawing out the correlation within countries between tax/GDP and mortality rates. We expect to find a weaker relationship in upper-middle-income countries, but a strong one in the group of poorer developing countries. We also expect that the results may suggest a stronger effect of tax/GDP than in the previous regressions, potentially because of omitted variable bias but also because it is to be hoped that development efforts in the more recent period have been more strongly concerned with reducing mortality rates than over the last half-century as a whole. There is however a risk that the smaller number of observations renders the regression weak and the association insignificant.

The results confirm the main hypotheses, and both the strength of the association and the significance of the findings with regard to the poorer countries is supported. We are then able to use this, in the lower half of Tables 3a and 3b, to generate our high-end estimates for the mortality impact of the missing tax revenues – assuming that such average associations are maintained.

Finally, a caveat should be noted. The data is drawn from the standard source, the World Bank's WDI. The scant coverage of even the most basic tax variables is a reflection of the neglect that this issue has suffered for too long in development circles. As a result, the number of observations is limited.

The International Monetary Fund (IMF) has a dataset, Government Financial Statistics, which contains much more detailed tax data and greater coverage. Sadly however, they do not make this freely available for either country researchers or those interested in this type of broad panel analysis. The value of making this freely available – in terms of potential transparency and accountability impacts – might well be thought to outweigh any financial return to the Fund from sales.

Christian Aid is working with partners including the Tax Justice Network to create a database that will provide much fuller coverage. We are also in correspondence with the IMF on the question of their dataset's availability.

This piece of work should eventually be replicated, once a full tax database is available, to confirm the associations

indicated here. Work using a fuller specification would also be valuable, to confirm the robustness of these results. What this exercise has generated is a relatively robust long-term association between tax/GDP and mortality rates, and an estimate of the more recent association for the period 2000-06. We do not attribute direct causality to the latter, but use it to estimate the potential mortality changes that might be associated with a particular increase in revenues.

In this way – using both the more robust causal regressions and the more recent short-term associations – we have been able to generate with some confidence a range of estimates of the potential mortality impact of the tax revenues lost to

evasion by businesses through abusive trade practices.

This is an area of work that has been neglected in econometric analysis, perhaps largely due to the difficulty of obtaining comprehensive data, and Christian Aid plans considerable further work on these issues. Christian Aid would welcome discussion of this work, including suggestions for possible sources of tax data and for technical collaboration.

Table 1: Estimation of tax losses

| Line | | Low-income countries | Lower-middle-income countries | Upper-middle-income countries | Developing country total | |
|------|--|----------------------------------|-------------------------------|-------------------------------|--------------------------|----------------|
| [1] | Ratio of total trade volume to tax revenues | 6.50 | 6.18 | 5.85 | | |
| [2] | Corporate tax rate | Per cent | 31.2 | 30.2 | 25.0 | |
| [3] | Tax/GDP ratio | Per cent | 13.6 | 16.1 | 17.6 | |
| [4] | Total tax revenues | US\$bn | 158.0 | 531.5 | 638.6 | |
| [5] | Tax lost to false invoicing and abusive transfer pricing | Per cent of current tax revenues | 14.2 | 13.1 | 10.2 | |
| [6] | | US\$bn each year | 22.4 | 69.6 | 65.3 | 157.3bn |

Notes

[1] Average by group for 2000-06, calculated from trade/GDP and tax/GDP ratios; WDI data.

[2] Higher marginal corporate tax rate, average by group for 2000-06; WDI data.

[3] Average by group for 2000-06, calculated from tax/GDP ratios; WDI data.

[4] Calculated as average tax/GDP by group for 2000-06, times group GDP in constant year 2000 US dollars, adjusted for inflation to year 2008 dollars.

[5] Using Ray Baker's 'conservative estimate' that 7 per cent of trade volumes is illicit capital movement, by false invoicing between unrelated parties and by abusive transfer pricing within multinational groups, which lies behind the total dirty-money estimate of US\$1.6 trillion as quoted by the World Bank. Calculated as 7 per cent of line [1], multiplied by line [2], which gives the tax due on the illicit capital moved via trade, as a percentage of current tax revenues.

[6] Line [5] as a share of line [4].

Table 2: Regression results

| | Long-term relationships, 1960-2006 | | | | Short-term relationships, 2000-06 | | | |
|--|------------------------------------|------------------------------|--------------------------|------------------------------|-----------------------------------|------------------------------|--------------------------|------------------------------|
| | Infant mortality (1a) | Under-five mortality (1b) | Infant mortality (2a) | Under-five mortality (2b) | Infant mortality (3a) | Under-five mortality (3b) | Infant mortality (4a) | Under-five mortality (4b) |
| Independent variables (in natural logs) | | | | | | | | |
| | | | LIC/LMIC | UMIC | LIC/LMIC | UMIC | | |
| GDP per capita (year 2000 US\$) | -19.30 (-7.32)*** | -29.25 (-4.52)*** | | | | | | |
| Aid/GDP (%) | 0.93 (1.93)* | 1.83 (1.32) | | | | | | |
| Tax/GDP (%) | -5.58 (-2.04)** | -10.21 (-1.85)* | -18.18 (-2.59)*** | -1.20 (-0.85) | -25.71 (-2.21)** | -2.03 (-0.96) | | |
| GDP per capita (year 2000 US\$), five-year lag | | -16.42 (-4.35)*** | | | -20.73 (-2.7)*** | | | |
| Aid/GDP (%), five-year lag | | 0.76 (1.39) | | | 1.70 (1.17) | | | |
| Tax/GDP (%), five-year lag | | -7.51 (-2.36)** | | | -14.78 (-2.59)*** | | | |
| Constant | 195.96 (10.46)*** | 179.45 (6.98)*** | 299.03 (6.85)*** | 248.33 (4.81)*** | 95.95 (5.22)*** | 17.97 (4.48)*** | 135.36 (4.42)*** | 26.10 (4.29)*** |
| R-sq: within | 0.35 | 0.28 | 0.31 | 0.27 | 0.26 | 0.02 | 0.23 | 0.05 |
| R-sq: between | 0.64 | 0.55 | 0.62 | 0.53 | 0.10 | 0.00 | 0.07 | 0.00 |
| R-sq: overall | 0.66 | 0.61 | 0.58 | 0.54 | 0.11 | 0.00 | 0.07 | 0.00 |
| Observations | 255 | 182 | 203 | 157 | 68 | 62 | 65 | 40 |
| Countries | 87 | 72 | 84 | 72 | 48 | 23 | 48 | 22 |

Notes

All regressions are fixed effects to capture the relationship between tax and mortality within countries. All data is from WDI. Significance of results is indicated by asterisks: *** significant at 2 per cent level, ** at 5 per cent level, * at 10 per cent level.

Table 3a: Total infant mortality impact

| Line | | Low-income countries | Lower-middle-income countries | Upper-middle-income countries | Developing country total |
|-------|--|----------------------|-------------------------------|-------------------------------|--------------------------|
| [7] | Infant mortality rate (Per 1,000 live births) | 78.9 | 34.4 | 27.4 | |
| [8] | Total infant mortality, 2000-07 (Millions) | 43.1 | 10.3 | 3.0 | 56.3 |
| | Low-end estimate | | | | |
| [9a] | Infant mortality impact of additional tax revenues (Per 1,000 live births) | -1.0 | -0.9 | -0.7 | |
| [10a] | Per cent | -1.3 | -2.7 | -2.7 | |
| [11a] | Potential fall in infant mortality: total, 2000-07 (Millions) | 0.5 | 0.3 | 0.1 | 0.9 |
| [12a] | Projected fall in infant mortality: total, 2000-15 (Millions) | 1.1 | 0.6 | 0.2 | 1.8 |
| | High-end estimate | | | | |
| [9b] | Infant mortality impact of additional tax revenues (Per 1,000 live births) | -2.4 | -2.2 | -0.1 | |
| [10b] | Per cent | -3.1 | -6.5 | -0.4 | |
| [11b] | Potential fall in infant mortality: total, 2000-07 (Millions) | 1.3 | 0.7 | 0.0 | 2.0 |
| [12b] | Projected fall in infant mortality: total, 2000-15 (Millions) | 2.6 | 1.3 | 0.0 | 4.0 |

Notes

[7] Average by group for 2000-06, calculated from WDI data.

[8] Line [7] scaled up for eight-year period 2000-07.

[9a] Historic impact of tax revenues on infant mortality. Implied sensitivity of mortality rate from panel regression analysis of data for all developing countries, 1960-2006.

[10a] Line [9a] as a percentage of line [7].

[11a] Line [10a] scaled up for eight-year period 2000-07.

[12a] Two times line [11a], ie total for 2000-15 assuming annual rate is constant to 2015.

[9b] Recent association of tax/GDP ratio with infant mortality. Implied sensitivity of mortality rate from panel regression analysis of data for developing countries by group, 2000-06.

[10b] Line [9b] as a percentage of line [7].

[11b] Line [10b] scaled up for eight-year period 2000-07.

[12b] Two times line [11b], ie total for 2000-15 assuming annual rate is constant to 2015.

Table 3b: Total under-five mortality impact

| Line | | Low-income countries | Lower-middle-income countries | Upper-middle-income countries | Developing country total | |
|--------------------------|--|----------------------|-------------------------------|-------------------------------|--------------------------|------|
| [13] | Under-five mortality rate (Per 1,000) | 120.5 | 44.5 | 32.1 | | |
| [14] | Total under-five mortality, 2000-07 | Millions | 65.7 | 13.3 | 3.5 | 82.5 |
| Low-end estimate | | | | | | |
| [15a] | Under-five mortality impact of additional tax revenues (Per 1,000) | -2.0 | -1.8 | -1.4 | | |
| [16a] | Per cent | -1.6 | -4.1 | -4.5 | | |
| [17a] | Potential fall in under-five mortality: total, 2000-07 | Millions | 1.1 | 0.5 | 0.2 | 1.8 |
| [18a] | Projected fall in under-five mortality: total, 2000-15 | Millions | 2.1 | 1.1 | 0.3 | 3.5 |
| High-end estimate | | | | | | |
| [15b] | Under-five mortality impact of additional tax revenues (Per 1,000) | -3.4 | -3.2 | -0.2 | | |
| [16b] | Per cent | -2.8 | -7.1 | -0.6 | | |
| [17b] | Potential fall in under-five mortality: total, 2000-07 | Millions | 1.9 | 0.9 | 0.0 | 2.8 |
| [18b] | Projected fall in under-five mortality: total, 2000-15 | Millions | 3.7 | 1.9 | 0.0 | 5.6 |

Notes

[13] Average by group for 2000-06, calculated from WDI data.

[14] Line [13] scaled up for eight-year period 2000-07.

[15a] Historic impact of tax revenues on under-five mortality. Implied sensitivity of mortality rate from panel regression analysis of data for all developing countries, 1960-2006.

[16a] Line [15a] as a percentage of line [13].

[17a] Line [16a] scaled up for eight-year period 2000-07.

[18a] Two times line [17a], ie total for 2000-15 assuming annual rate is constant to 2015.

[15b] Recent association of tax/GDP ratio with under-five mortality. Implied sensitivity of mortality rate from panel regression analysis of data for developing countries by group, 2000-06.

[16b] Line [15b] as a percentage of line [13].

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Acknowledgements

This report was written by Andrew Hogg, Judith Melby, Anjali Kwatra, Sarah Wilson, Alex Cobham, Rachel Baird, David McNair and Matthew Sowemimo. Edited by John Davison. Sub-edited by Sophy Kershaw, Louise Parfitt and Julia Bell. Production by Marta Rodriguez. Designed by Howdy.

With special thanks to John Christensen (director, International Secretariat, Tax Justice Network) and Richard Murphy (Tax Research LLP).

Introduction was written by John Davison.

Stripping the riches was written by Andrew Hogg, with thanks to Sony Kapoor and Willy Olsen.

Tanzania: the sharp end of the panga was written by Judith Melby. With thanks, in Tanzania, to Fredrik Glad-Gjernes and the office of Norwegian Church Aid; Tundu Lissu (Lawyers' Environmental Action Team); and Mark Curtis.

Malawi: the way forward? was written by Judith Melby, with thanks, in Malawi, to Rafiq Hajat (Institute for Policy Interaction) and Undule Mwakasungula (Centre for Human Rights and Rehabilitation).

The secret shore was written by Andrew Hogg, with thanks to David McNair (Christian Aid Dublin office); Ronen Palan (professor of international political economy, Department of Political Science and International Studies, University of Birmingham); and Sol Picciotto (emeritus professor, Lancaster University Law School).

The haven experts was written by Andrew Hogg, with thanks to Prem Sikka (professor of accounting, University of Essex).

India: tax-break winners and losers was written by Anjali Kwatra, with thanks, in India, to Aseem Shrivastava, Manshi Asher; Professor Jayati Ghosh and Professor Arun Kumar (Jawaharlal Nehru University, New Delhi); Satvir Singh Gulia, Vivekananda Dash; Amitabh Behar (National Centre for Advocacy Studies); Anand Kumar (Christian Aid India office); Ekta Parishad; and Centre for Education and Communication.

Why paying tax is good for you was written by Alex Cobham and Andrew Hogg.

Peru and Bolivia: a tale of two tax systems was written by Sarah Wilson and Rachel Baird, with thanks in Peru to Dina Guerra and Edith Montero (Christian Aid); Lucien Chauvin, Humberto Campodonico, Dan Collyns; Epifanio Baca and Nilton Quinones (Grupo Propuesta Ciudadana). Thanks, in Bolivia, to Emma Donlan and Hannah Morley (Christian Aid); Carlos Arze and Javier Gomez (CEDLA – Centre for Labour and Agricultural Development); Elyzabeth Peredo, Felix Vargas and Alexandra Flores (Fundacion Solon); and Andres Shipani.

Recommendations was written by Alex Cobham, David McNair, Andrew Hogg and Matthew Sowemimo.

Technical appendix was written by Alex Cobham, with thanks to Liam Wren-Lewis (University of Oxford).

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‘For the first time in the 200-year run of the free-market system, we have built and expanded an entire integrated global financial structure the basic purpose of which is to shift money from poor to rich. [It is] the ugliest chapter in global economic affairs since slavery...’

Raymond W Baker, a senior fellow at the US Center for International Policy,
and guest scholar at the Brookings Institution

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