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**LEGALITY OF TAX HAVENS AND TAX TRANSPARENCY IN THE CORPORATE SPHERE: A DEEPER LOOK INTO TAX AVOIDANCE**- Rohit Shibu<sup>1</sup>**Introduction**

Taxes have always been a hinderance to individuals and corporations alike. As a result, parties try to avoid or exempt themselves from having to complete this state ridden obligation on them. One of the means for such avoidance is also in the form of tax havens. Liechtenstein emerged as a tax haven with the establishment of the Anstalt in 1926, whereas Israel enacted tax haven legislation in 1969. In the Caribbean basin, the tax havens began expanding their presence in the market primarily during the late 1950s, which is viewed either positively or negatively depending on the observer. It is worth noting that there was a considerable surge in the adoption of tax haven practices during the 1960s to 1980s period, with numerous tax havens such as the Cayman Islands, Bahamas, Bermuda, Antigua, British Virgin Islands, Israel, Hong Kong, and others entering the market.<sup>2</sup>

**Tax havens**

A tax haven is a country or jurisdiction that offers low tax rates or zero tax rates to foreign investors and businesses. A tax haven is also defined as 'A country that imposes little or no tax on the profits from transactions carried on in that country'<sup>3</sup>. These countries typically have a more lenient tax regime and relaxed financial regulations, making them attractive for companies and individuals to shelter their income and assets from high tax rates in their home countries. As the world economy became more globalized, advancements in infrastructure, transportation, and communication resulted in

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<sup>2</sup>Orlov, Mykola. "The Concept of Tax Haven: A Legal Analysis." *Intertax*, vol. 32, no. 2, 2004, pp. 95-105.

<sup>3</sup>Bryan A. Garner (ed.), *Black's Law Dictionary*, 7th ed. (West Group, 2001), p. 1474

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a substantial decrease in the transaction costs associated with utilizing various tax planning strategies. As a result, both large corporations and individuals began to contemplate the use of foreign jurisdictions as a means of shielding their income from taxation on both domestic and international transactions.

Crafting a dependable definition of the phrase "tax haven" that takes into consideration the diverse range of tax haven practices employed by various states and jurisdictions has proven to be exceedingly challenging.<sup>4</sup>

Within a strictly public international law perspective, it cannot be said that a tax haven is illegal in its sense, or within its entirety. This is because it may encroach upon the sovereignty of states, a fundamental principle of public international law. It can result in a situation where more powerful states hold greater influence compared to weaker states, allowing them to impose their own notions of what is considered "good" or "bad".<sup>5</sup> Further, the system of tax laws operated by a state is its own discretion, and the same cannot be attributed to be good or bad by any other state outside the jurisdiction of the state.

Tax havens act as a tool for corporations to enjoy a reduction in their tax obligation without a necessary evasion of tax laws of their domestic country. Since most of these accounts are held offshore, there cannot be a mode for jurisdiction of local governments within these systems.<sup>6</sup>

For example, an analysis of Amazon's corporate filings by the progressive think tank Institute for Taxation and Economic Policy (ITEP) reveals that the e-commerce behemoth, led by the wealthiest person in the world, did not pay any federal taxes on its \$11.2 billion profit in the year 2019 year. Due to the availability of a sizeable tax credit and a notable tax exemption for remuneration distributed through company stock, Amazon obtained a federal tax rebate amounting to \$129 million in the same year, thus resulting in an effective federal tax rate of about -1 percent.<sup>7</sup> The way for these huge

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<sup>4</sup>Orlov, Mykola. "The Concept of Tax Haven: A Legal Analysis." *Intertax*, vol. 32, no. 2, 2004, pp. 95-105.

<sup>5</sup>Orlov, Mykola. "The Concept of Tax Haven: A Legal Analysis." *Intertax*, vol. 32, no. 2, 2004, pp. 95-105.

<sup>6</sup>Ferraz, Luiz Felipe. "New Definition of Tax Haven Increases Uncertainty." *International Tax Review*, vol. 19, no. 8, September 2008, pp. 76-79. HeinOnline

<sup>7</sup>"Amazon Paid No Federal Taxes on Billions of Profits Last Year." *The Washington Post*, 16 Feb. 2019, <https://www.washingtonpost.com/us-policy/2019/02/16/amazon-paid-no-federal-taxes-billion-profits-last-year/>.

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corporate conglomerates to avoid payment of taxes is one that is excessively problematic to domestic state parties. In cases where the higher ups within such large group companies can avoid taxes altogether, lower corporates end up contributing a big chunk to the tax pile.

Publicly traded enterprises, including Amazon, have a legal obligation to act in the best interests of their shareholders. Many firms interpret this as a directive to increase shareholder value using various methods, including minimizing their tax liabilities.<sup>8</sup> This increases the instances of corporate tax avoidance where the fine line between lawful and unlawful is to be balanced.

### **OECD and its role**

“Tax havens collectively cost governments between \$500 billion and \$600 billion a year in lost corporate tax revenue, depending on the estimate (Crivelli, de Mooij, and Keen 2015; Cobham and Jansky 2018), through legal and not-so-legal means. Of that lost revenue, low-income economies account for some \$200 billion—a larger hit as a percentage of GDP than advanced economies and more than the \$150 billion or so they receive each year in foreign development assistance. American Fortune 500 companies alone held an estimated \$2.6 trillion offshore in 2017, though a small portion of that has been repatriated following US tax reforms in 2018.”<sup>9</sup>

Corporations using tax avoidance methods like these cause huge losses to governments, which in turn end up either turning into tax hikes for individuals or smaller companies, or an increase in government budget deficit overall.

The Adani Group, within its scandal had also set up multiple shell corporations in order to transfer amounts to various tax havens which were later reinvested into the Group as a separate investment. The Hindenburg report states that they had “... found at least 38 Mauritius-based entities associated with Vinod Adani and Subir Mittra (the head of the Adani private family office). We also found Vinod Adani associated entities in other tax

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<sup>8</sup> "Amazon Paid No Federal Taxes on Billions of Profits Last Year." The Washington Post, 16 Feb. 2019, <https://www.washingtonpost.com/us-policy/2019/02/16/amazon-paid-no-federal-taxes-billion-profits-last-year/>.

<sup>9</sup> Shaxson, Nicholas. "Tackling Global Tax Havens." Finance & Development, vol. 56, no. 3, 2019, <https://www.imf.org/en/Publications/fandd/issues/2019/09/tackling-global-tax-havens-shaxson>.

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haven jurisdictions like Cyprus, the UAE, Singapore, and various Caribbean islands. Several of these entities have transacted with Adani entities without disclosing the related party nature of the dealings, seemingly in violation of the law, as evidenced throughout our report.”<sup>10</sup>

As a result, the OECD (Organisation for Economic Co-operation and Development) is aiming to develop relevant provisions and legislation in order to curb such avoidance of taxes. The Standard for Automatic Exchange of Financial Account Information in Tax Matters, created jointly by the OECD and G20 countries, reflects the global agreement on the automatic exchange of financial account information for tax reasons, in a mutually beneficial manner.<sup>11</sup>

India is a member of many of the committees of the OECD, mainly within the BEPS (Base Erosion and Profit Sharing) committee which aims at ensuring tax co-operation within the global sphere. Domestic tax base erosion and profit shifting (BEPS) due to multinational enterprises exploiting gaps and mismatches between different countries' tax systems affects all countries. Developing countries' higher reliance on corporate income tax means they suffer from BEPS disproportionately.

Business operates internationally, so governments must act together to tackle BEPS and restore trust in domestic and international tax systems. BEPS practices cost countries 100-240 billion USD in lost revenue annually, which is the equivalent to 4-10% of the global corporate income tax revenue.<sup>12</sup>

Despite taking such steps however, India has not yet become a full member of the OECD, and neither have quite a few countries. This is because, the Indian government apprehends the sort of display it would give out if it ended up joining with the OECD, since it involves certain commitments which could prove detrimental to its developing economy.

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<sup>10</sup>Hindenburg Research. "Adani Group: How The World's 3rd Richest Man Is Pulling The Largest Con In Corporate History." Hindenburg Research, 24 January 2023, <https://hindenburgresearch.com/adani/>.

<sup>11</sup>"Transparency and Exchange of Information for Tax Purposes." OECD, [date of access], <https://www.oecd.org/tax/transparency/what-we-do/>.

<sup>12</sup>"Base Erosion and Profit Shifting (BEPS)." OECD, <https://www.oecd.org/tax/beps/>.

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### Tax Transparency

Significant advancements have been achieved by the European Commission in promoting transparency and collaboration among Member States concerning tax-related matters. Specifically, Member States have reached an agreement to automatically share information on tax rulings (effective July 2017) and country-by-country reports of multinational companies (effective June 2018). Furthermore, they have established fresh regulations that allow tax authorities to access anti-money laundering data, which was suggested in response to the Panama Papers scandal. Additionally, the Commission proposed public country-by-country reporting for multinationals in April 2016 to provide greater accountability for companies' tax practices to the public. Currently, the Council and Parliament are negotiating this proposal.<sup>13</sup>

The OECD also aims at Tax transparency, especially corporate tax transparency among international states and bodies. It has created international tax standards such as the AEOI (Automatic Exchange of Information) and the EOIR (Exchange of Information on Request).

Under the AEOI Standard, countries are required to exchange information annually on financial accounts held by non-resident individuals and entities, using a standardized format. The exchanged information includes various details about the financial account such as the financial institution that maintains it, the account number, and the account balance. Additionally, information regarding the account holder, such as their name, address, date of birth, and taxpayer identification number, is also included in the exchange.<sup>14</sup>

However, the EOIR Standard enables tax authorities to make targeted requests to other tax authorities for information that can facilitate their tax investigations. Such information may include accounting records, bank statements, and ownership details of assets.

To effectively implement the EOIR Standard, each jurisdiction must be able to respond to requests from their exchange partners in a timely and efficient manner. This requires the

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<sup>13</sup> European Commission. "Questions and Answers on the Anti-Tax Avoidance Package." 21 June 2017, [https://ec.europa.eu/commission/presscorner/detail/en/MEMO\\_17\\_1677](https://ec.europa.eu/commission/presscorner/detail/en/MEMO_17_1677).

<sup>14</sup>"Transparency and Exchange of Information for Tax Purposes." OECD, [date of access], <https://www.oecd.org/tax/transparency/what-we-do/>.

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establishment of robust information exchange channels and mechanisms for ensuring compliance with relevant standards and guidelines.<sup>15</sup>

The implementation of both of these standards would help eliminate many problems that exist within the global sphere, however, working toward a “collective” goal of tax transparency and equitable distribution of wealth is not one shared by all member states. As a result, effective implementation of the schemes would be a hassle, especially within the context of public international law.

### **Indian Context**

The Indian government has taken steps to address the issue of tax evasion and avoidance, including through the introduction of the General Anti-Avoidance Rule (GAAR) in 2012. The GAAR is aimed at preventing tax avoidance schemes and has provisions to deal with transactions routed through tax havens.<sup>16</sup>

In addition, the Indian government has signed several international agreements to promote tax transparency and prevent tax evasion. For example, India has signed the Multilateral Competent Authority Agreement (MCAA) for the automatic exchange of tax information with other countries.<sup>17</sup>

### **Conclusion**

Tax Havens have enacted the embodiment of the spirit of many corporate conglomerate giants. Behaving to be perfect for their simple functioning, they provide adequate opaqueness to be as enticing as possible, whether it be to park funds, make transfers or simply in order to avoid taxation. Their offshore mode also enables the inclusion of further opaqueness and non-interference by any other state parties within funds of the corporate. However, tax havens cost governments billions of dollars in lost tax revenue each year, increase inequality, undermine democracy, and pose a risk to global financial

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<sup>15</sup>"Transparency and Exchange of Information for Tax Purposes." OECD, [date of access], <https://www.oecd.org/tax/transparency/what-we-do/>.

<sup>16</sup>Government of India. "General Anti-Avoidance Rule (GAAR) to be Implemented from April 1, 2017." Press Information Bureau, Ministry of Finance, 1 April 2017, <http://pib.nic.in/newsite/PrintRelease.aspx?relid=160050>.

<sup>17</sup>Government of India. "India Joins the Multilateral Competent Authority Agreement on Automatic Exchange of Financial Account Information." Press Information Bureau, Ministry of Finance, 3 June 2015, <http://pib.nic.in/newsite/PrintRelease.aspx?relid=122256>.

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stability. The jurisdictional issues arising out of such offshore accounts are also difficult to manoeuvre around. It is important for governments and international organizations to continue to work together to combat tax evasion and promote tax fairness.



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