Luxembourg: a tax haven by any other name? Professor on 'secret' tax deals

November 28 2014, by Ronen Palan

Luxembourg: a fairyland for tax avoidance? Credit: Claude Wians , CC BY-SA

The revelations that global and multinational businesses have been brokering "secret" tax deals with Luxembourg to avoid paying taxes in their home countries, may be the first time an entire country has been implicated in tax avoidance collusion.

A cache of leaked agreements uncovered by the International Consortium of Investigative Journalism (ICIJ) appears to show that major companies have used the tiny EU state to dramatically cut their tax liabilities.

The ICIJ's six-month investigation claims to have found household companies such as Aviva, HSBC, E-on, Tyco, Pepsi, IKEA and Deutsche Bank were among those which had taken advantage of legal tax avoidance schemes in Luxembourg.

Luxembourg is routinely named as a tax haven on many of the world's authoritative lists of tax havens, including the one compiled by me and my two co-authors, Richard Murphy and Christian Chavagneux. But Luxembourg has managed to remain "under the radar" not least because its politicians and bankers have been denying for years that it is, or ever was, a tax haven.

The revelations suggest Luxembourg has been playing a double game. Luxembourg has been quick to comply with new regulations proposed by the Organisation for Economic Co-operation and Development (OECD) and the EU. In 2011, the OECD global forum on transparency and exchange of information commended Luxembourg for introducing new rules governing banking information or information protected by secrecy rules.

But at the same time, the revelations show that 340 well-known foreign companies have entered into secret agreements with the Luxembourg authorities, brokered by the accounting firm PricewaterhouseCoopers. To take a random example that applies for many of these companies, the ICIJ have a letter to the Luxembourg tax administration written on a PwC letterhead, where FedEx lays down its plan to set up a limited liability company as a tax resident in Luxembourg – so subject in principle to Luxembourg's corporate income tax.

The letter then provides details of a proposed shareholding arrangement that will ensure, I quote, that "neither that Fedex SCS nor its shareholders will be subject to corporate income tax, Municipal Business Tax and Net Wealth tax in Luxembourg". The letter implies that Luxembourg will serve in effect as a tax haven for Fedex.

A scandal with a difference

There have been a number of other highly publicised tax cases recently. For instance, many in the US involved branches or even key individuals working in branches of well-known Swiss and Israeli banks in the US, including UBS, Credit Suisse or Bank Leumi, or alternatively branches of American banks in Switzerland.

But these tended to involve private firms. The Swiss government professed to have had no knowledge of such activities. Indeed, Swiss law prohibited Swiss banks, whether domestic or international, from providing any information on their clients to the Swiss state.

This is a scandal with a difference. The leaked PricewaterhouseCoopers books imply there has been systemic collusion between companies from all over the world and the Luxembourg authorities in flagrant contravention of EU rules. The documents suggest that preferential tax treatments were guaranteed to these companies prior to their incorporation in Luxembourg.

This is the first case of suspected collusion between a government and a foreign firm in tax avoidance matters that I am aware of. In that sense, the current scandal places Luxembourg on par with Greece whose officials allegedly provided misleading data on Greek national debt to the Commission.

More embarrassingly, all this took place during the time when the current president of the European Commission, Jean-Claude Juncker, served as the prime minister of Luxembourg from 1995-2013. It is difficult to imagine that the prime minister of such a small state was unaware such deals were taking place.

There is a difference between the court of law and the court of public opinion. But we know from recent cases that the EU Commission has tended to follow the court of public opinion with criminal investigations of its own, as was the case of Amazon. It is likely that the Commission will now investigate these leaks and may impose fines on Luxembourg. I doubt Juncker can ride this one out.

Source: The Conversation