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COUNTRY-BY-COUNTRY REPORTING AND OTHER FINANCIAL TRANSPARENCY MEASURES AFFECTING THE EUROPEAN UNION

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Country-by-Country Reporting and Other Financial Transparency Measures Affecting the European Union

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Abstract:
In this paper we use the recently developed Bilateral Financial Secrecy Index to evaluate which countries supply most secrecy to EU Member States. Then, we assess how well-aimed are two of the EU's recent policy efforts to increase financial transparency: automatic Country-by-Country Reporting information exchange (CbCRIE) and the blacklist and the greylist of non-cooperative jurisdictions. We find that more than one-third of the financial secrecy that the EU faces comes from within the EU itself, and that the United States, Switzerland, and the Cayman Islands are the largest non-EU suppliers of secrecy to EU Member States. We report that active CbCRIE relationships now cover 79 per cent of the secrecy faced by the EU, but there is considerable heterogeneity in the share of secrecy that is covered by CbCRIE across the individual EU Member States, pointing to the potential to better aim the efforts of policymakers in identifying the most critical secrecy jurisdictions for individual countries. We further find that the blacklist and the greylist of non-cooperative jurisdictions published by the European Commission overlap with our results for most of the critical jurisdictions, with the significant exception of the United States.

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Keywords: tax havens; secrecy jurisdictions; financial secrecy; financial transparency; offshore finance; automatic exchange of information; European Union

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1 Introduction

Financial secrecy supplied by secrecy jurisdictions enables individuals and companies to escape their home country's regulations and legislation, thereby undermining the ecosystems in which these agents generate their income and wealth. More specifically, secrecy jurisdictions allow the existence of cross-border illicit financial flows (IFFs) – illegal movements of money or capital related to, among others, corruption, money laundering, tax evasion, tax avoidance, and the financing of terrorism. Recent leaks of confidential documents have provided a glimpse of the world behind the veil of secrecy and highlight the magnitude of use of secrecy jurisdictions for illegal purposes. Tackling financial secrecy – or, in other words, improving financial transparency – is thus of great importance.

Actors involved or benefitting from the veil of secrecy attempt to exploit it on various levels and to various extent. In this paper, we build on the Tax Justice Network's Financial Secrecy Index, which ranks each jurisdiction's contribution to global financial secrecy, and its bilateral extension, the Bilateral Secrecy Financial Index (BFSI), as developed by Janský, Meinzer, and Palanský (2018). The BFSI identifies the largest suppliers of financial secrecy for each specific country, rather than at the global level. We use the BFSI in this paper to achieve two objectives. First, we estimate which secrecy jurisdictions supply the most secrecy to EU Member States. Second, we evaluate the progress of two recent policy efforts to increase financial transparency specifically for EU Member States: automatic Country-by-Country Reporting information exchange (CbCRIE) and the blacklist and greylist of non-cooperative jurisdictions published by the European Commission. We compare how well-aligned these policies are with our estimates of the importance of individual secrecy jurisdictions.

We report that more than one-third of the financial secrecy faced by the EU is supplied by other EU Member States and, together with the EU's overseas territories, almost half of all secrecy can be attributed to the EU countries themselves. The largest suppliers of secrecy from within the EU are the Netherlands and Luxembourg. The secrecy faced by the EU and supplied from elsewhere is mainly from the United States, followed by Switzerland and the Cayman Islands.

Using the results of the BFSI to assess the progress of the automatic exchange of CbC reports, we find that around 79 per cent of the secrecy faced by the EU is now covered by

active CbCRIE relationships, and this number has increased from 71 per cent between January 2018 and September 2019 due to new treaties coming into force in this period. Importantly, we find that there is considerable heterogeneity in the share of secrecy that is covered by CbCRIE across individual EU Member States, pointing to the potential to better aim the efforts of policymakers in identifying the most important secrecy jurisdictions for individual countries. We report that the jurisdictions that supply the most uncovered secrecy are the British Virgin Islands and the United States, followed by Curacao and the United Arab Emirates.

We find that the blacklist and greylist of non-cooperative jurisdictions published by the European Commission overlap with our results for most of the critical jurisdictions, with the significant exception of the United States.

On the basis of our analysis in this paper, we provide two concrete policy recommendations: First, Country-by-Country Reporting data collected from individual multinationals should be made publicly available by all jurisdictions to enable effective tracking of economic activity of multinational corporations by all tax authorities, as well as by researchers, and the public who would then be able to hold both multinationals and authorities to account. Second, we encourage countries to require local subsidiaries of multinational corporations to file CbCR directly with local authorities in case the relevant CbCR is not yet public or if local authorities cannot obtain it via automatic exchanges regardless of the reason.

The rest of this paper is structured in the following way. Section 2 provides a brief overview of relevant literature and explains the initiative behind country-by-country reporting. Section 3 presents the data and summarizes the methodology related to BFSI and its use in policy evaluation. In Section 4, we estimate which jurisdictions are the largest suppliers of secrecy to EU Member States, while Section 5 aims to assess the EU's policy efforts to enhance financial transparency with a special focus on automatic CbCRIE. Section 6 concludes with policy recommendations.

2 Why Country-by-Country Reporting and financial transparency matters

Many countries today serve as secrecy jurisdictions, yet systematic analyses of the world of financial secrecy from the point of view of individual countries that face this secrecy are relatively scarce. In this paper, we aim to contribute to three related strands of literature.

The first is the research on financial secrecy. Starting in 2009, the Tax Justice Network has been publishing the biannual Financial Secrecy Index, ranking the world's largest contributors to financial secrecy. As explained by Cobham, Janský, and Meinzer (2015) who present the conceptual framework of the index, the FSI places jurisdictions on a spectrum of secrecy, rather than using arbitrary criteria and thresholds to classify such countries (as done in most previous influential research, such as Hines and Rice (1994), Dharmapala and Hines (2009), or Zucman (2013). Thereby, the FSI sheds light on the fact that different jurisdictions can act as secrecy jurisdictions[1] in specific areas and to varying extents. The FSI also puts the spotlight on the role of large developed economies (as opposed to small Caribbean islands) acting as major players in the world of financial secrecy.

There is a wide range of research documenting the negative effects of financial secrecy, from the literature on money laundering (Schwarz 2011; Brigitte Unger et al. 2013; Unger 2017) and international political economy (Hakelberg and Schaub 2017; Rixen 2008; Seabrooke and Wigan 2014) to that on illicit financial flows (Cobham and Janský 2017; forthcoming). While we do not aim to estimate or discuss the negative effects of secrecy, we build on this literature in our conceptual framework, methodology, and policy recommendations.

With significant improvements in financial transparency in the form of the European Union Savings Directive, the OECD's Common Reporting Standards for automatic exchange of information, or country-by-country reporting (CbCR) requirements for large multinational corporations, the first evidence on the effects of financial secrecy has started to emerge. In a case study on large MNCs in the extractive industries (which were the first to introduce the CbCR requirements), Johannesen and Larsen (2016) find that the policy was associated with significant decreases in the affected firms' value. Zucman (2015) argues that the EU's

[1] While the FSI was the first systematic effort to quantify the level of secrecy in each jurisdiction, the term 'secrecy jurisdiction' itself had been used before - among the firsts to do so were the United States House of Representatives (1970) and Peet and Dickson (1979).

Savings Directive was largely ineffective as compared to other measures such as the US Foreign Account Tax Compliance Act, and similar results stem from a case study on four European countries by Rixen and Schwarz (2011). The new initiatives, some of which were voluntary, created some public pressure on firms that did not comply straight away, but the effects were, as expected, not overwhelming (Dyreng, Hoopes, and Wilde 2016). The post-crisis initiative towards the exchange of bank information from some of the most significant tax havens was celebrated as the end of bank secrecy, but as Johannesen and Zucman (2014) show, bank deposits have been merely relocated to other tax havens that did not join the information-sharing network.

The second strand of literature we add to is that on identifying secrecy jurisdictions that are important to specific countries or groups of countries. In particular, we review the Bilateral Financial Secrecy Index, explained in more detail in Section 3.2, as recently introduced by Janský, Meinzer, and Palanský (2018), and explore its results for the European Union as a whole as well as for individual Member States. While the Financial Secrecy Index provides a *global* perspective, it may not necessarily identify the jurisdictions representing the highest secrecy risks from the perspective of each specific country or group of countries (e.g., while Mauritius may pose relatively low risk on the global scale, ranking forty-ninth on the FSI in 2018, it is a very important supplier of secrecy to some countries, including India for which it ranks second on the BFSI). A number of researchers focused on individual country case studies and identify which secrecy jurisdictions are most important for them (such as Janský and Prats (2015) on India or Ledyaeva et al. (2015) on Russia), the BFSI represents the most systematic effort to track the heterogeneity in where the secrecy faced by individual countries is supplied from.

We compare these results to the EU's list of non-cooperative jurisdictions, which was published for the first time in December 2017 (European Commission 2017). The list is based on a continuous assessment of a number of criteria and we review this effort in more detail in Section 3.3.1. Countries that do not pass the assessment but make a commitment to implement changes to their legislation regarding cooperation with the EU are placed on a greylist and their commitments are regularly reviewed. While many of the drawbacks of a dichotomous approach to identifying tax havens remain and some of the choices within the process seem to be, as we argue below, at least partly politically motivated, the blacklisting

exercise has already had some success, as documented by several jurisdictions being delisted as updates to the list are published.

The third important literature we contribute to is that on automatic exchange of information. In this paper, we focus on one type of information exchange in particular - country-by-country reporting data. The Base Erosion and Profit Shifting (BEPS) Project, led by the OECD, aims to tackle international tax avoidance by high-profile multinationals, improve the coherence of international tax rules and ensure a more transparent tax environment. There are fifteen BEPS Actions that are currently being considered and over 130 countries and jurisdictions are collaborating on their implementation. In this paper, we focus on BEPS Action 13, Country-by-Country Reporting (CbCR), which aims to establish a common minimum standard on the reporting of profits of multinational corporations.

Under BEPS Action 13, a multinational corporation whose combined turnover exceeds the threshold of 750 million Euro has to fill an annual confidential report that breaks down key elements of the financial statements for each tax jurisdiction in which the group operates. This confidential Country-by-Country Report promises local tax authorities easy access to data on the global allocation of income, profit, tax paid and accrued, retained earnings, tangible assets, and economic activity across jurisdictions (OECD 2013). Thus, confidential CbCR strives to help tax administrations to assess transfer pricing risks. Prior to the OECD BEPS Action Plan, CbCR has been under discussion for over 30 years as a public financial reporting standard (Cobham, Janský, and Meinzer 2018). Public CbCR has been introduced in the European banking sector in 2013 and has been shown to significantly curb profit shifting by banks with tax haven operations (Overesch and Wolff 2019). In 2016, when filing of confidential CbCR was required for the first time, fifty-eight jurisdictions participated. As of October 2019, over eighty jurisdictions have implemented confidential CbCR within their individual legal frameworks. Existing research, while scarce so far, suggests that financial transparency created at least by public CbCR is a potentially powerful tool to curb abnormal rents of firms that have avoided tax through profit shifting (Johannesen and Larsen 2016; Overesch and Wolff 2019).

The essence of confidential CbCR information exchange is to share the collected data and to enhance the cooperation of tax administrations across countries. As of September 2019, over 2400 bilateral exchange relationships, most of them reciprocal, are activated for sharing CbC reports between tax authorities of different jurisdictions with the first automatic exchanges of

CbC reports taking place in June 2018. Such extensive international cooperation indicates that basically all multinationals with consolidated turnover over the threshold of 750 million Euro are already required to file a CbC report and that the number of reporting companies is converging to the actual number of existing large multinationals primarily targeted by the CbCR initiative (OECD 2013). In this paper, we use the BFSI to assess this development of the CbCR information-exchange network.

3 Methodology and data

In this section, we first describe how the Financial Secrecy Index is constructed and why and how its bilateral extension is defined. We also detail which data sources are used in the two indices. Finally, we outline two recent policy efforts that we later assess for the EU Member States using the Bilateral Financial Secrecy Index: the Country-by-Country Reporting information exchange (CbCRIE) framework led by the OECD and the blacklist and greylist of non-cooperative jurisdictions published by the European Commission.

3.1 Financial Secrecy Index

The Financial Secrecy Index (FSI) is a single ranking that estimates which jurisdictions most contribute to the global problem of financial secrecy. It was developed by the Tax Justice Network and consists of two parts - secrecy scores (SS) and global scale weights (GSW). Tax Justice Network has published the index biannually since 2009. In this paper, we build on the latest edition published in 2018 which covers 112 jurisdictions.

The secrecy score for each country represents a qualitative measure of financial secrecy and is composed of 20 indicators that cover various areas of financial secrecy: banking secrecy, trusts and foundations register, recorded company ownership, limited partnership transparency, public company ownership, country by country reporting, corporate tax disclosure, tax administration capacity, consistency of personal income tax regime, automatic information exchange, bilateral treaties, international legal cooperation, and so on. These twenty secrecy indicators can be grouped into four broad dimensions of secrecy: 1) ownership registration; 2) legal entity transparency; 3) integrity of tax and financial regulation; and 4) international standards and cooperation (Tax Justice Network 2018).

The secrecy score of a jurisdiction is calculated as the arithmetic average of the 20 indicators, with values ranging between 0 (full transparency) and 100 (full secrecy). The secrecy score

involves an analysis of the legal framework of each jurisdiction: its laws, regulations, and enforcement. However, a high secrecy score does not in itself indicate that a jurisdiction poses a risk for other countries, i.e. whether any foreign individual or company actually exploits the jurisdiction's secretive legal framework or not.

The second part of the FSI, the global scale weights (GSW), represents a quantitative measure and serves as a proxy for the actual use of jurisdiction's secretive legal framework by individuals or companies. Specifically, the GSW measures each jurisdiction's market share (percentage) of exports of offshore financial services (financial services offered to non-residents).

The Financial Secrecy Index combines both measures, the qualitative and the quantitative, into one value, which reflects the potential global harm done by each country. For the 2018 FSI edition, the Tax Justice Network uses the same formula as in the previous editions: for jurisdiction i, the FSI is defined as follows.

$$FSI_i = Secrecy\ Score_i{}^3 * \sqrt[3]{Global\ Scale\ Weight_i}$$

The applied method reflects the FSI's core objective: highlighting the importance of harmful secrecy regulations in contributing to global financial secrecy. The FSI ranks jurisdictions with respect to their secrecy and the scale of their offshore financial activities; however, the value of the index itself does not represent a quantity that could be translated into economic terms. Table 1 presents the top ten jurisdictions with the highest FSI values in 2018.

Table 1: Results of the Financial Secrecy Index 2018

Rank	Jurisdiction	FSI Value	Secrecy Score	Global Scale Weight
1	Switzerland	1589.6	76.5	4.5%
2	USA	1298.5	59.8	22.3%
3	Cayman Islands	1267.7	72.3	3.8%
4	Hong Kong	1243.7	71.1	4.2%
5	Singapore	1082	67.1	4.6%
6	Luxembourg	975.9	58.2	12.1%
7	Germany	769	59.1	5.2%
8	Taiwan	743.4	75.8	0.5%
9	United Arab Emirates	661.2	83.9	0.1%
10	Guernsey	658.9	72.5	0.5%

Source: FSI results from Tax Justice Network (2018).

3.2 The Bilateral Financial Secrecy Index

The Bilateral Financial Secrecy Index (BFSI) is a direct extension of the FSI and it was developed by Janský, Meinzer, and Palanský (2018). It estimates the importance of secrecy jurisdictions for each specific country individually rather than globally. To maintain consistency, the BFSI follows the FSI methodology as closely as possible. It employs the same indicators for the secrecy score, however, it adjusts the scores for the relationships within the EU. In particular, adjustments were made in the secrecy score of the last three indicators (Automatic information exchange, Bilateral treaties, and International legal cooperation) vis-à-vis other EU Member States (Tax Justice Network 2018).

Regarding the quantitative part of FSI, the global scale weight, the BFSI uses a different source of data than the GSW in the FSI – while the FSI uses data on exports of financial services from the IMF's Balance of Payments Statistics which are only available at the unilateral level, the BFSI requires data on a bilateral level. Janský, Meinzer, and Palanský (2018) thus use data on cross-border portfolio investment, namely assets, from the IMF's 2015 Coordinated Portfolio Investment Survey (CPIS) to construct the so-called bilateral scale weights (BSW). While there are other sources of bilateral data that could be relevant to use to construct the BSW (such as foreign direct investment), as Janský, Meinzer, and

Palanský (2018) argue, portfolio assets are likely to capture well the economic activity that may make the best use of financially secretive regulations in secrecy jurisdictions. The BSW is then defined analogously to GSW as the share of portfolio investment assets between country *i* and jurisdiction *i* on the total global value of cross-border portfolio investment.

The BFSI combines the secrecy score of secrecy jurisdiction *i* with the BSW of country *i* with respect to secrecy jurisdiction *i*:

$$BFSI_{ij} = Secrecy\ Score_j^3 * \sqrt[3]{Bilateral\ Scale\ Weight_{ij}}$$

This approach aims to capture the relative intensity of the economic relationship of the country's residents with different secrecy jurisdictions and the interaction of this activity with the secrecy offered by secrecy jurisdictions. The BFSI is derived for eighty-six countries which face financial secrecy supplied to them by up to 110 jurisdictions.

3.3 Assessing the EU's policy measures using BFSI

We use the BFSI to evaluate the success of two recent EU's policy measures. First, we compare the BFSI with the EU lists of non-cooperative jurisdictions for tax purposes to observe whether these measures coincide. Second, to evaluate the development of CbCRIE relationships, we study the extent to which countries have so far covered the secrecy they face by having activated CbCRIE with their secrecy suppliers.

3.3.1 EU lists of tax havens

In December 2017, Finance Ministers of EU Member States agreed for the first time ever on a list of non-cooperative jurisdictions for tax purposes. The initial blacklist consisted of seventeen countries that failed to meet the agreed standards. In addition, forty-seven countries have committed to addressing deficiencies in their tax systems and to meet the required criteria by the end of 2018, or 2019 for developing countries without financial centres, to avoid being listed (European Commission 2017). To ensure compliance of these countries, EU Member States agreed to monitor them by the Code of Conduct Group and the Commission. The EU blacklist was the result of extensive screening of 92 jurisdictions, using internationally recognised good governance standards in three areas: transparency, fair taxation and anti-BEPS measures (European Commission 2017).

Since December 2017, both the EU blacklist and greylist have been adjusted several times with the last update (as of this writing) on March 12, 2019. As of that update, the blacklist

consisted of 15 countries. Of those, 5 have taken no actions with respect to deficiencies in their tax systems since the first issue of the EU list of non-cooperative jurisdictions in 2017 (American Samoa, Guam, Samoa, Trinidad and Tobago, and US Virgin Islands). Three others (Barbados, United Arab Emirates and the Marshall Islands) were on the 2017 list; in 2018, they were moved to the greylist; and in 2019, they were blacklisted again as they have not taken any additional commitments since. For the same reasons, seven countries were moved from the greylist to the blacklist (Aruba, Belize, Bermuda, Fiji, Oman, Vanuatu and Dominica). The Commission will continue to monitor 34 countries that are now on the greylist.

3.3.2 Country-by-Country Reporting information exchange relationships

This section describes the data on bilateral exchange relationships that are currently in place for the automatic exchange of CbC reports between tax authorities in different countries. Each observation in our dataset represents a one-way exchange relationship between jurisdiction i and jurisdiction j. As described by OECD (2019): "The observations include exchanges between the eighty signatories to the CbC Multilateral Competent Authority Agreement, between EU Member States under EU Council Directive 2016/881/EU, and between signatories to bilateral competent authority agreements for exchanges under Double Tax Conventions or Tax Information Exchange Agreements, including 40 bilateral agreements with the United States." The EU Member States, in particular, have activated information exchange relationships with many countries – most of them are exchanging CbCR data with approximately sixty countries.

In order to analyze the spread of the bilateral exchange relationship network over time, we compare the network's extent at two points in time: January 2018 and September 2019. While by January 2018, about 2800 bilateral exchange relationships had been activated, by September 2019, this number increased to over 4100 activated relationships. This includes over 1,700 reciprocal information exchange relationships (amounting to over 3,400 one-sided relationships). The remaining 700 are only one-sided, i.e., information is shared by country i with country j but not the other way around.

To assess CbCRIE in light of financial secrecy, we compare it with the BFSI results and study whether the most important suppliers of secrecy to specific countries are covered by CbCRIE relationships. To do so, we calculate the share of secrecy faced by country i (as

measured by the BFSI) that is covered by active CbCRIE relationships. More formally, we define this share as follows:

$$Share\ of\ received/supplied\ BFSI\ covered\ by\ CbCR\ IE_i = \frac{\sum_{j=1}^{k} BFSI_{ij}}{\sum_{l=1}^{m} BFSI_{il}}$$

where k is the number of jurisdictions j with which country i has an activated CbCRIE relationship, and m is the number of jurisdictions l for which the BFSI is estimated for country i. In addition, in a similar way, we calculate the share of secrecy supplied by each jurisdiction to all other countries that is covered by CbCRIE.

4 Who supplies secrecy to EU member countries?

In this section, we use the BFSI to estimate which jurisdictions are the largest suppliers of secrecy to EU countries. Table 2 shows the top fifteen suppliers of secrecy along with their secrecy scores and information on how many EU Member States the jurisdictions have an active CbCRIE relationship. We observe that the largest supplier of secrecy are the United States which exchange CbCR data with only twenty-three of the EU Member States. We examine the network of information exchanges in more detail in Section 5. We also report that within the top fifteen suppliers of secrecy, four countries are from within the EU[2] - the Netherlands, Luxembourg, Germany, and France. As per the EU treaties, all of these countries exchange both types of information with all other Member States.

[2] In the future, however, the financial secrecy stemming from within the EU may be reduced if EU countries decide to properly implement the EU Anti-Money Laundering Directive of 2015 (AMLD 4) as amended in 2018 (AMLD 5). In this case, part of their secrecy score related to registration and publication of beneficial ownership information for companies, partnerships, and foundations should improve. If EU Member States decide to go beyond AMLD 5 and subject all (instead of some) trusts to beneficial ownership registration and disclosure, then the secrecy score of EU countries would improve even more. However, the financial secrecy affecting the EU from within will stay the same, if EU countries fail to properly implement the AMLD 5 (as it happened with Germany, the UK or Denmark with regard to AMLD 4) or to do it within the required time.

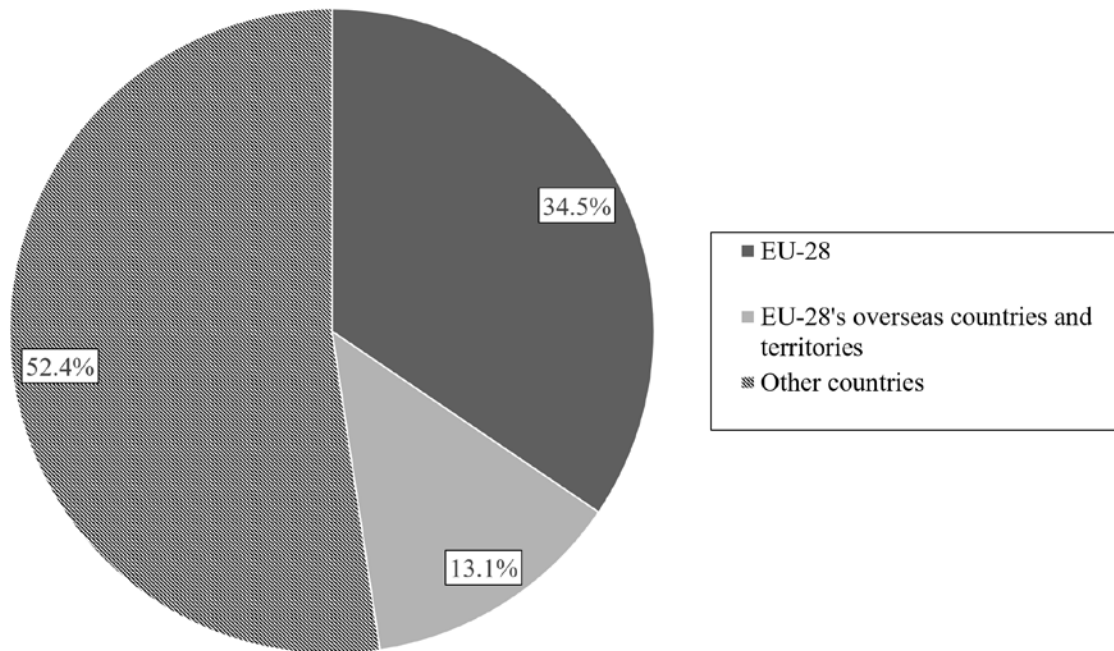
Table 2: Top fifteen suppliers of financial secrecy to EU-28, the number of EU-28 countries that receive CbCR information from them, and the number of EU-28 countries that send CbCR information to them

Rank	Country	BFSI supplied to EU-28	Secrecy Score	No. of EU countries receiving CbCR information from jurisdiction	No. of EU countries sending CbCR information to jurisdiction
1	United States	5519.6	59.8	23	23
2	Netherlands	4728.5	64.7	27	27
3	Luxembourg	4471.8	57.5	27	27
4	Switzerland	4318.9	72.6	25	28
5	Cayman Islands	4013.8	72.3	25	0
6	Germany	3901.8	58.2	27	27
7	Japan	2661.5	60.5	25	28
8	France	2646.9	51.0	27	27
9	United Arab Emirates	2503.5	83.8	24	0
10	Hong Kong	2455.6	71.1	25	28
11	Turkey	2350.3	68.0	0	0
12	Bermuda	2317.5	73.1	25	1
13	Jersey	2222.5	65.4	25	28
14	Taiwan	2205.9	75.8	0	0
15	Guernsey	2202.6	72.4	25	28

Source: Authors, results of BFSI from Janský, Meinzer and Palanský (2018), secrecy scores from Tax Justice Network (2018), data on CbCR information exchange from OECD (2019).

Indeed, as reported in Figure 1, we find that more than one-third of all secrecy faced by EU Member States comes from within the EU, with an additional thirteen per cent coming from EU countries' overseas countries and territories – mainly from the Cayman Islands, Bermuda, Jersey, and Guernsey, all of which are among the top fifteen suppliers of secrecy to the EU-28.

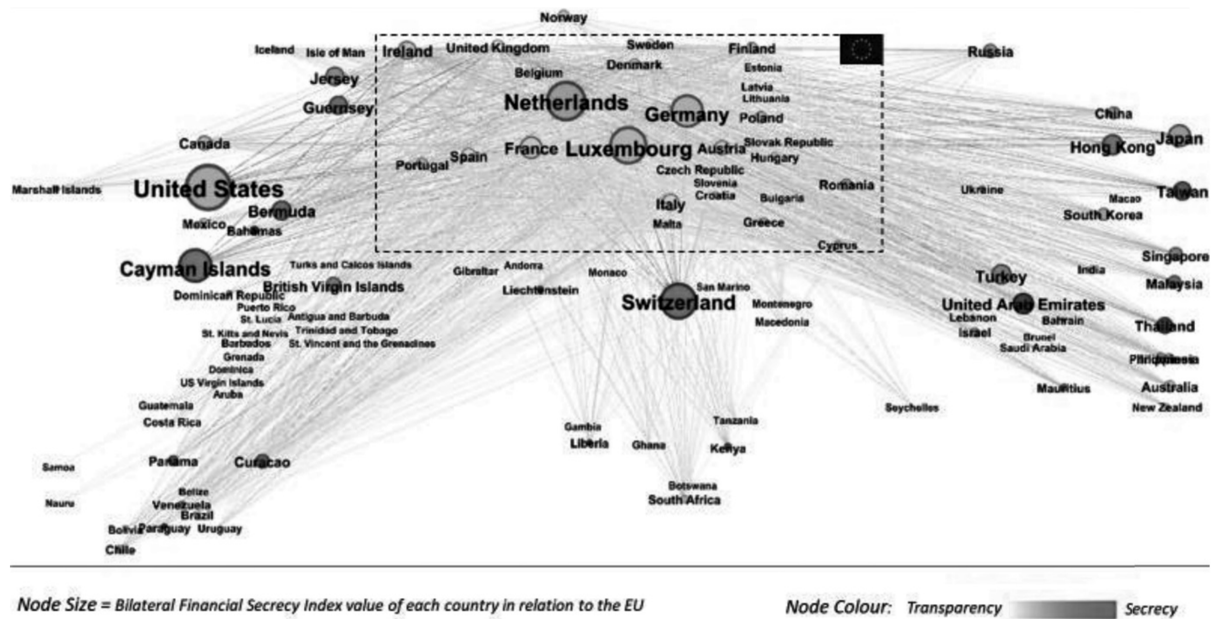
Figure 1: Distribution of suppliers of secrecy to EU-28 countries, by political group



Source: Authors based on the results of the BFSI (Janský, Meinzer and Palanský 2018).

Figure 2 shows the network of financial secrecy faced by the EU, illustrating the financial secrecy risks (BFSI value) created by each jurisdiction against all EU countries (size of bubble and number of links) and the secrecy score of these jurisdictions (bubble colour). Out of the total of 111 secrecy jurisdictions that supply financial secrecy to EU countries (located in the dashed-rectangle), the chart shows that the biggest bubbles (countries creating the most financial secrecy faced by EU countries) include many countries inside the EU (e.g., the Netherlands, Luxembourg, Germany and France). Other important secrecy jurisdictions include the United States, Switzerland, and the Cayman Islands. The bubble colour indicates that the jurisdictions creating financial secrecy faced by EU countries are rather secretive (e.g., the United Arab Emirates, Taiwan, Switzerland, and the Cayman Islands). Importantly, jurisdictions currently blacklisted by the EU (e.g., Samoa, US Virgin Islands, or Aruba) have very small bubbles, reflecting that they are not among the largest financial secrecy suppliers.

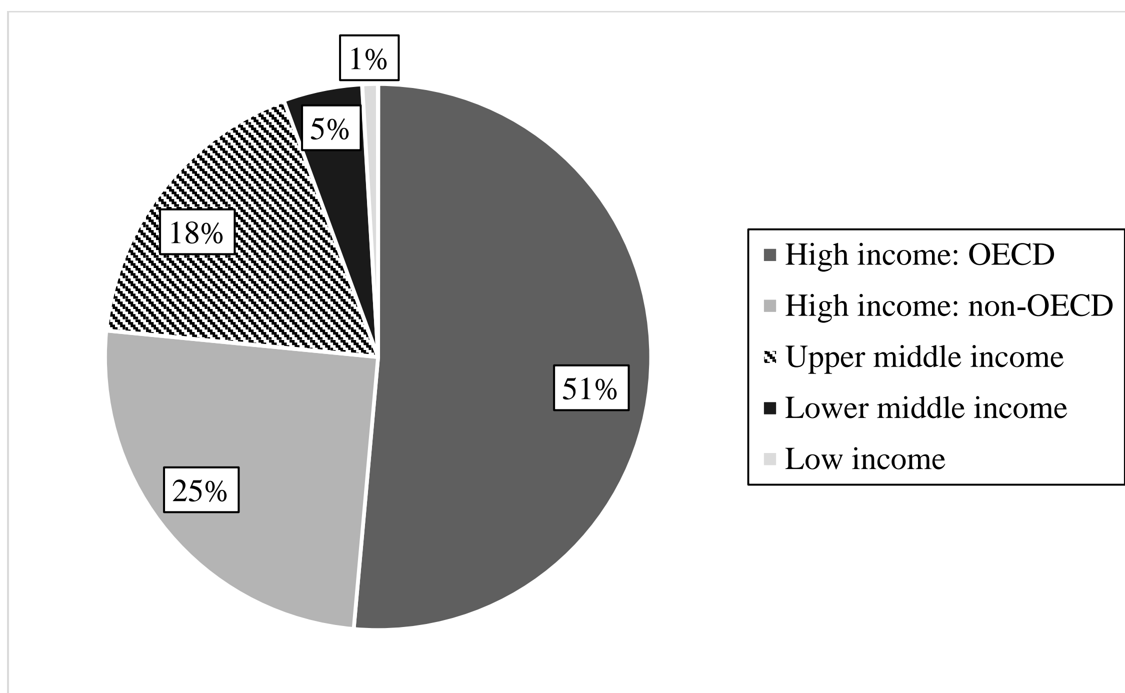
Figure 2: Financial secrecy affecting the EU, network map



Source: Authors

When breaking down the origins of financial secrecy faced by EU countries by income level, we observe in Figure 3 that 76 per cent is supplied high-income countries. More than half of all secrecy that the EU faces comes from OECD countries, and only 6 per cent originates from low and lower-middle income countries. The remaining 18 per cent is supplied by upper-middle income countries.

Figure 3: Distribution of suppliers of secrecy to EU-28 countries, by income group



Source: Authors based on the results of the BFSI (Janský, Meinzer, and Palanský 2018).

5 Assessing the EU's policy efforts using BFSI

Two recent policy efforts have been undertaken at the international level that aim at bringing more financial transparency. First, automatic exchange of information in several areas is now relatively widespread. As we show in this section, the BFSI is a tool that can be used to assess the progress of these efforts, and we do so here for one specific type of information to be exchanged: country-by-country reporting by large multinational corporations. Second, we compare the results of the BFSI with the blacklist and greylist of non-cooperative jurisdictions of the European Commission.

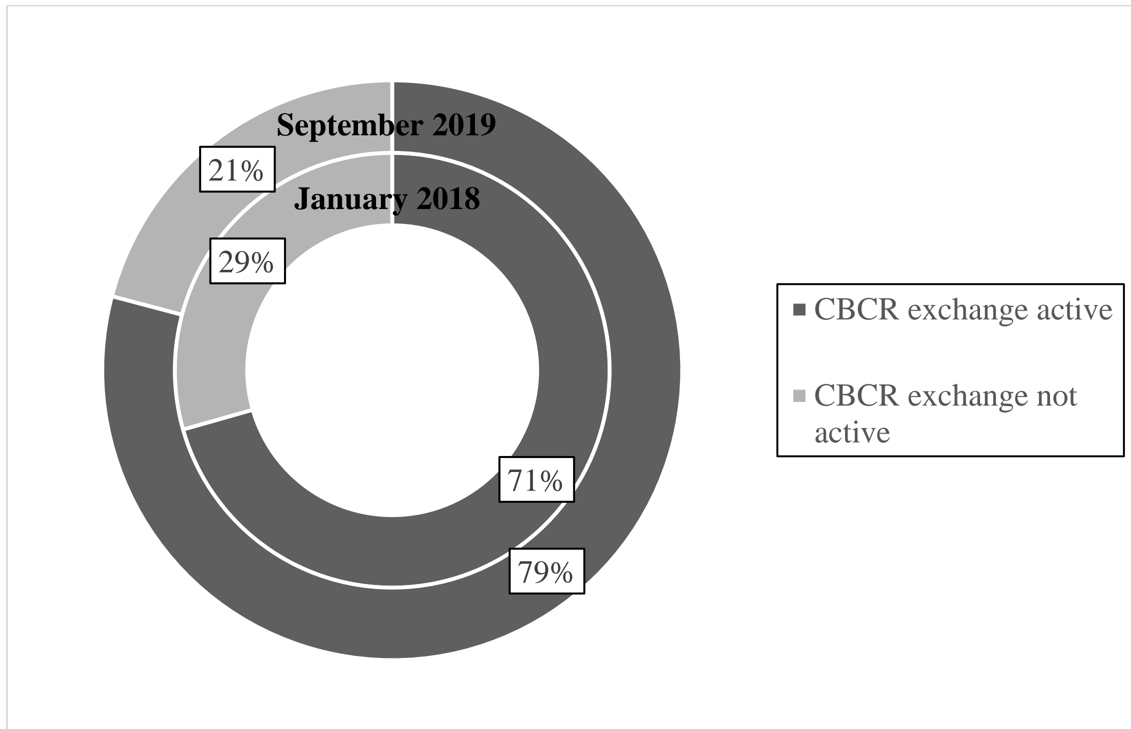
Automatic exchange of CbCR information is one of the aims of the OECD's BEPS framework. Figure 4 shows a map of the current state (as of September 2019) of the international network of exchanging jurisdictions with the size of the circle representing each country's population. Most major jurisdictions are now part of the network, however, there are important players that have not yet joined, including many high-secrecy jurisdictions in the Caribbean.

Figure 4: Map of CbCR information exchange network

Source: OECD (2019).

In Figure 5, we show the share of secrecy that is faced by EU-28 countries and is covered by active CbCRIE relationships. As of September 2019, this share is 79 per cent, with 8 per cent being added by exchanges activated between January 2018 and September 2019.

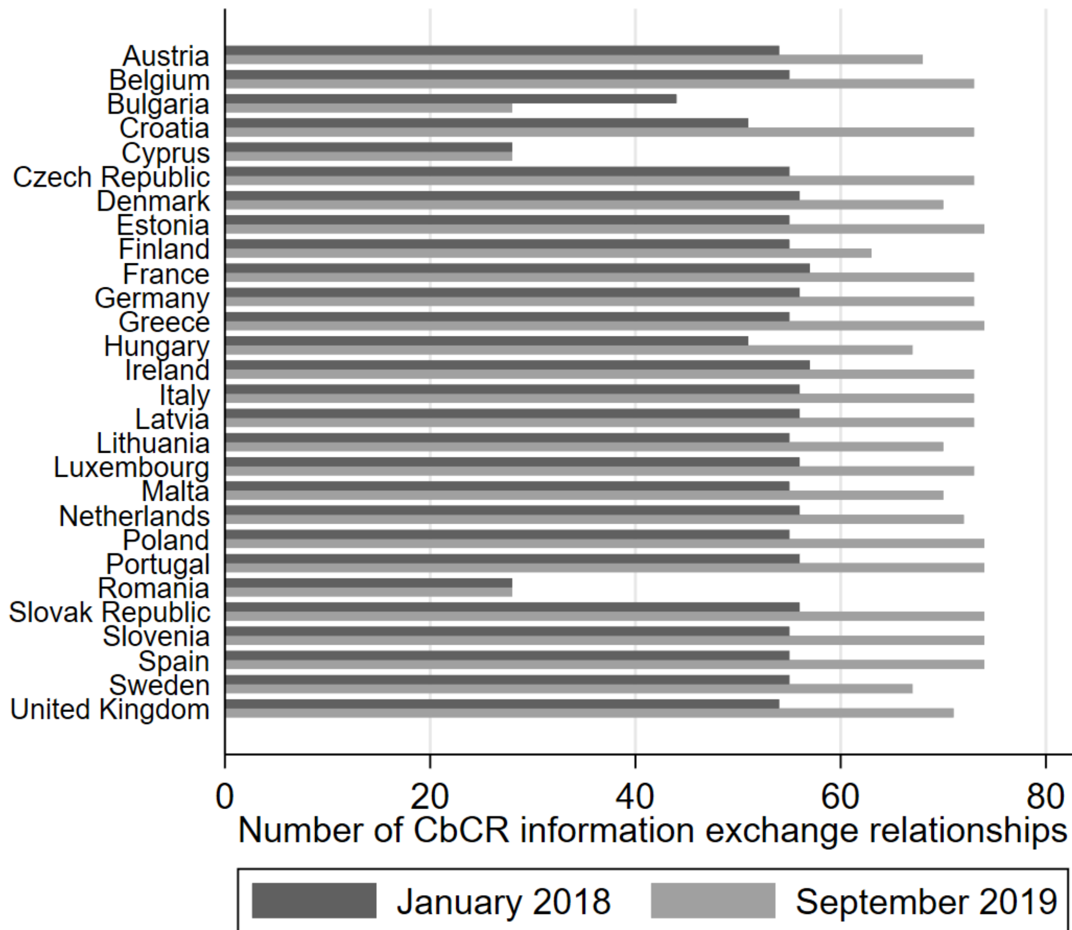
Figure 5: CbCR information exchange coverage of secrecy faced by the EU-28



Source: Authors.

In this period, most EU-28 countries activated around 10-15 new bilateral relationships, as documented in Figure 6. Among the exceptions to this trend are Bulgaria, Cyprus, and Romania, where no progress has been made and these countries only receive CbCR information from the rest of EU-28 (although they do send CbCR information to around 35 third-party countries). Most jurisdictions now receive CbCR information from around 70 jurisdictions, and most of these relationships are reciprocated by EU Member States.

Figure 6: Number of active CbCR information exchange relationships



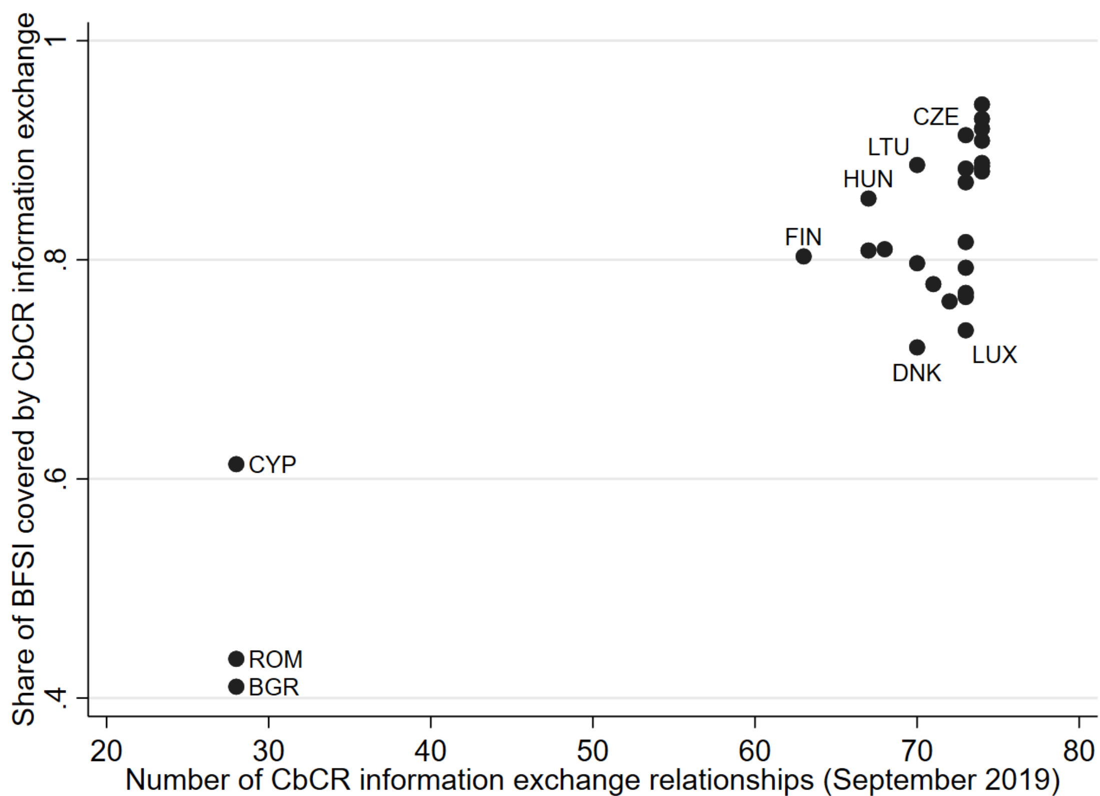
Source: Authors.

It is important to note that the approach we take here to calculate the number of CbCRIE relationships underestimates the true number of jurisdictions from which countries receive CbCR data. The reason is that we only consider bilateral exchange relationships that are currently in place for the automatic exchange of CbC reports between tax authorities as part of the OECD framework. However, there are two other ways in which an authority from country A might be able to obtain data from CbCR filed by multinationals that are headquartered in a jurisdiction not exchanging CbCR with country A on an automatic basis. The first is called surrogate filing, a scenario in which a multinational has a subsidiary in a country that does exchange information with country A, and it appoints this subsidiary to file the CbCR. This data then would be exchanged automatically. The second way is called local filing and it means that the local authority of country A asks the local subsidiary of the

multinational to file the CbCR. In our analysis, we do not consider these two ways, and we discuss the reasons for this in Section 6.

Despite similar numbers of activated CbCRIE relationships with third countries, the share of BFSI that is covered by these treaties varies substantially among EU countries, since different countries supply secrecy to EU Member States to different extents. As shown in Figure 7, the Czech Republic, for example, receives CbCR information from seventy-three countries and thereby covers ninety-one per cent of the secrecy it faces, while Luxembourg, having activated the exact same amount of treaties, only covers 73.5 per cent. The BFSI then easily allows to identify, for each country, the jurisdictions that are not yet covered by information exchange treaties and at the same time supply large amounts of secrecy. For Luxembourg, establishing CbCRIE with just five more countries - Taiwan, Thailand, British Virgin Islands, Turkey, and the Bahamas - would increase the share of BFSI covered by CbCRIE to eighty-three per cent.

Figure 7: Share of BFSI covered by active CbCR information exchange relationships vs. the number of active CbCR information exchange relationships as of September, 2019.



Source: Authors.

In Table 3, we show which jurisdictions supply the most BFSI uncovered by CbCRIE to EU Member States. The British Virgin Islands, which are only the twentieth-largest supplier of secrecy to the EU as a whole, do not share CbCR information with fifteen of the twenty-eight EU Member States to which they supply fifty-nine per cent of the secrecy they supply to the EU as a whole. At the same time, the British Virgin Islands notoriously act as a corporate tax haven, ranking at the top of the recently published Corporate Tax Haven Index (see Tax Justice Network, 2019). The jurisdictions that face most secrecy from the British Virgin Islands and at the same time do not receive CbCR information from them are Luxembourg, the United Kingdom, and Ireland.

The second country in the ranking of Table 3 is the United States, which do not share CbCR information with five EU countries: Cyprus, Romania, Bulgaria, and, importantly, Germany and France (with the latter two accounting for the bulk of the amount of 925.2 of uncovered BFSI). Interestingly, for Curacao, which is at the third place of the ranking of jurisdictions with the most uncovered secrecy, most of this uncovered BFSI is directed towards the Netherlands, which does not receive CbCR information from Curacao despite being part of the same Kingdom.

We also compare these results with a recent effort of the European Commission to blacklist non-cooperative jurisdictions. We observe that, out of the top fifteen largest suppliers of secrecy to the EU (as listed in Table 2), the blacklist and greylist have successfully identified all but the United States, Canada, and Japan. Of the top fifteen jurisdictions that supply the most BFSI that is uncovered by CbCRIE treaties, the lists miss five countries. The two lists are continually updated and jurisdictions monitored - Bermuda, for example, appeared on the blacklist for a short period between March and June 2019, when it moved back to the greylist following its commitment to address the European Commission's concerns until the end of 2019 (similarly to the Bahamas, British Virgin Islands, and the Cayman Islands). As of September 2019, out of the jurisdictions listed in Table 3, only United Arab Emirates are included on the blacklist.

One of the flaws of the EU's blacklisting exercise is its heavy reliance on the OECD tax standards, whose criteria are often very lenient and sometimes bent in favour of powerful players, and whose evaluating assessments are also sometimes biased. For example, the EU blacklist's sub-criterion 1.2 of criterion 1 on tax transparency requires a jurisdiction to obtain at least a "largely compliant" rating by the OECD's Global Forum peer review with respect

to its Exchange of Information on Request (EOIR) standard (Lips and Cobham 2018). To understand how irrelevant this criterion should be, consider that as of July 2018 and out of 119 reviewed jurisdictions by the Global Forum, the only jurisdictions that failed to have at least a "largely compliant" rating are: Trinidad & Tobago ("not compliant"), Anguilla, Curacao, Ghana, Kazakhstan, Sint Maarten, Turkey ("partially compliant"), and the Marshall Islands ("provisionally partially compliant"). This implies that the jurisdictions such as Panama, United Arab Emirates, British Virgin Islands, Switzerland, USA, and every other financial centre are considered at least "largely compliant".

As for the bending of the criteria, consider the OECD's recent moves to "update" the criteria for compliance with automatic information exchange. Here, a change in the criteria has allowed the USA to tick the box of compliance whilst refraining from participating in automatic information exchange (Knobel 2018a). Furthermore, the Global Forum in July of 2018 arrived at a biased assessment of the US' legal framework with respect to the availability of company ownership information. The Global Forum rated the US as largely compliant, although the US cannot even guarantee access to legal ownership information (Knobel 2018c). By relying on OECD standards and evaluations for a large part of the black and greylisting exercise, the EU partially imports OECD's biases against low- and medium-income countries, in favour of the largest, most powerful country(ies) in the world. The power of a jurisdiction, expressed in terms of absolute GDP, appears thus to have largely driven the blacklisting exercise (Lips and Cobham 2018).

Table 3: Top suppliers of secrecy that is uncovered by CbCR information exchange relationships with EU-28 countries.

Rank	Country	BFSI supplied to EU-28	Share of BFSI uncovered by CbCRIE	BFSI uncovered by CbCRIE	EU list, 03/2019
1	British Virgin Islands	1733.6	59.5%	**1030.8**	
2	United States	5519.6	16.8%	**925.2**	
3	Curacao	1679.5	11.0%	**185.0**	
4	United Arab Emirates	2503.5	5.6%	**140.5**	
5	Russia	1620.3	7.3%	**118.2**	
6	Switzerland	4318.9	1.8%	**76.7**	
7	Cayman Islands	4013.8	1.8%	**71.2**	
8	Seychelles	226.4	27.9%	**63.2**	
9	Bermuda	2317.5	2.7%	**61.7**	
10	Guernsey	2202.6	2.7%	**59.9**	
11	Jersey	2222.5	2.3%	**50.4**	
12	Canada	1724.3	2.3%	**40.3**	
13	Japan	2661.5	1.4%	**36.0**	
14	Isle of Man	583.6	5.9%	**34.1**	
15	Norway	1296.2	2.4%	**30.8**	

Source: Authors.

6 Conclusion and policy recommendations

The European Union faces large amounts of financial secrecy supplied to it by a number of secrecy jurisdictions around the world. To explore the patterns of this phenomenon, in this paper, we used the Bilateral Financial Secrecy Index (BFSI) developed by Janský, Meinzer, and Palanský (2018) to estimate which jurisdictions supply most secrecy to EU Member States. We then used the BFSI to assess the progress of two recent EU policy efforts to tackle financial secrecy: automatic exchange of Country-by-Country Reporting data and the blacklist and greylist published by the European Commission.

We find that thirty-four per cent of the financial secrecy the EU is facing is supplied by other EU Member States and a further thirteen per cent comes from the Member States' overseas countries and territories, mainly from the UK's Cayman Islands, Bermuda, and Guernsey. More than seventy-five per cent of financial secrecy faced by the EU comes from high-income countries and only six per cent comes from low and lower-middle income countries. The largest supplier of financial secrecy to the EU, according to the BFSI, are the United States, followed by the Netherlands, Luxembourg, Switzerland, and the Cayman Islands.

The results suggest that around seventy-nine per cent of the secrecy faced by EU Member States is now covered by active CbCRIE relationships, a number that has increased by 8 percentage points between January 2018 and September 2019. Most countries in the EU now receive CbCR information from around seventy countries, with the exception of Bulgaria, Cyprus, and Romania, which lag in this respect. We further compared the number of active CbCRIE relationships with the share of the secrecy that is covered by them, as estimated by the BFSI. We find that there is relatively high heterogeneity in the covered share of secrecy – countries that have signed a similar number of treaties have covered between seventy and ninety-four per cent of the secrecy they face. We argue that the BFSI can be used to identify the jurisdictions that do not yet automatically share information with EU Member States but at the same time are important suppliers of financial secrecy. The jurisdictions that supply the most uncovered secrecy to the EU Member States are the British Virgin Islands and the United States, followed by Curacao and the United Arab Emirates.

Assessing how well-aligned are the blacklist and greylist published by the European Commission with the results of the BFSI for EU Member States, we find that the lists do identify most of the EU's largest secrecy suppliers, with an important exception of the United States. At the same time, most of the large secrecy suppliers are now on the greylist, awaiting further assessment, and it remains to be seen whether they will implement the required measures to be removed from the list. We also argue that the criteria for the assessment of jurisdictions for the purposes of the blacklisting exercise rely heavily on the OECD tax standards, whose criteria are often very lenient and sometimes bent in favour of powerful players, and whose evaluating assessments are also sometimes biased.

We provide two concrete policy recommendations that stem from our analysis in this paper. First, we recommend that the Country-by-Country Reporting data collected from individual multinationals should be made publicly available by all countries to facilitate a proper

analysis of the scale of international corporate profit shifting, to enable effective public control of suspicious activity of multinational corporations, and to provide individual jurisdictions with the data necessary to correctly calculate corporate tax due by each multinational. This would also allow researchers, journalists and civil society organisations to hold multinational companies as well as authorities to account. This system would completely replace the current system of CbCRIE, freeing many resources and reducing costs for tax authorities – no information would need to be exchanged as it would all be publicly available. Second, until CbCR are made publicly available by multinationals, we encourage countries to require the local subsidiaries of multinational corporations to file a CbC report with local authorities in case their authorities cannot obtain this report via automatic information exchange, regardless of the reason.

6.1 Public disclosure of CbCR data

One of the purposes of CbCR is to enable reliable tracking of economic activity of multinational companies. One could argue that the CbCR does not involve confidential information. This explains why the European Union already requires banks and some extractive companies to publish this data, and some companies such as Vodafone have proposed to make their CbCR public (Knobel 2018b). However, the current OECD reporting requirements do not make essential information from the CbC reports publicly available – rather, the reports are shared via bilateral information exchange relationships. Therefore, data on the activity of a multinational corporation headquartered in country A that is collected through CbCR can be accessed only by selected authorities in specific countries where the multinational operates, and only if those countries meet all the OECD requirements described below. This cumbersome approach is non-transparent as it does not allow public accountability. It is not enough to know that a country has the applicable framework and that it is actually receiving the CbC report. It is just as important to know that they are actually using it to detect tax avoidance, on which some authorities have a bad track record. For example, the EU Commission published statistics on the Directive of Administrative Cooperation on automatic exchange of financial account data (DAC 2), revealing that some countries were not using the received information at all: "during the first year of DAC2 exchanges, (…) Bulgaria, Slovakia and Malta, reported not having opened the files received. (…) Nine states reported not using the information received via DAC2." (European Commission 2018) The same could happen with CbC reports.

This cumbersome OECD approach also introduces a bias against some countries, often developing ones, which have not yet established their network of information exchange (Knobel and Cobham 2016).

The relevant literature recognizes three critical channels of profit shifting in multinational corporations: (i) debt shifting, (ii) strategic relocation of intangible assets, and (iii) strategic transfer pricing, i.e., manipulating intra-group exports and import prices. Currently, according to financial reporting standards, multinationals consolidate these intra-group transactions with regular third-party trade in the annual financial statements. Therefore, possible purposeful mispricing and other aggressive tax planning strategies stay hidden from the public. The current OECD framework for CbCRIE thus blocks access to reliable information already collected about multinationals for trading partners, possible investors, consumers as well as financial regulators, and tax authorities in many cases.

Our key policy recommendation is to require public disclosure by all countries of firm-level CbCR data collected from individual multinationals. In principle, any jurisdiction can require all multinational companies incorporated and operating under its laws (including subsidiaries, branches, and holding companies) to publish financial information in their accounts on their global activity on a country-by-country basis. Appropriate reporting requirements can be implemented either through regulations issued by the stock exchange or by a legal or regulatory provision enacted by the competent regulatory or legislative body (Tax Justice Network 2018). Effectively, public disclosure of Country-by-Country reports would mean that the current system of information exchange would become redundant as all data would be publicly available. This new framework would bring several advantages. If public country-by-country information were available, investors and other market players would be better able to evaluate if a given corporation is exposed to reputational tax risks by relying on complex networks of subsidiaries in secrecy jurisdictions and tax havens, or whether it is heavily engaged in conflict-ridden countries. Tax authorities and audit institutions would be better able to make risk assessments of particular sectors or companies to guide their audit activity by comparing profit levels or tax payments to sales, assets and labour employed (Tax Justice Network 2018). It would further enhance additional control by the public and researchers, reduce bias towards more developed countries (which is present with the current system of information exchange, as discussed above), and eliminate gaps and loopholes which are present in the current rules (Knobel and Meinzer 2014).

In the ongoing first stage, the current threshold (of 750 million EUR in turnover) for companies that are required to file CbCR does have its merit – it prevents smaller companies from incurring losses due to higher reporting costs. However, once the system is well established and standards are developed, it would be desirable to impose CbCR requirements on smaller firms as well. In less developed countries, the firms generally reach lower values of turnover, and these countries would thus be prevented from benefiting from CbCR to a large extent. Instead, countries could set their own thresholds that would be lower than those set by other countries. The existing research (e.g., Janský and Palanský 2019, Cobham and Janský 2018) shows that low and lower-middle-income countries incur higher (as compared to more developed countries) tax revenue losses relative to their GDP as a result of international profit shifting. These countries could greatly benefit from using the lost tax revenue to develop local infrastructure more quickly and fund social programs that are required to accelerate economic growth. Thus, making CbCR data publicly available even for smaller multinationals could effectively lead to faster development in low- and lower-middle-income countries.

The form of the reporting to be made publicly available would be, in an ideal scenario, more comprehensive than the current reporting requirements. In particular, we recommend following the proposal of the Global Reporting Initiative (GRI), a leading sustainability reporting standard setter. GRI has published a tax reporting standard comprising full public disclosure of comprehensive CbCR in December 2019 (Global Reporting Initiative 2019). This standard would ensure that comprehensive information on multinational corporate activities is available in the public domain for use by different stakeholders (Bou Mansour 2019). However, as a voluntary standard, it will not be possible to address all loopholes and to ensure a level playing field. Therefore, multinational corporations of all sectors, listed and non-listed, should be required through an international binding convention to disclose critical information in their annual financial statements for each country in which they operate. This information should comprise their financial performance, including sales, purchases, and financing costs, all split by an intra-group and third party, pre-tax profit, labour costs, and the number of employees. Besides, the cost and net book value of its physical fixed assets, the gross and net assets, the tax charged, actual tax payments, tax liabilities, and deferred tax liabilities would be published on a country-by-country basis. Importantly, any standard should require, as is the case with the GRI tax standard mentioned above, and in contrast to the confidential OECD CbCR rules, that the CbCR reconciles with the multinational

companies' consolidated financial statements. It is worth noting that small- and medium-sized enterprises that operate in only one country are required by the nature of their business activity to report information in their annual financial statements that we propose here for multinational companies. The present rules of the game, therefore, disadvantage smaller enterprises relative to multinational corporations (Tax Justice Network 2018).

At the time of this writing, in January 2020, the OECD had planned to be already publishing aggregate statistics on CbCR collected from all countries that participate in the framework. However, the publication of this data has been postponed and the United States thus remain the only country in the world to publish these aggregate statistics (with Germany planning to join soon, Tax Justice Network 2020).

6.2 Robust local filing requirements

One could argue that the number of relationships to exchange CbCR automatically is actually irrelevant because local authorities would still be able to receive the CbCR data through two other ways allowed by the OECD. However, deliberate decisions by some countries such as choosing voluntary secrecy (to send but not to receive CbC reports) suggest that the other available means to access the CbCR will not always be pursued.

The existing OECD framework for the exchange of CbCR data requires as conditio sine qua non to have an international agreement between the local authority where the multinational operates and the country where the multinational is headquartered. This international agreement may be based on multilateral and bilateral agreements: 1) The Multilateral Convention on Administrative Assistance in Tax Matters, 2) Double Tax Agreement, or 3) Tax Information Exchange Agreements (OECD 2019). If this first condition of having an international agreement is met, there are three possibilities for a local authority to access the CbCR of a multinational operating there. First, if there is also a competent authority agreement (CAA) such as the Multilateral Competent Authority Agreement (MCAA) in force between both countries, the CbCR will be sent automatically by the headquarters' jurisdiction to the local authority. Second, if there is no CAA between both countries, then the multinational may appoint a subsidiary in a different country to file the CbCR, so that this second country will automatically send the CbCR to the local authority (assuming that this second country does have a CAA with the local authority's country). This is called surrogate filing. The third case refers to local filing. If none of the other two options are available (and the local authority is not refusing to sign an agreement with the headquarters' country), then

the local authority may request "local filing", requesting the local subsidiary of the multinational to file the CbCR (this third case involves no international exchange of information). All of these three options necessitate a binding international agreement between the local authority's jurisdiction and the jurisdiction where the multinational has its headquarters.

In addition to having all the agreements mentioned above, the OECD requires countries to comply with more conditions, including confidentiality provisions and rules for appropriate use of the received CbCR data to be able to keep receiving CbCR data, either internationally or locally. One of the key constraints of the OECD conditions relates to this: "the information in the Country-by-Country Report should not be used as a substitute for a detailed transfer pricing analysis of individual transactions and prices based on a full functional analysis and a full comparability analysis. The information in the Country-by-Country Report on its own does not constitute conclusive evidence that transfer prices are or are not appropriate. It should not be used by tax administrations to propose transfer pricing adjustments based on a global formulary apportionment of income. […] Jurisdictions should not propose adjustments to the income of any taxpayer on the basis of an income allocation formula based on the data from the Country-by-Country Report." (OECD 2017). These constraints prevent jurisdictions from efficiently countering illicit financial flows through tax adjustments that are based on determining misaligned profits of large multinationals in a simplified manner, and instead reinforces the jurisdiction's commitment to the OECD authorised transfer pricing approaches, which work largely to the detriment of lower income countries (Picciotto 2018, 44).

As described above, the OECD approach is cumbersome, complex, and limits the use of the CbCR data by local authorities. In line with Tax Justice Network (2018), our second policy recommendation is that countries require local filing (the third method to access the CbCR data mentioned above), not according to the OECD conditions, but whenever the local authorities cannot receive the CbCR from another country, for whatever reason (regardless of whether there is an international agreement or not with the headquarters' jurisdiction). This is referred to as "robust" local filing, because it ensures that the CbCR will always be accessed by a local authority: either through automatic exchanges or from a local subsidiary.

In 2018, the Financial Secrecy Index revealed, as part of its Key Financial Secrecy Indicator 9, that 19 jurisdictions were implementing robust local filing: Australia, Austria, Belgium, Canada, China, Denmark, France, Germany, Gibraltar, Hong Kong, Iceland, India, Ireland, Italy, Jersey, South Korea, Spain, United Kingdom and Uruguay. This conclusion was

reached based on a legal analysis of individual countries' legislations. However, further decisions by many of these countries to amend their legislation to comply with the OECD suggest that their original domestic laws establishing robust local filing may have been interpreted as such merely because of poor legal wording rather than an intention to apply robust local filing. An alternative explanation could be that the pressure by the Global Forum's peer reviews has resulted in countries adjusting their laws to avoid getting bad marks in the peer review assessment. In 2020 the Financial Secrecy Index revealed that only 9 countries still have robust local filing: France, Germany, Gibraltar, India, Russia, Spain, Taiwan, Uruguay and Vietnam.

These countries applying robust local filing will be able to obtain the CbCR even if they do not have an international agreement with the headquarters' country. However, it will be up to each country to decide to request either surrogate filing, local filing or robust filing, and if they access the information, to use it effectively to address tax abuse. In any of these cases, the public will have no access to the CbCR nor to know whether authorities are using it effectively. For this reason, not even robust local filing is a good replacement for our first policy recommendation – public disclosure of CbCR data at firm-level.

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