WHY TAX HAVENS CAUSE POVERTY

WEDNESDAY, JUNE 15, 2011

BBC explains tax scam in UK's Private Finance Initiative

BBC Radio 4 has just run a **brilliant programme** looking at Britain's Private Finance Initiative, which seeks to fund public projects with private capital (and get some of the costs off the government's books in the process.) It's been excoriated for inefficiency and abuse many times - and it's currently **being investigated** by the UK's National Audit Office for the umpteenth time.

Here's what PFI does, in a nutshell. A company builds, say, a hospital, and contracts to provide a range of specified services (though inside that latter part, scams abound). Private investors stump up money, under a deal that they are to be repaid through earnings from the hospital - principally, at the end of the day, taxpayers' money through the National Health Service funding of hospitals.

What happens, though, is that after the initial investments - the primary PFI market, one might call it - come the secondary investments: these PFI companies sell on these stakes - in effect, rights to receive a future income stream - on to others.

Before getting directly to the tax justice angle, let's start with information the programme digs out on astounding profit levels at PFI, with the help of a private sector analyst, Dexter Whitfield of the **European Strategy Services Unit**.

One such project they looked at - a hospital in Portsmouth suffering huge redundancies and ward closures - involved a construction firm, Carillion, putting in £12 million, and then selling its stake for £31m - a 160% nominal mark-up. That was high - but Whitfield estimated that the *average* mark-up for the health sector has been 66.7%.

Which raises a key question: has the taxpayer got value for money?

Well, first of all, it's hard to be sure. Margaret Hodge MP, Chair of the Public Accounts Committee, notes:

> "There has to be transparency around the system – so that if there is some profit over time in the funding of these pfi contracts, that profit can be shared with the taxpayer."

ABOUT ME

TJN

The Tax Justice Network (TJN) is an international, non-aligned network of researchers and activists with a shared concern about the harmful impacts of tax avoidance, tax competition and tax havens. www.taxjustice.net

VIEW MY COMPLETE PROFILE

PREVIOUS POSTS

shows that the government hasn't been able to keep up with who's doing what.

Note that when these profits are made on the secondary market - none of that, at all, goes back to the taxpayer. Now here comes the tax justice bit.

The government has a ready reply to those who say the taxpayer got a bad deal: if there are large profits on equity sales, then the government gets its share through capital gains tax. It's a slick argument - only the BBC reveals the gigantic fly dirtying this ointment: tax havens. This abridged transcript of part of the programme (we hope the BBC won't mind our doing this - it's an issue of tremendous public interest) highlights what's going on. (The comments may not be 100% accurate: this section starts at about 27:45 minutes in)

> **BBC:** One of its reasons [for justifying the super-profits] is that these profits are subject to capital gains tax, so the exchecquer gets a slice of them anyway. But one of the noticeable facts about the funds which have accumulated shareholdings in PFI is how many of them are based in tax havens. Guernsey and Jersey are particularly popular.
> . . .
> Nonetheless,the chairman of the **PPP Forum** [a PFI lobbying group] David Metter, argues that the Treasury is right to keep its hands off.
>
> **Metter:** “One has to pay tax on the capital gaims. You are already paying 30%. The question is whether the public sector should demand more or to increase the tax on this type of investment activity.
>
> **BBC:** is tax paid on those capital gains, if they are based in a Channel Islands tax haven?
>
> **Metter:** Well, the first thing to say is that all PFI project companies are UK based, and all of these companies pay tax as UK companies.
>
> **BBC:** But the parent companies tend to be based in tax havens, and so what happens then to the capital gains.?
>
> **Metter:** I was coming on to that. The next level is the question of shareholders and also the lenders to these project companies. We are attracting investment from all over the world, where often the lenders and the equity investors will be based in one tax environment investing into another tax environment, so they will be looking quite hard at their tax plannig and their investment strategy, since tax is a cost to their investment.
>
> **BBC:** when yopu say tax is paid – if they are based in tax havens, that tax

> **BBC:** Quite – so when you say there is a benefit for the taxpayer from capital gains tax (CGT) - that's not true if the company's based offshore.
>
> **Metter:** If the company is offshore, it may not be liable for CGT under certain circumstances. I am no expert in this area – my guess is this is a matter for tax lawyers.
>
> **BBC:** To clarify this crucial point, we turned to Richard Murphy, to explain the potential advantages in being based offshore:
>
> **Murphy:** In principle, an infrastructure fund that owns shares in private equity projects is liable to CGT if– and it is a very imporant if – they are resident in the UK. If the inferastructure fund is located in a tax haven eg the Channel Islands where there is no tax on those companies and certainly not on capital gains – they avoid that Capital gains tax liability altogether. Because it is where you *own* the shares that matters in this case – if those shares are owned outside the UK, even if they are in UK companies, there is no capital gains tax on their sale.
>
> **BBC:** So when the Treasury gave as one of its reasons for not demanding a slice of profits from PFI sales to the taxpayer, the Treasury was wrong.
>
> **Murphy:** The treasury has shown itself to be remarkably naïve with reard to private equity ownership. It seems to be quite oblivious to the fact that UK capital gains tax is residence based – it is incredibly easy to get around. Simply own the shares in an offshore company, make sure that company is managed offshore, and the company is outside UK tax.

It's heartening to see that the public, at least, is waking up to the scandal. This separate BBC story, entitled **Portsmouth hospital NHS cash 'destined for tax haven'** describes local unions in Portsmouth getting agitated about the Carillion deal.

Now what of the companies doing all this dealing on the secondary market? An insider the BBC contacted paints a picture of what's been happening:

> One of the phenomena we've seen is you've got what you might call 'aggregators' – sitting on large numbers of these PFI deals. Instead of having all these different deals for different schools and hospitals, we now have amuch smaller number of players who own these hospitals – who have bought these up and are aggregating them into large funds. If intermediaries can make large profits – that means almost by definition that the taxpayer got a bad deal at the start, otherwise these super-profits couldn't be made.

A last word here, from Treasure Islands, in this vein.

> often the predator unlocks value simply by being better at obtaining abusive, unproductive offshore tax privileges. Some make their best profits by seeking out and harvesting those small, genuinely innovative companies that haven't yet managed to unlock those abuses for themselves. . . . Debt rises, and ordinary people pay more tax or see their schools and hospitals fall into disrepair. And if the predators leave their earnings offshore they can defer tax on them indefinitely."

It really is the dark side of globalisation. And some of our leaders seem only too happy to let it continue. Do all these sales in the secondary market make finance more efficient? Keynes had a brilliant quote here:

> "Experience is accumulating that remoteness between ownership and operation is an evil in the relations among men, likely or certain in the long run to set up strains and enmities which will bring to nought the financial calculation."

Indeed. Add the tax scams to all this, and you've got a real mess.

POSTED BY TJN AT 2:15 AM

0

---

1 COMMENTS:

independent financial advisers said...

Taxes are collected from the people and it will serve as budgets for the upcoming projects of the government. It is just like they people are giving help on this field. Any issues on this matter would be a big deal for the people since they do own the money.

1:09 AM

POST A COMMENT

LINKS TO THIS POST:

CREATE A LINK

<< Home