

KEY FINANCIAL SECRECY INDICATORS

Key Financial Secrecy Indicator 12: Consistent Personal Income Tax

What is measured?

This indicator analyses whether a jurisdiction applies a Personal Income Tax (PIT) regime which is compatible with the (progressive) income tax systems of most jurisdictions worldwide, or if its laws provide laxity around citizenship and/or residency, and if its personal income tax legislation is narrow in scope, resulting in financial secrecy sinks for tax dodgers and criminals.

Two dimensions of a jurisdiction's legal framework are jointly analysed.

- 1) Comprehensive scope** of a PIT: it assesses if there is any PIT at all; if worldwide income is subject to this tax (instead of a territorial or remittance system); if a uniform tax regime applies (no opt-outs through lump sum taxation etc.); and if it is complete (including capital gains; no exemption or exclusion of specific types of income).
- 2) Tight citizenship and/or residency:** it assesses whether (i) citizenship (passports) can be acquired against a passive investment or payment only after a period of more than two years of physical presence in the jurisdiction (instead of obtaining citizenship against any investment or payment made by the person within a period of 2 years or less); and (ii) a certificate of "residency" can be acquired against a passive investment or payment.

For the purpose of this KFSI, a zero points secrecy score [full transparency] will be awarded to jurisdictions which levy a PIT with a comprehensive scope, regardless of the citizenship or residency rules. Jurisdictions that fail on the comprehensive worldwide personal income tax receive a partial secrecy score, depending on their scope and the tight or lax citizenship and residency rules. The highest 100 point secrecy score [full opacity] applies to jurisdictions that provide lax citizenship or residency rules while not levying any personal income tax. These jurisdictions export financial secrecy by creating incentives for non-

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residents to abuse passports/citizenship and residency certificates to circumvent tax information exchange and to escape litigation and law enforcement.

The secrecy scoring matrix is shown in Table 12.1, with full details of the assessment logic given in Table 12.5 below.

Table 12.1: Secrecy Scoring Matrix KFSI 12

		Citizenship/Residency	
		<u>Tight</u> <u>Citizenship/</u> <u>Residency</u> <u>acquisition</u>	<u>Lax</u> <u>Citizenship/</u> <u>Residency</u> <u>acquisition</u>
Regulation [Secrecy Score: 100 points = full secrecy; 0 points = full transparency]		Citizenship (by investment) only after at least 2 years of physical presence and resident status is not granted against investment	Citizenship (by investment) within 2 years of physical presence or resident status can be purchased
Personal Income Tax Regime	<u>No Personal Income Tax (PIT)</u> PIT does not exist or is not applied or a jurisdiction is part of Annex A under the MCAA (voluntary secrecy)	75	100
	<u>Incomprehensive PIT Regime</u> While there is a PIT regime, any of the subsequent limitations apply: Territorial scope: Only domestic source income is included, or worldwide income only on a remittance basis OR Incomplete scope: capital gains are not taxed, or specific types of income are exempt or excluded OR Opt Out Available: (covering worldwide income), there is an opt out	37.5	75

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	from the overall PIT regime (e.g. lump sum taxation, non-domiciled regime, etc.)		
	<p><u>Comprehensive PIT Regime</u> There is one single uniform PIT that taxes worldwide income (and the jurisdiction has not chosen voluntary secrecy under MCAA's Annex A)</p>	0	

All underlying data can be accessed freely in the  [Financial Secrecy Index database](#) (IDs 374, 435 and 489).

For a personal income tax to be considered **comprehensive in its scope**, there needs to be one **single uniform PIT** that applies the same tax base rules and a rate above zero percent equally to all natural persons considered tax residents. Any opt out from the general tax regime in a certain jurisdiction, e.g. through lump sum tax regimes for new residents, or residents considered to be non-domiciled for tax purposes, would imply that the jurisdiction does not have a single uniform PIT.

Furthermore, the single uniform PIT's tax base would need to include all income a tax resident is entitled to or paid anywhere in the world (**worldwide income criterion**). If (some or all) overseas income can remain untaxed, either because the jurisdiction only applies a territorial tax base or taxes on a remittance and/or accrual basis only, the PIT would not be considered comprehensive. For the question of a comprehensive PIT, the top personal income tax rate is disregarded.

In addition, the PIT needs to be **complete** in terms of the income covered. All capital gains earned worldwide should be part of PIT or be taxed separately – either as part of another tax, e.g. wealth tax, or independently – for the PIT to be considered complete. The same applies for any specific types of income, especially investment income: any investment income should not be exempt nor excluded from the overall tax base, or it should be taxed independently. For example, a jurisdiction that does not tax income, dividends, capital gains derived from foreign sources is therefore considered as having an incomplete PIT. Many jurisdictions, however, allow for tax exemption on capital gains from the sale of a private home or from real estate held longer than a certain number of years. We consider the PIT to be complete as long as the exemption from capital gains taxation on real estate applies after holding it for longer than 3 years or if it only applies to a privately held home.

In circumstances where jurisdictions exempt dividends paid by domestic companies or capital gains derived from the sales of domestic companies'

shares, we do not consider the PIT as incomplete, given that these exemptions are limited to income derived from domestic sources. By the same token, exemptions on employment income are out of scope of this indicator and are not taken into account in the PIT assessment.

For **citizenship programs to be considered tight**, citizenship and passports by investment or monetary payment should not be provided without a requirement to reside at least 2 years in the jurisdiction (whereby a year of residency means a physical presence of at least 183 days).

For **residency programs to be considered tight**, residency permits should not be available in exchange for passive investments, payments or on financial grounds only. If permits are available under such conditions, these should be revoked if the individual does not maintain a significant physical presence (more than 183 days in a year) in the jurisdiction. A resident permit is different from a simple tourist visa if it allows the individual to stay longer than one year in the jurisdiction. Permits that need to be renewed by a simple formal procedure after one year are also considered.

Consequently, jurisdictions that issue passports or residency permits to individuals who only purchase real estate or other financial assets in the country or show proof of high-net-worth will be considered as having lax citizenship and residency rules.

Jurisdictions identified by the [OECD](#) as having residency/citizenship programmes that potentially pose a high-risk to the integrity of the Common Reporting Standard (CRS)¹ are automatically considered for this indicator as having a lax citizenship/residency acquisition.

The information for this indicator was drawn mainly from the following sources: a) [OECD Automatic Exchange Portal](#)²; b) A database of residency and citizenship programmes entitled: "[Residence and Citizenship by Investment: An Updated Database on Immigrant Investor Programs](#)"³; c) Results of TJN Survey 2019⁴; d) Publication entitled: "Buying in: Residence and Citizenship by Investment"⁵; d) European Parliament publication entitled: "Citizenship by investment (CBI) and residency by investment (RBI) schemes in the EU"⁶; e) in some instances, we have also consulted additional relevant websites or the local legislation of jurisdictions.

Whenever we did not find any information online about residency/citizenship by investment programmes in a certain jurisdiction, we assumed these programmes do not exist and thus citizenship/residency acquisition is considered tight for that jurisdiction.

All underlying data can be accessed freely in the [Financial Secrecy Index database](#). To see the sources we are using for particular jurisdictions please consult the assessment logic in Table 5 at the end of this document and search for the corresponding info IDs (**IDs 374, 435 and 489**) in the database report of the respective jurisdiction.

Why is this important?

Most jurisdictions have adopted the *residence principle* with regards to the taxation of individuals. A jurisdiction levies taxes on the worldwide income received by an individual who resides within its boundaries. The underlying logic is that individuals who are resident in one country will make use of the country's public services which are funded by tax revenues⁷. It is not decisive *where* an individual derives their income from, therefore their worldwide income should be taken into account.

Jurisdictions that only tax income on a territorial basis, apply lump sum taxation, exempt some types of income, or do not use any income tax at all are therefore attractive for individuals wishing to escape law enforcement, to avoid taxation or wishing to avoid the assessment of their worldwide income. Without assessment of their worldwide income, the information available on any individual's finances is severely constrained. If an individual is engaged in illicit financial activity in another jurisdiction, relevant financial information available for answering requests for information exchange may not exist, shielding that individual from effective prosecution and facilitating the escape from accountability.

But also for a jurisdiction applying the residence principle, its enforcement relies on a tax administration's capacity to correctly assess the worldwide income of the jurisdiction's residents. This might be hampered by other jurisdictions with incomprehensive income tax regimes and/or jurisdictions that provide passports or residency status against investment. The reasoning for the way lax citizenship and residence by investment programs may lead to secrecy spill-overs resulting in lower or no taxation elsewhere, is explained below.

Until recently, tax administrations have relied almost exclusively on information exchange upon request: If a jurisdiction suspected an individual of tax evasion it could request information from the tax administrations of other jurisdictions ([see KFSI 19 on bilateral treaties for information exchange upon request](#)⁸). But if a jurisdiction does not tax worldwide income (or if worse- it does not levy any income tax) it will collect only insufficient (or no) tax information on its residents. Therefore, such jurisdictions are especially attractive for any individual who does not wish financial information to be collected.

To address some of these deficiencies and to rely less on the jurisdictions' specific tax systems, the Common Reporting Standard (CRS) for automatic exchange of information for tax purposes was devised and published by the OECD in February 2014. It provides a multilateral framework for exchanging details of accounts owned or controlled by individuals between participating jurisdictions, i.e. jurisdictions that have signed the [Multilateral Competent Authority Agreement](#) (MCAA). As of November 2019, 105 jurisdictions have signed the MCAA,⁹ although not every signatory exchanges data with every other signatory (see [KFSI 18 for details](#)¹⁰).

Financial institutions (FIs) in jurisdictions that have signed up to the CRS (i.e. 'participating jurisdictions'), will be required to collect and report account information about, among other, any (natural person) account holder or any natural person controlling some types¹¹ of companies, trusts or foundations, as long as any of these individuals (natural persons) are resident in any jurisdiction with which the former jurisdiction has an activated exchange relationship. The account holders and controlling persons are thus considered "reportable persons".

However, even a jurisdiction which has signed and implemented the CRS and has activated exchange relationships, can still contribute to financial secrecy. A crucial part of the CRS is the correct determination of an individual's residence for tax purposes because the tax residency determines to which jurisdiction the collected information will be sent.¹² In order to ascertain tax residency pursuant to the CRS, financial institutions of a participating jurisdiction need to collect specific information of any "reportable person".¹³ Table 12.2 underneath provides an overview of the process and indicia determining tax residency depending on the type of account.

Table 12.2: Determination of tax residence under the CRS

Pre-existing account		New account
Lower value (Less than 1 M USD)	Higher value (More than 1 M USD)	Any value
<p>Residence address based on documentary evidence</p> <p>Acceptable documentary evidence:</p> <p>Any government ID containing a current address such as identity card; driving license; voting card; certificate of residence</p> <p>OR</p> <p>When those do not contain a current address or any address: Formal notifications or assessments by a tax administration; electricity bill; water bill; landline bill; gas/oil bill</p> <p>OR</p> <p>Self-declaration under penalty of perjury</p>	<p>Residence address based on documentary evidence (see left column)</p> <p>AND</p> <p>Search for indicia indicating residence in reportable jurisdiction in bank's records</p> <p>Indicia are:</p> <p>Former residence address; mailing address; telephone numbers; standing instructions of fund transfer to an account in reportable jurisdiction; power of attorney to a person with address in rep. jurisdiction; "Hold-mail" or "In care of"-address in rep. jurisdiction</p> <p>AND</p> <p>Enquiry with relationship manager</p>	<p>Residence address based on documentary evidence (see left column)</p> <p>AND</p> <p>Comparison with data obtained under Anti-Money-Laundering and Know-Your-Customer procedures for other regulatory purposes which generally also require a documented permanent address and a proof of identity through passport</p>
<p><i>Source: CRS commentary on Section III¹⁴</i></p>	<p><i>Source: CRS Section III, §10</i></p>	<p><i>Source: CRS Section IV, FATF recommendation R.5¹⁵</i></p>

For a financial institution's pre-existing accounts of lower value (less than 1 Million USD), an individual is only required to self-certify its residence with a government document containing a current address (for example an ID, passport, driving license, residence certificate) or a utility bill or tax assessment containing the individual's name and address.¹⁶ However, the Common Reporting Standard requires the financial institution in the case of higher value accounts (more than 1 Million USD) to search its records for indicia (such as former residence addresses, other mailing addresses, telephone numbers, or instructions to transfer funds) that could also suggest a residence in another jurisdiction.¹⁷ If the financial institution found contradicting indicia (there is indicia about more than one

jurisdiction or the indicia does not match what the account holder declares as his/her residency) the financial institution has to obtain an explanation from the account holder. If the FI receives no explanation or if it is not satisfied with the explanation, the FI would need to send information to any jurisdiction that it finds indicia for.¹⁸ Moreover, in the case of new accounts, a financial institution must test the residence information provided by the client for reasonableness, notably based on information obtained through Anti-Money-Laundering and Know-Your-Customer procedures.¹⁹

This is where citizenship-by-investment or residency-by-investment comes into play. Economic citizenship programmes, passports of convenience, certificates of residence and similar phenomena and associated challenges of governance and integrity have been debated for a long time.²⁰ In recent years, however, several countries have started to loosen the criteria for obtaining citizenship and/or residency and provided various "economic citizenship programmes" where foreign individuals can [acquire passports](#)²¹ or residency permits by paying money into a state fund, investing in financial assets or real estate, renting an apartment in the jurisdiction or else.²²

An account holder living in country A (but trying to remain hidden from country A's authorities) could thus use a passport or a certificate of residency from country X to convince the financial institution that he/she is resident (for CRS purposes) in country X, even if in reality that person resides and works in country A. For example, if the client can produce a passport indicating citizenship or a certificate of residency indicating residency in the same jurisdiction as the FI, there is a greater probability that the person will be considered a non-reportable person.²³

Therefore, citizenship-by-investment and residency-by-investment programmes constitute a significant obstacle for the automatic exchange of information for tax purposes. Obviously, an individual wishing to evade taxes has an incentive to falsely declare tax residency in a jurisdiction that only applies a territorial income tax system, other kinds of incomprehensive income taxation or (worse) does not levy income tax at all.

Therefore, even if all jurisdictions become 'participating jurisdictions' to the CRS, the selling of passports or residency certificates by a jurisdiction could enable tax dodgers to avoid their information being reported to their relevant jurisdiction of residence by either:

- a) falsely declaring residence in a jurisdiction which doesn't have a comprehensive personal income tax and providing a passport or certificate of residence by the same jurisdiction. This way, the

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account information will end up being transmitted to the tax haven jurisdiction which will then ignore it or parts of it, given the account holder will not be liable for worldwide income tax there;

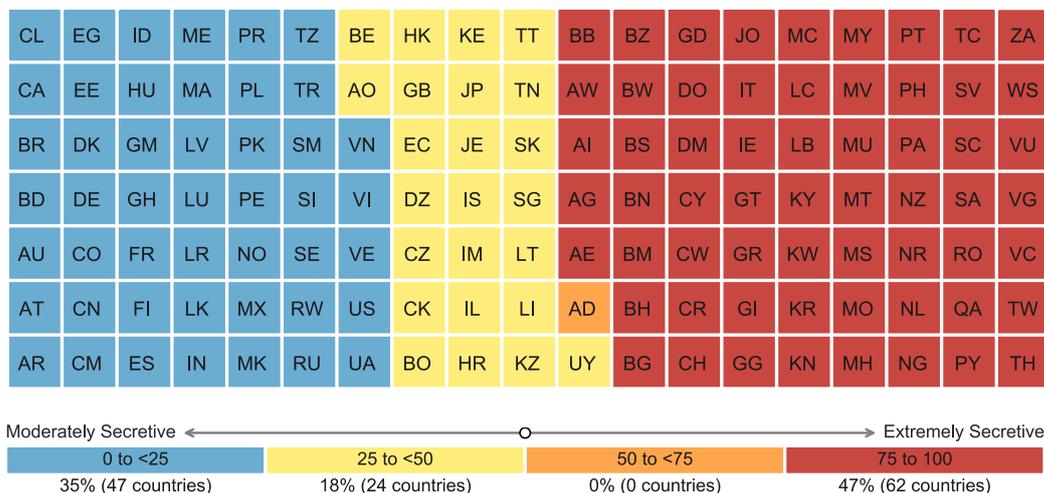
- b) falsely declaring residence in a jurisdiction which is listed in [Annex A](#) of the MCAA (i.e. jurisdictions which only send, but not receive any account information) or in a jurisdiction which is not committed to the CRS. This way, information will not be collected nor reported on those account holders.

And even if an individual was found guilty of tax evasion or other financial crimes, citizenship-by-investment or residency-by-investment could play another role. As Global Witness put it: *"After all, if the passport makes you a citizen of a country that has a non-extradition treaty with your country and enjoys strong rule of law you can sleep safe and sound in your luxury home".*²⁴

All underlying data can be accessed freely in the [Financial Secrecy Index database](#) (IDs 374, 435 and 489).

Results Overview

Figure 12.1: Consistent Personal Income Tax – Overview of Secrecy Score



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Figure 12.3: Voluntary Secrecy under MCAA's Annex A

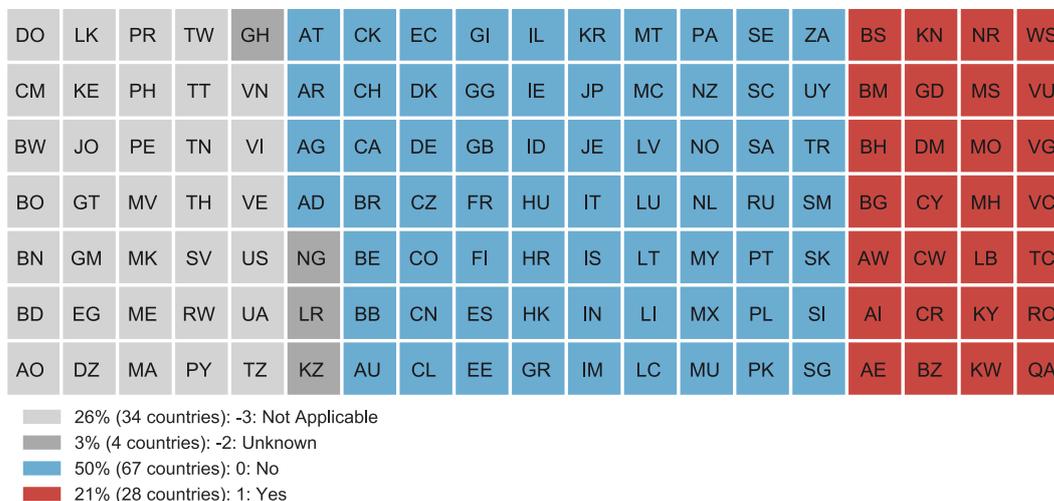
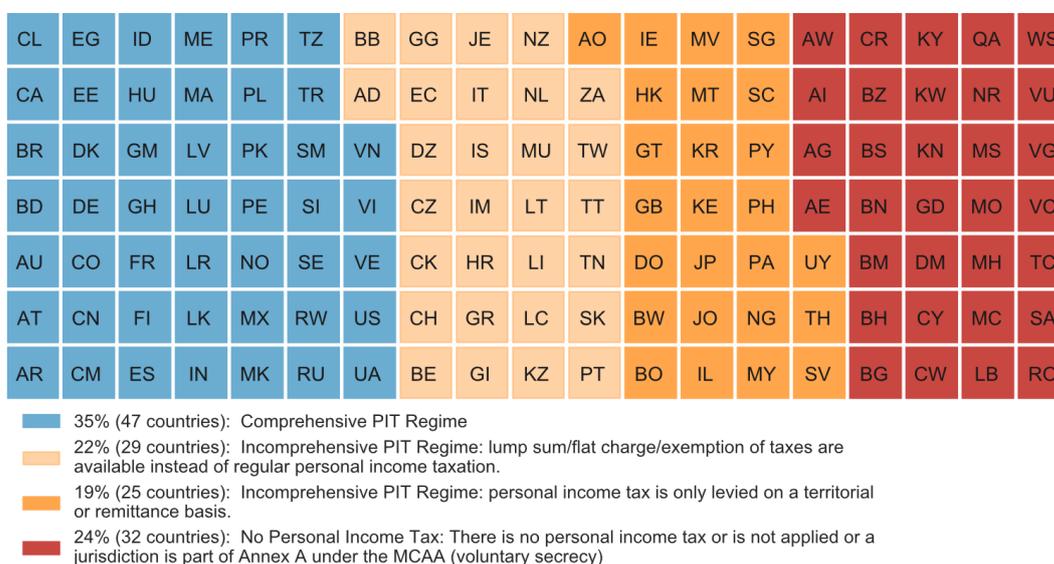


Figure 12.4: Comprehensive Personal Income Tax Regime

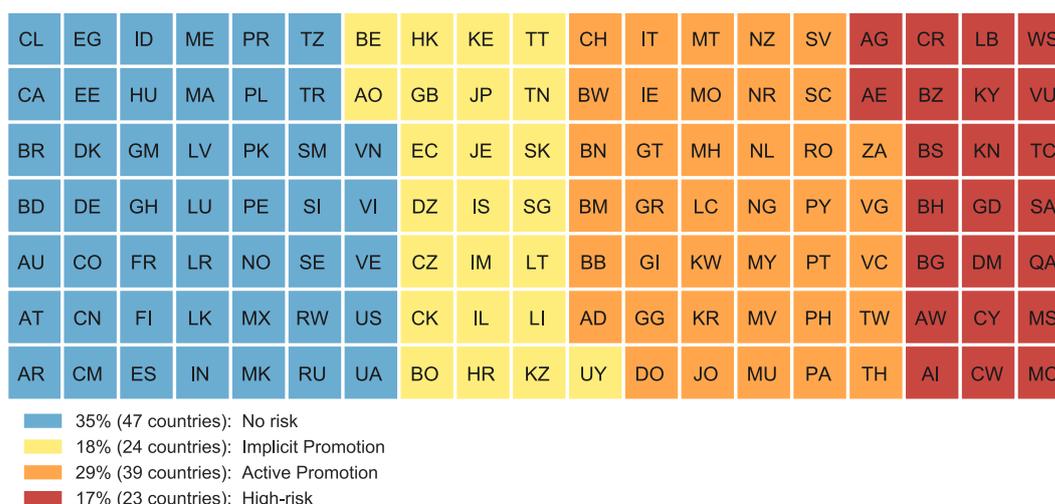


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Table 12.3: Consistency of Personal Income Tax Overview

	Secrecy Score	Number of Jurisdictions
<u>High-Risk</u> Lax Citizenship/Residency & either: (i) No Personal Income Tax; or (ii) Voluntary Secrecy under MCAA's Annex A (regardless of PIT regime)	100	23
<u>Active Promotion</u> (i) Lax Citizenship/Residency & Incomprehensive PIT; or (ii) Tight Citizenship/Residency & NO Personal Income Tax; or (iii) Tight Citizenship/Residency & Voluntary Secrecy under MCAA Annex A (regardless of PIT regime)	75	39
<u>Implicit Promotion</u> Tight Citizenship/Residency but Incomprehensive PIT Regime	37.5	24
<u>No risk</u> Comprehensive Personal Income Tax Regime (and no voluntary secrecy under MCAA's Annex A)	0	47

Figure 12.2: Consistency of Personal Income Tax Overview



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Table 12.4: Consistent Personal Income Tax - Secrecy Scores

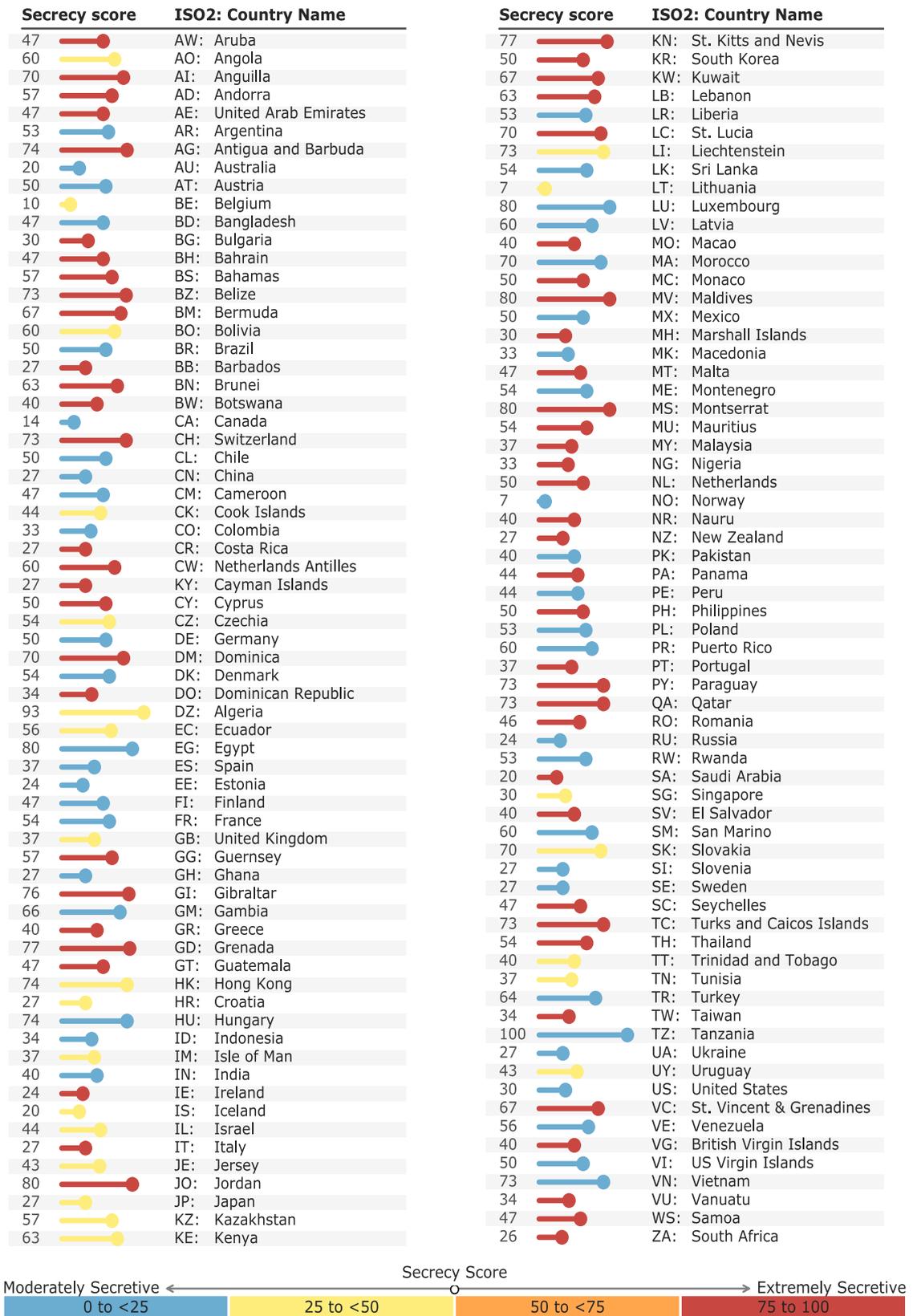


Table 12.5: Assessment Logic

Info_ID	Text_Info_ID	Answers (Codes applicable for all questions: -2: Unknown; -3: Not Applicable)	Valuation Secrecy Score
435	*Personal Income Taxation: Is there a personal income tax with a comprehensive scope?	0: No, there is no personal income tax; 1: No, personal income tax is only levied on a territorial or remittance basis; 2: No, lump sum/flat charge/exemption of taxes are available instead of regular personal income taxation; 3: Yes, there is a uniform personal income tax regime with a worldwide income tax base.	Integrated assessment of Personal Income Tax and Citizenship- or Residency-by-Investment Schemes. If there is a comprehensive personal income tax with worldwide scope, zero secrecy score. If no PIT or Annex A in CRS (see KFSI 18), and lax residency- or citizenship-by-investment rules: 100 secrecy score. Three intermediate scores for partial compliance (see Table 12.1: Secrecy Scoring Matrix KFSI 12).
374	*CRS MCAA Voluntary Secrecy: Has the jurisdiction chosen "voluntary secrecy" (listed under the MCAA's Annex A to prevent receiving information)?	YN	
489	*Citizenship-By-Investment and Residency-By-Investment Schemes: Can individuals acquire citizenship, passports or residency status in exchange for an investment or another payment without a prior requirement to spend more than 2 years in the jurisdiction?	YN	

Reference List

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<http://www.keepeek.com/Digital-Asset-Management/oecd/taxation/standard-for-automatic-exchange-of-financial-account-information-for-tax-matters_9789264216525-en> [accessed 14 February 2017]
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- Van Fossen, Anthony, 'Citizenship for Sale: Passports of Convenience from Pacific Island Tax Havens', *Commonwealth & Comparative Politics*, 45/2 (2007), 138–63
- Xu, Xin, Ahmed El-Ashram, and Judith Gold, *Too Much of a Good Thing? Prudent Management of Inflows under Economic Citizenship Programs*, 15–93 (2015)
<www.imf.org/~/media/Websites/IMF/imported-full-text-pdf/external/pubs/ft/wp/2015/_wp1593.ashx> [accessed 5 October 2017]

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- ¹ <https://www.oecd.org/tax/automatic-exchange/crs-implementation-and-assistance/residence-citizenship-by-investment/>; 22.12.2019.
- ² <https://www.oecd.org/tax/automatic-exchange/>; 22.12.2019.
- ³ Leila Adim, 'Residence and Citizenship by Investment: An Updated Database on Immigrant Investor Programs', 2019
<https://www.researchgate.net/publication/336746472_Residence_and_Citizenship_by_Investment_an_updated_database_on_Immigrant_Investor_Programs> [accessed 23 January 2020].
- ⁴ https://www.financialsecrecyindex.com/PDF/FSI2020_Questionnaire-MOF-NAO.xlsx; 22.12.2019.
- ⁵ Allison Christians, *Buying in: Residence and Citizenship by Investment* (Rochester, NY, 26 September 2017)
<<https://papers.ssrn.com/abstract=3043325>> [accessed 23 January 2020].
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- ⁷ Dietsch, P., & Rixen, T. (2014). Tax competition and global background justice. *Journal of Political Philosophy*, 22(2), 150-177., p. 159
- ⁸ <http://www.financialsecrecyindex.com/PDF/19-Bilateral-Treaties.pdf>; 22.12.2019.
- ⁹ <http://www.oecd.org/tax/automatic-exchange/international-framework-for-the-crs/crs-mcaa-signatories.pdf>; 22.12.2019.
- ¹⁰ <http://www.financialsecrecyindex.com/PDF/18-Automatic-Info-Exchange.pdf>
- ¹¹ Controlling persons will only be identified if the entity (company, trust or foundation) through which they hold an account is considered "passive" because most of its income is passive (e.g. interests, dividends, royalties, etc.).
- ¹² In principle, the only parameter that could quite clearly attribute tax residency of an individual to one jurisdiction and thus avoid both double-taxation and double-non-taxation is the test whether the individual effectively spends 183 days or more in the jurisdiction. However, since this is not always easy to assess and since it also theoretically possible that a frequently moving individual does not spend 183 days in a year in any jurisdiction, most jurisdictions use several indicators to determine tax residency, such as the disposal of a permanent home and the center of economic and personal interests of an individual.
- ¹⁴ OECD, *Standard for Automatic Exchange of Financial Account Information in Tax Matters. Including Commentaries.*, July 2014
<http://www.keepeek.com/Digital-Asset-Management/oecd/taxation/standard-for-automatic-exchange-of-financial-account-information-for-tax-matters_9789264216525-en> [accessed 14 February 2017].
- ¹⁵ Financial Action Task Force, *International Standards on Combating Money Laundering and the Financing of Terrorism & Proliferation - the FATF Recommendations*, 2012 <<http://www.fatf-gafi.org/topics/fatfrecommendations/documents/internationalstandardsoncombati>

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¹⁶ Model Competent Authority Agreement and Common Reporting Standard, Section III, B; Commentaries on the Model Competent Authority Agreement and Common Reporting Standard, Section III, B.

¹⁷ Model Competent Authority Agreement and Common Reporting Standard, Section III, B, C.

¹⁸ For pre-existing individual accounts: "A self-certification (and/or documentary evidence) would be needed in case of conflicting indicia, in the absence of which reporting would be done to all reportable jurisdictions for which indicia have been found." OECD, *Standard for Automatic Exchange of Financial Account Information in Tax Matters. Including Commentaries.*, 15–16.

¹⁹ As for new accounts, information collected pursuant to the anti-money laundering due diligence procedures is taken into account as part of a reasonableness test for determining the residency, but multiple reporting is not foreseen. For new accounts, sending information to multiple jurisdictions happens when there is a change of circumstances and the account holder does not explain the situation. In such case, information is sent to jurisdiction of original self-certification, and to the jurisdiction that is resulting from the "change of circumstances" OECD, *Standard for Automatic Exchange of Financial Account Information in Tax Matters. Including Commentaries.*, 129–46.

²⁰ For the "passports of convenience"-debate prior to 2007 see: Anthony Van Fossen, 'Citizenship for Sale: Passports of Convenience from Pacific Island Tax Havens', *Commonwealth & Comparative Politics*, 45/2 (2007), 138–63. A broader discussion of the issue is available by: Xin Xu, Ahmed El-Ashram and Judith Gold, *Too Much of a Good Thing? Prudent Management of Inflows under Economic Citizenship Programs*, 15–93 (2015)

<www.imf.org/~media/Websites/IMF/imported-full-text-pdf/external/pubs/ft/wp/2015/_wp1593.ashx> [accessed 5 October 2017].

²¹ https://www.theguardian.com/commentisfree/2017/sep/18/peak-injustice-world-without-borders-super-rich-buying-citizenship-migration?CMP=share_btn_tw; 23.01.2020. See also Karl Küpper and Oliver von Schweinitz, 'The Definition of "Residency" Under the Common Reporting Standard', *International Journal for Financial Services*, 2, 2015, 119–25.

²² See for example: Leila Adim, 'Residence and Citizenship by Investment: An Updated Database on Immigrant Investor Programs'; and Christians, *Buying In*. Examples of current citizenship by investment schemes, please consider [Cyprus](#), [Montenegro](#), [Dominica](#), [Malta](#), [Antigua and Barbuda](#), [Vanuatu](#).

²³ <https://francisweyzig.com/2017/09/24/defying-the-oecds-crackdown-on-tax-evasion/>; 23.01.2020.

²⁴ <https://www.globalwitness.org/en/blog/red-notice-golden-visas/>; 23.01.2020.