

## TAX HAVENS AND THE TERRORISM

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### ABSTRACT

In everyday language the term "tax haven" means economic and geographical area that offers a wide range of tax benefits where so called offshore companies are registered and carry on financial activities related to money laundering. Basically, an offshore company could operate under conditions of favorable tax only if it is recorded in a "tax haven." Using those companies situated in "tax havens", today, billions of US dollars are "recycled" in complicated financial operations supported by well-organized mechanisms and then, after "the black money" having origin in organized crime activities are reinserted in the legal economy and very often used to finance the terrorism.

**Keywords:** *tax heaven, organized crime, money laundering, offshore company.*

### 1. INTRODUCTION

The terrorism can be defined as a set of actions or threats endangering public order and affecting national security of a state [1]. These terrorist actions are always premeditated. Actions are motivated by extremist attitudes and aim to achieve political goals. These threats of terrorist targets both human and material factors in the sphere of state authority and civil society, as well. However, terrorist groups seek to capture public attention on them. For this, their actions were intended to produce psychological effects and strong emotional feelings. Basically, terrorist actions aimed at creating a state of fear, uncertainty and public panic. At present, the terrorist threat has gained a strong character borders. This is due to globalization, erasing the borders between states and enhanced mobility of people. In this situation actually add exacerbating ethnic and religious tensions in some areas of the world. Terrorist organizations are criminal groups that have a specific organization, logistics, recruitment and training system specific. They cannot operate without the necessary financial and material resources. For this reason, one of the most effective ways to fight terrorism is to prevent the financing of terrorist groups. Because of the way of action and immediate effects terrorist phenomenon has some similarities with the phenomenon of cross-border organized crime. However, beyond these similarities aims are totally different. Transnational organized crime is seeking financial or material benefits. Terrorist groups are pursuing political objectives - the destabilization of governments, winning autonomy or independence of territories, the release of imprisoned comrades etc. Cross border organized crime does not follow existing political and social system. Criminal activities must be conducted in a particular social setting. Therefore it takes a certain level of economic stability and social order to "thrive". There is direct links between money laundering and proceeds of crime and financing of terrorist groups. Profits from criminal activities are put in recycling circuit, so in the end the money appear legal and "honorable". Some of this money is sometimes used to finance terrorist groups. There are many theoreticians

and experts estimate that there are many cases in which money from recycling funds are used to finance terrorism. The terrorist activities can be divided into two different types: "individual initiative" and "organized initiative". A terrorist group interested to fulfill its aim planning in a rigorous way the final attack. But from thinking out the attack plan to the moment of the attack is a long way. In this period of time the group should gather intelligence, the technical means, and training of the terrorists and to have permanently the financial support. The financial support is a key element for terrorist groups.

Although there are many opinions, terrorist financing has two main sources:

a) the first source is the financial support given by different countries or organizations sympathetic. Organizations should have a large enough infrastructure to collect funds for terrorist groups. However, in recent years, sponsoring countries of the terrorism have come in decline. The place of these states was taken by wealthy sponsors. A rich person may provide substantial financial resources for funding terrorist groups. Terrorist groups differ from other criminal organizations taking in account the motivation and purpose. Organized crime groups are pursuing the profit and operate discreetly. The terrorist groups are operating not for financial purposes but for political aims. Terrorist groups are seeking to impose ideology and faith, using violence, threats and intimidation. Terrorist groups operate "on demand" and do everything possible to attract public attention about "operations" performed. For terrorist financing, funding source is usually "legal". The ultimate goal is not necessarily to attract more funds. Terrorist groups make calls to the community to raise funds for various purposes declarative. Most often goals are forged. Such fundraising is conducted on behalf of charitable organizations or charitable status. The collection is done by using patriotic, humanities, ethnic, national or historical reasons. Community members are convinced that giving money is for a good cause. In most cases, the charity is apparently legal for community that gives funds. Unfortunately, the money thus raised will be used to end lives and destroy property.

b) the second major source of money for terrorist groups is the profit from work that generates revenue. Often, terrorist groups are owner of factories, shops, transport means, real estate goods etc.

Of course, there are other possibilities for terrorist financing. Similar to criminal organizations, terrorist groups may gather money using different crimes or other illegal activity. After that, usually the money obtained from illegal activities is whitening and used in legal domain. Money obtained will be subjected to a recycling process. Basically, money laundering will intervene in this case. This is because black money proceeds of crime should be given an aura of respectability. Then they are returned to the legal circuit it and used in legal way. These banks, in pursuit of profit many years have refused to collaborate with state agencies. Most often, banks invoked in their secret banking operations. The banks put the conspiracy of the financial operations over law. Since 1980, the states of the world beginning to put the issue of customer identity checks on first place. Thus, gradually, countries have begun to introduce mandatory the identity checks for banks and financial institutions. Secondly, it was erased the limiting of the use of the safety deposit boxes. These boxes are attributed only to persons with whom the bank that was in business relationships or were reliable. In addition, has been established special training program for the staff of the banks. Staff must undergo training for identity control and to detect suspicious behavior of the customers. Also, for the first time, has been established for the first time the cooperation of banks with administrative and judicial authorities. To counter the financing of terrorism through money laundering is important to establish the criminalization of few actions. The conversion or transfer of property knowing that is originated from crimes is one of the priorities. Today, the money laundering is a complex activity involving many operators and the export of the funds in tax havens, using off shore companies [2].

## 2. TERRORISM ACTIONS IN WORLD

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### **3. TAX HAVENS AND THE OFFSHORE COMPANIES**

For complex financial activities, the operators involved in money laundering use the countries and geographical areas that the law provides favorable financial and tax conditions for offshore companies [2]. It should be emphasized that these offshore companies will not pay taxes not because they are using fraudulent accounting operations to get rid of the tax system, but because the applicable law in these countries and geographical areas provide the opportunity to avoid full or partial payment of taxes in the legal way. The tax havens have a crucial role in the mobility increasing of the fluxes of capitals and the interdependencies between different states, companies and citizens. In these complex equations, a key role is played by offshore companies. Offshore companies are companies created by the money laundering operators used to reduce taxes on profits of the "mother companies". The "mother company" is located usually in areas of high taxation and in its effort

to maximize the profits of these companies in tax haven areas. Often in practice, the "mother company" among other commercial operations "sells" to offshore company certain goods or capitals at a minimum price and offshore company will "resell" the goods or the mentioned money at a higher price. "Mother company" because minimum price charged will have a very small profit and therefore taxes will decrease considerably. On the other hand, offshore company will sell its products at a substantially higher price and will have a serious profit but not subject to high taxation, because the tax haven has a really low taxes system or even none. The creation of offshore investment companies is dedicated to provide more options in choosing investment objectives, allowing investors to focus on the best projects and to select areas that offer high potential income. Also, it guarantees the confidentiality of transactions concluded between the company and its clients. The offshore companies make favorable conditions for investment in offshore company and ensure the possibility of transferring resources available without violating currency laws and fiscal monetary circulation. Ownership of offshore company's credit allows you to lead a profitable credit policy, minimizing taxes and loans and improving credit and financial services for different customers. In addition, using an offshore company might be provided loans to businesses located in an area with higher taxes. In this way it is carrying out the transfer of foreign currency resources in a third country, without violating tax laws and monetary circulation and reduction or exemption from tax on profits earned in a country with high taxation. The offshore companies can be used, also, to minimize the different taxes without violating the law. Very often, in these cases, the same citizen is the owner and manager of companies, one local and one in another country. This creates the opportunity to transfer to a third country profits in the form of taxable dividends. Later, the money may be returned to the country in which the joint venture is registered as investment or as preferential loans.

An offshore holding company can be used to finance its subsidiaries under different jurisdictions in order to obtain tax reductions for interest on loans granted by the "mother company". In this case, it is holding off shore companies in an area where it will not pay any taxes. The profit obtained using this method can be used to finance other activities performed by holding or be reinvested for other purposes. Insurance companies working using an offshore company registered in a country with high taxation can be used to ensure risks of "mother company" in conditions more favorable than those offered by regular insurance companies. This method, using offshore insurance company may be used by insurance companies to ensure their risks and thus to achieve efficient tax planning. Offshore banking companies can be created by banks in order to accumulate profits in low-tax countries, as well as by group companies in order to unify financial resources and facilitate the movement of money within the group. An offshore bank can be used to finance international operations conducted by the founders of the bank, in order to avoid problems related to currency law. In the

area of tax havens could be created companies designed to be owner of different inherited properties. These companies offer the possibility of reducing or even eliminating inheritance taxes and fees and to increase the value of "profit". In this way it is simplifies the sales process of a property if the owner is a company. In this case, only the company's shares are sold and transferred to the new owner but the company remains the owner of that property. If the property is to be sold or donated will not be imposed by taxes for this process.

Offshore private funds provide partial or total reduction of income tax, capital or inheritance. Moreover, it is guaranteed distribution of income in strict accordance with the desire of the owner. Offshore investment funds pay no tax and no higher legal fees. In addition, dividends and interest are taxed at a very low level or are exempt from taxes. Bringing retail investors offer the opportunity to participate in different projects and save many costs related to study of the market.

In this context, founder enjoys the greatest benefits having the flexibility to conduct abroad sealing proceedings. Manager could invest in many countries without paying taxes and can perform multiple commercial activities. Offshore company registered in a tax haven is the company or the company having a wide range of uses that are specifically established by the owners and much less outside existing regulations. Of IMF data, today, about 7,000 billion dollars in financial assets are owned by different categories of offshore companies. It is estimated that the United States of America loses each year between 54 and 70 billion dollars from the budget because of tax exemptions [3] and therefore the U.S. government pays special attention to these issues. The international community is pushing for several years as offshore areas to become more transparent. Only five of 30 areas become more transparent because of these pressures. The invoked reason by those who refused "the pressure" is the transparent regions are considered discriminated among all these nations. Among those who made concessions in this domain are included Switzerland and Cyprus.

#### **4. CONTEMPORARY GLOBAL ECONOMY AND OFFSHORE COMPANIES**

At the first sight, setting up an offshore company is hard enough, but in reality the establishment and management of offshore companies is no more difficult than that of ordinary companies. After the moment of the establishment of the company is possible to increase or decrease the company's registered capital, transfer of shares and change managers more easily. These operations will take place under the umbrella of the local law. Can be relatively simple, both fusion and division of the offshore companies. Official cancellation is possible for the offshore companies without the need for submission of final accounting records in the jurisdiction in which it was initially registered. Currently in the world there are more than 40 "offshore regions" offering considerable tax and financial advantages. These traditional tax havens are located mainly in archipelagos (eg British Virgin Islands), the island republic (eg the Republic of Naur) or small countries (eg Panama).

Permissive legislation and the independence of these countries, encourage foreign investors to set up various companies on that territory. In most "offshore areas" serious business operation, security and protection of the secret foreign investments are guaranteed by law. What provide favorable tax status for a company? In all tax havens, tax benefits have a legal basis. For example, for companies registered in the British Virgin Islands, the tax benefits are provided by a law passed in 1984. Thus, offshore companies do not pay other types of taxes except 300 U.S. dollars, regardless of turnover. Islands as Bahamas and Belize established an annual tax amounted to 100 U.S. dollars and 150 U.S. dollars in Panama. It is clear that these tax benefits are substantial compared to what is required tax in European countries. Granting tax benefits to offshore companies is considered an advantage for a tax haven area? Tax havens are usually small countries with small population and the tourism and various services play the most important role [4]. Offshore companies in these countries provide substantial income. On one hand, it creates jobs because it requires the existence of firms, institutions registration, registered agents and banks recorded on this territory. On the other hand, due to payment and other financial obligations to the state (tax registration and re-registration) and other charges, the population gets a considerable income. Let's see some statistics. British Virgin Islands has 17,000 inhabitants and presently 300,000 offshore companies are registered in this country. If every company registered on the territory pays an annual tax of 300 U.S. dollars, the fees paid by offshore companies is 5,200 U.S. dollars per capita. The main purpose of setting up offshore companies in tax havens is to reduce taxes and take advantage of direct or indirect taxation. It should be emphasized that despite the fact that offshore companies are often considered tax-exempt companies in any part of the world there are companies fully and legally exempted from any tax and financial tasks. In general, the following principles apply in areas of the offshore companies: the company is obliged to pay a fixed annual fee, independent of turnover and profit society. These areas are: Virgin Islands, Bahamas, Belize, etc. The tax does not depend on turnover, but the registered capital of the company. The Liechtenstein Foundation annually pays 0.1% of the share capital. They are exempted from tax only incomes derived from activities performed abroad. In countries like Panama and Hong Kong companies can carry on domestic business activities and incomes are taxed based on a linear rate, while income from abroad are exempt from tax. In Hong Kong companies must declare separate internal revenue in its annual report, without other financial obligation. Taxation is all the time based on a linear rate. One of the most popular areas is Cyprus, where offshore companies pay 4.25% of the total net profit. In these areas, accounting and delivery of annual reports is mandatory. These facts and more other make the offshore companies very attractive for the operators involved in money laundering. Directly related to money laundering, the terrorism found out a very attractive financing source in this complex phenomena [5].

## 5. CONCLUSIONS

The complex issue of terrorism and the ways of funding has been and will remain in the attention of specialists. Even if the blocking of the terrorist financing remains in each state of the world's attention, only the international cooperation is able to solve the problem. Cooperation between law enforcement agencies, the establishment of common rules regarding tax havens and not least criminalizing of any actions related to recycling of funds is the only way to stop terrorist groups. All future actions to prevent and combat terrorism directly bind international legal, administrative and operative cooperation.

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