# Development assistance and banking policies undermine MDGs

Switzerland is not fully complying with its obligations under the Monterrey Consensus. Its level of ODA is too low, and it does its utmost to shy away from innovative mechanisms to finance development. Meanwhile, it remains a safe haven for tax evaders and those seeking refuge for capital. In so doing, Switzerland undermines the efforts of numerous developing countries to fight poverty and to achieve the MDGs on their own merits.

**Alliance Sud** [1]
Bruno Gurtner / Pepo Hofstetter

Switzerland adopted a very defensive stance during the discussions on financing the Millennium Development Goals (MDGs) at the United Nations Millennium+5 Summit held in September 2005 in New York. The Swiss Government is a coalition of three conservative parties and the Social Democratic Party. The right wing forms the majority, as it does in Parliament, and has championed a rigid austerity policy that provides tax relief for enterprises and the wealthy.

## ODA target not met

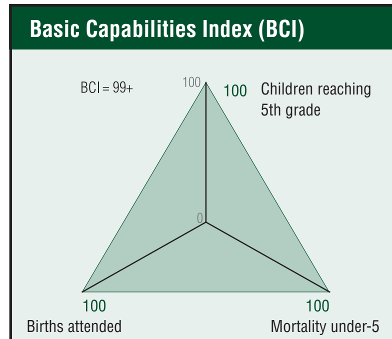
This austerity policy has a negative impact on the official development assistance (ODA) budget. Politicians have so far not succeeded in cutting ODA, a move that would not be well received by the public and Parliament. On the other hand, the NGOs have not managed to achieve an increase in ODA. In contrast to the "old" European Union member states, Switzerland, as a non-EU member, has refused to commit itself to an increase to 0.7% of gross national income (GNI) by 2015.

Switzerland has never recognized the target set by the United Nations and Organization for Economic Cooperation and Development (OECD) for the industrialized countries to spend at least 0.7% of their GNI on development cooperation. It has set itself a target of 0.4% by 2010 and is now boasting that it already reached that objective in 2004 (0.41%). This was achieved, however, through an accounting manoeuvre; aid expenditures have not risen, and no additional resources have been channelled to the South. Switzerland previously applied quite restrictive criteria to its definition of development assistance, but since 2004, it has also included spending on asylum seekers from developing countries during their first year of stay. In 2004 this accounted for about 10% of Swiss ODA, roughly CHF 200 million (USD 160 million).

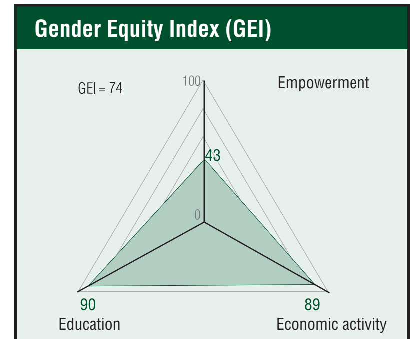
In 2005, as was the case for practically all industrialized countries, debt relief for Iraq and Nigeria was also included. However, this debt relief, consisting of export risk insurance payments totalling CHF 279 million (USD 219.4 million), had already been written off; nevertheless, it served to inflate Swiss ODA levels artificially to 0.44% of GNI. Along with the expenditures on asylum seekers and scholarships, the "virtual" aid granted by Switzerland last year accounted for 21% of its development assistance.

Swiss NGOs have criticized this contrived inflation of development assistance, and have demanded a deepened commitment from Switzerland with respect to the MDGs, including a coherent trade, economic and financial policy, as well as an increase in development assistance. In the coming year they will launch a major campaign urging the government to raise ODA to 0.7% of GNI by 2015.

**Basic Capabilities Index (BCI)**




**Gender Equity Index (GEI)**




## Innovative mechanisms: wait and see

The Swiss Government has also adopted a very defensive position in the discussion on innovative instruments for financing development assistance. In its MDG status report the government categorically stated that Switzerland in principle rejected global taxes – referring in particular to the so-called Tobin tax on foreign exchange transactions – as well as proposals on a global International Finance Facility (IFF) to support the MDGs. If proposals on a levy on airline tickets or an International Finance Facility for Immunization (IFFIm) obtain broad support, the government would be prepared to consider participation.

## Assistance to international tax evasion

Switzerland has not changed anything in the configuration of the Swiss financial centre. In its 2005 Peer Review of Swiss development policy[2] the OECD Development Assistance Committee (DAC) noted that the Swiss financial marketplace is highly attractive to flight capital from developing countries with weak financial systems and property rights, political instability, and poor monetary and fiscal policies. Switzerland therefore has a special responsibility: the Committee recommended that Switzerland should initiate an international debate on the problem of capital flight, its root causes and negative impact on developing countries.

Swiss banks manage one-third of all assets invested outside their country of origin. A large proportion of these funds are not properly taxed in those countries. As a result, developing countries are particularly plagued by major shortfalls in their tax revenue. This has a negative impact on poverty reduction and the achievement of the MDGs.[3]

Swiss banking secrecy is not the main instrument that facilitates tax evasion by rich foreign nationals. It can be lifted in the event of criminal activity. Rather, the decisive factor is a unique construct in tax law, namely the legal distinction between tax fraud and tax evasion. Forgery of documents (accounting balance sheets, profit and loss and income statements, etc.) is regarded as fraud. Such activity constitutes a criminal offence and may be punishable by imprisonment, or the perpetrator may be

1 Swiss Alliance of Development Organizations: Swissaid, Catholic Lenten Fund, Bread for All, Helvetas, Caritas, Interchurch Aid.

2 OECD (2005). "Switzerland (2005), DAC Peer Review. Main Findings and Recommendations". Available from: <www.oecd.org/document/43/0,2340,en_2649_34603_35105259_1_1_1_1,00.html>.

3 Cf. the article by Mike Lewis "Global Tax Evasion" in the thematic section of this Report.

fined up to CHF 30,000 (USD 24,250). The submission of insufficient data on income and assets, by intent or negligence, is considered tax evasion. In Switzerland this is subject only to administrative proceedings, such as the imposition of fines.

This discrepancy has serious implications on cross-border information exchange: in Switzerland the principle of dual criminality applies to any international judicial assistance and cooperation among competent authorities. In other words, Switzerland provides legal cooperation in cases where an offence is also punishable under Swiss law. Since tax evasion does not constitute a criminal offence, no such cooperation is granted. This provides an effective shield that protects foreign tax evaders seeking refuge from the fiscal authorities under whose jurisdiction they operate.

The elite from developing countries benefit considerably from these tax loopholes, for example, through funds placed in fiduciary arrangements. The banks invest these funds in their own name, but at the risk of the client. The *Financial Times* of London described this type of financial transaction as a perfect way to evade taxes. At the end of 2004, fiduciary assets entrusted to Swiss banks by wealthy customers from developing countries amounted to some USD 62.5 billion.[4] An additional USD 83 billion originated from Caribbean and European offshore financial centres. It is likely that as much as half of these funds come from developing countries, the major share of which is not appropriately taxed in the countries of origin and therefore represents missing tax revenue.

It is not possible to determine just how large the sums of flight capital and missing tax revenue are, since Switzerland's financial statistics are inadequate in this regard. Alliance Sud estimates that developing countries are losing out on USD 5 billion in tax revenue through monies managed by Swiss banks. This figure corresponds to five times the total sum Switzerland spends on development cooperation.

Knowing that the adoption of unilateral measures by Switzerland was unlikely to be accepted, due to the strong competition between financial centres, the OECD recommended that Switzerland should become a strong proponent of international reform. At the bilateral level, Switzerland should extend its agreement with the EU on the taxation of interest payments to include developing countries. Through such an agreement, along the lines of the agreement negotiated with the EU, interest earned on managed capital from developing countries would be returned to the countries of origin, to be used to combat poverty in those countries. The OECD has encouraged Switzerland to strengthen international exchange of information on taxation matters and to rectify the current situation of impunity with regard to tax evasion.

Almost a year has passed since those recommendations were made, but there are no signs that they will be implemented under official Swiss policy. Switzerland likes to draw the attention of the OECD to the mechanisms it has implemented that sustainably strengthen the financial systems of developing countries and all the steps it has taken to counter money laundering, yet it categorically refuses to extend the EU agreement to all developing countries. In response to questions raised in this regard before the Swiss parliament, the Government has stated that a successful strategy to combat capital flight needs to start in the countries of origin themselves.

Further announcements have made it clear that Switzerland does not intend to deviate one iota from its current policy. In November 2005, however, Switzerland participated for the first time (albeit as an observer) in a meeting of the OECD Global Forum on Taxation. At the Global Forum, OECD member countries and offshore financial centres meet and try to establish a common framework to improve transparency and strengthen information exchange on international taxation issues. As in the case of Belgium, Luxemburg and Austria, Switzerland had previously refused to participate because it was opposed to extensive information exchange. As a result of pressure from the OECD, many offshore financial centres in the meantime have somewhat improved their legislation and banking supervision, and are negotiating bilateral agreements on the exchange of information. Not without reason, they accuse the OECD of applying a lower standard to its own member countries than is required of other offshore centres.

When it made its first appearance at the meeting, Switzerland made it clear from the outset that it did not wish to commit itself: it does not at all feel bound by the conclusions of the Forum, and maintains its position, particularly with respect to banking secrecy. For years the government ignored the work of the United Nations Ad Hoc Group of Experts on International Cooperation in Tax Matters. Switzerland was represented at best by banking and industry executives. The group of experts was later upgraded to the status of a Committee following the 2002 International Conference on Financing for Development held in Monterrey. The Committee seeks to strengthen efforts to curb tax evasion and enhance processes of information exchange, for example, by aligning the provisions on exchange of information in its Model Double Taxation Convention between Developed and Developing Countries with those of a similar, but more comprehensive, OECD model law agreement. This has given Switzerland grounds enough to seek one of the 24 seats on the Committee, even though it had worked against the upgrading of the expert group behind the scenes. The representative of Switzerland, along with representatives of other interest groups, now works towards a "moderate" policy: exchange of information in taxation matters should not infringe on banking secrecy.

Alliance Sud believes that it is unacceptable for Switzerland to boast when it finally returns the millions stolen by former dictators like Sani Abacha of Nigeria and Ferdinand Marcos of the Philippines to their countries of origin. Alliance Sud calls on Switzerland to carry out much deeper structural changes within its financial centres. The current distinction between tax evasion and tax fraud must be abandoned. Switzerland must implement policies that lead to an effective international exchange of information on tax matters and apply customary international standards. This is why Alliance Sud is actively involved in the global Tax Justice Network.[5] ■

4 Swiss National Bank (SNB) (2005). *Banks in Switzerland*. Zurich, 2004 edition. Available from: <www.snb.ch>.

5 Additional information available from: <www.taxjustice.net>. Cf. also the article by Mike Lewis, *op cit*.