# PROFIT MANIPULATION WITH TAX HAVEN NETWORK AND THE ROLE OF AUDITING FIRMS

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# Chapter 1: Introduction to the Study

The tax haven situation refers to the combination of supportive and beneficial circumstances aiming to the evolution and expansion of tax avoidance functions. It is necessary to establish this exceptional environment of economic and political framework by adopting miscellaneous mechanisms and procedures such as offshore companies.

One of the primary characteristics of a tax haven country is, of course, the very low taxation or even the absence of it. What is more, the strictest confidence and the absolute discretion are considered to be of pivotal significance. Additionally, the existence of asubstantial, distinct and effective organization of financial services assists every customer's strategy for accomplishing a successful outcome. As a result, more and more protracted overseas financial contribution is observed. This specific factdepictsa welcome tremendous and rapid economic development. At this point someone could wonder why all the countries do not adjust their taxation infrastructure to appeal investments. The description of a tax haven country is encapsulated in proper management, limited nation and population and high GDP per capital, especially in the field of services. Consequently, those requirements could not be assimilated by all the countries worldwide.

There is not an actual and reliable interpretation of the notion of the Offshore Financial Center. Several lists are either established on determined carelessness or on objectivity that hardly analyze places that provide economic services to non-residents. The International Monetary Fund (IMF) notices that a more extensive explanation of OFC would be consisted of all the globally large-scale financial centers. Specifically, the IMF has reported the following: "a more practical definition is jurisdictions where the bulk of financial sector activity is offshore on both sides of the balance sheet".

In 2008, a survey was conducted by the International Monetary Fund and resulted in the existence of 46 confirmed tax heaven globally. As the world average GDP per capital is 54,42%, tax haven countries hold the significant percentage of 75. A supplemental characteristic to the aforementioned is that they abstain from any kind of multinational corporations and the sum of their citizens is below 1 million. So, we notice here that not all the countries could manage to combine these specific components of being a tax haven.

By historical standards, the advancement of tax havens is constant and complicated. One of the initials founders is ancient Greece. Greek merchants used to collect their commodities in the nearby islands with the objective to evade a custom duty on imports and exports, which were next conveyed in the city unlawfully. A crucial turning point of the tax havens accelerated progressionis considered to be when the legislation of limited liability companies was assimilated in England in the nineteenth century. Profit and income tax were then created. After the completion of First World War, the European economy inflated exceptionally the range of taxes. Subsequently, investors were nothing but gratified. Thus, they transferred their money in financially impartial countries, such as Switzerland, which lowered even more the diversity of its taxation.

Regarding the concept of “virtual” residence, it was first introduced by the British court. It represented enterprises recorded in Britain with no statement on being active. Therefore, they were not liable to the vatable levies. This strategy was imitated by Bermuda, Bahamas and ameliorated by Cayman Islands. A distinct point was noticed in 1934 that Switzerland enormously escalated the confidentiality status by incorporating it in the criminal law. Anyone opposed to that secrecy was simply imprisoned.

A remarkably propitious category derived from the tax haven notion is the multinational companies. A variety of favorable opportunities is granted to them by tax haven counties in order to assist them in better achieving tax avoidance and evasion. The approach they pursue is the establishment of subsidiaries in tax haven countries. Thus, the profit manipulation to those subs becomes effortless and dynamic. A supporting factor is the application of transfer pricing through tax havens by allowing the MNCs to shift the profits into reduced tax regime areas. The tax on the corporate profits at those places for non-resident businesses is remarkably diminished along with absolute information concealment even to the revenue authorities. This fact is generally analyzed and confirmed, since the specific MNCs disclosed lesser profits and paid insignificant amount of taxes.

The accountancy firms that have a prominent role to conduct against the tax evasion are the “Big4”. Their contribution is mainly based ona variety of advises and formation strategies to new companies. But it is not just that. They do deal with the government, too. They regularly present several proposals in relation to the prevailing tax structure or promotecoherent policy alterations. Along with the complete access to the customer’ssensitive financial information, Big 4demonstrate their power and competence to scale down the tax rates in favor of their clients. They have the responsibility not only of technical approval, affirmation of tax project and smooth exploration of administrative conditions but also, they appear to be the founders of specific business activity. Abundantly clear, they do havea substantial and well-established presence in tax consultancy. So, it is obvious that the interaction between the auditing procedures of Big 4 and the sustainability of MNC's tax haven subsidiaries is extensive.

## 1.1 Importance of the Study

The adverse implications on the economy and monetary marketplaces are quite discernible and understandable. OECD has, also, expressed profound considerations on the issue of tax evasion and profit manipulation by MNCs, due to the enormous value of illegitimate financial leakage. Furthermore, the Financial Action Task Force (FATF) has acknowledged a more and more developing corruption of the trade structure as one of the predominant methods to assimilate money laundering in lawful economy.Besides, the UK parliaments on their report in 2015 regarding the tax avoidance in accordance with the function of the accountancy firmsstate a deep interest and apprehension about MNCs tax avoidance and taxadvisor'sduty. Since all the Big 4try to discover every single loophole on the international tax law, it actually makes sense that they could provide their clients with dynamic and efficienttax avoidance arrangements.These issues are unambiguously of paramount importance and the development of productive and valuable administration over non-audit services by auditors is crucial and urgent.

## 1.2 Interested readers of the Study

As the world economy is continually evolving, a variety of strategies and methods in every singlesector are substituted by current, dynamic and productive ones. People whose main occupation is based on accounting and financial issuesneed to always remain enlightened and conversant with the ongoing facts.First of all, students that wish to maintain financial records or even a business in the near future need unequivocally to remain familiar with all the monetarychanges. Secondly, certified tax advisors and auditorsare imperative to apprehend and discernthe recentapproaches and techniques for their clients.What is more, ambitious investorsare desired by every nation, but they will finally choose the most appropriate one. To accomplice that they arenecessitated to be aware of the healthy MNCs and prevailing mechanisms, which both will contribute to profitable moves. Studying past events, successful or not, including the connection of Big 4 withentities owningtax haven subsidiaries and how the profit manipulation is step-by-step achieved,will definitely help them be more conscious regarding the threats of the most possible secure project.Besides, present or forthcoming businessmenand founders ofmajor corporations have to stay cognizant regarding the all the beneficial economic modifications.Since the topic of my study is a very common and repeated situation even no accountant people could enjoy in reading such studies. They will, then, have a brighter and more clarified point of view of the worldwide economy that affects,in an indirect though way, all of us.

## 1.3 Research Hypotheses and Problem

Tax haven countries are used to be called offshore financial centers, as well. With their financial field to approach higher standards than the domestic economy, it is easier to provide considerable tax and governing benefits along with globally banking facilities. The predominant origin of clients, who prefers the OFCs, is observed to derive from insecure and precarious states. Such states suffer from inadequate and impoverished tax accumulation, whereas the evaluation of the imminent risk is really challenging and complicated. The main question that occurs is to examine thoroughly, as long as possible, the basic determinants of the countries with the most investors that resort in OFCs. It is absolutely crucial to entirely comprehend the problem thatis generatingin worldwide capital flows by the tax havens. Specifically, in 2008, investments across 49 OFCs were estimated $6,1trillion dollars. This amount was almost commensuratewiththe aggregate investment fundsin UK, Germany and France. It is more than obvious to fully understand our hypothesis in order to provide the relevant answers concerning the insufficient tax payables.

What is more, the reason why several countries maintain connection with OFCsmay lead us to figure out the most pertinent strategy in order the problematiccondition to be better confined.At this particular moment, it would be of vast importance to enunciate that in 2007 and 2008, Cayman Islands were the prevailing proprietors of UK mortgage backed securities. Of course, the owners of those securities were not inhabitants of the Cayman Islands. So, what exactly has been disclosed and made vulnerable to the OFCs is simplyin conceivable.

The economy damage that needs to be confronted by the UK is even more documented by the statistical analysis of "Hines", the Intelligent Real Estate Investments office, in 2010. Explicitly, only the 6% of the recruitment contractsand tangible financial assets waspositioned in offshore areas of authority. Simultaneously, the astonishing and alarming 42% of the declared revenue was acquired in the same areas. It is absurd and unbelievable to accept that the second percentage is earned by the first one.

Clearly, the profit is manipulated through the OFCs to be reduced.According to Evans economists, examples of businesses to be surveyed could be Coca-Cola, Del Monte, Intel and Seagate Technologies.It is remarkable to note that the last company declared income with respective tax payable 5%. Its delegate person supported this fact by stating that the competition is veryharshand the financial advantages deriving from OFCsperform a very lucrative role that preservesthemon solidstandards.

On the other hand, there is a valuable element to consider.Countries that are locatednearby the tax havenscan better support their commercial banks to provide the most reduced interest rate dimensions. It is clearly anticipated that this situation has already inflated thecontroversy and competition between an onshore and offshore bank. Due to the fact of distance, the interest range could be approximately over 1,5%greater in case theremaining miles were doubled. Particularly, the currently improving nations are consisted of economic markets that are dictated by only a few enormous banks. As a result of this competition, the capital markets gain the essential features to enhance their presenceand develop. According to Rose and Spiegel, countries with an OFC neighbor contribute more on private sector by prolonging the credit and in return have a considerable sum of market borrowing. So, it makes total sense that banks do gain and report more money.

## 1.4 Purpose of the Study

The core intention of this study is to investigate not only the connection between the foreign investments and the OFCs but also the negative impact in present international finance.The prevailing economic conditionis considered to be on crisis. Unfortunately, due to the overwhelminglyheightened tax range,a variety of companiesconfrontan even more complicated and crucial sustainability issue, which of courseconstitutes anurgent settlement. They, eventually, are left with no other choice but to conclude to receive the most benefit of the opportunities offered in tax havens in order to survive and grow.Besides, the function of the accounting Big 4 companies will be described meticulously, since the MNCsthat prefer to be audited by them are likely to create and maintaina very profitable OFC subsidiary compared to the ones that did not selected them. The relation of all these facts intends to exhibit several quantitative evidences, composea replete study ofqualitative knowledgeand stimulate the readers to search more andattain a holisticview regarding the global economic market.

## 1.5 Preview of the next chapters

The study intends to scrutinize the impact of the Big 4 accountancy firms to the offshore centers created by Multinationals companies.Several papers that will support my researchemanate from honorary and distinguished personalities. They are either academic staff or employedin the field of corporate taxation system and justice. It really worths considering and analyzing their point of view. Afterwards, my main subject will be connected to their surveys by identifyingand making reference to common elements.

The investigation will keep developing by concentrating to the bottom lineof so many problems that tax havenscould provoke to the associate states.So, iwish to examine and evaluate theleading characteristics of a country,as a nation, to operate more on the OFCs and whether that action attracts or not more investors to them.These factors will explain why tax havens are notselected by every country. With the assistance of the Organization for Economic Co-operation and Development (OECD) and the International Monetary Fund (IMF), I will gather and categorize the countries with financial activity in OFCs and the countries considered as tax havens. Furthermore, the influence of OFCs in global movement of capital is very significant. OFCs with tremendous inward portfolio investment will be presented and compared to the non-OFCsrespective performance. As a result, readers will be able to fully comprehend the extend of the repercussion in international economic affairs and commerce.Next in order will be the reason why investorschoose the OFCs and to which gradenational characteristics determine the extent of the tax havens’ utility.Last but not least, investment arrangements of the countries included in the general sample, that range from low to high OFC involvement, will be presented. All the aforementioned components will behave as variablesfor my econometric model.In conclusion, the outcome of my estimations will be detailed discussedin order my investigationtopresent a much better perceptionand knowledgeof global finance.

# Chapter 2: Literature Review

Each and every physical person is obliged to pay taxes according to the submitted income. The same fact occurs to corporations, too. However, lots of them avoid that liability through various illegitimate ways and manage to reduce satisfactory the amount to be paid.The length of the lost taxes is ranging from 50€ to 70€ billion per year, to name but a few.This technique has been developed into an industry, which is called “the tax avoidance industry”.

Of course, the most significant components of this field could not have been anyone else but financial organizations combiningadvisorsandlawyers with expertise in taxation.The colossussegment of business tax management and effective configuration is the Big Four accountancy firms. They are considered to act in a valid and lawful way by many legislative officials.Although the existence of ardent advocates, there are some personalities that support a conflicting aspect. A more extensive reference will be conducted and discussed on the next chapter of my study.

The professor of Economics and Law in Michigan University has stated the following: “The definition of exactly what makes a tax haven may depend on the type of investment and requires a degree of judgment, but fortunately, those who have considered the issue keep compiling very similar lists. For example, in Hines and Rice (1994), my coauthor and I identified tax havens based on their low business ed tax havens based on their low business tax rates, self-promotion as financial centers, and whether they were identified as tax havens by other authoritative sources.” It is necessary to add that the OECD has prepared a related list of OFC’s, as “Diamond and Diamond”and “US Government Accountability Office (2008)” have completed.

The United States and many other nations with greater tax ranges have intermittently declared their intense consideration with regards to the way that tax havens disturb their general economy. For instance, they may corrode their internal levying of taxes. This could occur by allowing individuals to raise revenue via their bank accounts inseveral tax havens. With high confidentiality of the private information, the home governments could not have access to those files. Also, OFC assist the process of business income, which although it is earned in very high-tax jurisdictions, it is stated as acquired somewhere else.

The Corporate Europe Observatory administered the completion ofa researchespecially based on the character of the Big 4 companies. The crux was that their presence in European

Union’s political decisions, specifically in business tax avoidance, is ubiquitous and infinite.Their competence is enhanced and broadened by a diversity of instruments. First of all, community procurement agreements are awardedeach year to Big 4 that cost millions of euros aiming ateducation and investigation.

Thus, their impact could beeasily applied togovernmental endorsement and promotion regarding the tax arrangements. Secondly, the called “lobby groups” are very famous, since they are consisted of the “European Business Initiative on Taxation” group and the “European Contact” group. Their principal duty is to intervene in EU policy measuresfor the restraint of tax evasion. Associates of the Big 4 participate in those groups and their influence is very solid. Furthermore,consultative committee, such as the “Joint Transfer Pricing Forum” and the “Platform for Tax Good Governance”preserve a dominant characterconcerning the termination of tax avoidance.

A very felicitous and crucial example that depicts the enormous influence of the Big 4 is the prevention of the public country-by-country reporting. The European Union proposed and required businesses to be accountable regarding their profits to every country they could possibly operate. The point was to diminish income secrecy, which could not allowor approve profit shifting to tax havens.Finally, with the intervention of the Big 4, the obligatory disclosure of theabove sensitivematerial was prevented.

Nevertheless, in April 2016the fact of Panama Papers provoked intense feelings of indignation and resentment in society. This was considered as an outcome of the country-by-country reporting, which was more aggressiveand potent than ever predicted.After bounteous direct and solid endeavorsby the businessorganization to the European Parliament, a derogating measure was incorporated that permits the public confidentiality of the delicate information.

The Commission’s counseling group and the Platform for the Tax Good Governance created ferventand exquisite efforts to erode or even subvert the public reporting. Specifically, “the American Chamber of Commerce to the EU”, “The Business Europe”, “The German business lobby BDI” and its French correspondent participated in this surge of pressure. The first one contended that the general disclosure could disrupt thecompetition of the companies and contaminate the enticement for financial contribution in Europe. So, PWC and “Accountancy Europe”remain in the favor of the American Chamber and manipulate its tax politicalstance. Regarding the “BDI”, which was an advocate of the public reporting, clearly stated that only if the disclosure offiscalmaterial was belittled,it could may continueto support that strategy. As a result, the unification of the exceptional article was inevitable. So far, Luxembourg, Austria and Cyprus are in dispute over the public reportingand on the other hand Netherlands, France and Belgium are assented toit.

Having seriously considered the above research of the “Corporate Europe Observatory”, the managing director of the Tax Justice Network, “Alex Cobham”,expresses profound doubts over the function of the Big 4 firms.Heparticularly characterizes them as an auditmonopoly,whichisunambiguously supported by the government.Besides, he points out that theimpartial impression they strive to depict is thoroughly deceitful and dishonest, since it is part of their intention to exert influence over the stateregarding theglobal tax avoidance.Just as significant is his statement that the Big 4are authorized topromote the campaign against the business taxclarity, which perfidiously and unfairlyinsinuates the evenhandedperception and scrutiny of them.

According to him, as a result ofthe multinational profit shifting,the annual decrease in revenue approaches the $500 billion. The Big 4 accounting firms appear to facilitate that finding by assisting the MNCs to explore alternativeprocedures in restraints and controls by the tax authorities. He definitely suggests that the respective bodies of policy formulation to seriously contemplate aworldwide cooperation in order to confine the economy corruption and disturbance.

The research of the “Corporate Europe Observatory” was, also, authorized by Dr Yama Temouri. He is a senior professor in the Economics, Finance and Entrepreneurship department of the Aston Business University. As reported by him, there is an electronic collection of information, which is the dominant point of companies’ balance sheets supply. It is called “The Orbis” and is primarily related to the investigation of multinationals’ tax management and performance. He is acutely concerned about the organized deficiency of the collection of evidences regarding the tax havens. This fact could possibly lead the way to the significance understatement of the profit shifting. Thus, the outcome by the respective analysis would not be neutral but well-structured and controlled. On the other hand, if the county-by-country public disclosure system was mandatory by the government, MNCs would be forced to pursue it. As a result, a wider range of clues would be available to identify and clarify the extent of the use of tax havens by MNCs cooperating with the Big 4 accounting firms. We could then undoubtedly expound and present the literal correlation between them.

The Financial Stability Board (FSB) has reported a list with 37 places that appear a major offshore movement, in 2000. Even if that list is almost two decades old, it is fairly precise, systematic and authoritative.

The European Union (EU) has published a list of 30 territories that are characterized as no less than the 10-member state blacklist, in 2015. This fact wassubstantiated to be very contradictory and it is now exercisingthe EU blacklists determinants.

Taking into consideration that nations are more or less well-proportioned, the decision between the source and the residence taxation system is almost revenue impartial. It would make great sense to concentrate on apportioned performance and effectiveness by evading the respective taxes that pervert the investment arrangements.

The IMF Fiscal Affairs Department has declared in 2014: "The allocation of rights is especially important for low-income countries, however, as flows are for them commonly very asymmetric – they are essentially 'source' countries, the recipients of capital inflows and the site of production, not investors in business activities outside their borders … the network of bilateral double taxation treaties based on the OECD model significantly constrain the source country's rights."

It is very significant to separate the perception of how the OFCs assist enterprises to refrain from their profit taxes and how they could assist investors to refrain from their income taxes. The MNCs take advantage of the low taxation range in order to manipulate their profit into their subsidiaries or associated branches established in tax havens with a tremendouslow taxation level. The multinational investors handle the profit-shifting characteristics, such as the belittlement of the prices in intra-group sales and the price impose on their subsidiaries for intellectual property or administration services. As a result, they manage to annihilate the profit on high-tax nations.

A professor of Economics, mrs Alison Booth, of the Australian National University upon her survey in 2012 has reported the following: "Decades ago, economists could justly have been criticized for assuming that markets exist in a vacuum, and of ignoring the social and institutional foundations needed to support functioning markets. This is no longer the case. If anything, economists may now err on the side of placing too much emphasis on the role of institutions in development"

What is more, there are very famous accountants that have disclosed their position. Those could be the Acemoglu and Robinson, who in 2012 have expressed that "'good institutions' as the root cause of development. From the perspective of investors, the two most important aspects of economic institutions are property rights and contract enforcement". Besides, the Ogilvie and Carus in 2013 reported that "Property rights consist of rights of ownership, rights of use and rights of transfer. More important than the de jure nature of laws and regulations are their de facto application. Economists describe firms in developing countries as operating in an environment of 'deal making', where political connections matter and the rules are applied erratically".

Especially disadvantageous and adverse factors to global investments are considered to be the risk and the uncertainty. Pervasive and protracted empirical literatures record a diversity of ways that risk could have a negative impact on funding. For example, as Dixit has statedin 2010 "insecurity is greater, and has new dimensions, when the activity and transactions cross national borders … governments may violate the rights of foreigners with less fear of political consequences … courts may have open or hidden biases favoring their own nationals"

Dharmapala in his survey in 2008 has described that "It is 'folk economics' that capital should not be taxed to maximize productivity over the long run. This is a misconception. That said, conventional wisdom among economists has been that taxes on capital income come at a high price in terms of economic efficiency, especially when capital is mobile and can easily be relocated to lower-tax territories.43 In theory it would be desirable to tax immobile capital more heavily than mobile" He definitely demonstrates the association of OFCs and tax treaties efficiently permit nations to complete that fact.

Furthermore, Straub and Werningin 2014 have stated that "Some of the highly simplified theoretical models which suggested that a zero rate of capital taxation is optimal, turn out to have been misunderstood, and actually implied positive rates of capital taxation. Saez and Stantcheva in 2016 add to the above that "Other 'zero tax' results may rest on unrealistic assumptions, such as labor income being the only source of inequality. It does not take many theoretical steps towards greater realism, including the idea that capital ownership is highly concentrated, and society may have some interest in equity, to imply that capital income could optimally be taxed as highly as labor income"

The effect of bilateral treaties on investment is consisted ofambiguous and incomplete literature. Professor Busse in 2010 has concluded that “treaties do attract investment to developing countries, although whether tax rates or other attributes such as dispute resolution mechanisms are responsible, is not clear. The authors argue that other negative results reflect differences in sample or methodological problems”. The point of view from International Financial Institutions expressed in 2015 is based on the fact that tax motives are often very expensive and incompetent, while the documents derived from many surveys conclude that they are excessive.

Professor Dowd in his study in 2017 has clearly described that “When using OFCs, it is not always clear what the right ‘counterfactual’ for comparing tax payments against would be. In the context of profit-shifting by multinationals, researchers often compare reported taxes against a counterfactual based on profits being aligned with indicators of economic activity, such as assets or employees. The most natural counterfactual to set against investors’ use of an intermediary OFC is a direct investment.”

A great example of investment in OFC and the respective constraints is the Norfund case. After the publiccommission in 2009, more rigorous and severe controls were implemented on the Norfund’s use of the OFC’s. the Norwegian government enforced new protocols ” Norfund could only invest via countries in the OECD or countries with which Norway had a tax (or tax information exchange) agreement”. So, the Norfund was prevented from funding in Mauritius by those guidelines, since there was no exchange of general information. The outcome was a lot of difficulties to be faced, since Africa was not a participant anymore. During the years 2010 and 2011, there were not new investments contained in Mauritius. Less funding arrangements than scheduled were completed in Least Developed Countries and more loans were circulated than equity.As a result, a tax information exchange compliance was signed in 2012 with Mauritius and Norway was permitted again to invest with companies established there and the equity funds were easily and quickly escalated.

Campaigners try very hard to prove that issues are definitely created by tax havens influence more than the tax system. The “Tax Justice Network” has adopted the term “secrecy jurisdictions”. Important and appropriate elements to consider are whether the source countries tax authorities are aware of everything related with the tax collection and whether the identification of development financial institutions’ investors should be publicly disclosed. Professor Alstadsæterin 2017 stated that “Interviewees argued that DFIs’ fellow investors are typically institutions (such as pension funds, insurance companies and endowments) that would not risk illegally concealing capital income (tax evasion). The picture gets murkier in the case of private individuals (who may invest via intermediate entities), who occasionally participate in DFI investments, and some of who may attempt to evade taxes at residence. New evidence combining random audits with leaks from OFCs and population-wide wealth records in Scandinavia has revealed that individual tax evasion rises sharply with wealth"

Most Development Financial Institutions do not tend to cooperate with jurisdictions that are not obedient with the "OECD Global Forum on Transparency and Exchange of Information" process.Professor Oxfam in 2016 explained the aforementioned meticulously: "Most tax campaigners argue that the objective is to increase transparency across the system rather than push investors towards onshore OECD financial centers; although blacklisting particularly uncooperative jurisdictions may be part of the solution. In the long run, the solution is to automate the exchange of information between LDCs and all financial centers. Progress on this front is slow but would not be accelerated if DFIs stopped using OFCs. Some recommendations regarding how DFIs might play a more constructive role will be made in the concluding section of this paper".

It is undoubtful that a lot of damage has been provoked by the OFC's. Professor Zucman in 2015 estimated that "30% of Africans' and 22% of Latin Americans' financial wealth is held offshore (the figures are 10% and 8% for Europe and the USA). It is hard to know what evidence could be brought to bear on these arguments. The investments which DFIs participate in are a fraction of the wealth held in tax havens – estimates of which range from $4.5 trillion to $32 trillion (Tax Justice Network). Likewise, the professional service fees they generate are immaterial set against the overall market." But nobody knows who intends to act differently. DFI's support that it is not their responsibility to contravene the signals by their shareholders. The government of their shareholdersengage in global conferences, where they can settle such questions and designate suitable attitude and management. For instance, Non-governmental organizations are likely to consider the Global Forum as deficient and incompetentbut the DFI's believe that they should respect it, since it is settled by the country.

Development Financial Institutions regard their action as moving in existing limitations to boost capital into countries and fields so that they acquire positive effect on development. They do not endeavor to alter those constraints. Their duties are the enhancement of laws and the effective operation of judging system. They achieve those by establishing the competence and power of tax administrations and by implementing rules especially for confidentiality, such as jobs in the World Bank. Professor Vervynckt in 2014 advocates that “a key part of the role of DFIs is to promote private sector development at the local level. This implies helping create structures that allow for direct investments”. Consequently, DFIs should act more to confront the boundary of jurisdictions that are supposed to be appropriate for direct investment in correlation with other more advancement determinants.

## 2.1 Literature Theoretical Foundation

This paper scrutinizes the influence that the Big 4 achieve on the magnitude and the ramification of the MNCs with tax haven subsidiaries. The theoretical framework that encompasses the necessary material is based on the internalization theory of “Jones and Temouri in 2016” and “Rugman in 1981& 2010”. One of the most significant points of the Rugman’s research is the establishment of a dual matrix: the country-specific-advantage and the firm-specific-advantage.Pursuing this distinguishing perspective, he accomplished to improve theillustration ofthe method that firmsorganize to evade their tax liabilities creating after all an entire industry.The results are presented at a pyramid formulationin order to be entirely comprehended.

The internalization theory preserves its legitimacy and effectiveness over the past 30 years, whereas its dissemination into a diversity of global business activities is immense. It is fundamental to define the concept of the theory. Asauniversal principlethat delineates the horizon of corporations, there are a lot of divisions that is applied to. One of those is the MNCs field. The core objective is the exact description of the firm’s borderline and reaction to the dynamic developing conditions according to its culture. Concerning these variousfeasiblefeatures of the organizational performance, the better way to predict them is by associating the internalization theory with other principles.

Then, we could conceivean expandedaccumulation of possibilities. For example, the connection with the trade theory would explain the company’s transactions regarding its location, with the organization theory the worldwide joint ventures would be analyzed and with innovation theory the different categories of industry that a firm could engage in would be defined.

One of the most determining factors is the transaction expensein the general market. Managers are required to correlate it with the respective internal one and assess the harmony point that ascertains the firm's outlook.It is necessary the costs to be proportionate to each otherwith the objective to remain conducive to theeffectively productive managerial control.Due to the fact that there are several deficiencies in almost every field of the global industries, the above target cannot be always fulfilled.To adequately confront this situation, businesses are impelled to invent and coordinate their own internal market.MNCs pursue the fore mentioned rationale to surpass the restraints by their government and economically support their international activities.
Because of the confusion in the structure of the regulations, omissions and inconsistencies are easily to be detected. So, it is expected to take advantage of themregarding not only the taxation issues but the corporate arbitrage by trading their shares in multiple stock exchanges.Consequently,tax flexibility appears and inaugurates a new order of procedures,while firms are considered to elude the country's limitations.One of the best examples concerning the corporate arbitrage is the use of transfer pricing through the tax haven subsidiaries. The later allows the MNCs to manipulate their income by relocating it from high to low tax jurisdictions, where decimated rates apply, and remarkableconfidentiality is provided.

The research of "Jones and Temouri in 2016" examines the internalization theory by implementing the matrix of "Rugman (1981)" into the assumption of establishing a tax haven subsidiary or not by MNCs.Apart from this decision, they, also, endeavor to investigate the degree of the entire tax haven operation given the total size of that network.The assisting pyramid depicts that both FSAs and CSAs lie at the bottom, which implies that they are evenly as notable to one other. The range of the FSAs is consisted of not only financial details but also non-financial that could be geographically limitless. Thus, they could be much easierrelocatedto offshore areas. Afterwards, the incorporation of their structure to the new local FSAs is anticipated in an effort to be more competing.Tax havens are the appropriate place for the regenerated FSAs, as the MNCs manage to circumvent the market weaknesses and instability through them.In particular, MNCs introducean improved strategythat harmonizes the tax haven subsidiaries with the parent company. As a result, they achieve to bypass their corporate tax with the provided confidentiality to reach the summit grade, act as sources of funding for the MNCs group and as insurance companies toshelterpossible exposures not regularlyprotectedonshore.

Regarding the CSAs, it is truly important to be combined with the FSAs. CSAs are consisted of severalfactors by the offshore financial centers and the home country.This factgrants the opportunity to MNCs to establish, preserve and protect their perplexingsystem of organization. “Jones and Temouri” regard that countries with a more flexible market structure authorizemore smoothlythe MNCs to maintain tax haven actions in comparison with the strictly regulated ones.

Concerning the generalposition of the Big 4 accountancy firmsto the tax avoidance by the MNCs, the “Public Accounts Committee report (2015)” recognizes the vast significance of it. In the present case, PWC is distinguished due toa variety ofpromulgated evidencesby the “International Consortium of Investigative Journalists”, which revealed that exceptional tax regulations were arranged for different businesses with Luxemburg tax authorities.The Head of the taxation department in PWC profoundly insisted that they do refrain from tax evasion. However, he admitted the formulation of very specificstructures. Having considered his entire speech, the committee expounded concerns regarding the borderline between the approved tax avoidance and the assertive tax preparation. Apart from the technical assistance and the endorsement of the tax methodsoperated, Big 4 do reinforce the regulations’ exploration by being the founders or the vendors of unusual or unique strategiesutilized by MNCs.

## 2.2 Summary and Conclusions

To conclude with, the highest point of the pyramid illustrates the consolidation of both FSAs and CSAs. According to “Rugman (2010)”this structureexposesthe way that firm- and country-specific factors harmonize with each otherand revealsdifferent kinds of overseas Foreign Direct Investments (FDI), which practically is just the eclectic model(Dunning 1998-2000). Essentially, this fact isinstantlyrelevant withthe tax haven FDI. Undeniably, at the summit of the pyramid, it is much easier to consideratean entire industry establishing and formulatingits tax avoidance purposes. This would be consisted of the foundation of consultancy firms that mainly provideconsultation on the specific tax avoidance measures. Having contemplated about the progressionof this industry, we could realize that one of the crucial roles of the Big 4 accountancy firms is empowering MNEs to evade corporate tax through their subsidiary chain.

A noteworthy factis that all of the Big 4 international accountancy firms established their corporations in either the UK or the US and that three out of the four (PwC, Deloitte and EY) preserve their main offices in these two countries. As a result, the capacity to exploit the services proposed by the Big 4 is an inherent FSA, which is in accordance with the organizational framework developed in both home and host country settlements.

It is so vital that these challenges are verymeaningful. Especially, at the present period, bearing in mind the matter that essential regulatory-driven adjustmentsare being implementedwith intention to reform and upgrade the administrationregarding the non-audit services offered by auditors.

What is more, several tax executives and tutorsdemand the audited client to be granted with the authorization by the audit committee, right before the commence of the tax services. However, the principal procedures embolden companies to refrain from therespecting tax services by the auditors, particularly because of interests' conflict. But it is totally legitimate. Therefore, most of the businesses prefer to expand the cooperation with the auditor to tax and audit departments.Since the auditorincontrovertibly develops into an insider, it is actually reasonable, the firm's specializing and connection with sensitive financial evidences to be inevitable. Last but not least, the collaboration of the tax manager and CFO with the auditor is solid and exclusivethat the firm wishes to maintain the situation as it is.

# Chapter 3: Research Method

The core of this research isto examine the reason why some countries choose their development into OFCs andwhich national characteristic contribute to a country to utilize OFCs in comparison with others. Besides, another point to investigate is the crucial determinants of the countries with investors that increasingly prefer the cooperation with OFCs. The continuity of the study will connect the authorities that are establishedas OFCs and the total extent of the financial assets settled in these centers.An empirical methodology will pursue with intention to evaluate the national features leading to the OFC operation.

**Table 1: List of OFC's**

| Country | IMF List | OECD List | Country | IMF List | OECD List |
|---|---|---|---|---|---|
| Andorra | x | x | Liberia | x | x |
| Anguilla | x | x | Liechtenstein | x | x |
| Aruba | x | x | Luxembourg | x | x |
| Austria | | x | Macao | x | x |
| Bahamas | x | x | Maldives | | x |
| Bahrain | x | x | Malta | x | x |
| Barbados | x | x | Marshall Isl | x | x |
| Belgium | | x | Mauritius | x | x |
| Belize | x | x | Monaco | x | x |
| Bermuda | | x | Montserrat | x | x |
| Br Virgin Isl | x | x | Nauru | x | x |
| Brunei | x | x | Neth. Antilles | x | x |
| Cayman Isl | x | x | New Zealand | x | x |
| Cook Isl | x | x | Niue | x | x |
| Costa Rica | x | x | Panama | x | x |
| Curacao | x | x | Philippines | x | x |
| Cyprus | x | x | Pitcairn Isl | x | x |
| Djibouti | x | x | Samoa | x | x |
| Dominica | x | x | San Marino | x | x |
| Fr Polynesia | x | x | Seychelles | x | x |
| Gibraltar | x | x | Singapore | x | x |
| Grenada | x | x | Sint Maarten | x | x |
| Guatemala | | x | St. Kitts and Nevis | x | x |
| Guernsey | x | x | St. Lucia | x | x |
| Hong Kong | x | x | St. Vincent | x | x |
| Hungary | | x | Switzerland | x | x |
| Ireland | x | x | Turks and Caicos | x | x |
| Isle of Man | x | x | UAE | x | x |
| Jersey | x | x | Uruguay | x | x |
| Kiribati | | x | US Virgin Isl | | x |
| Latvia | | x | Vanuatu | x | x |
| Lebanon | x | x | | | |

Reference: IMF 2011 and OECD 2009

To begin with, the definition and the assessing of an OFC will be presented.Observing at the table 2, we will see that all OFCs gatheredare separated into two sources: the IMF and the OECD.By the first one, OFC is presented as a jurisdiction consisted of that financial operation that connects overseas debtors and creditors.In particular, it is based on thetotal amount ofthe commercial cycle that is associated with offshore participants on both sides of the agreement.

Regarding the second source, a nation is considered as a tax haven if there is an appropriate system of taxationwith intention to provide high-level economic services and restrained publication of sensitive information.

Table 2: Inward Portofolio Investment, 2008& 2009

| | 2008 | | | 2002 | | |
|---|---|---|---|---|---|---|
| | PI | PI/GDP | PI/Pop | PI | PI/GDP | PI/Pop |
| USA | $4,645 | 0.3 | $15,276 | $2,458 | 0.2 | $8,547 |
| UK | $2,650 | 1.0 | $43,156 | $1,323 | 0.8 | $22,308 |
| Germany | $2,185 | 0.6 | $26,614 | $1,189 | 0.6 | $14,419 |
| France | $1,817 | 0.6 | $28,305 | $760 | 0.5 | $12,322 |
| Netherlands | $1,412 | 1.6 | $85,866 | $803 | 1.8 | $49,724 |
| Italy | $1,291 | 0.6 | $21,580 | $707 | 0.6 | $12,364 |
| Spain | $1,062 | 0.7 | $23,316 | $329 | 0.5 | $7,962 |
| Japan | $1,002 | 0.2 | $7,849 | $439 | 0.1 | $3,442 |
| Luxembourg | $1,483 | 25.7 | $3,034,368 | $648 | 28.7 | $1,453,311 |
| Cayman Islands | $1,305 | 423.9 | $23,596,347 | $535 | 262.7 | $11,855,021 |
| Ireland | $962 | 3.6 | $217,364 | $236 | 1.9 | $60,135 |
| Switzerland | $469 | 0.9 | $61,286 | $228 | 0.8 | $31,341 |
| Austria | $343 | 0.8 | $41,096 | $136 | 0.7 | $16,824 |
| Bermuda | $295 | 48.3 | $4,593,006 | $139 | 35.3 | $2,214,518 |
| Belgium | $295 | 0.6 | $27,528 | $186 | 0.7 | $18,044 |
| Jersey | $265 | 52 | $2,791,183 | $48 | 21.6 | $529,591 |
| Hong Kong | $181 | 0.8 | $25,951 | $69 | 0.4 | $10,233 |
| Netherlands Antilles | $128 | 31.9 | $647,662 | $70 | 24.5 | $326,574 |
| 39 Other OFCS | $434 | 0.3 | $2,753 | $176 | 0.3 | $1,256 |

Reference: IMF's CPIS database 2008 and 2002

As the table 2 displays, we could perceive that the IMF record is embodied in the OECD one. But after the observation of the list, there are several cases that are exceptions. Such as Hungary, Austria and Belgium that are supposed to hold immensefiscal standards. However, they are not described as OFC by the IMF but as tax haven by the OECD.

Along the same lines stand the Bermuda, US Virgin Islands and Maldives, which are only registered as tax havens by the OECD. Since, they do not fulfill IMF's expectations concerning the offshore financial operations, they are not considered as OFCs by that organization.

A diversity of researches is related withwhy specific nations develop into OFCs. For instance, the "Dharmapala and Hines (2009)" paperdetected that OFCs accomplished a significant result on the "World Bank's cross-country measures of governance quality". These measures are consisted ofcorruption restriction, law implementation,political coherence,government's efficient performanceand accountability. Actually, they do make perfect sense, sincetheupgraded managementthat is granted to the investor's country is a beneficiary factor.Otherwise, the investors would not prefer OFCs.

A vital function in international investments is performed by OFCs. At the third table, we could monitor that the most valued countriesin global funds are the OFCs. In the upper half, the eight most considerable non-OFCs that receive portfolio investment stand.The USguides the path by introducing $4,6 trillion dollars of PI at the beginning of 2009.Moving to the next column, it appears a ratio of PI to GDP. As US's PI is 30% as high as its GDP, on a per capita base its inward PI is $15,000 per citizen.In more general sense, the PIof almost all the countries has been escalated. This fact implies a developedworldwide integration of economic markets.

Concerning the substantial OFCs recipients of PI, we could detect that there are distinctdiscrepanciesamong the 10 greatest centers.The champion of the investments seems to be the Luxembourg with its PI to attain the $1,5 trillion, which is 26 times larger than its GDP. This fact performs$3 million the per capita investment.In order to obtain a more holistic approach, we could contemplate theamount of $1,3 trillion that was contributed in Cayman Islands in 2008. With their population not to exceed the 55,000 residents, the GDP remains at $3 billion. Besides, the inward PI is calculated to be 424 times larger than their GDP, while the total of $23,6 million to be invested per Cayman citizen.These evidences demonstrate thatthe ability to draw the attention of the investments derives primarily from tax and governance benefits. According to the study of “Evans (2009)”, an office building in Cayman Islands called “Ugland House”hosts the official address of approximately 19,000 companies. To conclude with the sample, if we sum the PI of the 49 OFCs, we could realize that the $6,1 trillion is very close to that invested in Japan, France, Germany and Italy combined. So, OFCs possess an extremely significant level in global finance.

## 3.1 Empirical Methodology

This part of the research is designated to analyzethe root motive of investors that resort to OFCs. In the very first place, the lowest point of taxation system prevails.Thus, companies are empowered to abstain from taxation by either implying undisclosed proceedsprotected by an OFC or establishing a subsidiary office in an OFC. The way that this strategy operates is very simple. Right after the creation of the subsidiary, the parent firmperforms payments to it regarding transactions that have been extremely overvalued or even never occurred.The resulted income is categorized at the minimumtaxation range. An additionaldecisive element is considered to be the low and unsteady administrative and legislative level of the OFCs. Enterprises take fully advantage of that fact in order to circumvent the demanding and rigid regulations that dominate in their home country.Besides,clients originated by financially and politicallyprecarious countriesare granted with worldwide banking services. This could assists in the protection of theirfortune from national monitoringand further investigation.

Taken into profound consideration that fore mentioned, we could determine the country attributes that possess significant role to which investors prefer OFCs. Due to the fact that the main target of those investors is tax evasion in their homeland, it makes sense that some tax controls are justifiably implemented.The “Heritage Foundation’s index of economic freedom” assisted in the current research to apprehend the specific measures. First and foremost, the Fiscal Freedom measure is presented to be as a part of tax liabilities derived from the government. It is ranging from 0 to 1, while 1 portrays the bottom tax charges and 0 the exact opposite, tremendous tax charges.This exact variable is expected to appear an inverse relationship with OFC, since the advantages of utilizingan OFC are lower as the fiscal freedom escalates. Besides, the Investment Freedom measure calibrates several limitationsas the investment fundsproceed across markets.One scenario is that less of those limitations on capital flows are probable to develop the adoption of OFCs by facilitating the investment process there. A second scenario suggests that a nation with restrictions on global funds may assist the investors to deposit their money in an OFC to achieve better flexibility. Moreover, the Financial Freedom measureestimates the autonomy from political domination in monetarycenters. As this variable expands, investors are not in favor of moving to an OFC. Consequently, Financial Freedom holds negative correlation to OFC investment.In order to better perceive a holistic approach ofEconomic Freedom, the research encompasses the cumulative formula of it. Specifically, it is consisted of all the three preceding variables in combination with indicators regarding the business, trade, labor market and monetary freedom, property rights preservation, political consumption and freedom from adulteration.

An additional encourage factor of using an OFC is the security of investments from governmental confiscation and expropriation. The indicator of Property Rights protection is illustrated as an appraisal of howindividuals could aggregateproperty rights, which aredefended by unambiguous laws empowered by the country.The higher this indicator is, the more property rights are safeguardedalong withless OFC utility. To support this variable, details on the corruption control by “World Bank’s Worldwide Governance Indicators” are gathered. It generally includesconceptsconcerning which public authority is operated for personal benefitregardless its minor or major extend.

Furthermore, it is really significant to mention two nationwide administration variables. The performance of the government and the efficiency of the law implementation. Evidences ofthe regulatory conditionare derived from the “Worldwide Governance Indicators”. These will mainly depictseveral approaches of the political capacity to develop and materialize substantial rules empower and stimulate private field growth.Moreover, information regarding the government performanceis collected, too. Specifically, it primarily reveals concepts of the public and civil services character,the extent of the political constrains liberty, the value of policyestablishment and exercise as well as the integrity of authority’s engagement to similar tactics.

The next national-level aspect to investigate is whether the large economies have the propensity to handle OFC’s more than the lesser ones. This fact could be appraised by taking into consideration both the aggregate GDP and community’s inhabitants. Besides, a supplementary point of discussion is the typical income in a country. If prosperous countries use OFC’s more than other is well represented on the GDP per capital. It makes absolute sense, since larger savings rates will produce more capital for investment, especially in an OFC. In order to better evaluate it, an indicator of national savings over GDP is introduced, too. Last but not least, investors are probable to appear more inclined to transfer their money to places with a soaring inflation range and that is why the annual inflation rate is taken into account.

What is more, another challenge to considerate iswhy a country's funds areprofoundly aligned with OFC's. Thus, the country's aggregate outward portfolio investment that ends in an OFC needs to be calculated. The "IMF's Coordinated Portfolio Investment Survey" is absolutely of great assistance by accumulating reciprocalcapital grants regarding a huge variety of 63 nations across the years 2001-2009.These countries invest in more than 243 foreign areas of authority, 49 of which are segregated as OFC's.

The third table demonstrates a general review of the investment arrangements concerning the countries being scrutinized according always to the "IMF OFC'slist in 2009".Those holding the apical proportion of the OFC investmentare 12 and are placed on the top half of the range.On the opposite site, the 12 lowest countries are those with the slightest contribution in OFC finds.Analyzing this specific table, someone could comprehend the prodigious heterogeneity in OFC investment portions.First and foremost, Russia is a dominator with 65,3% of fundsproceeding to OFC's.

As a result of this fact, several issuesses emerge against Russia, such as extortions, frauds and powerless real estate privileges.On the other hand, Iceland maintains the 40% of the investment in OFC's, while its property rights are reasonably solid. Moreover, the nation of Kazakhstan preserves an obvious weakgrade of those rightsaccompanied by the minimum OFC investment allotment of 0,2%. In both areas of the table, rich and poor countries do exist with profitable or not economic system and effective or not government quality.All the aforementioned factors are necessary to appraise the holisticmotivations of investing in an OFC.

<u>The econometric model to be used in the calculations is the following</u>:

$$OFCI_{i,t} = \beta_0+\beta_1 EconFree_{i,t} + \beta_2 FiscalFree_{i,t} + \beta_3 InvFree_{i,t} + \beta_4 FinFree_{i,t} + \beta_5 Prop_{i,t} + \beta_6 Corrupt_{i,t} + \beta_7 RegQ_{i,t} + \beta_8 GovEff_{i,t} + \beta_9 InGDP_{i,t} + \beta_{10} InGDPpc_{i,t} + \beta_{11} InPop_{i,t} + \beta_{12} Sav_{i,t} + \beta_{13} Inf_{i,t} + \alpha_i + \delta_t + u_{i,t}.$$

First of all, to calculate the amountsin table 3 of the outward investment, the value of this fund is used. It is mainly derived from the "Coordinated Portfolio Investment Survey of IMF details collection". Secondly, the totals of the country's outward investment for both OECD and IMF listsare evaluated. By dividing these two estimates, the share of the OFC investmentoccurs.Just to remind that the countries categorized in top and bottom place are extracted by the classification of the IMF as OFC's.

Table 3: Share of Outward Investment in OFC's

| | 2009 | | 2001 | |
|---|---|---|---|---|
| | IMF List | OECD List | IMF List | OECD List |
| *Top 12* | | | | |
| Russia | 65.3% | 66.3% | 41.2% | 43.4% |
| India | 58.2% | 58.2% | . | . |
| Kuwait | 48.8% | 49.3% | . | . |
| Iceland | 44.5% | 44.6% | 25.4% | 25.8% |
| Hungary | 43.9% | 52.1% | 6.2% | 7.9% |
| Chile | 38.7% | 39.0% | 39.7% | 39.9% |
| Portugal | 38.0% | 39.8% | 29.6% | 33.7% |
| Indonesia | 32.3% | 32.6% | 27.5% | 27.5% |
| Italy | 32.3% | 35.7% | 28.7% | 30.5% |
| Malaysia | 32.2% | 33.0% | 38.2% | 50.4% |
| Czech Rep | 29.6% | 40.5% | 33.4% | 44.4% |
| Brazil | 29.3% | 47.7% | 37.5% | 39.9% |
| *Bottom 12* | | | | |
| Australia | 7.7% | 10.0% | 6.9% | 7.1% |
| Panama | 7.1% | 9.6% | 5.5% | 6.8% |
| Argentina | 6.8% | 6.8% | 0.2% | 0.5% |
| Ireland | 6.7% | 8.7% | 3.1% | 4.8% |
| Cyprus | 6.6% | 8.1% | 9.4% | 10.2% |
| Costa Rica | 6.4% | 13.2% | 46.9% | 52.8% |
| Mexico | 5.5% | 5.5% | . | . |
| Uruguay | 4.6% | 6.0% | 4.1% | 5.0% |
| Venezuela | 3.1% | 3.1% | 1.1% | 1.1% |
| New Zealand | 2.0% | 2.1% | 1.6% | 1.6% |
| Kazakhstan | 2.0% | 3.4% | 0.7% | 0.7% |
| Philippines | 1.5% | 1.5% | 5.6% | 5.6% |
| Average (63 obs) | 19.3% | 23.1% | 17.3% | 20.2% |
| Standard Deviation | 13.6% | 14.7% | 13.8% | 14.9% |

Reference: IMF and OECD 2009 and IMF and OECD 2001

The analysis of the econometric model follows. The $OFCI_{i,t}$is the share of the requestedoutcome by the country i in year t. Next to the line, the EconFree, FiscalFree, InvFree and FinFreestand for "Economic Freedom, Fiscal Freedom, Investment Freedom and Financial Freedom" respectively. The abbreviation of Property rights is the "Prop" and the Corruption's is the "Corrupt". The "RegQ" is the "regulatory quality" and the "GovEff" is the government effectiveness. Population, GDP and GDP per capita are logged. Meanwhile, the savings and inflation grades are articulated as decimals. A lot of country and year stable effects are comprised in the survey, too.

# Chapter 4: Data Analysis and Discussion

With reference to the table 3, brackets describe the P-value. The share of "outward portfolio investment" in OFC's for each nation is the dependent variable.

The table 4 confers the conclusions obtained by the econometric model. The first factor to be discussed is the government involvement in the economic field. The variables that evaluate this effect conclude to a diversity of outcomes.

The coefficients on economic freedom are significantly negative for IMF and OECD interpretation of OFC's. Its standard deviation is 0,092, which implies that one of its growth will presumably diminish the portion of OFC investment by 7,8% grades regarding the IMF list and 12,1% grades the OECD list. This exact consequence is totally harmonized with the philosophy that investors, who are based on countries with substantial government economic omnipresence will definitely pursue the OFC's. After taking into consideration the elements of the Economic Freedom index, someone could realize the existence of several intriguing and captivating facts. The Fiscal Freedom estimates the taxation liberty of the nation. A significantly positive coefficient appears concerning this variable with standard deviation 0,15. As a result, the escalation in OFC investment portion is approximately 5% to 7% just for one standard deviation advancement. This outcome seems to be kind of paradox, since countries with minimum taxation give the impression to develop more and more OFC funding. But this is probable to be considered as an adverse causality. For example, a country maybe compelled to belittle its taxes in order to avert people from maintaining their money in an OFC in case this specific country has to deal with a tremendous magnitude of OFC competition. With regards to the Investment freedom, it is palpable that it holds a significantly positive coefficient. An alteration of one-point standard deviation could clearly lead to an escalation of 2-3% in OFC funding portion. This fact implies that less regulations could support such investments on global range. On the other hand, Financial Freedom has a vast negative influence on OFC investment, but just for the IMF list.

If one-point increase occurs in standard deviation, a decrease of 1,7% would be induced in OFC funding portion.

The main crux of this notion is that the government intervention in economic markets is really constrained.

Table 4: The Determinants of OFC Investment

| | IMF List | OECD List |
|---|---|---|
| Economic Freedom | -0.844 | -1.306 |
| | [0.000] | [0.000] |
| Fiscal Freedom | 0.308 | 0.449 |
| | [0.000] | [0.000] |
| Investmet Freedom | 0.115 | 0.162 |
| | [0.019] | [0.002] |
| Financial Freedom | -0.093 | -0.013 |
| | [0.067] | [0.810] |
| Property Rights | 0.051 | 0.025 |
| | [0.408] | [0.691] |
| Control of Corruption | -0.057 | -0.059 |
| | [0.003] | [0.004] |
| Regulatory Quality | 0.096 | 0.159 |
| | [0.000] | [0.000] |
| Government Effectiveness | 0.079 | 0.074 |
| | [0.003] | [0.007] |
| $\ln GDP$ | 0.065 | 0.080 |
| | [0.624] | [0.559] |
| $\ln GDPpc$ | -0.057 | -0.078 |
| | [0.669] | [0.572] |
| $\ln Pop$ | -0.042 | -0.055 |
| | [0.753] | [0.689] |
| Savings Rate | 0.002 | 0.002 |
| | [0.006] | [0.010] |
| Inflation | 0.000 | 0.000 |
| | [0.979] | [0.810] |
| Constant | -0.132 | 0.022 |
| | [0.424] | [0.895] |
| $R^2$ | 0.207 | 0.250 |
| Obs | 542 | 541 |

Reference: IMF and OECD 2009 and IMF and OECD 2001

Having an effect only on IMF list and not on OECD's indicates that this variable provides the countries of the second list, exceptional prospects. This definitely needs to be investigated much more, generally speaking. Concerning the variables of property rights and corruption, someone could easily comprehend the existence of conflicting consequences. First and foremost, the security of real estate privileges does not perform an important impact on OFC investment dividend. Taking into consideration the heterogeneity of nations in table 3, this could possibly not seem shocking and unanticipated. However, corruption is not likely to be totally involved. The respective variable of its control is significantly negative for both requirements and holds a standard deviation of 1.012. As a result, one-point of its development in government corruption control provokes almost 6% reduction in OFC investment portion. So, investors in countries with high levels of corruption do handle the global banking services granted by OFC's.

It's noteworthy to point out that a good and effective governance has an enormous impact of OFC funding contributions. A substantial quality of the regulatory systems leads the country to deal with more and more OFC investment. For the IMF list, moving one-point upwards in standard deviation of this variable, then a 7,3% increase would appear. But when it comes to the OECD list, an advancement of 12,2% would occur. The capability and the potency of the government illustrate a positive consequence on OFC funding shares, despite its lower degree. If this variable depicts one-point increment in its standard deviation, the OFC investment allotments would escalate by 6.5% more.

This beneficial influence advocates that nations with such powerful, productive authorities and strict implementation of their law tend to regularly take advantage of OFC's. A possible interpretation of this fact could be that investors of these countries have an imperative necessity to resort to OFC's, because it is difficult to them to equivocate and evade regulations in effective administered nations rather than in deficient ones.

Regarding the fiscal intensity, population, medium income and inflation, there is no clear correlation with OFC funding portions. Just the savings percentage seems to be important. With its standard deviation to reach the 10,3 points, a one standard deviation growth in the savings grade will possibly provoke the OFC investment dividends to develop approximately by 2% more. So, a nation with such an immense variable is expected to dispose more available money concerning contributions, even if those are based inland or abroad. The way they prefer to offer their funds is considered to be limited in comparison with the way of countries having more reduced savings ratios.

# Chapter 5: Conclusion

Concisely, the principal intention of the present survey is to estimate the country level determinants that mainly have an impact on which investors resort to OFC's systems. The study's primary outcome indicates that the economic freedom is the notable impediment to OFC contributions. Investors in this country are progressively deterred from OFC's, whereas this variable develops. It is difficult to define absolutely the term of economic freedom, since it is a generic one. Its exact elements concede several perplexing conclusions. It is commonly accepted that the countries which apply minimum taxes urge their investors to operate more to an OFC center. Although that fact could derive from reverse causality, the competition based on the OFC's is definitely decreases the tax scale in nearby places. The OFC funding is being boosted by the lack of regulations on global capital while the less government connection in economic markets causes its reduction. The countries with solid implementation of their rules maintain more OFC investment. Specifically, their investors find it really difficult to evade the internal regulations. As a result, they do designate an OFC with weak law enforcement to conserve their fortune. Beyond any doubt, if a country attempts to diminish the OFC funding, it would ideal to manage its domestic corruption issue, since it is forcing the economic placement into the OFC's. Having entirely comprehend the determinants that motivate investors to make use of the OFC's is doubtlessly significant for a variety of reasons. Investments in OFC's are likely to serve as heavy levying of taxes, especially during the debt crises that the globe suffers from. Besides, it is challenging to determine a country's potentiality of risk vulnerability, when the OFC contribution is at an immense grade. That is happening because the OFC is described as a mediator between the final purpose and the investment point of supply. The higher the level of the OFC funding, the more dangerous it is for the country to finally be exposed to risk, even if its balance sheet may have stated otherwise. If someone could better imagine the countries with excessive OFC publicity, its assistance would be priceless to precisely evaluate the risk in global capital trades. As professor Levy in 2014 and Grindle in 2004 reported Elsewhere in development, we are constantly reminded that development actors should not impose simplistic blueprints, and should recognize the imperfections of real world markets and fit practice around these realities. Ideas such as 'working with the grain' and 'good enough governance' are met with widespread approval from practitioners.

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