

Civil Society Recommendations to African Governments

on

Tax and related aspects at the

**Africa Regional Consultations towards the Third Conference on Financing for
Development, 23rd and 24th March 2015**

Addis Ababa, Ethiopia

Submitted by

Tax Justice Network –Africa (TJN-A)

On behalf of CSOs

March 2015

Summary of CSO Recommendations to African governments

1. *African countries should push for the centrality of taxation as both the most important source of financing for development needs and the key lever to fight inequality.*
2. *African countries should call for the establishment of a new intergovernmental body on tax matters with a clear mandate*
3. *African countries should stand together to ensure that FfD process not only recognises the importance of measures to increase transparency and accountability within the private sector as it does in Article 25 of the Zero draft but also that it commits the countries to act.*
4. *African countries should implement the recommendations contained in the AU/UNECA high level panel (HLP) on IFF report.*
5. *African countries should push for the integration of women's rights into the FfD agenda as an important issue which has relevance for tax policy*
6. *African countries should push for commitment to the principle of redistribution via taxation and ensure the global data collection effort envisaged within the SDGs includes tracking the equity implications of tax policy*
7. *African countries should call for the recognition of international cooperation on tax as a key priority related to financing within the new global partnership for sustainable development.*
8. *African countries should make an explicit statement that MNCs paying their share of tax will be a major means of financing the SDGs.*

Introduction

It is now clear that the MDG process relied too heavily on overseas development assistance (ODA). This shortcoming needs to be overcome and the issues of tax dodging and illicit financial flows fully addressed, if the Financing for Development Conference, scheduled to take place in Addis Ababa in July 2015, is to deliver on the financing needs of the Post-2015 Agenda. The Africa regional consultation on the FfD should also result in an African Common Position on FfD. The recently launched “**High Level Panel Report on Illicit Financial Flows from Africa**”¹, endorsed by African Heads of State and Government on January 30, 2015, comprises recommendations which African countries should promote within the FfD process and commit themselves collectively to implement them within the framework of continental cooperation and in individual African Countries. This position also reflects the very recently published ‘Zero Draft of the Addis Ababa Accord’ as presented by the co-chairs.²

African countries should recognise the central role of taxation in development as a prominent issue. Despite the perception that Africa survives on ODA, resources raised from taxation are far superior to ODA. When a country depends on its tax revenue, the substantial burden of coordinating between and reporting to multiple donors disappears. Countries become more accountable to citizens and can pursue, in a more cost-effective and integrated manner, national development goals. The accountability mismatch disappears as countries become accountable for revenue-raising as well as the delivery of progress.

While a focus on self-financing through taxation has much to recommend it, it is also clearly the case that many African countries are not collecting sufficient amounts via taxation systems. New research finds that many non-resource rich African countries have tax collection levels below 15% of GDP,³ indicating the weak levels of tax collection across the developing world. But it is also evident that there is a lot of room for improvement. Yet this improvement cannot be at the expense of the people in poverty via focus on regressive taxes. African countries lose too much due to tax evasion and avoidance, poor enforcement of direct taxation of assets and income, and widespread tax incentives and exemptions, which result in large fiscal losses. The substantial problem of illicit financial flows and the large amounts of resources leaving African countries untaxed is now well recognised. As the HLP report clearly demonstrates, illicit outflows are larger than inflows from aid and that a large proportion is driven by tax abuse via trade mispricing practices. As a result national and international tax issues are inextricably linked and are both fundamentally important in financing for development (FfD) debates.

The purpose of this paper is to inform the Africa Regional Consultation on Financing for Development taking place in Addis Ababa end of March 2015. It summarises recommendations that should be incorporated in Africa’s Common Position on FfD and ultimately in the final formulation of the tax relevant components of the outcome document

¹ http://www.uneca.org/sites/default/files/publications/iff_main_report_english.pdf

² <http://www.un.org/esa/ffd/wp-content/uploads/2015/03/1ds-zero-draft-outcome.pdf>

³ Prichard, Wilson, Cobham, Alex and Goodall, Andrew, *The ICTD Government Revenue Dataset*, The International Centre for Tax and Development, Working Paper 19, 2014

of the Financing Development Conference which will take place mid-July in Addis Ababa, Ethiopia.

Tax and the Financing for Development Agenda

Revenue-raising from taxation is now consistently recognised as an important part of the FfD agenda. In addition, the attention paid to illicit financial flows and the commitment to enhance efforts to combat tax evasion and avoidance via more international cooperation are also welcome. Even though Articles 7 and 17 of the Zero Draft attempts to do so, there is need for all countries particularly African countries to embrace the centrality of taxation as both the most important source of financing for development needs and the key lever to fight inequality.

While it is not sensible to ignore any financing options all forms of financing are not equal. Tax is the most sustainable and reliable source of financing for all states. It enhances both the accountability of governments to citizens⁴ and of businesses to society. It is also the key lever to reduce income inequality in society. While ODA will still play an important role - especially for the poorest countries - the importance of a well-functioning system of taxation cannot be overstated.

However, this has not been well reflected in discussions which often have a significant imbalance emphasizing heavily private finance.⁵ This is problematic for a whole host of reasons. For example, it is already clear that foreign direct investment (FDI) flows to the non-resource rich African countries are very low. The quality of FDI and the benefits that African countries ultimately derive have been repeatedly called into question, with many African countries unable to ensure linkages with local firms, dynamic accumulation of capital, technology transfer, high quality job creation and skills transfer. FDI flows are often accompanied by significant outflows of resources and of course the profit-seeking nature of FDI means this form of financing does not flow to many important sectors of public service provision. While these limitations are not sufficiently addressed, conversely one of the greatest benefits of FDI – the tax it can yield - is insufficiently dealt with. Tax has been historically ignored due to an over-reliance on ODA. It now appears that there is a danger that the fundamental role of tax and the urgent need to reform international tax rules will be overlooked in favour of a skewed focus on private finance.

Financing for Development and International Taxation Issues

While generally tackling tax evasion and avoidance, and the many shortcomings with international taxation rules, have consistently received attention in FfD preparatory work, there is still a lack of clarity in terms of the concrete measures to be taken. One of the biggest priorities for the FfD process must be the creation of a properly functioning and resourced international body with a mandate to deal fully with global taxation issues. The Zero Draft is taking small step forward by changing the UN Tax Committee from an expert one to

⁴ Prichard et.al. 2014, ICTD Working Paper: <http://www.ictd.ac/en/publications/taxation-non-tax-revenue-and-democracy-new-evidence-using-new-cross-country-data>

⁵ See for example: Report of the Intergovernmental Committee of Experts on Sustainable Development Financing (ICESDF), 8th August 2014)

intergovernmental one in Article 28. While a step in right direction, it is insufficient and proper UN tax body with clear mandate to focus its effort on financing for development via curbing tax evasion and avoidance is needed. We appeal to African countries to share this position within the FfD negotiations, especially the upcoming drafting session taking place from 13th April in New York. Currently a substantial part of work on international tax matters takes place under the auspices of the G20 and is practically taken forward by the OECD. This has meant that two important processes - regarding automatic exchange of tax information and ‘base erosion and profit shifting’ (BEPS) – have excluded most African and other developing countries from negotiations and decision-making. There have been repeated requests to address this global tax governance problem, including from the G77 which has proposed that the UN Committee of Experts on International Cooperation in Tax Matters be upgraded to an intergovernmental body.

Financing for Development and Commercial Tax Evasion and Avoidance

A much greater acknowledgement is needed that the FfD process will ensure that multinationals pay their share of taxes ‘where their economic activities take place and value is created’. Given the shortcomings in current global tax rules and the ease with which MNCs are able to reduce enormously the taxes they pay⁶ the fiscal losses for all countries are momentous. Research has also shown that poorer countries generally suffer the greatest shrinkage of the tax base as a result of corporate profit shifting and the multinational tax base of some lower income countries could even be double their current size.⁷ Without a doubt this is the most obvious area where a global effort to make things fairer would result in direct and large revenue raising for African countries. This should be considered as one of the most important means of mobilising resources to enable African countries to implement their development goals.

African countries should stand together to ensure that FfD process not only recognises the importance of measures to increase transparency and accountability within the private sector as it does in Article 25 of the Zero draft but also that it commits the countries to act and does not stop at toothless declarations. This is critical given the risks within the international financial system that were revealed during the global economic and financial crisis, as well as to ensure multinationals pay their fair share of taxes. While private sector investment - with pursuance of legitimate profit making - will play an important role in promoting sustainable development, the responsibility of the private sector in relation to tax must be more strongly emphasized. The practice of multinational companies who promote, use and benefit from the global “tax avoidance industry” is not compatible with the role of the private sector in contributing to Africa’s development.

⁶ The OECD has found that some multinationals use strategies that allow them to pay as little as 5% in corporate taxes when smaller businesses are paying up to 30%. See: OECD, *Addressing Base Erosion and Profit Shifting*, A study commissioned for the G20, 2013.

⁷ Note that current data does not capture the global nature of profit shifting particularly in relation to developing countries. See: Cobham, A. and Loretz, S., *International Distribution of the Corporate Tax Base: Implications of Different Apportionment Factors under Unitary Taxation*, International Centre for Tax and Development, Working Paper 27, 2014.

Financing for Development and Domestic Tax Policy

It is also clear that the much broader aspects of taxation and development related to strengthening national tax systems - and most critically ensuring tax systems are pro-poor and progressive in nature – have been dealt with in the FfD process to date not in sufficiently clear way. Despite a clear commitment made in Doha to undertake efforts to enhance tax revenue “with an overarching view to make tax systems more pro-poor”⁸ To this point the Article 18 in the Zero draft of the Addis Ababa Accord could be a good guiding principle.

African countries must do their own homework and take responsibility to pursue effective domestic resource mobilisation strategies and to develop fair and efficient tax systems. However it is imperative that these efforts be complemented by international action. Currently there is a ‘disabling environment’ due to the existence of secrecy jurisdictions, opaque financial practices, inappropriate global tax rules, a proliferation of tax competition and harmful tax practices, and a lack of financial transparency. Truly global cooperation is necessary to make progress and many of the recommendations concentrate on this area.

In addition it is important to consider recommendations for action in light of the ‘**common but differentiated responsibility**’ principle. This concept is well-established within the field of climate change but is also relevant to taxation. All countries have a common responsibility to reduce illicit financial flows and combat tax evasion and avoidance. But given developed countries largely control the international financial system, dictate global tax rules and headquarter and regulate most multinational enterprises, it should be clear that developed countries have differentiated responsibilities. They must act urgently to ensure financial transparency increases and global tax rules are reformed specifically to benefit developing countries whose taxing rights have been undermined. Automatic exchange of tax information is another example where common and differentiated responsibility comes into play given the reciprocity challenges. African countries should be able to receive information even if they cannot provide it. This would not be a permanent waiver of reciprocity but would exist for an agreed time period. Throughout the recommendations below the enhanced responsibilities of developed countries to take action are highlighted.

1. Overarching recommendations civil society proposes to African countries to promote in the FfD process

- *Recognise the centrality of tax within the FfD agenda given it is the key source of financing for sustainable development with multiple benefits.*
- *Recognise explicitly that taxation is both a means of financing and a tool to reduce inequality.*
- *Commit to the principle of redistribution via taxation and ensure the global data collection effort envisaged within the SDGs includes tracking the equity implications of tax policy*
- *Recognise that international cooperation on tax is the key priority related to financing within the new global partnership for sustainable development.*

⁸ United Nation, *Doha Declaration on Financing for Development*, International Conference on Financing for Development, 2008

- *Make an explicit statement that MNCs paying their share of tax will be a major means of financing the SDGs.*

2. Recommendations regarding financial transparency and accountability

Improving financial transparency is critical. There is already progress in some areas. A number of countries have committed to public registries of beneficial ownership. The OECD has published a new international standard for automatic exchange of tax information – the Common Reporting Standard - and a number of countries are piloting it. However, it is still unclear if developing countries will be included in multilateral automatic exchange or required to seek bilateral agreements and how the issue of reciprocity will be dealt with. The OECD has also created a template for country-by-country reporting, a major achievement. Going forward in this area entails measures being taken by developed and developing countries, with developed countries having the most urgent responsibility to enact financial transparency measures. Concrete measures must be agreed in Addis Abba to define the process going forward.

As stated in the HLP recommendations in the Report on IFF from Africa, we recommend that countries commit to:

- *A complete elimination of secrecy of beneficial ownership worldwide. This entails all countries committing to the creation of public registers of beneficial ownership for all legal persons and arrangements.*
- *Adopting a common standard of multilateral automatic information exchange, with differentiated responsibilities for developing countries which lack the capacity to provide information over a specified time period.*
- *The effective implementation of annual country-by-country reporting by multinational companies operating in their territory. All country-by-country reports must be immediately available to all tax authorities and must also be made public to enable greater accountability of companies, tax authorities and governments to their citizens.*

3. Recommendations regarding international cooperation on tax matters

A strengthened global partnership aiming to finance and achieve the SDGs should unquestionably focus on international tax matters first. Such a prioritisation is not yet guaranteed, however, the UN Secretary General has reiterated a call for the establishment of an intergovernmental committee on tax cooperation. A very concrete commitment is needed in this area to solve what is a significant gap in global governance in the tax arena. Countries must commit to:

- *Establishing a new intergovernmental body on international cooperation in tax matters and providing the resources necessary to allow the body to operate effectively. It should be of a commensurate size to the OECD and with a similar technical resource capacity. All states should have full rights of participation in the new body.*

- *Charging this body with developing a new multilateral instrument to further strengthen international cooperation on tax matters. This instrument should set high level principles regarding global tax cooperation, including proposing structural reforms to the currently skewed international tax system and making practical commitments to action.*
- *Providing this body with a comprehensive mandate for action including issues such as: base erosion and profit shifting, tax and investment treaties, tax incentives, taxation of extractive industries, beneficial ownership transparency, country-by-country reporting, automatic exchange of information for tax purposes, alternatives to the arm's length approach, promotion of progressive tax systems and minimising harmful spill-over effects of tax policies.*
- *Giving responsibility to this body to facilitate direct cooperation between countries to minimise tax competition and ensuring collaboration of tax authorities of member countries to exchange information and experience and jointly assess the tax dodging risks of specific multinational companies.*

4. Civil Society recommendations to African Governments regarding domestic tax policy

It is encouraging that strengthening revenue-raising in African countries is being recognised as an urgent task. However, it should also be recognised that ensuring revenue is raised in a progressive manner is a critical element which has received insufficient attention. Caution should be exercised when commitments to raise tax/GDP ratios are being considered. Such a commitment must be linked explicitly to tax equity, ensuring African countries focus on the direct taxation of wealth, income and assets, the removal of tax incentives and exemptions benefiting large corporate actors and efforts to eliminate loopholes and improve enforcement.

The integration of women's rights into the FfD agenda is also an important issue which has relevance for tax policy. The loss of tax revenues due to tax evasion and avoidance significantly reduces the funds available to finance policies aimed at fulfilling the human rights of women and girls. Women in most societies are over represented in the lowest quintiles of income distribution and bear the brunt of regressive taxation which overburdens the poor. Progressive and effective tax systems are therefore particularly important for women. In this area African countries should commit to:

- *Enhancing domestic resource mobilisation by adopting a full range of progressive taxation measures as a primary means of funding national development goals. Tax policy design and implementation must actively seek to reduce income inequality.*
- *Taking urgent action to minimise tax expenditure by significantly reducing tax incentives and exemptions. Tax expenditure statements must be published annually alongside national budget statements and progress tracked in this area.*
- *Work collaboratively with other African countries to set common standards and minimise the corrosive effect of tax wars. As a priority starting point, collaboration could be achieved in relation to tax incentives.*
- *Providing opportunities for citizens to make their voices heard regarding tax policy and how revenue raised is spent.*

- *Enhancing national statistical capabilities to monitor and evaluate the performance of all tax types, the size of the tax gap and how the tax burden is being shared.*
- *Ensuring fiscal policies are gender sensitive. This should include assessing and tracking the tax burden on poor men and women.*
- *Review bilateral taxation treaties with developed countries to ensure that African countries are getting their fair share of revenue.*