

BIAC Discussion Points on Tax and Development

April, 2011

General Points

One of the most important advances in the development agenda over the past twenty years, has been the insight that tax, and a functioning tax system, are increasingly recognised as the most critical factors in allowing developing countries to build a strong civil society. Tackling this challenge will require international concerted efforts among *all* countries, developed and developing alike, while business has an important role to play as well. Many developing economies are burdened with severe domestic challenges such as persistent poverty, corruption, political instability, burdensome bureaucracy, and ageing infrastructures, among others.

Aid flows will continue to play a strong part in addressing these domestic challenges, but aid alone will not bring about the required changes that are needed to boost strong, sustainable and balanced growth in these countries. The required gearshift in development will only happen as a result of also mobilising the foreign and domestic private sectors in order to boost their investment in infrastructure, agriculture, and other economic sectors, and through developing countries reaping some of the benefits of that growth through functioning tax systems, it is important that a larger share of the aid budget is spent on capacity building for tax administrations – the current proportion of 0.7% is too low

The private sector can play an important role in capacity building and domestic resource mobilisation, as it relates to taxation. As a first step, there has to be a predictable and attractive enabling policy framework in place to inspire market confidence and to attract private sector investment which generates tax revenues for countries. This entails: rule of law; clear, predictable and transparent legislative frameworks; open competitive markets for trade and investment; fiscal transparency; human resources development; good governance; anti-corruption; fair competition policy; and so on – issues relating to taxation should be considered in this context as well as the broader policy context. Bringing together both public and private sectors, such as via public-private partnerships and leveraging aid for attracting private investment, will be essential in order to generate the necessary financing for development while reducing risks for investors. The private sector can also help more directly, by sharing expertise with tax authorities, and working with them as partners.

Capacity building for tax administration requires the development of good policy and good tax administration. It is important that the funding is provided to pay tax administrators, to provide both the hardware and software tools needed and to fund training.

Further to the G20 Seoul Summit's Multi-Year Action Plan on Development, BIAC welcomes and encourages OECD focus on development policy -- including the establishment of the joint CFA DAC informal task force on Tax and Development -- that goes beyond aid and we believe that work related to taxation is especially relevant to development polices which foster sustainable economic growth and societal well being.

OECD Project on Taxation and Domestic Resource Mobilisation: BIAC Key Messages

Domestic resource mobilization, as it relates to taxation, should maintain as a primary objective the development of competitive, transparent and predictable tax systems. The following are a number of key points, which BIAC believes should guide the OECD work on tax and development:

- Generally, it is important that this project have clearly defined development objectives for each issue under consideration that are understood and adhered to by all participants to the project.
- It is important that policy coherence remains a consideration throughout the project. This is relevant on two levels:
 - Policy Coherence as it pertains to the policy framework for investment and economic growth, which is fundamental to the generation of tax revenues;
 - Policy Coherence as it pertains to the coordination of work among the international organizations, which are currently examining these issues. The output of the Task Force should be relevant and coordinated with other international organizations, the international financial institutions and regional initiatives.
- Developing countries should take an active role in the project, which is also supported by a multi-stakeholder process.

The following are key BIAC messages for each of the four areas of work being undertaken as part of this project:

1. Statebuilding, accountability and effective capacity development:

Capacity building for tax administration/revenue institutions is an important and fundamental infrastructure development for developing countries to move from aid to sustainable revenue. This is critical for local development. It enables countries to benefit from investment and local economic activity in the country. It is a basis to

develop the public infrastructure and services and a social benefit system in a sustainable way, and the transformation from informal to formal economies.

- **Good governance is a prerequisite for successful capacity building for revenue institutions.** Transparency and accountability must apply also to governments in this respect, and corruption must be eradicated. To help facilitate this, aid should be allocated to provide support for tax administrations in the form of competitive salaries for tax officials and the technological infrastructure for a modern tax administration including both hardware and software.
- **Raising tax revenues from FDI also requires that the developing country has a supportive regulatory/investment environment to attract and support sustainable business activity.**
- **A coherent funding programme needs to be developed to facilitate capacity development. Such a programme should be agreed by a partnership of aid organizations, developing country tax administrations, international organizations and the business community.**

2. More effective transfer pricing regimes in developing countries:

The project should continue to promote the arms length principle and provide guidance and a focus for discussion on the effective understanding and application of the OECD Transfer pricing Guidelines, and the principles contained in the OECD Model tax Convention as relevant.

- Capacity building and technical assistance regarding transfer pricing in developing countries is needed.
- OECD guidance to developing countries on the application of the arm's length principle to relevant transactions is important. Business can assist in this capacity building.

3. Increased transparency in the reporting of financial data by MNEs

- It is necessary to put in place sensible assessment of the role of transparency/disclosure in driving development as it relates to international business taxation.
- The OECD work related to “country by country reporting” must have a clear development objective. In this respect the various current initiatives for Extractive Industries should be tested and evaluated before any wider steps are taken.
- Transparency should also be considered in context of how it may contribute to more the integrity, efficient and effective tax collection on the part of revenue authorities.

4. **Countering International tax evasion/avoidance and improving transparency and exchange of information**

- The OECD Global Forum on Information exchange and transparency, which comprises 90+ countries, is an important forum through its analysis and peer review mechanism, for addressing issues related to transparency and exchange of information as it relates to taxation.
- This work should focus in particular on enforcement aimed at illegal activity through effective transparency and exchange of information (including multi-lateral exchanges of information between governments)
- The work of the forum on tax administration (FTA) can be a useful contribution to the work of the Task Force.

Business supports the need to build capacity in tax administration and policy development and seeks an active role in the coalition of interests to achieve this.