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Bringing taxation into the post-2015 development framework

Significant new finance will be needed to realise the welcome ambition of the post-2015 development process. While aid will remain crucial for the foreseeable future, additional alternative financing sources must be a feature of the future development financing framework.

Of the options on the table, taxation is amongst the most likely to raise the necessary amount of new and additional money. Tax, and its avoidance, has received extensive political and public attention recently. Making tax a greater source of development finance would require action from all countries to ensure that the global rules of taxation work more predictably and more clearly, and are better enforced. This would comprise a clampdown on tax avoidance and ensure that all taxpayers contribute fairly to public finances. Measures to support increases in the amount of tax that developing countries are able to raise from wealthy domestic taxpayers will also be needed.

Options

In the context of the High Level Panel's Bali meeting, which focuses on global partnerships and means of implementation, options include:

1. ensure that international treaties and agreements safeguard developing countries' taxing rights on cross-border income and capital
2. increase transparency including in tax havens and in companies themselves
3. support countries in building regional agreements to address tax competition and excessive tax incentives.

Increased levels of aid should also be made available to build the capacity of developing countries' tax authorities and revenue collection systems. But such capacity-building assistance will be able to make a positive contribution only if tax authorities gain the legal tools provided by option 1, the access to information generated by option 2, and the protection against other jurisdictions' harmful fiscal and juridical regimes produced by options 1 and 3.

Ideally, the post-2015 framework would enable progress towards reaching a universal domestic resource 'floor' consisting of, for example a narrowing of the corporate tax gap in developing countries – potentially leading to a 20% increase on the current corporate tax take[5] and/or an increase in overall developing country tax take overall as a proportion of GDP, potentially reaching a tax/GDP ratio of 25%.

Financing potential

Together, policy changes along these lines could increase the proportion of their income that developing countries raise in tax – globally and from multinational corporations specifically - by a significant amount.

Apart from the potential sums involved, there would be many other advantages to a focus on tax as a source of development finance. The necessary measures would improve transparency, accountability and governance; provide greater predictability for business; put developing countries in the driving seat of their own development; and contribute to inclusive, equitable growth.

Palm tree paradise? Domestic action to prevent international tax leaks

In the Dominican Republic, tourism is a crucial part of the economy; it accounts for 10% of GDP and a third of foreign investment. Within tourism, the all-inclusive multinational hotel sector accounts for the vast majority. An audit by the Transfer Pricing Department found some strange characteristics of this industry. 80% of all rooms in this sector are 'sold' to related companies located in tax havens. Yet these sales were made at a unit cost lower than the unit income per hotel room, according to prices advertised online and in tour operator catalogues. The all-inclusive sector in the Dominican Republic declared losses, repeatedly, for over 10 years, while apparently being underpaid for hotel rooms whose revenues went to related companies in tax havens. In other words, it appeared that profits were being shifted to low-tax jurisdictions and losses declared in the host country.

After the sector was fully audited, the Supreme Administrative Court confirmed irregularities. This led to the design of a customized transfer pricing regime, based on a thorough analysis of business models in the industry, and using publicly available information on the price by end users for hotel rooms. The Dominican Republic's tax authority also created a dedicated Transfer Pricing Unit in 2011, initiated a debate amongst all stakeholders on clarifying transfer pricing rules, and imposed a new obligation for taxpayers to submit transfer pricing documentation.[6]

Global partnership in the MDGs and new challenges post 2015

The post-2015 process is showing welcome ambition. There is the possibility of agreement around ending extreme poverty, there is attention to gender equality as a cross cutting issue, and it is a far more participatory process than the previous one. Discussions within the High Level Panel have so far focused on development outcomes, but increasing attention is now starting to go to financing, within the context of a renewed global partnership. Although no one has yet braved an estimate of the numbers, significant new finance will clearly be needed to realise the ambition. A post-2015 agreement that genuinely commits to a new global partnership for development is likely to be the only way to secure global political agreement on the new framework overall.

The final millennium development goal, MDG8 – Develop a Global Partnership on Development – was important in focusing on the need for all actors to contribute to global development. It encompassed targets on many aspects of global policy – "to develop further an open, rule-based, predictable, non-discriminatory trading and financial system." It also focused on non-quantified targets such as the special needs of least developed countries, landlocked countries and small island developing states, debt relief, aid, affordability of essential medicines and access to technology. Indicators captured parts of this agenda.

Since 2000, some gains have been made in many of these areas. In 2007 the UN set up the 'MDG Gap Task Force' to monitor implementation of MDG8. The task force reported progress in the first few years, but has more recently seen backsliding, saying that "the waning of support for the global partnership for development may be understandable in the context of a protracted economic and financial crisis."[7] Moreover, MDG8 has often been forgotten during discussions of the MDGs, and it is unlikely that the

"Just as the developed countries have been interested in tax havens and stopping tax evasion, we are saying that many of the tax havens and so on also have monies of developing countries…Developing countries have a duty for proper governance to stop monies flowing out. But developed countries also have a duty to return those monies back to them because it could be significantly more than the aid."
Ngozi Okonjo-Iweala, Nigerian finance minister.[1]

progress that has occurred is related to the existence of MDG8 – "there is scant evidence that this [MDG8] has had any impact on rich country behaviour", says one typical assessment.[8] The generally 'soft' nature of the targets may be one reason why it was possible to overlook MDG8; lack of global political commitment to the substance of the targets is another.

In 2013, as the post-2015 agenda develops, the world faces a new set of challenges. The post-2015 agenda itself will likely be more challenging than the MDG agenda was. Ending extreme poverty means reaching the most vulnerable and excluded people, the hardest to reach. This will need financing, as well as changes to underlying causes of poverty and inequality. Yet, the global context approaching 2015 is very different from that in the late 1990s, when the MDGs were negotiated. As well as the continuing economic downturn, global geopolitical formations are changing rapidly, and dealing with climate change is more widely recognised as urgent. In this context, while traditional aid must remain part of the financing for the next generation of development goals at least, we need to find new and additional sources of finance to complement aid.

Financing for development – where we are

The largest sources, by far, of public sector finance in developing countries are public revenues and aid. Tax revenues are on average equivalent to 13% of GDP in low-income countries and 20.7% in upper middle income countries.[9] Aid, meanwhile, constitutes around 10% of GDP in low-income countries (and

Children on their way to school, Walking past a Glencore-owned mine in Zambia. The company stands accused of tax dodging on a massive scale. PHOTO: ACTIONAID

Ups and downs in Zambia

Tax revenue as a proportion of GDP has increased by nearly a third in Zambia between 2009 and 2011, according to IMF statistics, although a fall is projected for 2012.[24] Nonetheless it remains low compared to other lower-middle-income countries, possibly as little as 10-12%.[25]

Mining tax arrears have recently been a major political issue in Zambia, and an important one given that mining provides 37% of GDP. The country has moved from effectively subsidising the mining industry by about 4% of GDP, to receiving around 4% of GDP in taxes from mining.[26] Non-mining taxes, however, are declining, and there are plans to strengthen tax administration.

In February 2013, ActionAid revealed that excessive tax incentives and tax avoidance is also a problem in other sectors in Zambia. We estimated that a combination of company-specific tax breaks for, and tax-haven-linked avoidance by, a single company - the Zambian sugar subsidiary of UK-based multinational Associated British Foods - has cost the Zambian government US$27 million since 2007.[27] The estimated avoidance alone is equivalent to the revenue needed to put an additional 48,000 Zambian schoolchildren in school – in a country where only 53% of schoolchildren complete their primary education.[28]

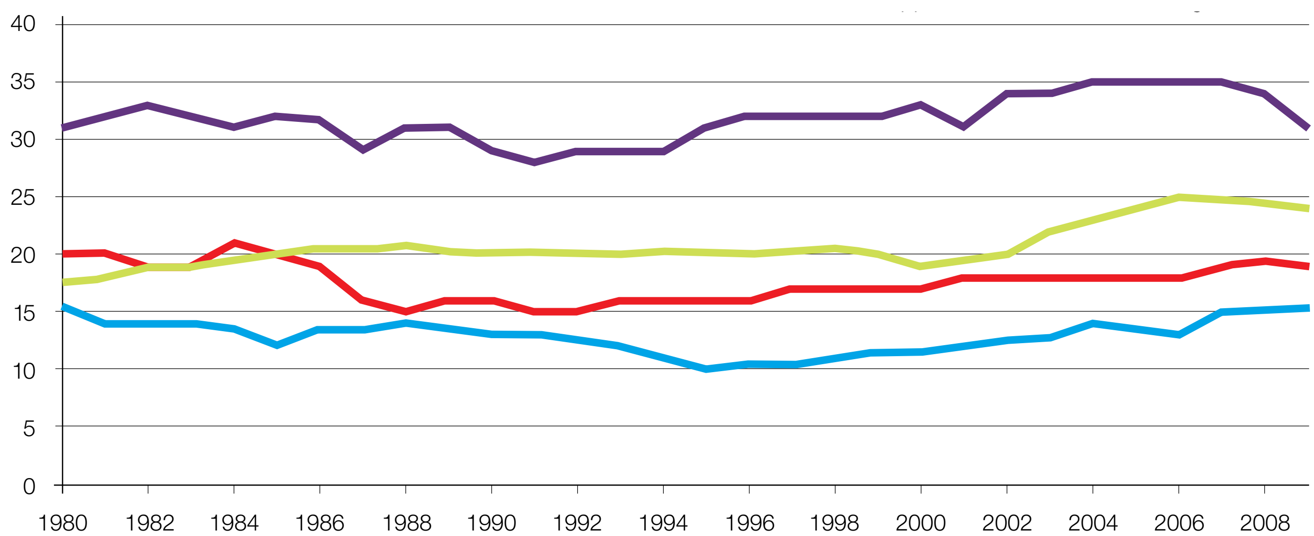
considerably less in middle-income countries).[10]

Both sources of finance link to some extent with growth. Developing country growth has been relatively strong since the late 1990s, and so far more resilient during the global financial and economic crisis.[12] But this economic progress in terms of GDP growth has in many places failed to deliver proportional benefits for poverty reduction and social development. One reason is that countries have not always been able to secure commensurate public revenues alongside growth.

Meanwhile, growth has been generally weaker in developed countries and especially following the financial crisis of 2008. This may be affecting aid levels, which recovered during the 2000s but now appear to be levelling off. A 2005 UN estimate of the amount of revenue required to meet the MDGs equated to OECD countries contributing 0.54% of GNI in aid by 2015.[13] By 2011 OECD countries were in fact contributing 0.33% of GNI (about US$133 billion a year); the figure was slightly lower in real terms than the peak in 2010.[14] The importance of aid is illustrated by a recent nine-country study of finance needed to reach the MDGs. It concluded that five of the countries studied (Egypt, the Philippines, South Africa, Tunisia and Uzbekistan) could feasibly finance their MDG strategy by increasing domestic tax revenues. In the other four countries (Kyrgyzstan, Senegal, Uganda and Yemen), domestic resource mobilisation needed to be complemented with additional foreign aid in order to meet the costs.[15] While the timeline on post-2015 may be longer, the situation will probably similarly vary from country to country.

There are a number of newly emerging possible sources of development finance, illustrated in Table 1. Of these, domestic resource mobilisation arguably best combines revenue potential with political feasibility.

Tax revenues as a share of GDP[11]



Source: IMF staff estimates
Note: Group medians and dynamic income groups

"Aggressive tax avoidance is a serious cancer eating into the fiscal base of many countries"
Pravin Gordhan, Finance Minister, South Africa.[2]

Table 1 - Emerging sources of development finance

Source	Magnitude	Comments
Private foundations	US$22 billion a year (2009)[16]	Increase of over 100% since 2000. Innovative. Some concerns about focus on 'low hanging fruit' and lack of democratic accountability.[17]
South-south development co-operation	US$15 billion a year[18]	Much has taken the form of technical co-operation and infrastructure investment.
Public money leveraging private	€519 million (US$675 million) estimated to leverage concessional loans of €9.56 billion (US$12.42 billion).[19]	Investment may not be additional; development benefits may be unclear; transparency often lacking; low level of support to developing country companies.[20] May attract investment where return insufficient without leverage, but range of suitable projects narrow.
Financial transaction tax (FTT)	FTT of 0.1% in 11 EU countries will raise estimated annual €74billion (US$96.7 billion).[21]	EU FTT could provide model for others. Important to ensure some of the revenue funds development. Political challenge to reach global FTT.
Special drawing rights (SDR)	Future SDR issue could allocate SDR100 -160 billion to developing countries[22]	IMF reserve asset. Could free up resources for development. Most applicable to countries with current account surplus. Would require change in IMF articles of agreement; politically challenging.
Aid (ODA)	US$133 billion in 2011	A critical source of development finance for the next generation at least, especially for fragile states, but levels not currently rising as they did through the 2000s.
Domestic resource mobilisation	Average additional US$66 billion per year over last 10 years.[23]	A source of finance that can deliver the required volume of finance, and may contribute to the post - 2015 agenda in other ways as well. Conducive political environment.

The potential of tax in the post-2015 agenda[29]

Making tax a greater source of development finance would require action from all countries to ensure that the global rules of taxation work more fairly, predictably and clearly, and are better enforced. Another part of the picture would be measures for developing countries to increase the amount of tax they are able to raise from wealthy domestic taxpayers. Together, policy changes along these lines could increase the proportion of income that developing countries raise in tax by a wide margin.

Tax and tax avoidance in the spotlight

Tax and tax avoidance has received extensive political and public attention recently – although concern about it is not new. For example, in 2009 South African Finance Minister Pravin Gordhan said that aggressive tax avoidance was "a serious cancer eating into the fiscal base of many countries."[30] Reports to the G20 from consortia of international organisations have set out innovative potential policy changes;[31] the UN has produced a practical manual on transfer pricing;[32] the IMF has set up a trust fund to finance development of tax systems;[33] and new regional tax cooperation bodies, including the Africa Tax Administration Forum (ATAF), have come into being.[34] Political pressure has led northern politicians to promise clampdowns on tax havens and tax avoidance.[35] The Economist says "Indignation has been greatest in Europe... various governments have rushed out anti-avoidance 'action plans' and general anti-abuse rules...the political heat has risen in America, too."[36] While only a few years ago legal tax avoidance was accepted as a way to conduct business, the climate is so utterly different today that the OECD has recently published a report starting with the premise that the international tax system needs an overhaul because of tax avoidance.[37] Timing is everything in politics, and there may never be a better time than now to radically overhaul the global tax system.

Finance potential

Tax has the potential to be a major finance source post 2015. In some developing countries, tax revenues have already increased faster than growth.[38] Nonetheless tax/GDP ratios remain low, on average 13% in low-income countries and around 18% in lower-middle income (compared with about 35% in high-income countries).[39]

These averages mask the fact that there have been great improvements in tax take in some countries while others have stagnated. Between 2002 and 2009, those low- and lower-middle income countries that have improved their tax/GDP ratios have done so by, on average, just over 3% of GDP, or 0.44% per year.[40] Furthermore, improvements in tax takes have been seen at every level of tax/GDP ratio, suggesting that for the low- and lower-middle income countries, no ceiling of improvement has been reached. This gives an idea of the potential of tax based on past performance; it would be even more with greater policy focus and effort. The IMF points out that "effort"[41] is not low in all developing countries, but that significant additional revenue could be raised where performance is weakest."[42]

The idea of tax as a source of development finance is hardly new. It played a significant role in the 2002 Monterrey Financing for Development report. Domestic resource mobilisation is already the largest source of development finance. Apart from a handful of the very poorest countries, developing countries already mobilise their own resources to finance the majority of their government spending.[43]

But while tax has many advantages it is not a silver bullet. For some of the poorest and some conflict-affected or conflict-emergent countries, tax may hold little short-term potential, and aid alone is still the most relevant financing option.

"Taxation is key to increasing our legitimacy and ability to make our own decisions."
Mary Baine, Commissioner General, Rwanda Revenue Service[3]

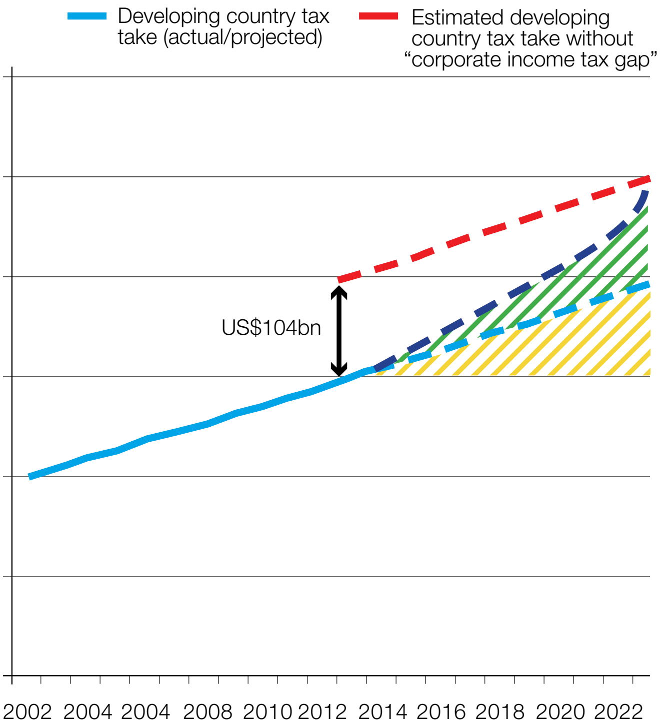
Why tax is the most promising development finance option

Thoughtful, smart approaches to taxation could have a plethora of developmental impacts within the post-2015 agenda.

Domestic resource mobilisation is a feasible way to raise a lot of finance

As we saw in the above two sections, it is possible to raise major sums of development finance through tax; indeed, this may be the most realistic and feasible way to complement aid to the necessary extent to fund the post-2015 agenda. Tax may fund universal public services, adaptation to climate change, social security, or whatever post-2015 priorities emerge.

Additional potential revenues from closing the corporate tax gap



The average annual increase in developing country tax take in the last decade, where an increase has taken place, is 0.44% of GDP. If this rise continues, it will already lead to significant revenue growth (yellow-shading) over coming years.

Specific action on closing the 'corporate tax gap' would raise additional revenues. We estimate that the typical 'corporate tax gap' in developing countries (the difference between actual tax collected and expected tax collected), due to tax avoidance and evasion, is around 20%.[44] At current developing country tax levels, this is some US$104 billion annually. Closing this gap over 10 years could raise some US$520bn additional revenue by 2022.

Accountable and transparent governance goes hand-in-hand with taxation

Development of a sound tax system fosters accountability between citizens and government, via development of the social contract, and thereby encourages better governance. To raise taxes, governments need to bargain and negotiate with the population (including all potential taxpayers) and must put considerable organisational and political effort into doing so.[45] This fosters accountability of government to citizens, an essential dimension of development that is lacking in many countries.[46] The Head of the Uganda Revenue Authority, Allen Kagira, has said: "We should elevate ourselves from being just tax collectors and administrators to being state builders."[47]

This strengthening of the social contract requires transparency in both the revenue and the spending side of national budgets; the public is likely to comply with taxation demands where spending has clear public benefit and where this is verified. Fiscal transparency can thus support revenue raising efforts, as well as being a cornerstone of tackling corruption, including through enabling civil society to play its core role as a watchdog. National-level fiscal transparency also dovetails with efforts to tackle tax avoidance and tax havens at the global level.

Predictability and level playing field for business

Clearer and better enforced international tax rules and domestic tax systems would provide a more predictable and sustainable environment for business; predictability is amongst the most important requirements for many businesses in developing and emerging economies. For example, more efficient and transparent rules-based transfer pricing administration would be good for everyone, because outcomes would be more stable and predictable, and because transaction costs would be lower. Moreover, enlightened businesses recognise that their contribution to public spending in investee countries through tax revenues will ultimately lead to a more stable business environment, and more opportunities for them in those countries.

Critically, smaller domestic businesses are also put at a disadvantage if multinational companies are able to secure reduced tax rates and/or engage in tax avoidance schemes. As the UK finance minister George Osborne says, “some [large multinationals] are exploiting the rules by getting profits out of high tax countries and into tax havens, allowing them to pay as little as 5% in corporate taxes while smaller businesses are paying up to 30%.”[49] Tackling this issue is important in order to level the playing field, making smaller domestic businesses more competitive.

Developing countries in the driving seat of their own development

An increased role for taxation in funding development would both afford developing countries greater autonomy in the setting of policy priorities and increase accountability between government and citizens, likely encouraging more interest in forging an agreed national definition of development priorities. Although the role of aid remains crucial, in the longer term increased taxation would mean aid would represent a smaller part of the financing pie. This would make any reductions in aid – or potential reductions in aid - less damaging. An early meeting of the African Tax Administrators Forum (ATAF) stated: “One of the most pressing issues facing our continent is to embark on a path to free African countries from their dependence on foreign assistance and indebtedness. An indispensable condition of this is the strengthening of our capacity to mobilise domestic resources.”[50] It will however be important for a new financing framework to commit to maintaining actual aid levels going forward, even if the proportion of financing from aid falls.

Inclusive, equitable growth

Where public services and infrastructure are at suboptimal levels (as is the case in most developing countries) increasing taxation may be used to boost growth, by providing the means to fill these gaps. Lower tax rates are often offered in the belief that countries need to remain ‘competitive’ in order to attract foreign direct investment. And yet, in fact, investment decisions are largely based on factors such as market potential, and the availability of relevant skills and infrastructure, with levels of taxation and tax incentives playing only a minor role.[50]

Tax can be a means of redistribution at the global, national and subnational levels, both geographically and between social groups; this is necessary to ensure that growth translates into poverty reduction, as part of a broader agenda of tackling inequalities. Progressive taxation can directly reduce inequality of income and other inequalities, including between women and men and between social groups. The way in which public revenues are spent can also have a net redistributive impact, for example through improving education, supporting women smallholder famers, providing services to reduce women’s unpaid care work, running sustainable social protection systems – and in many other ways.

This central role of taxation is already being discussed by the UN post-2015 inequalities Thematic Consultation advisory group. The leading Indian economic thinker Jayati Ghosh attending the Copenhagen inequalities meeting writes, “Where are

"[Multinationals' tax avoidance] strategies, though technically legal, erode the tax base of many countries and threaten the stability of the international tax system."
Angel Gurria, Secretary General, OECD[4]

the resources for such desirable policies [to reduce inequalities] to come from? Fiscal policies were explicitly under consideration, particularly tax policies that seek to improve collection from sectors and agents that have benefited disproportionately from aggregate income growth. Many leaders talked about tax strategies – not just higher tax rates, but better and more effective implementation of existing tax laws and closing tax loopholes. This clearly requires international co-ordination."[52]

Financing global public goods

It is worth mentioning also that global fiscal mechanisms such as financial transaction taxes may prove the most feasible method of funding increasingly important global public goods.

The benefits of international tax cooperation: tax justice for Timor Leste

Timor Leste has been engaged for almost a decade in a struggle to access the books, held in Australia, of some Australian companies that have profited from Timor Leste's offshore oil and gas deposits since 2004. The Timorese government was unable to audit the expenditures and deductions that companies were claiming to reduce their taxable profits in Timor Leste. In 2010 an arrangement with Australia's Taxation Office reportedly enabled the Timorese government to recover US$362 million in taxes due from Australian companies, equivalent to nearly four times the country's annual health spending. On the basis of their findings, the government says it is now reviewing expenditure deductions in other oil companies that may net a further US$3 billion in revenue. And Australia's public purse may ultimately benefit too: the Australian National Audit Office is now reportedly examining the accuracy of taxes and royalties declared by companies operating in the Timor Sea.[53]

Global partnership to increase tax revenue

Enabling increases in developing countries' tax revenue should be a central part of the post-2015 global partnership for development. This will require changing the rules and standards governing international tax co-operation, and supporting efforts by developing countries to strengthen tax administrations.

1 Measures to support domestic resource mobilisation

a Improving tax collection efficiency

Improvements to tax administration (such as reorganising revenue authorities and creating Large Taxpayer Units) can reap dividends; at least one experienced commentator considers the sustained work of implementing 'plain vanilla' taxes to be crucial.[54] Taxpayer education is another key element, in countries where tax morale is low or wide participation in the tax system relatively new. However, while reform of tax administration is often necessary, it is not the only way to improve tax take. On its own, tax collection improvements will not adequately tackle tax evasion and avoidance.

b Raising revenue levels through changes to domestic tax policy

Taxing in different ways – changing tax policy – can also very effectively increase tax take. However there is no universal blueprint. The best mix of policies will always be domestically owned, and will differ markedly from country to country.

The received wisdom in this area – to broaden the tax base, reduce rates and replace trade taxes lost during liberalisation with other indirect taxes – pays inadequate attention to the impacts of taxation on inequality. The UNDP says that, "progressive taxes are needed to avoid heavy burdens on goods and services that the poor consume disproportionately."[55] A commitment to progressivity may prioritise direct income taxes, and perhaps wealth taxes. Though it is worth noting that all taxes can be made more or less progressive. For example VAT (which has a regressive reputation) can be either regressive or progressive, from both income and gender perspectives,[56] if it is accompanied by a progressive system of exemptions for essential items. Sometimes indirect taxes may raise more revenue for pro-poor public spending more quickly than direct taxes. Distributional analysis, as well as revenue potential analysis, is crucial to inform tax policy changes.

As well as affecting tax paid by domestic taxpayers, developing country domestic tax policy changes may also increase revenue from foreign investors. For example, countries may decide to reduce tax incentives to investors, which in some countries amount to up to 5% of GDP – a huge revenue loss. Yet the evidence is that tax incentives often have little impact on investment decisions.[57] Countries may also seek to reduce tax avoidance and abuse through better regulation around transfer pricing, or direct anti-avoidance measures. This area of policy is a crucially important interface between the domestic and international areas of tax policy discussion.

2 Changes to international tax rules

International tax policy is a crucial lever for increasing the finance available for development, because much tax evasion and avoidance takes place across borders. Wealthy individuals and multinational companies shift money around the world exploiting legal loopholes to avoid tax, and also evade taxes by leveraging the secrecy provided by tax havens.

The OECD has said that developing countries lose up to three times as much money to tax havens as they receive in aid.[60] The Tax Justice Network estimates that US$21–32 trillion in financial wealth is being hidden by rich individuals in tax havens.[61] If the income generated by this wealth were taxed at 30% (a typical rate for developing countries), it could generate revenues of US$190–280 billion a year. Changing the rules and standards around global taxation could yield significant revenues for developing and developed countries. It may be particularly important for developing countries – as UK Chancellor George Osborne has acknowledged, "often the poorer a nation is, the more it needs the tax revenues, but also the weaker its capacity to tackle tax avoidance."

The out-of-date international taxation framework needs review, with respect both to how taxing rights are shared between states, and to their enforcement. The OECD itself, the most influential international tax standard-setting body, now acknowledges that a clampdown on tax avoidance is overdue – "the international common principles drawn from national experience to share tax jurisdiction may not have kept pace with the changing business environment."[62]

African co-operation against tax avoidance and evasion

In December 2010, ActionAid estimated that multinational brewer SABMiller was avoiding £20 million annually in tax payments to African and South Asian countries, using a range of tax avoidance techniques. This caught the attention of tax officials across Africa and further afield. In June 2011, a number of tax authorities from African countries featured in the report met in South Africa, intending to consider its findings. For legal reasons, the participants were barred from discussing some of the crucial specifics of SABMiller's taxpayer records. To surmount this, ATAF has facilitated the development of a new multilateral tax information-sharing treaty. This treaty will allow African countries to work together to investigate the tax affairs of multinational companies operating across the continent.[58] The Economist commented, "Galvanised by the SABMiller case, tax authorities in emerging markets are starting to push back against the multinationals, setting up cross-border bodies to share expertise."[59]

It may also be possible and desirable to propose within the post-2015 framework that rule changes might enhance international redistribution of the corporate tax base, from developed to developing countries. The UN Tax Committee has been working on such rule changes for some years, but its standards are often displaced by competing OECD standards more favourable to developed countries. Ensuring that international tax agreements with developing countries – whether bilateral or multilateral – permit those countries to tax cross-border capital and income arising in their jurisdictions, would have two impacts: it would both protect (and even privilege) poorer capital-importing countries' taxing rights, where those countries choose to do so; and would enhance protection against income-shifting into low-tax jurisdictions, and other forms of tax avoidance. The revenue losses - and opportunities for tax avoidance - generated by international tax agreements that fail to protect source taxation are illustrated by 'treaty-shopping' identified by ActionAid's investigation of one UK-headed multinational.

Protecting source taxation in developing countries

Taxing payments to non-residents of interest, dividends, fees and royalties is an important way for developing countries (and many developed countries) to tax a share of cross-border income. In some cases, developing countries choose voluntarily to reduce these taxing rights in bilateral tax treaties, principally to incentivise foreign investment. But giving up such rights altogether in one bilateral treaty can act as a loophole exploited by taxpayers with no real link to, or investment from, the country in question.

Ordinarily Zambia, like many other countries, withholds a 20% tax on cross-border management fees and interest income. Zambia earmarks some of this withheld tax specifically for government development programmes – helping to fund Zambia's own fight against poverty. Almost uniquely, however, the bilateral tax treaty signed back in 1971 between Zambia and Ireland denies Zambia any right to tax such payments.

ActionAid's investigation of the UK-headed multinational Associated British Foods found that substantial management fees, and interest payments on foreign bank loans to ABF's Zambian sugar operation, Zambia Sugar, are being routed through a special subsidiary registered in Dublin.

This Irish subsidiary appears to have no real office or activities in Ireland itself. Management services are apparently being provided from South Africa and elsewhere; while interest on the bank loans is returning to the UK branches of the banks that originally lent the money. Routing Zambia Sugar's payments via Ireland – at least on paper - has seen Zambia lose millions of dollars in foregone tax.[63]

Zambia is one of Ireland's nine 'development partners' and a major recipient of Irish overseas aid. Yet we estimate that since 2007, this single company's 'treaty shopping' transactions via Ireland may have deprived the Zambian government of revenues equivalent to one in every 14 Euros of Irish development aid to Zambia.

The OECD has proposed some measures to stop 'treaty-shopping', but abuse continues.[64] More fundamentally, some developing countries have started to renegotiate or even cancel loophole-ridden tax treaties where they are suffering 'treaty shopping' abuse: Indonesia cancelled its tax treaty with Mauritius for precisely this reason in 2004; and Argentina with Switzerland in 2012. Mongolia cancelled its tax treaties with the Netherlands in 2012, and is considering ending treaties with Luxembourg, Kuwait and the UAE.

Beyond changes to the international tax rules, there is still an urgent need to remove both the opacity of tax havens and internationally-harmful tax regimes. As well as playing their part in facilitating tax avoidance by multinationals, these jurisdictions facilitate tax evasion by companies and wealthy individuals. One avenue of reform would be to strengthen arrangements for information exchange between tax authorities in different countries, but it would need to move much further and faster than the current process started by the G20 in April 2009;[66] the report by a consortium of international organisations to the G20 Development Working Group in November 2011 contains many very useful proposals.[67]

Finally, the interdependence of the international tax system means that changes to the tax rules of one country can have inadvertent impacts (which may be positive or negative) on others. To ensure clarity on this kind of impact, and the potential to mitigate negative impacts, the IMF, OECD, UN and World Bank has recommended that 'spillover analyses' of all such changes should be conducted by developed countries.[68]

Options for the post-2015 framework

Tax has enormous potential to raise much of the development finance – potentially US$1.25 trillion over the next decade which is additional to and complementing aid – that will be needed to implement the post-2015 framework; it may also support parts of the framework directly, for example, in stimulating pro-poor growth.

In the context of the discussions being held in Bali in March 2013 on the global partnership for development, this will require first and foremost a global commitment to changing international tax rules to prevent avoidance and evasion, and protect developing-countries taxing rights. This will mean changing international standards, for example, to:

- ensure that international treaties and agreements safeguard developing countries' taxing rights on cross-border income and capital
- increase transparency including in tax havens and in companies themselves
- support countries in building regional agreements to address tax competition and excessive tax incentives.

Both the legal and informational tools provided by the reforms to international standards suggested above, and capacity to use these tools, will be required. Alongside these global efforts, therefore, the post – 2015 framework can provide complementary support for capacity building for developing country tax authorities.

Ideally, the post-2015 framework would enable progress towards reaching a universal domestic resource 'floor' consisting of, for example:

- a narrowing of the corporate tax gap in developing countries – potentially leading to a 20% increase on the current corporate tax take.[69]
- An increase in overall developing country tax take overall as a proportion of GDP, potentially reaching a tax/GDP ratio of 25%, for example (an ambitious but progressive target).

1 Interview with ABC News, 14 September 2009, http://www.abc.net.au/sundayprofile/stories/2684786.htm

2 Vanessa Houlder, 'Tax officials on trail of wealth hidden offshore', Financial Times, 30 May 2009

3 ActionAid interview, Kigali, Rwanda, July 2009

4 http://economia.icaew.com/news/february2013/oecd-urges-avoidance-overhaul

5 20% is an ActionAid estimate of MNC corporate tax gap in developing countries; see also European Commission and PriceWaterhouse Coopers (2012), Transfer pricing and developing countries – final report

6 Montero, WM (2012), Practice and legislation in transfer pricing, presentation at Tax Justice Network seminar on transfer pricing, Helsinki, 13-15 June 2012

7 UN MDG Gap Task Force (2012), The global partnership for development: making rhetoric a reality

8 Green D, Hale S and Lockwood M (2012), How can a post-2015 agreement drive real change? The political economy of global commitments, Oxfam Discussion Papers

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