

Taxation



WHY IS INTERNATIONAL CO-OPERATION IMPORTANT FOR DEVELOPMENT?

Taxation is key to promoting sustainable growth and poverty reduction. It provides developing countries with a stable and predictable fiscal environment to promote growth and to finance their development needs. Combined with economic growth, it reduces long-term reliance on aid. Its key role in mobilising domestic resources was re-affirmed at the Seoul G20 Summit. It is closely linked to other areas of economic governance covered in this report: tax havens and lack of transparency in reporting of profits and tax payments paid in resource-rich developing countries are linked to corruption, financial crime, money laundering, and illicit financial flows. These issues are in turn linked to illicit trade in arms, conflict and fragility. Taxation also plays a key role in ensuring good governance by promoting the accountability of government to citizens.

Much needs to be done by countries themselves, working nation-

ally and regionally through organisations such as the African Tax Administration Forum (ATAF), to improve administrative capacity, broaden the tax base, and increase tax revenue as a proportion of GDP – whilst striking the right balance between an attractive tax regime for investment and growth, and securing the necessary revenues for public spending.

At the same time, international co-operation is essential in the following key areas:

- improving the capacity of tax administrations in developing countries;
- tackling the problem of offshore non-compliance;
- ensuring the consistent application of international standards on transfer pricing;
- optimising transparency in reporting by multinational enterprises (MNEs) in order to help ensure their full compliance with developing country tax regimes.

WHERE ARE WE NOW AND WHAT NEEDS TO HAPPEN NEXT?

(i) Raising capacity in tax administrations

Most of the tax challenges above are faced both by developing and developed countries but their impact is much larger where administrative capacity and compliance habits are weak • which is an unfortunate reality for many developing countries. Many, though not all, low income countries have tax administrations which may be plagued by corruption; have poorly trained and underpaid officials; use antiquated administrative structures; and suffer from weak risk management and poorly articulated strategic goals.

A tax system is only as good as its administration. Improving revenue administration is essential for enhanced and fairer revenue mobilisation, and for wider governance improvement. Working with key regional initiatives such as ATAF helps to put control of the developmental agenda firmly in the hands of developing countries themselves.

The next steps include:

- the Task Force on Tax and Development will provide a report on how less developed countries can improve the capacity of tax administrations, which will be fed into the G20 Working Group on Development.
- strengthening direct support for revenue and customs sectors which up to now has attracted a minimal share of aid; contributing to changing donor perspectives to view funding of tax systems as vital to the future of developing countries.

(ii) Tackling offshore non-compliance

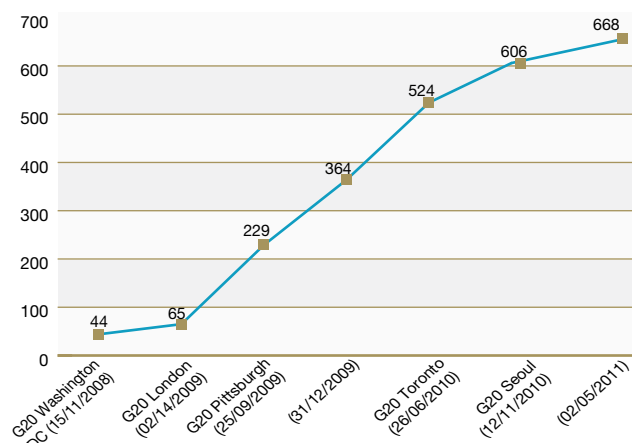
Estimates of the revenue loss to developing countries as a consequence of offshore non-compliance vary greatly, but most exceed by some distance the level of official development assistance

- around USD 120 billion annually. Improving the exchange of information helps authorities to tackle the problem.

The economic crisis and recent cross-border tax evasion scandals have heightened the political drive to ensure rapid implementation of the OECD's tax transparency and information exchange standards, through the OECD-hosted Global Forum. These require the exchange of information on all tax matters requested by jurisdictions on the basis of international tax agreements. All of the 97 countries covered by the Global Forum have now committed to the Forum's standards of tax information exchange and transparency. More than 600 agreements have been signed since April 2009 and many more are under negotiation. Eighteen peer reviews of jurisdictions' implementation of the standards for

More progress on exchange of tax information in past couple of years than in all of the previous decade

Tax Information Exchange Agreements (TIEAs)/ Double Tax Conventions (DTCs) Signed between G20 Summits



Source: OECD, Centre for Tax Policy and Administration, April 2011.

transparency and exchange of information have been finalised. The Forum is expected to deliver up to 40 reviews each year and 60 by the 2011 G20 Summit. The Seoul G20 communiqué asked the Global Forum to swiftly progress the reviews and report progress to the 2011 Summit.

The next steps include:

- implementation in all jurisdictions of the agreed standards on transparency and exchange of information; and prompt action to address any weaknesses identified in the peer review process;
- support to help developing countries benefit from a more transparent and co-operative tax environment, including the development of the necessary capacity in domestic tax policy and administration.

(iii) Ensuring consistent application of international standards on transfer pricing

International transfer pricing standards determine the 'price' to be paid in respect of transactions between different taxable entities which are part of the same MNE, thus determining the tax that should be paid in each jurisdiction. The incomplete and inconsistent application of international standards on transfer pricing, inadequate legislation, or a lack of basic tax capacity in developing countries can mean that transfer prices used by MNEs may depart from the arm's length standard and lead to profits being shifted to low-tax jurisdictions, resulting in lower revenue for normal-rate jurisdictions, including developing countries. A structured dialogue with developing countries on capacities in policy and technical areas, including developing administrative frameworks for an efficient, effective, and fair implementation of transfer pricing regimes, is underway in a joint DAC/CFA initiative on "tax and development" with support from the G20.

The next step are:

- opening of dialogue and development of guidance to assist countries in the development and enforcement of transfer pricing legislation in accordance with individual country needs and priorities, including providing model legislation.
- creating an inclusive Global Forum on Transfer Pricing for developed and developing countries.

(iv) Optimising transparency in MNE reporting

This is the subject of active political debate in many countries, and between non-governmental organisations (NGOs) and business. To improve tax transparency and compliance in developing countries, NGOs have proposed that MNEs provide detailed reports on a country-by-country basis in annual financial statements. These

would include, for example, a disclosure of the countries in which MNEs operate and the financial performance of each, indentifying both third-party and intra-group trade, labour-related information, and pre-tax profits as well as taxes paid. Proponents suggest that country-by-country reporting would discourage profit shifting, reduce corruption, increase corporate social responsibility and facilitate corporate governance. Critics dispute the benefits and point to the potentially heavy compliance burden and the increased costs of auditing and reporting which would be incurred by MNEs.

The next step is:

- objective technical appraisal of the pros and cons of introducing country-by-country reporting, which may extend beyond tax matters into broader issues of disclosure.

HOW CAN THE OECD, WORKING WITH OTHER INTERNATIONAL ORGANISATIONS, HELP TO ACHIEVE THIS?

The OECD has been working on the issues of transparency and exchange of information for over 15 years. The OECD-hosted Global Forum on Transparency and Exchange of Information for Tax Purposes is the multilateral framework within which work in the area of transparency and exchange of information has been carried out by both the OECD and non-OECD economies since 2000. One hundred and one countries have joined the Forum, which has launched a two-phase peer review process applying to all members and also partner countries on the implementation of standards on transparency and exchange of information. An informal Tax and Development Task Force, including developing countries, NGOs, business, and international organisations, was established in January 2010 to support the leading work of the Global Forum and ensure that developing countries benefit fully from increased transparency through tax information exchange.

The OECD also produces internationally comparable statistics and monitors and assesses national tax policies and systems. It helps to share good practices and develop administrative capacity, through multilateral mechanisms such as the International Tax Dialogue.

It also undertakes work on tax evasion, harmful tax practices, and increasing transparency in MNE reporting through the MNE Guidelines, which encourage compliance with tax laws and regulations. The OECD will contribute to these priorities as follows:

(i) Raising capacity in tax administrations

Enhancing co-operation between the African Tax Administration Forum and the Forum on Tax Administration to strengthen the linkage between taxation, accountability of governments to their citizens and state building. A report by the Task Force on Tax and Development on these issues, and the linkage between tax and aid, will be available by the end of 2011.

(ii) Tackling offshore non-compliance

Swiftly progressing the Global Forum's peer review process, helping developing countries to benefit from increased transparency, including by helping to set up exchange of information agreements and administrative structures to implement them.

(iii) Ensuring consistent application of international standards on transfer pricing

Broadening the scope of the OECD's work to help developing countries apply international transfer pricing standards and guidelines to protect their tax bases, whilst providing an investment-friendly environment. A series of dialogue events on OECD standards and guidance will be delivered for developing countries; those in Africa will take place under the auspices of the ATAF.

(iv) Optimising transparency in MNE reporting

The OECD's Investment Committee is working with its numerous non-OECD partners and stakeholders to update the Guidelines for MNEs during 2011, including whether these should be revised to address country-by-country reporting and whether the matter is limited to taxation or if a broader approach to disclosure is required. The OECD's Tax and Development Task Force will support the OECD's Committee on Fiscal Affairs to undertake an objective technical appraisal of this issue.



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