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VIEWPOINT PAPER

Benefits and Costs of the IFF Targets for the Post-2015 Development Agenda

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Post-2015 Consensus

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Introduction

The purpose of the paper was to analyse the targets aimed at reducing illicit financial flows and tax evasion as well as increasing stolen asset recovery that were proposed by the UN High Level Panel on the Post-2015 Development. The author posits that the recommended targets are unlikely to be adequate due to doubts over exact volumes involved and the lack of clear lines of accountability to identify policy obligation. The author offers alternative targets and using obtainable data, suggests that these are feasible in presenting high ratios of benefit to cost.[1]

This View Point paper attempts to outline the complications involved in implementing the alternative targets proposed by the author and points out how greater inclusion and dialogue between South CSOs, the private sector, OECD and non-OECD governments will help correct the deficits, and in doing so, also provides additional perspectives that have been overlooked by the author.

Comments

The paper begins with a wholesome contextual description of Illicit Financial Flows (IFFs) and its impacts to the economy and inequality. The publication, however, misses a crucial definition on Beneficial Ownership in the same way IFFs have been delineated in great detail. A universally acceptable understanding of the concept would have been useful if the zero target (to reduce the legal persons and arrangements for which beneficial ownership info is not publicly available) is to be achievable under Post-2015. For example, a commentary on OECD Model tax convention laments:

> "Beneficial Ownership has been introduced in the OECD -model treaty to try to eliminate the avoidance of (withholding) taxes in especially structured transactions. However, only in the domestic tax laws of just a few countries, the term Beneficial Ownership (or a similar local definition achieving the same) has been defined. In most countries the term Beneficial Ownership did not even exist in domestic (tax) legislation. In the countries which had a definition of Beneficial Ownership this definition stems from its local trust laws (mostly in common law countries)."[2]

The Committee of Experts on International Cooperation in Tax Matters discusses the concept of Beneficial Ownership and its various interpretations.[3]

The paper offers a stylised representation of major IFF types. A brief explanation of the structural factors that create the environment for IFFs would have been helpful to situate the proposed targets in terms of how they will deal with the problem. A UNDP publication

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[1] For a full description of the UN Proposed targets and those suggested by the author, see: Post-2015 Consensus: Illicit Financial Flows Alex Cobham, April 2014
[2] Commentary on: OECD Model tax convention: Revised proposals concerning the meaning of "Beneficial Owner" in articles 10, 11 and 12 Source: http://www.oecd.org/ctp/treaties/BENOWNMLL_vanBladel.pdf
[3] Concept of Beneficial Ownership: Discussion of Key Issues and Proposals for Changes to the UN Model Commentary. Source: http://www.un.org/esa/ffd/tax/sixthsession/BeneficialOwnership.pdf

on 'Illicit Financial Flows from the Least Developed Countries: 1990-2008,' details the drivers and dynamics of IFFs including the structural issues.[4] These include rising trade openness devoid of oversight and regulation and the existence of an underground economy and political instability.

Together with the proceeds from tax evasion, IFFs also typically involve earnings from criminal activities. The paper could have presented more clarity on how the proposed alternative targets for universal beneficial ownership, automatic exchange of tax information and country-by-country reporting can help curb the problem in context of trafficking of drugs and humans and poaching. Focus area 17 on Ecosystems and biodiversity of the proposed by the co-chairs in February 2014 references the need to stop poaching and trafficking of endangered species.[5] Since country in- and outflows of money make possible the financing of such illegal activities and sometimes these funds make their way to the hands of public officials, corrupting governments, this should be elaborated more and anti-money-laundering considerations should also be fleshed out in greater detail in the document.

The paper overlooks the importance of building a business case to support the alternative targets. The targets for universal beneficial ownership, automatic exchange of tax information and country-by-country reporting are likely to be resisted by MNCs although the author cites a recent PwC poll of business leaders that found 59% in favour of publication of information generated by multinationals' country-by-country reporting. There is growing discourse, however, of the importance of corporations going beyond embracing transparency as a compliance issue and taking it as a strategic imperative. It is worthwhile, hence, to outline these benefits in the literature to quell any fears from individuals sympathetic towards businesses within the Post-2015 discussions.

Besides, the private sector's buy-in is crucial if these proposed targets are to be achieved. Elaine Dezenski, of the World Economic Forum's Partnering Against Corruption Initiative is an example of those making a business case for transparency.[6] It is worth noting in the paper, moreover, that some MNCs are already leading the way with reporting payments they make in countries they operate. For instance, Tullow Oil recently captured headlines by becoming the first oil company to disclose its payments to foreign governments on a country-by-country and project-by-project basis.[7] Similarly, although the American Petroleum Institute (API) filed a lawsuit and won against the US Securities and Exchange Commission (SEC) regarding its plans to enforce Section 1504 of the Dodd Frank Wall

[4] Illicit Financial Flows from the Least Developed Countries: 1990-2008: http://www.gfintegrity.org/wp-content/uploads/2014/05/IFFs_from_LDCs_web.pdf
[5] http://sustainabledevelopment.un.org/content/documents/3276focusareas.pdf
[6] The Business Case for Fighting Corruption. Source: https://blog.transparency.org/2012/09/24/the-business-case-for-fighting-corruption/
[7] Tullow steps up transparency in reporting: http://www.ft.com/intl/cms/s/0/67ed17c8-b12f-11e3-9548-00144feab7de.html#axzz35TGlKb96

Street Reform Act (2010) which compels project-level disclosure for oil companies, one of its members, Norwegian state-owned oil company Statoil, withheld its support from it.[8]
This brings us to the importance of a multi-stakeholder platform to monitor progress towards and ultimately help meet these targets suggested by the author. Initiatives that involve businesses, governments and civil society bring together the expertise from different perspectives and are crucial in the emergence of common solutions to complex problems such as this concerning IFFs. For instance, the Kimberley Process (KP) is a joint initiative involving governments, businesses and civil society to curtail the flow of conflict diamonds (also known as blood diamonds) that help to finance rebel insurgencies and bids to overthrow legitimate governments.[9] The Extractive Industries Transparency Initiative (EITI) for transparency of transactions between governments and companies in the mining and oil industries,[10] and the Global Reporting Initiative (GRI) for comparable reporting on economic, ecological and social impacts of company activities.[11]

The document mentions that illicit outflows are substantially larger than Official Development Assistance (ODA). While this is true, some actual numbers might be helpful in painting a picture that reflects the real magnitude of IFFs. Developing nations desire to graduate from aid and hence these figures help bring the Post-2015 IFF debate from the perspective of the developing world. GFI estimates the ratio of IFFs out of developing countries in comparison to ODA at $1 of assistance to $10 lost in illicit outflows.[12]

Consequently, the literature survey in the document has missed the civil society dimension. Should they be adopted, the proposed alternative post-2015 targets will create a huge opportunity in helping reduce illicit financial flows but it would be useful to acknowledge that those at the frontline of making it work will be country-level CSOs. This is recognised by both politicians and CSOs in the developing world.[13]

Although very detailed, the section on discussing the costs and benefits of beneficial ownership disclosure, automatic tax information exchange and multinationals' country-by-country reporting does so from a northern perspective. To counterbalance, it would be worthwhile to consider the costs and benefits of, for example, the publication of registers of beneficial ownership of companies, trusts and foundations to developing countries. A consideration of the costs and benefits from a southern perspective will help pre-empt voices that there will be high implementation costs for governments of developing nations. Already, there is claim that African countries do not have the resources and capacity to set

[8] Norway's national oil company Statoil withholds support from US anti-transparency lawsuit: http://www.globalwitness.org/library/norway%E2%80%99s-national-oil-company-statoil-withholds-support-us-anti-transparency-lawsuit
[9] See Kimberley Process (KP) website for more information: http://www.kimberleyprocess.com
[10] EITI website: http://eiti.org/
[11] Global Reporting Initiative website: https://www.globalreporting.org
[12] Global Financial Integrity Mission Statement. Source: http://www.gfintegrity.org/?option=com_content&task=view&id=300&Itemid=99999999
[13] Civil society critical in monitoring illicit financial flows, Mbeki. Source: http://www.uneca.org/media-centre/stories/civil-society-critical-monitoring-illicit-financial-flows-mbeki#.U6gTbUA4T9o

up the relevant structures which will provide the required information.[14] . Similarly, when considering KPMG's Global Transfer Pricing Services professionals' recent claim that 'tax authority resources are not efficiently used when significant efforts are required to sort through large amounts of information,' and that provision of substantial amounts of information 'is costly to both MNEs and tax authorities,'[15] one has to assume that less resourced authorities will bear a heavier burden, warranting more investigation into this from a developing nation perspective.

The paper mentions the emergence of an 'early adopters' group that has begun the process to pilot the OECD Common Reporting Standard (CRS).[16] To be able to reach the target to 'reduce to zero the cross-border trade and investment relationships between jurisdictions for which there is no bilateral automatic exchange of tax information,' all countries will have to adopt the CRS or establish similar measures. The paper mentions that there are a few developing countries that have adopted it but neither gives the reader a glimpse of the proportion nor lists some of the countries. South Africa, for example, is part of this 'early adopters' group and the only African country.[17] This is important to demonstrate the scale of the task that lies ahead. This discussion on the CRS also offers opportunity to propose a way forward for regions like Africa, under the African Tax Administration Forum (ATAF), to create a similar framework. Indeed, last year the South African Finance Minister Pravin Gordhan was quoted as saying:

> "South Africa has been working with more than 28 fellow African nations through the African Tax Administration Forum (ATAF) to improve the efficacy of their tax legislation and administrations."[18]

Moreover, ATAF last year worked together with the OECD's Task Force on Tax and Development and published a " how to" Guide on Exchange of Information.[19] Descriptions of such developments portray a sense of inevitability with regards to CRS-like setups across the world. More information in the paper about what African tax administrations through ATAF and others like the Interamerican Center of Tax Administration (CIAT) are planning might have helped shed more light on the progress to-date.

[14] Global standard on exchange of tax information will help fight against tax evasion: http://www.fanews.co.za/article/tax/16/tax/1016/global-standard-on-exchange-of-tax-information-will-help-fight-against-tax-evasion/15871

[15] KPMG, 2014: Comments on the OECD Discussion Draft on Transfer Pricing Documentation and Country by Country Reporting: http://www.kpmg.com/Global/en/services/Tax/Global-Transfer-Pricing-Services/Documents/oecd-transfer-pricing-documentation-feb-2014.pdf

[16] On 13 February 2014, OECD released a common reporting standard (CRS) document aimed at creating an automatic exchange of tax information as the new international standard for tax authorities: http://www.oecd.org/ctp/exchange-of-tax-information/automatic-exchange-of-financial-account-information.htm

[17] Joint Statement by the Early Adopters Group, 19 March 2014: http://www.oecd.org/tax/transparency/AEOIjointstatement.pdf

[18] South Africa and UK agree to work together to tackle offshore tax evasion: https://www.gov.uk/government/news/south-africa-and-uk-agree-to-work-together-to-tackle-offshore-tax-evasion

[19] Practical Guide on Exchange of information for Developing Countries: http://www.oecd.org/ctp/tax-global/practical_guide_exchange_of_information.pdf

Staying with the OECD, as the organisation is leading this process to create a multilateral system for automatic exchange of information, it should make more efforts to include tax administrations that are not from its member countries. This will be crucial if these alternative targets are to be achieved. There is belief from the developing South, however, that the OECD is citing governance and capacity limitations of African countries as reason to limit their full participation from the beginning, as this could slow down the process.[20] The Financial Transparency Coalition (FTC) has echoed this by asserting that: 'the OECD has done little to dispel its reputation as the "rich men's club" by effectively ruling out the active participation of developing countries in shaping the tax reform agenda. Developing countries' communication channels with the OECD process are restricted to the UN, the Task Force on Tax and Development, and the OECD Global Relations Programme, which the OECD says will provide "useful insights" and a "useful platform" for "the particular concerns of developing countries."[21] FTC continues: 'Restricting developing country participation to these separate venues should not be confused for equal participation in the OECD's decision-making process.'

Future work could highlight some insights on how this conundrum can be reconciled because if Africans are not involved at the outset, the system will lack their input and the proposed targets will be hard to achieve without their buy-in. There is adequate indication, after all, that ATAF members are keen and open for collaboration. For instance, Oupa Magashula, the Commissioner of the South African Revenue Service and Chairperson of ATAF Council states:

> "While ATAF is driven by its African membership, the importance of its partnerships with other tax administrations, technical and development institutions cannot be overstated. The organization has developed its work program of strategic dialogue, research and capacity building to take advantage of, and build on the work of, full partnerships with these institutions.
>
> … through a shared vision of state building, governance and domestic resource mobilization, continuing interaction will assist both ATAF and its development partners to make Africa a better place for its people."

He also emphasizes the importance of working with MNCs and a multi-stakeholder approach:

> "I see a significant role for multinationals in providing assistance to ATAF by working with us collaboratively on the many initiatives that we will be pursuing. Furthermore, ATAF will also look into creating regular dialogue sessions between

[20] Structural Transformation and the Challenge of Financing Africa's Development Post-2015: a Narrative (pg 11): http://www.acordinternational.org/silo/files/structural-transformation-and-the-financing-challenges--johannesburg-reflections.pdf
[21] OECD BEPS report confirms the international tax system is failing rich and poor nations, FTC, 2013: http://www.financialtransparency.org/2013/07/19/oecd-beps-report-confirms-the-international-tax-system-is-failing-rich-and-poor-nations/

> heads of tax administrations and representatives of multinationals on issues of common concern."[22]

The paper also misses the opportunity to highlight what work the UN Tax Committee (UN TC) is doing with developing countries and whether or not it is coordinating countries to develop joint proposals on country-by-country reporting and beneficial ownership at the sub-regional level (eg East African Community). FTC advises that the UN TC be 'strengthened to participate more fully as representative of a broader group of countries.'23 This is particularly relevant in the context of Post-2015 discussions. For instance, "The United Nations' Role in International Tax Policy" provides an analytical view on the role of the UN and the work done in improving global tax cooperation[24] and is a document that gives context for those looking to examine the possibility of UN TC anchoring the implementation of these proposed alternative targets.

Conclusion

This View Point paper set to offer a summary of the potential pitfalls involved in implementing the alternative targets for reducing IFFs and tax evasion as well as increasing stolen asset recovery proposed by the author of 'Post-2015 Consensus: Illicit Financial Flows' and argues that greater inclusion and a multi-stakeholder approach to dialogue will help improve the applicability of the alternative targets proposed.

Hopefully the view point provides critiques that will be useful for future efforts to build upon enormous work thus far in the area of redressing the existing inequalities in the global financial system.

[22] Interview with Mr. Oupa Magashula Commissioner of the South African Revenue Service and Chairperson of the African Tax Administration Forum (ATAF) Council, Tax Policy and Controversy Briefing A quarterly review of global tax policy and controversy developments: http://www.ey.com/Publication/vwLUAssets/June_2010_Tax_policy_and_controversy_briefing/$FILE/TPC4_08June10.pdf

[23] FTC, 2013, ibid.

[24] The United Nations' Role in International Tax Policy: http://www.ngosonffd.org/wp-content/uploads/2010/11/UN-Role-in-International-Tax-Policy-2012.pdf

This paper was written by Semkae Kilonzo, Coordinator at Policy Forum. The project brings together more than 50 top economists, NGOs, international agencies and businesses to identify the goals with the greatest benefit-to-cost ratio for the next set of UN development goals.

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