# Supporting the Development of More Effective Tax Systems

A REPORT TO THE G-20 DEVELOPMENT WORKING GROUP BY THE IMF, OECD, UN AND WORLD BANK

# Supporting the Development of More Effective Tax Systems

A REPORT TO THE G-20 DEVELOPMENT WORKING GROUP
BY THE IMF, OECD, UN AND WORLD BANK

This report has been prepared by the organisations mandated at the G-20 Seoul Summit: the International Monetary Fund, the Organisation for Economic Co-operation and Development, the United Nations and the World Bank. These organisations have worked with regional organisations, such as the African Tax Administration Forum and the Inter-American Center of Tax Administrations, and its preparation has also benefitted from wide consultation with other organisations working in the tax area. There has also been extensive consultation with developing countries, Civil Society Organisations, academic and business representatives through their participation in meetings and discussions organised by the IMF and their participation in the Task Force on Tax and Development. The report is prepared under the responsibility of the Secretariats and Staff of the four mandated organisations. It reflects a broad consensus among these staff, but should not necessarily be regarded as the officially-endorsed views of those organisations or their member states.

# *Table of contents*

**Chapter 1. Overview and Recommendations for Action** ............................................ **7**

Background ..................................................................................................... 8
About this report ............................................................................................. 9
The challenges facing developing countries.................................................... 10
Moving forward .............................................................................................. 12

**Chapter 2. Key Capacity Contrainsts Faced by Developing Countries and Recommendations on Capacity Building** ................................................ **15**

Introduction ..................................................................................................... 16
Current situation.............................................................................................. 16
How the G-20 countries can better help developing countries' efforts ........................ 21
Summary of recommendations.......................................................................... 30

**Chapter 3. Identifying Ways to Help Developing Countries Tax Multinational Enterprises (MNEs) through Effective Transfer Pricing Rules** ............................... **31**

Introduction ..................................................................................................... 32
Current position............................................................................................... 32
Gaps and unmet needs....................................................................................... 34
Summary of recommendations.......................................................................... 35

**Chapter 4. Setting up Objective Measures to Track Progress in the Capacity Improvement of LIC'S Tax Administration Systems** ............................................... **37**

Current situation.............................................................................................. 38
Drawing the regional threads together ............................................................... 40
Summary of recommendations.......................................................................... 42

**Chapter 5. Developing a Knowledge Management Platform to Support the Tax Capacity of Developing Countries**................................................................. **43**

Overview ......................................................................................................... 44
Current situation.............................................................................................. 44
Access to TA information ................................................................................. 45
Wider south-south co-operation ......................................................................... 46
Knowledge management platforms.................................................................... 48
Gaps and unmet needs....................................................................................... 50
Summary of recommendations.......................................................................... 52

# *Abbreviations*

| | |
|---|---|
| **ADB** | Asian Development Bank |
| **AfDB** | African Development Bank |
| **ATAF** | African Tax Administration Forum |
| **ATAIC** | Association of Tax Authorities of Islamic Countries |
| **CAPTAC-DR** | Centro Regional de Asistencia Técnica de Centroamérica, Panamá y República Dominicana / Central America, Panama, and Dominican Republic Regional Technical Assistance Center |
| **CATA** | Commonwealth Association of Tax Administrators |
| **CIAT** | Centro Interamericano de Administraciones Tributarias / Inter-American Center of Tax Administrations |
| **CIT** | Corporate Income Tax |
| **CREDAF** | Centre de Rencontres et d'Études des Dirigeants des Administrations Fiscales |
| **CSO** | Civil Society Organisations |
| **DAC** | Development Assistance Committee |
| **DFID** | (UK Government) Department for International Development |
| **DRM** | Domestic Resource Mobilisation |
| **EC** | European Commission |
| **EITI** | Extractive Industries Transparency Initiative |
| **EU** | European Union |
| **FDI** | Foreign Direct Investment |
| **FTA** | Forum on Tax Administration |
| **G-20** | The Group of Twenty (G-20) Finance Ministers and Central Bank Governors |
| **GDP** | Gross Domestic Product |
| **GOVNET** | OECD/DAC Network on Governance |
| **GTSP** | World Bank's Global Tax Simplification Programme |
| **ICTD** | International Centre for Tax and Development |
| **IDB (also IADB)** | Inter-American Development Bank |
| **IFIs** | International Financial Institutions |
| **IMF** | International Monetary Fund |
| **IOTA** | Intra-European Organization of Tax Administrations |
| **IT** | Information Technology |

| | |
|---|---|
| **ITC** | International Tax Compact |
| **ITD** | International Tax Dialogue |
| **KM** | Knowledge Management |
| **LDCs** | Least-Developed Countries |
| **LICs** | Low Income Countries |
| **MDGs** | Millennium Development Goals |
| **MNEs** | Multinational Enterprises |
| **NGO** | Non-Governmental Organisation |
| **ODA** | Official Development Assistance |
| **OECD** | Organisation for Economic Co-operation and Development |
| **PEFA** | Public Expenditure and Financial Accountability |
| **PIT** | Personal Income Tax |
| **PITAA** | Pacific Islands Tax Administrators Association |
| **S4TP** | South-South Sharing of Successful Tax Practices |
| **SGATAR** | Study Group on Asian Tax Administration and Research |
| **SME** | Small and Medium Enterprises |
| **SSA** | Sub-Saharan Africa |
| **TA** | Technical Assistance |
| **UN** | United Nations |
| **UNDP** | United Nations Development Programme |
| **USAID** | United States Agency for International Development |
| **USD** | United States Dollar |
| **VAT** | Value-Added Tax |
| **WB** | World Bank |
| **WCO** | World Customs Organization |

# *Chapter 1*

# An Overview and Recommendations for Action

## Background

Taxation provides governments with the funds needed to invest in development, relieve poverty and deliver public services. It offers an antidote to aid dependence in developing countries and provides fiscal reliance and sustainability that is needed to promote growth. Tax system design is also closely linked to domestic and international investment decisions, including in terms of transparency and fairness. Strengthening domestic resource mobilisation is not just a question of raising revenue: it is also about designing a tax system that promotes inclusiveness, encourages good governance, matches society's views on appropriate income and wealth inequalities and promotes social justice.

Taxation is integral to strengthening the effective functioning of the state and to the social contract between governments and citizens. By encouraging dialogue between states and their citizens, the taxation process is central to more effective and accountable states. Reforms which begin in tax administration may spread to other parts of the public sector.

The Doha Declaration confirms the need to step up efforts to enhance tax collection, investment and other private flows, with a view to supporting pro-poor development. Yet half of sub Saharan African countries still mobilise less than 17% of their GDP in tax revenues, below the minimum level of 20% considered by the UN as necessary to achieve the Millennium Development Goals[1]. Several Asian and Latin American countries fare little better. In addition, many tax systems have little impact on reducing inequalities in income and wealth and only a small proportion of citizens are within the tax system. To help developing countries, the G-20, and the donor community, need to ensure that the assistance directed at tax system development is coherent and effective.

Moving towards simpler, more equitable and transparent tax systems and a broadening of the tax base has been a concern in many developing countries for many years, and the organisations preparing this report have been active in the area for decades. But it has recently taken on a higher political profile as the wider development community has increasingly recognised the centrality of taxation in development. This is an extremely welcome and important development.

[1] What Will It Take To Achieve the Millennium Development Goals? An International Assessment, UNDP, June 2010, page 26.

## About this report

This report responds to the G-20 request reproduced in the box below.

**Action 1: Support the Development of More Effective Tax Systems**

We ask the expanded OECD Task Force on Tax and Development, UN, IMF, World Bank and regional organisations such as the Inter-American Center for Tax Administration and African Tax Administration Forum and other relevant organisations to:

- Identify key capacity constraints faced by developing countries in their tax systems and make recommendations on capacity building to *(i)* improve efficiency and transparency of tax administrations and *(ii)* strengthen tax policies to broaden the tax base and combat tax avoidance and evasion (*June 2011*);
- Develop a knowledge management platform and promote South-South Cooperation to support the capacity of developing countries in tax policy and administration systems (*Medium-term*);
- Survey and disseminate all G-20 and international organisations' actions on supporting tax systems in developing countries (*June 2011*);
- Set up objective measures to track progress in the capacity improvement of LICs' tax administration systems (*June 2011*); and
- Identify ways to help developing countries' tax Multinational Enterprises (MNEs) through effective transfer pricing. (*June 2011*)

The results will be reported at the Summit in France. (*November 2011*)

The report focuses on how the G-20 can contribute to strengthening the enabling environment in which tax systems can be developed, building on the extensive work that has already been done by multilateral institutions and bilateral donors. It is not a comprehensive plan for how tax can be used to promote development. Rather, it sets out how the G-20 can show leadership and provides political support to ongoing initiatives and identifies areas which need to be reinforced.

The issues discussed in this report are closely linked to those addressed in the other pillars, especially infrastructure, social protection and investment, as well as the issues in the G-20 Working Group on Corruption. Without adequate revenues developing countries cannot invest in the physical and social infrastructure required for sustainable development, and addressing governance issues in the tax area is critical to wider governance reform.

The report first looks at the key issue of capacity building in tax administrations and tax policy design (Chapter 2); then it examines issues related to transfer pricing (Chapter 3). Chapter 4 addresses benchmarking and performance indicators and

Chapter 5 provides a survey of existing bilateral and multilateral actions to support tax systems in developing countries plus proposals to develop knowledge management platforms.

This report has been prepared by the organisations mandated at the G-20 Seoul Summit: the IMF, the OECD, the United Nations and the World Bank. These organisations have worked with regional organisations, such as ATAF and CIAT, and its preparation has also benefitted from wide consultation with other organisations working in the tax area. There has also been extensive consultation with developing countries, CSOs, academic and business representatives through their participation in meetings and web based discussions organised by the IMF[2] and their participation in the Task Force on Tax and Development[3]. The report is prepared under the responsibility of the Secretariats and Staff of the four mandated organisations. It reflects a broad consensus among these staff, but should not necessarily be regarded as the officially-endorsed views of those organisations or their member states.

## The challenges facing developing countries[4]

Significant progress has been made by many developing countries but weak capacity, corruption and the missing reciprocal link between tax and public and social expenditures remain as challenges. The vicious circle of low tax morale and compliance — which reduces the lifeblood for funding public services — needs to be broken.

The external environment poses increasing challenges. The continued heavy dependence of many countries on trade tax revenues, for instance, means that continued trade liberalisation poses significant challenges in recovering revenue from other sources. Striking the right balance between an attractive tax regime for domestic and foreign investment, by using tax incentives for example, and securing the necessary revenues for public spending, is a key policy dilemma. Competition between developing countries for investment can trigger a race to the bottom. Developing countries face challenges in designing and implementing effective transfer pricing and information exchange regimes and more generally in improving transparency. These issues are being addressed as the debate over transparency in the reporting of financial data by

[2] The IMF held key meetings in Nairobi and Washington which brought together country officials from over 100 developed and developing countries, donor organisations, CSOs, academics and business. A paper on the issue was discussed by its Executive Board in March 2011.

[3] The Task Force on Tax and Development brings together developed and developing countries with NGOs and business to discuss how tax systems can be used to promote development.

[4] Used here, the term 'developing countries' refers to countries with per capita GDP below USD 3 945, corresponding to "low income" and "lower middle income" countries in the World Bank classification.

Multinational Enterprises intensifies and as developed and developing countries alike gear up to take 'whole-of-government' action to address illicit financial flows.[5]

Many of these and other tax challenges faced by developing countries affect more advanced economies too. Specific challenges that loom especially large in developing countries include:

- *Weak tax administrations.* A well functioning tax administration is key to mobilising domestic resources in developing countries and the design of the tax system should be influenced by the ability of tax administrations to administer it. Yet many administrations continue to be staffed by poorly trained and low paid officials, have structures which do not encourage an integrated approach to different taxes, and are marked by imbalanced service and enforcement functions;
- *Low taxpayer morale, corruption and poor governance are often deeply entrenched*. Corruption indicators are strongly associated with low revenue (indeed corruption functions like a tax itself, and is likely to be a particularly regressive and inefficient form of taxation), as are other governance indicators (weak rule of law, political instability). Causation can run both ways, but the centrality of tax collection as an exercise of state power gives addressing governance issues in tax collection wider importance;
- Dealing with sectors that are '*hard-to-tax*' everywhere, including small businesses, small farms, and professionals. This is particularly important where administrative capacity and incentives to comply are weak. 'Informality' is extensive in developing countries—perhaps 40% of GDP on average, up to 60% in many—but is arguably not in itself the problem: micro traders may be informal, for instance, but are also likely to have income and sales well below any reasonable tax threshold; and much of the most egregious evasion is by qualified professionals. The issue is perhaps better framed as one of *non-compliance*. Estimates of non-compliance are scarce, but Value-Added Tax (VAT) 'gaps' have been put at 50-60% in some developing countries, compared to 7-13% in developed countries.

There are of course significant differences among developing countries. Probably the most important is in natural resource wealth. Geography also matters. Small islands are better able to impose taxes at the border than are landlocked countries. Post-conflict countries, with shattered administrations and tax bases, face particular difficulties, and successor states are often especially eager to establish investor-friendly reputations. History also has a role, with differing legal traditions reflecting various colonial pasts, being associated with different revenue performance.

[5] See the Oslo Dialogue (http://www.oecd.org/dataoecd/14/0/47425987.pdf).

While the challenges are substantial, there are also grounds for optimism. Several African and Latin American countries have made significant advances, often in the most challenging governance environments. The call for change is increasingly coming from developing countries themselves. In Africa, the creation of the African Tax Administration Forum, driven, managed, and operationally funded by Africans, provides a key platform for peer learning, capacity development and dialogue on domestic and international tax issues. In the Americas, the Centro Interamericano de Administraciones Tributarias (CIAT) is a well established platform for regional action. Other regions have similar organisations. Increasingly the organisations and bilateral donors that work in this area are strengthening their co-operation, including under the umbrella of the International Tax Dialogue[6]. This has led to a network of donors which encourages both South-South and North-South Cooperation.

## Moving forward

This report does not make recommendations for actions at the level of developing countries themselves. It recognises that there cannot be a "one-size-fits-all" approach to tax for development. What it does do is to set out what concrete deliverables can be provided in response to the mandate given to international organisations at the Seoul Summit. Proposals focus on strengthening the enabling framework, as shaped by the G-20 countries, within which developing countries seek to raise their tax revenues in ways which promote statebuilding and a fair distribution of the tax burden.

The chapters in this report include several specific actions that could be taken to support the development of more effective tax systems; these are identified at the end of each chapter. The box below summarises the key actions under three broad messages:

- Deepening international co-operation;
- Multinational Enterprise transparency and compliance;
- Measuring progress.

[6] The International Tax Dialogue (ITD) is a collaborative initiative involving the EC, IDB, IMF, OECD, UK-DFID and World Bank Group to encourage and facilitate discussion of tax matters among national tax officials, international organisations, and a range of other key stakeholders. CIAT, ATAF and the UN now work with the ITD.

## Summary of Recommendations

| MAIN POLITICAL MESSAGES | SUPPORTING G-20 ACTIONS |
|---|---|
| **Message 1. Deepening International Co-operation.**<br>*We commit to deepening international co-operation and strengthening long term support to developing countries to help them mobilise domestic tax resources fairly and effectively, as the cornerstone of statebuilding, social inclusiveness and better governance.* | We will:<br>• Review the level of our assistance dedicated to supporting tax systems in developing countries.<br>• Undertake 'spill over' analyses of the impact of any significant changes in our own tax systems on those of developing countries, and support efforts to develop tools to counter tax evasion and avoidance in developing countries.<br>• Share our efforts to identify, quantify and make more transparent tax expenditures and request the international organisations to develop an analytical framework to assess the cost & benefits of special tax treatments and develop guidance for countries using tax incentives to attract FDI.<br>• Make transparent our exemptions on ODA funded goods and services, and encourage other donors to follow.<br>• Link tax and expenditure in our assistance programmes, ensuring taxation promotes statebuilding, accountability and equity, encouraging other donors to do likewise. |
| **Message 2. Multinational Enterprise transparency and compliance.**<br>*We will require Multinational Enterprises to improve tax transparency and compliance in developing countries and place good tax compliance more firmly at the centre of their corporate governance and risk assessment systems.* | We will:<br>• Promote the Multilateral Convention on Administrative Assistance in Tax Matters, support spontaneous information sharing in international tax fraud cases and include anti treaty shopping provisions in our tax treaties with developing countries.<br>• Request international organisations to advise G-20 leaders on how to make improvements in the transparency in the operations of MNEs in developing countries, taking into account the current debate on country-by-country reporting, best practice in business, and developments in national legislation (*e.g.* Dodd Frank in the US).<br>• Strongly encourage MNEs to provide the relevant and necessary information to developing countries in which they operate, and apply domestic rules to ensure that the transfer pricing practices of any particular entity do not result in a misallocation of profit out of its jurisdiction.<br>• Urge international organisations and other donors to strengthen their programmes to assist developing countries to effectively implement transfer pricing rules, in the context of their broader tax administration capacity development efforts. |
| **Message 3. Measuring progress.**<br>*We commit to working with developing countries to track results from their own revenue raising efforts and the efforts of their international partners.* | We will:<br>• Encourage international organisations to map assistance programmes on an ongoing basis, improve the reporting of those programmes, and develop dedicated knowledge management platforms.<br>• Share our own benchmarking of performance and structure of our tax administrations; support international and regional organisations (*e.g.* ATAF) to benchmark tax administrations and to develop a core set of indicators to monitor and assess capacity improvement in tax administrations and other revenue related areas.<br>• Urge international and regional organisations to improve the quality and consistency of statistics on tax systems of developing countries. |

# *Chapter 2*

# Identify Key Capacity Constraints Faced by Developing Countries in their Tax Systems and Make Recommendations on Capacity Building to:

## *(I)* Improve Efficiency and Transparency of Tax Administrations and;

## *(II)* Strengthen Tax Policies to Broaden the Tax Base and Combat Tax Avoidance and Evasion

## Introduction

This chapter briefly identifies core achievements in strengthening revenue mobilisation in developing countries, the fundamental constraints that remain, and lessons on how they can be addressed. It then identifies possible actions which the G-20 countries, working with developing countries, could take. It finds considerable scope for the G-20 countries to support the efforts of developing countries, including through their role as pivotal actors in international tax relations, showing leadership in addressing tax problems common to both developed and developing countries, in realising gains from increased international co-operation, and in helping to shape the work of international organisations.[7]

## Current situation

### *Background*

In examining the challenges faced by developing countries, it must be stressed that increased revenue—although extremely important in order to foster development, where spent correctly—is not the only consideration in assessing tax systems and their performance. Distributional concerns are particularly important, bearing in mind that the equity consequences of taxation can only be meaningfully assessed in conjunction with the spending that taxes finance. Also critical are: effects on economic growth; impact on governance and state-building; incentives (or disincentives) for undertaking private sector activities; and the potential role of taxation in addressing externalities, such as those affecting the environment.

It should further be recognised that "capacity" in its narrow sense—referring to resources, human and institutional—is necessary but not sufficient for progress to be made. Such capacity as does exist must be channelled into productive and appropriate directions. This requires that it not be dissipated in, for example, administering special tax treatments that serve little useful purpose, and that incentive structures—both within the revenue administration[8] and the wider judicial and political system—discourage corruption at all levels. Political will is necessary over extended periods of time to reform tax systems and administrations, and to address these broader concerns.

---

[7] DAC/OECD, *The Challenge of Capacity Development, Towards Good Practice* identifies three analytical levels at which capacity development objectives may need to be pursued: 1) individual, 2) organisational, and 3) the enabling environment. The first two of these are closely related to resourcing issues; the focus here is therefore on the ability of G-20 countries to reshape the third.

[8] Throughout this report, references to tax or revenue administration include customs administration as well as domestic administration.

### *Mobilising Domestic Tax Resources*[9]

Revenue requirements for relieving poverty and improving physical and social infrastructure are substantial. Achieving the Millennium Development Goals, for instance, may require some low-income countries to raise their tax-GDP ratios by around four percentage points.[10] But the quality of measures also matters: increasing revenue by further taxing readily compliant taxpayers can worsen distortions and perceived inequities; conversely, reducing reliance on trade taxes can bring real structural gains that outweigh short-term revenue difficulties. More fundamentally, the centrality of taxation in the exercise of state power means that more efficient, transparent and fairer tax systems, and less corrupt tax administration, can spearhead improvement in wider governance relations.

Experience shows that progress can be made. Given strong political will several developing countries have significantly improved their tax performance over relatively short periods. Common elements of success are sustained political commitment at the highest levels, administrative reforms aligned closely with policy changes, and strong leadership of the revenue administration—all of which may encounter powerful opposition.

Empirical estimates suggest that "effort"—the ratio of actual revenues to potential[11]—is not low in all developing countries, but that significant additional revenue could be raised in those countries where performance is weakest. Those with the lowest tax-GDP ratios also tend to be those with the lowest effort. In one study, out of 15 developing countries with tax-GDP ratios below 15%, for instance, 13 had estimated effort below their group median; raising it to the median would increase their revenue by an average of about 3% of GDP.

Several countries have shown the feasibility of substantially increasing domestic revenues. While some show little movement in tax-GDP ratios over extended periods, others have made impressive progress. One good performer, for instance,

[9] The summary assessment here of constraints and lessons in revenue mobilisation in developing countries draws on IMF (2011), IMF (2011), "Revenue Mobilization in Developing Countries", at http://www.imf.org/external/np/pp/eng/2011/030811.pdf

[10] United Nations (2005), *Investing in Development* (New York: United Nations).

[11] By 'potential revenue' is meant the amount that, given the revenue raised in countries with similar characteristics, it appears possible to collect. The formalisation of this concept, econometrics of its implementation and results referred to here are in IMF (2011), op.cit and Carola Pessino and Ricardo Fenochietto (2010), "Determining Countries' Tax Efforts," *Hacienda Pública Espanola/Revista de Economía Pública*, Vol. 195, pp. 61-83.

increased its tax-GDP ratio from 6 to 13% over the 1990s to around 17% now. Some have achieved sustained revenue increases of 4–5% of GDP in just a few years.

There are important design links between different tax policy instruments. Perhaps most fundamentally, one theme is that pressures on revenue from trade liberalisation, regional integration and tax competition mean that, *absent greater international policy coordination*, the search for additional revenue will likely focus on relatively immobile bases — most obviously labour, consumption, and real estate.

Whilst domestic political will and leadership is the primary driver of capacity development, partnerships with international assistance providers can play an important role. International organisations have been very active in providing technical tax advice to developing countries for many years, although until recently tax has been somewhat neglected by much of the international community as a development issue, relative to expenditure issues. At present, only a very small proportion of international financial support to development is aimed at improving the tax systems developing countries.[12]

### *Key challenges for tax reform*

Each country must design its own reform package, and political will and ownership are essential for success. There is no "one size fits all" — but there are lessons that can help guide countries as they move forward in the tax reform process.

Perhaps most fundamental is the need to promote the virtuous circle by which increased trust between both taxpayers (in the use to which revenue is put and in the behaviour of tax officials) and tax administration (in the willingness of taxpayers to meet their obligations) reinforces voluntary compliance and good governance To this end, combining improvements in revenue administration with supportive — efficient, fair, effective — tax policies is essential. While it may be too much to assert, as the adage has it, that in developing countries, "tax administration *is* tax policy" — tax policy sets the framework within which the revenue administration must operate — in practice, the distinction between administration and policy is especially hard to make in developing countries. But there is no doubt that weak and often corrupt tax administrations, inadequately paid officials, extensive non-compliance and informality, weak organisational structures and political interference remain a fundamental barrier to effective and fair taxation, and to building wider trust between government and citizens.

[12] "Taxation as State-Building: Reforming Tax Systems for Political Stability and Sustainable Economic Growth—A Practitioner's Guide," World Bank Group/DfiD (2009), reports that of USD 7.1 billion spent in 2005 on bilateral aid for administration, economic policy and public sector financial management, 1.7% was devoted to tax-related assistance. OECD DAC reports that in 2009 USD 1.276 billion was spent on donor aid to non-tax public financial management activities, with USD 45.7 million going to tax-related activities.

Specifically:

- Progress has been made in reforming revenue administrations, but modern risk-management techniques are not yet widely applied;

- Many revenue administrations continue to suffer from serious problems of governance, though the progress made recently in some countries shows what can be achieved;

- High-income individuals can and must be taxed more effectively, not least to build the wider sense of fairness needed to support compliance more widely — by removing opportunities for avoidance and strengthening detection and enforcement;

- Although the personal income tax (PIT) is particularly difficult to enforce in developing countries with weak administrations, movement to explicitly schedular structures — in contrast to the near-universal advice of 20 - plus years to move to global systems[13] — can improve effectiveness and fairness;

- The value added tax (VAT) has greater revenue potential than most other instruments, but realising this in many cases requires expanding the base — by eliminating exemptions, unifying rates, and improving compliance — rather than increasing standard rates;

- More systematic attention needs to be given to replacing revenue lost from trade liberalisation — most middle-income countries have readily recovered lost revenue from domestic sources, but the same has not been true of low-income countries (though sub-Saharan African countries have on average done slightly better than others in this regard);[14]

- Incentives, including corporate income tax (CIT) exemptions in free trade zones, continue to undermine revenue from the CIT; where governance is poor, they may do little to attract investment — and when they do attract foreign direct investment (FDI), this may well be at the expense of domestic investment

[13] A "schedular" system is one in which income of different types—*e.g.*, wages, interest, rents, self-employment—is taxed under separate rate schedules (thus making progressivity harder to implement, but third party withholding and reporting more effective); a "global" system, in contrast, is based on the notion that all income increases the recipient's welfare in the same way, and therefore combines income from all sources for each taxpayer and applies a single, often progressive, rate schedule to the total.

[14] Baunsgaard and Keen (2010), "Tax revenue and (or?) trade liberalization," *Journal of Public Economics*, Vol. 94, pp. 563-577; see also Tax Policy Reform and Economic Growth, *OECD Tax Policy Study No.20*, 2010.

or FDI into some other country. Tax-driven investment may also prove transitory;

- The CIT is in any event likely to come under continued pressure from globalisation in coming years, as international tax competition continues to lead to lower rates of CIT around the world;
- Profit-shifting by multinationals is an increasing concern; strengthening capacity and legislative frameworks is important, which will require a greater engagement between LDCs, developed countries and business;
- Many resource-rich countries still struggle to design and implement fiscal regimes that are not only transparent but also capable of securing a reasonable share — and one reasonably responsive to commodity prices — of resource rents, an issue that recent discoveries are bringing to the fore in more developing countries.
- Establishing streamlined tax regimes for small businesses, and extending to them the methods of taxpayer segmentation — partitioning taxpayers into subgroups (by size and other characteristics) and tailoring treatment according to their capacities and needs — although unlikely to yield significant short-term revenue gain, is important for the longer-term development and perceived legitimacy of the tax system;
- Capacity within governments to carry out tax policy analysis is often weak, and a significant hindrance to better design and fuller ownership;
- Tax expenditure analysis should become a routine exercise, as it is necessary for efficient, transparent and fair systems;
- Improving the effectiveness and visibility of public spending financed by taxation can promote the trust on which voluntary tax compliance rests; and
- Sustainable tax reform can be obtained only with equally sustained political commitment from the highest levels; even where reform is successfully begun, backsliding can occur.

Importantly, not all of these problems are unique to developing countries. Addressing the severe fiscal challenges that many advanced economies now face will require understanding and reviewing the tax expenditures they provide;[15] and the

[15] See for instance IMF (2010), *From Stimulus to Consolidation: Revenue and Expenditure Policies in Advanced and Emerging Economies*, at http://www.imf.org/external/np/pp/eng/2010/043010a.pdf, and

challenges that international mobility creates for taxing multinationals and high wealth individuals are shared, to varying degrees, by all. These common issues and interests provide a basis for intensified co-operation, as discussed below.

## How the G-20 countries can better help developing countries' efforts

The challenges just described reflect capacity development needs in developing countries to which, as yet, the G-20 and the international donor community more broadly appear to have attached relatively little importance. As noted earlier, to date direct support for revenue and customs sectors has attracted a minimal share of aid (around 0.1% of ODA annually) despite some compelling evidence that aid directed at capacity development in the revenue and customs sectors in the developing world has been money well spent — an important result given the mixed record of technical assistance in supporting other public sector functions (see World Bank Independent Evaluation Group report 2008, for example). There are no quick fixes, and sustained results have come from cases where external support has taken a comprehensive institutional approach and been delivered over a period of years, if not decades. Active involvement of developing countries in regional organisations of revenue administrations and international fora on taxation is also essential to enhancing tax administration co-operation: for example CIAT has played a critical role in promoting the exchange of experiences and ideas in the taxation field including South-South exchange (as with the co-operation, to give just one example, between Chile and Kenya on tax IT systems). In all cases, demand is critical, whether expressed bilaterally or multilaterally, hence the importance of initiatives such as the African Tax Administration Forum—a tax administration organisation based in Africa that is cooperating and learning from CIAT, the oldest organisation of tax administrators. (See also Chapter 5). Success stories suggest that outsiders have delivered support according to local needs, in line with the principles of the Paris Declaration on Aid Effectiveness.

At the same time, G-20 and other donors need to be alert to the risk that aid itself may discourage recipients from strengthening their domestic tax regimes. General budget support, for example, may provide a positive way of engaging government in high level dialogue on issues related to improving the tax system in the broadest terms. However, tax issues may not be priorities for policy discussion, disbursements may not be linked to revenue objectives,[16] and fungibility with own source revenues could

the appendix on tax expenditures in IMF (2011) *Fiscal Monitor*, at IMF Fiscal Monitor -- Shifting Gears: Tackling Challenges on the Road to Fiscal Adjustment, April 2011; see also Tax Policy Reform and Fiscal Consolidation, Tax Policy Brief, OECD December 2010.

[16] IMF conditionality does frequently focus on revenue issues. Fund-supported programs are making increasing use of structural revenue measures as part of government-owned strategies to increase

discourage revenue mobilisation. Moreover, tax-related indicators sometimes emphasise revenue ratios at the expense of alternatives relating to operational and governance matters.[17]

Against a background of relatively weak institutional capacity and poor cultures of tax compliance, most developing countries face a long struggle to improve revenue performance in an efficient, fair and consensual way. These difficulties are compounded by the increasing globalisation of their economies through foreign investment, trade and labour mobility, a process to which tax systems need to adjust if the benefits are to be fully realised. Other than by the provision of external assistance and financing, this is the context in which the G-20 countries interact most directly with the tax systems of developing countries, and so in which they could be most supportive.

There are two broad ways in which the G-20 countries can better work with developing countries to support their revenue mobilisation efforts: leading by example in addressing common issues and furthering common interests, and as shareholders or members of the international organisations most closely concerned with taxation and development.

***Common issues, common interests — leading by example and developing partnerships***

***Improving transparency***

Several international initiatives are underway that are primarily intended to address corruption but which also have important implications for tax transparency. In the area of natural resources — of critical importance to many developing countries, and likely if anything to become increasingly so — the Extractive Industries Transparency Initiative (EITI), in particular, supports improved governance in resource-rich countries through the verification and full publication of company payments and government revenues from oil, gas and mining. The G-20 could also encourage countries to examine the recently enacted Dodd-Frank legislation in the US [18] (which in effect makes participation in the EITI approach compulsory for certain companies).

economic growth and reduce poverty. IMF (2011), *Revenue Mobilization and Developing Countries*, at http://www.imf.org/external/np/pp/eng/2011/030811.pdf.

[17] See "Appropriate Aid Modalities for Supporting Tax Systems," Nathan Associates, for the International Tax Compact of the German Federal Ministry of Economic Cooperation and Development, German Financial Cooperation, and the OECD/DAC Tax and Governance Task Force (GOVNET), draft March 2011.

[18] One aspect of the U.S. "Dodd-Frank Act" (2010), which in general implements wide-ranging changes to the regulatory environment for the financial industry, mandates that certain companies engaged in the extractive industries disclose in annual reports data concerning all "payments" made by

Whether and how to extend EITI and the Dodd-Frank legislation to sectors other than extractive industries is the subject of international debate. It is not yet clear whether, and how, some of the recent calls for such "country-by-country reporting" would if implemented be effective in the existing international income tax system. Sceptics fear that excessive reporting may simply overwhelm tax administrations in information which is not easily applied to measure legal tax burdens; advocates see it as a potentially important advance in transparency, with many NGOs feeling that reporting of this kind would facilitate a more informed debate between civil society, business and government. The G-20 countries could encourage the international organisations (including accounting and other bodies, as relevant) to accelerate exploratory work on how to promote transparency, including through country-by-country reporting as a standard for MNEs, and best practices currently used in the corporate sector, ensuring throughout that any proposals be directed at assisting tax administrations in developing countries.

***Tax expenditures and exemptions***

Identifying, quantifying and publicising tax expenditures — the revenue cost of preferential tax treatments — is widely recognised as a key element of fiscal transparency and, as such, a potentially powerful tool in avoiding and scaling back preferences that do not generate some offsetting social benefit. The regular production of such analyses is a core element, for instance, of both the IMF's *Manual on Fiscal Transparency*[19] and the OECD's *Best Practices for Budget Transparency*. Several (though by no means all) G-20 countries routinely produce such analyses, and so, increasingly, do some developing countries. For the latter, tax expenditure analyses can be an extremely important first step in assessing the costs and benefits of, for instance: tax incentives (however well-intentioned) aimed at attracting foreign investment, which may well prove counter-productive both for the country itself and, even more certainly, the wider international community; tax exemptions to special domestic interests; and indirect tax preferences motivated by equity concerns. Even the mere publication of exemptions and identity of groups of beneficiaries, without the cost estimates of a full tax expenditure analysis, could transform the ability of citizens and civil society to engage in the debate. This is an area in which the G-20 can support the idea and practice of routine tax expenditure analysis as a key element of good fiscal governance by sharing their experiences in this area, holding themselves to a high standard in their own reporting, and encouraging international organisations, working with other bodies also

---

the company (and all controlled subsidiaries or other entities) to governments. Until the SEC agrees implementation regulations it remains unclear, however, how in practice the legislation will operate.

[19] At http://www.imf.org/external/np/fad/trans/manual.html and www.oecd.org/dataoecd/33/13/1905258.pdf respectively.

active in this area,[20] to provide clear guidance, sensitive to countries' differing capacities, for reporting tax expenditures.

Tax expenditure analysis is itself just a first step towards a thorough evaluation of preferential treatments and action on those found not to generate net social gains. No country can be expected to change its domestic tax policy just as an example to others. It remains the case, nonetheless, that developing countries often take how G-20 countries address particular tax issues as the "right" answer, and — special treatment once granted being extraordinarily hard to remove — that this risks entrenching inappropriate preferential treatments.[21] The impediment to good practice this creates is not trivial. It makes it still more important that the example provided by G-20 members is not only reporting tax expenditures but also evaluating them and acting on the result.

Tax breaks aimed at foreign direct investment—largely to Multinational Enterprises (MNEs) domiciled in G-20 countries—are an especially significant form of tax expenditure in many developing countries, in many cases significantly undermining their tax revenue base. Developing countries sometimes believe — often correctly — that an attempt to hold the line against Multinational Enterprises negotiating for "necessary" tax breaks will simply drive the investment in question into a neighbouring country. This sort of bargaining frequently results in a "race to the bottom," in which countries in a region are made collectively worse off, to the benefit of the multinational investors. Studies also suggest that tax-driven investment does not provide a stable source of investment in the recipient country. Addressing this problem requires a closer partnership between LDCs, developed countries and business. Such a dialogue could lead to a code of best practice for MNEs. G-20 countries should encourage and support developing countries in their efforts to resist pressure to grant such mutually damaging tax breaks. Developing countries themselves may be able to mitigate the damage to their revenue bases by stronger regional co-operation — a process that G-20 countries should encourage.

Since such exemptions are often granted through special agreements negotiated without the involvement of tax administrations or officials in charge of tax policy, they can undermine the ability of the tax authorities to object to special tax exemptions granted by other branches of the government through agreements related to private investment projects (*e.g.* through an investment contract concluded with a foreign

[20] CIAT in particular has established a working group for the measurement of tax expenditures, to assist member countries that do not have significant experience in the area. This will be accomplished by providing them with a Handbook of Best Practices being developed by delegates from six countries that do have such experience. Along with the Handbook, the working group has been building a database of existing tax expenditures in the countries subject to CIAT's study, including their fiscal cost.

[21] Reduced VAT rates on equity grounds, for instance, even though they are clearly highly inefficient means to that end

enterprise planning a major investment). G-20 countries should encourage their resident companies to ensure that, if tax exemptions are to be granted, the tax authorities of the developing countries are fully involved in the negotiation and design of these exemptions

Another form of exemption that has proved especially problematic for many developing countries is the practice of exempting from taxation donor — funded projects — sometimes in all respects, not merely from tariffs on importation. This further stretches the limited administrative capacities of many developing countries, risking leakage of "donor" goods into the economy without taxation. Where donors are willing to provide direct budget support, insisting on such exemptions makes little sense.

***Strengthening compliance and facilitating mutual assistance***

An effective set of tools to address tax avoidance and evasion is critical in defending the revenue bases of both G-20 and developing countries and much work has already been done both by international organisations and countries alike. Building on this work, G-20 countries, working through the Forum on Tax Administration and others could develop a menu or tool kit of measures to counter avoidance and evasion. This should include an appreciation of countries' experience with counter measures so that developing countries can make an informed choice about the best way forward. For instance, experience in countries that have a strong general anti-avoidance rule in their tax law indicates that this approach can be a very effective deterrent and enforcement instrument. The tool kits could build on existing work including in the important area of improving the availability of timely and relevant information.[22] The specific measures or combination of measures that will be most effective in the context of a particular country will vary. Measures could include targeted or general anti-avoidance rules, penalty regimes for taxpayers or schemes promoters, litigation strategies and the direction of resources to particular taxpayer segments.

The underpinning of any response to evasion and avoidance in both G-20 and developing countries is the availability of timely and relevant information. The availability of information at an early stage helps to improve risk assessment and to make efficient use of the resources available, thereby improving overall compliance. At the same time it allows the tax policy function to make timely and informed decisions on the appropriate legal framework. Different strategies are being used to achieve this objective, ranging from voluntary to mandatory measures including reporting obligations relating to tax schemes or tax risks more generally.

[22] See *e.g.* OECD (2011) *Tackling Aggressive Tax Planning through Improved Transparency and Disclosure*, OECD, Paris, http://www.oecd.org/dataoecd/7/29/47020506.pdf and Barrie Russell, *Developing a Taxpayer Compliance Program*, http://www.imf.org/external/pubs/ft/tnm/2010/tnm1017.pdf.

Tax evasion (*e.g.* arising from informal but taxable activities) remains a large and intractable problem for many G-20 and developing economies. There are no "silver bullet" solutions enabling immediate success. Increasingly, the approach of the most advanced economies entails the systematic use of risk management techniques, applied at both strategic and operational levels, to identify, assess and treat the major compliance risks, using a variety of risk treatment strategies (*e.g.* legislation, education, service, soft and hard enforcement measures). G-20 countries could support developing countries by providing structured guidance on the use of such techniques[23].

G-20 countries could support developing countries efforts to enforce tax laws through spontaneous exchange of information, in particular in international tax fraud cases. This would assist developing countries' tax administrations in identifying potential cases for investigation and generate information to help respond to global tax threats and international schemes.

More generally, effective and simplified exchange of information from G-20 countries to developing countries is critical[24]. In the context of the Global Forum on Transparency and Exchange of Information for Tax Purposes, significant progress on this problem is being made. The topic is covered in the report on Action 2 of this Pillar 8, so is not explored here.

Similarly, G-20 countries could act in concert with or on behalf of developing countries in parallel to their own actions with regard to offshore income and wealth sources. In developing countries, as in G-20 countries, wealthy citizens are frequently the beneficiaries of income from offshore wealth holdings. Developing countries have even less ability than more advanced administrations to combat this problem and to reach this income, despite their legitimate claims to do so under their existing national law. G-20 countries can and do take actions against their citizens who fail to report such income. As in the case above, collaboration with developing countries through mutual assistance — on a broader basis than at present — would be of great significance not only to developing country revenues, but — in particular — with regard to governance and statebuilding through the tax system of those countries. Taxpayers are well aware in many cases that elite citizens are the beneficiaries of substantial untaxed income,

---

[23] See OECD (2010) *A Framework for Successful Offshore Voluntary Compliance Programmes*, Centre for Tax Policy and Administration, OECD, Paris; see also IMF Technical Notes and Manuals TNM/10/03 (2010) Taxpayer Audit – Development of Effective Plans, Edmund Biber, 14 April 2010

[24] Note the Multilateral Convention on Administrative Assistance in Tax Matters has been opened up to all countries at the request of the G-20 with effect from 1 June 2011, see www.oecd.org/ctp/eoi/mutual.

undermining faith in the government as a whole.[25] Providing support to developing countries in properly taxing their residents' offshore income also requires that G-20 countries ensure that they have access to information from their own financial institutions about accounts held by residents of developing countries, so they will be capable of providing that information to the developing country tax administration.

An emerging concern in several developing countries is the difficulty of imposing the tax to which they are entitled on capital gains that ultimately arise from assets located in that country when the transactions in which those gains are realised take place elsewhere. While the appropriate scope of taxing rights over foreign transactions may be a subject of legitimate international debate, it is generally acknowledged that gains from shares whose value is primarily derived from underlying real property in the source country are a legitimate source of taxation there, regardless of the "location" of the share transaction. This is a particular concern in relation to natural resources — which generally fall within this international norm — and the sums involved are significant from developing countries' perspective. In those cases where the legitimate taxing right is acknowledged, the primary issue appears to be one of implementation, and the question then arises as to whether G-20 countries would be willing to do more to assist developing countries, whether in identifying the transactions, and/or in providing "mutual assistance", including not only information exchange but also assistance in recovery, simultaneous audit, or tax examination abroad (as is frequently provided for under tax treaties—though many developing countries may not be party to such treaties with the developed countries where the transactions take place, or may not always receive the assistance they need even where such provisions exist). This is a highly technical matter that will require closer investigation before recommendations can be made.

The G-20 countries' lead role in the debate on international tax system creates an obligation on them to ensure its smooth functioning. In that context, it would be appropriate for G-20 countries to undertake "spillover analyses" of any proposed changes to their tax systems that may have a significant impact on the fiscal circumstances of developing countries. Trade agreements are an obvious example — tariffs remain a key source of revenue in many developing countries. But there can be important effects from other G-20 tax policies too, including in their international tax regimes (in moving, for instance, from residence to territorial systems).[26] While such

[25] See OECD (2009), *Engaging With High Net Worth Individuals on Tax Compliance*, Foreword by Pravin Gordhan, FTA, OECD, Paris.

[26] Reduced tax rates in capital importing countries may have more bite in attracting foreign investment when the capital exporter operates a territorial rather than a residence system, because under the latter, but not the former, the effect of that reduced rate is in principle undone when profits are repatriated. The implication is that a movement to territorial taxation may intensify international tax competition. See Peter Mullins, 2006, "Moving to Territoriality? Implications for the U.S. and the Rest of the World", *Tax Notes International*, Vol.43 (10), September 4, 2006, pp.839-53.

analyses will of course not necessarily alter the course adopted, they may point to remedial measures to be incorporated into the reform and should be published for the international community to reflect upon — at a minimum, to enable developing countries to respond with parallel changes to their own systems if that would be helpful in protecting their revenue bases. Ideally, a "baseline analysis" along these lines would be undertaken immediately.

It is important that double tax treaties serve the interests of both partners, and both the OECD and the UN are very alive to this concern in their models and continuing work. Treaties can encourage investment not only by providing for reduced withholding tax rates, but also through, for example, non-discrimination clauses and dispute resolution procedures. The extensive treaty networks of most G-20 countries with developing countries reflect the belief, on both sides, that they generate very substantial advantages. Nonetheless, where investment and income flows are unbalanced — as is typically the case between developed and developing countries — treaties substantially reducing or eliminating withholding rates on interest, dividends and fees can operate to the revenue disadvantage of the source (developing) country unless the treaty package adequately encourages offsetting revenue-producing investment or unless the burden of the unreduced rate is effectively borne by the developing country payer. It is important that G-20 countries recognise in their negotiations that reductions in a developing country's taxing jurisdiction may significantly erode its tax base. This is especially so if the benefits of the treaty are effectively available to third country residents through treaty shopping arrangements. G-20 countries should thus be prepared, for instance, to include anti-treaty shopping provisions in their treaties with developing countries, and to help those countries evaluate appropriate anti-treaty shopping policies, while preserving the benefits to be derived from the treaty relationships.

### *Acting as members or shareholders in international organisations*

To help developing countries link revenue and expenditure management, the G-20 countries could encourage international organisations to more thoroughly assess, and then act upon, linkages of tax and expenditure policies in their technical assistance. It is generally accepted that equity goals cannot be achieved only, or even largely, on the tax side — but rather that appropriately targeted expenditures are more effective in this regard. In most low-income developing countries, targeted spending schemes, especially targeted transfers to individuals or families, are more difficult to implement than in developed countries, given existing administrative and analytic capacity constraints, although progress is being made in this regard (in part through use of innovative schemes for conditional transfers linked to, *e.g.*, children's school attendance records, vaccinations, and the like). There has been insufficient analysis of how taxation can be linked to these goals, beyond simplistic calls for earmarking, experience with which has often been discouraging. It is now increasingly recognised that the tax-spending links

could be more strongly made, not least in the context of fostering statebuilding.[27] Results of such analysis can then be brought to bear in multilateral and bilateral technical assistance — and most importantly, by the developing countries themselves. It will be important to bear in mind, however, that such integrated analyses of tax and spending measures can be quite resource-intensive.

The G-20 countries should encourage the IMF and World Bank, working with other international and regional organisations as appropriate, to develop and make available better revenue data sets for developing countries with consistent methodology, building on data they currently collect. This would permit far better economic analysis of developing country taxation, and more improvements in revenue administration in those countries through better analysis of tax gaps, and effects thereon. Such data — adjusted to be consistent, and stratified by revenue source and levels of government — do exist for the OECD and EU countries, and greatly facilitate this sort of analysis for these economies.

[27] This issue is discussed extensively in OECD (2010), *Citizen-State Relations: Improving Governance through Tax Reform*, OECD, Paris.

## Summary of Recommendations

Estimate and publish tax expenditures, and the costs of special provisions, in regular tax expenditure budgets. G-20 countries could lead and encourage a more rigorous assessment of the costs and benefits of such provisions.

Develop analytical frameworks, suitable to the varying needs and circumstances of different countries, to assess the costs and benefits of preferential tax treatments, including in particular tax incentives aimed at FDI, and provide guidelines for countries which use such incentives.

Disclose and consider reducing the scope of tax exemptions required by G-20 countries from country recipients of aid-funded projects.

Undertake "spillover" analyses of proposed changes to tax law in G-20 countries, for example in trade and international taxation—which could have effects on the fiscal circumstances of developing countries.

Encourage international organisations to more thoroughly assess and act upon linkages of tax and expenditure policies in their technical assistance to developing countries.

Encourage the IMF and World Bank, working with other international and regional organisations as appropriate, to further develop and make publicly available consistent and detailed revenue data sets for the developing countries.

Encourage the international organisations, including the Forum on Tax Administration, to develop a tool kit of measures to counter tax evasion and avoidance, based on best practice and guidelines adapted to the needs of developing countries.

Promote the Multilateral Convention on Administrative Assistance in Tax Matters.

The report has also identified the examination of improving the transparency of MNEs, through country-by-country reporting for example, as an issue for further study.

# *Chapter 3*

# Identifying Ways to Help Developing Countries Tax Multinational Enterprises (MNEs) through Effective Transfer Pricing Rules

## Introduction

This chapter explains the significance of transfer pricing for developing countries and identifies possible G-20 leadership messages to G-20 countries, other donors, business and international organisations.

Multinational Enterprises (MNEs) operating in developing countries can, and in many cases already do, make a significant contribution to tax revenue. They may, however, use aggressive tax planning techniques, including through transfer pricing, to shift part of their profits to low tax jurisdictions. When this occurs developing countries forgo revenue that is much needed to invest in the physical and social infrastructure required to achieve sustained growth. Given the high profile of MNEs in the local economies of many developing countries, such behaviour may undermine the legitimacy of local institutions and discourage voluntary compliance by other taxpayers.

## Current position

MNEs consist of groups of associated companies or branches which are located in a number of countries. The companies or branches that make up such groups typically conduct transactions with each other, and some estimates suggest that as much as 40% of global trade takes place between constituent members of MNEs. Typically, such transactions include the purchase/sale of goods, the provision of services, including financial services, sales or leases of tangible property and the sale or licence of intangible property. Transfer pricing refers to the prices in place for such transactions within MNEs. Intra-group cross-border transactions, conducted at a price (*i.e.* a "transfer price"), are normal and legitimate features of MNEs. Financial records derived from these transactions are used to assess the profitability of the different parts of an MNE and set internal rewards and incentives.

From a tax perspective, transfer pricing is primarily important because it influences the amount of profit that MNEs report in each of the jurisdictions in which they conduct business. Transfer pricing becomes an issue when, for whatever reason, MNEs conduct their intra-group transactions at prices that distort the allocation of income or expenses among associated enterprises or their branches in comparison to that which would be expected if normal market forces were to apply - that is, on an "arm's length" basis. Transactions conducted on non-arm's length terms have the potential to result in a significant misallocation of tax revenue between governments. Concerns about potential tax losses from transfer pricing are shared by developed and developing countries alike.

It is to protect against such potential revenue loss that governments introduce transfer pricing rules, which require their taxpayers to report tax profit on the basis that intra-group transactions are conducted on arm's length terms, *i.e.* in accordance with the arm's length principle.[28] Transfer pricing rules primarily target cross-border transactions. However, some countries apply transfer pricing or similar rules to purely domestic transactions in order to address potential profit-shifting from high to low tax regimes (*e.g.* into the free zones). Similarly transfer pricing may be used to circumvent exchange controls or to enable an MNE to shift profits out of potentially unstable countries.

Transfer pricing is a key potential instrument for aggressive tax planning by MNEs but of course it is not the only one. For instance, MNEs may use aggressive financial structures including the use of hybrid entities, instruments and transfers to create multiple deductions or credits, to create deductions without inclusions, and/or to reduce or avoid withholding taxes (sometimes relying on treaty shopping). They may also use schemes that create artificial losses, defer recognition of income/gain or losses, or convert one income type into another.

The arm's length principle is the basis of Article 9 of the UN and OECD Model Tax Conventions and is discussed in depth in the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations. It provides that, for the purposes of determining the taxable profits of associated enterprises, the conditions of commercial and financial transactions between them should not differ from those that would be made between independent enterprises in comparable circumstances. In the absence of a common approach between governments, the application of transfer pricing rules can potentially give rise to economic double taxation, which has the potential to hinder international trade and investment. Tax conventions typically include provisions designed to avoid double taxation and resolve disputes between countries over the correct application of internationally agreed principles.

International support to developing countries in the area of transfer pricing is provided by a number of agencies including the UN, OECD, IMF, ATAF, EC, CIAT and the World Bank. The multi-stakeholder Task Force on Tax and Development, hosted by the OECD, and which includes developing countries in its membership, is focusing on a) better understanding, articulating and promoting developing country needs on specific issues of transfer pricing; b) strengthening assistance in the adoption and effective implementation of transfer pricing rules and encouraging co-ordination among the agencies involved; and c) ensuring that international standards and approaches to transfer pricing are relevant to and effective for developing countries.

[28] Some academics and NGOs have proposed alternative approaches (such as 'formulary apportionment') that do not allocate taxable profits in this way, though no governments have used this approach in an international context.

## Gaps and unmet needs

Many developing countries report that they face practical difficulties in effectively implementing transfer pricing rules. Many of these difficulties are also common to developed countries, but in practice such problems are likely to be more acute for developing countries. These may include difficulties: a) in drafting clear legislation and guidance; b) in building tax administration expertise and experience in transfer pricing to enable them to carry out effective audits; c) in obtaining the information needed from taxpayers in order to select cases for audit or carry out effective audits; and d) in obtaining public information on arm's length conditions, *i.e.* the conditions (for example, price or profit margin) in place for independent enterprises conducting comparable transactions under comparable circumstances. There is a very strong demand from developing countries to support them in the adoption and implementation of transfer pricing rules in accordance with internationally developed principles.

More needs to be done to assist developing countries in adopting and effectively implementing transfer pricing rules in accordance with individual country needs and priorities – including: a) diagnosing transfer pricing regulatory needs; b) development of legislation and related guidance; c) adoption of related administrative provisions (*e.g.* documentation requirements); d) building databases on arm's length comparable data[29], including comparables (adjusted where necessary) derived from other countries; e) building administrative structures and processes to manage the application of transfer pricing rules – for example risk-based case selection processes; f) building relevant skills (including economics, commercial, analytical, legal, audit and information management skills); and g) building effective, transparent and equitable dispute prevention and resolution processes (in both domestic and international contexts).

In order to avoid double taxation and create a predictable business climate, it is important to achieve an internationally consistent approach to transfer pricing, recognising that the needs of countries will vary according to their patterns of international trade, administrative capacity, and their policy needs and priorities. It is equally important that internationally developed principles on transfer pricing are relevant to, and can be effectively applied by, developing countries. There is thus a need to work more intensively with developing countries so as to enhance their input into and/or participation in the development of international standards and approaches to transfer pricing, to ensure that they reflect the needs and realities of such countries, and that these countries can implement these standards effectively. International standards and approaches might be made more relevant for developing countries through, for example, the development of additional guidance designed to address the challenges identified by developing countries that hinder their effective implementation of transfer pricing rules (such as those described in the first paragraph above).

[29] Supported where appropriate by the creation of national registries of unlisted companies.

## Summary of Recommendations

### *a) Improving Support*

G-20 countries and international organisations should strengthen their programmes to assist developing countries diagnose their transfer pricing regulatory needs and adopt, and then effectively implement, transfer pricing rules matched to their specific needs in accordance with their patterns of international trade, administrative capacity, and their policy needs and priorities. Such assistance should be focused on the areas described in the second paragraph above. Assistance needs to address more than simply legislative needs, recognising that effective implementation of transfer pricing rules requires an effective administrative framework and audit capacity.

G-20 countries should strongly encourage MNEs to provide developing countries in which they operate with information that is relevant or required by law in order to allow each of them to verify that MNEs follow country transfer pricing rules and that their transfer pricing does not result in a misallocation of profit out of its jurisdiction. G-20 countries and international organisations should support initiatives aimed at improving the ability of developing country tax administrations to require MNEs to provide them with information that is relevant in the context of a transfer pricing audit, bearing in mind the need to avoid imposing excessive and disproportionate documentation requirements.

G-20 countries and international organisations should support initiatives designed to assist developing countries to identify and effectively address implementation issues (*e.g.* lack of comparables in a domestic context, lack of relevant skills, lack of effective dispute prevention and resolution mechanisms) that may hinder their effective application of transfer pricing rules. This should be enhanced by ensuring that internationally developed guidance on transfer pricing is relevant to, and can be effectively applied by, developing countries in a broadly consistent manner.

G-20 countries and international organisations should assist developing countries to enter into, and develop their ability to effectively implement, bilateral and multilateral agreements to allow the exchange of information with other counties (see recommendations under Action 2). G-20 countries should also widen their network of bilateral tax conventions, as appropriate, with developing countries.

International organisations and donors could be encouraged to achieve better coordination between transfer pricing capacity-building programmes (regional, bilateral and multilateral) in accordance with their respective mandates, and making full use of the International Tax Dialogue, while ensuring that developing country perspectives are fully integrated into such work.

### *b) Improving Governance Framework*

Given the importance of a strong administrative framework in order to implement transfer pricing rules in an effective, transparent and equitable manner, international organisations and donors should work together to provide more integrated support to join up broader tax administration capacity development with capacity-building efforts in the area of transfer pricing.

G-20 countries could mandate relevant international organisations to assist developing countries to put in place mechanisms to better understand the impact of the adoption of transfer pricing legislation, including costs and benefits, modes of implementation available, and effects on the business environment and in attracting FDI.

# *Chapter 4*

# Setting up Objective Measures to Track Progress in the Capacity Improvement of LIC'S Tax Administration Systems

Developing robust indicators of revenue agency performance will be extremely challenging given the variation in the degree of sophistication of management information systems within these organisations across the world. Significant questions remain over what can be said to constitute best practice and how to measure it across the whole of a revenue administration's operations, although consensus exists in certain areas. The goal of the work programme set out in this chapter is to provide mechanisms and measures which help develop cultures of continuous improvement and incremental achievements in performance. An external perspective complements the view from within a country's own revenue administrations. Measures can be related to strategic approaches, organisational structures, processes, management systems and human resource factors.

## Current situation: substantial work has already been undertaken in this area, and several initiatives are underway

The FTA (a grouping of 43 heads of tax authorities including all G-20 countries) publishes the most comprehensive international comparisons of revenue bodies in its publication "Tax Administration in OECD and Selected non-OECD Countries: Comparative Information Series". The latest edition was published in February 2011 covering 49 countries (including all G-20 countries except Brazil, which will be in the next edition) and contains a wide range of data and indicators on the performance of revenue administrations. The FTA also publishes 'best practice' reports – 28 have been produced so far – for selected aspects of tax administration and reports of survey findings on administration-related topics (*e.g.* the use of technology in delivering services to taxpayers).

In its technical assistance (TA) work the IMF has for many years used objective measures to assess progress and guide the development of reform programmes (though the confidentiality of advice means these are not published). The IMF also publishes a wide range of books, papers, technical notes and manuals on issues of tax administration and policy specifically aimed at developing countries and often integrating administration closely with policy issues. The new donor-financed Topical Trust Fund in Tax Policy Administration mandates the IMF to work on a benchmarking tool to measure progress on administration reforms.

The World Bank has developed Actionable Governance Indicators to assist national authorities monitor progress in the implementation of country-led reforms. These include the PEFA (Public Expenditure and Financial Accountability) Framework, which includes a subset of four high level tax administration indicators. The PEFA Steering Committee has initiated a feasibility study for developing a drill down tool on tax administration, to address the limitation of these indicators. The report will be discussed at the next Steering Committee in June 2011. In view of the fact that are

important aspects of tax administration that are not covered by the PEFA framework, the WB has developed an "Integrated Assessment Model for Tax Administration" which will be implemented as a pilot later in 2011.

In addition, the World Bank Group's Global Tax Simplification Program (GTSP) has put together guidance on good practice for revenue administrations for large taxpayer administration as well as on international taxation. Additionally, the group has launched separate guidance for small and micro enterprise administration. The group is also preparing regional analyses of the effectiveness of SME tax administration in Asia and Africa.

Regional development banks and regional tax organisations have also been working in this area with work between CAPTAC, CIAT, the IDB and the IMF currently underway, including planned meetings to share their experience with ATAF. The 2010 publication of the African Economic Outlook by the African Development Bank and the OECD Development Centre also contains useful information on tax administrations in Africa through its focus on Public Resource Mobilisation, as does IMF (2011). The Asian Development Bank and SGATAR do not carry out any systematic measurement of capacity in tax administration systems in Asia.

Recent work through the ITD (funded by DFID and led by the IMF) has piloted the development of common indicators in sub-Saharan Africa. The pilot study set out indicators following the example and methods in the work of the Forum on Tax Administration. It also included elements of the IMF’s approach to identifying gaps in capacity in its work with developing countries, and drew on substantial input from ATAF. The pilot study has been published by the ITD (www.itd.org).

The report is based on a survey of countries in Sub-Sahara Africa (SSA). It was prepared on a pilot basis in order to test the process and to scope the information included in the survey. The survey was issued to over 20 countries, selected to achieve a balance of regional representation, level of development, government structure and size of country, as well as consideration of availability of data. Fifteen countries completed the survey: Benin, Ethiopia, Botswana, Ghana, Kenya, Malawi, Mauritius, Rwanda, Senegal, Sierra Leone, South Africa, Tanzania, Uganda and Zambia.

The survey seeks to compare, for illustration purposes only, approaches and practices across participating SSA and Forum on Tax Administration (FTA) countries. The survey aims to contribute to building a picture of tax administrations across regions and levels of development. ATAF is working with the ITD to develop a second phase of this work that will involve expanded country coverage in Africa and a further refinement of the selection of indicators collected. In this way, a more complete picture of how effectively tax administrations are working can be developed. The project is also

intended to build regional capacity through the process of indicator selection and methodological discussion itself.

The intention is for ATAF and ITD to start work on the second phase of this work soon with those countries involved, as well as developing plans for future work on indicators in 2012 and 2013. The plan is expected to include showing how such benchmarking type information feeds through into actual progressive reform of tax administration.

As part of this process, the pilot study was discussed and participation in the next phase encouraged at an IMF conference, with the participation of other international organisations, on DRM in Kenya in March 2011. ATAF held a meeting in April 2011 on the research conducted through the ITD to gain high-level buy-in from heads and senior officials of African Tax Administrations, and discuss and agree the process for this work programme in terms of survey instruments, country coverage, mechanisms for delivering data inputs and their interpretation. This is the first step in delivering a benchmarking type process that could provide diagnostic information for revenue authorities and providers of technical assistance.

In Latin America and the Caribbean, CIAT the Inter-American Development Bank and CAPTAC -DR (the IMF Technical Assistance Center in Central America) is developing a publication regarding a diagnosis of Latin American tax administrations which will identify best practices. It is expected that the study will be completed end 2011.

## Drawing the regional threads together

It is planned that the results of the analysis discussed above will be the basis of further ATAF-facilitated regional workshops with tax officials from those participating countries. These workshops will help ensure that the work on indicators of revenue capabilities evolves in a way that continues to be operationally relevant to African tax administrations over the long term as the operation of revenue authorities themselves evolve, including in processes and technology. This exercise will also benefit from input by CIAT, CATA and CREDAF along with the IMF and World Bank and other relevant organisations including the FTA working in the area of tax administration.

A further objective of ATAF is to utilise the measurement indicators developed for the second phase study to develop a model framework and a complementary diagnostic tool for African tax administrations to assist them according to their respective levels of development.

While there are existing tools to draw on (including also those of the WCO), it is imperative that further work is carried out to agree a group of core indicators that would allow more meaningful assessment of tax administrations and the progress of their reforms worldwide — which will be a challenging task.

More in-depth evaluations at regional level and amongst countries with similar levels of development could form the basis of a performance self-assessment tool that could inform governments and providers of technical assistance where the greatest obstacles to improved revenue administration exist at country level. ATAF sees the development of such a tool as a priority. This could include the development of both quantitative indicators assessing the use of modern management practices as well as more strategic qualitative assessments amongst smaller groups of countries.

Objective, codified and accessible knowledge on the capability of tax administration systems in Asia, Central Asia and the Middle East is extremely limited. It will be important to engage the ADB and other regional organisations in this work now that tax issues have increased in importance to the international community.

Overall an effort should be made to try to pull together the FTA, IMF, WB, and regional standards into a broadly consistent set of global standards, recognising that this would need to reflect the different stages of development in different countries.

**Summary of Recommendations**

Expand or increase publication of benchmarking work in the G-20 countries and publish improved tax gap analyses that themselves serve as benchmarks of good practice.

Asian G-20 countries could engage the ADB to facilitate the collection of similar comparative information to that collected by the FTA.

Encourage all interested multilateral and regional organisations operating in the tax field to work together in the development of a core set of indicators that would support meaningful monitoring and assessment of capacity improvement in tax administrations and other revenue related areas.

Ensure that improvements and lessons learnt in carrying out further measurement and analysis of capacity improvements in tax administration systems in different regions – especially that of emerging G-20 countries - is shared between regions and disseminated effectively via knowledge-sharing platforms in the tax area to the wider tax policy and administrative community.

Develop a strong partnership with ATAF, in the context of the ITD and its members, to revise and extend the coverage of the ITD African pilot study by further developing and agreeing a core group of relevant indicators of revenue body capabilities, efficiency and effectiveness, ensuring wider country coverage to enable countries to self-assess their performance, benchmark themselves against comparators as appropriate, and develop related diagnostic tools so as to provide a sound basis for identifying key obstacles to improved tax administration in the region and allocating resources to deal with them.

# *Chapter 5*

# Develop a Knowledge Management Platform and Promote South-South Cooperation to Support the Capacity of Developing Countries in Tax Policy and Administration Systems

# and

# Survey and Disseminate all G-20 and International Organisations' Actions on Supporting Tax Systems in Developing Countries

## Overview

This chapter provides:

a. An overview of the different platforms that currently supply information on international co-operation on capacity building in the area of taxation. It also briefly describes the linkages between these platforms, their main gaps and how these could be filled.

b. A summary of the main characteristics of existing knowledge management platforms and a review of opportunities for and challenges in developing them further; including by creating linkages between them in order to ensure that the broadest range of experiences is used to help tailor national policies.

c. A review of current "South-South Cooperation" in tax matters. It also indicates how further work and international co-operation in this area might strengthen tax systems.

## Current situation

In recent years, a convergence of economic and political factors has increased the level and depth of international co-operation in tax matters between developed and developing countries. Increasingly businesses operating in multiple countries are actually based in emerging economies, increasing the importance of shared rules and interpretation if conflict between revenue authorities is to be avoided. Out of this growing trend has arisen the need for more transparent and updated information on current and future activities, technical assistance (TA) providers and the financing of the assistance to support capacity building on taxation. There is scope for improving the information on TA activities undertaken by multilateral organisations[30], but even more for improving access to information related to bilateral actions.

In the field of taxation, both donors and recipients already have a fair knowledge of what they need and what is available, in particular at country level. But more readily available and more detailed information in this area would help TA providers and the agencies financing this assistance to design their support programmes. It would also help country authorities to get a better sense of what kind of assistance

[30] Confidentiality restrictions limit the information that can be shared on the substance of TA advice, except by the recipient countries themselves. The focus here is therefore on the fact and broad nature of advice being given.

may be needed and made available to them, and under what terms and procedures. Information on particular expertise developed by bilateral agencies on some topics may be very valuable and also help increased collaboration with multilateral agencies. This is particularly relevant in the case of new South-South Cooperation that falls outside the traditional development assistance (ODA). The more easily accessible information is, the more it would help all agencies involved to improve their efforts to coordinate their activities, to gauge whether funding for capacity building efforts is sufficient, and to evaluate effectiveness of capacity building activities.

## Access to technical assistance information

Providers already co-operate, mainly on a country basis, whether in the field or at more centralised levels including in the International Tax Dialogue (ITD) and bilaterally. There are already some provisions enabling the sharing of substantive materials in specific cases where all involved are directly working with the country(ies) in question. However, improved mechanisms to allow efficient collaboration could enhance the overall effectiveness of assistance programmes.

There are different platforms/reports that currently supply information on international co-operation on capacity building in the area of taxation. This information varies in terms of the range of data provided as well as the extent of their details regarding activities, providers and modalities of financing.

The ITD database[31] of technical assistance activities is a focal point for the collection and sharing of information on bilateral and multilateral technical assistance activities in relation to tax policy and administration. This information is publicly-available and searchable on provider, location, topics, intended audience, type of activity and dates for past, current and future activities (subject to confidentiality and security concerns). Details of over 1 500 activities provided by all ITD partners (DFID, EC, IADB, IMF, OECD and WB), CIAT, and USAID are currently available. In terms of resources allocated to these activities, the OECD-DAC statistics[32] include some information on past international financing for co-operation on capacity building in the area of taxation. Both ITD database and OECD-DAC statistics are regularly updated so capture the current status at any point.

Recently, several mapping studies on co-operation on capacity building in taxation have been undertaken by different organisations: the International Tax Compact (ITC)[33] and the UN Committee of Experts (in a report on capacity building prepared by

[31] http://www.itdweb.org/Pages/TechAssist.aspx

[32] http://stats.oecd.org/WBOS/Default.aspx?DatasetCode=CRSNEW

[33] http://taxcompact.net/documents.html

IMF staff) [34]. These (one-off) studies provide a static snapshot of activities, not a dynamic picture over time.

## Wider South-South Cooperation

The most direct mechanisms for both South-South and North-South Cooperation in tax matters are regional and other groupings, typically focused more on administration than on policy[35]. These include: the African Tax Administration Forum (ATAF), the Association of Tax Authorities of Islamic Countries (ATAIC), the Commonwealth Association of Tax Administrators (CATA), the Inter-American Center of Tax Administrations (CIAT), the Centre de Rencontres et d'Études des Dirigeants des Administrations Fiscales (CREDAF), the Forum on Tax Administration (FTA), the Intra-European Organization of Tax Administrations (IOTA), the Pacific Islands Tax Administrators Association (PITAA), and the Study Group on Asian Taxation Administration and Research (SGATAR). These organisations differ in their resourcing, activities and breadth of focus. There are also some bilateral exchanges of expertise between developing countries, *e.g.* study tours. These though appear to remain fairly limited.

### Tax Knowledge Sharing Fora

***A. The International Tax Dialogue (ITD):***

1. The ITD, established in 2002, is a joint initiative of leading organisations working on tax issues: the EU, IDB, IMF, OECD, UK-DFID, and World Bank Group. The ITD decided in January 2011 to encourage the UN, CIAT and ATAF to join the ITD.
2. As part of its work the ITD organises biennial global conferences on relevant tax policy and administration topics. The first three conferences have been hosted by three G-20 countries; Italy in 2005, Argentina in 2007, and China in 2009; the next will be hosted by India in December 2011 and will focus on Tax and Inequality. These conferences are targeted to ministers and senior tax officials from both developed and developing countries.

***B. The OECD Informal Task Force on Tax and Development:***

1. The OECD Informal Task Force on Tax and Development, created in 2010, works to promote co-operation between governments, business and civil society organisations to identify ways in which tax systems can work to promote development.

---

[34] Michielse, Geerten and Thuronyi, Victor (2010); "Overview of co-operation on capacity building on taxation"; Report prepared for the UN Committee of Experts on International Cooperation in Tax Matters; http://www.un.org/esa/ffd/tax/sixthsession/OverviewCapacityBldg.pdf

[35] We do not discuss here mechanisms for tax co-ordination within trading blocs, such as WAEMU, CEMAC, and the EAC, focused on delineating and enforcing common policies. The focus here is on softer forms of co-operation.

### Tax Knowledge Sharing Fora *(cont.)*

***C. The United Nations (UN):***

1. The UN Committee of Experts on International Cooperation in Tax Matters provides a framework for dialogue with a view to enhancing and promoting international tax co-operation among national tax authorities and to considering how new and emerging issues could affect international co-operation in tax matters. The Committee comprises 25 members nominated by governments and appointed by the UN Secretary-General. It is supported by a small secretariat.
2. Some relevant work has also been undertaken through the South-South Sharing of Successful Tax Practices (S4TP) project, as described in the main text.

***D. African Tax Administration Forum (ATAF):***

1. ATAF is a recently created organisation (2009) that brings together heads of African tax administrations and their representatives to discuss the progress made, challenges faced and possible new directions for African tax policy and administration.
2. ATAF aims to become a platform to allow African administrators to articulate African tax priorities, anchor good practices, and build capacity in African tax policy and administration through peer learning and knowledge development.
3. ATAF is currently closely working with multilaterals and regional bodies directly (AfDB, CIAT, IMF, OECD, WB) and through the ITD to develop these capacities.

***E. Inter-American Center of Tax Administrations (CIAT):***

1. CIAT is a well established forum for knowledge sharing mainly focused on tax administration issues in the Latin American and Caribbean region. CIAT currently has 38 member countries and associate member countries from 4 continents: 29 countries of the Americas, 6 European countries, 2 African countries and 1 Asian country.
2. CIAT promotes timely dissemination of relevant information and the exchange of ideas and experiences through general assemblies, technical conferences, seminars and publications.

***F. Other Bilateral and Multi-Donor Initiatives:***

1. The German Government funds the International Tax Compact (ITC) which encourages tax networks and exchange of experiences that can help identify and address areas of concern in the international tax arena.
2. The UK and Norwegian Governments fund the International Centre for Tax and Development (ICTD) which will commission, disseminate and build networks of researchers and users of tax policy and administration studies, particularly on the interface between the technical aspects of these and the linkage to statebuilding and the political economy of development.

International organisations also undertake various activities to support direct South-South interactions. These include training courses, workshops and regional events that are organised by several international organisations. The IMF, in just one recent example of its long-standing activities of this kind, organised a conference in Nairobi in March 2011 on Domestic Resource Mobilisation issues in sub-Saharan Africa, attended

by more than 100 officials from 37 countries in the region, as well as a global event in Washington DC. The OECD's Global Relations Programme brings together officials from developing countries to exchange experiences in the area of international tax issues, putting on an average of 75 events a year, with around 40 000 from developing countries having participated since the programme began. The UN is, for example increasingly bringing together key southern participants in meetings to share experiences on specific issues such as transfer pricing and double tax treaties and their implementation, including through its South-South Sharing of Successful Tax Practices (S4TP) project (http://www.s4tp.org/), a partnership with the Special Unit on South-South Cooperation of the United Nations Development Program (UNDP), and two NGOs.

The IMF's seven regional assistance centres[36] (with two more planned)[37] are one of the best examples of South-South advice. Each has one or more resident tax experts, normally recruited from within the region, and makes substantial use of local experts in delivering advice, following programmes approved by steering committees with strong representation from those countries. The IMF's and other IFIs long-term resident experts are commonly drawn from the region, and of course so are some of the headquarters staff. ATAF, CIAT, OECD, the ITD and the UN also directly promote South-South Cooperation.

## Knowledge management platforms

In addition to the knowledge sharing fora discussed above, there are also a number of 'knowledge management (KM) platforms'. The term as used in this way refers to IT-based systems for information pooling and access. KM platforms have a role in South-South Cooperation (and in co-operation with and between advanced countries), but the knowledge fora encompass a wider set of mechanisms and activities. These might include, for instance, advice and discussion with counterparts in other developing countries, workshops, conferences as well as online information access and online fora.

There are already several KM platforms whose purposes include promotion of South-South Cooperation in tax policy and administration by sharing codified knowledge. Chief among these are the global Internet sites of the ITD and the UN Committee of Experts on International Co-operation in Tax. ATAF and CIAT also operate Internet sites.

[36] These serve: Eastern Africa, West Africa, Central Africa, the Middle East, Central America, the Caribbean and the Pacific islands.

[37] An additional centre in Southern Africa will open shortly, and another is planned for Central Asia.

The management and sharing of tax knowledge is not an end in itself. It only helps if actually used by countries to adopt better tax policies and improve tax administration.

### Tax Knowledge Management Platforms

***A. The International Tax Dialogue (ITD)- http://www.itdweb.org:***

1. The ITD is a well established IT forum for regular exchange of information and good practice among a wide variety of countries.
2. The ITD operates a free, multilingual, multinational Internet site. Over 3 000 documents on tax policy and tax administration issues from around the world are currently available online with new documents added daily. These come both from contributing countries and from the organisations that are the ITD partners. The ITD website had over 32 000 hits in January 2011 with more than 130 countries visiting this site.
3. ITD partners, particularly the IMF, the World Bank and the OECD generate a wealth of knowledge through publications, annual meetings, Committee meetings, workshops and conferences.

***B. The United Nations (UN) - http://www.un.org/esa/ffd/tax:***

1. The United Nations website platform in the tax area relates especially to the work of the UN Committee of Experts on International Cooperation in Tax Matters. The website of the Committee, maintained by the UN secretariat, is in one respect a knowledge management platform in areas addressed by the Committee, and is being re-developed to more fully meet this need.

***C. Inter-American Center of Tax Administrations (CIAT)- http://www.ciat.org:***

1. CIAT operates a bilingual (English, Spanish) Internet site.
2. CIAT also offers e-learning courses, which are aimed to complement rather than to replace face-to-face capacity building activities.
3. CIAT has recently launched an e-forum (CIATalk) to facilitate an informal space for opinion on matters of tax policy and tax administration to members of MyCiat Community.

***D. African Tax Administration Forum (ATAF)- http://www.ataftax.net:***

1. ATAF is in the process of designing and implementing an IT-based knowledge sharing platform as part of its business plan in the area of capability building. The main objective of this platform is to promote and facilitate mutual co-operation among African tax administrations and other relevant and interested stakeholders so as to improve the efficacy of their tax legislation and administrations.

## Gaps and unmet needs

Despite achievements so far, it is clear that more effort needs to be devoted to developing and making widely available a fully comprehensive and continuously updated technical assistance database. Sharing information will come increasingly important if assistance in the tax area is increased.

Aside from the ITD database of TA activity by specific providers, a common denominator of all of existing studies is that they are static; *i.e.* they offer a picture of the situation at a particular point in time, and have not often been repeated on a regular basis. In addition, in most cases information is obtained through public documents and/or websites of the institutions concerned, which does not guarantee that these studies reflect the latest information.

The ITD is currently working with regional agencies (*e.g.* ATAF and CIAT) to help develop a regional forward-looking mapping of international co-operation on capacity building. From this collaboration it is expected that TA providers and recipients, as well as donor institutions and countries, will be able to benefit by avoiding resource duplication, as well as improving the effectiveness of bilateral and multi-donor funded fora.

TA activities on taxation are often embedded in projects with a broader scope and are currently difficult to track as donors generally do not identify the cost of individual components. As a consequence, the relationship between a list of activities provided and the amount of financing devoted to such activities is very difficult to identify. A comprehensive project is currently being undertaken jointly by the ITD, the ITC and OECD-DAC to analyse this information gap. Its main objective is to review and summarise data provided by OECD-DAC aid statistics and further existing mapping studies/data, such as:

- the reports delivered within the scope of the International Tax Compact;
- World Bank and IMF databases on technical assistance;
- the report prepared for the UN Committee of Experts (by IMF staff) on capacity building; and
- the ITD database on capacity building.

This ongoing work will include an overview of modalities, instruments and approaches of the different donors, analysis of information gaps from the perspective of different users; assessment of alternative options to fill information gaps; assessment of possibilities and challenges to provide such reporting on a regular (*e.g.* annual) basis and to establish public online access to this information.

The need to strengthen existing regional structures to facilitate and encourage South-South networks of knowledge sharing is also apparent. Mechanisms operating at this level help to ensure those platforms are focused on meeting as effectively as possible the needs of countries in particular regions. The case for further action in this area in Asia is particularly strong.

Connecting mechanisms between regional and international platforms would allow users to focus on regional initiatives where relevant, but also access wider experience and good practices, which would strengthen and broaden knowledge sharing (not only South-South, but among all types of countries) and dialogue. In addition, these connecting mechanisms would avoid unnecessary duplication, while recognising the value of showing differing approaches to particular issues. One resource issue, which results in practice in a real constraint in sharing experiences across regions, is the need to improve provision of simultaneous interpretation and translated material in order to be able to disseminate information to a wider audience.

Increasing the number of systematic demand driven smaller events at regional level with carefully targeted audiences and participation may also be helpful in building and sustaining smaller, sustainable communities of tax officials (*e.g.* the ITD is currently working with collaborating institutions including CIAT and ATAF to expand the number of regional events in Latin America, Africa and Asia). There is also the need to improve links between regional events and the ITD Global Conferences. Other bodies such as the ITC and ICTD will also be organising smaller closely targeted events related to their respective tax and development agendas.

## Summary of Recommendations

***a) Mapping International Assistance***

Encourage technical assistance providers, especially bilateral providers which are not as well documented as multi-lateral providers, to establish mechanisms to regularly provide information on tax-related technical assistance (by country/region and broad topic activities), for inclusion on the ITD website (unless the recipient wishes otherwise) by the 2012 Summit.

Encourage OECD-DAC to work together and with donors towards more comprehensive, relevant and user-friendly statistics on the financial resources devoted to tax-related technical assistance activities.

***b) Knowledge Management Platforms***

Greater involvement of emerging market G-20 countries in delivering advice and exchanging their experiences in a south –south context could be especially productive.

Encourage countries to actively participate in regional and global knowledge sharing platforms, including their design and improvement, and to facilitate communication amongst tax officials in sharing good practice (particularly in Asia).

Encourage all countries and interested organisations to work together towards a more efficient and effective use of regional platforms by means of the ITD and UN.

Encourage development of automatic software-based technical linkages between regional and international platforms with the objective to strengthen and broaden sharing knowledge mechanisms.

Assist in the translation of knowledge materials and with interpretation in face-to-face events into the major G-20 languages: Arabic, Chinese, English, French, Portuguese, Russian and Spanish.