Keynote speech ITC workshop

Ladies and Gentlemen,

It is my pleasure to welcome you in Brussels to this workshop of the International Tax Compact we organise jointly with the Spanish Presidency and the German Federal Ministry of Economic Cooperation and Development. The strengthened focus on tax issues at the G20 and the OECD, as well as your impressive presence today, are testimony to the fact that from all quarters, there is willingness and new momentum to tackle this issue and secure more revenue towards development goals. The International Tax Compact reflects the increasing importance of taxes and tax governance in the development agenda and highlights our commitment to ensure increased domestic resource mobilisation.

First in Monterrey and then in Doha in 2008, the International Community has underlined the importance of domestic revenues for development. The European Commission has recognised the necessity to do more to enable developing countries to raise additional domestic revenues. Together with the European Parliament we have organised a conference on "Tax and Development" last year in December many of you attended. We wanted to raise awareness about the importance of the topic and examine what we could do at the level of the Commission to improve our development policies. Currently we are preparing a Communication on "Good Governance in Tax Matters in the Context of Development cooperation". I would like to take this keynote speech as an opportunity to present some of our ideas to you. But before doing so, let us take a look at where we stand.

Domestic revenue collection is very low in many developing countries which depend on aid to have functioning States that provide services to their populations. Mozambique is a case in point: development assistance accounts for 15% of GDP (and 42% of its budget) whereas its tax revenues only account for 12% of GDP. One may wonder if, and for how long, this situation is sustainable? How long will developing countries like Mozambique depend on foreign aid, which is less predictable than tax revenue? It will be a challenge to convince public opinion in Europe to increase our aid if we can't point in any clear way to a time, however remote, when domestic revenues will become a far more significant source of development finance in our partner countries. In this context allow me to strongly underline that our endeavour to support domestic revenue mobilisation does in no way mean that we will scale back our efforts to increase our official development assistance. The EU stays committed to reaching the 0.7% of GNI by 2015.

Undertaking tax reforms to promote growth and ensure development is not a new idea. What is new is how we look at tax reform. For too long we have ignored the importance of a broad tax base for sustainable development. We have been looking at tax systems from an economic perspective; too often considering that taxes where merely part of the investment climate and used tax reform as an instrument to foster foreign direct investment. While this is certainly an important aspect, we have neglected the beneficial impact a broad tax base can have on good governance and democratic accountability. We have neglected that taxes are at the centre of state building, and that whoever believes in the state as an actor for development and provider of public services, needs to strengthen its capacities to raise tax revenues.

It is time for a change. It is time to take into account the crucial role taxes play for development. The fact that this meeting brings together tax officials from four different
continents proves that from all sides there is clear political will to do more to mobilise own resources. Not only to raise more revenues and to reduce aid dependency, but also in order to foster ownership and enhance democratic accountability in developing countries.

Poor countries are confronted with many constraints when attempting to increase tax revenues. The level of their development and the structure of their economies have a severe bearing on the domestic tax effort. In many developing countries more than 40% of the economy is informal, a considerable challenge to revenue mobilisation. Inefficient tax administrations, unclear tax legislation, lacking capacities are common obstacles, as are tax evasion and avoidance. Better revenue collection is needed. It requires improvements in tax administration and tax policy reform. Especially in countries where natural resources abound it is necessary to make sure tax revenues be used in accordance with poverty reduction strategies.

Ladies and Gentlemen,

The hardest thing to understand in the world is the income tax. This is Albert Einstein, the taxpayer, speaking. Like Einstein at his time, people nowadays – no matter how smart they are – often struggle to understand how to fill in their tax forms. This is due to complicated procedures, unclear and sometimes even contradictory regulation. Making tax compliance easier is of utmost importance to ensure revenue collection. Procedures need to be smoother and a proliferation of tax exemptions should be avoided in order to make it simpler for taxpayers to comply with tax legislation. This would also make it easier for authorities to collect taxes, discourage tax evasion and would help to attract foreign direct investment. Surveys indeed suggest that it is not just the level of taxation but also the total tax compliance cost that determines investment in developing countries.

Obviously a simpler tax system must be coherent with the need of having a fair tax system seeking vertical and horizontal equity. Exchanging best practices in this field is extremely valuable. Initiatives such as the International Tax Compact are ideal platforms for exchanging views and experiences on tax reforms and their impact on political, economic and social development. It will certainly be inspirational for our own work as a development partner.

Ladies and Gentlemen,

Allow me now to present to you some of the key ideas of the Communication the Commission is currently preparing on Good Governance in Tax Matters in the Context of Development Cooperation.

Developing an improved policy framework for good governance in tax matters is needed now more than ever because it is at this time of a global economic and financial crisis where we can't spare efforts to enhance support to developing countries in establishing fair tax systems that benefit the poor, ensure growth, enlarge the tax base and contribute to democratic accountability. To achieve this it is essential to support developing countries' tax efforts, as it is necessary to involve developing countries more and better in international tax cooperation. Our Communication will look at domestic and international factors that hamper developing countries' ability to raise tax revenues and will propose adequate response to the challenges we face.
On a domestic level we want to step up efforts to improve the effectiveness of EU support to tax systems. This will include several building blocks. The first one will be to look at a more comprehensive approach to tax administration and tax reform. This would include governance aspects but also private sector development, macroeconomic stability and social protection. The European Commission will also make sure that raising domestic revenues as well as good governance in tax matters be included in the policy dialogue the European Union conducts with Budget Support recipients. We will also increase support to multilateral and regional initiatives on tax administration and tax reform especially when they are demand-led. The African Tax Administration Forum is a good example of such an initiative. Our effort to promote regional integration will also include measures to support the harmonisation of tax systems and to increase efficiency of customs border services. And last but not least, we have to improve donor coordination, including a more effective EU division of labour in our partner countries.

Many developing nations share the sentiment of having been left out of international cooperation in tax matters. While this may partly be due to a lack of capacities to effectively participate in the international discussion, a key factor is that tax fraud had not been sufficiently recognised as a serious threat to development. Yet studies suggest that the amount of money that developing countries lose because of tax fraud amounts to several hundred billion euro annually. Money needed to finance health or education programmes is shifted abroad, often to non-cooperative jurisdictions. It is time to stop the erosion of developing countries' tax base by involving them adequately in the international fight against tax evasion and avoidance. Tax treaties that allow for an effective exchange of information have to be extended to developing countries, and support has do be given to developing countries' tax authorities in order to help them to make good use of them.

The European Commission is looking at ways and means to enhance developing countries participation in international tax cooperation. We need to ensure that all countries – no matter how poor - can participate in information exchange in tax matters. This means that those developing countries that have not signed any agreement on exchange of information should be supported to do so. A bilateral approach does not seem sufficient, and the possibility to extend existing multilateral conventions such as the Convention on Mutual Administrative Assistance should be explored. Another important matter is how information is exchanged. Is it enough if information is exchanged on request? Or should information be exchanged automatically? This would mean that information has to be standardised. Developing countries would probably need technical assistance to exchange information automatically. We will hopefully have the opportunity to discuss these and other relevant issues with you in the working groups.

Not only wealthy individuals and domestic companies, but also multinational corporations operating in developing countries often don’t pay their fair share of taxes. The international financial system is overly complex, if not opaque. While capital easily crosses borders, tax authorities operate on a national level and often lack information about the global activities of multinational corporations. Civil society has been strongly pushing towards more transparency in accounting standards. One suggestion here is to introduce country-by-country reporting, that would provide detailed information about companies operating internationally. It would make it compulsory for multinational companies to give information about the countries where they operate and under which name, how much profits they make and how many people they employ. All this would certainly help tax authorities to assess the tax liabilities of some of the most important taxpayers and contribute to reduce aggressive tax
avoidance. Here again developing and developed countries have to act together to make sure taxes are paid where profits arise.

In that context the European Commission welcomes that the Committee of Fiscal Affairs and the Development Assistance Committee of the OECD are organising a joint meeting – the first one of its kind - to address the specific situation of developing countries in international tax cooperation.

Ladies and gentlemen,

This is just a brief summary of some topics we would like to address in our forthcoming communication. Your feedback would be most helpful so that we can further sharpen our policy focus and develop a balanced and realistic view of what can be achieved together. Allow me to underline that the Commission will do everything it can to ensure that developing countries be given the necessary instruments to raise more taxes and to fight effectively harmful tax practices. It is about more than just money. It is about ensuring the sustainability of development. It is about reducing aid dependency and increasing developing countries ownership and sovereignty.

I wish you much success with the workshop.

Thank you for your attention.